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## Tesla, Inc. NasdaqGS:TSLA

### FQ4 2015 Earnings Call Transcripts

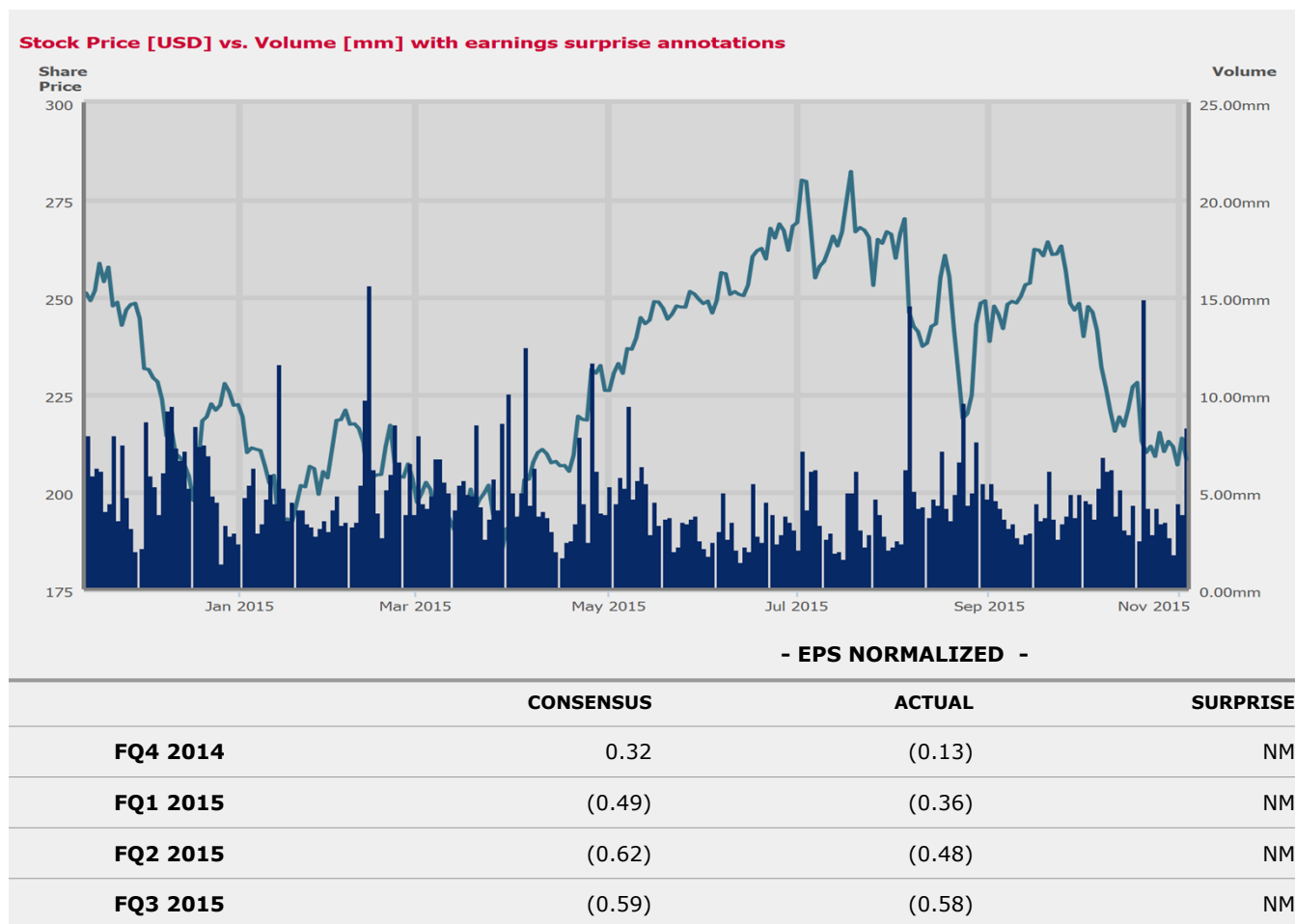
Wednesday, February 10, 2016 10:30 PM GMT

### S&P Capital IQ Estimates

	-FQ4 2015-			-FQ1 2016-	-FY 2015-		
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL	
<b>EPS Normalized</b>	0.11	(0.87)	NM	(0.09)	(1.26)	(2.30)	
<b>Revenue (mm)</b>	1802.49	1747.02	▼ (3.08 %)	1837.57	5353.20	5291.54	

Currency: USD

Consensus as of Feb-10-2016 12:42 PM GMT



# Call Participants

## EXECUTIVES

### Elon R. Musk

Co-Founder, Chairman, Chief Executive Officer and Product Architect

### Emmanuel Rosner

CLSA Limited, Research Division

### Jason S. Wheeler

Former Chief Financial Officer

### James Joseph Albertine

Stifel, Nicolaus & Company, Incorporated, Research Division

### Jeff Evanson

Vice President of Investor Relations

### John Joseph Murphy

BofA Merrill Lynch, Research Division

### Jeffrey B. Straubel

Chief Technology Officer

### Patrick Kenenhan Archambault

Goldman Sachs Group Inc., Research Division

### Jonathan McNeill

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### Rod Avraham Lache

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## ANALYSTS

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Morgan Stanley, Research Division

### Ryan J. Brinkman

JP Morgan Chase & Co, Research Division

### Andrea Susan James

Dougherty & Company LLC, Research Division

### Tyler Charles Frank

Robert W. Baird & Co. Incorporated, Research Division

### Brian Arthur Johnson

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### Colin Langan

UBS Investment Bank, Research Division

### Dana Hull

### Dee-Ann Durbin

### Colin William Rusch

Oppenheimer & Co. Inc., Research Division

### Mike Ramsey

### Phil Lebeau

### Daniel Galves

Crédit Suisse AG, Research Division

# Presentation

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## Operator

Good day, ladies and gentlemen, and thank you for your patience. You've joined Tesla Motors, Inc. Fourth Quarter 2015 Financial Results Q&A Conference Call. [Operator Instructions]

I would now like to turn the call over to your host, Mr. Jeffrey Evanson. Sir, you may begin.

## Jeff Evanson

*Vice President of Investor Relations*

Thank you, Latiff, and good afternoon, everyone. Welcome to Tesla's Fourth Quarter and Full Year 2015 Q&A Webcast. I'm joined today by Elon Musk, Tesla Chairman and CEO; J.B. Straubel, our CTO; CFO, Jason Wheeler; and Jon McNeill, President of Global Sales, Service and Delivery.

Our Q4 results are announced in the update letter at the same link as this webcast. As usual, this letter includes GAAP and non-GAAP financial information and reconciliations between the 2.

During our call, we will discuss our business outlook and make forward-looking statements. These are based on our predictions and expectations as of today. Actual events or results could differ materially due to a number of risks and uncertainties, including those mentioned in our most recent Form 10-Q filed with the SEC.

We're going to start today's call with some comments by Elon and then Jason, and then we'll go into the Q&A session. [Operator Instructions]

And with that, I'll turn it over to you, Elon.

## Elon R. Musk

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Thank you. So I think the newsletter probably speaks for itself, but I'll add some commentary on some of the lead points.

So obviously, we had a huge increase in Model S deliveries year-on-year in Q4 last year, going up 76%. We had a huge change in our core operational cash flow, which you can really see in the chart, and it's really quite dramatic. That's why I think it's interesting to look at in chart form. It goes from negative to significantly positive in Q4 last year. And then we made modest improvements in Model S gross margin, getting to about 25% excluding onetime items, and we feel pretty good about where we're tracking to probably get close to 30% by the -- by about Q4 this year.

And then something I'm personally quite excited about is that we expect to be positive cash flow starting next month and then continue on into Q2 and beyond. And that's -- there's only one caveat there that's including the asset-backed line, and the asset-backed line is -- that's just funding for cars that are en route to customers. So particularly as sales to international markets increases, there's more finished goods inventory on its way to customers. And so inclusive of the asset-backed line, which really I think is -- was accurately regarded as a slight decrease in the gross margin of the car by about roughly 0.1% or thereabouts. Apart from that, we're positive cash flow.

And then we're expecting to be profitable for 2016 on a non-GAAP basis. And I personally think that, that is actually the correct way to think -- to look at it because of the way that GAAP treats lease accounting. And -- but then nonetheless, despite the lease accounting stuff, we anticipate being profitable by GAAP standards in Q4 of this year.

And then we're really looking forward to the -- building the Model 3 on -- at the end of next month. I think this is going to be really well received and then getting into production and delivery at the end of next year.

Touching on a few things that are in the bulk of the newsletter. I think the chart on vehicle demand is really interesting. And to the degree that this represents a microcosm of how Tesla vehicles will be received in other vehicle segments, it augurs extremely well for the future. So the Model S was the best-selling premium sedan in the United States last year of any kind. And our sales actually increased by 51%, whereas everybody else's sales declined and the overall market segment declined by about 1%. So I think this is -- it's really rare to see situations like this. And I think this is despite us being really quite underpenetrated in the Northeast. I think there's a lot of room for growth in the Northeast particularly in the U.S. and in international markets in general.

So -- but essentially, getting to a 25% market share of all premium sedans in the U.S. is, I think, a great achievement of the Tesla team. And I think it's also great for the world because it means that's 25,000 fewer gas guzzlers that are on the road. I'd like to thank all the customers that went out and bought that car because I think they're making a difference for the environment. And of course, they're helping pay for the future development of the Model 3, which is the more affordable mass-market car. That's where we put all of the revenue we receive from the Model S and X. So it's really important to bear that in mind, that S and X are what pay for the Model 3.

And that's -- and one additional note is that Tesla does not advertise. We don't pay for any endorsements. We do not discount our cars for anyone, including me. I pay full retail price. Whereas those actions are -- all of our competitors take those actions. So that's, I think, quite interesting. We also have far fewer sales outlets than our competitors. Essentially, there's a lot of degrees of freedom that we are not exercising that we could, in theory, exercise.

I think -- oh, and if you look at the text, it's worth noting that this is not just uniquely true in the United States. But in Switzerland, we outsold -- the Model S outsold the Mercedes S-Class, the BMW 7 Series, Porsche Panamera and the Audi 8 combined and also outsold the Mercedes E-Class. And in Germany, we outsold the Porsche Panamera. So I think these are pretty good situations. I mean, this is even in places that have no incentives. Obviously, incentives are certainly helpful. They're a catalyst for sales. They're -- so Tesla always appreciates the incentives, and I think they make a difference in accelerating the advent of electric vehicles. But sometimes incentives are characterized as it's sort of all about incentives or not at all about incentives. And it's really important to appreciate that incentives are an accelerant. But that's the reality of them.

Jason, do you want to add anything?

### **Jason S. Wheeler**

*Former Chief Financial Officer*

Sure, absolutely. Thanks, Elon. First of all, I look forward to working with everybody. I'm super excited to be here, as excited as I was on the first day I walked through the door.

Just 3 quick things I want to touch on real quick. Number one, gross margin, lots of moving parts this quarter. And let me walk you guys through it a little bit. We had over \$67 million in Model X ramp-up costs and nonrecurring items in the quarter, as Elon mentioned. Correcting for these items, automotive gross margin, excluding ZEV credits, would have been 25%.

First thing, the major component here is labor and overhead and depreciation related to the Model X launch. The way for you all to think about this is towards end of Q3 and into Q4, we had to bring the workforce into the factory to build these wonderful vehicles. Also, as soon as start-up production starts, the clock starts hitting on depreciation as well. So that's what's going on there. We also had some asset impairments, one with our old paint shop. And we've now got a state-of-the-art paint shop in place, which is going to give us the capacity that we need all the way through Model 3...

### **Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes, that's 10,000 cars a week too.

### **Jason S. Wheeler**

*Former Chief Financial Officer*

Yes, 10,000 cars a week. So this is a good story, and these are assets that we had purchased all -- go all the way back to the NUMMI days. So we got every bit of life out of those assets as we possibly could.

The other big piece here is we had an E&O write-off, excess and obsolescence. This is a result of better production control and inventory management systems that we put in place. The place is moving really fast, and we took some time, Elon talked about this in Q2 on the earnings call during the shutdown, putting better systems in place to track this. We're moving to a place where we're tracking E&O on a real-time basis and bringing those facts to the table when we're making decisions. So we shouldn't be in this position again.

Next thing I wanted to talk about just real quickly was cash flow. And Elon covered this, and I think the chart on the face of the shareholder letter really gets there. But we were within striking distance of positive operating cash flows there. And when you add back the leasing proceeds that we get of \$209 million, it's a great step change in the right direction to getting us to net cash flow positive.

Also CapEx, we guided to \$500 million last quarter on the call, and we closed out at \$411 million for the quarter. That all resulted in ending cash balance being at \$1.2 billion, which I think showcases our strong improvement in cash management and discipline with the company.

Finally and really quickly, talk about capital structure. We closed the warehouse line that we previously had before and opened the ABL, as Elon mentioned. Think of this as a shift to lower-cost financing. We've got a better deal on this line. So I think it's a better way to think about that. Intended uses, one, we'll continue to monetize our direct leases as we did with the warehouse line. But it also creates an option for us to finance our ramp in FGI as the Model X hits full production scale.

I'll just close by saying my mandate from Elon is clear: Cash is king. And there's some real steps that we're taking as a company to get ourselves to net cash flow positive for the year...

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

And profitability.

**Jason S. Wheeler**

*Former Chief Financial Officer*

And profitability. One more, it's just capital efficiency in CapEx. CapEx in 2016, as we said in the past, will be less than it was in 2015. We started to see some of this in Q4. It will continue. We're also getting to a point where we have operating leverage in the business. We'll continue to aggressively manage our growth in expenses. And then finally, and I walk around and I'm on this every day, is a relentless focus on automotive unit cost reductions.

So that's my mandate. Again, I'm happy to be here. And Elon, if you've got nothing else, we go to Q&A.

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes. Actually, I guess one other point that's sort of interesting to note is that Tesla is approximately doubling its cumulative sales every year. So this is -- I'm not sure if this has happened in the car industry for maybe a century. But like we started the beginning of last year with 50,000 cars en route, then we ended with 100,000. This year, we're maybe 60% to 80%. So if we're at the high end of that range, we again sort of potentially double the size of the fleet. And I just think that's pretty exciting and unusual.

So thank you. We'll go to Q&A.

**Jeff Evanson**

*Vice President of Investor Relations*

All right. Latiff, let's take the first question, please.

## Question and Answer

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### Operator

Our first question comes from the line of Brian Johnson of Barclays.

#### Brian Arthur Johnson

*Barclays PLC, Research Division*

Welcome, Jason. Just want to ask a couple of questions revolving around the cash flow. I'm sure that people will go into some of the X ramp and delivery numbers. First, you produced about 14,000. You delivered 17,000 vehicles. That would imply 3,443 reduction in new finished goods, at least the S inventory, which could generate \$250 million. Yet your inventory is roughly flat quarter-over-quarter. What's -- what, before we get the K and the Q, are the puts and takes there?

#### Jason S. Wheeler

*Former Chief Financial Officer*

I think you touched on it. We managed to do a really nice job of selling inventory cars at the end of the year.

#### Brian Arthur Johnson

*Barclays PLC, Research Division*

But on the balance sheet, the inventory number -- and cash and inventory stayed about the same.

#### Jason S. Wheeler

*Former Chief Financial Officer*

So there's a couple of things going on in there. So one is the finished goods but also -- doing a nice job on the finished goods inventory but also just the ramp-up of the parts that we need to get full production with Model X.

#### Brian Arthur Johnson

*Barclays PLC, Research Division*

Okay. So it's sort of the work in process on the X. Second, can you kind of just refresh -- can you kind of update us given the change from the revolver to the ABL? What is currently drawn on the ABL? What's the available borrowing base? How much of that is, as you think about next year, going to be used to support increased on-balance sheet leasing versus increases in finished goods inventory? And what's your remaining, if the banks were to come in kind of borrowing base that would be left unpledged?

#### Jason S. Wheeler

*Former Chief Financial Officer*

Yes, sure. So on where we closed Q4 at, I think we were \$135 million fully drawn on it. And then in terms of the borrowing base, there's a lot of detailed numbers behind that. I think the most important thing to point out here is the increase to \$1 billion that we did with our banking partners. And then there are some restrictions there, and we don't want to max that out. So we're going to monitor it carefully and just make sure we do the things to do. We don't want to live on this drug.

#### Elon R. Musk

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes, and I mean, we have a collection of lenders. So it's like if hypothetically one lender were to get -- were to decide not to split the ABL, then would distribute it. So it's not a single currency. And we found that the appetite with lenders is very strong for the ABL because it's a finished product that's going to a known customer. So it's not -- there's no -- sort of there's no channel to stuff because there isn't a channel. So it's just up in transit to customers, primarily overseas.

**Jason S. Wheeler**

*Former Chief Financial Officer*

Yes. It grows with the inventory balance...

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes.

**Jason S. Wheeler**

*Former Chief Financial Officer*

Against cars that have orders placed against them.

**Brian Arthur Johnson**

*Barclays PLC, Research Division*

But it sounds like you could draw -- even if inventory, finished goods inventory, was flat, you could -- could you still draw on it? Or does it have to track to a direct increase in finished goods inventory?

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes. Yes, it does track to finished goods inventory. Basically, it's a finished goods loan.

**Operator**

Our next question comes from the line of Colin Rusch of Oppenheimer.

**Colin William Rusch**

*Oppenheimer & Co. Inc., Research Division*

So you're coming to, in the next couple quarters, to the end of some of the initial leases on the Model Ss. Can you talk a little bit about your preparations for that and your expectations as we move throughout this year on what will happen with those cars and how many of them are actually going to get returned?

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Sure. Jon, do you want to talk about that?

**Jonathan McNeill**

*President of Global Sales and Service*

Sure. So we actually started on that early and launched the campaign in the second half of 2015 to reach out to folks who had cars coming off lease. And one of the attractive things to those folks who were coming off a lease is have a car that's equipped with Autopilot. And Autopilot is certainly one of the core stories of what's going on here at Tesla. It's really exciting. And so we're finding that folks are willing to upgrade their Tesla as part of this campaign. And so we've got this formal program where we're really providing a smooth transition period for these cars. In addition to that, we're finding there's a very healthy aftermarket for these cars. And the trade-in values, or the trading values in the market are significantly above our residual reserves on the cars, which is giving us some flexibility in terms of our financing partners offering very attractive monthly payments and loan terms because the cars are holding -- the Teslas are holding value at a much higher rate than we thought. So I think the short answer is we're out ahead of it, and we're getting really good reception and conversion from customers. We're excited about even next generation of Tesla, which is an Autopilot-equipped car.

**Colin William Rusch**

*Oppenheimer & Co. Inc., Research Division*



Okay, great. And then just the follow-up. There's some pretty significant legislation update in the Toxic Substances Control Act that passed through the Congress in December. As you guys look at a lot of the details in terms of ramp in the Gigafactory, can you talk a little bit about where you're seeing as the impact so far with the updated substances and how they might be treated as we go forward here?

**Jeffrey B. Straubel**  
*Chief Technology Officer*

This is J.B. I can jump in there. We haven't seen any immediate impacts from those results or changes. The materials we're using at the Gigafactory are not particularly toxic substances. They're...

**Elon R. Musk**  
*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes. The Gigafactory have 0 toxic output.

**Jeffrey B. Straubel**  
*Chief Technology Officer*

Yes, it's -- so in terms of large industrial factories, it's an incredibly clean one. In terms -- there's really no emission -- no air emissions and the raw materials are largely base metals and things like that.

**Operator**

Our next question comes from Adam Jonas of Morgan Stanley.

**Adam Michael Jonas**  
*Morgan Stanley, Research Division*

Two quick ones. First, can you confirm reports that Jim Keller, kind of a legend in the microprocessor world, has joined the company to head hardware engineering at Tesla Autopilot? And if that's correct, does that signal that Tesla might be moving to design some of their own silicone?

**Elon R. Musk**  
*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Well, I mean, I think it's public knowledge that Jim Keller has joined. I mean we have a lot of talented people that join Tesla all the time. I mean Jim is an indicator of that, and just some will get a bit more press than others. But it's -- I think the talent level that's joining Tesla is really incredible. It's -- with regards to the latter part of your question, we just -- no comment, yes.

**Adam Michael Jonas**  
*Morgan Stanley, Research Division*

Okay. And then just a follow-up. On test drives, outside of company-sponsored events, kind of surprised we haven't seen any full comprehensive independent test drives in the major magazines. Is there anything kind of preventing -- and I think people on the call can understand if there would be of the earlier produced units that maybe you wouldn't want released quite yet. But is there anything preventing the magazines from gaining access to the early vehicles, the Model Xs, conducting a full road test of the vehicle? And if there is, when can we expect kind of some of the first reviews do you think?

**Elon R. Musk**  
*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Well, we -- I mean, I guess we've not provided cars to the media because -- largely because we -- to the degree that we could suppress demand for the X, we did. So we took basically every action we could to suppress demand for the X because production wasn't -- we needed to get production up. There was no point in amplifying demand if the production cannot meet that demand. So we did our best to really suppress demand or certainly not encourage demand. That will obviously change in the balance of this year as we get cars to stores because there have been no Model Xs at the stores, no Model Xs available for test drives. And -- but I mean, in the coming months, I think probably next month, you'll start seeing



such things, some reviews in magazines and whatnot. The feedback from customers we've gotten has been very positive.

**Operator**

Our next question comes from Emmanuel Rosner of CLSA.

**Emmanuel Rosner**

*CLSA Limited, Research Division*

I wanted to ask you first, can you give us a little more color on what exactly happened with the Q4 launch? I mean, in the letter, you sort of like implied that it sort of like took maybe a little bit longer than expected. So what sort of, like, issues have you encountered? And what have you learned that sort of like gives you confidence that in your next launch, maybe the Model 3, you can actually ramp that up significantly quicker?

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes, I think that's a great question. I think the statement we made with the Model X, which I really think we've taken to heart at Tesla, is that we put too many new features and technologies, too many great things all at once into a product. In retrospect, it would have been a better decision to do fewer things with the first version of Model X and then roll in the capabilities and features and new technologies over time in subsequent years. So I do think that there were some hubris there with the X. So the net result, however, is that I think the Model X is an amazing car. I honestly think it's probably the best. I mean, I think it's the best car ever. I'm not sure anyone's going to make a car like this again. I'm not sure Tesla would make a car like this again. So yes, I mean, I'd be surprised if -- if somebody buys the X, and particularly as the software gets refined, if it's not the product they love more than any product they've ever bought, I would be surprised.

**Jeffrey B. Straubel**

*Chief Technology Officer*

Yes. I mean, maybe it's worth also just commenting that even some of the most innovative features on X that caused some challenges in Q4 have really been largely overcome today.

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes, that's true.

**Jeffrey B. Straubel**

*Chief Technology Officer*

The operation of the falcon door, the sourcing and supply of the large glass windscreen, I mean, these things are working very well and are not a bottleneck at this point.

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Exactly. But some of the things that cause those issues are somewhat counterintuitive. They're not the obvious things. I mean, for at least a few weeks, I mean, maybe 3 or 4 weeks actually, the constraint was the chrome finish on the bright work around the window, the front window, okay. And you think like how on earth could that be the constraint, but it was...

**Jeffrey B. Straubel**

*Chief Technology Officer*

Or seals.

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Or seals, yes. The seals are -- yes, the seals have been really huge bane [ph]. Essentially, the seals had to be redesigned. And then the seals that we did have had to be worked by hand in order to sort of fit correctly. Yes, seals are a bane. We had a lot of issues with obviously secondary seat. We've now in-sourced that capability. Yes, we really don't see any fundamental issues.

**Emmanuel Rosner**

*CLSA Limited, Research Division*

Okay. So it sounds like it's basically mostly behind you. So as we move forward into the year, so you're talking about this Model X production rate of 1,000 vehicles a week in Q2, is that an exit rate? Or is that an average for Q2? And can you just more generally give us how you see the overall mix for the year of S versus X play out in terms of deliveries?

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

I mean some of the stuff is there. You have as good a crystal ball as we do. But the -- let's see, the -- 1,000 a week would probably be a peak production week in Q2. So like average, I don't know what the average is going to be exactly, but maybe 700 or 800, something like that. So that's good for that. I think we feel confident of hitting 1,000 a week certainly towards the mid to end of Q2. And then for the exact mix, I mean, I think we need to see how customers react when both cars are in the showrooms, and then we'll adjust accordingly. But we expect the combined delivery number average over the year of 1,600 to 1,800 per week.

**Operator**

Our next question comes from the line of Colin Langan of UBS.

**Colin Langan**

*UBS Investment Bank, Research Division*

Can you just kind of walk through what are the key short-term drivers? Because you're still -- of cash, I'm sorry -- kind of still burning \$200 million this quarter. Is it just really all volume to get back to get cash flow positive by Q2? You also touched on CapEx. Do you have it -- you're saying it's going to be flat to down, but there's -- it seems like there's an awful lot of work going on in the company. I mean, how do you keep CapEx down as you have all these growth plans?

**Jason S. Wheeler**

*Former Chief Financial Officer*

Yes, sure. So the key drivers on cash flow positive. So as I said in my earlier comments, it's a great step in that operations, the business is selling cars and energy products is now producing enough cash for us to start to pay for our investments. And if you look at the Q4 dynamics, that cash flow from core operations, as we're calling it, produced 40% to 45% of the cash that we needed for the CapEx in the quarter. So that is certainly a big piece of it, too. Another piece of it, as I mentioned, is just going to be operating leverage. We need to be very diligent about how we grow operating costs, certainly. And then the other big element to it is certainly continuing to drive cost downs on the vehicles, and there's lots of ways to do that. We're getting better at our manufacturing processes. We're reducing scrap. We're reducing excess and obsolescence. As we talk about in the letter, the car continues to be more and more reliable. So that reduces our warranty, and that actually has a cash impact when the cars show up less at the service centers.

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes. In fact, can I -- I'd just like to reemphasize that. We are seeing dramatic improvements in reliability and reductions in servicing needs. This is important. Sorry, go on.

**Jason S. Wheeler**

*Former Chief Financial Officer*

Yes, yes. No, absolutely. And then the other piece, you talked about CapEx and how can it be down. Well, we made a bulk of the investments that we need for Model X in 2015. So in '16, we're going to continue to invest, but we'll really, towards the back half of the year, start to see some initial investment in Model 3. We'll continue to invest in the Gigafactory to get to where we want to be with production there. And then we'll continue to expand the service center, the retail locations and the Supercharger network as well. But there's a lot of the big pieces that we needed to spend in CapEx to get to where we are today were spent in the past, yes.

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes. And I think it's just important to bear in mind that the overall market for SUVs and sedans is roughly the same. So there are -- globally, it's split almost 50-50. And so the X is kind of like half of our volume. And so if you set a company up to produce X and -- let me use -- not use the variable X. If you set a company up to produce a certain amount of revenue and then it produces maybe just over half that amount of revenue but has the cost base associated with it, but then obviously, the -- things will not be pretty from a cash flow and profitability standpoint. Necessarily, this is going to be true. But then as the X production rises, then that changes, then we achieve the target revenue with the reasonable cost bases, and the whole picture changes dramatically for profitability and cash flow.

**Jason S. Wheeler**

*Former Chief Financial Officer*

Absolutely. And the only other last thing I would add, too, is we've had a significant run-up investment over the last couple of years. Now it's time to absorb that and look for just greater capital efficiency.

**Colin Langan**

*UBS Investment Bank, Research Division*

Got it. And just one final question. Sorry, just one final question. Can you just remind us if we're -- are you still on track for storage of 400 million to 500 million this year and 2 to 5 next year? Or is that on track?

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

I mean, J.B., do you want comment on that? I mean, it's -- I mean, one thing I can say with respect to energy, like we do see this being a very enormous market. But we're -- it's an exponential growth market. So exactly where the calendar falls on the S-curve exponential makes quite a big difference on revenue. So it will be heavily weighted to the fourth quarter. J.B., do you want to add anything?

**Jeffrey B. Straubel**

*Chief Technology Officer*

Yes, that's exactly right. I mean, it's not a linear extrapolation throughout this year at all. So I think we're being fairly cautious in trying to make sure that we don't overpromise here and understand what's going to happen in Q4. It's a little bit tricky to know how that will grow. Production is on track. We feel really good about that. Production started off as planned in the Gigafactory in Q4. Deliveries are on track, and we're starting shipments of Powerwalls and Powerpacks worldwide. And we're growing out the sales operations, and the sales teams are on their work. So from an execution point of view, I think we feel really good with where we're at. It's just it's early days to predict how exactly that exponential growth is going to really integrate.

**Operator**

Our next question comes from the line of Patrick Archambault of Goldman Sachs.

**Patrick Kenehan Archambault**

*Goldman Sachs Group Inc., Research Division*

I wanted to build just on Emmanuel's question. Can you just tell us, what is the current run rate of X production, where we stand today towards the middle of February? And can we talk a little bit about how you get to that ramp? I mean, it sounds like 1,000 is the target that would obviously mathematically get you to think about half your production. So that's pretty much full ramp, but it seems like that's a pretty big distance from where you are now. And maybe we can walk through the pieces that gets you there in terms of training employees, getting the supply base in order, getting some of the quality issues resolved. That would be my first question.

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

I mean, I don't think we want to comment with that level of granularity but -- because unless people actually understand how production works, they will reach incorrect conclusions. I mean, we want to stick to what our projections are and leave it at that.

**Patrick Kenehan Archambault**

*Goldman Sachs Group Inc., Research Division*

Okay. I guess just in terms of another ramp-oriented question, if I may. It does seem that given the forecast that you have for, I think, 16,000 deliveries this year, getting to...

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

This quarter.

**Patrick Kenehan Archambault**

*Goldman Sachs Group Inc., Research Division*

Assuming 80 -- for this quarter, excuse me, getting to 80,000 to 90,000 would imply a run rate that's about 40% higher than where you are in Q1. But you also made a comment that inventories may -- that a lot of that is going to be international and there may be some in-process inventory being built out to service that. So maybe we can talk a little bit about that ramp.

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes, the international stuff is mostly Q2. So that's really when the international ramp starts. There's still inventory in process for, of course, North America because it takes longer to get a car to the East Coast, particularly for like a blizzard or something. But -- so that's, to me, a factor in finished goods. But finished goods necessarily ramps as we fill the pipeline for overseas sales, which is next quarter.

**Operator**

Our next question comes from Dan Galves of Credit Suisse.

**Daniel Galves**

*Crédit Suisse AG, Research Division*

First one has to do with operating expenses. Hopefully, I'm not getting the numbers wrong, but it seems like 20% growth in 2016 versus 2015 implies like relatively flat versus the Q4 run rate. Is that achievable to essentially keep the operating expenses pretty consistent throughout 2016?

**Jason S. Wheeler**

*Former Chief Financial Officer*

Yes, certainly. This is Jason. Yes, we definitely believe that we can do that. There was a bit of a dog's breakfast in Q4. We had some things in there. I'll just give you a couple of examples. So we had some aged receivables from some service revenues in Europe that we ended up having to write off. That was one thing. We had some R&D tooling that had come to the end of its useful life that we had to write off as

well. So there's some noise in the Q4 number, for sure, but I'm very confident in the projection and the forecast that we've given for 2016 relative to 2015.

**Daniel Galves**

*Crédit Suisse AG, Research Division*

Okay, great. Yes, yes, no problem. And one other, if I could. There's been a lot of negative chatter about Gigafactory related to signing up of other partners, precursor partners, supply agreements for access to raw materials and just kind of the general size of the plant. I was wondering if you could give us an update on kind of where you stand and if you see any challenges to get up to the 35 gigawatt hours of cell production by 2020, 50 of packs.

**Jeffrey B. Straubel**

*Chief Technology Officer*

Sure. I mean, generally, relative to the initial forecast and time lines, we feel pretty comfortable on where we're at. I think there has been a lot of drama and a lot of negativity in the reporting on this, and some around the headcount recently that I think a lot of people picked up on. And maybe just to talk about that one in particular, that recent sort of hiring headcount discussion cued off of numbers that we reported that were effective essentially in the middle of 2015. And then those were essentially compared against where we had predicted to be at the end of 2015. So they weren't really even really apples to apples. In our very -- most recent reports that we made with the Governor's Office of Economic Development, we had reported, I think, around 272 net hires for the year at the end of 2015 against what -- we had a target of 300. So I mean, the general plan is, I guess, getting actually quite closely to what we had laid out back in 2014. I think because it's a fast growth, we have to be really careful at what snapshot in time you actually look at and what you compare that against. But we still have the same confidence. We're still on track to produce 15 gigawatt hours of cells and -- I'm sorry, 35 gigawatt hours of cells and 50 gigawatt hours of packs, 15 of that going to Tesla Energy, the rest going to Model 3 and vehicles. That still is on track, and we're on track to start cell production at the -- toward the end of this year.

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Basically, I think as to the best of our knowledge, you should not worry about the Gigafactory as a constraint for Model 3. That is -- does not appear to be anywhere near the critical path for Model 3. So -- and if I can just sort of maybe say a few words about the Gigafactory and like Nevada and the incentives and all that. One of the most bothersome things that I see in the media is sort of overrepresentation of the Nevada incentives. The thing to bear in mind for the \$1.3 billion in incentives for Nevada is that in order for us to achieve that, we have to develop about \$100 billion in revenue from the Gigafactory. And those incentives occur over 20 years, representing approximately a 1% discount on the cost of the Gigafactory. The reason it's a big number, and I should say it does proportion -- it is a big number in the absolute terms, but it is disproportionately small relative to incentives, let's say, Boeing would receive for keeping an aircraft factory in Washington. The reason it's this big is because the Gigafactory will be the largest footprint building in the world when it is done. Our Tesla Fremont factory is currently #2. And if you're curious, #1 is a flower auction house in the Netherlands. And you can look this up on Wikipedia. So it sort of makes sense that if something is kind of like the biggest thing on earth, it's probably going to have incentives that are maybe big in the absolute but small in relative terms. And the fundamental driver of the decision that -- not the exclusive driver but the primary driver of the decision was pace of execution for the Gigafactory. That was the primary reason for Nevada over other options. And that -- I believe that this decision is bearing fruit because we are seeing it move at a very good pace.

**Daniel Galves**

*Crédit Suisse AG, Research Division*

Welcome, Jason. Sorry.

**Jason S. Wheeler**

*Former Chief Financial Officer*

All of those incentives are also performance-based.

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes, exactly.

**Jason S. Wheeler**

*Former Chief Financial Officer*

We don't receive them unless we execute along the path toward the milestones.

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Right, and even some of those we do receive have clawback provision.

**Jason S. Wheeler**

*Former Chief Financial Officer*

Exactly.

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

I mean, essentially, like I wrote a blog about this, there is no way for Nevada to lose. The way that Nevada set up the incentive structure is it is a no-lose proposition for them. So they did an awesome job on behalf of the state. I mean you can read the blog that I wrote called The House Always Wins, which is true, and so -- anyway, it's really annoying to see this stuff misrepresented in the press.

**Operator**

Our next question comes from the line of John Murphy of Bank of America Merrill Lynch.

**John Joseph Murphy**

*BofA Merrill Lynch, Research Division*

Just a first question. I mean, Elon, you made a very interesting comment about the Model X being the best car ever produced. And it sounds like you think it might be better than the Model S. I mean, as you get...

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Maybe I'm biased, obviously.

**John Joseph Murphy**

*BofA Merrill Lynch, Research Division*

Well, yes, I mean, it's your newest car, so it makes sense -- your newest vehicle, I should say, so it makes sense. But I mean, as you look at getting that production ramped up and availability out there to consumers, what would the selling point be on the Model S then? I mean, could you get this mix significantly above 50% crossovers or Model X because the price premium is really not that great? Why wouldn't you sell a whole lot more Model X than Model S? And could you?

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes, I think this is a question of owner preference. I mean, I personally still prefer to drive the Model S over the X because I'm kind of a -- I like the lower position of a sedan. And the S, in terms of performance, is about 10% better in an acceleration or handling or whatnot than the X. So it really depends on optimization. If you like sort of a high seating position, like an amazing amount of room and functionality and just sort of the feeling of high visibility like -- I mean, because the -- one of the



best features, maybe the best feature, of the X is the cockpit-style front windshield, which gives you this amazing panoramic view as you're driving. And so like if -- which, like, a lot of people like that in an SUV, and so that's the reason that they buy that. So I think it really depends on personal preference. And we'll see what the results are once we actually put the vehicle in the stores and people take test drives.

**John Joseph Murphy**

*BofA Merrill Lynch, Research Division*

And when you think about all the content that you're putting in the X and the upgradability of the S and the X over time, I mean, how do you think about planned obsolescence, which is sort of a real necessary part of almost any business to generate incremental sales from your existing customer base?

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

I guess I -- I mean, our view of planned -- we don't plan to obsolete things. We just relentlessly make things better. So for example, for the S, there's an average of 20 improvements per week. Most of these are little tiny nuance things that most people wouldn't notice, but it is a continuous improvement process. That's why I say when people say, well, when should they buy Model S, like what model year, it's like we don't really have model years. We keep improving the car. If you want to wait until the car stops improving, you'll be waiting forever.

**John Joseph Murphy**

*BofA Merrill Lynch, Research Division*

Okay. And then just one follow-up just on the cash flow for 2016. Obviously, a lot of progress has been made more recently. As we think about the positive net cash flow and the increase in the cash balance on a year-over-year basis, will that include -- I'm just trying to be clear -- the potential draw on the ABL over time as that's needed to run the business? Or does that net cash increase not include whatever draw that happens on the ABL in 2016?

**Jason S. Wheeler**

*Former Chief Financial Officer*

That includes the draw on the ABL to finance finished goods.

**Operator**

Our next question comes from Jamie Albertine of Stifel.

**James Joseph Albertine**

*Stifel, Nicolaus & Company, Incorporated, Research Division*

On the Model 3, if I may, just I think a lot of folks are trying to do work as it relates on the margin trajectory over time. And it's clearly going to be volume dependent and sort of timing around the launch. But I was wondering if you could help us understand. Just given that it's 1/3 of the transaction price of roughly your initial Model X deliveries, what are some of the efficiencies you're hoping that you can sort of draw upon maybe beyond just sort of the battery reduction -- battery cost reductions? What are you leveraging in the Model 3 from investments you've already made and sort of the knowledge you have around sort of initial launch costs and the higher-price vehicles at this point?

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes, I think the way to think of the cost difference is really that the Model 3, being a sedan, is about 20% lighter than -- and actually quite a bit less complex to manufacture than the Model S. The Model S was really the first car we ever made ourselves. So it was -- we were designing to make it work as opposed to designing it from ease of manufacturing, whereas the 3 is really designed for ease of manufacturing. And then we expect, through economies of scale and just general design improvements, to get another 30% improvement. So that's where the 50% improvement comes relative to the S. So sort of 35k versus



70k of 3 versus S is the way to think about the difference. And our default plan, as we've done in the past, is that the initial sales are relatively highly optioned versions of the car because, obviously, we've got to pay back the investment of all the tooling and everything. So that sort of makes sense to have the higher-optioned versions first. So that's what we did with the S and obviously, again with the X. While it was sort of unfortunate that -- of the way the X pricing got reported that they reported the sort of fully optioned signature series as though it was the base price volume number in some publications. So this was just a misunderstanding of how things work. I mean, it's -- and I think it's also normal procedures in many other industries like for -- if Intel comes out with a new CPU or faster CPU or NVIDIA comes out with a new graphics card, the -- in the beginning, it's a lot more expensive. And then over time, the price drops.

**James Joseph Albertine**

*Stifel, Nicolaus & Company, Incorporated, Research Division*

Just a clarification, Elon, on the economies of scale. It's sort of -- should I think about that and sort of the -- running through the paint shop as an example, given you said 10,000 unit per week sort of goal there? And then separately, what could we expect -- or when should we expect to start hearing about the Model 3 production line? Where do you, within the facility, plan to build it, at what point? Is it sort of going to be the same lead time as we saw with the Model X?

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes, but I mean, there will be a production ramp for the 3. It's always been tricky in the past to predict those production ramps, but yes, yes. You guys want to add?

**Jeffrey B. Straubel**

*Chief Technology Officer*

I think in the development plan that we have now, we have substantially more time and placeholders put into the schedule to really refine the product ahead of the production ramp. I mean, to a question that came earlier, I think that's something we've really taken to heart in the launch of the X as we look to higher volumes and what we hope will be a steeper ramp with Model 3. I think we've learned some important lessons on how to do that well, and having a really robust pilot build in the plant and enforcing rigorous numbers there.

**Operator**

Our next question comes from Andrea James of Dougherty & Company.

**Andrea Susan James**

*Dougherty & Company LLC, Research Division*

Welcome, Jason. Just a practical one about the factory. You have different choke points at different points in time. It's been general assembly. It's been the cells. Last count, it was body lines 1 and 2. So I'm just asking about the status of body line 2 and when you hope to migrate maybe Model S production on to that body line.

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

I think we're getting a bit too much into the internal decisions of Tesla. We don't want to over -- like if we say something that's related to an internal decision at Tesla, then it can overconstrain our decisions. And we need to have some flexibility there. So we'd prefer to not to comment on the details of when different production lines are moving around.

**Andrea Susan James**

*Dougherty & Company LLC, Research Division*

Okay. And then maybe longer term then. What is your updated thinking on your cost per kilowatt hour by the end of the decade, especially as you source your raw materials at the Gigafactory?

**Elon R. Musk***Co-Founder, Chairman, Chief Executive Officer and Product Architect*

I think that's quite a sensitive number, but it's -- I mean, it's probably -- it's less than what we see most people are estimating. So we see most people overestimating cost per kilowatt hour, but that is a proprietary number.

**Andrea Susan James***Dougherty & Company LLC, Research Division*

And I think in the past, you said you'd be disappointed if it was not below \$100.

**Elon R. Musk***Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes, in the long term, yes.

**Operator**

Our next question comes from Ryan Brinkman of JP Morgan.

**Ryan J. Brinkman***JP Morgan Chase & Co, Research Division*

A question for Jason probably. Other automakers sometimes talk about what they call minimum cash, the amount of cash that they need to end the quarter with in order to fund intraquarter working capital swings, even in the event total change in working capital during the quarter were negligible. I'm curious what you think your minimum cash needs are. And is that something you can share with the investment community? And then just more broadly, what total amount of cash or gross liquidity do you prefer to run the business with?

**Jason S. Wheeler***Former Chief Financial Officer*

Yes, sure. I mean we don't go over the workings of how we do those calculations internally, but \$1 billion is a nice comfort level. And you see we're starting to make the moves on the ABL, and it's to give ourselves more flexibility there. And then just reiterate a comment I made at the very beginning, cash is king, and I'm walking around collecting it.

**Ryan J. Brinkman***JP Morgan Chase & Co, Research Division*

Okay, great. And then just last question. On the Gigafactory, you've already given some updates. But maybe you could just talk about how much of the planned CapEx of 2016 relates to the Gigafactory. And then maybe an update on the relationship with your partners there, maybe Panasonic or any others, how those relationships are progressing relative to their expected future contributions.

**Jason S. Wheeler***Former Chief Financial Officer*

Sure, and it's a great question. And we're -- like I say, we're really excited about the Gigafactory, and things are on schedule. We're not at this time going to break out the detailed CapEx plans. I gave it to you thematically earlier. Certainly, Gigafactory towards the end of the year, we'll start to see some Model 3 investment. And then throughout the year, we'll see investments in sales, service and the Supercharger network.

**Jeffrey B. Straubel***Chief Technology Officer*

Maybe just quickly on the Panasonic piece. They continue to be an excellent partner in the project. And I think you've seen probably in the recent months some additional statements from them with ongoing capital commitments to the project as planned. Those are kind of happening in the right sequence.

They've also started hiring for the project and training people. So things are going as well as we could hope there.

### Operator

Our next question comes from Ben Kallo of Robert W. Baird.

### Tyler Charles Frank

*Robert W. Baird & Co. Incorporated, Research Division*

It's Tyler Frank on for Ben. Can you comment on the overall expectations for deliveries throughout the year? If we back out the 16,000 for Q1, it looks like about 23,000 per quarter for Q3 -- or Q2 through Q4, which it seems like you should be there with production given the Model X expectations and the Model S production expectations as well.

### Elon R. Musk

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Like I say, I know you'd love to have sort of more granularity, but it's difficult for us to give you granularity that we ourselves don't have. That's excessive precision. I don't want to give false precision, so it's -- I -- we feel good about like the overall number, but it might be around as to how it gets to that overall number. And there's always unforeseen things that occur. So that's why we kind of need some flexibility so we don't provide false precision and then people hold us to false precision.

### Tyler Charles Frank

*Robert W. Baird & Co. Incorporated, Research Division*

Okay. And then can you comment on what you're seeing for overall demand in the China market? And then what markets do you expect to move into next with which [indiscernible] and how that ramp will go?

### Elon R. Musk

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes, China is not a huge market for us and hasn't been historically. It is something we expect in the long term will be a big market and ultimately, probably our biggest market. So I think there's a lot of long-term opportunity there. So that's -- it would be -- it's difficult to say what's going to happen with China in the short term except that it doesn't really have a big effect on Tesla. Yes, I mean, long term, it would be. In terms of the new markets, I'm really excited to launch in Mexico this year. I'll be heading out to Mexico City, and we're going to -- I think there's actually quite a good opportunity there. And some of our customers -- we actually have customers in Mexico already, but having a significant presence there, I think, is going to be great. And some of our most supportive customers are actually in Mexico.

### Tyler Charles Frank

*Robert W. Baird & Co. Incorporated, Research Division*

Then a quick follow-up. There's been some rumors and commentary that the Model 3 launch may not be an actual full vehicle. Can you talk about what we should expect at the launch event at the end of March?

### Elon R. Musk

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes, we're trying to decide whether we should show all the cards or keep a few cards close to the vest. I haven't made the decision yet.

### Operator

Our next question comes from Rod Lache of Deutsche Bank.

### Rod Avraham Lache

*Deutsche Bank AG, Research Division*

You commented earlier, Elon, on the Model S versus the Model X demand being personal preference on passenger car versus SUV. And I was just wondering if you have any thoughts on whether Model S demand would or could be affected once the Model 3 is revealed. Do you think that those vehicles ultimately go to different customers? Or is there a plan to avoid cannibalization there?

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes, I mean, I think there's -- that they are different market segments, much as, say, the BMW 7 Series and 5 Series are -- and 6 are different -- they're different market segments from the 3 Series. And you should think of the Model 3 as sort of sort of -- for really competing in kind of the BMW 3 Series or Audi A4 market, and so if you want the sort of ultimate machine, you'd really want to get the Model S. But the Model 3 will be a great car.

**Jeffrey B. Straubel**

*Chief Technology Officer*

Yes. Maybe also just as an anecdote, there was a lot of concern when we launched the X about cannibalization of Model S demand. And we actually saw just the opposite, which was the increased interest and awareness and just customer engagement actually drove higher Model S sales even as the X was launched. So -- and those are actually much closer in terms of vehicle capability as we just talked about.

**Rod Avraham Lache**

*Deutsche Bank AG, Research Division*

Yes, yes, it makes sense. And I was hoping just on the financial side, can you give us just a little bit of a sense of how challenging it would be -- it will be to get to that 25% Model X gross margin? And can you comment at all on how you're expecting for the overall company gross margins would look this year? Are you expecting them to be able to stay above 25% even with the Model X ramping?

**Jason S. Wheeler**

*Former Chief Financial Officer*

Sure. So as we said in the letter, 25% by the end of the year for Model X -- sorry, I'm a little under the weather -- and 30% for the Model S. So you can do the math on what the blended rate will look like. In terms of getting to 25% for Model X, we have to think about it as we've got many years of history with the Model S right now. And that is learning that can certainly be applied to what we're doing with Model X. So we're comfortable that we're going to be able to drive gross margin in the right direction with Model X significantly throughout the year.

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes. And I mean, in the long run, we expect the gross margins of S and X to converge around the 30% number. So they should, in the long run, both be around 30%. That's our target. It's just -- as Jason was saying, because the X is the newer vehicle, we're just earlier on the learning curve for the X than the S.

**Rod Avraham Lache**

*Deutsche Bank AG, Research Division*

Okay. It sounds looks like it's not -- you're benefiting from some learning curves. So the margins, even initially, could be, okay, north of the 20% range. Is that a reasonable expectation, then kind of ramping up to that level? Or is it a more challenging kind of ramp?

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

I mean, I really look at it like where does it end up as opposed to where does it -- what happens in the very near term. And it's hard for us to predict exactly where it is in the near term. Like just think of that sort of S-curve and say like, where are you on the S-curve. And if you have a rapidly changing slope on

a curve, it's really hard to say, "Okay, let's pick a date," because you can move that date by a week and have a huge difference. But that's why it's hard for us to give you an exact number. But we kind of know where the S-curve will end up and as it starts to asymptote, then it gets much more predictable.

### **Operator**

Our next question comes from Dana Hull of Bloomberg News.

### **Dana Hull**

So as you think out 4 to 5 years to 2020 when you want to produce 500,000 cars each year, can you get there without building another assembly plant or a second Gigafactory?

### **Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes. Specifically, the -- for the Fremont plant, in fact, historically has produced almost 500,000 cars a year. So when it was a GM -- sorry, we can hear your keys quite loudly. The -- when it's -- when it was a Toyota GM plant, it produced almost 500,000 cars a year. We're comfortable that it can get back to that level. And then the Gigafactory is designed to support 500,000 cars a year worth of batteries, plus have 15 gigawatt hours left over for stationary storage.

### **Dana Hull**

Okay. So no need for a second Gigafactory like before something like [indiscernible]?

### **Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Correct. No need for a Gigafactory, correct.

### **Dana Hull**

Okay. And then for Jason, the shareholder letter says you plan to open about 80 retail locations and service centers and energize about 300 new Supercharger locations. Can you give us some commentary on where exactly those new service centers and retail locations might be? Is it mostly the Northeast of the U.S. or also globally?

### **Jason S. Wheeler**

*Former Chief Financial Officer*

Sure. So I think the general theme is two-pronged. We're densifying in markets where we already exist. And where demand has increased significantly, we've got to put service centers. And we try to actually predict ahead of that where we're going to need those. But as Elon referenced, we are opening new markets this year. But I think, in general, we're going deeper in markets where we are. And in addition, we're opening a significant number of stores in China and in the Northeast of the U.S. as we increase our awareness and our share in those markets. But you'll see service centers and retail locations opening across all of our markets, including Europe.

### **Operator**

Our next question comes from Mike Ramsey of The Wall Street Journal.

### **Mike Ramsey**

I guess I was hoping that maybe you can kind of give me an encapsulating feeling on the quarter. What -- it's sort of a mixed bag from an outsider's perspective. The losses are -- were pretty high and maybe higher than what people expected. But you're giving a very aggressive forecast. Do you feel like the company is on the right track and that you're past some of your hiccups? I guess I'm looking for a 40,000-foot analysis.

### **Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes, I feel very good about things right now. I mean, it was -- the last several months have been quite excruciating, I'd say. I mean, many late nights and weekends, but I think we're through the worst of it at this point.

**Mike Ramsey**

Okay. And I had wanted to ask a little bit about also your plans for consolidation. And Dana asked about whether the Gigafactory could handle the Model 3. I'm curious. I haven't been there. There are so many folks working over there now that aren't even building cars. You have engineers and stuff there. Can you give me a little idea about whether and when you might have to think about consolidating your operations in the Bay Area?

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

I'm not sure what you mean by consolidating. We are kind of spread out because in addition to Fremont -- the Fremont factory complex and headquarters in Palo Alto, we do have a number of other facilities in the Bay Area. But man, it's -- I'm not sure how we'd consolidate. We'd have to build a really big facility for that.

**Mike Ramsey**

So you might just keep taking over buildings all around, okay. All right.

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes, I think, man, it's something like the 7 million square feet of real estate at this point around the Bay Area, something like that.

**Jeffrey B. Straubel**

*Chief Technology Officer*

Yes, and we've seen the Gigafactory actually being a kind of helpful pressure outlet for some things in the Bay Area.

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Plus expansion in the Lathrop, Stockton area.

**Jeffrey B. Straubel**

*Chief Technology Officer*

Yes. We're going the other way.

**Operator**

The next question comes from Dee-Ann Durbin of Associated Press.

**Dee-Ann Durbin**

Considering now that the Chevy Bolt is going to go on sale at the end of this year, so that'll be a full year that it's on sale before Model 3 arrives, does that -- I mean, has it taken any wind out of your sails? And -- or do you think, again, that these are very different customers? If you're comparing to an Audi A4, for example, are people still going to be attracted to the Model 3 even though they'll have that option on the market quite a while before the Model 3 arrives?

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*



Well, I mean, I would sort of point you to the market share of large luxury vehicles or large premium sedan sales in the U.S. that I talked about earlier in the call. We're currently outsell everyone in that category and had a 51% market growth last year where everyone else declined and the market as a whole declined. So I mean, if Model 3 is at all similar in its market segment, it doesn't seem like we're going to be demand constrained.

**Dee-Ann Durbin**

Okay. And I know you don't do any marketing, but I'm wondering if you would ever possibly reconsider that. It struck me when you were saying that you aren't where you could be on the East Coast and that may be because people need more educating about how the car performs in the snow or whatever, do you think there's ever a point at which you might reconsider and do some very targeted marketing in places where you think you could do better?

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes, I don't think it's in the near -- I don't think we'd do that in the near term. But in the long term, I think I could see us doing advertising where that advertising was interesting, entertaining and people don't regret seeing it, which unfortunately, is not the case for most advertising. So I mean, if there's sort of something interesting and artistic or just like you -- it's entertaining, it's like wouldn't waste people's time if they saw it. And also, I think we need to have a more affordable, high-volume car, before that makes sense, like the Model 3, so that it's more accessible. So if we do mass media, then it's more likely that somebody could buy the car. And that's kind of the point when it would be something we'd consider.

**Operator**

Our next question comes from the line of Phil LeBeau of CNBC.

**Phil Lebeau**

Elon, I'm curious if you are noticing any impact in terms of reservations, orders in terms of the market volatility that we're seeing, the growing questions about instability in our economy, elsewhere, fall-off in the wealth effect, if you will. Are you guys noticing any slowdown in the pace of orders?

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Jon, do you want to...

**Jonathan McNeill**

*President of Global Sales and Service*

Yes, I think, Phil, it's a great question. And actually, the answer is no. The demand is very strong. We're up significantly over 2014 in the same period. And for both -- for S and X, we -- both the order rate on S and the conversion rate to orders on X has been very strong. And we're not seeing that impact at this point in time across really all of our markets, both domestic and international.

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes. I mean, that said, we don't want to be complacent about demand generation. And as we mentioned, there's a bunch of stores opening that -- in markets where we really haven't had a store or any kind of meaningful store. I mean, our store in Manhattan, you basically need to be shown like almost to find it. So unless you hunt us down, you won't find the store. I think we obviously need to change that and put stores where people are likely to encounter them, kind of like a fishing boat or something. It's like you just don't -- you want to be where the fish are. It's like not in some sort of random barren location. So that's kind of what we're doing. So we're not complacent about demand. And just in case we see things take a turn for the worse, we want to overshoot on demand generation by our stores.

**Jeff Evanson**



*Vice President of Investor Relations*

All right, everyone, that concludes the Q&A session of the call. Thank you so much for joining us today, and we look forward to seeing you all in the future.

**Elon R. Musk**

*Co-Founder, Chairman, Chief Executive Officer and Product Architect*

Yes. Thanks, everyone.

**Operator**

Ladies and gentlemen, you may disconnect your lines at this time. That does conclude your call. Have a great day.

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