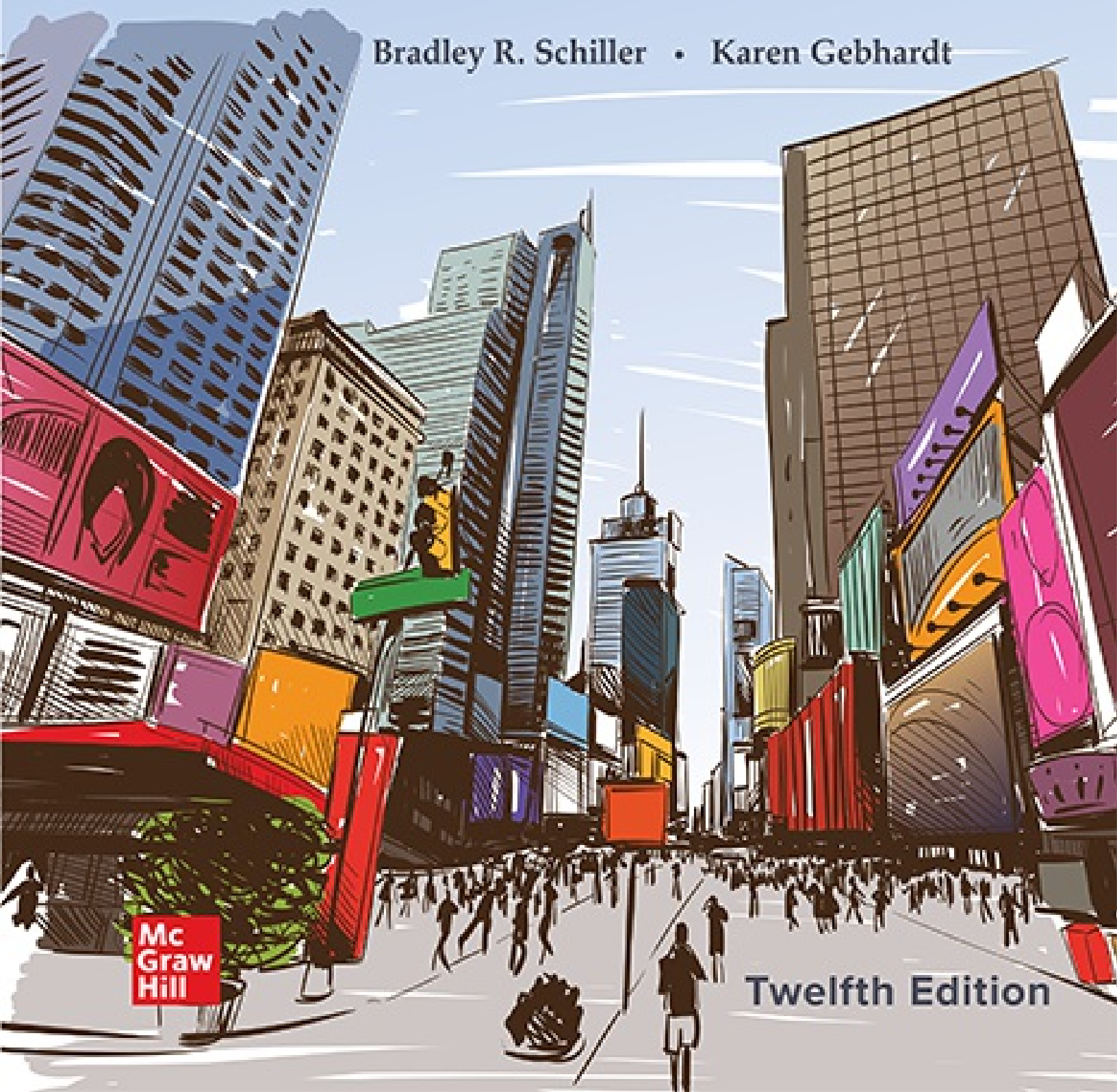


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Essentials of Economics

Bradley R. Schiller • Karen Gebhardt



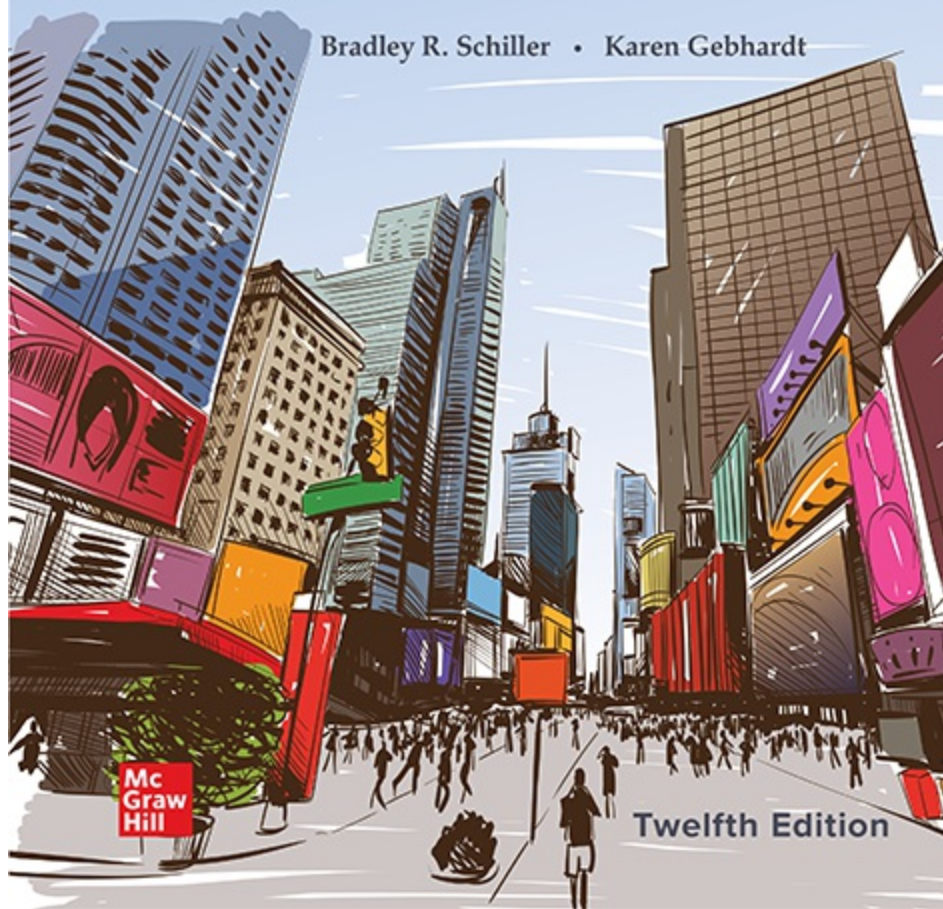
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Twelfth Edition

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Essentials *of* Economics

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Bradley R. Schiller

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ESSENTIALS OF ECONOMICS

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ABOUT THE AUTHORS

Bradley R. Schiller has over four decades of experience teaching introductory economics at American University, the University of California (Berkeley and Santa Cruz), the University of Maryland, and the University of Nevada (Reno). He has given guest lectures at more than 300 colleges ranging from Fresno, California, to Istanbul, Turkey. Dr. Schiller's unique contribution to teaching is his ability to relate basic principles to current socioeconomic problems, institutions, and public policy decisions. This perspective is evident throughout *Essentials of Economics*.



Courtesy of Bradley R. Schiller

Dr. Schiller derives this policy focus from his extensive experience as a Washington consultant. He has been a consultant to most major federal agencies, many congressional committees, and political candidates. In addition, he has evaluated scores of government programs and helped design others. His studies of income inequality, poverty, discrimination, training programs, tax reform, pensions, welfare, Social Security, and lifetime wage patterns have appeared in both professional journals and popular media. Dr. Schiller is also a frequent commentator on economic policy for television, radio, and newspapers.

Dr. Schiller received his PhD from Harvard and his BA degree, with great

distinction, from the University of California (Berkeley). When not teaching, writing, or consulting, Professor Schiller is typically on a tennis court, schussing down a ski slope, or enjoying the crystal blue waters of Lake Tahoe.

Karen Gebhardt is a faculty member in the Department of Economics and is the Director of the Online Economics Program at the University of Colorado Boulder. Dr. Gebhardt has a passion for teaching economics. She regularly instructs courses in all modalities (online, on campus, hybrid, remote) from introductory courses in macro- and microeconomics, to upper-division courses in microeconomics, international trade, and managerial economics and graduate courses in environmental economics and public finance.



Dr. Karen Gebhardt

She is an early adopter of teaching with technology and advocates strongly for it because she sees the difference it makes in student engagement and learning. Dr. Gebhardt was the recipient of the Water Pik Excellence in Education Award in 2006 and was awarded the Best Teacher Award in 2015 while she was at Colorado State University.

Dr. Gebhardt's research interests, publications, and presentations involve the economics and online education and the economics of human-wildlife interaction. Before returning to academia, she worked as an economist at the U.S. Department of Agriculture/Animal and Plant Health Inspection Service/Wildlife Services/National Wildlife Research Center, conducting research related to the interactions of humans and wildlife. Her current research focuses on using data to improve student learning outcomes in

economics education with an emphasis on improving grades and completion rates in online courses.

In her free time, Dr. Gebhardt enjoys learning about new teaching methods that integrate technology and going rock climbing and camping in the Colorado Rockies and beyond.

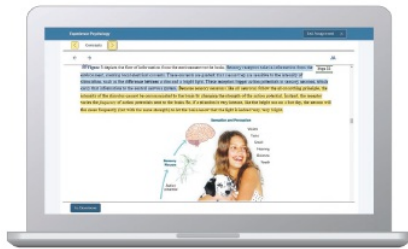


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PREFACE

It's hard to imagine a better time to be teaching economics. The world's economies attained solid growth and record living standards in 2015–2019. Then the coronavirus struck. The resulting pandemic and associated lockdowns caused the sharpest, deepest, and—thankfully, shortest—recession in modern times. In the span of less than a year, we experienced both the peak and the trough of the business cycle. In the process, we saw a surge in curiosity about what makes economies “tick.”

Varied responses to the pandemic have also spurred intense debates about what kinds of government intervention are most effective in ending recessions and fostering further growth. Here in the United States, we witnessed a dramatic change in policy priorities when President Biden took the reins from President Trump. The shifts in policy range from micro issues like minimum wages and environmental regulation to the big macro decisions about the size and scope of government stimulus programs.

These two developments have effectively created a unique “laboratory” for identifying basic economic concepts, observing the trajectories of business cycles, and assessing the potential of various policy options. Hopefully, this twelfth edition of *Essentials* delivers the sense of urgency and relevance that the current situation merits.

WHAT, HOW, FOR WHOM?

The core theme that weaves through the entire text is the need to find the best possible answers to the basic questions of WHAT, HOW, and FOR WHOM. Is WHAT we produce today the optimal mix of output? Could we do better? And are we producing goods and services in safe, environmentally sound, and efficient ways? Or should we look how to change HOW things get produced? And what about the distribution of those products? Is the current answer to the FOR WHOM question fair? These are the core questions every society must ponder. In [Chapter 1](#), students get an introduction to these questions and the different mechanisms (market and nonmarket) that nations use to answer them. They learn that markets sometimes fail to generate the

best-possible answers to these three core questions, but also that government intervention may fail as well. Critical thinking is required from the get-go.

A GLOBAL PORTRAIT OF THE U.S. ECONOMY

To put some meat on the abstract bones of the economy, *Essentials* offers a unique portrait of the U.S. economy. Few students easily relate to the abstraction of the economy. They hear about specific dimensions of the economy but rarely see all the pieces put together. [Chapter 2](#) fills this void by providing a bird’s-eye view of the U.S. economy. This descriptive chapter is organized around the three basic questions of WHAT, HOW, and FOR WHOM to produce. The current answer to the WHAT question is summarized with data on GDP and its components. Historical and global comparisons are provided to underscore the significance of America’s \$23 trillion economy. Similar perspectives are offered on the structure of production and the U.S. distribution of income. An early look at the role of government in shaping economic outcomes is also provided. This colorful global portrait is a critical tool in acquainting students with the broad dimensions of the U.S. economy and is unique to this text.

Page vii

REAL-WORLD EMPHASIS

The decision to include a descriptive chapter on the U.S. economy reflects a basic commitment to a real-world context. Students rarely get interested in stories about the mythical widget manufacturers that inhabit so many economics textbooks. But glimmers of interest—even some enthusiasm—surface when real-world illustrations, not fables, are offered.

The real-world approach of *Essentials* is reinforced by the boxed **News Wires** that appear in every chapter. The 72 News Wires offer up-to-date domestic and international applications of economic concepts. Some new examples that will particularly interest your students include:

- The opportunity cost (famine) of North Korea’s submarine-based rocket program.
- The impact of lower gas prices on sales of electric vehicles.
- The diversity in starting pay for various college majors.

- Taylor Swift’s use of dynamic pricing for concerts.
- Starbucks price hikes and iPhone price cuts.
- Tesla’s new gigafactory in Austin, Texas.
- The impact of COVID stimulus payments on consumer spending.
- The price-fixing conspiracy on canned tuna.
- The extraordinary turnout for Amazon’s Career Day.
- How the strong dollar has made European vacations cheaper.

This is just a sampling of the stream of real-world applications that cascades throughout this text. Thirty of the News Wires are new to this edition.

NEWS WIRE	INSATIABLE WANTS
<p>Never Enough Money! A public opinion poll asked Americans how much money they would need each year to be “happy.” In general, people said they needed twice as much income as they had at present to be happy.</p>  <p>Tom B Payne/Shutterstock</p> <p>Source: CNN/ORC Poll, May 29–June 1, 2014.</p>	
<p>POLICY POINT: People always want more than they have. Even multimillionaires say they don’t have enough to live “comfortably.”</p>	

POLICY PERSPECTIVES

Every chapter starts out with real-world applications of core concepts. As the chapters unfold, empirical illustrations continue to enliven the text analysis. The chapters end with a **Policy Perspectives** section that challenges the student to apply new concepts to real-world issues. At the end of [Chapter 1](#), students are asked to recognize the opportunity costs of President Biden’s “free” health care proposals. At the end of [Chapter 3](#)’s introduction to supply

and demand, students are asked to ponder the consequences of imposing price controls in the wake of natural disasters and pandemics. At the end of the monopoly chapter ([Chapter 7](#)), students are asked to consider the ramifications and desirability of “breaking up Big Tech.” At the end of the fiscal policy chapter ([Chapter 12](#)), students are asked to consider the deficit and debt implications of President Biden’s fiscal stimulus packages. The capstone chapter (Theory versus Reality, [Chapter 17](#)) requires students to assess the desirability of more or less government intervention in the economy.

FOCUS ON CORE CONCEPTS

It’s impossible to squeeze all the content—and the excitement—of both micro- and macroeconomics into a one-semester course, much less an abbreviated intro text. But economics is, after all, the science of choice. Instructors who teach a one-term survey of economics know how hard the content choices can be. There are too many topics, too many economic events, and too little time.

Few textbooks confront this scarcity problem directly. Some one-semester books are nearly as long as full-blown principles texts. The shorter ones tend to condense topics and omit the additional explanations, illustrations, and applications that are especially important in survey courses. Students and teachers alike get frustrated trying to pick out the essentials from abridged principles texts.

Essentials of Economics lives up to its name by making the difficult choices. The standard table of contents has been pruned to the core. The surviving topics are the essence of economic concepts. In microeconomics, for example, the focus is on the polar models of perfect competition and monopoly. These models are represented as the endpoints of a spectrum of market structures. Intermediate market structures—oligopoly, monopolistic competition, and the like—are noted but not analyzed. The goal here is simply to convey the sense that market structure is an important determinant of market outcomes. The contrast between the extremes of monopoly and perfect competition is sufficient to convey this essential message. The omission of other market structures from the outline also leaves more space for explaining and illustrating *how* market structure affects market behavior.

The same commitment to essentials is evident in the section on

macroeconomics. Rather than attempt to cover all the salient macro models, the focus here is on a straightforward presentation of the aggregate supply–demand framework. The classical, Keynesian, and monetarist perspectives on aggregate demand (AD) and aggregate supply (AS) are discussed within that common, consistent framework. There is no discussion of neo-Keynesianism, rational expectations, public choice, or Marxist models. The level of abstraction required for such models is neither necessary nor appropriate in an introductory survey course. Texts that include such models tend to raise more questions than survey instructors can hope to answer. In *Essentials* students are exposed to only the ideas needed for a basic understanding of how macro economies function.

CENTRAL THEME

The central goal of this text is to convey a sense of how economic *systems* affect economic *outcomes*. When we look back on the twentieth century, we see how some economies flourished while others languished. Even the “winners” had recurrent episodes of slow, or negative, growth. The central analytical issue is how various economic systems influenced those diverse growth records. Was the relatively superior track record of the United States a historical fluke or a by-product of its commitment to market capitalism? Were the long economic expansions of the 1980s and 1990s the result of enlightened macro policy, more efficient markets, or just good luck? What roles did policy, markets, and (bad) luck play in the Great Recession of 2008–2009 and the pandemic crisis and recovery of 2020–2021?

A recurrent theme in *Essentials* is the notion that economic institutions and policies *matter*. Economic prosperity isn’t a random occurrence. The right institutions and policies can foster or impede economic progress. The challenge is to know when and how to intervene.

This central theme is the focus of [Chapter 1](#). Our economic Page ix accomplishments and insatiable materialism set the stage for a discussion of production possibilities. The role of economic systems and choices is illustrated with the starkly different “guns versus butter” decisions in North and South Korea, Russia, and the United States. The potential for both market failure (or success) and government failure (or success) is highlighted. After reading [Chapter 1](#), students should sense that “the economy” is relevant to their lives and that our collective choices on how the economy is structured

are important.

THEORY AND REALITY

In becoming acquainted with the U.S. economy, students will inevitably learn about the woes of the business cycle. As the course progresses, they will not fail to notice a huge gap between the pat solutions of economic theory and the dismal realities of occasional recession. This experience will kindle one of the most persistent and perplexing questions students have. If the theory is so good, why is the economy such a mess?

Economists like to pretend that the theory is perfect but politicians aren't. That's part of the answer, to be sure. But it isn't fair to either politicians or economists. In reality, the design and implementation of economic policy are impeded by incomplete information, changing circumstances, goal trade-offs, and politics. [Chapter 17](#) examines these real-world complications. In this signature chapter, students get a more complete explanation of why the real world doesn't always live up to the promises of economic theory.

NEW IN THIS EDITION

The dedication of *Essentials* to introducing core economic principles in a real-world context requires every edition to focus on trending policies and front-page developments. As in earlier editions, this twelfth edition strives to arouse interest in economic theories by illustrating them in the context of actual institutions, policy debates, and global developments. The following list highlights both the essential focus of each chapter and the new material that enlivens its presentation:

[Chapter 1: The Challenge of Economics](#)—The first challenge for any intro econ course is to instill in students the concept of *scarcity*. They surely have experience in making difficult choices among competing goods, but rarely project that experience to the nation as a whole. Political debates hardly advance the cause, with nearly every politician promising free college, free medical care, free child care, free housing, and generous income guarantees. But we know it ain't so. So, we start with an obligation to convey the essences of scarcity and the inevitability of *opportunity costs*. [Chapter 1](#) illustrates the sacrifice of “butter” implied by North Korea's stepped-up

ballistic missile program and global patterns of military spending. President Biden's American Rescue Plan, infrastructure proposals, and health care promises are also examined from an opportunity cost perspective.

Chapter 2: The U.S. Economy—The purpose of this chapter is to give students a real-world perspective on the relative size and scope of the American economy. Is China's economy larger than America's economy? Are we falling behind other world economies? The popular press often gives these impressions. But the reality is very different, as the global comparisons in [Chapter 2](#) confirm. This chapter carefully looks at WHAT nations produce, HOW they produce, and FOR WHOM they produce. News Wires on global happiness rankings, inequality, and manufacturing give added color to the statistical comparisons.

Chapter 3: Supply and Demand—This chapter shows how the market mechanism works: how the forces of supply and demand interact to determine both prices and quantities for various goods. Relevant News Wires include the impact of alcohol prices on college drinking, pricing of the Apple iPhone 12 Pro, gasoline prices and EV sales, and price spikes in the wake of natural disasters. The unintended effects of (disequilibrium) price ceilings are illustrated with San Francisco rent controls and price ceilings imposed in natural disasters.

Micro

Chapter 4: Consumer Demand—This chapter starts by looking at patterns of U.S. consumption, then analyzing the demand factors that shape those patterns. The elasticity of demand gets a lot of attention, as illustrated by iPhone 11 price cuts, Oregon's 2021 \$2 per pack cigarette price hike, and Starbucks' 2020 price increases. The Policy Perspective feature examines the calls for more regulation of advertising.

Chapter 5: Supply Decisions—The key point of this chapter is the difference between what firms *can* produce (as illustrated by the production function) and what they *want* to produce (as illustrated by profit-maximization calculations). The critical role of marginal costs in the production decision is highlighted. Tesla's decision to build a gigafactory in Austin, Texas, illustrates the distinction between long-run *investment decisions* and short-run *production decisions*.

Chapter 6: Competition—This first look at market structure emphasizes the lack of pricing power possessed by small, competitive firms. Perfectly

competitive firms must relentlessly pursue cost reductions, quality improvements, and product innovation if they are to survive and prosper. Although few firms are perfectly competitive, competitive dynamics keep all firms on their toes. How firms locate the optimal rate of production with the use of market prices and marginal costs is highlighted. The Policy Perspective considers how competitive forces help rather than hurt society.

Chapter 7: Monopoly—As a survey introduction to economics, *Essentials* focuses on the differences between only two market structures: perfect competition and monopoly. [Chapter 7](#) illustrates in detail the differences in structure, behavior, and outcomes of these two polar cases. This two-way contrast underscores the importance of market structures for social welfare. A step-by-step comparison of behavioral decisions and outcomes provides a vivid perspective on this central concern. The Policy Perspective examines recent proposals for breaking up Big Tech.

Chapter 8: The Labor Market—The 2020 presidential election brought a lot of labor market issues back onto the front page. President Biden has declared his support for a \$15 minimum wage, easier unionization, expanded private-sector benefits, and significant tax changes. This chapter first illustrates how market forces establish wages and employment levels, then examines how various interventions alter market outcomes. The overwhelming response to Amazon’s Career Day showcases labor supply, while 2020–2021 airline layoffs show the consequences of reduced labor demand. Alabama’s Nick Saban’s 2021 bonus and salary illustrate the link between pay and marginal revenue product.

Chapter 9: Government Intervention—In our mixed economy, the purpose and impacts of government intervention must be understood. This chapter identifies the core rationale for government intervention and offers a slew of timely examples, including COVID vaccinations, Israel’s 2021 Iron Dome upgrades, and President Biden’s decision to halt the Keystone pipeline. The decline in public trust in government is noted.

Macro

Chapter 10: The Business Cycle—The 2020 recession gave students a real-world lesson in how business cycles work. This chapter continues that lesson with a history of cycles and an examination of how they affect employment, inflation, and the distribution of income. The goal here is to get students to recognize why macro instability is a foremost societal concern. News Wires

look at the 2020 recession and 2021 recovery, holiday hiring surges, and 2020–2021 tuition hikes.

Chapter 11: Aggregate Supply and Demand—This chapter gives students a conceptual overview of how market and nonmarket forces shape macro outcomes. Aggregate supply (AS) and aggregate demand (AD) are explained, with an emphasis on the importance of the shifts that can both foster growth and trigger instability. The message is clear: Either AS or AD must shift if macro outcomes are to change. News Wires on the COVID pandemic (AS and AD shifts), the unemployment surge that resulted, and President Biden’s stimulus packages enliven the discussion.

Chapter 12: Fiscal Policy—This chapter highlights the potential Page xi of changes in government spending and taxes to shift the AD curve. The power of the multiplier is illustrated in the context of the AS/AD framework, an intuitively simpler approach than the traditional Keynesian model. The AS/AD model also offers a straightforward mechanism for illustrating how the multiplier can simultaneously affect both output and price levels, something the Keynesian model can’t do. President Trump’s 2017 tax cuts and President Biden’s several stimulus packages offer plenty of illustrations. The impact of fiscal policy on budget deficits is also examined.

Chapter 13: Money and Banks—Apple Pay and bitcoins are used to illustrate differences between *payment services* and *money*. The various methods of payment consumers actually use are noted, again distinguishing payment services from money. The core of the chapter depicts how deposit creation and the money multiplier work, using a step-by-step illustration of each. By the way, the Fed changed its money supply measures in October 2020, simplifying the M concept. The Policy Perspective explains why bitcoins don’t satisfy the definition of “money.”

Chapter 14: Monetary Policy—Students get an overview of how the Federal Reserve is organized and the role that Jerome Powell plays. Then the three basic tools of monetary policy are illustrated, with an emphasis on how open-market operations work. The chapter shows how the various tools of monetary policy can shift the AD curve, ultimately affecting both prices and output. The extraordinary steps taken by both American and Chinese monetary authorities to end the 2020 recession are discussed.

Chapter 15: Economic Growth—The ultimate challenge of every society is to grow its economy and raise living standards over time. This chapter reviews the world’s growth experiences, then examines the factors that foster

or retard growth. The declines in living standards and even longevity caused by the coronavirus pandemic are a grim reminder of why economic growth is so important—and, yes, desirable.

International

Chapter 16: International Trade—Students often wonder why we trade with other nations at all because we can produce just about everything ourselves. Many politicians exploit these doubts by claiming that trade kills jobs and saps America’s economic power. In this context, it is critically important that students understand the nature and benefits of comparative advantage. That is the focus of this chapter. The chapter also discusses the sources of resistance to trade and the impact of trade barriers on employment and living standards. President Trump’s extended trade war with China and his attacks on NAFTA provide plenty of discussion material.

Capstone

Chapter 17: Theory versus Reality—This unique chapter confronts the perpetual question of why economies don’t function better if our economic theories are so perfect. The chapter starts by reviewing the major policy tools and their idealized uses. Then we contrast those expectations with our less-than-perfect economic record. What causes this performance gap? A variety of institutional, political, and implementation constraints are illustrated. President Trump’s feuds with the Fed and President Biden’s inability to secure bipartisan support are part of the story. The chapter ends by asking students whether they favor more or less policy intervention, given the mixed bag of past successes and failures.

ASSURANCE OF LEARNING READY

Many educational institutions today are focused on the notion of *assurance of learning*, an important element of some accreditation standards. *Essentials of Economics* is designed specifically to support your assurance of learning initiatives with a simple yet powerful solution.

Each test bank question for *Essentials of Economics* maps to a specific chapter learning objective listed in the text. You can use Connect Economics or our test generator software to easily query for learning objectives that directly relate to the learning objectives for your course. You can then use the

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The statements contained in *Essentials of Economics* are provided only as a guide for the users of this textbook. The AACSB leaves content coverage and assessment within the purview of individual schools, the mission of the school, and the faculty. While *Essentials of Economics* and the teaching package make no claim of any specific AACSB qualification or evaluation, we have within *Essentials of Economics* labeled selected questions according to the six general knowledge and skills areas.

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Page xiii

INSTRUCTOR'S RESOURCE MANUAL

The Instructor's Resource Manual is designed to assist instructors as they cope with the demands of teaching a survey of economics in a single term. The manual has been fully updated for this edition by Larry Olanrewaju of John Tyler Community College. Each chapter of the Instructor's Resource Manual contains the following features:

- *What is this chapter all about?* A brief summary of the chapter.
- *New to this edition* A list of changes and updates to the chapter since the last edition.

- *Lecture launchers* Designed to offer suggestions on how to launch specific topics in each chapter.
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- *News Wires* A list of News Wires from the text is provided for easy reference.
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- *Answers to the chapter questions and problems* The *Instructor's Resource Manual* provides answers to the end-of-chapter questions and problems in the text, along with explanations of how the answers were derived.
- *Flipped and online class applications* These activities can be used as an in-class assignment or as an integrated part of your online or hybrid course. In many of these assignments, students will interact with websites to gather and interpret data. Also available on the website.
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Test Bank

The Test Bank has been rigorously revised to align with the new edition and incorporate a variety of algorithmic problems to further ensure academic integrity and provide an opportunity for students to be assessed on the same content while receiving a variation of questions. Co-author Karen Gebhardt and Alpna Bhatia of the University of Colorado assure a high level of quality and consistency of the test questions and the greatest possible correlation with the content of the text. All questions are coded according to chapter

learning objectives, AACSB Assurance of Learning, and Bloom’s Taxonomy guidelines. The computerized Test Bank is available through Test Builder in Connect.

Test Builder is a cloud-based tool that enables instructors to format tests that can be printed or administered within an LMS. Test Builder offers a modern, streamlined interface for easy content configuration that matches course needs, without requiring a download. Test Builder allow you to:

- Access all test bank content from a specific title.
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Remote Proctoring and Browser-Locking Capabilities

Page xiv

New remote proctoring and browser-locking capabilities, hosted by Proctorio within Connect, provide control of the assessment environment by enabling security options and verifying the identity of the student.

Seamlessly integrated within Connect, these services allow instructors to control students’ assessment experience by restricting browser activity, recording students’ activity, and verifying students are doing their own work.

Instant and detailed reporting gives instructors an at-a-glance view of potential academic integrity concerns, thereby avoiding personal bias and supporting evidence-based claims.

PowerPoints

Roshan Khattry of Spokane Falls Community College and Stephen Slice of University of South Carolina have prepared and reviewed a concise set of Instructor PowerPoint presentations to complement the new edition. Developed using Microsoft PowerPoint software, these slides are a step-by-step review of the key points in each of the book’s chapters. They are equally useful to the student in the classroom as lecture aids or for personal review at

home or the computer lab. The slides use animation to show students how graphs build and shift.

Flipped and Online Class Applications

To keep *Essentials* connected to the real world, flipped and online class applications, updated by Charles Newton of Houston Community College, appear in the Instructor Resources section in Connect for each chapter. These require the student to access data or materials on a website and then use, summarize, or explain this external material in the context of the chapter's core economic concepts. The *Instructor's Resource Manual* provides answers to the web-based activities.

Digital Image Library

A digital image library of all figures from the textbook is available on the Instructor's Resource section in Connect. Professors can insert the exact images from the textbook into their presentation slides or simply post them for student viewing on their course management site.

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Page xv

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