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EFFECTS OF BRAND VALUE ON STOCK RETURN IN INDONESIA

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**Abstract.** We study the relationship between brand value and stock return in Indonesian market, using brand value published in annual reports by Brand Finance between 2014-2020. Using the capital asset pricing model (CAPM) and Fama-French plus momentum factor, we find that brand value does not have positive effects on stock returns. Portfolio of stocks with higher brand value does not yield higher return and lower risk compared to benchmark portfolio. Further analysis also shows that brand values published by Brand Finance are not fully reflected in Indonesian market.

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**Abstrak.** Kami mempelajari hubungan antara nilai merek dan pengembalian saham di pasar Indonesia, dengan menggunakan nilai merek yang diterbitkan dalam laporan tahunan oleh Brand Finance antara 2014-2020. Dengan menggunakan model penetapan harga aset modal (CAPM) dan faktor Fama-French plus momentum, kami menemukan bahwa nilai merek tidak berpengaruh positif terhadap return saham. Portofolio saham dengan brand value yang lebih tinggi tidak menghasilkan return yang lebih tinggi dan risiko yang lebih rendah dibandingkan portofolio benchmark. Analisis lebih lanjut juga menunjukkan bahwa brand value yang diterbitkan oleh Brand Finance tidak sepenuhnya tercermin di pasar Indonesia

## INTRODUCTION

One of the topics that have attracted the attention of researchers for many years is about marketing activities and its impact on financial performance. Marketing activities are a component of brand building, therefore brands have a crucial role in determining the effectiveness of marketing activities. Top leaders in business have prioritized brand development over the last decade, understanding that brands are among the most precious intangible assets (Keller & Lehmann, 2006). In marketing literature, the term “brand equity” was coined in attempt to describe the connection between brands and customers (Wood, 2000). According to concept of brand equity by Aaker (1991), it is composed of privately-owned brand assets such as , brand awareness, perceived quality, brand association, brand loyalty and others. Based on the same study, it is also argued that brand equity generates value to firm, it is also implied that strong brand equity creates financial benefits for firms. Subsequent studies (Crass et al., 2019; Fischer & Himme, 2017; Krasnikov et al., 2009) also proved how brand equity affects the value and performance of a firm.

Study conducted by Aaker & Jacobson (1994) shows a positive correlation between changes in stock return and quality perceptions, strengthened the result provided by Aaker (1991) that stated brand equity has positive impact for firms on financial aspect. Barth et al. (1998) found that estimates of brand value are reflected in share price of a firm, and brand value are positively related to market share, advertising expense, and operating margin. Madden et al. (2006) discovered that stocks with strong brand valuation outperformed the overall market with less risk. According to Fehle et al. (2008), stocks with strong brand yield returns that are significantly higher than average. Additionally, Hsu et al. (2013) demonstrated positive correlation between stock performance and brand value. All the studies mentioned proved a positive connection between stock returns and brand value, however these studies are relatively limited to companies that are listed on AMEX, NYSE, and NASDAQ, and hence the results need to be evaluated in different markets as mentioned in study by Bank et al. (2020).

Similar studies with related topic were conducted in Turkish stock market. Study by Bank et al. (2020) analyses the brand value from annual reports issued by Brand Finance between 2007-2015 to investigate the relationship between brand value and stock return. According to the study’s findings, portfolio of stocks with strong brand value provides significant higher abnormal returns while being less risky than portfolios with weaker brand value. Bank et al. (2020) mentioned several studies related to the topic in their paper: Basgoze et al. (2016) demonstrated firms with strong brand outperformed the market in Turkey, and Bayrakdaroğlu & Mirgen (2016) found positive correlation between stock returns and brand value in Turkish stock market.

Inspired by the studies conducted by Madden et al. (2006), Fehle et al. (2008), and Bank et al. (2020), the aim of this study is to investigate the relationship between brand value and stock returns of companies listed in the Jakarta Composite Index (ISHG), Indonesia. This study is conducted by using the brand valuation of Indonesian firms released by Brand Finance, in an annual ranking called “top 100 most valuable companies in Indonesia” that are reported in SWA magazine. The reason that this study uses the data published by Brand Finance is mainly because Brand Finance is the only independent brand valuation consultancy that annually published the top 100 most valuable companies for Indonesian market since 2013. We construct a portfolio of stocks whose firms are included in the report, while stocks that are not included in the report will be included in a different portfolio that will be used as a benchmark for comparison. We also use

Sharpe-Lintner capital asset pricing model and Fama French with momentum factor model for further analysis.

## LITERATURE REVIEW

### **Brand Value and Stock Return**

Assets of a firm are categorized as tangible and intangible assets. Typically, tangible asset is asset with physical form and finite monetary value. Intangible asset is a non-monetary asset that lacks physical form in nature. Intangible assets allow firms to generate cash flows that exceed the return on tangible assets, while also increase earning power of physical assets of the firm (Simon & Sullivan, 1993). Kotler & Keller (2016) defined brand as a symbol, name, design, sign, term, or mix of them, which distinguishes a seller from the competitors, and they argued that for firms to manage their value properly, it is incumbent to realize brand as one of the most valuable intangible assets. To strengthen the argument that brand is one of the most valuable intangible assets, Lane & Jacobson (1995) argued that brand names have the ability to create earnings above the earnings generated by tangible assets. Intangible assets of firm, according to Simon & Sullivan (1993), include patents, franchises, research and development (R&D), trademarks, goodwill, and brand equity. Firms can earn marginal cash flow generated by brand equity in a variety of ways, such as attract new customers and recapture old customers by enhancing programs, provide leverage in the distribution channel, supports premium pricing, provide growth by brand extensions, enhance brand loyalty, and provide competitive advantage over competitors (Aaker, 1991).

The term "brand equity" has become one major and important topic for the past few decades as an intangible asset. Among researchers, there are multiple definitions of brand equity, but in literatures it has been looked on from consumer-based perspective, financial perspective, or the combination of them (Kim et al., 2003). There are numerous widely accepted definitions of customer-based perspective brand equity. Farquhar (1989) defines brand equity as the added value that brands endow to products. According to Aaker (1991), brand equity is a set of liabilities and brand assets associated with name and symbol of a brand, that increase or decrease a product value or service value to a firm and/or to its customers. Brand equity, as described by Keller (1993), is the difference between how customers respond to a brand's marketing when they are aware of it. Feldwick (1996) defined brand equity in three distinct concepts: brand valuation (brand value), which is a brand's total value as a separable asset whether an asset is sold or listed as an asset on the balance sheet; brand strength, which is a measurement of how attached a customer to a brand; brand description, that describes the consumer's associations and beliefs of a brand. Marketers often use "brand equity" to mention about brand strength or brand description (Wood, 2000). From financial perspective, brand equity is described as incremental cash flows of branded products on top of the sale of unbranded products Simon & Sullivan (1993). A firm's market value provides an estimate of future cash flows that are accountable to all assets of the firm, and hence the value of brand equity is extracted from the market value, separating brand equity from other firm's assets (Simon and Sullivan, 1993). From the combination perspective that incorporate both customer-based and financial perspective, Anderson (2007) proposed that brand equity is a financial value gained from the customer reaction to a brand's marketing activity. Study by Conchar et al. (2005) found positive relationship between promotional

spending and advertising of a firm and the firm's market value. As mentioned in study by Bank et al. (2020), the combined perspective provided opportunities for Brand Finance as a consulting firm to develop brand valuation methods that include both consumer-based and financial perspective.

Simon & Sullivan (1993) argued that the increased brand equity's value is included in the expected future returns. Study by Aaker & Jacobson (1994) discovered positive correlation between changes in quality perceptions and stock return. Quality measures include information about future-term performance. A product quality measure has explanatory power that is comparable to ROI, and this relation between perceived product quality and stock return is an encouragement for those who seeking to justify investing in product quality (Aaker & Jacobson, 1994). Kerin & Sethuraman (1998) provided an empirically validated positive relationship between market-to-book (M/B) ratio and brand value of firms. Barth et al. (1998) found significantly and positively relation of brand value estimates and stocks prices and returns. Srivastava et al. (1998) developed a conceptual framework that linked market-based assets (which include brands) to shareholder value. In line with those studies, Madden et al. (2006) showed that firms with strong brand deliver higher returns with less risk. Fehle et al. (2008) found strong brand firms deliver significant above-average returns, economically and statistically. Mizik & Jacobson (2008) concluded that brand assets influence the firm's financial performance in the future. Hsu et al. (2013) demonstrated positive correlation between stock performance and brand value. Kirk et al. (2013) found that brand valuation and stock prices are related significantly on contemporaneous basis and on one year time-lagged basis. Belo et al. (2013) demonstrated that firms with more brand capital intensive activities outperform firms with less brand capital intensive activities in terms of average stock returns. More recent studies in Turkish stock market also provided similar results. Basgoze et al. (2016) found stocks that have higher brand value generate abnormal positive returns. Bayrakdaroglu & Mirgen (2016) found positive correlation between stock returns and brand value. Bank et al. (2020) discovered that portfolio of stocks with strong brand may deliver significantly abnormal returns while also posing significantly lower risk. All the findings in the studies mentioned indicate that brand value has positive correlation with price and return of stocks, and thus the following hypothesis is established:

**H1: Brand value has positive effects on the stock return.**

## DATA AND METHODOLOGY

Following previous studies by Madden et al. (2006), Fehle et al. (2008), and Bank et al. (2020), this study is using the brand valuation published by independent company. There are several companies that are well known for their brand valuation and evaluation consulting service, such as Kantar, Interbrand, Brand Finance, etc. These companies annually published rankings of the most valuable brands in the world. This study aims to show the relationship between brand value and stock returns in Indonesian market, therefore we use the brand values provided by Brand Finance, as the only one of the mentioned companies that release "the top 100 most valuable companies" annual reports for Indonesian market. Since we couldn't access the data published by Brand Finance directly, the annual reports are collected from SWA magazines. By the time this study is conducted, Brand Finance has published the annual reports for Indonesian market from 2013-2020, but it is quite unfortunate that SWA magazine is only able to provide the data

from 2014-2020, hence the data of 2013 and 2021 are excluded from this study. Companies that owned two or more brands that are listed in the annual reports, thus in this case the company should only be counted as 1 (one) for each year. The monthly stock price and return are obtained from database provided by S&P Capital IQ and Indonesian Stock Exchange website ([www.idx.co.id](http://www.idx.co.id)). In this study, the risk-free rate represents the monthly return of Indonesian 10-Year Bond (Indonesia 10Y). Delisted company are excluded from this research due to data limitations.

Companies that are listed in both the Indonesian Composite Index (IHSG) and the annual ranking reports are considered as “Strong Brand Portfolio” (SB portfolio), while companies will be included in “Weak Brand Portfolio” (WB portfolio) if they are listed in IHSG but not the annual reports. Following Bank et al. (2020), once the portfolios of strong and weak brand are constructed, the following step is to apply value weighting (VW) and equal weighting (EW) method to all portfolios. Another portfolio, which is basically a modified SB portfolio, is constructed according to brand value and will be called as MVIB (most valuable Indonesian brand) portfolio. The purpose of MVIB portfolio is to prove whether the stock returns of strong brand firms are influenced by the brand value published by Brand Finance, by comparing it with other benchmark weighted portfolios. For this MVIB weighted portfolio, each company’s brand value in the annual reports is divided by the total sum of brand values for each year. As the result, brand value for every company in every related year could be obtained.

### Empirical Model

Following Bank et al. (2020) and Madden et al. (2006), to further analyse the data in this study, the regressions that will be used are the Sharpe-Lintner capital asset pricing model (CAPM) and Fama French with momentum factor model. CAPM with its simple logic and prediction often used to describes the relationship and risk measurement between risk and expected return (Fama & French, 2003). The CAPM implies that an asset’s average excess return (return minus risk-free interest rate,  $R_{it} - R_{ft}$ ) is expounded by the average CAPM risk premium (beta times averages value of  $R_{mt} - R_{ft}$ ). This suggests that the intercept termed as “Jensen’s alpha” in time series regression for each asset is zero (Fama & French, 2004). The CAPM is written as follows:

$$R_{it} - R_{ft} = \alpha_i + \beta_{im}(R_{mt} - R_{ft}) + \varepsilon_{it}$$

Where:

$R_{it}$  = return of portfolio i at time t

$R_{ft}$  = risk-free rate of return at time t

$R_{mt} - R_{ft}$  = excess return on market portfolio

The CAPM itself has been an object full of criticism for many years. Many studies have been conducted regarding the limitations of CAPM and these studies have led to the conclusion that the lack of empirical successes are fatal. Further studies were conducted in response to this issue, thus Fama and French (1993) introduce a more complicated model to describe expected returns, which widely known as the three-factor model. The equation of the model is written as follows:

$$R_{it} - R_{ft} = \alpha_i + \beta_{im}[R_{Mt} - R_{ft}] + \beta_{is}SMB_t + \beta_{ih}HML_t + \varepsilon_{it}$$

The momentum effect of Jegadeesh & Titman (1993), as mentioned by Fama and French (2004), is the three-factor model’s biggest problem. One of the responses by Carhart (1997) is to incorporate momentum into the three-factor model, therefore the following formulation of the model is used:

$$R_{it} - R_{ft} = \alpha_i + \beta_{im}[R_{Mt} - R_{ft}] + \beta_{is}SMB_t + \beta_{ih}HML_t + \beta_{iu}UMD_t + \varepsilon_{it}$$

Where:

$SMB_t$  = difference between return small and large stock portfolio returns.

$HML_t$  = difference between return on high book-to-market stocks portfolio and return on low book-to-market stocks portfolio.

$UMD_t$  = difference between the returns on the highest and lowest performing stocks

## RESULTS

The base of SB portfolio includes 113 companies that appear at least once in “top 100 most valuable companies” annual reports for Indonesian market during 2014-2020. Out of the 113 companies, 2 companies in the list have been delisted from Indonesian Stock Exchange, and thus excluded from the portfolio due to data limitation. Therefore, the total number of companies in the portfolio are 111 companies, which on average, brand values estimated by Brand Finance composed 24.47 percent of a company's market capitalization with standard deviation of 37.57 percent.

In order to assess the performance of stocks in SB portfolio, we evaluate and compare the performance of portfolio of strong brand companies and the portfolio of weak brand companies. The value and equal weighting methods are used to construct portfolios of both strong and weak brand companies. The historical returns of these portfolios, value and equal weighted, are respectively illustrated in Figure 1 and Figure 2. The historical return of the market (IHSG) is included in both illustrations as comparison.

Figure 1 – Monthly SB and WB Portfolios with Value Weighting

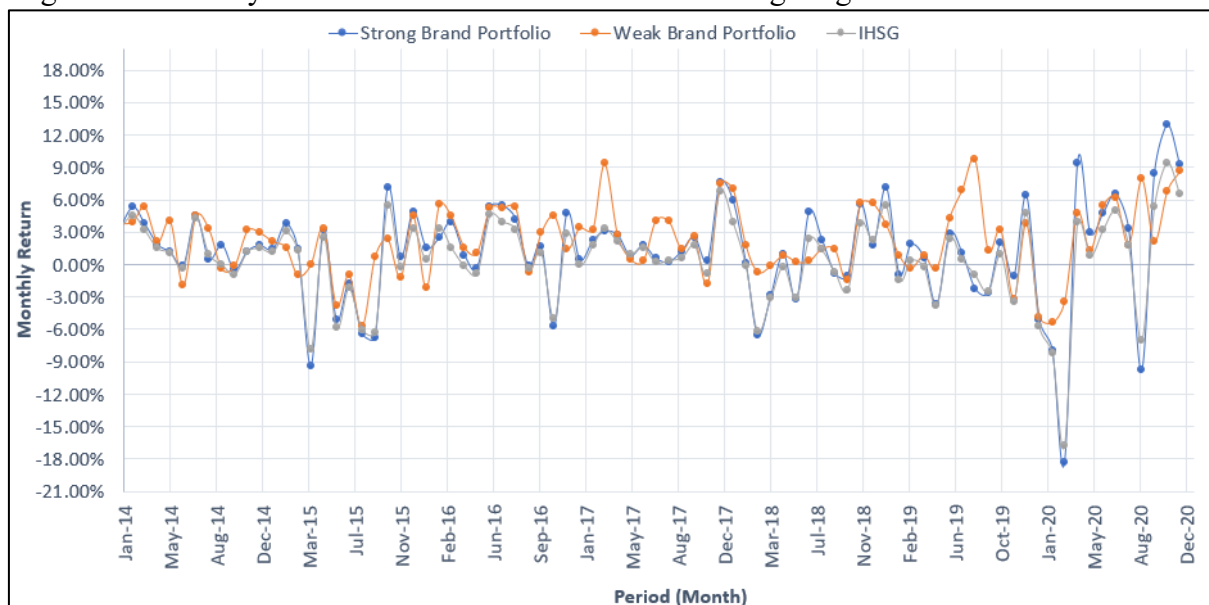
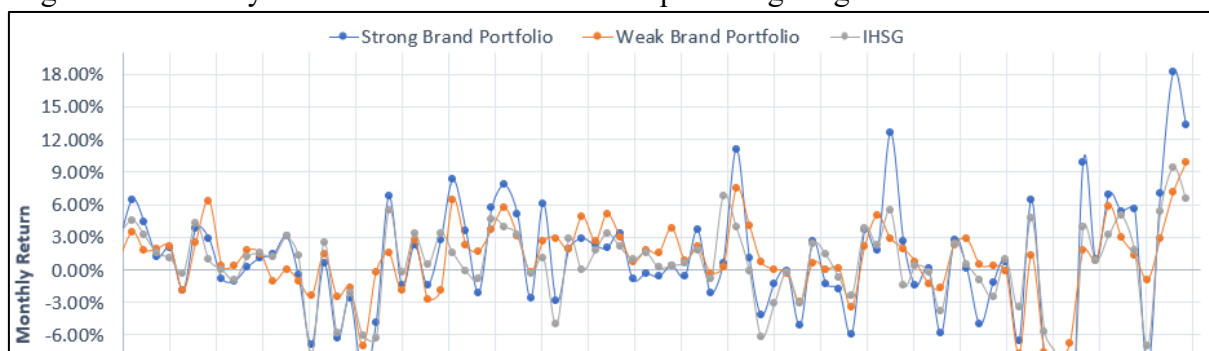


Figure 2 – Monthly SB and WB Portfolios with Equal Weighting



Based on the two time series graphs, although couldn't be considered a pattern, one visible point is that SB portfolio has more negative returns compared to WB portfolio. The statistical calculation results show that value weighted SB portfolio yielded average monthly returns of 1.19 percent and equal weighted SB portfolio on monthly average returned 0.85 percent. Meanwhile, with the same period, value and equal weighted WB portfolio returned 2.26 percent and 1.01 percent per month, respectively. Both SB and WB portfolio shows higher return than the market, which yielded average monthly returns of 0.48 percent, but the WB portfolio on average yielded higher returns. The standard deviation of SB portfolios are 4.71 percent for value weighted and 5.61 percent for equal weighted, while WB portfolios are 3.26 percent for value weighted and 3.30 percent for equal weighted. From the descriptive statistics, WB portfolios show not only higher monthly average return but also less risk compared to SB portfolios. The statistic results are presented in Table 1.

Table 1 – SB and WB Portfolios' Monthly Returns (Summary Statistics)

	Value Weighted Return		Equal Weighted Return	
	Strong Brand	Weak Brand	Strong Brand	Weak Brand
Mean	0.0119	0.0226	0.0085	0.0101
Standard deviation	0.0471	0.0326	0.0561	0.033
Median	0.0165	0.0214	0.0079	0.0137
Max	0.1290	0.0969	0.1818	0.0986
Min	-0.1826	-0.0576	-0.2022	-0.0866
Observations	84	84	84	84

The values in Table 1 are obtained from monthly returns data. The average return for SB portfolios, value and equal weighted, are lower than the WB portfolios, and at the same time, the standard deviation of SB portfolios are higher than the WB portfolios, in the same weighting method. These statistics are implying that the WB portfolios provide higher returns with lower risk compared to the SB portfolios. For further analysis, we use CAPM and Fama French regressions to provide better assessments. The results of regression for SB portfolio and WB portfolio, value and equal weighted, are presented in Table 2.

Table 2 – Results of Regressions for SB and WB Portfolios

	Value Weighted	Equal Weighted
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	Strong Brand		Weak Brand		Strong Brand		Weak Brand	
	CAPM	Fama French	CAPM	Fama French	CAPM	Fama French	CAPM	Fama French
Alpha	0.0073 (6.88)***	0.0084 (7.01)***	0.0171 (6.13)***	0.0142 (4.35)***	0.0040 (1.45)	0.0010 (0.42)	0.0047 (1.78)*	-0.0024 (-0.93)
Market	1.1626 (43.61)***	1.0852 (29.89)***	0.5170 (7.31)***	0.5769 (5.83)***	1.2620 (17.96)***	1.049 (14.12)***	0.5702 (8.50)***	0.6956 (8.74)***
SMB		-0.1278 (-2.11)***		0.3005 (1.82)*		-0.0376 (-0.30)		0.6185 (4.65)***
HML		-0.0294 (-0.88)		0.1137 (1.25)		0.30156 (4.42)***		0.3215 (4.40)***
UMD		-0.0675 (-2.31)**		-0.1486 (-1.87)*		-0.2942 (-4.93)***		-0.2258 (- 3.53)***
Adj. R <sup>2</sup>	0.9582	0.9621	0.3873	0.4143	0.7949	0.08879	0.4617	0.6297
Observations	84	84	84	84	84	84	84	84

Note: SMB = difference between returns of small and large firms' portfolios; HML = difference between returns on high and low book-to-market ratio portfolios; UMD = momentum. \*\*\*, \*\*, and \* indicates level of significance at <1%, <5%, and <10% respectively.

The results of regressions show that WB portfolios have higher alphas compared to the SB portfolio, except for Fama French regression with equal weighting method. The value weighted portfolio returns also statistically more significant than the equal weighted portfolios, with most of the equal weighted portfolios show insignificant results, except for equal weighted WB portfolio CAPM regression. In line with the descriptive statistics, the WB portfolios also display lower market risk than the SB portfolios, with all highly significant results. So far, the WB portfolios are shown to yield higher returns with less risk, which contrary with the founding by Bank et al. (2020). The different results might possibly because of the difference in market. This study is using data from Indonesian stock market, while other studies are researching different market, thus might lead to different results.

For further analysis, the betas of the other factor in the Fama French model are examined. The SMB betas are highly significant for value weighted SB portfolio and equal weighted WB portfolio, with insignificant result for equal weighted SB portfolio. Negative SMB betas in SB portfolios indicate that the SB portfolios are constructed of large stocks, with the returns vary more with other large stocks than with small stocks. HML betas are highly significant in equal weighted portfolios, while not significant in value weighted portfolios. All HML betas are positive, except for value weighted SB portfolio which has negative HML beta. According to Madden et al. (2006), the negative HML beta implying that brand values, due to accounting rules/conventions, are not reflected in the book value, although it should be reflected in the market value. The UMD betas are negative and significant for all portfolios. All these findings, however, do not provide much explanation related to market risk and returns of the portfolios.

### Robustness Analysis

Despite all the above findings, the impact and magnitude of brand value on stock returns still has not yet taken into account. Following Bank et al. (2020), Fehle et al. (2008), and Madden et al. (2006), a new portfolio formed by using the brand values by as the new portfolio weight. This new portfolio is a reconstructed portfolio of stocks with strong brand that rebalanced annually



based on the brand value. Each company’s brand value in the annual reports is divided by the total sum of brand values for each year. By doing this, each company's brand value for the related year could be found. This new portfolio will be called MVIB (Most Valuable Indonesian Brand) portfolio. The time series graph of MVIB portfolio are shown in Figure 3 and Figure 4, with Figure 3 has historical market return (IHSG) included as comparison and Figure 4 includes SB portfolios with value and equal weighting as comparison.

Figure 3 – Monthly MVIB (Most Valuable Indonesian Brand) Portfolio (1)

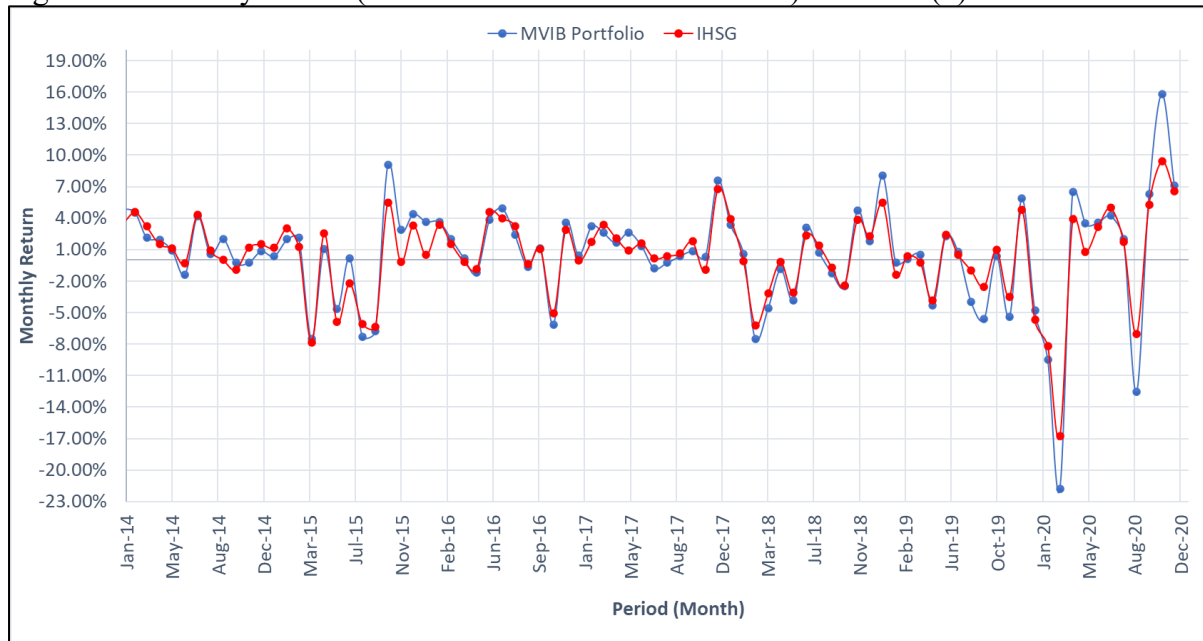
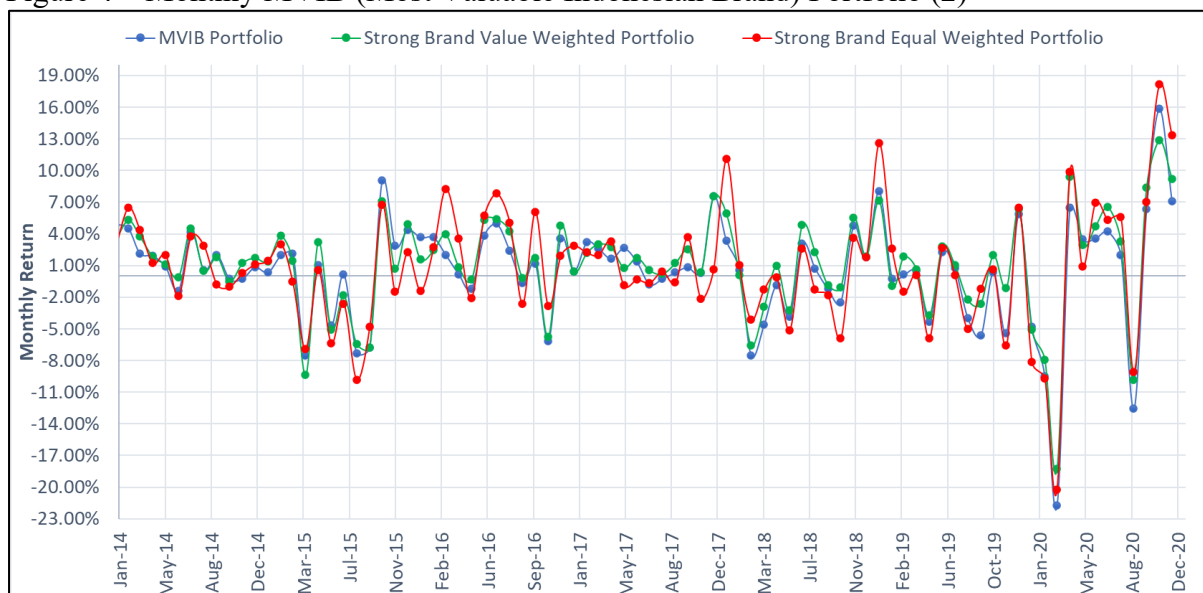


Figure 4 – Monthly MVIB (Most Valuable Indonesian Brand) Portfolio (2)



From Figure 3 and Figure 4 show that there are no major differences between the MVIB portfolio and the other value and equal weighted SB portfolios. The statistics, however, show that MVIB portfolio yielded average return of only 0.55% and standard deviation of 5.02%. This means that MVIB portfolio yields the lowest return compared to the other portfolios, and with higher risk compared to most portfolios, only second to equal weighted WB portfolio. The MVIB portfolio

also yields return of -21.75%, which is the lowest among all portfolios. The summary statistics of MVIB portfolio is shown in Table 3.

Table 3 – MVIB Portfolio (Summary Statistics)

MVIB Portfolio	
Mean	0.0055
Standard deviation	0.0502
Median	0.0089
Max	0.1584
Min	-0.2175
Observations	84

The statistics from Table 3 lead to several possibilities, that the brand values published by Brand Finance have negative effects on returns or the brand values are not priced in the market. For further analysis, we also conduct regression using CAPM and Fama French for MVIB portfolio, and the results are displayed in Table 4.

Table 4 – Results of Regressions for MVIB Portfolio

	MVIB Portfolio	
	CAPM	Fama French
Alpha	0.0010 (0.61)	0.0012 (0.64)
Market	1.2110 (30.37)***	1.1535 (20.25)***
SMB		-0.0736 (-0.77)
HML		0.0201 (0.38)
UMD		-0.0440 (-0.96)
Adj. R <sup>2</sup>	0.9174	0.9167
Observations	84	84

Based on Table 4, the alphas for both regressions are lower than any other portfolios, only roughly the same as Fama French regressions of equal weighted SB portfolio. More than that, the alphas for both regressions are also insignificant. These particular findings are contrary to Madden et al. (2006) and considerably consistent with Bank et al. (2020), that portfolio based on brand values yield lower returns. The market risk of MVIB portfolio, especially in Fama French regressions, are significantly higher than the other portfolios, while in CAPM regression its only below equal weighted SB portfolio, which has the highest risk. The findings about the risk in this research is contrary to both Madden et al. (2006) and Bank et al. (2020). All other Fama French factors also show insignificant results.

With these results, it is confirmed that portfolio based on brand values does not yield higher returns and does not have lower risk. It is also can be confirmed that by using brand values as the weight for portfolios, the brand values are not reflected in the market. These findings imply that brand values do not have positive impact on stock returns in Indonesian market, however, it does not mean that brand values have negative impact on stock returns. The reason why WB portfolios

have better performance, in term of return and risk, compared to SB portfolios might be because of other factors. The results of this research may also be impacted by the insufficiency of the asset pricing models that were used to explain the returns.

## CONCLUSION

Inspired by Bank et al. (2020) and Madden et al. (2006), we conducted study in Indonesian market about correlation stock returns and between brand value. We constructed portfolio of stocks that are included in annual reports for the period of 2014-2020 that are released by Brand Finance, which called the strong brand (SB) portfolio by using the monthly stock returns. We also constructed another portfolio for benchmark called the weak brand (WB) portfolio, that consisted of all the remaining stocks in Indonesian stock index but not mentioned in Brand Finance's annual report. Summary statistics of the research displayed that SB portfolio generates lower return with higher risk compared to WB portfolio. Analysis using CAPM and Fama French model showed that WB portfolio significantly yields higher return with market value weighting, less significant or insignificant with equal weighting, and with significantly lower risk in all weighted portfolios. When we reconstructed the portfolio of stocks with brand according to brand value, the MVIB portfolio, the alpha for CAPM and Fama French model are both insignificant with significant higher market risk compared to other portfolios with different weighting methods.

Based on our findings, it is implied that portfolio of stocks with higher brand value does not yield higher returns and does not provide lower risk, which are contrary to Bank et al. (2020) and Madden et al. (2006). Brand value do not have positive impact on stock return in Indonesian market. One thing that should be taken as consideration is the possibility that the Brand Finance's brand values are not fully reflected in Indonesian market. It is also possible that the results are influenced by the insufficiency of the asset pricing models used in this study to explain the returns. More detailed explanation of why brand value in Indonesian market does not give positive impact on stock returns or what other factor that may influence the results of this study, could be used as a basis for further study.

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