

Hi, thanks for taking my questions and congratulations on the rocket launch.

Elon Musk

Thank you.

Andrea James

So just quickly can you help me get to a free cash flow figure, looks like you can do \$1.5 billion in CapEx, but what's going to be the operating cash flow to offset that?

Deepak Ahuja

Yes, we will have clearly significant - Deepak here, hi Andrea.

Andrea James

Hi.

Deepak Ahuja

We would have significant positive operating cash flow, obviously as our business --our volume gross and our gross margin continues to improve. We'll also have some cash used on our direct leasing program. Our expectation is that we will establish shop via warehouse line for leasing cars and that will continue to grow and fund the big portion for leasing funding required. So overall, we feel pretty comfortable where we are in terms of our 2015 look from a cash burn perspective.

Andrea James

So maybe about \$1 billion is that about inline of cash burn?

Deepak Ahuja

Should be less than that.

Andrea James

Okay.

Deepak Ahuja

Yes, considering that we will have a lease warehouse line which continues to expand.

Andrea James

Got it. And so then another point, it looks like you expanded your residual value guarantee into extra markets late last year. And then I saw last week you're giving and recharging, home charging to focus in China. So I guess my question is it looks like you have really pretty good demand, global wait times increases, so why continue to give incentives to buy the cars if demand is so high?

Deepak Ahuja

Sorry Straubel.

JB Straubel

Well, I think fundamentally in China, we want to make sure we are not creating any hurdles or issues that create a negative customer experience. And charging installation given the varied regulations and challenges there has been a difficult customer experience and they want to overcome that by providing [indiscernible].

Elon Musk

Yes, but this is also something that's considered standard in China, just like buying an BMW i3 or Elite something that considers the standard things. So we're just matching what competitors do. But this whole China thing has been blown way out of portion. We didn't execute people well on China last year, but it didn't really matter or people couldn't quite get that, like it's not like the all these extra cars we could have produced and it's only we'd had bunch more customers in China, we could have [indiscernible] those cars.

We have production constraint. So I wish we weren't but we were. So look forward to getting to demand constrain in the future. Essentially, it didn't matter whether we, meaning to the company as a whole, whether we saw a lot of cars in China or a small number of cars in China, [indiscernible] couple of cars to U.S. or Europe as in China. So it wasn't a high priority for the company, because it wasn't a constraining factor. Now obviously, in the long-term we do want to succeed in China and make sure we're doing a good job. And I think just like the rest of the world, China wants to have the best products and we think the Model S is the best car in world and that's indicated by a multiple outside assessment. I am pretty sure that people in China want the best car in the world. So that's something we got to make sure, we take that right foundation for future growth. But it was essentially irrelevant to last year.

That's an important point. And the biggest issue which we're still fighting to address is this perception that is as difficult to charge your car in China. This is false it is not difficult to charge your car in China. Unfortunately, this

sounds kind of brain dead but our sales team was telling people that it was difficult to charge in China. Even though this is not true like that is pretty silly. And so I put the guy who was in charge of the supercharger rollout in China, is doing an awesome job, an engineer basically, he's not a sales person, in charge of China to make sure that charging is super easy and excellent. He's not a marketing guys or sales guy, he is like, he is an engineer and he's an operations guys and he's going to make sure that people have, where customers are trying to have a fantastic experience and then just like in other countries those customers become our sales force and the product sales grow by word of mouth.

Andrea James

So, is this a company philosophy because it seems like you are putting engineers in charge of customer service even globally, with Jerome, I mean is customer service an engineering problem?

Elon Musk

I think if you have got people that are good at creative problem solving and they will – they'll be good at creative problem solving. I tend to view I guess it is my own bias that most of things, since I am an engineer I can view things as an engineering problem. But not everything is an engineering problem, but I think it is like you got to design the system and sometimes those systems are in the form of a car or discharging or it is way that you communicate with prospective customers it just create a problem solving [indiscernible] always as a creative problem solver who just gives back getting it right and that is what we are doing. And I am confident that soon, by the end of this year that will be in really good shape in China and yes I'm pretty optimistic about it. I don't think that's some sort of unique issue in China and if you look at sales, sales, our sales in Hong Kong our sales in Hong Kong are excellence. But we don't have that misconception of charging issue in Hong Kong. And everybody lives in apartment building as well, so it is not like it is super easy to get local charging. . And so I'm confident that just as we've seen high demand in every other part of the world that we'll see it in China as well.

Andrea James

And just to the point that thank you for the clarity on China. Just to my point on the residual value guarantee. Is that something that you plan on keeping and why keep it and what are your thoughts about that?

Elon Musk

Yes. That's a good question. I've actually debated like should we keep it or shouldn't we keep it because it is moot. The residual value guarantee matches what other premium sedans. And see after three year time period but our actual residual values are substantially above that, so never actually matters. And we are not like paying up residual value guarantee are actually volumes especially about that so never actually matters, we are not going to paying out residual value guarantees because the car is worth more than the residual value and - this kind of messes up our accounting because we have to treat it like a pseudo-lease. On the other hand, if we withdrew it, then does that mean - would people take that as a lack of confidence in our product and if they might, they might misconstrue it as such. So even though it's moot and it doesn't really matter, it's just there to provide confidence to the customers. Yes, so I think, we'll probably keep it even though it makes our financials look worse than they are really are.

So, I think it's really important, because we get some criticism about GAAP versus non-GAAP, as though like when we do non-GAAP we're actually trying to trick people, and so thinking something is better than it is. But actually it's not true, I don't - I think that the way the accounting rules currently work don't give a correct picture, we're trying to give a more correct picture of non-GAAP, not a less correct picture. The difference between -- from our gross margin GAAP and non-GAAP were basically the same.

So, when we look for revenue the difference between the GAAP and non-GAAP it's just - it comes down to just two things, this residual value guarantee, where we - as we just talked about, it moot . But because of the pseudo-lease we have to recognize the revenue overtime, even though we got the cash immediately. So our cash flow with non-GAAP is the accurate representation of cash flow, which is what really matters.

And yes, so and then even in non-GAAP, we don't - for leases that we do internally, they actually aren't even covered in non-GAAP.

JB Straubel

And we didn't receive the full cash up front. So it's aligned with our cash flow.

Elon Musk

Exactly, exactly it is aligned to cash flow.

JB Straubel

Right, whereas in some other auto company the moment they sell the car to a dealership, we understand they recognizable full revenue, but even though

the financing entity might lease that car and so they don't have the cash flows, but they have a GAAP revenue. So in some sense our non-GAAP revenue is pretty clean and it aligns up well with our cash flow.

Elon Musk

Yes, this is really important, because we're into one point to emphasize, because like - because there might be -- are we perhaps exaggerating our revenues relative to how other car companies may represent their revenues. And what Deepak just said is a very good point. What the other car companies will do is they will sell the cars to the dealer groups, but then they will then turn around and refinance those same cars. So they are sending it through the laundromat, it is basically what they're doing.

In our case, since we are not sending it through laundromat, it's much, actually more correct. Because if we do a lease it's all internal and we're not trying to sort of send it through some third-party where actually the risk is still assumed by the parent car company.

So yes, and then even for leases that we do ourselves, we can securitize those leases whenever we want. So, we can take those leases, fund them and put them into a securitization program or just get a warehouse loan to recover the capital. The reason we're using our existing capital is just basically common sense, because we've got a big bank balance that's earning a 0.1% or basically nothing, actually minus whatever the inflation rate is. And so, it makes more sense for us to put that capital to work with consumer leases and current 2% to 3% that's basically what it amounts to, but whenever we want to recover that capital we can do so through warehouse balance securitization. Yes.

JB Straubel

Thank you for taking my questions.

Deepak Ahuja

Yes so financials are better than they appear, not worse. That's really is the key point.

Operator

Thank you. Our next question comes from Brian Johnson with Barclays. Your line is open.

Brian Johnson

Yes, good evening. I wanted to explore a bit where you see the trajectory of CapEx and OpEx. You gave some guidance for next year, but as we kind of think ahead to the Gigafactory and as we think ahead to the model -- the Gen 3 launch, how do you see those trends going over the next several years.

JB Straubel

We are going to spend staggering amounts of money on CapEx. I mean for a good reason and with the great ROI. And it's important to not look at the CapEx in isolation because like that CapEx obviously is being done for reason in order to capture substantial future revenue flow. I am just saying the back-of-the-envelope -- if you make certain assumptions I emphasize these are just certain assumptions. I'm not saying they are true although they will occur, but I bet that they do occur, personally, that is my personal opinion. I mean if you take this year's revenue around \$6 billion or thereabout and if we are able to maintain a 30% growth rate for ten years added to your 10% profitability number and have 20PE, our market cap would be basically the same as Apple today. Now that's going to require a bit - on the order of \$700 billion#. Obviously, getting [indiscernible] acquire some significant CapEx.

But I'm hopeful that we can do this without any significant dilution to the company. So maybe minor dilution, but nothing serious.

Brian Johnson

And how about in terms of operating expense and do you have a target for reported margins versus kind of thinking about your remarks in the second press conference at [indiscernible] where margins would be if you'd stop growing? Is there a difference between the margins on the non-GAAP basis we'd actually see, versus what they would be if you weren't making those kind of investments?

Deepak Ahuja

You mean profit margin as opposed to gross margin?

Brian Johnson

Yes, yes the operating margin.

Deepak Ahuja

Yes, I mean, we could easily get to 10%, 15%. I probably if we - say somewhere between 10% or 15%. Because some of that gross margins that

this year will probably, by the end of the year be somewhere around 30%. Then if 20 of those points go to sort of fixed cost and R&D and what not and then at least 10 leftover for profitability. And we are expecting to be non-GAAP profitable.

Elon Musk

And we have been non-GAAP profitable for two years now 2013# and 2014.

Deepak Ahuja

Yes I'd like to emphasize that doesn't mean [indiscernible] profitable, it means really profitable. It difficult to pass your question Brian in terms of separating OpEx between the fast growing company like Tesla versus steady-state, clearly we want to invest in the future, but we want to do it efficiently and we are going to focus on being efficient with our OpEx fundamentally this year.

Elon Musk

That is a key thing. The simple math of headcount requires this. We're basically little over 10,000 people aiming for somewhere over 55,000 cars this year. Just get to 0.5 million cars a year if we do not improve our productivity per person, we would need 100,000 people. I am not sure we would really park. So clearly there need to be dramatic improvement in productivity which are underway.

Brian Johnson

Right, and so when you said 10% was that 10% whilst still growing to the millions of cars target you talked about in 2025, or that's kind of 10% when you get to that millions of cars target?

Elon Musk

Yes I think it's important we're actually to be able to maintain 10% profitability in spite of nutty growth, because you just run out of way to spend money. It is good to become like Apple. They're just running out of way to spend money. They spend money like it is water over there and they still can't spend enough of it?

JB Straubel

I think for us we are a single vehicle platform company at this point for our engineering expenses have their ebbs and flows. So that has an impact, but as we grow will become a portfolio of vehicle platforms even with nutty growth we can get to a very good operating margin.

Elon Musk

Yes, it's sort of planned like we are doing this -- and it's mentioned in the letter, but there is massive infrastructure expansion going on like really massive like setting up service centers worldwide, creating an ubiquitous Supercharger network worldwide, just across all these countries growing with customs and the unique elements for each country. We are massively increasing this sort of scope and scale of Tesla in order to lay a foundation for future growth.

Brian Johnson

Okay, great. And just final question more for Deepak. When does CapEx slow into depreciation and gross margin, what kind of timeframes for the CapEx in terms of depreciable life spends, are you assuming on things like Gigafactory, factory drilling and so forth?

Deepak Ahuja

So to answer your first question, when assets are put to use for production and delivery of cars, that's when depreciation kicks off, so a lot of our spend this year is on production capacity expansion and Model X tooling. Those the assets saw depreciation when Model X starts producing. The Gigafactory assets clearly will go into -- would be depreciated when we start producing cells that are being used for production and it depends on our revenue growth.

And the life of -- the depreciation life depends on the kind of asset. It can vary from five years for tooling to longer if its equipment, and if it's facility then it could be for 15 to 30 years. We follow the generally accepted principles there in our expected life of use to come up with those figures.

Brian Johnson

Okay, great, okay, thanks.

Operator

Thank you. Our next question comes from Adam Jonas with Morgan Stanley. Your line is open.

Adam Jonas

Good evening, everybody. First back China, do you have any concerns about your ability to pursue business in China on terms that protect your interests? What I mean is like, if you look at the German manufacturers, they don't seem to have any problem with 50/50 JV structures or with bit local partners

and not having control on selling through franchisers. Are you able to - are those terms that you are comfortable doing business with in China?

Deepak Ahuja

Well, I think we definitely going to - want to have local manufacturing or some amount of local R&D as well in the future in China. It's not going to make a ton of sense for the long term to be building a huge number of cars in California and shipping them to China. But right now we're still at the early stages, so it's difficult to say exactly what happens in the future. I mean, our goals in the short-term in China is just very straightforward which is just to build out our service and Supercharger infrastructure and just get the basic foundational elements there, and we are not going through dealers as we are not going through dealers anywhere in the world. So our activities in China currently are housed and Tesla-owned and it sort of depends on what the evolving landscape is in China as to whether, where, and how a JV would have to be setup .

Adam Jonas

Okay, Elon just on the patents, it's been eight months since you opened up the patents for competitors to use, any takers of any significant technology? I'm not aware of any. Are or you surprised there have not been more, and is this just a function of just -- kind of is it hubris and pride, or your competitors they just don't have the kind of intellectual capabilities or software engineering depth to kind of contextualize what you have to offer.

Elon Musk

I'm quite sure that there will be -- and that actually manufacturers are currently [indiscernible] use our patents, but just important to remember the design cycle from the point of which you can use intellectual property, you've got sort of incorporate the design, that design's got to -- you've got to do detailed engineering and design, you got to tool things out, and then you've got to go to production. So probably, the first time you see companies -- anyone using our IP would be three years after we announced.

Adam Jonas

Okay. And then finally, Elon just you mentioned, I think you said staggering amounts or obscene - amounts of money on CapEx. Companies that usually have those kinds of spending ambitions at this point in the growth phase also have a pretty developed relationship with capital markets to help fund that growth, and yourself an Enterprise has been -- I think done that quite successfully. Any heuristics, you can kind of leave us with as people kind of contemplate more cash burn being necessary to fund great things and great

projects that will ultimately payoff. But any kind of rule of the thumb of minimum levels of liquidity or the kind of things you'd look at to decide whether you need to kind of refill the capital tank? Thanks.

Elon Musk

We don't have any plans for raising money right now. And I think we can get to that sort of crazy level that I described earlier with really minimal dilution. It's really going to be very much -- overwhelming amount of that would come from operating cash flow. So yes, I feel generally pretty good about getting to that level with minor to moderate dilution. The only reason we'd raise money is -- and I'm not saying we really don't have any plans to raise money, but the only reason I could mention we would do it is just to have a bigger cash cushion that will be in the -- in case there's a big downturn in the economy or something like that.

Adam Jonas

Thanks very much.

Elon Musk

Okay.

Operator

Thank you, our next question comes from John Lovallo with Bank of America. Your line is open.

John Lovallo

Hey guys, thanks for taking the call. First question is your cash burn continues to be pretty aggressive here. So the question is, if demand is strong as you guys are saying, and really the issue is on the supply side, why wouldn't you raise prices in all regions to at least set off - offset the FX headwinds. And the reason I'm asking this is, if you get more demand than you can handle, this won't hurt deliveries, it should also clearly benefit cash flow and investors and it will also support the residual values for your current owners. So it sounds like a win-win all around, so can you just address that please?

Elon Musk

Well, I actually kind of think our car is expensive as it is. It's really not a cheap car. For a huge number of our customers, it's the most expensive car that they have ever bought, and they didn't think they would ever buy a car that costs \$100,000. So I'm reluctant to raise that price as we start running

into fundamental affordability limits. As it is, we are expecting to be significantly - have significant positive cash flow in the latter half of the year.

So yes, I mean, there'll be sort of a short-term debt, but it's clearly quite positive at the end of the year, and then going into 2016, even more so.

Deepak Ahuja

And I think that's completely linked to a major product launch. Especially in the automotive industry, you have to invest in the CapEx for manufacturing capacity and then the cash flow comes through when you launch.

Elon Musk

Yes.

John Lovallo

Just to be clear on that, when you say you're going to be cash flow positive by the end of the year, that's after CapEx?

Deepak Ahuja

That's our - yes, that is expectation and I think we got to have focus on the long-term, while this is a short-term issue in terms of timing of CapEx versus revenue.

Elon Musk

But yes, - but to answer your question, yes, even in the face of significant CapEx, we expect to be cash flow positive in Q4.

John Lovallo

In Q4? Okay.

JB Straubel

I mean, that will happen somewhere in late Q3, but it's - it will be reflected most clearly in Q4.

Deepak Ahuja

And it's linked with the volume production of Model X.

JB Straubel

Yes, exactly, we've got to get Model X. It could give - we have plenty of CapEx related to Model X.

John Lovallo

Yes.

JB Straubel

We have also invested in a bunch of things that actually, our volume numbers that are really better associated with Model III, so that \$0.25 billion dollar paint shop upgrade is intended to be able to handle 10,000 cars a week.

John Lovallo

Okay, thanks. And then the next question is - there has been a lot of discussions about persistent drivetrain issues, and we've heard everything from different customers from persistent humming noises to complete failures, so the question is, I mean how pervasive is the drivetrain issue? What is the cost to replace a drivetrain? And I was a little surprised to see that the warranty reserves would not move up quarter-over-quarter?

Elon Musk

Yes. I think there is a lot of noise on the forums, but it's not quite as bad as people make -- for most people, they don't experience any drivetrain issue at all. There was a period of time, basically for a month or two about a year ago where -- it was kind of getting into the weeds, but the application of grease on the spline of the motor was incorrect, and that caused the spline to wear out and stripped the spline on the drag in on the motor. So that particularly affected sports, and unfortunately it happened to coincide with a - when a whole batch of cars headed for Norway. So unfortunately -- it disproportionately affected the Norwegian customers. We've taken great pains to try to address. Essentially what it amounted to fix that issue for example is just to you've got a full drive unit and then send it to get remanufactured where we replaced the rotor and...

JB Straubel

And maybe to the warranty, this is JB, to the warranty reserve question, we've actually improved quite a bit a lot in our efficiency at repairing the drive unit. So it might be swapped for a given customer, but that unit doesn't get trashed, it gets repaired. And the elements that need to get repaired are increasingly narrow, and we are really targeting them quite directly, even the rotor can be repaired at this point.

Elon Musk

Yes. And there was a differential clunk that was causing a differential clunk which can actually be fixed with a two-part shim in the service center, so we were able to figure out the service center fix to address that without even dropping the drive unit.

JB Straubel

Okay. All of the new units being built today, of course get all these fixes proactively as we learn the new product improves.

John Lovallo

That's helpful. And then finally, Elon, I just wanted to ask you about your comment about GAAP profitability not being reached until 2020, and I know you guys say that the non-GAAP ways – is way to think about it, and I'm not disagreeing with that here, but what I am suggesting is that if there's not going to be GAAP profitability until 2020, and we kind of walk down from The Street's consensus non-GAAP number to a GAAP number by adding back stock comp, adding back non-cash interest expense, and making an assumption on the leasing, my estimate would suggest that Street estimates are 30% to 60% too high because the GAAP component of that non-GAAP number would need to be eliminated. So if you guys could just help me think about if that math is incorrect, and more importantly, what is the path to profitability for Tesla?

Elon Musk

Sure, I think people read too much into my comment because I was asked, when do I think Tesla will have full-year GAAP profitability, and sort of then you are going to the sort of residual varying [indiscernible] question like do we continue doing that or do we not continue doing that, because the half of the cars are financed, right. So, that basically chops our revenue in half in a lot of cases.

John Lovallo

Leasing as well.

Elon Musk

I mean leasing, so if leasing and residual value guarantee of half the cars that would basically [indiscernible] affect revenue recognition, and then is it – if it is a quarter basis or is it a full year. That's why I said it's probably 2020, it's the full year, and it's GAAP. That's - what that actually means is

that Tesla's free cash flow is incredible in 2020, it's able to overwhelm even the non-GAAP stuff. So, I think people didn't understand that what I said was extremely optimistic, not a pessimistic statement.

John Lovallo

Okay, thank you guys.

Operator

Our next question comes from the Ben Kallo with Robert W. Baird. Your line is open.

Ben Kallo

Hi, thank you for taking my question. A couple of different ones, first kind of a lower level one, as far as the X goes in timing, could you just talk about -- I know you reiterated deliveries in Q3 and just your confidence level around that, and then maybe one of the questions we get a lot is if we extend that to the Gen 3 and your 2017 timeframe, can you just talk about what work you're doing there and how confident you're getting to that timeline?

Elon Musk

Yes, it's fair criticism, implied criticism. --This feels like this paradox here is like we're sort of halfway there at any given point, but really at this - the X design is done. So, it's just a question of tooling and supply chain at this point, and then making sure as we do the ramp up on X that our quality is excellent. It doesn't [indiscernible], obviously we want to make sure we have a really great experience, we don't have them - have any sort of issues or problems, but it is really - just like I said, it is just tooling and supply chain, and we're trying to make that go as fast as possible. So, we're highly confident of delivering our first customer cars this summer and then spooling up to significant volume in Q4.

Now with respect to Model 3, we definitely don't want the delays that affected the X to affect the Model 3, and we're really - we are being quite contentious about this, and I mean there are things that we could do with the Model 3 platform that are really adventurous but with the schedule risk. So what we're going to do is we're going to have something that is going to be an amazing car, but it won't be the most adventurous version of the Model 3 to begin with, but we will then have the more sort of different version of the Model 3 on the Model 3 platform following the initial version, so that we can stay on track for Model 3.

We got a quite adventurous with the X, and we don't want - we don't want to be - that would be too risky given the Gigafactory and everything sort of has to happen on time. We're not going to go super crazy with the design of the initial version of the 3. So, I do feel confident that we can make that happen in the second half of 2017.

Ben Kallo

Great.

Elon Musk

As long as we stick to those principles.

Ben Kallo

Great. And question on innovation and releasing new features, what did you learned from the dual motor as far as the timing of new releases and how that impacts demand and how you do that going forward. I know you guys are constantly innovating on the car, but does that disrupt demand at all and how do you do that that you are now specifically during Model years, big advances.

Elon Musk

This is a problem that we struggle with. It's really tricky because -- we basically have one car with variation. This would be much easier if we had different cars. It's tough for us to announce [indiscernible] in advance that there is going to be some new version of the car because then we are like worried about starting near term sales. A lot of people wait to see what it is. So it is a real tricky thing and then we also, it is difficult to forecast the exact demand since we haven't [indiscernible] the car. We really have to guess, like how many people want P85D, we have no idea. It turns out a lot, okay, really a lot. And then we say, oh, we have too much demand for the P85D and now we got to figure out how to do that and then how many people are going to pick the next gen [seat] [ph] as it turns out also a lot. So we couldn't make [enough seats]. So I mean I'd love to figure out how to [indiscernible] about this in the future. But, yes.

Deepak Ahuja

I think one thing in particular that we are working toward is to be sure that we are really ready to meet the production demands at a much higher percentage mix if we announce something new, or an innovative new feature. And that is definitely I think a lesson we learned.

Elon Musk

Yes, agreed.

Ben Kallo

And my last one is on the storage side of the business. Can you just talk about any developments there? We have heard some utilities looking for RFPs for utility scale projects. Are you guys at a position where you can start bidding on those RFPs or entering those RFPs, just give some update there and thanks guys.

Elon Musk

[Stationary] [ph] storage?

Ben Kallo

Yes, [stationary] [ph] storage.

Elon Musk

Yes, [indiscernible] we are bidding on a lot of RFPs already. Do you want to [indiscernible]?

JB Straubel

I don't want to go into super amount of detail on this but you are correct. Of course there's a lot of interest and a lot of utilities are working in this space. And we are talking to almost all of them. It's early stage stuff and a lot of these projects are very far out, since the procurement cycle for utilities is so long. But this is a business that certainly is gaining an increasing amount of our attention.

Elon Musk

Yes, but we're going to do -- we're going to unveil the Tesla home battery [indiscernible] consumer battery that will be for use in and people's houses or businesses, fairly soon. We have the design done and it should start going into production probably about six months or so. We probably got a date to have sort of product unveiling, it's probably in the next month or two. It's really great. I'm really excited about it.

Ben Kallo

Thanks guys.

Operator

Our next question comes from Ryan Brinkman with JP Morgan. Your line is open.

Ryan Brinkman

Hi, thanks for taking my question. Can you give us a sense for what you think your gross margin would have been in the quarter if not for the 1,400 deliveries that were pushed into 1Q?

Elon Musk

Actually [indiscernible] I mean there were a bunch of things that coincided, because we had to expedite - [indiscernible] expedited shipping [indiscernible] make those numbers, we had massive [indiscernible] shipping. And then the euro was also falling. If those things hadn't occurred I mean we're going to be somewhere in the order of 28%, yeah, somewhere around there.

Ryan Brinkman

Okay, that's helpful. And then just last question, is there any additional color you can give us on just the cadence of sales and production throughout 2015 - beyond - I'm curious why the deliveries are expected to be flat in 1Q versus 4Q given that they should benefit from the push out of those holiday deliveries and why production is forecast down sequentially too given that the full year has [guided] [ph] up so much and sort of beyond 1Q, what can you tell us in terms of when you expect to the implied inflection to occur in 2Q or 3Q what the catalyst is for that, whether it's a capacity bump up again or Model X or something like that. Thanks.

Elon Musk

Yes. And just clarify, [indiscernible] estimated 28%, that's 28% excluding ZEV credit. So if you added ZEV credit on top of that it would be, I don't know, 29% or 30% something like that. So yes, in terms of the production from Q4 to Q1 being relatively flat, there is a couple of reasons that, they're actually two fewer weeks of production in Q1 versus Q4. One is because we had to give - we wanted [indiscernible] and certainly so gave people the first week of January off, because they have been working for Christmas and New Year's and Thanksgiving in a lot of cases. So they just, just to give people a break we didn't operate the factory in first week of January. And also [indiscernible] and then there is also one fewer production week in Q1. So that's basically minus two weeks.

And then, in Q1 we're focused on productivity improvement and making a groundwork for higher volume in the remainder of the year. But obviously if

you do the math, it doesn't mean there is going to be a very big scale up as you get towards the end of the year.

Deepak Ahuja

And we had over 10,000 orders one hand, so it's not a demand issue that we're delivering [indiscernible] number, get a lot of cars in transit as we are again, adjusting our global mix of deliveries.

Ryan Brinkman

Okay, all right.

Elon Musk

A lot of cars in transits [indiscernible].

Ryan Brinkman

Thank you.

Operator

Our next question comes from Patrick Archambault with Goldman Sachs. Your line is open.

Patrick Archambault

Thank you, yes, good evening. I just wanted to follow-up actually just on some of the comments you made about being less adventures for the X relative - for the Model 3, excuse me, relative to the X and playing it a little bit safer. Can you just give us a sense of what some of these characteristics and features are that you might have at one point been considering for the initial version that maybe put in place for a later model upgrade.

Elon Musk

We can't tell you that. I mean - so yes, this is - yes, with the X we had the Falcon Wing door, which is a first sort of double X rating gullwing door basically we called Falcon Wing door. Getting that right and making sure it works really well and [indiscernible] mechanic, but is a fundamental improvement in utility and aesthetics for cars is extremely difficult. And as a reason, I'll [do] [ph] when I've done this. And then the second row on the Model X is like it is a second row is [indiscernible] of sculptural beauty they're amazing. They are the nicest second row seats you've ever seen in any car ever. That actually might have been harder than the door. And there was some other things about the X that people don't know about yet.

But those who went to driving schedule [indiscernible] second row seat and the door. So then going to Model 3, we want to - and I think we want to have particularly in super high volume. It's something that [indiscernible] that for this feature we lose a year of production. That's - it would make more sense just go with something that we know people are going to love, that's going to be incredibly beautiful and functional and an amazing car. And then innovate in more, I don't know, [indiscernible] directions on that platform with future iterations where we are not - we can then put aside any schedule and volume concern.

Patrick Archambault

Understood, certainly looking forward to seeing the X. Have you guys said when - is there going to be any sort of advanced - sort of showing of it at any auto shows or anything some of the more bench prototype ahead of the launch that we should be looking forward to?

Elon Musk

Because there are these sort of different features that I mentioned [indiscernible] we're not going to show it until gets delivered.

Patrick Archambault

Interesting, okay, okay. Switching gears a little bit back on China, just on orders, I understand that the deliveries have been significantly impacted by a number of the issues that you've described but how have orders been trending in China? Especially now that you've made some replacements, on the management side, you seem to have a solution well in hand that's being implemented to address some of the concerns whether they were justified or not. How have you seen kind of the Model S order book track, pre and sort of post those issues?

Elon Musk

Well, [Tom's] [ph] only have been in charge for a short period of time, but - the trend is positive already. So I think [indiscernible] improving every week. And it's some of the like elementary things that we were missing before like maps and directions - so the car didn't have maps and directions in China which was important. So now it does, and we don't have like onboard [indiscernible] working which we will have soon, so there is a lot of functionality that's just getting out [indiscernible], pretty helpful. So yes, the trend is positive. I don't have any significant concerns about it right now.

Patrick Archambault

I mean it had been - some had reported that orders had been coming in somewhere in the neighborhood of a 100 a day and - which all obviously point to a pretty good annual run rate and is that sort of at least the order of magnitude that you're trending at and that you can get back to in the shorter-term?

Elon Musk

The problem last year was that we had a whole bunch of speculators that were basically trying to buy [indiscernible] the cars and resell them at a higher price, which was not something we allow. So it gave like an inflated sense of demand in the beginning, it wasn't real.

Deepak Ahuja

Yeah. I don't think we were at 100 a day at any time.

Elon Musk

Yes.

Deepak Ahuja

Even [indiscernible] 50,000 plus car shipped in China alone, [indiscernible] any annualized rate. I don't know what the source is.

Patrick Archambault

Okay, that's helpful color though. Last one for me is just more of an accounting clarification. I think in one of the pages you talk about direct leasing, impacting, I guess reducing, sorry, both non-GAAP and GAAP profitability. I think we understand why it reduces GAAP profitability. We've actually addressed that a lot in this call, but non-GAAP I was just wondering why that would be impacted.

Deepak Ahuja

Yes, because we still hold the title for the car and we haven't collected full cash on the car. And so we don't recognize direct leased cars even in our non-GAAP financials, pretty simple.

Patrick Archambault

Understood. Okay. Thanks a lot guys.

Elon Musk

Yes, but as I mentioned that we can always free up that cash by securitizing our internal leases and/or by just getting warehouse loan facility. So [indiscernible] yes, [indiscernible], I guess what I would consider our real revenue is actually higher than our non-GAAP revenue, because of the internal [leases] [ph].

Patrick Archambault

Got it. Okay, great. Thanks a lot guys.

Elon Musk

And I mean the vehicles delivered to customers is really the key metrics that I'd focus on. We don't give people a car unless they've paid for it. Paid for it somehow and the average price for car is pretty obvious, so that's really the key number.

Patrick Archambault

Okay. Thank you.

Elon Musk

Yes.

Operator

Next question comes from Rod Lache of Deutsche Bank. Your line is open.

Rod Lache

Hi, everybody. I apologize if this has been answered. I'd some phone problems here, but I was hoping you might be able to help us with what you see as the run rate of sales for Model S right now and that bridge to the 55,000. Should we look at the 40,000 deliveries or maybe it's 46,000 if you annualize what you did and add in the delayed Model D? Is that a run rate, and then to get from here to 55,000, where is China now? What does it need to be and what actually are you including for the Model X this year?

Elon Musk

Yes. So [indiscernible] even if our sales in China were zero this year, zero, I'm still confident we could do the 55,000 cars, [they might be zero] [ph]. So as far as what the mix is between S and X, it's really tricky, I wish I could tell you with accuracy, but it really depends on how the production ramp goes with the X when we start up this summer. And even small changes in that ramp can have quite a dramatic effect on X production.

Deepak Ahuja

So, actually for the calendar year because it's late.

Elon Musk

Exactly.

Deepak Ahuja

Long-term makes no difference.

Elon Musk

Yes, exactly. If we are producing and I would say 800 Xs a week, and if - several weeks it's like several thousand cars. So it's just really - it's really tricky to predict it from - I can much easier predict like next year. Assuming people like the car, that's where you start to see, yes, I don't know, 40,000, 30,000 40,000 at least. Maybe, 50,000, let's call it 30,000 to 50,000 Xs next year.

Rod Lache

Okay. And clearly up until now as you pointed out, you've been able to hit all these numbers without any advertising and marketing.

Elon Musk

And no endorsements, and no discounts.

Rod Lache

Right, to get...

Elon Musk

We haven't paid anyone to pretend that they like our car.

Rod Lache

Right, and...

Elon Musk

Which is a very important point.

Rod Lache

And no franchise dealers and you know all these things that you know - people had said that you might need to do, you've been able to do it without any of them. But I'm just curious about kind of longer-term to get to the volume objectives that you are looking for this year and beyond, is - are all of those in your view achievable while avoiding the franchise dealer model, while holding back on advertising and marketing and while in some cases even raising prices for example, in Europe to adjust for currency or any of those impediments to the demand objectives that you have and would you modify the strategy in any way to achieve these volume numbers?

Elon Musk

I think we're going to be okay on the demand side for this year. I mean maybe something changes next year but I think we'll be okay and I don't think we're going to have to do a bunch of advertising or [indiscernible] with the dealers or anything like that this year and or discount the cars or anything like that. So if I - I do want to emphasize that whenever you feel like a celebrity or some prominent person driving our car they all paid full retail. There was no discount. We didn't give them the car, they are buying the car and they are driving because they really believe in the car, not because someone paid them to pretend that they do. So we may give them credit for the people [indiscernible] brought the car. So yes, I think we - I do have a secret weapon on the demand side that will probably start to deploy later this year for demand generation. We'll see how that goes. It isn't totally necessary but I think and it could be pretty interesting, I could [indiscernible] dealers.

Rod Lache

Okay. And just one last question I had, you mentioned in your letter that the margin was pressured half by revenue and half by cost factors. The FX part of this was pretty clear but there was a comment in there about deferred autopilot revenue, could you just explain, maybe just elaborate a little bit on what you meant actually in that description of the margin variance?

Deepak Ahuja

On that particular one, Rod, we announced several features that the autopilot functionality or hardware will deliver. Those features - although the hardware is in the car, some of them will get activated through software releases later this year. And so based on the [indiscernible] aspect of revenue for accounting we had to defer some of that revenue into 2015. And I think it's as simple as that. Yes.

Rod Lache

Okay. That variance versus the 28% original objective or is that versus - what was that comparison against?

Deepak Ahuja

That was, yes, it's part of that because we had to figure out the accounting for it, work through the whole thing and it - as we deferred a significant amount there that had an impact to our otherwise delivered car gross margins that would have been there.

Elon Musk

It's like another 0.5% or something like that.

Deepak Ahuja

Yes, that's right.

Elon Musk

Maybe 0.5% to 0.7% or something.

Deepak Ahuja

Yes.

Elon Musk

And - but most of that deferral will be taken care of this quarter with the software release next month which will add a bunch more functionality to the car. Right now, I'm really excited about the software release we have planned for next month. There is a bunch of features in it that are going to positively affect entire fleet and then of course we'll add more autopilot capability.

JB Straubel

That is simply exciting.

Elon Musk

Yes, it's going to be a really, really good release.

Rod Lache

Thank you.

Deepak Ahuja

Patrick, before we go to the next question, I just want to do a time check with Elon, we're coming up on hour mark, and we have several more questioners in the queue.

Elon Musk

Yes, we can keep running.

Deepak Ahuja

Okay, all right, Patrick.

Operator

Our next question comes from Dan Galves with Credit Suisse. Your line is open.

Dan Galves

Hi, thanks good evening. I just had a question on the delivery guidance, if you adjust that for in this additional in transit vehicles I am just trying to get a sense of whether you feel like that's your best guess on kind of your max production for 2015 because my sense coming to the year around a 1000 a week is you could produce a lot more than that. So I am just getting a sense of - what part of that is demand constraint and what part is production constraint?

Elon Musk

Well, I mean we are all going to try to do a little better than the 55 number. So we're saying 55 plus, but we're going to try do a little better than that. But it is - it's really dependent on how the X ramp goes that can have quite a - if it happens, okay, later, it's going to [indiscernible] that could affect the delivered number quite significantly, also when I say delivered, it's like we got to also factor in, it's like lots of cars in ships...

Deepak Ahuja

Correct, the gap between production and delivery time.

Elon Musk

Yes.

Deepak Ahuja

And then we need to consider there could be disruption during launch of X and so when you are looking at that broad number of 55,000 or

[indiscernible] there are things we need to consider through the year what happens.

Elon Musk

Yes, this 55 is like a number we're pretty comfortable with achieving on deliveries and, yes, we are [indiscernible] making a conscious decision to focus on productivity this quarter, not just on ramping production, [indiscernible] production stability, in order to get that efficiency, like when we need to be building a firm foundation before future growth. And if we just in helter-skelter, production ramp, trying to just grow production numbers is really hard to get productivity and that kind of fixes the foundational elements. So the conscious decision this quarter to [indiscernible] improve our core productivity. I mean running at [indiscernible].

Our Fremont plan is pretty big and it's hard to park. So we need to just get these productivity improvements in place so we can grow our production volume without proportionately growing headcount.

Dan Galves

That makes a lot of sense. And then just one kind of housekeeping question, you put the chart at the beginning of the shareholder letter with revenue guidance for 2015. Is there anything in there for trade-in sales, for used car sales? And do you have any sort of sense of kind of what type of drag on gross margin sale of trade-ins will be?

Deepak Ahuja

There's a small amount of that and we are just getting into that business now and our goal is certainly not to make that same kind of money on our used cars.

Elon Musk

Yeah, used cars also affect the capital - [we don't have] [ph] any capital in there really, [indiscernible] turnaround capitals [indiscernible], so it's actually like the used car - your margin is actually - it's on a ROI basis is extremely good.

Deepak Ahuja

Right, when the dealers do make lot more gross margin on used cars than new cars, and that's not our intention but the ROI is still really good for us.

Elon Musk

Yes. But we're going to separate that out so that we can see new car gross margin versus used car, service and other things.

Deepak Ahuja

Which brings up a good point that as we said at - towards the end of our shareholder letter, starting for 2015 financials we are going to show our income statement slightly differently, the automotive revenues and cost of goods sold is truly new-car sales and then we have services and other sections of the income statement that has all these other things including trade-ins and....

Elon Musk

Yes, so we will break it out so you can see clearly like what's the new Model S gross margin, what's the used, what's other things, yeah.

Dan Galves

Yes, it's really appreciated, thanks.

Elon Musk

All right.

Operator

Our next question comes from Trip Chowdhry with Global Equity Research, your line is open.

Trip Chowdhry

Thank you. Two quick questions. We see a lot of similarity between Apple and Tesla, both cos - both companies go for perfection, performance and design. But we don't see Apple making a \$30 iPhone. I was just wondering instead of focusing on Model 3, and we just focused on say Model S, say Model X, but made them even better, you just focus on increasing the range to say 400 miles, 450 miles, you already have the roadster which is at 400 miles now, I think that would make Tesla very differentiated.

Elon Musk

Not quite 400 miles. The Roadster is sort of more like 360, but close to 400 miles, yes, with the upgrade. Capable of doing LA, San Francisco, but yes. And so, yes, I mean the goal of Tesla, from the beginning, has always been to accelerate the advent of sustainable transport, and to make electric cars happen much faster than what was [indiscernible]. So in order to do that we

have to make lots of cars and we need to make them a heck a lot more affordable than S and X are today. Even with the Model 3 though, I mean it is sort of a mass market premium car. It's not – it's still premium, but it's mass market premium, at 35K, it's not a, yes, it's above average car.

JB Straubel

Yes, I think it's also not an either/or decision. We definitely will keep making S and X better and we will keep improving that platform really as much as a technology rollout. So we're going in both of those directions.

Trip Chowdhry

Perfect, thank you.

Operator

Our next question comes from Andrew Fung with CLSA. Your line is open.

Andrew Fung

Thanks for taking my question. So the Gigafactory seems to be making some good progress in terms of construction. Could you provide an update on how the development of the battery supply chain is progressing and perhaps any notable challenges or perhaps positive surprises that have occurred with that process.

JB Straubel

Sure, I can take that one, this is JB. So far we've been pretty pleased with the supply chain development. We're spending a lot of time visiting more and more of the supply chain partners and understanding and learning about all those different markets. That learning is progressing quickly and I think we're getting a much more clear picture of exactly how we will achieve the cost reductions we've talked about. I don't want to go into too many specifics on exactly sort of what we've learned in which places. But I would say there is a lot - maybe more incremental positivity on some of the commodities and some of the ways I think we can secure and procure pricing on some of the larger commodity prices that go into the cell.

Andrew Fung

Great, and any sense of when you guys may announce additional either suppliers or partners for the Gigafactory.

JB Straubel

We want to be a little bit cautious about doing that too soon. There is obviously a lot of work going on and discussion with all of those partners, but I think we just - we want to be careful to make sure that all the agreements and decision on the - where that partnership is headed is very clear. So we will wait until, it's really done and ready to announce.

Andrew Fung

Great, thank you.

Operator

Next question comes from Andrea James with Dougherty & Company. Your line is open.

Andrea James

Thanks for taking my follow-up, why did you guys promise the Roadster 3.0 this year?

Elon Musk

It's just a long-standing obligation we have, it's not something that economically is a win for us, but it's just an obligation to our early adopters of Tesla; we said we'd provide a significant upgrade to the roadster and that's what we're doing. And I think - it's okay, I mean it's not a big, big thing one way or the other, slightly economically just [unfavorable to] [ph] Tesla.

Andrea James

And so if I read through on the range communication on the Roadster 3.0 and I just apply that sort of same range gain to the Model S I guess I get a 350 mile to 400 mile range Model S by say 2017. Is that the right, I mean, is that - is all the gains there translatable?

Elon Musk

It's not simple to put an exact time on it, if you, like 2017, probably not in 2017, at some point, yes. I don't know if that - whether that's 2017, but it's not 2017 but it might be say 2019 or 2020 or something like that. [Indiscernible] We can make the Model S go 400 miles today, if we wanted to by just increasing the pack size.

Andrea James

Great. I mean at the same - I meant at the same cost, same pack cost say give \$22,000 pack, will be 400 mile range the next couple of years, but seems that is a bit too aggressive.

Elon Musk

Next couple years is a bit too aggressive. If you go five years out, that might be the case. That's not a prediction, that's just speculation. But I'd say it's not two years but it might be five years.

Andrea James

Okay, and then just I feel like we should just generally ask your thoughts on oil, although it's a pretty broad question. So may be just general thoughts on oil, but then more pointedly what it does to the residual value of the cars and then also maybe the corresponding offset with lifting the value of ZEV credits as more gas guzzling cars are sold, I don't know, there you go.

Elon Musk

Well, as far as oil is concerned, I mean, I'm not an expert on oil business. But obviously fracking has massively increased the available oil reserves worldwide, fracking [indiscernible] more expensive than standard oil drilling so there is sort of a cost of doing it that sets a floor on fracking. It's really anyone's guess as to what happens with oil prices long-term. Demand is certainly going to increase, sort of like how well the supply go to match that. But for sure oil companies are going to be scaling back their investments in new oil fields massively with low price for oil today. So expect that - I'd expect that as...

Andrea James

But as it translates to the impacts on demand for your vehicles, and then also the residual value of those vehicles.

Elon Musk

It certainly has some effects but I wouldn't say - it's not a dramatic effect. I mean it's, I call it a moderate effect. And I'm not - it is not changing any of my projections [indiscernible].