

First question, how many vehicles are coming clean off the line with no material rework at this point? And I'm just curious, has any model really come pure off the line at all without much rework? Thanks.

Elon Musk

We do get some cars that are required meaningful rework. But generally we're trying to maintain extremely standard of qualities. So if we see some that's even a minor aesthetic issue, we want to correct that. And now that most vehicles require some work to correct minor issues. A lot of issues are not something that mostly would even notice, but we're trying to get as close to perfect as possible.

Nonetheless, we are able to get to a production rate, which is annualized at 10,000 cars a year. And I feel really good about where we are with respect to manufacturing the vehicles.

Adam Jonas - Morgan Stanley

If you think about all the issues that were affecting the early production of the vehicle, what are the key ones that you've solved, which ones have yet to be solved, and is the list of new problems growing, meaning, are there any additional new problems that you're finding or all the issues that you know in terms of either quality or supply known and that's a shrinking list now?

Elon Musk

Our biggest issue has been getting all of the parts of the vehicle on time for suppliers and at a very high quality. I think we're through those issues. There are no supply issues that I'm aware of right now, that prevent us from achieving at an annualized production rate of 20,000 vehicles a year, basically within next four, five weeks.

So it's looking good. That's not to say something couldn't crop up, but it's looking quite good. And we're seeing a rapid decline in the number of correct issues that needs to be corrected as vehicles come up in the line. So it's getting better very quickly. So right now, I feel very optimistic about with the way things are. And I'm not aware of any issues in front of us getting to the 20,000 units to our annualized production volume.

Adam Jonas - Morgan Stanley

Deepak, just a couple of very quick ones for you. On the reservation outlook, I know you're targeting a new high-water mark in terms of unit reservations over 13,200 by yearend. But when we look at the reservation balance on the

balance sheet, should we assume that that's going to be lower, and if it is lower, can you give any kind of lower bound of that, meaning should it be going to still be over \$100 million end of year?

Deepak Ahuja

Yes, I think it definitely will be over \$100 million. And you're right, to the extent signature reservations come off. We have collected a much higher deposit on them compared to general production reservations. So there would be some adjustment in our reservations balance to account for that.

Adam Jonas - Morgan Stanley

And then on R&D, you gave the flat 4Q guidance around \$60 million. That is a quite a bit higher, I think many people on the call would have expected. Are you able to explain kind of why is it running higher and is \$60 million a quarter a run rate, we should use going in the next year?

Elon Musk

Yes, I think we should be, as the letter has indicated this is still a 19% reduction from the prior quarter, and that's primarily as we have pulled out all the manufacturing related expenses. Most of our R&D count now is people at this point, and we are focused on future product development, bunch of actions still continue to improve our products. So I think that's fairly reasonable rate going forward.

Operator

Our next question is from Patrick Archambault of Goldman Sachs.

Patrick Archambault - Goldman Sachs

I guess I just wanted to follow one clarification and then a separate question, just on Adam's question. We can affirm that what's left in terms of challenges is really sort of fit and finish challenges, kind of that are related to the assembly process rather than the availability of the right amount of components. So is that a correct interpretation?

Elon Musk

Yes. So right now we're able to build cars at the 10,000 year-to-year annualized rate with the parts we need. And as of today, I don't know if any part that would prevent us from getting to the 20,000 year-to-year level in four or five weeks. So it looks like once a plain sailing, but it looks like, solid sailing in that direction. So I think those gross could come up, that I'm not

aware of any obstacles to that as of to getting there right now, touchwood, it's looking quite good.

And I should say, I mean, overall, I feel Tesla was really kind of past the point of high risk. Several months ago, I said I thought that the coming several months would be really the test for Tesla. And it's the classic phrase of, going through the valley of death, and I feel as that we are through that valley at this point.

Patrick Archambault - Goldman Sachs

And then maybe one for Deepak, just at a high level can you maybe just give us a little bit on the landscape of capital investments. You've clearly from an R&D point transition to the X, but then there is also I assume early engineering done the Gen III. So how should we think about sort of a lumpiness of your R&D and capital spending patterns as we kind of look at to the next 18 months or so?

Deepak Ahuja

I think what I would prefer to do is that the next earnings call provide formal, a sense of the trends we would have on our R&D expenses for 2013. But I think broadly speaking the factors that affect R&D would be as you said our new product development which includes Model X, Model S. And we're going to be working on a right-hand-drive version, European version, there are few other things. And it's our continued improvements in manufacturing and design that we will be focused on.

So there will be some degree of lumpiness. But nothing there will be as significant as we saw in 2012, because all the manufacturing expenses are no longer in R&D. And we've continued to stay that way.

Elon Musk

Just to clarify what is interpreted by Deepak's statement is that the left-hand-drive European version has very little work left to do to it. In fact, we have two EU approved vehicles in EU right now during the initial market. We just started marketing in EU. So the real incremental R&D is with respect to, as Deepak mentioned the right-hand-drive version of the EU version, which had applied to Japan and Hong Kong and few other places.

And then there are a few other variants of the Model S that we will kind of put next year that I think is going to be pretty exciting. In addition to, of course, we were getting into the Model X and starting the initial design work of the third generation S market vehicle.

Operator

Our next question is from Amir Rozwadowski of Barclays.

Amir Rozwadowski - Barclays

Touching on the sort of the new reservation activity, you mentioned sort of new reservations in the quarter were roughly around 2,900 with net reservations around 1,700 and cancellations have crept up. I was wondering, if you could give us a little bit of color in terms of what's driving sort of the cancellation activity? Do you expect it to diminish at some point and perhaps also do you expect to transition to much more of a real time sort of orders/delivery type model versus what we've seen obviously in the early stages of the launch of the vehicle with sort of the reservation type model?

Elon Musk

I'm sure I can answer a part and then I'll turn it to George to add some more details. I think that the way things are going with Tesla, it will be a while before we transition to any kind of real time meaning like you can just go in and buy a car. And given the way to pursue effectively settlements right now and expect to be at least for a few quarters and continue new high-water marks and new reservations.

I think it could be quite a while before someone can just walk in and buy a car. It could be as far as to 2014 before that's even possible. So it's certainly correct. If they're assuming the car to put down a reservation, and not to be able to impression that they will just be able to at some point buy car and just have it in the line. I often encounter this sentiment with people where they can just wait and then just be able to buy a car and I think it's going to a long time before that's the case. George, would you like to add anything to that?

George Blankenship

It's been a lot of time in the story, I think here is what's happening is, our increase in reservations is a combination of several things. One is we have more stores open and as we open more stores, we're getting in front of more, and more, and more people everyday. I mean, we've seen 1.8 million people through our stores year-to-date, but the last quarter was a significant increase over previous quarters, because of more stores being open and we've got five more opening by December 1 of this year, all in high-traffic, high-visibility locations.

And as we open up the new stores, more and more people are coming and say, who is Tesla, and we're getting that increase in awareness in significant

ways. And I think we're reaping some of the benefit of having been open now for about 18 months with these new design stores where we getting a lot of traffic.

And then I think next is the awards. We're getting some very, very positive awards that we're letting people know about. And that's reinforcing that the car is quite extraordinary and somebody else is saying, besides us. We got a lot of press right after the June 22 start, and now we've got more recently with Automobile Magazine, Yahoo! Autos, thus making real positive.

And then there is one other element that we're experiencing in California, specifically where we've delivered a lot of cars is that they're putting cars on the road now that people are taking other people out to dinner with, they're going to movies, they're going to shows with, they're going to their house and people are seeing the cars, oh my god, how do I get one of these. And so our customer base that had actually received their cars are actually selling cars for us, making reservations for us.

And so we got, the really big effect going on right now, which is really positive. And as far as timelines when people would be able to come in and buy a car right away, I don't see that anytime in the near future, in fact that's not even the goal. The goal will always be that there is a reservation time, so that we can build your cars specifically for you. So I don't see that on the horizon at all at this point.

Elon Musk

I get to know a customer, who's received a car, and told me weirdly, how many additional cars they sold to people that they know, in some cases, strangers on the street. It really is spreading quite wildly by word of mouth. It's worth noting that at Telsa store does not spend any money on advertising.

Amir Rozwadowski - Barclays

And it does seem like you folks are benefiting from this halo effect as you get vehicles on the road, just on the flipside with respect to cancellations. However, I mean do you expect sort of to reach a threshold, which there's less cancellation activity, just given that now you have more stores out there, perhaps it's a little bit timeframe, rather is a timeframe to wait for a car, perhaps it's compressing a bit as you start to deliver these vehicles? Just trying to understand the dynamics for sort of net reservations there?

George Blankenship

We do a lot of watching of this and I also saw that. And what's happening is the refunds that are happening now were very, very expected. We're going through people, through the reservations that were made in 2009, 2010, lots of changes that's happened at different points in time.

And by the time we get into Q1, what will happen is, the waiting time between when you make your reservation and when you actually configure your car, will go from two-and-a-half to three years, and then down to literally a couple of months. So the time will just be minimal. The time will be minimal, and therefore there won't be a reason to be canceling. So we see this becoming a non-issue in North America as we get into the beginning of next year, I mean the refund count will go down a lot.

Amir Rozwadowski - Barclays

And then, lastly if I may, looking at your guidance for sort of delivery this year, it seems there's a modest down tick from your prior expectations of around 2,700 to 3,250 versus now regarding the release around 2,500 to 3,000. Is that largely attributed to some of the supply issue that you guys had already mention, and should we expect this to be sort of, now that it seems like those are behind you or is this sort of a fairly achievable target from your perspective?

Deepak Ahuja

Just to clarify there, Amir, our guidance hasn't changed. The 2,500 to 3,000 deliveries is for Q4, while the 2,750 to 3,250 was the full year guidance, and that includes Q3 deliveries.

Jeff Evanson

We've consumed 20 minutes here, getting through just a few of you, so let's just leave it to one question and one follow-up, please. Operator, let's have the next question please.

Operator

Our next question is from Aditya Satghare of Lazard.

Aditya Satghare - Lazard

I wanted to better understand your prepared remarks about the gross margin target by the end of the year. So could you give us a sense of, if you were to take away the cost of the ramp up and say cost of additional rework, where would the gross margin stand today?

Elon Musk

That's interesting, hypothetical. Well, I guess I would say assuming that we're at the 20,000 unit per year production rate, which we've been quite at, because the gross margin is really affected by the ramp. And assuming that it's too fast-forward, five weeks or something like that. And if you take out the short-term cost issues associated with the ramp, and just the things that we sort of have put on hold. If you take non-cost down issues that we put on hold to ensure that we make around, we would be at the 25% gross margin level.

Aditya Satghare - Lazard

My follow-up question was on the delivery mix for 4Q. So could you give us some more color as to, how is the mix sort of shaping out was this year prior to expectations going into the last quarter?

Elon Musk

It's right on track, exactly what we expected.

Operator

Our next question is from Aaron Chew of Maxim.

Aaron Chew - Maxim

I know you offered decent amount of updates on reservations, is there anyway you can offer some insight into how reservations on a gross of net basis returning in October? Maybe even some general highlights and how they turned it on a monthly basis through 3Q?

Deepak Ahuja

I think we would prefer not to give specific monthly numbers. But I think George gave you a good sense earlier, that given our continued store openings, the visibility of the car and the recent awards that the car has won, certainly seem a good up tick recently.

Aaron Chew - Maxim

For my follow-up, wondering if you guys can offer any further insights beyond what was mentioned on the website with regard to the lawsuit. I'm sure it's a sensitive matter, so there's only so much you guys can say. But maybe some general thoughts on timing, whether damages are being sought, and what implications you guys think maybe to your store strategy, if they were to win?

Elon Musk

We got to be a little bit cautious about commenting on ongoing lawsuits and any other perspective, a traditional process. But we feel, we're quite optimistic with respect to our legal position. We really feel strong that we're in the right, and it's worth noting that thus far no injunctions have been issued. So we really feel optimistic that we will prevail in these cases, and that we are strongly on the side of what the law intended to occur. So other than that there are no great insights, except to say that we feel really optimistic about where we are.

Operator

Our next question is from Carter Driscoll of Capstone Investments.

Carter Driscoll - Capstone Investments

First question is, trying to get a little closer to an ASP figure, could you talk about what maybe the average option package size or range has been so far for the signature series? And how you see that potentially playing out as your mix shift changes, so that the similar range is a percentage of the base model, your expectations there? And then, I have follow-up.

Elon Musk

Right now we're still working our way through this industry, which is quite a heavy optioned version of the car. We've been surprised by the level of interest in the performance version of the car till that takes us a bit by a surprise and actually causes us some slight challenges in meeting the production ramp for components that are specific to the performance version of the car, I feel which will surprise us by how many people were interested in that.

And looking ahead, our option mix still looks like it's quite rich actually. So it's really looking, I'd say, maybe a little better than anticipated, but usually that could change. We don't have a crystal ball as to say how things could go long-term, but it's been better than I expected in terms of the number of things, that we were interested in having on the car. So George or Deepak, if you want to add to that.

George Blankenship

I agree with that. One of the option that has been most favorable, we see if that the performance, and the signature version of the car as Elon said was highly optioned and there really weren't a lot of options on that car, specifically because of the signature car, as we moved into the general production reservations.

Very happy with performance and from the other options, that we weren't sure how well they've been received. And they've been received very, very well. So I agree with Elon that we're slightly ahead of where we thought we would be with options.

Elon Musk

With that said, a lot of customers really ask for more options. So we will try to roll out a few more extras that people could buy, that like and maybe a few of the people can retroactively add to their car.

Carter Driscoll - Capstone Investments

My quick follow-up is I think you had talked just a few weeks ago about potentially reaching cash flow, breaking it by end of November. I think in your written commentary, you think it's closer to the end of the year. Could you talk about whether that was expediting cost, supplier issues, some net reservations changing, could you talk about what changed that date by approximately a month, and you're confident that it will December now?

George Blankenship

Well, we haven't really changed the date by a month. So I think we actually expect that to occur as we previously expected. But the things can shift around by a week or two, but not really much more than that. And I think actually it will be as expected.

Elon Musk

Just to reinforce that point Carter that there is no change in that sense.

Operator

Our next question is from John Lovallo of Merrill Lynch.

John Lovallo - Merrill Lynch

First question is if you think about the Daimler contract and just kind of the shift in timing, I mean can you just talk about maybe what were the drivers of that shift?

Deepak Ahuja

It was really not something significant. We were sorting out some of the technical specification to the milestones. And that was required for us to make sure we were doing revenue recognition, correctly. And those issues are all pretty much behind us.

Elon Musk

Essentially the project is proceeding actually at the expected pace. We're just being conservative about the revenue recognition. And we want to make sure. We don't run the risk of the restatement, not with respect to the Daimler contract. So operationally, it's proceeding as expected, but which is being a little bit on the conservative side, and otherwise our revenue would actually be higher than what we currently stated.

George Blankenship

That's a very good point that operationally the program is proceeding very well and has been.

Elon Musk

Actually our revenue would be higher if we've been less conservative in the recognition of our revenue.

John Lovallo - Merrill Lynch

And then if I could just follow-up with a maybe a quick kind of housekeeping question here. I was under the impression that the interest expense would flip to closer to \$2 million, once production began on the Model S, am I incorrect on that or was there's some kind of change?

Deepak Ahuja

It's little more in Q4 and Q3. We were still capitalizing since a lot of our assets were under construction during the quarter.

Operator

Our next question is from Elaine Kwei of Jefferies.

Elaine Kwei - Jefferies

I think most of my questions have been touched on, but just a big picture one, what's the eventual vision for the Supercharger network. Is this going to be expanded to the 60 kilowatt and the 40 kilowatt, and possibly even the future mainstream mass-market Gen III vehicle or what's the thought there?

Elon Musk

It would actually apply to the 85 kilowatt version automatically, that's just being included. And then for, a couple of thousand dollars, you can get the Supercharger hardware added to the 60 kilowatt version. We're not currently

planning or adding it to the 40 kilowatt version, because we see that as, the customer buying that is really buying it because they don't really make long business trips. So it tends to be a more of a car that you'd want to use for travel just within a greater metropolitan area.

We do expect to have a Supercharger network to be used by the particularly by the Model X, and by our third-generation vehicle. But we're thinking that if you want to have a nominal range, at least on the order of 200 miles of range, at 55 miles an hour, for the Supercharger network. And that's basic a basic version. But we do expect that the vast majority of cost that we produce going forward to have access to the Supercharger network, like said apart from the very lowest version of the model which is for those who are just almost going to take long distance trip.

Elaine Kwei - Jefferies

And just one follow-up. Will there still be any deliveries of new Roadsters in 4Q or is that done now? And had you planned to also sell the pre-owned Roadster or was that one of your recent development? And do you see yourself also dominating that re-sell market for any future Model S or Model X or other vehicle?

Elon Musk

Yes. There will be a few more Roadsters. These are just ones in terms of Europe and Asia. So there's not very many left, so it's not going to be a huge number. But in terms of, used Roadsters, yes, we do expect to do a decent business in used Roadsters, and doing the same with Model S and Model X. And I think that's going to be interesting revenue source for us in the future. George, is there anything you'd like add to that?

George Blankenship

All of the Roadsters that are remaining that are new are in Europe and Asia, and right-hand-driving is basically done except for a couple of demos. We're putting together international program that actually brings back Roadsters. And this will translate to Model S, in the future Model X.

So that we actually manage that process and so we control the value of that secondary part of the market. We think that's very important. So we actually have a staff that's dedicated to specifically managing used Roadsters now in North America, based out of California. So we think it's an important part of business opportunity for us going forward.

Operator

Our next is from Ben Schuman of Pacific Crest.

Ben Schuman - Pacific Crest

Am I, right understanding the half way to 25% gross margin expectation as sort of a snapshot exiting Q4? And if so can you give us some color on what the overall gross margin could be in Q4?

Deepak Ahuja

We want to be sure we are beating our numbers here. So we want to be careful. But it should be relatively close. And I think we want to just help give the sense that we'd be around the right track, and as Elon said looking beyond, we're on track to get to 25%.

Ben Schuman - Pacific Crest

And then you hired all the employees you need in terms of manufacturing to get to the 20,000 unit run rate, and how long is it typically taking you guys to get new factory employees around that?

Elon Musk

We've hired almost all of the people that we need for the 20,000 unit a year to ramp. And typically it's 54 on board and trained is around two to three week process. So I think really things are in place to get to that run rate in four or five weeks.

Operator

Our next question is from Dan Galves of Deutsche Bank.

Dan Galves - Deutsche Bank

Just wanted to dig into this comment on that absent cost and efficiencies. You're now at production rate capable of generating positive operating cash flow. Just trying to keep it simple, your operating expenses excluding stock-based comp are running above \$350 million annualized right now. If we used \$25,000 gross margin per unit, you would need to do about \$14,000 units per year to breakeven on that.

I'm just wondering if you can give me any additional color on what's involved in that or what I'm missing in that calculation. And then if you could talk about your cash breakeven point going forward as ASP is likely will come down at some point, but the gross margin it looks like will continue to improve from current levels, but if you could give us any more color on that calculation?

Elon Musk

Dan, the other elements of the balance sheet items that effect including how our inventories and ASPs get managed and our reservation is balance. So when we look at that on a combined basis, from an operational perspective, we're comfortable with the message that we have provided in the letter.

Dan Galves - Deutsche Bank

So that includes some more working balance sheet changes

Elon Musk

Right.

Dan Galves - Deutsche Bank

And could you give us an update on where you stand in terms of homologation of the vehicle in Europe. When you expect that to launch and what's the ability of people in Europe to make reservations currently and how many have?

Elon Musk

We've made huge progress on homologation. We designed the Model S from the beginning to meet the European and American specs. And in fact, specs in Japan and Asia, as much as possible. So we believe that some of those specs were usually exclusive. And in fact, we have two, Model S us with German plates currently driving around that we completed as part of our European media launch recently.

So we believe that there is very little to get the European spec in homologation ready for production. We could start production of those units sooner than kind of the March, April timeframe next year. But there is not really a need to do that, since we can fully install our production with North American demand, rather than increase the complication of managing all those cars in Europe. And we want to stay focused in North America just for a few more months, before we start ship cars over to Europe, and then Asia shortly thereafter.

Dan Galves - Deutsche Bank

And are people able to make reservations in Europe now.

Elon Musk

Yes, absolutely.

Deepak Ahuja

As George can add some more insight there, clearly we've seen an up tick with recent activities and so we've just begun the launch of the Model S marketing activities in Europe. So overall we have probably around 15%, 20% of our reservations in Europe.

Operator

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

Andrea James - Dougherty & Company

If I make some assumption that how many people you're calling to lock in, I think I calculated that the cancellation rate for lock in's is about 1 and 10, and so is that about right? And how does that compare to what you're expecting?

Deepak Ahuja

I think our cancellations rates for people that we reach out to confirm a booking is in the 10% to 15% range. It depends on how old some of these were. So you're in right ballpark. Fair Andrea? George anything else you may want to add.

George Blankenship

No it's just that the number was completely expected to be where it is, and is expected to go down as we get into Q1.

Elon Musk

Actually, you said that the rate of cancellations for people that have locked in, the cancellation for people that have actually confirmed that their options is extremely low. There are very few people that cancel once they've decided what their options are going to be. The cancellation seems to occur before they've decided, but that's where the 10% to 15% cancellation occurs.

Andrea James - Dougherty & Company

And looking at your September 25 communication on growth reservations and then I look at what you're saying today, it looks like you've booked up 300 new reservations in the last five days of Q3. Is that sound all right? And I think that's where you want to be and it sounds like you got there already?

George Blankenship]

I would say it's a bit of rounding there. So it's in the ball park, but there is a bit of rounding.

Operator

Our next question is from Michael Lew of Needham.

Michael Lew - Needham

With regard to the Superchargers, has it yet been a factor or do you expect it to be an influencing factor in the general reservationists population and whether or not they choose, let's say, an 85 kilowatt hour model versus a 40 kilowatt hour vehicle?

Elon Musk

Yes, I think so. I think there are lot of reasons to take the higher range car, assuming the performance elements, it gets little faster, its acceleration is very high top speed, that the warranty is a little bit better, but I think the more you travel long distance with Supercharger, the fact that you'll able to travel full free anywhere in America long distance, I think is pretty appealing.

And you'll probably just open the Superchargers system open to the public and I really think it's a wonderful experience when you use it. I actually drove with my all five of my kids in the Model S with luggage in the front trunk. So fully loaded, all the way from LA to San Francisco and it was really a great road trip.

And with no hitches, and when we had stopped for meal, or the restroom by the time we came back the, care was ready to go, so I think it's really exceeded my expectations actually for what I was hoping it would be and how well it would function. So I am really excited about it and I think as people use it, it's really going to open their open eyes, as to what an electric car could be like, and just not having to go to a gas station, and invest in fumes and pay how much money for gas. Tesla's free long distance, powered by sunlight, I think is quite a revolution, I think.

Michael Lew - Needham

Have they also drove incremental demand or increase from OEMs like for powertrain agreements, just given its high rate or fast charging capabilities?

Elon Musk

Well, our partners with Mercedes and Skoda, both of them been more interested in shorter range vehicles rather than tackling long range problem.

It was certainly something we would be happy to give access to. We have to give an access to it, but I think it needs just a bit of a larger battery pack than they're currently specking for car.

Michael Lew - Needham

Where there new increase since the unveiling of the Superchargers and OEM select new platforms in the future? I mean let's put it this way, 10 minutes is a lot faster than and we hate hours?

Elon Musk

Yes, true. Surprisingly there haven't been a lot of increases on that front. Maybe it's just taking time to sink in. And I think it's currently in the main mind frame that it's more of a greater metropolitan area travel vehicle, in the other case the RAV4 and the V Class Mercedes. And I think once they see how customers are adopting and using the Supercharger network, their interest will peak. I really don't think people realize just how cool it is. It's just works. It's one of those things where it's even better than it sounds. It's better than the marketing.

Michael Lew - Needham

One last question, you've highlighted the role of word of mouth, the roll it's played in driving reservations. Could you give us a sense or gage of what percentage or what number of net adds in 3Q where by word of mouth, if there's a figure out there? I don't know if you've tracked it that way?

Elon Musk

It's essentially almost all our word of mouth or media, because it's the advertising that we do.

Michael Lew - Needham

I guess, I meant store walk-ins or shall we walk in to see design centre?

Elon Musk

Sure. George, would you probably answer the question.

George Blankenship

We don't have the exact numbers on which ones were customer references, because some of them are multiple customer references, some of them come to the stores specifically, because they went to dinner the night before

with somebody who's received a car and then they come in to the store. They get more information and make a reservation.

We don't track it specifically by customer. But when we start to look at geographic areas where we have the most delivered cars, those areas are really starting to escalate very quickly in reservations for more cars. So we don't have it down to a specific percentage or number. It's just when you look at the overall picture, you can see that where we have the most cars delivered, reservations are escalating significantly.

Michael Lew - Needham

So on that note, I guess, you would also apply towards cancellation rates. So it's fair to say in the areas where there are fewer vehicles on the road, you'll probably experience more cancellations. Is that the way to look at it?

George Blankenship

I haven't really tracked it that way. I haven't really backed into it that way. So couldn't really quantify that that for you.

Elon Musk

I mean, that's probably true anecdotally. Just given the delivered amount of car is incredibly good. So I've not accounted anyone, who said that they tried the car and then didn't like it. It tends to be very opposite.

Operator

Our last question is from Ben Kallo of Robert W. Baird.

Ben Kallo - Robert W. Baird

I was wondering, we get a lot of questions about the 25% gross margin. How much of battery cost reductions are built into it, you mean that target if any? And then how do you view any cost reductions on the battery side as upside to the gross margin?

Elon Musk

Just separate out the battery, there is the sale of cost and then there is the battery balancing system cost. So we really not moving any significant production and sale cost into getting through 25% gross margin. There are bunch of reductions associated with the pack cost.

But we have really good insight into those and anecdotal path to get those done in a fairly short period of time, so not really worried about battery pack

cost at all. In fact, I think just overall we've got a really good handle on getting to 25%. I've very high confidence of getting there. My goal is to exceed 25%, and not just stop at that point.

Operator

Thank you. I would now like to turn the conference back over to Jeff Evanson for closing remarks.

Jeff Evanson

And thank you everyone for joining us this morning. We look forward to seeing in the coming weeks, either on the factory tour tomorrow in Chicago at R.W. Baird's Industrial Conference or at other events through the remainder of the year. Goodbye everyone.