REGIONAL HIGHLIGHTS

Federal Reserve Bank of Philadelphia

First Quarter 1999

Annual Review

Region's Economy Maintains Momentum

- *First-Quarter Job Growth Close to 1998 Pace*
- *Improvement Seen in Manufacturing*
- *Little Change Expected in State Unemployment Rates*

The economy in the tri-state region (Pennsylvania, New Jersey, and Delaware) slowed in 1998, especially in the second half of the year. Much of the slowdown was concentrated in manufacturing, but industrial output picked up in the first quarter of this year. In 1998, nonfarm jobs in the region increased 1.5 percent on a fourth-quarter-over-fourth-quarter basis. And job growth in the first quarter of 1999 is running just slightly below that pace. The unemployment rate for the three states declined to 4.3 percent in the first quarter—its lowest level in almost a decade.

Manufacturing was the only major sector of the private economy to record any job losses for the three states as a whole last year (0.8 percent). Responses to the Philadelphia Fed's Business Outlook Survey of manufacturers reflected last year's weakness in the industrial sector (Figure 1). The index of general activity from the survey was negative in the final four months of 1998. The index has recovered since then, and the most recent reading (April 1999) was the highest in two and one-half years. Even though factory jobs continued to decline in the first quarter of this year, the worst may be over for manufacturing in the region. The expectations index from the Business Outlook Survey has recovered from its low readings in the second half of 1998. The improvement may not be accompanied by job gains, however, because productivity growth in manufacturing has been high, averaging more than 4 percent in each of the past three years.

For the tri-state region, the gain in construction jobs last year more than made up for the losses in manufacturing. Construction employment was up more than 4 percent. Residential construction benefitted from good job growth and low mortgage rates; housing permits for the year as a whole increased more than 11 percent in the three states, slightly faster than in the nation. Over the course of the current economic expansion, however, housing construction has fared much better in the nation than in the region. Last year, permits at the national level reached 90 percent of their mid-1980s peak. In the tri-state region they were only about 60 percent of their highest level in the 1980s. Construction of commercial buildings (offices, retail space, hotels, and warehouses) also increased strongly last year. The square footage of commercial space put under contract was up about 22 percent in both the nation and the region. In the tri-state area last year, however, contracts reached only 75 percent of the peak experienced in the 1980s, while at the national level they essentially matched their mid-1980s' peak.

Nationally, rapid job growth in financial and nonfinancial services has driven the demand for new office space. In the tri-state region, nonfinancial service jobs have been growing much faster than jobs in the broad financial service category (finance, insurance, and real estate). Among the fastest growing subcategories in nonfinancial services have been business support services, which include computer programming and data processing, and research and management services, which include accounting and auditing. The decline in jobs at banks and other depository institutions held down the growth in financial service jobs in the tri-state region last year.

The government sector in the tri-state area lost jobs for the third consecutive year in 1998. Federal government jobs in the three states declined by more than 6000, or 3.5 percent. Among the three states, only Delaware had any increase in state payrolls, and only Pennsylvania had any increase in local government jobs. The private sector provided all the net new jobs in the tri-state region in 1998 and about 90 percent of net new jobs in the nation.

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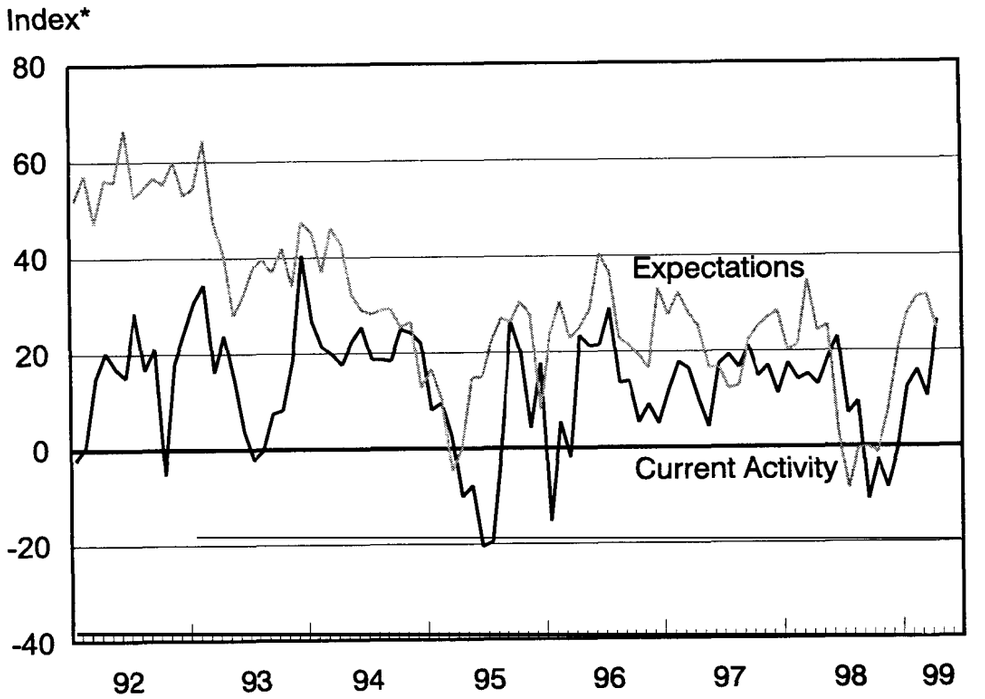
Figure 1
BUSINESS OUTLOOK SURVEY
General Activity Index



*Index represents percentage of respondents reporting an increase minus percentage reporting a decrease.

THE THREE STATES

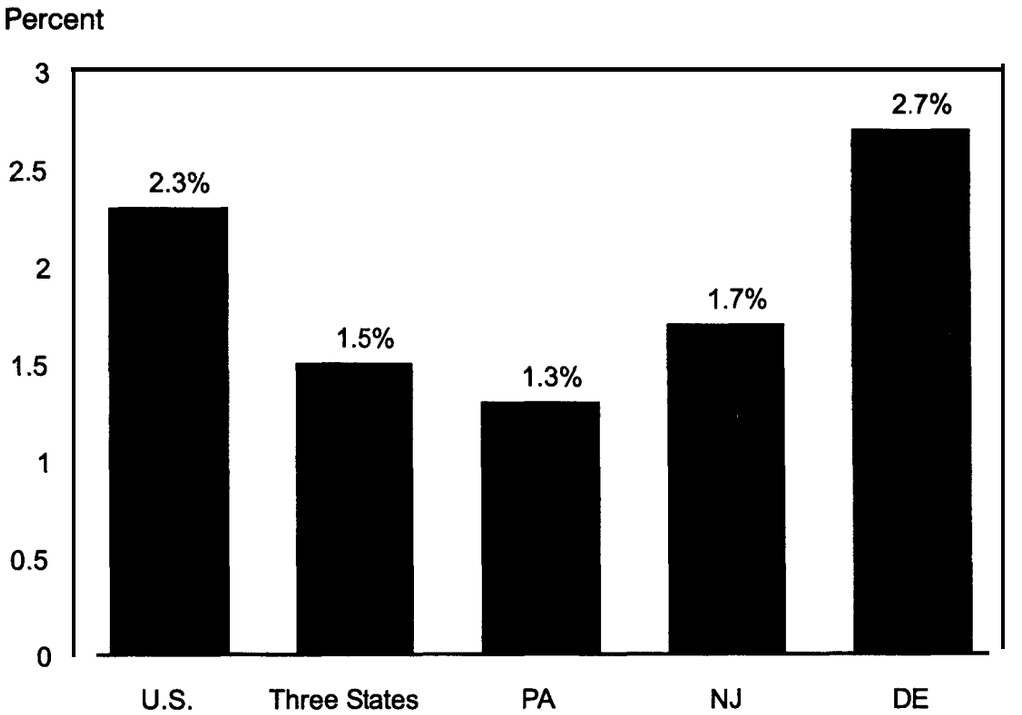
Pennsylvania had the slowest job growth among the three states in the Third Federal Reserve District last year (Figure 2). Growth in the fourth quarter was especially slow in the state and picked up only slightly in the first quarter of this year: so far in 1999 the state's job growth has averaged less than 1 percent at an annual rate. Pennsylvania's unemployment rate continues to fall, however. In the first quarter the rate dropped below 4.5 percent for the first time since 1989.

In the private sector, manufacturing was the only major industry group in Pennsylvania to lose jobs in 1998 (0.4 percent), and the losses continued into 1999. Pennsylvania lost manufacturing jobs at only half the national rate last year, however, and not every manufacturing industry in the state suffered losses. Some, such as lumber and wood products; furniture and fixtures; and stone, clay, glass, and concrete, had job increases of more than 4 percent on a fourth-quarter-over-fourth-quarter basis. Many of these increases were related to the strength in the construction industry.

Construction had the largest job increase of any major industry in Pennsylvania last year (4.4 percent). Both the residential and nonresidential sectors contributed to the gain. Housing permits in the state were up more than 8 percent for the year as a whole, and the value and square footage of nonresidential buildings put under contract were up more than 20 percent. The strong growth in construction jobs continued unabated in the first quarter of this year.

Besides construction, nonfinancial services was the only other major sector in Pennsylvania to have job growth greater than 2 percent last year. The fastest growing subcategory in this group was business support services (6.7 percent). Jobs in social services, which includes day care for children and residential care for adults, increased more than 5 percent. Surprisingly, job growth in Pennsylvania's nonfinancial services slowed to less than a 0.5 percent annual rate in the first quarter of this year.

Figure 2
NONFARM JOB GROWTH
1997: IV - 1998: IV



Job growth in Pennsylvania's financial service sector (finance, insurance, and real estate) was limited last year by the 2.4 percent loss of jobs at banks and other depository institutions. In the insurance industry, jobs at independent agents and brokers increased 3.5 percent, but there were no net job gains at large insurance carriers and underwriters. The largest job increases among the broad financial services last year were for real estate agents and brokers (5 percent). Overall job growth in financial services in the state has slowed in recent months. Growth declined from 1.7 percent last year to an annual rate of only 1.1 percent in the first quarter of this year.

The government sector lost 0.8 percent of its jobs in Pennsylvania last year, the third year in a row that government employment decreased in the state. The federal government reduced employment by almost 5000 (4.3 percent), and state payrolls were down by more than 1000 (0.7 percent). The 1700 additional positions at the local government level (0.4 percent) did not offset the losses of these federal and state jobs.

In New Jersey, nonfarm jobs increased 1.7 percent last year on a fourth-quarter-over-fourth-quarter basis, and they have been growing at the same rate in the first quarter of this year. The state has not experienced the kind of slowdown in the last two quarters that Pennsylvania has. The unemployment rate for New Jersey was 4.3 percent in the first quarter, the same as the national rate for the first time since 1991.

The fastest growing category of jobs in New Jersey last year was nonfinancial services (3.9 percent). Since it is also the largest category of jobs in the state, nonfinancial services was responsible for more than half the net new jobs in New Jersey. On a percentage basis, social services led the gain in nonfinancial service jobs with an increase of 7.5 percent. Jobs in business support services grew more than 5.5 percent, and employment in both private education and health services increased 2 percent or more.

The financial service sector (finance, insurance, and real estate) was stronger in New Jersey than in Pennsylvania last year. Total financial service jobs increased 2.9 percent in New Jersey last year despite the loss of 3.4 percent of the jobs at banks and other depository institutions.

Construction jobs in New Jersey were up 3.7 percent last year, and they have increased at an even more rapid pace in the first quarter of this year. The residential market provided most of the strength. Housing permits were up almost 17 percent for 1998 as a whole, but they are still less than half their peak level in the 1980s. Existing home sales increased more than 13 percent in New Jersey last year, and home prices appreciated almost 5 percent. On the nonresidential side, total building contracts in New Jersey were basically flat last year, but contracts for commercial buildings (offices, retail space, and hotels) were up more than 10 percent.

Manufacturing was the major weak spot in New Jersey's economy last year. The state lost 1.7 percent of its manufacturing jobs, and losses continued at an even faster pace in the first quarter of this year. Some of the biggest percentage losses among the manufacturing industries last year were in fabricated metals, textiles, and apparel. Over the course of this expansion, New Jersey has lost about 17 percent of its manufacturing jobs. This repeats the pattern of the 1980s when the state suffered serious manufacturing job losses even during years of good overall job growth.

As in Pennsylvania, government jobs declined in New Jersey last year (0.4 percent). The federal government eliminated more than 1400 jobs in the state, and the state and local governments cut another 100 jobs.

Delaware had the strongest job growth of any of the three states in the region last year (2.7 percent), and for the fourth year in a row Delaware's growth was higher than the national average. The strong job growth continued into the first quarter of 1999. The state's unemployment rate for the first quarter was 3.1 percent, about a percentage point below its level a year ago and more than a percentage point below the national average.

Even Delaware's manufacturing sector had significant job growth on a fourth-quarter-over-fourth-quarter basis in 1998 (1.6 percent), but many of those jobs were lost in the first quarter of this year. The gain in factory jobs last year resulted, in part, from stepped-up production at the state's automobile plants in the fourth quarter.

About three quarters of the new jobs in Delaware last year were generated in trade or financial and nonfinancial services. Jobs in the wholesale and retail trade sector increased almost 3 percent, and jobs in both financial and nonfinancial services increased 3.3 percent. Delaware was the only state in the Third District to have any job growth at commercial banks and other depository institutions, even though the growth was only 1 percent.

Job growth in the construction industry was slower in Delaware than in the other two states in the District, but it was still a healthy 2.8 percent. Housing permits were up more than 11 percent for the year as a whole, and the value of nonresidential building contracts was up about 25 percent. Continued strong growth in office-related employment should sustain the nonresidential building market.

AROUND THE DISTRICT

The Philadelphia Area

Jobs in the Philadelphia metropolitan area increased 1.7 percent last year, and even in the city of Philadelphia, nonfarm jobs increased 0.3 percent on a fourth-quarter-over-fourth-quarter basis. Growth continued in both the metro area and the city in the first quarter of this year. The unemployment rate in the metro area declined to 4 percent in the first quarter, and in the city it fell to 5.6 percent.

The fastest growing employment category in the entire metro area was construction (5.6 percent) even though construction jobs declined in the city. Housing permits in the metropolitan area for the year as a whole were up 4.4 percent, and nonresidential building contracts were up more than 20 percent. A large number of hotel projects got underway in the city last year, but most of the nonresidential building construction in the Philadelphia area occurred in the suburbs. The pattern of city and suburban office vacancies reflects the relative strength of the suburban market (Figure 3). While office vacancy rates in center city have declined slightly from their peak about two years ago, in the suburbs they fell from 20 percent in 1992 to less than 7 percent by the end of 1998. Suburban vacancy rates are now lower than center city rates—a reversal of the historical pattern.

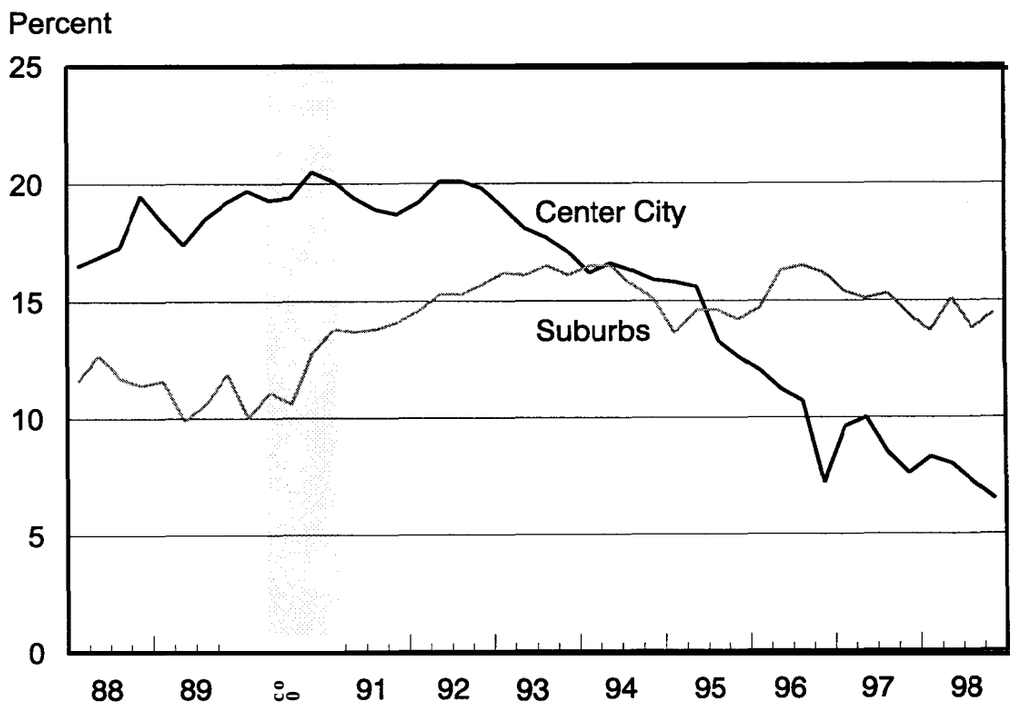
While construction had the largest percentage gain in new jobs in the Philadelphia metro area last year, the greatest absolute number of new jobs was in nonfinancial services—more than 28,000 jobs, or an increase of 3.5 percent. Among the nonfinancial services, business support services and social services each gained about 7 percent.

The financial service industries (finance, insurance, and real estate) added almost 3000 jobs in the Philadelphia area last year (1.8 percent). All of the job growth was among securities firms, mutual funds, and other investment management companies. The metro area lost 2000 jobs at banks and other depository institutions—all of them in the city of Philadelphia.

The Philadelphia metro area also lost more than 1 percent of its government jobs last year. State payrolls in the area were reduced by 2000 and federal payrolls by more than 1000. Even local government jobs declined by a few hundred on a fourth-quarter-over-fourth-quarter basis.

The loss in manufacturing jobs in the Philadelphia area (about 2000) was less than the loss in government jobs. On a percentage basis, the Philadelphia area lost fewer manufacturing jobs in 1998 than the nation as a whole. And there were job increases in the chemical industry, which

Figure 3
OFFICE VACANCY RATES
Philadelphia



Source: Coldwell - Banker

includes pharmaceuticals, and in some manufacturing industries that supply material to the construction industry. The metro area continued to shed manufacturing jobs in the first quarter of this year, but at a slower rate than the nation.

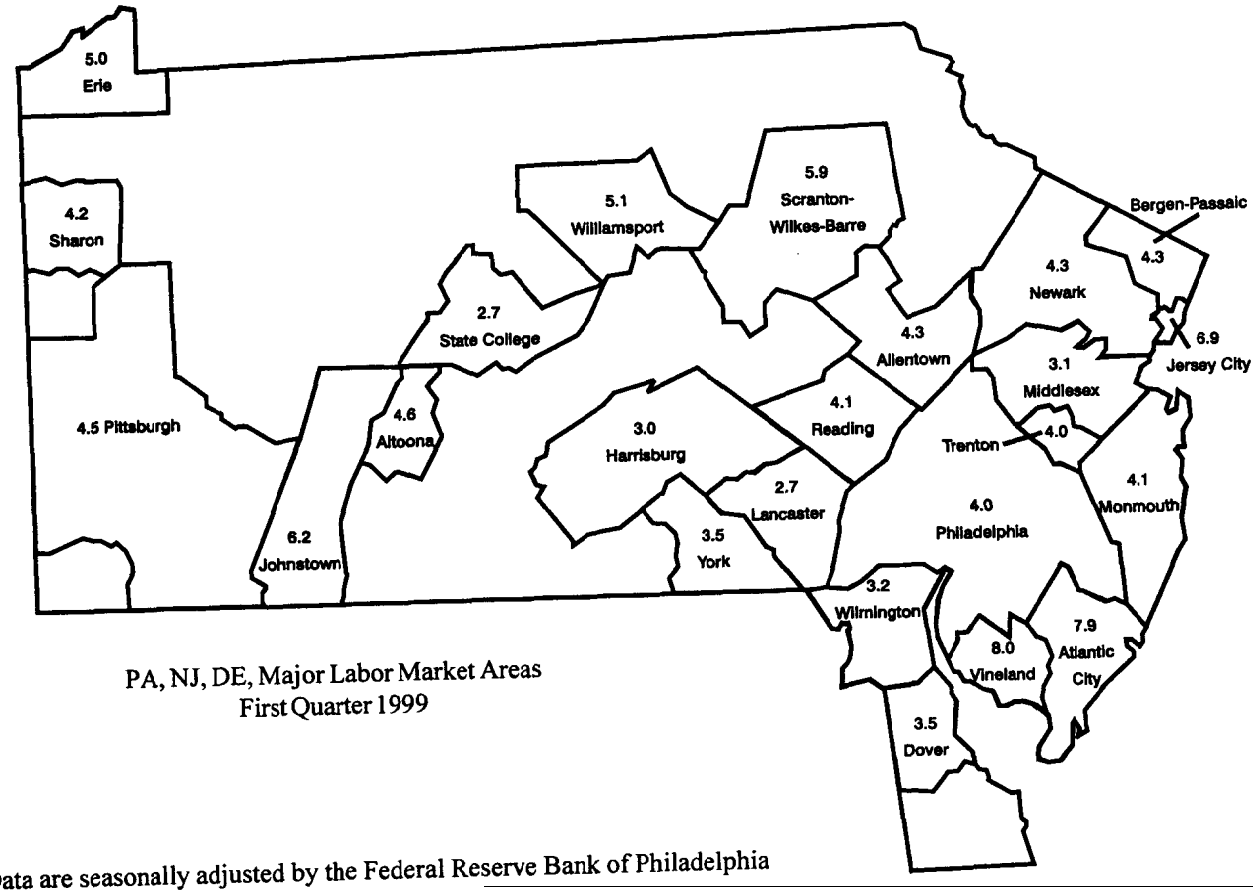
The South Central Pennsylvania Labor Markets

The three labor markets in south central Pennsylvania (Harrisburg, Lancaster, and York) have traditionally had some of the highest job growth and lowest unemployment rates in the state (Figure 4).

Harrisburg had the fastest growth of any labor market in Pennsylvania last year (2.2 percent). Every sector of the private economy had some job growth, and losses in the government sector were minimal as reductions at the federal level were mostly offset by increases at the state and local levels. The largest job gains in Harrisburg were in nonfinancial services (3.7 percent), and more than 50 percent of these gains were in business support services, such as computer programming and advertising. The manufacturing sector added almost 1000 jobs (2.1 percent), many of them in the food industry. Several other sectors of the Harrisburg economy grew by 2 percent or more—construction, trade, and transportation and public utilities. Among the transportation industries, trucking and warehousing continues to expand rapidly. The area's unemployment rate has been about 3 percent for more than a year, and it is currently the third lowest among the state's 14 labor markets.

The Lancaster area had job growth of 2 percent last year, and in the first quarter of 1999 growth was running at more than twice that rate. In the private economy, growth rates in 1998 ranged from more than 7 percent for construction to 0.5 percent for wholesale and retail trade. About 900 jobs were added in the construction industry— almost 20 percent of the net new jobs in the area. After a decline in the preceding year, housing permits were up more than 45 percent in Lancaster last year. Despite the large

Figure 4
THREE-STATE UNEMPLOYMENT RATES*



PA, NJ, DE, Major Labor Market Areas
First Quarter 1999

*Data are seasonally adjusted by the Federal Reserve Bank of Philadelphia

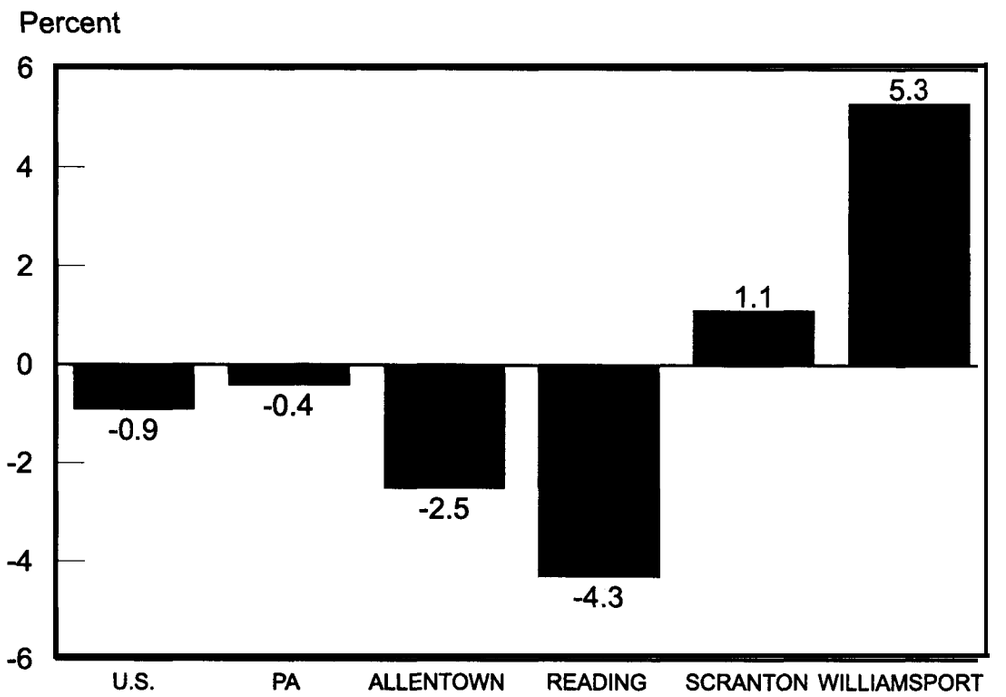
percentage job gain in construction, the largest absolute number of new jobs in Lancaster last year were in nonfinancial services—more than 2000. These new jobs were scattered across a wide range of services, including business support, education, and health. Government jobs declined 1.7 percent on a fourth-quarter-over-fourth-quarter basis, primarily because of cutbacks at the state and local government levels. Lancaster's unemployment rate has been below 3 percent for more than a year. In the first quarter of 1999 it was 2.7 percent; together with State College, Lancaster has the lowest unemployment rate in Pennsylvania.

In the last two years, York has broken with its tradition of being one of the fastest growing economies in the state. Two years ago the metro area had a slight decline in jobs, and last year York had the second slowest job growth in Pennsylvania (1.1 percent). Last year's slow job growth was primarily due to the loss of more than 800 manufacturing jobs (1.7 percent). Large job losses in the industrial machinery and equipment industry swamped small gains in some manufacturing industries. York was able to register overall job gains for the year owing to an increase of more than 1000 jobs in retail trade, about 600 in construction, and almost 400 each in transportation and nonfinancial services. An increase of more than 11 percent in housing permits for the year supported the job growth in the construction industry. Despite York's relatively slow job growth last year, its unemployment rate remained below 4 percent and was the fourth lowest in the state in the first quarter this year.

Reading and the Lehigh Valley

Reading had the slowest job growth of any metropolitan area in Pennsylvania last year (0.7 percent). Overall job growth was hampered by the loss of almost 2000 jobs in the manufacturing sector (4.3 percent), primarily in transportation equipment (Figure 5). The manufacturing losses were more than offset by gains in nonfinancial services (5.4 percent).

Figure 5
MANUFACTURING JOB GROWTH
1997: IV - 1998: IV



Transportation and public utilities firms and local government also had significant job increases, but the construction industry and trade sector lost jobs. Because of slow job growth, Reading's unemployment rate rose in the second half of last year. Growth picked up, however, in the first quarter of this year, and the unemployment rate fell to 4.1 percent.

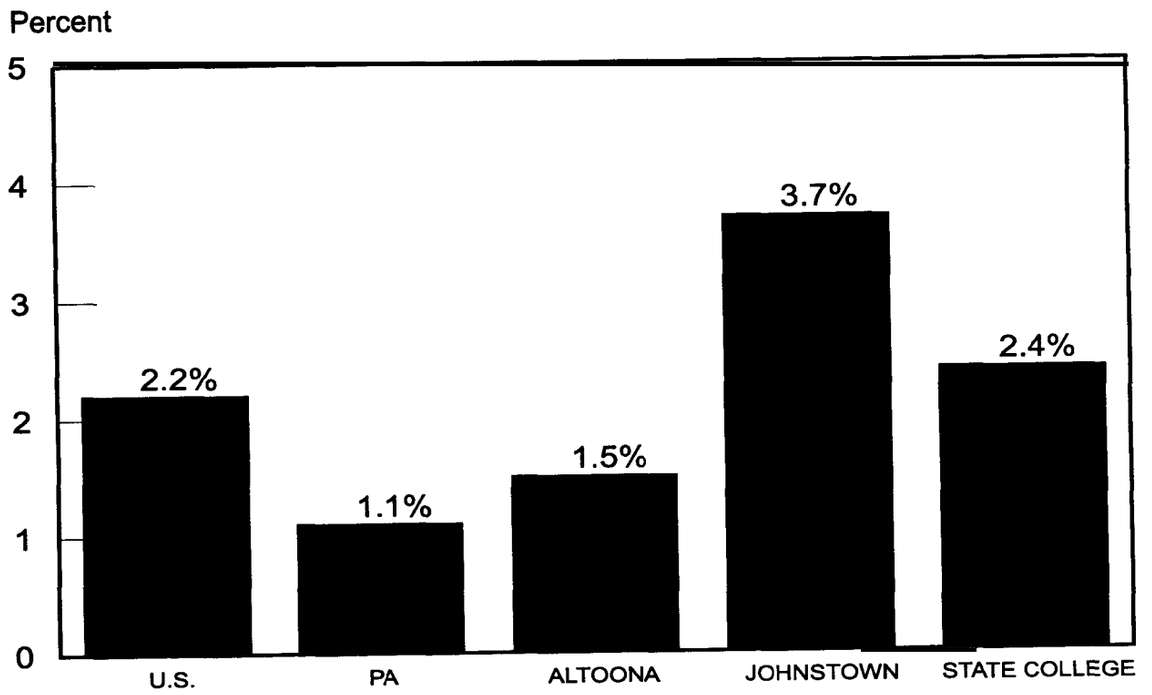
Allentown also had a substantial loss of manufacturing jobs last year (2.5 percent). The 4.1 percent growth in nonfinancial services, however, added more than 3000 jobs to the Allentown economy, most of them in business support services. The trade sector added more than 1500 jobs (3 percent), and financial services added almost 900 jobs (6.6 percent). Despite overall job growth of 2 percent in 1998, Allentown's unemployment rate rose in the second half of the year. But job growth continued at a very strong pace in the first quarter of this year, and the unemployment rate fell to 4.3 percent, slightly below its level a year ago.

Northeastern Pennsylvania and Williamsport

Total nonfarm jobs in the Scranton-Wilkes-Barre area increased 1.5 percent last year with gains across all major industry groups. The largest percentage increase was in construction (3.8 percent), but the largest absolute number of new jobs was in nonfinancial services, which added more than 1300 jobs (1.7 percent). Manufacturing in the Scranton area bucked the state and national trend and added almost 600 jobs (1.1 percent). The manufacturing job growth was concentrated in the durable goods industries. Job levels in the Scranton area continued to increase in the first quarter of this year, but at a slightly slower pace. The area's unemployment rate has been 1 to 2 percent above the state average for most of the decade, and the first-quarter rate was 5.9 percent compared with 4.4 percent for the state.

Williamsport also had job growth of 1.5 percent in 1998, but the growth was not across the board. Financial service

Figure 6
WHOLESALE AND RETAIL TRADE JOB GROWTH
1997: IV - 1998: IV



employment (finance, insurance, and real estate) was flat, and the government sector lost jobs. Nonfinancial services gained less than 100 jobs (0.1 percent). The engine behind Williamsport's growth last year was manufacturing; factory jobs increased 5.3 percent and accounted for almost all the net new jobs in the area (Figure 5). The increases were in both the durable and nondurable manufacturing industries. Total job growth in Williamsport continued in the first quarter of this year, but in contrast to 1998, growth was spread across every major industry group. Williamsport's unemployment rate in the first quarter was 5.1 percent, a percentage point below its level a year ago.

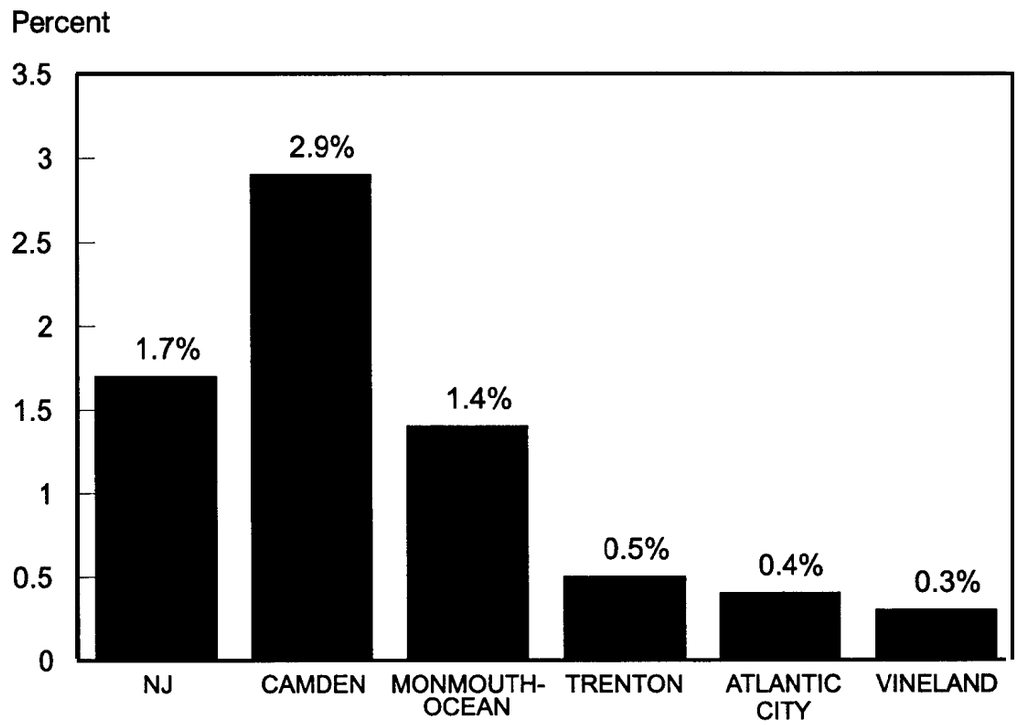
Central and Western Pennsylvania

Because of the presence of the state university, about one third of State College's nonfarm jobs are classified as state government positions, and all levels of government account for almost 40 percent of the jobs in the area. Although government jobs increased only minimally last year, total nonfarm jobs were up a healthy 1.5 percent. The largest percentage increase and greatest number of new jobs were in the manufacturing sector (up 5.5 percent). Trade and nonfinancial services also added a large number of new jobs in the State College area last year. The first-quarter unemployment rate in State College was 2.7 percent, making it—together with Lancaster's—the lowest in the state.

Altoona's job growth last year (1.8 percent) exceeded the state average for the second year in a row. The biggest percentage gain was in construction (6.6 percent). The largest absolute number of new jobs (about 400) were in nonfinancial services. Wholesale and retail trade added more than 200 jobs. Financial service firms (finance, insurance, and real estate) lost a few jobs last year. But in contrast to the state as a whole, the government sector added jobs. In the first quarter of this year job growth in Altoona continued at a brisk pace, and the unemployment rate remained at 4.6 percent, the same as the fourth quarter of 1998.

Jobs in Johnstown increased 1.4

Figure 7
NONFARM JOB GROWTH
1997: IV - 1998: IV



percent in 1998, more than reversing the losses of the previous year. The biggest gains in both absolute and percentage terms were in wholesale and retail trade (Figure 6). There were also substantial job gains in nonfinancial services and manufacturing (1.6 percent in both). New manufacturing jobs were concentrated in the durable goods industries. There were some minor job losses in the financial service industries (finance, insurance, and real estate), but the sector regained these jobs in the first quarter of this year. Total nonfarm jobs in Johnstown increased strongly in the first quarter, and the unemployment rate was 6.2 percent, almost a percentage point below its level a year ago.

Central and Southern New Jersey

Job growth among the central and southern New Jersey labor markets varied widely last year from almost 3 percent in the Camden labor market to 0.5 percent or less in Trenton, Atlantic City and Vineland (Figure 7).

The Camden labor market, which includes Burlington, Camden, and Gloucester counties, is part of the Philadelphia metropolitan area, but it is the largest labor market in southern New Jersey. Last year, jobs in the Camden area increased 2.9 percent on a fourth-quarter-over-fourth-quarter basis. The broad financial service sector (finance, insurance, and real estate) grew 8.6 percent, despite the loss of jobs at banks and other depository institutions. Construction jobs in the Camden market increased more than 6 percent. But the largest absolute number of new jobs was in wholesale and retail trade (more than 4000 jobs) and nonfinancial services (more than 5000 jobs). Jobs in both these sectors increased more than 3 percent. The manufacturing sector lost jobs, but at a much slower rate than the state as a whole. After rapid growth in 1998, job growth in the Camden labor market slowed down in the first quarter of this year.

Last year Monmouth-Ocean had its slowest job growth since 1991, but the area's growth rate was still solid. The loss of more than 1000 jobs in manufacturing

Figure 8
STATE FORECASTS

	PA	NJ	DE
Nonfarm Job Growth 1998: IV to 1999: IV	1.1%	1.6%	2.3%
Real Personal Income 1998: IV to 1999: IV	1.7%	2.5%	2.5%
Unemployment Rate Level 1999: IV	4.5%	4.4%	3.5%
Housing Permits Annual Change 1998-1999	-3.1%	-0.6%	-0.8%

and more than 600 in the government sector kept overall job growth at 1.4 percent, somewhat below the state average. The manufacturing losses were concentrated in the nondurable goods industries, especially chemicals. The government job losses were about equally divided between the federal and state levels. Monmouth-Ocean was able to maintain respectable job growth primarily because of an increase of more than 5500 jobs in nonfinancial services (4.5 percent). The construction industry also added more than 400 jobs (2.4 percent). Housing permits were up more than 14 percent last year after increasing 15 to 20 percent in the previous two years. Job growth in Monmouth-Ocean was very rapid in the first quarter of this year, and the unemployment rate fell to 4.1 percent, more than a half percentage point below its level a year ago.

The Trenton labor market had job growth of only 0.5 percent in 1998. The major hindrance to faster overall growth was the 10.3 percent decline in manufacturing jobs, most of them in the durable goods industries. The government sector lost more than 700 jobs (1.4 percent), most of them at the state level. Only the nonfinancial service sector had strong job gains in the Trenton labor market last year (4.4 percent). Among the nonfinancial services, business support services gained about 900 jobs (6.8 percent). Trenton's job market weakened further this year with job losses in the first quarter. Nevertheless, the area's 4.0 percent unemployment rate remains lower than the state average.

The Atlantic City labor market (Atlantic and Cape May counties) had meager job growth of 0.4 percent last year. The only major sector with any substantial increase in jobs was nonfinancial services (1.6 percent), and almost none of that growth was among casino hotel workers. The wholesale and retail trade sector was the only other sector with any job gains last year (0.6 percent). Financial service jobs (finance, insurance, and real estate) declined 1.1 percent, primarily because of a loss of about 300 jobs at banks and other depository institutions. Job growth in Atlantic City picked up strongly in the first quarter of this year, and the unemployment rate dropped below 8 percent for the first time since 1990.

Vineland had the slowest job growth of any labor market in New Jersey last year (0.3 percent). The area gained less than 200 jobs on a fourth-quarter-over-fourth-quarter basis. The only sectors with any substantial growth were nonfinancial services and government. Each had job growth of more than 3 percent and added more than 400 jobs. All the new government jobs were at the state and local levels. The construction industry had a large percentage gain (8.6 percent) but added less than 200 positions. Vineland had substantial job gains in the first quarter of this year, but the area's unemployment rate (8 percent) is still the highest in the state.

The Delaware Labor Markets

Jobs in the Wilmington labor market grew 3 percent last year, mostly on the strength in trade and financial and nonfinancial services. Nonfinancial services created the greatest number of new jobs (almost 4000), and growth occurred across most subcategories of nonfinancial services, including business support, health, legal, management, and social services. Among financial service firms, banks and other depository institutions added about 600 jobs. Wilmington's manufacturing sector added 800 jobs on a fourth-quarter-over-fourth-quarter basis, about half of them in transportation equipment. Overall job growth continued at a rapid pace in the first quarter, and Wilmington's unemployment rate fell to 3.2 percent, its lowest level in more than two decades.

Nonfarm jobs in Dover increased 5 percent last year on a fourth-quarter-over-fourth-quarter basis, and every major job category recorded some growth. Wholesale and retail trade was the weakest sector with 0.5 percent job growth, and construction was the strongest growing sector (11.5 percent). Nonfinancial services, which grew 6.9 percent, added the largest number of jobs (about 800). Even government jobs in Dover increased almost 6 percent. All the new government positions were at the state and local levels, and most of them were in education. Dover's job market continued to grow strongly in the first quarter of this year, and the unemployment rate dropped to 3.5 percent.

Outlook for the Region

Job growth in the tri-state region slowed in 1998, but the state unemployment rates still declined to their lowest levels in almost 10 years. We are projecting a slight slowdown in job growth in each of the three states on a fourth-quarter-over-fourth-quarter basis this year (Figure 8). In the first quarter of 1999 jobs in New Jersey grew at the rate we projected. Jobs in Pennsylvania grew at an annual rate below 1 percent and slower than our projections. In Delaware, jobs in the first quarter grew at a 4.5 percent annual pace, about twice the rate we projected. But this rate is unsustainable given the state's low unemployment rate.

The housing sector was strong in 1998. We are forecasting permits to level off this year with only small declines in each of the three states. Real personal income is projected to climb 1.7 percent in Pennsylvania and 2.5 percent in both New Jersey and Delaware this year. The state unemployment rates are projected to dip slightly in the first half of 1999, but by the end of the year, they should be little changed from their levels in the fourth quarter of 1998.

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