

## Greece: Third Bailout Not To Be Agreed Until Mid-Year

Today's News in Detail | Latest Issues of Sovereign Debt Update |  
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### Summary

**Greece – third bailout package under discussion but not to be agreed until mid-year.** Germany ready to put together a new package for €10-€20bn, but no decision is likely before May EU elections. Greece says ready to accept a new bailout only if it encompasses merely “*structural measures*”, not additional austerity.

**ECB AQR press conference reveals few new details.** ECB Vice President Constancio and the chairwoman of the ECB Supervisory Board Nouy affirmed that the ECB would carry out a “*demanding and very rigorous*” bank assessment.

**ECB President Draghi to seek public Bundesbank support for ending SMP sterilization.**

**ECB's Lautenschläger promotes SSM in front of European Parliament,** noting that the single supervisory mechanism (SSM) should be able to spot risks in the European banking system more quickly.

**Juncker to be main centre-right candidate for European Commission President.**

**Germany to offer limited support for EU treaty renegotiation.**

**French expenditure review process starts in earnest and corporate tax reform discussions continue.**

**Italy – Q4 13 GDP growth at 0.2-0.3% QQ, Labour Minister says,** amid strong growth in manufacturing, while construction and services are still suffering.

**Italy – state sector cash balance posts surplus of €0.8bn in January,** on higher tax revenues (property tax introduced in January and good VAT receipts).

**Spain – Manufacturing PMI rose to 52.2 in Jan, employment PMI exceeds the 50 threshold for the first time since October 2010.**

**Spain – Registered unemployment rises by 113k in January** on seasonal factors, continues to decline in adjusted terms.

**Spain – Electricity prices to rise a further 0.2% in February,** adding to the 2.3% rise in January, according to daily EI Economista.

**Spanish data – Car sales rose by 7.6%YY in Jan** vs. 18.2%YY in Dec, Anfac data showed. **Consumer confidence up by 6.7pts in Jan to 77.7, a new record high.**

**Slovakia – Solid fiscal revenue performance continues in January.** Dynamics in EU funds inflow and tax collection will be key for another outperformance of the budget in 2014.

4 February 2014

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With thanks to Antonio Montilla

Economics

Western Europe

Industrialised G7 Countries

### Recent Research

#### Euro Area — Assessing Vulnerabilities to an EM Slowdown

3 February 2014

Exports of goods to EM countries as pct of GDP are highest in Belgium, Netherlands, Germany, Austria, Italy, Greece and Switzerland. Of course, any adverse effects on growth from an EM slowdown may be cushioned in part by a real income boost if prices of imported commodities weaken, but this effect is relatively even across economies.

Michael Saunders

#### ECB Preview — ECB Likely to Resist Pressure to Act at February Meeting

31 January 2014

The Jan HICP (0.74% YY) increases pressure on the ECB. But we believe that it is unlikely to cut in its refi. rate just yet, preferring to wait for March to review its forecasts and whether to adjust its policy stance. We still forecast

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## Today's News in Detail

### Greece – third bailout package for Greece not decided until mid-year.

Bloomberg reported yesterday the German Deputy FinMin Steffen Kampeter saying that a third bailout programme for Greece is a possibility, but that the decision would not be taken before the end of April/May when all the necessary data will be available. Kampeter said the size of the new package will be way smaller than the previous two bailouts and added that Germany's priority is to have Greece returning to market financing as soon as possible. A German FinMin spokesman said the timing of a third bailout could be mid-2014, while he ruled out categorically a debt haircut on official loans. A senior Greek government official reported by *Ekathimerini* noted the government is open to any discussion about a third package as long as it encompasses only “*structural measures*” and not additional fiscal austerity. Comment: a third bailout for Greece is finally on the table, probably following the acknowledgement by all parties involved that Greece's financing gap for 2014-16 is unlikely to be filled (or not entirely) by market funding and that there are few chances that the ECB/euro area central banks will agree to roll over their holdings of Greek bonds. Redemptions of these securities represent the bulk of Greece's financing needs over the next three years, together with interest payments on outstanding debt (for around €6.5bn, or 4.1% of GDP, in 2013). However, we doubt a third package will be agreed before the EU Parliament elections in May, given how sensitive is the issue among creditors' voters as well as among Greek voters (as a new bailout would surely require additional conditionality from Greece). We reckon European lenders do not want to increase the chances (already quite high) of a severe defeat at the EU elections for the ruling party New Democracy. A victory for opposition party SYRIZA may well force the country into early elections later on this year.

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**ECB AQR press conference reveals few new details.** At a press conference on the asset quality review (AQR), ECB Vice President Vitor Constancio and the newly installed head of the ECB Supervisory Board Danielle Nouy affirmed that the ECB would carry out a “*demanding and very rigorous*” bank assessment and that they would “*uphold the reputation of the ECB and not put it at risk*”. The ECB officials defended the assessment's choice of capital hurdles, noting that both for the AQR and the stress test, they were one percent above the regulatory minima and that leverage ratios for major European banks were at a similar level as US banks. Few new details were released. The final methodology for the AQR is due to be published by the end of the first quarter, but the release already noted that certain assets (the so-called ‘Level 3 assets’) that were particularly risky and hard to value, i.e. mainly relatively illiquid assets which were mostly valued using internal models, were to be singled out for special attention. In addition, 29 institutions with a relatively high share of such assets would also be assessed more thoroughly than the rest.

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**ECB President Draghi to seek Bundesbank support for ending SMP sterilisation.** Following reports that the Bundesbank could support ending liquidity absorption for the securities markets programme (SMP), Bloomberg reports (referring to euro-area central bank officials familiar with the debate) that ECB President Mario Draghi would only consider ending the sterilisation of the SMP if it was “*openly backed*” by the Bundesbank. This would be for the Bundesbank to help sell the move to the German public in order to avoid a backlash.

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a cut the refi rate to 0% and the negative deposit rate to -0.1% in 2Q. But with a modest rebound in activity and reduced fragmentation, the timing is uncertain. An smaller move is possible in March, contingent on lower HICP, EM crisis and/or higher MMKT rates.

Guillaume Menuet

### Euro Economics Weekly — The Euro Area Now and Japan Then: Separated by One Large Shock

31 January 2014

The euro area is not currently in deflation. But, with very low inflation, ample slack and sluggish growth, we believe the euro area is — like mid-90s Japan — potentially just one major adverse shock away from deflation. To be sure, there are some differences but, in our view, the commonalities outweigh the differences. It is not inevitable that the euro area will be hit by a similar shock but, if it is, then — like Japan — the region could well be tipped into deflation.

Ebrahim Rahbari | Guillaume Menuet | Giada Giani | Michael Saunders | Ann O'Kelly

### Euro Area — Inflation Surprises Once Again to the Downside in January

31 January 2014

Euro area inflation fell to 0.7% YY in January, from 0.8% in December and is back in line with the October 2013 trough. The consensus was looking for an uptick to 0.9% (as surveyed last week before the weaker-than-expected German HICP data). This was the second sizable undershoot in the last four months (with one marginal overshoot and one in line), with a cumulated surprise of -0.5pp since last October.

Giada Giani

### UK Economics Weekly — Is Growth Credit-Led?

31 January 2014

Sceptics of our strong growth forecast often argue that the rebound is a credit-led bubble and hence inherently fragile. We disagree. The household debt/income ratio — and indeed, the overall private sector debt/GDP ratio — continues to fall. More broadly, the

### **ECB's Lautenschläger promotes SSM in front of European Parliament.**

Bloomberg reports that ECB Executive Board Member Sabine Lautenschläger said that the single supervisory mechanism (SSM) should be able to spot risks in the European banking system more quickly, speaking at a confirmation hearing for her role as Deputy Chair of the SSM in front of the European Parliament. She said that the SSM would draw on a broader and better basis of information on euro area banks. She added that lawmakers and governments must follow up on the SSM and establish an effective single resolution mechanism quickly and said she hoped that the legislative process would be completed *"in good time to"* allow the SRM to become operational by the end of this year. The EP's economic and monetary affairs committee endorsed Lautenschläger's appointment, setting the stage for a vote this week by a full session of the parliament.

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### **Juncker to be main centre-right candidate for European Commission President.**

The FT reports that Jean-Claude Juncker, the former PM of Luxembourg and Eurogroup President, is the frontrunner to become the candidate of the EU's group of centre-right parties EPP for European Commission President. The article reports that Juncker has received the backing of key leaders, including German Chancellor Merkel. The official nomination is due at a nominating convention in Dublin. Other contenders for the candidacy include the current EU Commissioner Barnier, Finnish PM Katainen and the former Lithuanian PM Dombrovskis, while Irish PM Kenny has reportedly declined to run.

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**Germany to offer limited support for EU treaty renegotiation.** Bloomberg reports that the German foreign minister Frank-Walter Steinmeier offered the UK limited support on renegotiating the treaties of the European Union. At a joint press conference in London with British foreign minister William Hague, Steinmeier said that Germany wanted to see Britain's influence in the *"midst"* of the EU, not on *"the sidelines."* Steinmeier said Germany was *"not against discussing an adaptation of the treaties"*, but cautioned that it would be *"exaggerating to say that the UK and Germany are pulling in exactly the same direction"*, noting that Germany saw clear benefits from EU integration and was against initiatives to unravel it.

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**French expenditure review process starts in earnest - Les Echos** notes that Budget minister Bernard Cazeneuve is beginning his consultations about the 2015-17 budget this week, aiming to identify at least €50bn of expenditure savings, to reduce the budget deficit, finance the 'Responsibility Pact' and lower taxation (possibly ahead of 2017). One by one all the ministers will be quizzed about their proposals to reduce spending and their respective budgetary ceilings will be communicated by April. With a budget of around €40bn or 2% of GDP (€14bn of which amounts to fiscal spending: tax optimisation, reduced VAT on renovation work, etc) the housing ministry will be on the main candidates for some belt-tightening. For 2015, the lion's share of expenditure savings is expected to stem from the social security and local authorities after substantial efforts by the central government in the 2014 budget. Comment: the ambitious expenditure review has the merit of starting earlier than usual, a prudent strategy given the complexity of the process and the likely back-and-forth between ministries and the budget minister on where the axe will have to fall. PM Jean-Marc Ayrault has confirmed that he will pay particular attention to the process. Marginally better GDP dynamics could help a little during 2014, allowing the government to deliver slightly more generous tax cuts to the corporate sector in 2015, particularly for SMEs.

**French corporate tax reform discussions continue - La Tribune** reports that

period of balance sheet retrenchment probably is ending. Corporate liquidity is the best for over 50 years, and this is likely to feed through to solid job growth, higher pay growth and a business investment recovery in coming quarters.

[Michael Saunders | Ann O'Kelly](#)

### **Norway — Weak Momentum In Private Spending**

**31 January 2014**

Momentum in Norwegian retail sales and domestic spending on goods remained weak in the fourth quarter, and we see downside risks to Norges Bank's 0.4% Q/Q 4Q forecast. Lower growth in households' purchasing power, slightly higher unemployment and mounting uncertainty about housing market trends will likely continue to weigh on private spending growth ahead.

[Tina Mortensen](#)

### **Euro Area — Bank Lending Survey Confirms Supply-Side Improvement**

**30 January 2014**

The Jan bank lending survey showed a further improvement in lending standards. Our aggregate measure indicates that, the net proportion of banks loosening lending standards rose to its highest level since Q4-06. This useful leading indicator of GFCF two quarters ahead points to investment spending moving into positive territory in 4Q-13. The suggested 3% run rate at the start of 2H-14 implies some slight upward risks to our base case.

[Guillaume Menuet](#)

### **UK — Highlights of the BoE Data and EC Survey**

**30 January 2014**

Today's data have several interesting points, with solid gains in mortgage approvals and corporate liquidity, lower corporate borrowing costs, strong gilt purchases among overseas investors and very strong readings for the UK in the EC survey.

[Michael Saunders](#)

### **Scandi Economics Update —**

the French Finance and Budget ministry have agreed to cancel the temporary 10.7% surcharge on corporate profits (increased from 5% last autumn), with some announcements expected in the 2015 budget. Finance Minister Pierre Moscovici also hinted at a widening of the corporate tax base (only a third of firms pay it), allowing the government to lower the rates. Note that in his campaign manifesto, Mr. Hollande was targeting a 35% corporate tax rate for the largest firms, 30% for intermediate firms and 15% for SMEs, having estimated that the measure would cost €2bn in lost revenues. Comment: this will be the hot topic in the spring, with businesses hoping for some relief in fiscal pressure to be in a better position to hire and invest, provided that profit margins are rebuilt. Negotiations between employer organisations and labour unions are continuing and are unlikely to deliver a deal before March at the earliest. What is needed now from the government is a clear message about the need for change, and the early signs are encouraging.

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**Italy – Q4 13 GDP growth at 0.2%-0.3% QQ, Labour Minister says.** Enrico Giovannini said the Italian economy has finally posted positive growth, by 0.2%-0.3% QQ in Q4, after eight consecutive quarters of contraction. Official data on Q4 13 GDP will be released on Feb 14. The strong driver for growth is manufacturing, while construction and services are still suffering, Giovannini said. Comment: we expect Q4 13 GDP to expand by 0.2% QQ, amid a rebound in industrial output supported mainly by export demand. The impact of the repayment of government arrears (€22bn or 1.4% of GDP) in the last six months has been boosting corporate liquidity (as evidenced by rising corporate bank deposits) part of which has probably been spent on new investment. Employment continued to decline at the end of last year (-0.1% MM in Dec, -0.3% QQ in Q4 13), suggesting that there remains limited need for businesses to expand the workforce.

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**Italy – state sector cash balance posts surplus of €0.8bn in January,** better than the cash deficit of €2.4bn recorded in January 2013. The Italian Treasury press release said higher tax revenues mainly contributed to the improvement relative to Jan 13, as the introduction of the revised property taxes (“mini-IMU” and TARES) were collected in January. It also notes positive dynamics for VAT tax revenues. Comment: a rising tax burden has offset a new upward trend in primary spending throughout 2013. It looks likely this trend will continue in 2014, with possibly limited efforts by the government to cut back on public spending. This will likely continue to represent a burden on the recovery in domestic demand.

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**Spain – Manufacturing PMI rose to its highest level since Apr-10, employment PMI rises above 50.** The Markit manufacturing PMI rose to 52.2 in Jan from 50.8 in Dec, standing now 0.5sd above its long term average. The employment index rose for the first time above the expansionary threshold of 50 since October 2010 (and the second time in the last 77 months). Comment: the strong reading suggests the recovery in the manufacturing sector is gathering pace at the beginning of 2014, amid strong external demand. This should continue to translate into marginal job creation in this sector, supported by on-going wage moderation (negotiated wage growth has been stable at around 0.6% YY in the past 12 months) and labour shortages probably becoming an issue fairly soon.

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**Spain - Registered unemployment rises by 113k in January,** but continues to fall in seasonally-adjusted terms. When adjusted for seasonal factors, we compute that unemployment fell by 0.5% MM in January, after MM reductions of

## Norwegian FSA Reviews Tighter Capital and Loan Standards

4 February 2014

**Norway** — FSA reviews tighter capital and loan standards — Easier rules for oil fund to raise returns — Norges Bank speech — PMI rebounds in January.

**Sweden** — Riksbank's business survey — Strong pick up in PMI in January.

**Denmark** — January currency reserves; focus on interventions

[Tina Mortensen](#)

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1.4% and 0.9% in December and November, respectively. Comment: the rise was driven by strong seasonal factors, as January tends to show the highest MM increase in registered unemployment over the year. The underlying trend continues to show a marginal reduction in jobless claims, as observed since Aug 2013. Registered unemployment, however, has recently been less representative of the developments in the labour market compared with the labour force survey, due to changes in the criteria to access jobless benefits and to long-term unemployed becoming ineligible. Total unemployment as measured by the labour force survey stood at 5.9mIn in 4Q 13, against 4.7mIn jobless claimants.

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**Spain – Electricity prices to rise by a further 0.2% in February**, according to daily *El Economista* citing the Official Gazette published last week. The increase should add to the 2.3% rise which took place in January, and came as a result of the government's decision to increase the weight of fixed power generation costs in final electricity bills. Comment: the total tariff increase for the beginning of the year continues to be much smaller than the one resulting from the electricity auction held on 19 December, which would have pointed to a rise in electricity tariffs of more than 11%. The government decided to annul the result of the auction due to alleged irregularities, and has pledged to change the mechanism of electricity price setting for this year to avoid excessive price volatility.

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**Spain – Car sales rose by 7.6% YY in January**, after an 18.2% YY increase in December and 3.3% rise over 2013, data from the Association of Car Manufacturers (Anfac) showed yesterday. The increase in car registrations continued to be strongly affected by the government's car subsidy scheme PIVE (recently extended by an amount of €175m), with car sales to private persons rising by 13% YY, Anfac noted. Separately, **Spain's consumer confidence rose by 6.7 points in January** to 77.7, a new record high, the Centre for Sociological Research (CIS) reported yesterday. Improvement was due to both better perceptions of the current situation (up by 8.2pts to 62, also new record high), and consumer' expectations (up by 5.2pts to 93.4). In particular, the data showed an improvement in consumer perception of labour market opportunities (up by 9.5pts MoM).

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**Slovakia – Solid fiscal revenue performance continues in January.**

Jaromir Sindel +420 233 061 485

January central government cash budget showed a deficit of €123mn, which is wider compared to €-63mn a year ago, reflecting larger expenditure that offset solid revenue dynamics. We estimate the 12m cumulative deficit reached 2.9% of GDP, slightly wider compared to 2.8% a month ago, but narrower compared to 5.6% a year ago (the primary deficit likely reached 1.2% of GDP, compared to -3.8% a year ago). Recent performance suggests to us mixed implications: the seasonality of both expenditures and revenues would indicate an annual deficit around 5.1% of GDP in 2014, which is wider than the planned -4.5% (-2.8% in 2013). However, recent dynamics in revenues and expenditures suggest a deficit around 2.1%, which seems to us too optimistic owing to larger expenditure in January and also because 2013's better-than-expected budget reflected not only lower current expenditure and larger tax revenue, but also larger EU fund inflow (which, nevertheless, has also continued in January). Thus, the dynamics of EU funds inflow and tax collection will be key for another outperformance of the budget in 2014.

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**Latest Issues of Sovereign Debt Update**

**ECB Liquidity Policy under the Spotlight**

**3 February 2014**

Bundesbank favours end to sterilization operations, says Dow Jones. ECB's Coeuré says tools exist to ease, even if policy rate close to ZLB. EBA gives more stress test details. Eurogroup President to be full time role? EU's Rehn says reforms may become precondition for deficit deadline extensions. Spain's Rajoy repeats pledge of 2015 tax cuts. Spain's current account surplus widens. EU lenders prepare for third Greek bailout programme, says Spiegel. Greek stress tests delayed again to early Feb.

[Ebrahim Rahbari](#) | [Guillaume Menuet](#) | [Giada Giani](#)

## **ECB's Coeuré on Declining Fragmentation**

**31 January 2014**

ECB's Coeuré on clear signs of declining financial fragmentation. ECB asks banks for data on restructured loans. ECB lending survey confirms supply-side improvement. Germany: tax receipts up, retail sales and inflation weaker than expected. French PM launches household income tax reform. Belgian budget deficit shrinks but misses target. Italy's Lower House starts voting on electoral reform bill in secret ballot. Spain's HICP remains subdued. Portugal's IP jumps, retail sales slow.

[Guillaume Menuet](#) | [Giada Giani](#) | [Ebrahim Rahbari](#)

## **ECB's Noyer Warns About A Strong Euro**

**30 January 2014**

Noyer: stronger euro contrary to ECB price stability goal. EC's bank reform proposal. ECB's new Supervisory Board meets. Banks in Europe lose market share in property lending. German Cabinet approves pension reform. Banks' exposure to govt debt falls faster in Spain than in Italy. Italian business confidence rises. Spain's bank bailout programme completed. Spain's shadow economy at 25% of GDP. 4Q GDP in Spain and Belgium. Greek corporate deposits rebound. Moody's on Portugal. Slovenia update.

[Giada Giani](#) | [Guillaume Menuet](#) | [Ebrahim Rahbari](#)

## **German High Court: “Contentious Discussions” on OMT**

**29 January 2014**

German Constitutional Court decision on OMT reportedly delayed. Approval of EU bank reform unlikely before EP elections. Lithuanian membership of eurozone could change ECB voting rules. Rise in German consumer confidence and in inward FDI. French talks on corporate tax reform. Storm over Hollande-Harz meeting. Italy's consumer confidence rises, wage growth falls, electoral reform faces delay. Spain's deficit on target, economy to grow by 1% says EconMin, IMF recommends further wage cuts.

[Giada Giani](#) | [Guillaume Menuet](#) | [Ebrahim Rahbari](#)

## **ECB's Noyer Not Particularly Worried about EM**

**28 January 2014**

ECB's Noyer downplays EM financial upset. Structural reforms to be Eurogroup priority. Legal hurdles for AQR bank valuations. Faster pay-in period for resolution funds? Direct bank recap plans by 10 March. FTT again. A euro-area Parliament? French jobless rise, tough start to Responsibility Pact talks. Dutch data flow improves. Belgian politics update. Spain's fiscal overhaul proposal in Feb. Too early to decide on Portugal's bailout exit, no progress on Greece. Economic sentiment in Slovenia.

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## Macroeconomic Research

### European Economic Forecast Highlights — January 2014

23 January 2014

This companion to Global Economic Outlook and Strategy - January 2014 gives detailed quarterly forecasts for the main European countries to end 2015 and annual forecasts to 2018 for growth, inflation, current balance, fiscal balance, primary balance and government debt.

[Ann O'Kelly](#) | [Michael Saunders](#) | [Guillaume Menuet](#) | [Giada Giani](#) | [Ebrahim Rahbari](#)

### Global Economic Outlook and Strategy — January 2014

22 January 2014

We are pushing up our global growth forecasts this month, and now look for global GDP growth (at current exchange rates) to rise from 2.5% in 2013 to 3.3% in 2014 and 3.4% in 2015, up by 0.1pp for 2013, 0.2pp for 2014 and 0.1pp for 2015 from our previous forecast. This year will, we expect, mark a return to sustained above-average global growth rates, whereas global growth has been below average for three consecutive years (2011-13) and indeed in five of the last six years.

[Willem Buiter](#) | [Nathan Sheets](#) | [Michael Saunders](#) | [Robert V DiClemente](#) | [Kiichi Murashima](#)

### Emerging Markets Macro and Strategy Outlook — The 'Fragile 5': A Progress Report

GEMS, Asia, CEEMEA, Global, Latin America – 24 January 2014

The 'F5' - Brazil, India, Indonesia, South Africa and Turkey - were at the heart of EM's underperformance in 2013, but investors have become more discriminating lately: the IDR, BRL and INR have been the best-performing EM currencies since the start of the year, while the ZAR and TRY have been the worst. We don't pretend to have a full 'theory' of how investors should discriminate among these economies over the next few months, but some trends are becoming clear.

[Guillermo Mondino](#) | [David Lubin](#) | [Johanna Chua](#)

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# Appendix A-1

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