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Rediscovering Rolling Planning: Controller's Roadmap for Implementing Rolling Instruments in SMEs

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Abstract

Advocates of rolling planning instruments believe they are superior to traditional, static tools. Yet only a minority of enterprises employs them. This study briefly compares and contrasts traditional controlling tools with their rolling counterparts. It then considers why many enterprises have failed to adopt rolling planning instruments and presents a strategy that might facilitate their doing so.

***Keywords*: Business Drivers, Controlling, Forward Visibility, Rolling Budgets, Rolling Forecasts, Scenario Analysis**

1. Introduction

Traditionally, classic business administration has had a clear orientation on the fiscal year. Both the statement of comprehensive income and the closing statement of financial position are annually-based. The high general acceptance of an annual orientation creates a framework, which facilitates time-series comparisons of a single enterprise's performance and comparisons at a given point in time between enterprises. However, the environmental conditions of many enterprises often are so unstable that annually-oriented plans require updating several times in the course of a business year. Accordingly, a survey of over 200 organizations found that 80 percent of them expected to have quarterly rolling forecasts and budgets in place by 2005 [1]. Despite the touted advantages of rolling instruments, though, seven years later still only a minority of enterprises employs them.

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On the other hand, the marked increase in various forms of economic volatility (demand, overall business conditions, input and output prices, exchange rates and costs of workforce talent) in the aftermath of the 2007-2009 financial crisis appears to be forcing companies to rethink their approaches to planning [2]. At least for some enterprises, the world seems to be moving too fast to plan even one year ahead. Furthermore, by focusing solely on annual goals, management risks steering the enterprise in the wrong direction due to its failure to take important information beyond the fiscal year's end adequately into consideration.

Hence, as shown below, recent survey results indicate that, while still far from ubiquitous, the usage of rolling planning instruments indeed seems to be increasing. This study explains why more enterprises don't have them in their controlling toolkits yet. To do so, it begins by describing the traditional, static planning tools most enterprises employ, together with these tools' shortcomings. It then turns to the more advanced, rolling forecasting and budgeting instruments found at leading firms. In comparing and contrasting static with continuous planning instruments, it reports results from various surveys, conducted mostly in German-speaking countries, about their use. After discussing reasons why the employment of dynamic devices is less widespread than it might be, it develops a strategy to facilitate their adoption and implementation.

2. Shortcomings of Static Instruments

Results from a survey among controllers in Austrian, German, and Swiss small- and medium-sized enterprises (SMEs) with regard to the quality and costs of their planning illustrate nicely the Janus-like view managers have of traditional, static planning. On the one hand, they complain about the large amounts of time and money consumed relative to the modest utility gained from preparing annual forecasts and budgets. On the other hand, most managers don't believe they can make do without them [3]!

In answering a question about the resources budgeting alone consumes, 10 % of the surveyed firms reported needing more than 20 man-months to complete this task. Only 39 % of the businesses said they needed fewer than 3 man-months. Results from a survey of larger enterprises are broadly similar. In over 68 % of the companies, the controlling staff reported annual budget preparation requiring between eleven and twenty weeks. More than half the enterprises took between 4 and 6 months for their operational planning and budgeting. Indeed, several firms said they spent more than 31 calendar weeks on these processes [4].

Results from a third survey are particularly interesting because the researchers repeated their 2006 study with the same panel in 2010. The number of full-time equivalent (FTE) positions devoted to budgeting per 1 billion € in sales revenue grew from 5.56 to 7.49. Meanwhile the number of drafts necessary before authorization of the budget rose from three to four, and the number of workdays required for planning and budgeting increased from 60 to 80. On average, budget preparation alone consumed twenty-eight days, with a quarter of the firms reporting they needed more than forty-five days to complete the task [5]. Supporting the findings about these trends, another survey discovered 64 % of controllers saying their planning took too much time and 47 % of them expecting planning costs and efforts would be higher in 2011 than in 2010 [6].

Furthermore, the amount of detail involved in annual budget planning is very high. Over 50 % of the surveyed SMEs budget at least 50 cost centers, while 25 % base their budgets on more than 100 cost centers. The same is true for the number of general ledger accounts taken into consideration [3]. It is noteworthy that the degree of detail increases with the number of positions planned. Yet details about the incorporation of strategic measures into annual budget planning often are inadequate – or altogether absent [4, 5].

In larger enterprises, the high degree of detail in budget planning is an important influence on the amounts of manpower and time consumed too. Decomposing the overall budget problem down to the lowest hierarchical level requisite for detailed analysis consumes large quantities of such resources. Moreover, wasteful resource consumption occurs every time negotiating partners loop through the planning cycle to revise their draft until they finally approve the annual operating budget. Large firms usually commit 75 % to 95 % of their total controlling capacity to operational planning during the time they are engaged in budget preparation [7]. Also worthy of mention is the fact that only 36 % of the respondents really believe in their

budget. 57 % of them assess the crunched numbers generated from all that work as moderately realistic at best. Comparison of actual results with forecasts shows further that this self-assessment markedly overestimates budget quality. After only three months, events have overtaken more than half of all traditional, static budgets. Relative to the planning period, only about 6 % of the budgets examined proved to be reasonably accurate. In addition, linking the budget numbers to benchmarks in the form of personal performance contracts hardly improves budget accuracy [3]. Comparable figures from another survey show 12 % of controllers don't think their own plans are worth the paper on which they are printed, while another 53 % view them as a point of orientation at best. Moreover, 54 % of controllers believe their budgets always are overtaken by events within six months of authorization and the other 46 % think that often to be the case [6]!

Among the reasons given (multiple responses possible) why actual results vary from forecasts and budget plans, the most frequently mentioned are: changes in the business and economic environment (67 %), imprecise or too aggressive forecasts (54 %), and poor data quality or missing data (41 %). Participants also cited the overly long duration of the budgeting process itself (23 %) [8].

In fact, the relationship between accuracy and the length of time required for forecasting and budgeting apparently is an inverse one. While 50 % of the enterprises needing less than a week produced actual results within ± 5 % of their predictions, only 11 % of the companies taking a month or more were equally precise [9]. A similar study of the relationship between the efficiency of forecasting and budgeting processes and their effectiveness arrives at the same conclusion [5].

Researchers therefore rightly wonder whether highly detailed forecasts and budgets really are necessary and efficient. Unfortunately, top management seldom considers the high cost involved relative to the meager benefit derived from such detailed instruments. It then is no wonder that cost, product, and strategic controlling considerations often receive little attention in the planning process. Whatever their utility in the past, traditional, static budgets apparently no longer constitute an adequate basis for modern operational controlling. It therefore is all the more surprising that five of six surveyed controllers can't imagine working without them [10]! Likewise controllers either don't view reduction of planning cost and effort as an important topic (41 %) or, while recognizing it as an important problem, have not done anything about it yet (24 %) [6]!

More-effective forecasting-and-budgeting capabilities were top-of-the-mind for CFOs in 2011, with 84 % making them a priority, followed closely by improving the accuracy, shortening the cycle time, and increasing the efficiency of forecasting performance at 81 % (multiple mentions possible) (Hackett Group, 2011). Greater accuracy (42 %) and closer linkage between strategy and execution (31 %) long have been high priorities, whereas CFOs generally have held shorter cycle time (9 %) and switching to rolling instruments (7 %) to be less urgent [11].

Although not viewed as their top priority, CFOs nevertheless have clear ideas about what would boost confidence in their forecasts the most. Those measures (multiple responses possible) would be: further automation of IT-systems and -tools (42 %); more scenario planning and sensitivity analyses (42 %); switching to a rolling format (40 %); reduction in detail as well as a stronger focus on business drivers (35 %); and better input data quality (34 %) [12].

3. What Are Rolling Forecasts and Budgets?

Rolling forecasts and budgets are key elements of a planning system distinguished by regular adjustments and increasing detail as the information situation improves. In principle, the "rolling concept" is not new because enterprises have been preparing certain sub-budgets on a continuous basis for a long time [13].Cash planning, undertaken every month or quarter, probably is the most familiar of these sub-budgets. Both midterm and long-term plans are rolling instruments too. In actual practice, though, a rolling approach to operational budgeting remains unusual.

The most important characteristics of rolling plans in contrast to traditional forecasts and budgets are:

- constant horizon independent of the fiscal year
- periodicity (as a rule, quarterly preparation)
- combination of more detailed planning in early periods and less detailed planning in later periods
- planning focuses mainly on monetary and nonmonetary business drivers that influence monetary results (revenues and costs)

Underlying all rolling forecasts and budgets is a constant time horizon. In a given individual case the dynamism and complexity of the environment determine the number of the quarters or months for prognostication [14]. Normally the time interval covered lies between five quarters (or thirteen months) and eight quarters (or twenty-four months), because beyond two years' time the reliability of the prognosis declines markedly. Survey results show about two-thirds (67 %) of enterprises still rely exclusively on traditional, static budgets. Of the 33 % of enterprises, whose planning system contains at least some rolling elements, 7 % have a time horizon of four quarters, 6 % five quarters, 4 % six quarters, 9 % a flexible number of quarters, and 7 % some other horizon such as two quarters or three years [9].

Many enterprises, which have introduced both rolling forecasts and budgets, use them in combination with a traditional annual budget plan. This approach determines the lower boundary of five quarters (or thirteen months), because at the latest with the beginning of the fourth quarter (or twelfth month) forecast and budget values must completely cover the next fiscal year. In addition, the inclusion of at least five quarters (or thirteen months) facilitates comparison of the same quarter (or month) of different years (e.g., the first quarter of 20XX with the first quarter of 20XX+1). Especially in the construction industry and the merchandising sector, with their strong seasonal variations in revenues, such comparisons are helpful for controlling an enterprise's operations.

Rolling revisions ensure that, despite the passage of time, the length of the period covered remains constant, while currently available, improved information is integrated into them. In doing so, one distinguishes between the quarters with regard to the degree of detail. As a rule, one prepares more detailed forecasts and budgets for the next quarter (Q1 in January 20XX) than for the later quarters (Q2 20XX, Q3 20XX, Q4 20XX, Q1 20XX+1).

Relative to traditional, static planning as an annual one-time event, rolling forecasts and budgets offer an enterprise's management clear gains in near-time controlling information. These gains pertain not only to the revenue budget, but also to the production budget, and to the budgeting of inputs as well as to work-in-process and finished goods inventories. Because they always are based on the most recent information available, a high degree of actuality is an important characteristic of rolling instruments. Near-time information is important above all for exchange-listed companies because the share price is sensitive to forecasts of the business's future development. With rolling instruments, one already can make a statement at the beginning of the second quarter 20XX about how an enterprise's business likely will develop during the first two quarters of 20XX+1, thereby providing much earlier guidance for stakeholders' expectations than traditional, static methods afford.

Unfortunately, the terms "rolling forecast" and "rolling budget" often are used as synonyms for a dynamic, continuous planning process. This imprecision leads to confusion because the two terms actually apply to related, but different instruments. The important difference concerns their goal orientation. A rolling budget usually has linkage to a binding service contract between the management levels with relative goals (ideally defined through benchmarking) to be attained within certain guidelines and on the basis of specific, concrete measures. Management periodically re-evaluates and adjusts these goals accordingly. The adjusted rolling budget thus represents an authorized plan of action to attain a certain goal condition.

In contrast, in the case of rolling forecasts, there generally is no monthly or quarterly goal adjustment process. Instead, the purpose is to predict the future state of the enterprise's business development as accurately as possible. The goals remain constant for a fiscal year, so that one can calculate an updated

"standard cost-forecast variance." The rolling forecast then just provides a framework, in which individual business units plan their operational activities. Accordingly, it somewhat resembles the flexible budget, also frequently used in cost accounting, where the degree of capacity utilization serves to correct the standard costs involved.

4. Rolling Instruments

To overcome the shortcomings of traditional, static tools, enterprises with better or advanced methods use at least some rolling instruments in their planning. The following description, though, applies just to those few enterprises, whose planning practices are best in their class. Environmental changes, not the fiscal year, trigger their planning. Accordingly, they continuously adjust their planning framework to internal and external events. While they also have clear rules to coordinate planning and to resolve disputes, coordination and quality assurance are independent of the planning process. Their reporting is flexible and scenario-based.

They understand the most important variables driving their business and use them as an integral element of their departments' controlling and reporting. The inclusion of key business drivers in all planning models provides linkage between strategy and operations. It also facilitates a reduction in planning detail, thus promoting greater efficiency and effectiveness. Because 20 % of the ledger accounts comprise 80 % of an enterprise's total expenses, one can focus attention largely on them. For purposes of controlling the remaining 80 % of the ledger accounts, comparisons of actual results from the prior and current periods often are adequate, thus reducing planning effort markedly and minimizing the number of coordination rounds required [4]. Responsibility for the planning model and the associated drivers lies with the operational business units.

Best-in-class enterprises quantify the effects of strategic initiatives and link them with both operational planning and business drivers. They establish fixed feedback loops in their strategic planning in order to make the adjustments necessary to obtain the „buy-in" of subordinated operational units. In setting operational goals for these units, best-in-class enterprises rely on performance comparisons relative to internal and external benchmarks ("beat the competition and beat the budget"). For performance evaluations, they eliminate factors over which managers have no influence ("split luck from effort"). For resource allocation purposes, on the other hand, best-in-class enterprises use an internal marketplace, where a project's contribution to value serves as the basis for investment decisions.

Best-in-class enterprises understand planning as a continuous process, linked to rolling prognoses. Built on key business drivers, the prognoses undergo regular, periodic updating as well as revision in response to environmental changes. Because prognoses can lead to coordinated, cross-functional operational countermeasures, their accuracy is a crucial item in the responsible managers' personal performance contract.

In their financial and sales planning, these businesses use scenario modelling with both internal and external parameters. Largely automated, this modelling is grounded on enterprise-wide assumptions as the core elements of all planning and decision processes. The planning staff generates detailed supplements and emergency schemes for certain scenarios and risks as required.

The prognoses and plans also include future-oriented elements like sales-funnels as well as measures of market potential and sales effectiveness. Planning for production, procurement, and support functions also concentrates on key business drivers in a uniform model. Production and supply chain planning simulates different levels of capacity usage and product priorities, while paying close attention to the efficiency of various manufacturing sites. A "make or buy"-decision framework is in place for introducing products managing risk, and compensating for demand peaks.

Best-in-class solution support provides for acquisition of new hard- and software based on a long-term strategy, which in turn is coordinated with the enterprise's strategy. It covers the complete planning cycle, linking horizontal functional areas with vertical hierarchical levels. It thus facilitates enterprise-wide, efficient cooperation, coordination, and communication. The solution support promotes complex scenario modeling at all echelons, while systematically including available actual-data as the foundation for planning and

prognoses.

5. Why Aren't All Enterprises Striving to Become Best-in-Class?

In view of the advantages described above, the question naturally arises as to why many firms still engage in traditional, static planning. Indeed, top management's behavior in this regard seems contradictory. On one hand, the senior management team sees the desirability of reducing the amount of detailed planning content (33 %), in part by making more realistic assumptions and adopting top-down guidelines for budgeting. On the other hand, in practice, only 28 % say they use a top-down planning approach [4].

Further instances of such schizophrenic behavior abound. For example, CFOs view linkage between strategic with operational planning as a key success factor (98 %), but more than a quarter of them (26 %) admit they do not have it in place in their own enterprise. 45 % of CFOs agree that scenario planning is important or very important, yet just 15 % of them engage in it. 53 % of CFOs believe first-class IT support is essential for successful planning efforts, but only 22 % of them report having automated planning support in their organization [4].

For practical reasons, both executives and operational managers may prefer more detailed budgets. They offer executives a vehicle for maintaining greater control over subordinates. They also afford managers with operating responsibilities greater security that they are making "correct" decisions. Among other reasons researchers give for companies nevertheless retaining traditional planning instruments are the following [15].

- The annual goal-setting process in the sense of management by objectives by itself is rather costly in terms of manpower, money, and time. To repeat this process every quarter or month simply could prove to be prohibitively expensive.
- One can't ignore the annual basis of various planning objects such as the planned balance sheet. An annual orientation is inherent in many standard business practices and external stakeholders expect a similar orientation in enterprise planning. Moreover, many firms have tied management incentive systems to the attainment of annual goals, necessitating generation of corresponding numbers.
- An annual orientation promotes stability. Too frequent adjustments can cause managers to doubt the binding nature of the budget plan. It is seldom the case that all the decisions involved have been reached by consensus. Calling the planned goals and measures to attain them into question every month or quarter could touch off unproductive squabbling, potentially paralyzing management when it needs to take action.
- Simple ignorance of the possibilities of combining periodic and continuous planning inhibits adoption of rolling instruments too

The above reasons are somewhat surprising because the specific combination of periodic and rolling instruments necessary for implementation of best-in-class planning, of course, varies across organizations and stages of business development. Thus, for example, an immediate switchover to continuous forecasts and/or rolling budgets may prove useful in one company, but not in the next. In addition, the possibility of gradual implementation within an organization is an important characteristic and a great advantage of best-in-class planning. Managers and employees thus can learn how to use the new instruments step-by-step and consequently fewer problems are likely to occur during the introductory phase. Over time, users become increasingly adept in applying the instruments and can plan operational measures without difficulty. Accompanying this development is a gradual, forced reduction in the importance of traditional, static planning instruments.

CFOs themselves give more reasons for their reluctance to introduce rolling planning: the time taken from other controlling tasks for the necessary administration and merging of the data involved (53 %); the time responsible personnel from the respective cost centers and functional areas must spend making revisions (47 %); resistance of the responsible managers to investing the time necessary to revise forecasts and budgets more frequently (42 %); and the financial costs of additional forecasting and budgeting rounds (25 %) [8].

It is noteworthy that CFOs especially "fear" the mechanical activities of administration and data merging. These areas are precisely the ones in which IT-tools can be most helpful. Automation thus appears to be a critical factor for the success of rolling planning.

6. Strategy for Introducing and Implementing Rolling Planning

Given the circumstances, how should one now proceed to introduce rolling planning instruments? Adopting a pro-active stance is important. In light of the ambivalence and reluctance associated with top management's behavior described in the previous section, an element of stealth may be necessary too. The project itself then could consist of the following fourteen points:

1) Start fresh. It is important to avoid basing the new planning instruments on the (often Excel-based) tools existing in the organization. The new planning structure should suit the model, not the previous planning tools' capabilities. To begin moving top management's thinking in this direction, one might begin by interviewing senior managers to identify key business drivers and questions they likely will want answered in the future. One way to do so is to brainstorm with them about plausible future scenarios and then build the key business drivers into the planning model's design [1].
2) Obtain commitment of top management and the finance team. Both need to comprehend and commit themselves to the rolling instrument methodology. They must understand that the business drivers will tie back to strategic decisions that senior managers may need to make in the future and the financial consequences associated with those decisions. It also is important that top management and the finance team agree that rolling forecasts and budgets will make the planning process easier, quicker, and more realistic. Here, workshops with presentations by experts, organizations with rolling forecasts, and an in-house team, whose members are likely candidates to lead such a project, should prove helpful. Assuming top management commits to the project, it then will need to set aside time to give more feedback on business drivers, visit sites already employing rolling instruments, and approve the investment in the chosen planning software, all on a "tight" time schedule. It also is important to have agreement from all the accountants to abandon any ingrained fixation on looking at details. Top management must be mindful that forecasting and budgeting are core activities and require adequate financing.
3) Progress by stealth. Unless top management decides to take the lead in introducing rolling instruments, the best way to implement the required changes may be by stealth. This approach may involve first justifying investment in the planning system to improve forecasting and end-of-month reporting. Then, when the system is in place and the forecasting and budgeting instruments are running smoothly, top management well may be willing to switch from a fiscal-year to a rolling focus.
4) Choose a small team. The project team should have from two to four members with in -depth organizational knowledge and an appropriate mix of skills including: self-starters, innovators, good presenters and communicators as well as closers; ability to bring others onboard; and general ledger experience. Its members should be committed at least half-time to the project to avoid meeting cancellations due to other responsibilities. Project coordinators at the different business units will support the team with information about their business unit's operations and feedback about their area. Top management's involvement should be left to an advisory capacity. In the future, the individuals principally maintaining the forecast should be its primary users.
5) Avoid overly complex models. Some accountants and planners design extremely complex Excel-based models, which are both difficult and time-consuming to use, lack version control, produce consolidation headaches and low levels of confidence in the resulting numbers. Model planning tools should be relatively simple to employ. Nevertheless, in-house staff members will need to attend in-

depth training, so they can be fully aware of the planning system's capabilities and have had the opportunity to use it themselves.

6) Find an external wise man. The project team will need an on-call external adviser to provide wise council without becoming a team member. This mentor should ensure that the team keeps the project's "big picture" in view and thus avoids losing itself in the details, while also safeguarding against the software provider's consultants taking the team in a direction it should not go.
7) Contract external PR-expertise for internal promotion. The project team must focus as much on marketing the new concept to budget holders as much as it needs to train them. Budget holders must grasp how the new planning process is going to facilitate management of their business. They will need to hear success stories throughout the implementation phase. Accordingly, the project needs PR-expertise behind it. The project team should issue no presentation, email, memo, or paper unless the PR-expert has vetted it first.
8) Design the model in-house. The project team members always must design the model themselves. That means the proper roles for planning tool consultants are advisers and trainers, but definitely designers. Circumscribing consultants' role in this fashion saves substantial amounts of money, while ensuring that the model's designers are people who thoroughly understand the enterprise's business.
9) Apply Pareto's 80:20 rule. The team needs to spend its time forecasting and budgeting the major categories requiring substantial creative thinking and short-circuiting categories subject to automation. Examples of the former are: revenues; salary and wages; benefits; training, travel, and conferences; operational equipment; property costs; and promotional activities. Some examples of readily automated categories are: repairs and maintenance of operational equipment; office equipment, computers, and consumables; telecommunication costs; motor pool costs; building maintenance; depreciation; miscellaneous costs. Several useful rules-of-thumb are: limit the categories forecast by budget holders to no more than twelve; identify categories subject to automation and provide those numbers; display individual lines only if they represent 20 % of the total (e.g. show an individual revenue line only if it constitutes more than 20 % of total revenue). This latter rule applies at both budget holder and consolidated levels. However, forecasts should be detailed enough for any news, good or bad, to be translatable into action. In any event, allow budget holders to have some flexibility in the categories to best reflect their operation.
10) Information from outside the organization should drive the rolling planning process, which also should reflect all the information available inside the organization. External information is essential. Without it the forecast simply is a recast of what already is known and therefore provides little benefit for users. Furthermore it is difficult to forecast out to a meaningful horizon without using indicators of demand from outside the organization.
11) Don't link the planning system to fixed targets for incentive schemes. To the extent possible, keep it free from the influence of personal contracts and incentives. Where necessary, use relative targets (say, growth in market share > market growth by 1 %). Of course, there may be sales targets or goals for cost reduction, but avoid assuming one will achieve them. However, if there are planned events, which will help achieve those goals, rolling forecasts and budgets should include them.
12) Have trend graphs for every category forecasted. One can achieve better quality through trend analyses. There is no place for hidden reserves when a budget holder is accountable for past and future trends. In addition, if available for all categories budget holders must forecast, trend graphs may increase forecasting accuracy.
13) Ensure there always are at least 4 in-house experts on the new system, one of whom should "own" it. Select at least four or five in-house staff members to become experts on the planning system, one of whom should be the CFO and ensure they are in the focus group. Until rolling planning becomes more

widespread, these individuals very well may be recruited by other enterprises to head their rolling planning switchover projects. So, one always should maintain this level of in-house competence.

14) Always test the planning system to see whether it is influencing forecasting and budgeting behavior as intended and whether managers are making better decisions.

7. Conclusion and Suggestions for Future Research

When planning with rolling instruments it is worth reflecting upon a prognosis, with which everyone is familiar – the weather forecast. It presents us with two interesting characteristics that we accept without question. The first characteristic is integrity. We assume that one has updated it recently, and that it embodies all there is to know about the influences upon our weather. If it turns out to be wrong, we accept that it was due to something unknown or unpredictable.

The second characteristic is trust. If the forecast suggests bad weather ahead we don't normally ignore it, or seek a second opinion. We get out the umbrellas.

Where successfully implemented, rolling instruments should lead to major changes in managers' behavior. These tools now should drive the search for new business. For example, they should form the basis for capacity planning in plants and in overhead areas. They should support managers in negotiations with customers. They should prompt critical reviews of overheads required for the future. They should be the cornerstone of midterm and longer-term plans. Whether such changes in behavior indeed occur, forecasts become more precise, budget variances smaller, profits larger, and share price growth higher are proper questions for future research.

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