

Online Trust and Financial Performance: A Case of Bookstores

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With the rapid growth of electronic commerce, developing online consumer trust is crucial for success of online transactions. Companies that design websites that online shoppers perceive to be trustworthy show stable growth in their financial performance. This study offers a review of online bookstores' trustworthiness as evaluated by study respondents and tracks performance of two companies. Our analysis of the financial performance links online trust and companies' profitability.

INTRODUCTION

Electronic commerce – or e-commerce – is understood as an exchange of values (selling tangible and intangible products) online (Mukherjee and Nath, 2007; Torres, et al., 2014). With its increased popularity, the question for retailers is not whether to participate or not to participate in e-commerce but rather how to communicate with customers via hedonic and utilitarian website features (Richard and Habibi, 2016).

Companies cannot ignore the significant role that trust plays in their business operations. Building trust is viewed as a strategy of long-term investment in loyal customers as loyal customers spend more money, enhance a company's reputation through word of mouth, and are less likely to switch to a competitor (Frost, et al., 2010). Trust is especially important in an online environment, where buyers are dependent on unknown e-vendors who may behave in an opportunistic way and take advantage of buyers' vulnerability (Gefen and Straub, 2003).

The relationship between trust and customer's intention to purchase a product online has been established by numerous studies (Eastlick, et al, 2006; Gefen and Straub, 2003; Kim, et al., 2008; Liu, et al., 2004); however, direct correlations of online trust and company's financial performance had not been studied in depth.

Academic studies of the concept of online trust encompass areas ranging from investigating the impact of privacy and security on trust and behavioral intention to examining the role of web site appeal on developing initial trust leading to a consumer's initiation of an interaction. Regardless of the focus of the investigation, studies and models of trust emphasize that a consumer's decision to trust or not to trust is based on evaluation of other party trustworthiness (Altinay, et al., 2014; Dietz, et al., 2010). In the case

of positive evaluation, a trusting relationship develops between an e-vendor and an online buyer which is likely to lead to repeat purchases and long-term continuing benefits (Frost, et al., 2010).

The first part of this study explores customers' perceptions of online trust cues incorporated into the design of a commercial web site. It analyses customers' perceptions of the website trustworthiness and identifies trust cues used by consumers to evaluate a website.

The second part of the study reviews financial statements of the websites in an attempt to track trends in revenues and profits. The results of the financial analysis were compared to the results of customers' evaluation of websites' trustworthiness.

THEORETICAL BACKGROUND

Online Trust

Traditionally, the definition of trust implied a type of relationship between two or more people which was described as "*the willingness of a party to be vulnerable to the actions of another party based on the expectation that the other will perform a particular action important to the trustor irrespective of the ability to monitor or control that other party*" (Mayer, et al., 1995, p.712, emphasized in the original). It reflects an individual's attitude toward a risky situation impacting that individual's behaviour. In a commercial situation, this attitude leads to the intention to purchase (McKnight, et al., 2002) which meets the ultimate goal of a business.

Technological developments and the increase in e-commerce transactions have extended the notion of trust to the relationship between a human (customer) and the Internet, an artefact created by humans. This extension of traditional trust into online trust is clarified in the following definition of online trust: "a consumer willingness to engage in an online transactional relationship, despite being vulnerable to the seller as a result of the lack of verifiable and adequate knowledge of the vendor, the product/service being sold and no guaranteed assurance of how or where disputes will be resolved" (Austin, et al., 2006, p. 25). This definition reflects a consensus among online trust researchers that the nature of, and basic meaning of, online trust is not different from the concept of face-to-face trust (Shankar, et al. 2002; Jarvenpaa and Rao, 2003; Corritore, et al. 2003, Wang and Emurian, 2005).

The online trust elements or "building blocks of trust models" (Jarvenpaa and Rao, 2003 p. 231) are the same as in traditional trust (Wang and Emurian, 2005):

1. online trust, just like traditional trust, is developed between two parties: trustor and trustee (although a trustee is a web site or a vendor who uses the Internet to represent its business)
2. online trust occurs in an environment that is highly complex and uncertain,
3. a trustor shows vulnerability and
4. a trustor takes a risk while the decision to take a risk is affected by trustor's personal traits and existing technology.

Although those four elements are the same, the virtual environment in which online trust develops is quite different from the traditional face-to-face environment. In the virtual environment, traditional observations of human behavior are impossible. There is no eye contact between a trustor and a trustee. There are no handshakes between the parties. There is only a website which serves as a storefront for an online company (McKnight, et al., 2002; Hampton-Sosa and Koufaris, 2005).

There are some other aspects of e-commerce that add risk to online shopping. For example, the customer is committed to an exchange transaction before the vendor is (as the customer has to pay in advance), there is also space and time separation between paying for the product and receiving it (Riegelsberger and Sasse, 2001). Customers cannot determine the quality of the product offered online and the choice of technology that the e-vendor uses for online transactions is beyond the customer's control (Cheung and Lee, 2006; Grabner-Kraeuter and Kaluscha, 2008).

To overcome the problem of online transactions as being "faceless and intangible" (Beldad, et al., 2010, p. 857), e-vendors design web sites with cues that signal their trustworthiness. Online customers

review those cues which become the basis for judging how trustworthy the online vendor is and whether it can be trusted.

Customer Buying Behavior and Marketing Implications

Consumers see Internet as the information and business medium (Goldsmith and Bridges, 2000; Goldsmith, 2001; Goldsmith and Goldsmith, 2002; UCLA, 2000, 2001, 2003). According to Yen and Chang (2015), technology can enhance consumers' perceptions of shopping experiences.

Studies have shown that trust has a positive influence on buying behavior. Trust can reduce uncertainty during the consumer shopping process (Morrow, et al., 2004; Kenning, 2007; Hamer, 2011). Customer loyalty, prior to which customer trust has to be established, is related to profitability (Hallowell, 1996). Customer loyalty also helps companies' financial performance. Loyal customers tend to have close relationship with the company. Customer loyalty will boost sales, increase market share, and lead to positive Word of Mouth (Khan and Rizwan, 2014; Gee, et. al, 2008). Studies done by Liang et al. (2009) and Smith and Wright (2004) have proven that customer loyalty will have a positive impact on companies' profitability.

According to Toma (2016, p. 90), those American companies that implemented customer relationship management, saw the following results during the first three years of the program:

- A minimum 10% per year increase in gross sales revenue per sales
- A minimum 5% decrease in general and administrative cost of sales
- A minimum 5% increase in win rates for forecasted sales
- A minimum 5% improvement in the quality rating provided by customers

Furthermore, companies can increase prices without a negative impact on sales performance since loyal customers are less price elastic (Smith and Wright, 2004; Belás and Gabčová, 2016).

As consumers' Internet activities continue to grow, companies are able to generate massive amount information about consumers. Handling privacy and security of in the Internet of Things (IoT) will be an issue addressed by many companies (Britton, 2016). More and more consumers are paying with their virtual wallet. How to store and secure the financial data will be another issue that companies need to address.

Evaluation of Financial Performance

In the traditional environment, trust was found to influence the decision consideration but not the actual purchase; however, in the online environment, trust affects the purchase intentions (Shankar, et al., 2002; Urban, et al., 2009) which in turn, impact the overall company's performance. Thus, developing online trust is important for a variety of stakeholders, including customers, employees, suppliers, distributors, partners, and stockholders (Shankar, et al., 2002).

Although there have been very limited previous studies on the relationship between customer trust and financial performance, some studies focus on companies in one country setting (e.g., Luo, et al., 2004; Luo, et al., 2008), whereas others tend to be at the conceptual framework level (Shankar, et al., 2002).

The technological development in electronic systems has also brought about significant impact for online customers in the financial industry. However, in the finance field, the issue of online trust and financial performance has been investigated mainly from the perspective of online trust for brokers and trading platforms and individual investors' satisfaction and investment performance (Balasubramanian et al., 2003; Roca, et al., 2009; Barber and Odean, 2002). For example, Balasubramanian, et al. (2003) examine the link between online investors' perceived trustworthiness of the online broker and the investors' satisfaction and found a positive relationship between these two variables using the method of survey study. Another study by Barber and Odean (2002) find that increased trust on online brokers from online individual investors leads to worse investing and trading performance than they use phone-based brokers because these investors get a "feeling of empowerment" and trade too much than they should. None of the studies have looked the customers' online trust and the financial performance of the brokers

in the finance field. Given the growing prevalence of online shopping, the link between online trust and companies' financial performance is relevant and meaningful as a main topic of discussion for this paper.

Method

Unlike the majority of studies of online trust which are conducted using quantitative methods, this research employed a qualitative research framework for the first part of the study built around the repertory grid technique (Kelly, 1963). The theoretical foundation for this framework was created based on several theories developed across multiple disciplines. For example, the theory of information asymmetry between transacting parties (Akerlof, 1970) and the economics signaling theory (Spence, 2002) explained why signals of trustworthiness are formed and communicated. The psychological theory of personal constructs (Kelly, 1963) shows how perceptions are construed. The prominence-interpretation theory (Fogg, 2003) provides a basis for identification of cues and their importance. Symbolic interactionism (Blumer, 1980; Denzin, 1969) and value-congruity relationship theories (Kumar, 2013) focus on consumer behavior. The commitment-trust theory of marketing management (Morgan and Hunt, 1994) emphasizes the role of consumer trust in keeping customers satisfied, and the significance of strategic planning for gaining and retaining customers.

To obtain and analyze online buyers' subjective opinions about web site trust cues, and to reveal individual patterns, this study utilized the repertory grid technique. That technique had not previously been used in studies of online trust cues. This was done in response to the call for more qualitative studies of trust (Mollering, 2006), where research methods look into and evaluate the respondents' experiences and perceptions rather than a researcher's expectations.

The repertory grid technique has been introduced by Kelly (1963) as an extension of his personal constructs theory. Kelly's (1963) theory is based on two major assumptions:

- (1) people act as scientists who explore the world around them, develop constructs in an attempt to create meaning and make sense out of events, and use those constructs to anticipate future events in their lives. If those constructs are not validated, then people change constructs;
- (2) relations between constructs are organized in an interpretation system that, on the one hand, helps to understand an event but, on the other hand, restricts people's behavior.

As applied in the context of identifying and interpreting online trust cues, Kelly's (1963) personal constructs theory describes an online consumer behavior pattern: customers explore online stores and, based on their shopping experiences, develop constructs that are organized into a system that guides their future behavior. Therefore, the theoretical foundation and methodological framework selected for this study meet the goals of customer-focused research into the online trust building process.

Data Collection and Analysis

Seventy volunteers from three countries, Germany, Russia, and the United States, contributed to a qualitative exploratory study of online trust cues embedded in a commercial web site. Using a repertory grid and evaluating five online bookstores, participants shared their own perceptions of which web site elements and properties they identified as trust signals. As a result of the study, 433 constructs were elicited and analyzed. Two independent reviewers contributed to the first stage of the analysis – categorization and a reliability check of the grouping all constructs into categories. It was established that signals that are identified by online shoppers as trust cues could be divided into 14 categories. Although the number of categories for each country was the same, the variety of categories was different. For example:

- The United States sample consisted of: ease of use, sales, guarantees, reputation, design, physical location, scalability, security, customization, customer feedback, company information, customer support, services, and social media.
- The German sample consisted of: ease of use, sales, customer feedback, ease of payment, design, services, reputation, language, customer support, guarantees, security, delivery, company information, and social network.

- The Russian sample consisted of: company information, customer feedback, customer support, customization, delivery, design, ease of use, guarantees, language, location, reputation, sales, social network, and transparency.

The answer to the research question identified specific categories of trust cues as recognized and described by online consumers. This comprehensive list of 433 constructs, grouped into fourteen categories, by itself offers a practical contribution to businesses with an online presence. It shows which web site elements are noticed and valued by customers, thus allowing for a more customer focused approach in web design.

In preparation for data analysis, all constructs solicited from respondents were independently categorized by this researcher and two reviewers. This provided objective groupings of the online trust cues identified by the respondents. To triangulate the data, four types of content analysis were applied: distribution of constructs in categories (Curtis, et al. 2008; Goffin, et al., 2006), frequency of construct usage (Boyle, 2005; Goffin and Koners, 2011), importance (Fogg, 2003; Tomico, et al., 2009), and hierarchical placement of constructs (Crudge and Johnson, 2007). Based on the results of these types of content analysis, the websites were rated according to the perceived trustworthiness (from the customers' perspective). The results of web sites' levels of perceived trustworthiness as evaluated by all participants of this study are presented in Table 1. The number was calculated as an average of the ratings on the seven-point Likert scale within each sample.

Although it appears that Russian participants were more cautious about evaluating book stores (as the difference in the range of the evaluation varies from 2.90 – 5.05 as compared to the USA respondents 2.38 – 5.95, or the German contributors 2.77 – 6.12), the final result is the same. On the continuum from the web site perceived by the respondents to be the most trustworthy to that perceived to be the least trustworthy, the online stores used in the study are ranked in the same order by all three samples: Amazon, followed by BAM! Books-A-Million! These two were followed by Alibris, Powell's Books, and Biblio.

**TABLE 1
RESULTS OF THE WEB SITE EVALUATIONS**

Web site	USA sample (average score on the seven-point scale)	German sample (average score on the seven-point scale)	Russian sample (average score on the seven-point scale)
Alibris	4.68	4.32	4.82
Amazon	5.95	6.12	5.05
BAM! Books-A-Million!	5.22	4.33	4.86
Biblio	4.44	3.99	4.58
Powell's Books	4.62	4.07	4.81

The findings of the first part of this study are validated by its research procedure as it incorporated the following ways of ensuring the quality of a study as proposed by Kassarian (1977), Sekaran (1983), and Silverman (2010):

- A research method appropriate for the study of consumers' perceptions was used to gather subjective descriptions of web site trustworthiness. The repertory grid technique used in this research is an extension of the personal construct theory developed by Kelly (1963) for the analysis of how people construe meaning and make sense of the phenomena occurring in their personal lives.
- This cross-cultural study involved three countries rather than traditional two (Sekaran, 1983).
- The inter-coder agreement between two independent reviewers and the researcher achieved a level above 90% for categorization of constructs in all three samples, which is found to be acceptable (Jankowicz, 2004).
- Triangulation of four types of analysis offered different ways of reviewing the elicited data to ensure that all constructs were analysed. This approach of plurality (Frost, et al., 2010) considered various aspects of constructs related to perceived trustworthiness of web sites as described by the study's participants.

Financial Analysis of Websites

This study provides an empirical case review and attempts to shed light on this important link between online trust and firm financial performance. Due to the private status of three companies when the surveys were conducted, financial statements are not available on these companies' websites or other regulatory agencies. However, as we can see from Table 2, we obtain these companies' financial performance through fairly reliable anecdotal evidence and reports that are available online.

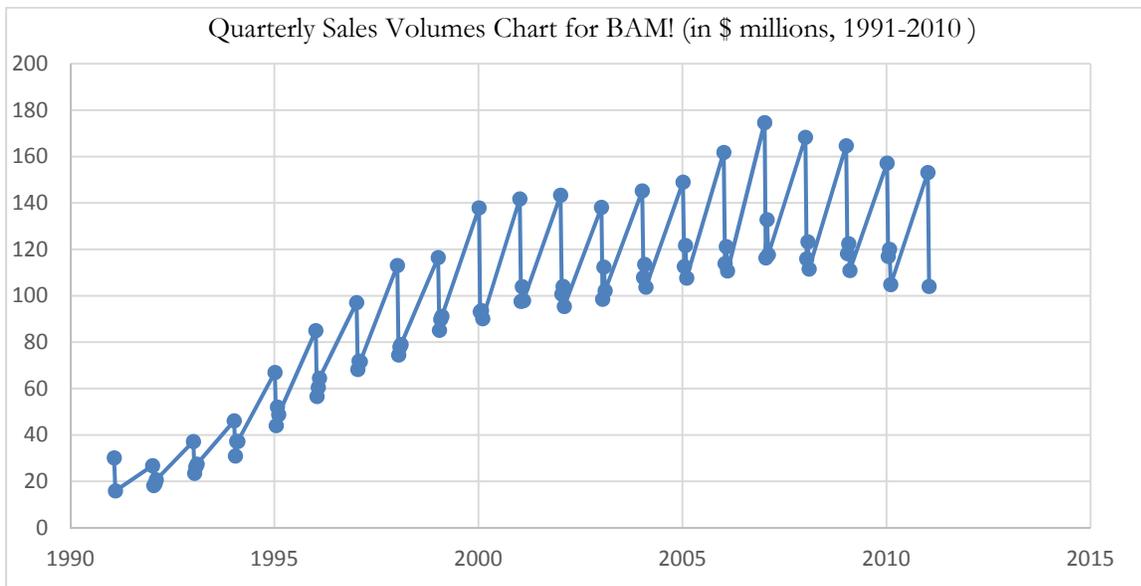
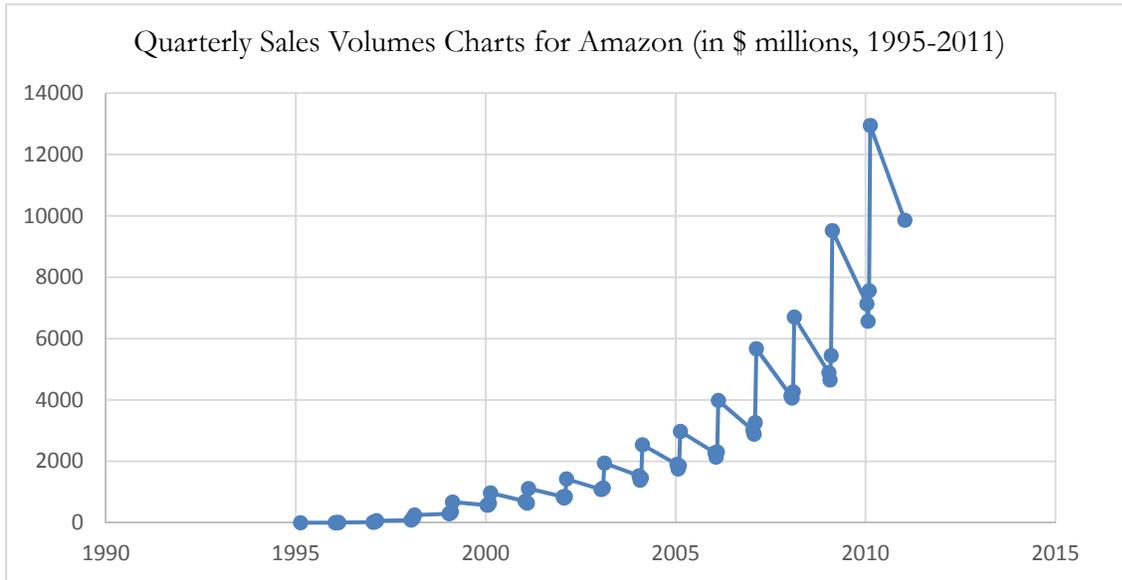
TABLE 2
BASIC CHARACTERISTICS AND PERFORMANCE OF THE FIVE CASES¹

Characteristics	Alibris	Amazon	BAM!	Biblio	Powell's
Firm status	Private	Public	Public (went private in Dec.2015)	Private	Private
Year founded	1997	1994	1917	2000	1971
Headquarters	Emeryville, California	Seattle, Washington	Birmingham, Alabama	Asheville, North Carolina	Portland, Oregon
Sales	\$100 Million (8/15/2013)	\$107 billion (2015)	509 million (FY 2010)	N/A	\$45 million (as of 2009)
# of employees	120	222,400 (Oct. 2015)	250+	10 (2010)	about 500

The sales revenues of the firms under study in this paper demonstrate a considerably close correlation with the results regarding online trust from Table 1. The companies that rank higher from the online trust survey also generate high sales revenues. To see the time trends of the sales revenue, we also obtain sales data for two public companies (Amazon.com and BAM!) from the U.S. Securities and Exchange

Commission's (SEC) Electronic Data Gathering, Analysis, and Retrieval system (EDGAR). As Figure 1 shows, the quarterly sales volumes for Amazon and BAM! in the recent years have been steady and growing overall, although there are seasonal variations for these revenues.

FIGURE 1
QUARTERLY SALES VOLUMES CHARTS FOR AMAZON AND BAM!



The quarterly revenues for the two companies are based on different starting points and numerical scales due to the different sizes of the two companies. For the purpose of examining the company's trend over the years in terms of the financial performance and compare those trends, we also calculate the percentage change of the two companies' annual revenues and compare them in Table 3 to show the revenue growths in terms of annual percentage changes for the two companies over the years. Table 3

demonstrates that Amazon.com has a much stable and higher revenue growth than BAM! over the years with available data.

TABLE 3
COMPARING ANNUAL REVENUE: AMAZON.COM VS. BAM!

Year	Amazon		BAM!	
	Annual revenue	Change (%)	Annual revenue	Change (%)
1995	0.1		52.9	40%
1996	3.9	2981%	66.6	26%
1997	36.9	839%	77.2	16%
1998	152.5	313%	86.1	12%
1999	410.0	169%	95.7	11%
2000	690.5	68%	103.7	8%
2001	780.6	13%	110.3	6%
2002	983.2	26%	110.9	1%
2003	1315.9	34%	112.8	2%
2004	1730.3	31%	117.6	4%
2005	2122.5	23%	122.7	4%
2006	2677.8	26%	126.9	3%
2007	3708.8	39%	135.4	7%
2008	4791.5	29%	129.8	-4%
2009	6127.3	28%	129.0	-1%
2010	8551.0	40%	124.8	-3%

To gain more understanding of the financial trends of those two companies - Amazon and BAM!, we also demonstrate comparisons of a few profitability ratios based on their financial reports. The specific ratios we use to compare the two companies are return on assets (ROA), market-to-book (M/B), and cash flow from operations (CFO).

Table 4 compares financial performance measurements over the past 19 years for Amazon.com and BAM!. Panel A compares ROA, Return on Assets, defined as Income before extraordinary items scaled by total assets. ROA measures overall efficiency of firm in managing assets and generating profits. For example, in the year of 2004, the ROA for Amazon.com is 18.1%, which indicates that Amazon.com generates 18.1 cents of profits out of every dollar of invested assets. For the same year, the ROA for BAM! Is 3.4%, which means that BAM! Generates only 3.4 cents of profit out of every dollar it invests in assets.

Panel B, compares M/B, market-to-book, the market value of equity (shares outstanding * fiscal year closing price) scaled by Total book value of shareholders' equity. M/B is a financial ratio used to compare a company's current market price to its book value. A higher M/B ratio implies that investors expect the company to create more value from a given set of assets, and that the market value of the firm's assets is significantly higher than their accounting value. For instance, in the year of 2005, the M/B for Amazon.com is 79.7, which shows that the investors are very optimistic about the market value of company's assets, with a 79.7 multiple of its accounting value. However, for the same year, the M/B for BAM! Is only 1.3, which means that investor expect its market value is only 1.3 times of its accounting value.

TABLE 4
COMPARING FINANCIAL PERFORMANCE: AMAZON.COM VS. BAM!

Year	Panel A: ROA			Panel B: MB			Panel C: CFO		
	AMZN	BAMM	Difference	AMZN	BAMM	Difference	AMZN	BAMM	Difference
1995	-28.0%	3.9%	-31.9%	N/A	1.6		-21.4%	-7.7%	-13.7%
1996	-69.8%	2.5%	-72.3%	N/A	1.1		-21.0%	1.1%	-22.1%
1997	-18.5%	2.8%	-21.4%	50.6	1.0	49.6	2.4%	2.3%	0.0%
1998	-19.2%	1.7%	-20.9%	122.9	1.7	121.2	4.8%	6.5%	-1.7%
1999	-29.1%	2.1%	-31.2%	98.7	1.1	97.6	-3.7%	4.3%	-8.0%
2000	-66.1%	1.0%	-67.1%	-5.7	0.3	-6.1	-6.1%	2.9%	-9.0%
2001	-34.0%	1.3%	-35.3%	-2.8	0.4	-3.2	-7.3%	8.4%	-15.7%
2002	-7.5%	0.8%	-8.4%	-5.4	0.3	-5.7	8.8%	3.5%	5.2%
2003	1.6%	2.5%	-0.9%	-20.5	0.8	-21.3	18.1%	11.7%	6.4%
2004	18.1%	3.4%	14.7%	-79.9	1.1	-81.0	17.4%	15.7%	1.8%
2005	9.0%	4.2%	4.8%	79.7	1.3	78.4	19.8%	11.8%	8.1%
2006	4.4%	6.2%	-1.9%	37.9	2.0	35.9	16.1%	7.0%	9.1%
2007	7.3%	5.8%	1.5%	32.2	1.7	30.5	21.7%	12.1%	9.6%
2008	7.8%	3.8%	4.0%	8.2	0.4	7.9	20.4%	14.0%	6.4%
2009	6.5%	5.1%	1.5%	11.4	0.9	10.5	23.8%	11.7%	12.1%
2010	6.1%	3.3%	2.9%	11.8	0.8	11.1	18.6%	10.8%	7.8%
2011	2.5%	-0.8%	3.3%	10.2	0.3	9.8	15.4%	9.6%	5.8%
2012	-0.1%	0.9%	-1.0%	13.9	0.3	13.6	12.8%	5.3%	7.6%
2013	0.7%	-2.5%	3.1%	18.8	0.3	18.5	13.6%	1.5%	12.2%

Panel C shows *CFO*, defined as cash flow from operations, and divided by beginning-of-period total assets. *CFO* is the amount of cash generated from/used by a business enterprise's normal, ongoing operations during an accounting period scaled by total assets. Since the company's ongoing operations is regarded as its core business, this ratio provides additional information in addition to the traditional profit ratio such as ROA and market ratio such as M/B. For example, in the year of 2006, the *CFO* for Amazon.com is 16.1%, which means that the company generates 16.1 cents of cash from every dollar of its total assets, compared to the *CFO* for BAM! in the same year of 7.0%, which indicates the company only generates 7 cents of cash from every dollar of its total assets.

Table 4 shows the comparisons of these ratios between Amazon.com and BAM! over the past nineteen years. Although in the first few years of this time period, Amazon.com had some bad years in terms of ROA, M/B, and *CFO*, it caught up with BAM! in the next few years and gained the upper hand for most of the following years except for a couple of exceptions such as the years of 2006 and 2012 for ROA. The pattern emerged from the comparisons provide further evidence that the higher trust level for Amazon.com translates into higher profitability for this company as well. It is reasonable to suggest that there is some noticeable association between online trust on a company and its subsequent financial performance.

DISCUSSION

Earlier research of the relationship between trust and business performance took one of the two approaches: economic or psychological. Economic approach was based on the transaction costs while psychological – on the impact of trust and loyalty on the company's financial situation (Singh and Sirdeshmukh, 2000).

The economic perspective based on the transaction-cost economics acknowledges that the productivity of a value chain depends on both production costs and transaction costs (Dyer and Chu, 2006; Williamson, 1981). Production costs are directly related to the process of creating a value for a customer. Transaction costs occur both before and after the exchange as businesses first search for partners and developing contracts, and then monitor and control whether all contract obligations are fulfilled (Bromiley and Cummings, 1995). The financial analysis of the business performance gives a look into the internal operations.

The psychological perspective reflects the role of trust within an organization as well as consumer trust toward that organization. The first part of this study used this approach as it focused on customer evaluation of a company's trustworthiness.

The results of this study support Singh and Sirdeshmukh (2000) proposition that the economic and psychological approaches can work together in order to enhance customer loyalty and trust which impact the company's performance.

Trust in exchange relationships is valuable as previous research (Dyer and Chu, 2006; Sako, 2006; Williamson, 1981) showed that trust:

- Reduces transaction costs and allows for greater flexibility in adjusting to changing business environment
- Results in improved information sharing that leads to continuous improvement and learning
- Invests into future returns

CONCLUSION

Research of business strategies shows that new developments in the area of telecommunications and increased number of business financial transactions in the virtual environment force managers to implement e-commerce strategies, which emphasize value creation and value capturing (Torres, et al., 2014). These business strategies alone, however, do not guarantee success. Business models should be focusing on how meet customers' needs and differentiate themselves. One of the differentiation variables is a company's non-imitable relationships with customers based on trust and loyalty (Morgan and Hunt, 1994; Torres, et al., 2014). Creating these customer relationships has experienced a significant increase during the last decade as the Internet provided companies a tool to customize product offers and employ direct interaction with customers, which "have enabled companies for successfully and profitably satisfying their customers" (Habul, et al., 2012, p. 27).

ENDNOTES

¹ The sources for the sales revenues are as follows:

For Alibris, <https://oregon.tie.org/event/40/mentor-connect-kanth-gopalpur>.

For Amazon.com, <http://www.sec.gov/Archives/edgar/data/1018724/000101872416000170/amzn-20151231xex991.htm>.

For BAM!, it is from the 10-K report of 2010.

For Powell's, <http://www.bizjournals.com/portland/stories/2010/03/01/daily57.html>.

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