

6-August-2010

Tesla Motors (TSLA)

Manufactures high-performance electric vehicles and powertrain components.

Investment Rating: Marketperform

Pricing Update

Stock Data *(in mil, except per share)*

Current Price (6-Aug-2010)	\$19.75
Shares Outstanding	103.6
Market Capitalization	\$2,047.0
Enterprise Value	\$1,911.7

IPO Data

Offer Date	6/28/2010
Offer Price	\$17.00
Price Range	\$14.00 - \$16.00
Shares Offered (% insider)	13.3 (10%)
Deal Size	\$226.1
Use of Proceeds	Capex

IPO Underwriters *(*bookrunner)*

Goldman, Sachs & Co.*	Morgan Stanley*
J.P. Morgan*	Deutsche Bank Securities*

Key Financial Data *(\$ in mil)*

Income Model	FY Ended Dec			
	2009A	2010E	2011E	2012E
Sales	\$111.9	\$113.2	\$126.0	\$610.0
EBITDA	-43.5	-90.8	-99.1	7.6
Net Income	-55.7	-133.5	-161.0	-83.5
EPS	-0.72	-1.37	-1.55	-0.80
Gross %	9%	21%	21%	23%
EBITDA %	-39%	-80%	-79%	1%

Balance Sheet		As of 3/31/10 (adj.)
Cash	\$169.5	
Total Assets	253.3	
Total Debt	46.4	
Shareholders' Equity	229.2	

Corporate Data

Employees	680
Year Founded	2003
Headquarters	Palo Alto, CA
Phone Number	(650) 413-4000
Web Address	www.teslamotors.com

Rating Analysis

Very Weak Neutral Very Strong

Long-Term

Company Fundamentals	<div><div></div><div></div><div></div><div></div><div></div></div>
Corporate Governance	<div><div></div><div></div><div></div><div></div><div></div></div>

Short-Term

Relative Valuation	<div><div></div><div></div><div></div><div></div><div></div></div>
Technical Strength	<div><div></div><div></div><div></div><div></div><div></div></div>

Tesla zooms off the line in strong debut; remains on track for 2012 sedan launch.

Tesla Motors raised \$226 million in its upsized IPO by offering 13.3 million shares at \$17, above its \$14 to \$16 range. The company sold 20% more shares than originally anticipated and filled the overallotment. Heavy media coverage and investor interest in this intriguing growth story drove a 41% first day return on high volume, although the stock has since settled in the \$20 range. Following the IPO, the company announced a strategic agreement with Toyota in July and reiterated its mid-2012 target for the Model S launch on its 2Q earnings call.

Valuation hinges on a successful Model S debut. We focused our valuation analysis on an absolute approach given Tesla's lack of close comparables and the growth inflection point associated with the 2012 Model S launch. Looking out to 2014, our DCF analysis suggests that annual production of 20,000 Model S units supports a valuation in the \$14-\$16 range, without any contribution from future model rollouts. For investors that believe this sales target is conservative, an annual production assumption of roughly 30,000 units implies a fair value just above \$30.

Initiate coverage at marketperform. Though the successful launch of the Roadster provides proof-of-concept and valuable brand cachet, Tesla faces substantial execution risk as it burns roughly \$650 million to get its luxury sedan to production. Multiple major auto firms plan to launch competing electric vehicles by 2011 and Tesla's integrated sales model is untested at scale. Given the early stage of the business, we are disappointed by the insider selling and the fact that the CEO splits time with other companies. That said, our DCF suggests that the valuation is not unreasonable if management can reach its sales targets for the Model S, and we are encouraged to see the traction its technology has gained with strategic partners (and investors) Daimler and Toyota. At its core, however, this deal remains a bet that Tesla can evolve into a legitimate player in the global automotive marketplace.

Bull Insights

- Planned launch of mainstream models creates massive addressable market
- Roadster sales and development agreements validate powertrain technology
- \$465 million in low interest DOE loans provide balance sheet flexibility
- Raised more than \$300 million from investors including Daimler and VCs

Bear Insights

- Highly unprofitable and expects cash burn to accelerate into sedan launch
- Multiple major auto manufacturers plan to launch competing EVs by 2011
- CEO sold on the IPO and will split time with other companies
- Relies on government subsidies and widespread EV acceptance is uncertain

Company Fundamentals
Rating: Weak
Overview:

Backed by PayPal co-founder Elon Musk and a host of big-name investors, Tesla Motors was the first company to commercially produce a highway-capable, fully-electric vehicle (EV). With access to \$465 million in low-interest loans from the US Dept. of Energy, Tesla recently acquired a production facility on the cheap and seeks to leverage its proprietary electric powertrain technology to produce a line of mainstream EVs, starting with the launch of its Model S luxury sedan in 2012. Initially targeting a 1% share of the global premium sedan market, the company plans to use a common powertrain platform to support a diversified line of vehicles.

Rating Rationale:

Tesla's successful commercialization of its high-performance Roadster provides proof-of-concept for its on-the-come mass market products and helped build the company's brand without a significant marketing investment. Though a low interest loan from the DOE will help offset cash burn, the company faces substantial execution risk in launching its luxury sedan, which will be manufactured at a much larger scale and faces uncertain demand in a nascent end market. Additionally, multiple major auto firms plan to roll out competing EVs by 2011.

Business:

Designs and manufactures high-performance fully electric vehicles (88%) and advanced EV powertrain components (12%). Its two-seat convertible Roadster, introduced in late 2008, is the first and currently only federally-compliant, highway capable EV produced at commercial scale. Has sold over 1,200 Roadsters to customers in 28 countries, primarily in the US and Europe (int'l sales are 56%). Roadster has a lithium ion battery pack with capacity of 53 kwh and a range of 236 miles on a single charge. Base price is \$109,000 before \$7,500 federal tax credit. Model S is a four-door, five-passenger luxury sedan with range options between 160-300 miles and a base price of \$57,400 before federal tax credits; the company has already received 2,800 refundable reservations with commercial production slated for 2012. Vehicles can recharge in 7 hours on a household appliance outlet (40 amp/240 volt) or 4.5 hours on a specially-installed 70 amp/240 volt high power connection. Sells and services vehicles directly via a network of 13 major market stores (<5,000 sq. ft.); plans to increase network to 50 stores in coordination with the Model S launch. Currently, Roadster body and chassis are manufactured at a Lotus-owned facility in England. In May 2010, purchased an existing production facility in CA from a Toyota/GM joint venture for \$42 million; targets initial annual production of 20,000 Model S units and capacity can be increased to 50,000 with minimal capex. Is transitioning its powertrain component manufacturing to its Palo Alto facility. Has been approved for \$465 million in DOE loans, which will cover 80% of eligible costs for manufacturing build-out. Plans to roll out a suite of EVs over time, including a lower price point model (~\$30k) in 2014 or later. Holds 14 patents and 97 applications.

Competition:

The launch of the Model S will put Tesla in the global premium sedan market (2 million vehicles in 2008). Existing luxury sedan competitors include Audi, BMW, Lexus and Mercedes. Nissan, BYD Auto, Ford and GM all plan to introduce competing plug-in vehicles by the end of 2011. Other well-financed emerging EV vendors include Fisker, Coda, Wrightspeed and eWolf.

Key Issues:

Is highly unprofitable and expects cash burn to accelerate as it invests in R&D, manufacturing capacity and new Tesla stores. Does not expect to reach operating breakeven until it begins significant deliveries of the Model S in 2012, at the earliest. Electric vehicle demand is subject to quality/safety concerns, grid capacity and reliability, availability of government incentives and developments in competing technologies (e.g. internal combustion, fuel cells, ethanol, CNG). Currently has a drivable early prototype of the Model S, but faces significant hurdles to commercialization including finalized design, component sourcing, safety testing and manufacturing plant build-out. Experienced an eight month delay in launching the Tesla Roadster and could experience similar delays for the Model S. Sales & service model is unproven and may result in slower expansion than a franchising strategy. Anticipates that IPO and private placement proceeds, plus cash on hand and DOE loan (\$689 million) will fund operations for only 24 months.

Income Statement Data

<i>FY Dec (\$ in mil)</i>	2007	2008	2009
Sales	\$0.1	\$14.7	\$111.9
Gross Margin	87.7%	-7.7%	8.5%
EBITDA Margin	--	-501.4%	-38.9%
Operating Margin	--	-532.5%	-46.4%
Net Margin	--	-561.5%	-49.8%

Cash Flow Data

CFFO	-\$53.5	-\$52.4	-\$80.8
Less: Capex	9.8	10.6	11.9
Free Cash Flow	-63.3	-63.0	-92.7

Additional Data

Roadsters Sold	--	107	830
ASP (in \$k)	--	\$105	\$125
Roadster revenue	--	\$11.2	\$103.7

Latest Results and Outlook

Recent Financial Trends:

For the three months ended June 2010, sales grew 5% despite a 23% decline in Roadster volume, which was more than offset by a 24% improvement in Roadster ASP and the commencement of development revenues from Daimler (\$4.4 million). Gross margin improved to 22%, compared with 8% in the 2Q09, as a result of Roadster component cost reductions and the timing of costs related to the Daimler development agreement. However, cash operating losses expanded sharply as a result of continued investments in R&D and SG&A headcount and cash flow from operations fell to -\$18 million.

In July, the company announced an agreement with Toyota to develop an electric powertrain for the RAV4 and expects to begin recognizing development revenues in the 2H10. The company provided guidance for full year revenues in the range of \$100-\$115 million.

Outlook:

Tesla's fortunes are closely tied to the development and rollout of its second generation Model S sedan, and with the support of up to \$465 million in low-interest loans from the government, the company plans to invest heavily in its newly acquired production facility. Leading up to the 2012 sedan launch, Tesla should continue to generate revenue from the sale of roughly 600 Roadsters per year (~\$100 million) in addition to increasing component and development business from Daimler and Toyota. Nonetheless, the company will continue to incur significant operating losses due to ramping R&D and SG&A expense, and will borrow heavily under its DOE loan to fund expected capex of \$100-\$125 million in 2010, followed by an estimated \$250 million in 2011.

Assuming Model S deliveries begin by mid 2012, we currently expect EBITDA to reach breakeven in 2012 on sales of 10,000 units at an expected ASP of roughly \$60,000 (~\$600 million). However, Tesla expects existing sources of funding to dry up within 24 months, and we assume it adds \$200 million in debt in 2012 to offset continuing cash burn. At targeted production levels in 2013 (20,000 units), the company could generate revenue of \$1.5 billion, EBITDA of \$175 million and EPS of \$0.63. That said, we note that a 10,000 unit swing in our volume assumption causes EPS to rise (fall) to approximately \$2.00 (breakeven). Management's long-term operating model calls for gross margins of 25% and operating margins ranging from 12-16%, though our model falls at the lower end of this range (11%), owing to expected competitive forces. The company plans to launch additional models in 2014 or later (van, cabriolet, SUV), which would materially expand its addressable market and could support \$4-\$5 billion in annual sales or greater.

Interim Results - 3 months ended

(\$ in mil)	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
Sales	\$26.9	\$45.5	\$18.6	\$20.8	\$28.4
Gross Profit	2.1	7.7	1.8	3.9	6.3
EBITDA	-6.2	-2.1	-20.0	-20.5	-22.8
Operating Income	-8.1	-4.3	-22.9	-26.0	-31.4
Net Income	-10.9	-4.6	-24.2	-29.5	-38.5
EPS	-0.14	-0.06	-0.31	-0.38	-0.37

Margins

Gross Margin	7.8%	16.9%	9.6%	18.5%	22.0%
Operating Margin	-30.0%	-9.4%	-123.4%	-124.9%	-110.4%
Net Margin	-40.3%	-10.1%	-130.4%	-141.8%	-135.6%

Cash Flow Data

Operating Income	-8.1	-4.3	-22.9	-26.0	-31.4
Plus: D&A/Non-Cash	1.8	2.2	2.9	5.5	8.6
EBITDA	-6.2	-2.1	-20.0	-20.5	-22.8
CFFO	-12.2	-23.5	-29.0	-27.3	-17.9
Less: Capex	2.5	2.3	6.2	5.5	9.2
Free Cash Flow	-14.7	-25.7	-35.2	-32.8	-27.1

Additional Data

Tesla Roadsters Sold	200	324	124	126	141
ASP (in \$k)	\$127	\$127	\$143	\$159	\$158
Roadster revenue	\$25.4	\$41.0	\$17.7	\$20.1	\$22.2

Balance Sheet Data

(\$ in mil)	Actual 3/31/10	Actual 6/30/10	Post IPO 6/30/10
Cash	\$77.0	\$47.3	\$181.6
Total Assets	160.8	148.0	382.3
Total Debt	46.4	46.4	46.4
Shareholders' Equity	44.2	26.2	260.5

Corporate Governance
Rating: Weak

Tesla has raised nearly \$320 million since 2003 from its CEO, key development partner Daimler and a group of reputable venture backers. Additionally, Toyota invested \$50 million at the IPO price in a concurrent private placement and has announced its intention to cooperate with the company on the development of EVs. Prior to December 2009, CEO Elon Musk did not receive any compensation for his services (he currently only accepts \$1 in salary) and half of his December 2009 option grant (\$24 million fair value) vests based on development milestones for the Model S sedan. That said, we cannot overlook the fact that the CEO will split time as he continues to serve as CEO/Chairman of Space Exploration Technologies and Chairman of SolarCity. Several insiders sold on the offering and overallotment, including the CEO and key venture backer VantagePoint; while small on an absolute basis, we find it inappropriate given the early stage of Tesla's business. Finally, only one of eight directors is independent by our standards.

Key Executive	Age	Position	Corporate Background
Elon Musk	38	Chairman & CEO	Co-founder. Chairman since 2004 and CEO since Oct. 2008. He also serves as the CEO and Chairman of advanced rocket producer Space Exploration Technologies (since 2002) and Chairman of solar installation company SolarCity (since 2006). Co-founded PayPal, which was acquired by eBay in 2002 (\$1.5 billion) and enterprise software and services firm Zip2, which was acquired by Compaq in 1999.
Deepak Ahuja	47	CFO	Since July 2008. Served in multiple roles at Ford from August 1993 to July 2008, including Vehicle Line Controller of Small Cars Product Development (2006-2008) and CFO for Ford of Southern Africa (2003-2006).
Jeffrey Straubel	34	CTO	Since May 2005. Previously served as Principal Engineer, Drive Systems from March 2004 to May 2005. Earlier, was CTO and co-founder of aerospace firm Volacom.

Key Shareholder	Holdings	Additional Details
Elon Musk	28.5%	Co-founder. Has invested \$48.4 million in preferred stock and convertible notes since 2007 at an average cost basis of just over \$1 per share. Includes 1.2 million options at a strike price of \$6.63. Sold 5% of his holdings (\$24 million) on the IPO.
Daimler	8.0%	Invested \$57.5 million in 2009 at an average cost basis of roughly \$7.50. Holds one board seat.
Abu Dhabi Government	7.8%	Invested \$65 million in 2009 at a cost basis of \$8.91. Holds one board seat.
VantagePoint Venture Partners	6.6%	San Bruno, CA-based VC firm. Invested \$10.6 million since 2007 at an average cost basis of roughly \$7.50. Sold 13% of its holdings (\$16 million) on the IPO and overallotment.
Valor Equity Partners	5.2%	Chicago-IL based middle-market PE firm. Invested \$10.8 million since 2007 at an average cost basis of \$3.25 per share. Holds one board seat.
Toyota	3.2%	Invested \$50 million at the IPO price in a concurrent private placement.
Draper Fisher	3.0%	Has one board seat. Invested in May 2006.

Relative Valuation
Rating: Neutral

We focused our valuation analysis on an absolute approach given Tesla's lack of close comparables and the growth inflection point associated with the 2012 Model S launch. Looking out to 2014, our DCF analysis suggests that annual production of 20,000 Model S units supports a valuation in the mid teens, without any contribution from future model rollouts. For investors that believe this sales target is conservative, an annual production assumption of roughly 30,000 units implies a fair value just above \$30.

Valuation Methods

	DCF – 28,000 units	DCF – 20,000 units
Methodology	30x 2014 Net	25x 2014 Net
Implied Value	\$30.58	\$14.51
Upside/Downside	+56%	-26%

View DCF Model at www.ipointelligence.com/iporesearch/
Comparable Financial Analysis

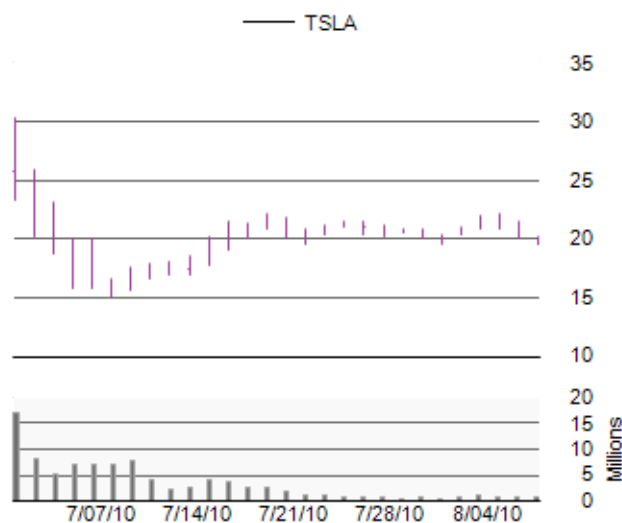
<i>IPO and Key Peers</i>	<i>Sales (US\$)</i>	<i>GM</i>	<i>EBITDA</i>	<i>EBIT</i>	<i>Net</i>	<i>ROE</i>	<i>ROIC</i>	<i>Debt- to-Cap</i>	<i>Sales 2010E</i>	<i>Sales 2011E</i>	<i>Sales 2012E</i>	<i>'10-'12 CAGR</i>
Tesla Motors	\$113	17.3%	-57.7%	-74.6%	-85.5%	-54.0%	-19.4%	15.1%	\$113	\$126	\$610	132%
A123 Systems	\$96	-13.0%	-86.9%	-107.0%	-106.7%	-15.5%	-5.0%	3.8%	\$135	\$286	\$657	119%
China Bak Battery	\$217	14.6%	3.5%	-3.0%	-11.8%	2.4%	5.5%	53.6%	\$236	\$310	\$400	30%
Advanced Battery Tech	\$72	45.5%	32.2%	27.3%	40.8%	0.0%	18.9%	0.0%	\$103	\$150	\$185	34%
Ener1	\$46	10.2%	-107.2%	-125.8%	-134.0%	-18.5%	-6.4%	18.9%	\$92	\$231	\$319	87%
Energysys	\$1,579	22.9%	10.8%	7.9%	3.9%	14.6%	12.7%	30.9%	\$1,789	\$1,943	\$2,084	8%
BYD Auto	\$5,829	21.7%	16.8%	12.3%	9.6%	32.4%	26.9%	16.1%	\$9,271	\$11,547	\$13,887	22%
Nissan	\$87,594	18.2%	12.9%	4.1%	0.6%	9.0%	8.3%	55.2%	\$94,579	\$101,682	\$108,146	7%
Ford	\$129,207	12.8%	7.5%	2.6%	5.1%	-144.7%	5.5%	104.3%	\$114,017	\$123,041	\$127,198	6%
Toyota	\$220,822	12.0%	8.2%	0.8%	1.1%	6.4%	4.8%	53.4%	\$224,967	\$236,237	\$253,211	6%
Group Average		16.1%	-11.3%	-20.1%	-21.3%	-12.7%	7.9%	37.4%	\$49,465	\$52,825	\$56,232	35%

Note: All dollars are in millions. All financial metrics are based on LTM data; return metrics are based on forward estimates.

Comparable Valuation Analysis

<i>IPO and Key Peers</i>	<i>Ticker</i>	<i>Price</i>	<i>Market Value</i>	<i>Enterprise Value</i>	<i>EV/Sales</i>			<i>EV-to-EBITDA</i>			<i>LT Growth</i>	<i>P/B</i>
Tesla Motors	TSLA	\$19.59	\$2,029	\$1,894	16.7x	15.0x	3.1x	--	--	249.8x	50%	7.8x
A123 Systems	AONE	\$10.68	\$1,103	\$713	5.3x	2.5x	1.1x	--	--	18.7x	35%	2.2x
China Bak Battery	CBAK	\$1.62	\$102	\$261	1.1x	0.8x	0.7x	10.1x	7.7x	6.0x	30%	0.6x
Advanced Battery Tech	ABAT	\$3.52	\$242	\$186	1.8x	1.2x	1.0x	6.1x	4.2x	3.4x	30%	1.7x
Ener1	HEV	\$3.32	\$451	\$478	5.2x	2.1x	1.5x	--	--	--	50%	2.9x
Energysys	ENS	\$24.20	\$1,165	\$1,315	0.7x	0.7x	0.6x	6.4x	5.5x	4.9x	16%	1.5x
BYD Auto	1211 HK	HK\$52.05	\$14,374	\$14,572	1.8x	1.4x	1.2x	11.9x	9.7x	8.2x	40%	5.1x
Nissan	7201 JP	¥669.00	\$32,411	\$67,338	0.7x	0.7x	0.6x	6.4x	6.0x	5.2x	14%	0.9x
Ford	F	\$13.04	\$54,038	\$137,904	1.2x	1.1x	1.1x	13.4x	12.0x	10.9x	14%	-9.9x
Toyota	7203 JP	¥3,115.00	\$113,827	\$209,779	0.9x	0.9x	0.8x	11.6x	9.7x	8.4x	14%	0.9x
Group Average (battery OEMs)*					2.7x	1.5x	1.0x	8.6x	6.8x	8.2x	33%	2.3x
Group Average (auto OEMs)					0.9x	0.8x	0.8x	8.6x	7.5x	6.6x	17%	1.2x

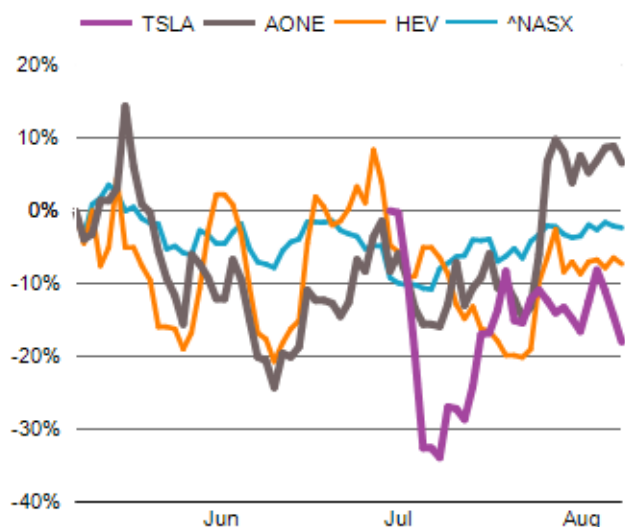
Note: All dollars are in millions except for per share amounts. *Includes AONE, CBAK, ABAT, HEV, ENS, and BYD Auto.

Technical Strength
Rating: Strong
**Stock Performance of IPO and its Peer Group
TSLA**


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IPO Performance Data

First Day	41%
Aftermarket	-18%
Total Return	15%
Quiet Period Release	8/8/2010
Lock-up Release	12/25/2010
Days to Lock-Up Release	141
Shares Available for Sale	77,814,390
Percent of Total Shares Outstanding	75%

TSLA vs Key Publicly-Traded Peers vs Index


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Publicly - Traded Peer Group

Key Peers	Ticker	Stock Price	1-Mo. Return	3-Mo. Return	YTD Return
Tesla Motors	TSLA	\$19.59	15%	15%*	15%*
A123 Systems	AONE	\$10.68	26%	7%	-52%
China Bak Battery Inc	CBAK	\$1.62	-3%	-13%	-42%
Advanced Battery Technolog	ABAT	\$3.52	15%	14%	-12%
Ener1 Inc	HEV	\$3.32	-2%	-7%	-48%
Energysys	ENS	\$24.20	15%	2%	11%
Byd Co Ltd-H	1211 HK	HK\$52.05	-8%	-22%	-24%
Ford Motor Co	F	\$13.04	28%	11%	30%
Indexes					
Nasdaq Composite Index	CCMP	2,261.80	1%	-6%	0%
S&P 500 Index	SPX	1,095.31	1%	-6%	-2%
FTSE Renaissance IPO Index	IPOS	214.97	3%	-4%	-1%

Stock prices as of 08/06/10. *Return from IPO.

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Outperform	20%
Marketperform	74.9%
Underperform	5.1%

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The following table details the history of all RC research recommendations on **TSLA** since its initial public offering.

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