Your Paper

You

November 6, 2024

Question 1: Reformulation

1. Reformulate the income statement to be suitable for financial statement analysis and valuation.

Reformulated PNDL	2023	2022	2021
Revenues (O)	1 802 184,00	1 430 208,00	749 381,00
Other operating income (O)	24 080,00	8 040,00	4 060,00
Total revenues and other operating income	*1 826 264,00*	*1 438 248,00*	*753 441,00*
Voyage expenses and commissions (O)	618 595,00	605 544,00	392 697,00
Ship operating expenses (O)	176 533,00	175 164,00	164 246,00
Administrative expenses (O)	53 528,00	47 374,00	26 424,00
Contingent rental income (O)		- 623,00	- 3 606,00
-Total operating expenses	848 656,00	827 459,00	579 761,00
EBITDA	**977 608,00**	**610 789,00**	**173 680,00**
Depreciation (O)	230 942,00	165 170,00	165 205,00
EBIT	**746 666,00**	**445 619,00**	**8 475,00**
- Income tax expense	- 205,00	- 412,00	- 4 633,00
-/+ Tax shield from NFE	- 19 818,92	6 722,32	- 4 130,50
Operating tax expense	- 20 023,92	6 310,32	- 8 763,50
NOPAT	**726 642,08**	**451 929,32**	**- 288,50**
Finance income (F)	18 065,00	1 479,00	121,00
Finance expense (F)	- 171 336,00	- 45 330,00	- 44 244,00
Gain on marketable securities (F)	22 989,00	58 359,00	7 677,00
Share of results of associated companies (F)	3 383,00	14 243,00	- 724,00
Foreign currency translation gain (loss) (F)	- 39,00	226,00	28,00
Dividends received (F)	36 852,00	1 579,00	18 367,00
Net Financial Expense (NFE)	**- 90 086,00**	**30 556,00**	**- 18 775,00**
+/- Tax Shield from NFE	19 818,92	- 6 722,32	4 130,50
Net income	**656 375,00**	**475 763,00**	**- 14 933,00**

2. Reformulate the balance sheet to NOA format step by step, i.e., doing the TA format, then the CE format, and finally, the NOA format.

We start off by presenting the balance sheet. !!!! Write some words to justify our choice of categorization of financing or operating. !!!!

Assets	2023	2022
Current Assets		
Cash and cash equivalents (F)	308 322,00	254 525,00
Marketable securities (F)	7 432,00	236 281,00
Trade and other receivables (O)	124 647,00	139 467,00
Related party receivables (O)	19 292,00	13 485,00
Inventories (O)	135 161,00	107 114,00
Voyages in progress (O)	110 061,00	110 638,00
Prepaid expenses and accrued income (O)	15 753,00	14 255,00
Other current assets (O)	7 258,00	5 285,00
Total current assets	**727 926,00**	**881 050,00**
Non-current Assets		
Newbuildings (O)		47 991,00
Vessels and equipment (O)	4 633 169,00	3 650 652,00
Right-of-use assets (O)	2 236,00	3 108,00
Goodwill (O)	112 452,00	112 452,00
Derivative instruments receivable (O)	39 117,00	53 993,00
Investment in associated companies (O)	12 386,00	16 302,00
Loan notes receivable (O)		1 388,00
Prepaid consideration (O)	349 151,00	
Other non-current assets (O)	6 329,00	1 507,00
Total non-current assets	**5 154 840,00**	**3 887 393,00**
Total Assets	**5 882 766,00**	**4 768 443,00**

Liabilities and Equity	2023	2022
Current liabilities		
Short-term debt and current portion of long-term debt (F)	261 999,00	277 854,00
Current portion of obligations under leases (O) Assumption	1 104,00	1 024,00
Related party payables (O)	47 719,00	31 248,00
Trade and other payables (O)	98 232,00	81 533,00
Total current liabilities	**409 054,00**	**391 659,00**
Non-current liabilities		
Long-term debt (F)	3 194 464,00	2 112 460,00
Obligations under leases (F)	1 430,00	2 372,00
Other non-current payables (O)	472,00	2 053,00
Total non-current liabilities	**3 196 366,00**	**2 116 885,00**
Total Liabilities	**3 605 420,00**	**2 508 544,00**
Equity		
Share capital	222 623,00	222 623,00
Additional paid in capital	604 687,00	604 687,00
Contributed surplus	1 004 094,00	1 004 094,00
Accumulated other reserves	415,00	454,00
Retained earnings	445 999,00	428 513,00
Total equity attributable to the shareholders of the Company	**2 277 818,00**	**2 260 371,00**
Non-controlling interest	- 472,00	- 472,00
Total Equity	**2 277 346,00**	**2 259 899,00**
Total liabilities and equity	**5 882 766,00**	**4 768 443,00**

From our balance sheet we group together the items into 7 groups. For assets we assign each item to either Operating Non-Current Assets(ONCA), Financial assets(FA) or Operating Current Assets(OCA). Our liabilities and equity items are assigned to either Equity(E), Operating Non-Current Liabilities(ONCL), Interest Bearing Debt(IBD), or Operating Current Liabilities.

TA Format

Assets	2023	2022
Newbuildings (O)	-	47 991,00
Vessels and equipment (O)	4 633 169,00	3 650 652,00
Right-of-use assets (O)	2 236,00	3 108,00
Goodwill (O)	112 452,00	112 452,00
Loan notes receivable (O)		1 388,00
Derivative instruments receivable (O)	39 117,00	53 993,00
Investment in associated companies (O)	12 386,00	16 302,00
Prepaid consideration (O)	349 151,00	-
Other non-current assets (O)	6 329,00	1 507,00
ONCA	**5 154 840,00**	**3 887 393,00**
Cash and cash equivalents (F)	308 322,00	254 525,00
Marketable securities (F)	7 432,00	236 281,00
FA	**315 754,00**	**490 806,00**
Trade and other receivables (O)	124 647,00	139 467,00
Related party receivables (O)	19 292,00	13 485,00
Inventories (O)	135 161,00	107 114,00
Voyages in progress (O)	110 061,00	110 638,00
Prepaid expenses and accrued income (O)	15 753,00	14 255,00
Other current assets (O)	7 258,00	5 285,00
OCA	**412 172,00**	**390 244,00**
TA (ONCA+FA+OCA)	**5 882 766,00**	**4 768 443,00**

Liabilities and Equity	2023	2022
Equity		
Share capital	222 623,00	222 623,00
Additional paid in capital	604 687,00	604 687,00
Contributed surplus	1 004 094,00	1 004 094,00
Accumulated other reserves	415,00	454,00
Retained earnings	445 999,00	428 513,00
Total equity attributable to the shareholders of the Company	**2 277 818,00**	**2 260 371,00**
Non-controlling interest	- 472,00	- 472,00
E	**2 277 346,00**	**2 259 899,00**
Other non-current payables (O)	472,00	2 053,00
ONCL	**472,00**	**2 053,00**
Short-term debt and current portion of long-term debt (F)	261 999,00	277 854,00
Long-term debt (F)	3 194 464,00	2 112 460,00
Obligations under leases (F)	1 430,00	2 372,00
IBD	**3 457 893,00**	**2 392 686,00**
Related party payables (O)	47 719,00	31 248,00
Trade and other payables (O)	98 232,00	81 533,00
Current portion of obligations under leases (O) Assumption	1 104,00	1 024,00
OCL	**147 055,00**	**113 805,00**
Total E+ONCL+IBD+OCL	**5 882 766,00**	**4 768 443,00**

To go from TA format to CE format, we.....

CE Format

Capital Employed	2023	2022
Newbuildings (O)	-	47 991,00
Vessels and equipment (O)	4 633 169,00	3 650 652,00
Right-of-use assets (O)	2 236,00	3 108,00
Goodwill (O)	112 452,00	112 452,00
Loan notes receivable (O)	-	1 388,00
Derivative instruments receivable (O)	39 117,00	53 993,00
Investment in associated companies (O)	12 386,00	16 302,00
Prepaid consideration (O)	349 151,00	-
Other non-current assets (O)	6 329,00	1 507,00
Other non-current payables (O)	- 472,00	- 2 053,00
NONCA	**5 154 368,00**	**3 885 340,00**
Trade and other receivables (O)	124 647,00	139 467,00
Related party receivables (O)	19 292,00	13 485,00
Inventories (O)	135 161,00	107 114,00
Voyages in progress (O)	110 061,00	110 638,00
Prepaid expenses and accrued income (O)	15 753,00	14 255,00
Other current assets (O)	7 258,00	5 285,00
Related party payables (O)	- 47 719,00	- 31 248,00
Trade and other payables (O)	- 98 232,00	- 81 533,00
Current portion of obligations under leases (O) Assumption	- 1 104,00	- 1 024,00
NOWC	**265 117,00**	**276 439,00**
NOA (NONCA + NOWC)	**5 419 485,00**	**4 161 779,00**
Cash and cash equivalents (F)	308 322,00	254 525,00
Marketable securities (F)	7 432,00	236 281,00
FA	**315 754,00**	**490 806,00**
Total CE (FA + NONCA + NOWC)	**5 735 239,00**	**4 652 585,00**

Equity and IBD	2023	2022
Share capital	222 623,00	222 623,00
Additional paid in capital	604 687,00	604 687,00
Contributed surplus	1 004 094,00	1 004 094,00
Accumulated other reserves	415,00	454,00
Retained earnings	445 999,00	428 513,00
Total equity attributable to the shareholders of the Company	**2 277 818,00**	**2 260 371,00**
Non-controlling interest	- 472,00	- 472,00
E	**2 277 346,00**	**2 259 899,00**
Short-term debt and current portion of long-term debt (F)	261 999,00	277 854,00
Long-term debt (F)	3 194 464,00	2 112 460,00
Obligations under leases (F)	1 430,00	2 372,00
IBD	**3 457 893,00**	**2 392 686,00**
Total E+IBD	**5 735 239,00**	**4 652 585,00**

Lastly, to go from CE format to the final NOA format, we .....

NOA format					
Invested Capital	**2023**	**2022**		**Equity and net interest-bearing debt**	**2023**	**2022**
Newbuildings (O)	-	47 991,00		Share capital	222 623,00	222 623,00
Vessels and equipment (O)	4 633 169,00	3 650 652,00		Additional paid in capital	604 687,00	604 687,00
Right-of-use assets (O)	2 236,00	3 108,00		Contributed surplus	1 004 094,00	1 004 094,00
Goodwill (O)	112 452,00	112 452,00		Accumulated other reserves	415,00	454,00
Loan notes receivable (O)	-	1 388,00		Retained earnings	445 999,00	428 513,00
Derivative instruments receivable (O)	39 117,00	53 993,00		**Total equity attributable to the shareholders of the Company**	**2 277 818,00**	**2 260 371,00**
Investment in associated companies (O)	12 386,00	16 302,00		Non-controlling interest	- 472,00	- 472,00
Prepaid consideration (O)	349 151,00	-		**E**	**2 277 346,00**	**2 259 899,00**
Other non-current assets (O)	6 329,00	1 507,00		Short-term debt and current portion of long-term debt (F)	261 999,00	277 854,00
Other non-current payables (O)	- 472,00	- 2 053,00		Long-term debt (F)	3 194 464,00	2 112 460,00
NONCA	**5 154 368,00**	**3 885 340,00**		Obligations under leases (F)	1 430,00	2 372,00
				Cash and cash equivalents (F)	- 308 322,00	- 254 525,00
Trade and other receivables (O)	124 647,00	139 467,00		Marketable securities (F)	- 7 432,00	- 236 281,00
Related party receivables (O)	19 292,00	13 485,00		**NIBD**	**3 142 139,00**	**1 901 880,00**
Inventories (O)	135 161,00	107 114,00				
Voyages in progress (O)	110 061,00	110 638,00				
Prepaid expenses and accrued income (O)	15 753,00	14 255,00				
Other current assets (O)	7 258,00	5 285,00				
Related party payables (O)	- 47 719,00	- 31 248,00				
Trade and other payables (O)	- 98 232,00	- 81 533,00				
Current portion of obligations under leases (O) Assumption	- 1 104,00	- 1 024,00				
NOWC	**265 117,00**	**276 439,00**				
NOA (NONCA + NOWC)	**5 419 485,00**	**4 161 779,00**		**Total E + NIBD**	**5 419 485,00**	**4 161 779,00**

3. Find the FCFF, the FCFE, and the cash surplus for the year 2023.

CASH FLOW	2023
NOPAT	726 642,08
+Depreciation	230 942,00
-Change in NOWC	11 322,00
-Change in NONCA	- 1 499 970,00
FCFF	**- 531 063,92**
+Change in NIBD excluding cash	1 294 056,00
Net Financial Expense	- 90 086,00
+/-Tax-shield from NFE	19 818,92
FCFE	**692 725,00**
-S. dividends	- 638 928,00
Cash surplus	**53 797,00**

Some notes on what has been done....

4. Show that the calculated cash surplus for 2023 is correct.

We know that the cash at the end of the year must be equal to the cash at the beginning of the year plus the cash surplus. Therefore, we first calculate what the cash at the end of the year should be according to the cash surplus we calculated and the cash at the beginning of the year.

cash beginning period	254 525,00
+Cash surplus	53 797,00
Cash end of the period	308 322,00

Following, we compare our result with the actual end of year cash and cash equivalents which we find in the Frontline Annual Report 2023.

Net cash used in investing activities		**(1,235,456)**	(257,320)	(374,419)
Financing activities				
Net proceeds from issuance of shares	**20**	**—**	—	52,447
Proceeds from issuance of debt	**17**	**1,609,449**	651,248	403,868

Repayment of debt	**17**	**(536,587)**	(597,834)	(219,521)
Repayment of obligations under leases	**18**	**(862)**	(2,123)	(9,284)
Lease termination payments	**22**	**—**	(4,456)	—
Cash dividends paid	**8**	**(638,928)**	(33,393)	—
Net cash provided by financing activities		**433,072**	13,442	227,510
Net change in cash and cash equivalents		**53,797**	141,452	(61,648)
Cash and cash equivalents at beginning of year		**254,525**	113,073	174,721
Cash and cash equivalents at end of year		**308,322**	254,525	113,073
Supplemental disclosure of cash flow information:				
Income taxes paid	**7**	**122**	199	4,986

See accompanying Notes that are an integral part of these Consolidated Financial Statements.

As we can see from the Annual Report, our calculated end of year cash and cash equivalents balance is the same as the one listed in the Annual Report, confirming that the calculated cash surplus for 2023 is correct.

Question 2: A three-period consumption-savings model

The utility function associated with this exercise is:

$$U^{(c_1,c_2,c_3)} = \frac{c_1^{1-\gamma}}{1-\gamma} + \beta\frac{c_2^{1-\gamma}}{1-\gamma} + \beta^2\frac{c_3^{1-\gamma}}{1-\gamma}$$

The budget constraints are:

$$a_{t+1} = (1+r)a_t + y_t - c_t$$

Where $y_3 = 0$ and we assume inherited wealth so $a_0 = \underline{a}$.

1. Derive the intertemporal budget constraint.

To start off, we write out the functions for savings in each period.

$$a_1 = (1+r)a + y_1 - c_1$$

$$a_2 = (1+r)a_1 + y_2 - c_2$$

As we can see, we can input the function for a_1 into the function of a_2 which yields

$$a_2 = (1+r)((1+r)a + y_1 - c_1) + y_2 - c_2$$

Now since there is no income in period three, the consumption in period three is limited by the savings and prices. Defined as a function we have:

$$c_3 = (1+r)a_2$$

We continue to expand this function by substituting in our expanded function of a_2 to get:

$$c_3 = (1+r)^2((1+r)a + y_1 - c_1) + (1+r)y_2 - (1+r)c_2$$

By Moving all consumption terms to the LHS and the income terms(including inherited savings a) to the RHS, we are left with the equation:

$$(1+r)^2c_1 + (1+r)c_2 + c_3 = (1+r)^3a + (1+r)^2y_1 + (1+r)y_2$$

What remains is to divide both sides by $(1+r)^2$ to get the answer to this question. This gives us the intertemporal budget contraint:

$$c_1 + \frac{c_2}{1+r} + \frac{c_3}{(1+r)^2} = y_1 + \frac{y_2}{(1+r)} + (1+r)a$$

2. Derive the Euler equations.

By the use of the utility function defined above, we set up the Lagrangian for this exercise:

$$\mathcal{L}(c;\lambda) = u(c_1) + \beta u(c_2) + \beta^2 u(c_3) - \lambda\left(c_1 + \frac{c_2}{1+r} + \frac{c_3}{(1+r)^2} - a - y_1 - \frac{y_2}{(1+r)}\right)$$

Where the u functions are partitions of the utility function U, defined as:

$$u(c_1) = \frac{c_1^{1-\gamma}}{1-\gamma} \qquad u(c_2) = \frac{c_2^{1-\gamma}}{1-\gamma} \qquad u(c_3) = \frac{c_3^{1-\gamma}}{1-\gamma}$$

Continuing, we solve for the First-Order conditions:

$$\text{I:} \quad c_1^{-\gamma} - \lambda = 0$$

$$\text{II:} \quad \beta c_2^{-\gamma} - \frac{\lambda}{1+r} = 0$$

$$\text{III:} \quad \beta^2 c_3^{-\gamma} - \frac{\lambda}{(1+r)^2} = 0$$

The roman numerals are identifiers making it easier to distinguish which equations we refer to. Now that we have the FOCs, we start by solving for lambda in equation I:

$$\text{I:} \quad \lambda = c_1^{-\gamma}$$

Using this definition of λ in equation II, we get that:

$$\text{II:} \quad \beta c_2^{-\gamma} = \frac{\lambda}{1+r} \quad \rightarrow \quad c_1^{-\gamma} = \beta(1+r)c_2^{-\gamma}$$

Using the definition of λ to solve equation III we get:

$$\text{III:} \quad \beta^2 c_3^{-\gamma} - \frac{\lambda}{(1+r)^2} = 0 \quad \rightarrow \quad c_1^{-\gamma} = \beta^2(1+r)^2 c_3^{-\gamma}$$

Lastly, we can use the definition of $c_1^{1-\gamma}$ derived from equation II to solve equation III for $c_2^{1-\gamma}$ instead. This results in the equation:

$$c_2^{-\gamma} = \frac{\beta^2(1+r)^2 c_3^{-\gamma}}{\beta(1+r)} \quad \rightarrow \quad c_2^{-\gamma} = \beta(1+r)c_3^{-\gamma}$$

Hence, we conclude that the Euler equations for this exercise is:

$$c_i^{-\gamma} = \beta(1+r)c_{i+1}^{-\gamma}, \qquad \text{for } i = 1, 2$$

3. Compute optimal consumption and savings for the first period.

We start off by rewriting the Euler equations:

$$c_1^{-\gamma} = \beta(1+r)c_2^{-\gamma} \quad \rightarrow \quad c_2 = \beta^{\frac{1}{\gamma}}(1+r)^{\frac{1}{\gamma}}c_1$$

$$c_1^{-\gamma} = \beta^2(1+r)^2c_3^{-\gamma} \quad \rightarrow \quad c_3 = \beta^{\frac{2}{\gamma}}(1+r)^{\frac{2}{\gamma}}c_1$$

Now that we have defined c_2 and c_3 as functions of c_1, we can now use the intertemporal budget constraint and solve for c_1:

$$c_1\left(1+\beta^{\frac{1}{\gamma}}(1+r)^{\frac{1}{\gamma}-1}+\beta^{\frac{2}{\gamma}}(1+r)^{\frac{2}{\gamma}-2}\right) = y_1 + \frac{y_2}{(1+r)} + (1+r)a$$

From this equation, we can conclude that the optimal consumption for the first period is:

$$c_1 = \frac{y_1 + \frac{y_2}{(1+r)} + (1+r)a}{\left(1+\beta^{\frac{1}{\gamma}}(1+r)^{\frac{1}{\gamma}-1}+\beta^{\frac{2}{\gamma}}(1+r)^{2(\frac{1}{\gamma}-1)}\right)}$$

And optimal savings for the first period is:

$$a_2 = (1+r)^2a_0 + y_1 - c_1$$

I think??????

4. Discuss the impact of the discount factor, and the elasticity of intertemporal substitution (EIS = $1/\gamma$) on savings.

The higher EIS is the more the consumer will save. The higher β is the more the consumer will save.

Question 3: Portfolio Diversification

Linh will solve this

References