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Tom's Recommendation: Tesla Motors

Tom Gardner and Alex Scherer, CFA | November 16, 2012

CURRENT PRICE: [TSLA](#) \$ 1006.55 ↑ \$ 12.23 (1.2%) as of 11/16/2012 4:00 PM EST

Automobile Magazine awarded the **Tesla Motors** ([NASDAQ: TSLA](#)) Model S sedan its Car of the Year award last month, declaring: "It's the performance that won us over. The crazy speed builds silently and then pulls back the edges of your face. It had all of us endangering our licenses." An accurate description of the car, it applies equally well to the company that created it. Tesla's performance bringing the Model S to market is worthy of its own set of awards, including a spot on the *Stock Advisor* scorecard — and in your portfolio.

Not Your Father's Oldsmobile

Tesla is a young, California-based business currently selling its second all-electric vehicle. The Model S luxury four-door sedan seats seven and delivers sleek design, high performance, and an up-to-300-mile all-electric range for its premium \$60,000 (and up) price tag. More Silicon Valley than Detroit, Tesla is redefining the entire automotive experience, including design, manufacturing, sales, service, and fuel. The company owns its retail stores and service centers directly. Software updates over Wi-Fi allow Tesla to upgrade your Model S while it's in your garage. And the company is building a network for speedily supercharging your Model S (for free) on long-distance trips.

We can't overemphasize how important co-founder and CEO Elon Musk is to our confidence in Tesla. Musk is a proven winner who is invested financially (he owns 24% of Tesla's stock) and emotionally in his business. He scores high marks with us for working passionately, even obsessively, to delight customers first and Wall Street later. His mission is to help move the world toward more sustainable energy use as well as to make a profit. That passion and long-term focus can sometimes make for a bumpy ride — such as when his perfectionism led him to personally inspect batches of Signature Series sedans, delaying deliveries unexpectedly. But we like his awareness

TESLA MOTORS

Tesla makes and sells high-performance luxury electric vehicles.

Track It!

WHY BUY:

- Its dynamic co-founder and CEO is heavily invested alongside outside shareholders.
- A significant ramp-up in sales and jump to profitability is under way.
- We see long-term opportunity well beyond the high-end luxury vehicle niche.

KEY FACTS:

- **Headquarters:** Palo Alto, Calif.
- **Website:** [www.teslamotors.com](#)
- **Recent Price:** \$31.61
- **Risk Rating:** [12 — Coconut*](#)
- **Position in Industry:** Disruptor
- **Market Cap:** \$3,597
- **Cash/Debt:** \$86 / \$465
- **Revenue ('10/'11/TTM):** \$117 / \$204 / \$146
- **Earnings ('10/'11/TTM):** (\$154) / (\$254) / (\$387)
- **Insider Ownership:** 29%
- **Biggest Threat:** Major product recall

that a platinum reputation for quality from day one is the key to loyal customers and a powerful, differentiated brand.

Zero to 60

Musk's approach to production smacks of Steve Jobs, which has scared analysts and investors as new cars crept slowly off the line the past few months. But the payoff is real: Accolades including that Car of the Year honor from *Automobile Magazine* as well as one from *Motor Trend* are the most prominent, but countless blogs, tweets, and other media from Model S buyers and the mainstream and automotive press rave about the car. Tesla "has managed to blend the innovation of a [tech] start-up, the execution of a world-class automaker, and, yes, the chutzpah of its visionary leader" was one reviewer's verdict. We expect the ecstatic feedback — and sales — to multiply from here.

Deliveries are under way. The company shipped 250 vehicles last quarter and is now producing nearly that many each week. Tesla's rapid ramp-up puts it on a path to 20,000 cars sold next year, with orders in for more than 13,200 — zealous customers (including Alex and, most likely, my brother) are waiting upwards of a year for delivery, but that will shorten next year as production ramps up.

Management expects another 50% increase in sales in 2014 with the release of the Model X crossover SUV, meaning investors can look forward to a nearly sevenfold sales uptick in two years. The road map beyond these two critical launches is the real prize for long-term investors, though, because Tesla's ultimate goal is a third-generation mass-market-priced sedan that will begin to fill out Tesla's Fremont, Calif., plant capacity of 500,000 cars annually.

Pegging a fair value for Tesla is more a matter of conjecture than for most of our stocks. Here's one possible scenario: If Tesla maintains its trajectory, it will achieve positive free cash flow this quarter, meet demand of 20,000 or more Model S cars in 2013, and augment that with a Model X launch that can help the company to earnings of nearly \$3 per share by 2014. Today's \$31 stock price conveys the doubts cynical investors have about Tesla's audacious plan. Therein lies the opportunity to start buying in thirds, building the size of your stake (at likely higher prices but with less uncertainty) as Musk continues to pull off his innovative coup.

Risks and When We'd Sell

With the flagship Model S the only car on Tesla's lot (the original Roadster premium sportscar has finished its production run), the next four quarters are critical. Serious production delays or product recalls could lead customers to cancel their Model S reservations and drive Tesla to search for cash infusions, taking a heavy toll on shareholders.

Tesla's David-versus-Goliath mission presents other road hazards. Dealers are lining up against its company-owned store strategy, suing in states where they think Tesla is breaching franchising regulations. And the car maker's poster-child position as a green energy start-up receiving government funding has made it a political hot potato. Since Tesla is only now reaching positive cash flow, slip-ups or reputational damage can have a greater than normal impact on the stock price — so size your investment accordingly and drive slowly, Fool.

The Foolish Bottom Line

- **The Team Says:** Nice ride!

GET STARTED

- [ADD TSLA to My Scorecard](#)
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Data as of 11/13/12. Dollar amounts in millions except recent price

DUELING FOOLS: TESLA MOTORS

By the Ǝǝıı ! ǝıǝı ƆTeam

David: Tesla Motors ([NASDAQ: TSLA](#)) co-founder Elon Musk also co-founded PayPal — my third-ever *Stock Advisor* recommendation — so he's clearly a winner. But he does more than run Tesla, right?

Tom: Since PayPal, Musk has been juggling leadership roles at three disruptive companies — Tesla, SpaceX (which last month sent the first privately funded rocket to the international Space Station), and Solar City, a solar-power installer planning its IPO. It's a heavy load, but one he's pulled off with great success for years now. Dreaming up and successfully launching any one of these groundbreaking businesses is a heroic task; that Musk has done it four times solidifies his reputation as an innovative disruptor extraordinaire.

For the rest of the Dueling Fools feature, stay tuned for your next Stock Advisor email update Nov. 30. [Click here](#) to opt in.



This is a younger company and riskier opportunity than you'll usually find on my side of the *Stock Advisor* scorecard, investing in Tesla means shouldering uncertainty in return for potential high-speed performance. (It's even worth my brother's inevitable accusations that I stole it from his *Rule Breakers* scorecard.) That said, with production nearing full throttle and Tesla on the cusp of positive profits and free cash flow, it looks like the right time to hop in the passenger seat for a drive you'll not soon forget. 🚗

The Motley Fool owns shares of Apple and Tesla Motors. See the team's and David and Tom Gardner's holdings [here](#).

**Note: After publication, we changed Tesla's Risk Rating from 11 to 12. [Read why here](#).*

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