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ATLANTIC CAPITAL MARKETS

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Tesla - On the charge

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Tesla, Inc. or as it was formerly known Tesla Motors Inc, is an American electric vehicle and clean energy company based in California. The company specialises most notably in electric vehicle manufacturing but do also produce other electricity solutions such as battery energy storage from home to grid and through its SolarCity subsidiary solar panel and solar roof tile manufacturing. With the global shift to focus more on environmentally friendly solutions and carbon footprints Tesla are certainly in prime position to benefit....But is the recent rally in the share price justifiable based on the numbers so far? Is this share simply full of hype and a bubble ready to go pop? Or simply the beginning of something much much bigger.

A Brief History

Tesla was founded in July 2003, by the engineers Martin Eberhard and Marc Tarpenning, under the name of Tesla Motors. Interestingly Elon Musk was responsible for 98% of the initial funding and served as Chairman of the Board however wasn't the first CEO. He appointed Martin Eberhard to be the first CEO. Then in its 2004 Series A funding Tesla Motors was joined by Elon Musk, J. B. Straubel and Ian Wright, all of whom are retroactively allowed to call themselves co-founders of the company.

Tesla operates multiple production and assembly plants, such as: its main vehicle manufacturing facility at Tesla Factory in Fremont, California; Giga Nevada near Reno, Nevada; Giga New York in Buffalo, New York; and Giga Shanghai in Shanghai, China.

Products

As of 2019, Tesla Cars product range included the Model S, Model X, and Model 3 cars. It is accepting reservations for the Model Y, Roadster due for release this year, and the recently unveiled controversially styled Cybertruck. With all the hype and focus on the cars it is easy to forget that Tesla are not simply a car manufacturer but they also sell a range of environmentally friendly energy solutions for your home and business as well, these include the Powerwall, Powerpack, and Megapack batteries, solar panels and solar roof tiles.

The Powerwall:- Tesla Powerwall 2 is a solar battery for homes and small businesses that stores the sun's energy and delivers clean electricity when the sun isn't shining. The second edition Powerwall is a complete home energy solution. Powerwall 2 uses a built-in inverter to convert DC energy to the AC energy required in our homes. This lowers cost and complexity.

The Powerpack:- The Powerpack is the company's utility-scale rechargeable battery, designed to store energy for off-grid and supplemental power systems, including large facilities and the electric grid. Like Powerwall, Tesla's battery for home and small business use, Powerpack is based on lithium ion battery technology but ultimately used for larger scale applications.

The Megapack batteries:- Released in 2019 the megapacks are a grid energy storage battery with a capacity of three megawatt hours designed for battery storage power station use. Megapacks significantly reduce the complexity of large-scale battery storage and provides an easy installation and connection process. Each Megapack comes from the factory fully-assembled with up to 3 megawatt hours (MWhs) of storage and 1.5 MW of inverter capacity, building on Powerpack's engineering with an AC interface and 60% increase in energy density to achieve significant cost and time savings compared to other battery systems and traditional fossil fuel power plants.

Solar roof:- Tesla and SolarCity developed a solar roof system that integrates the solar cells and modules inside the structure of the roof rather than just panels on a roof. The idea is to design something that looks just like normal roof tiles when installed buy actually each tile is a solar panel.

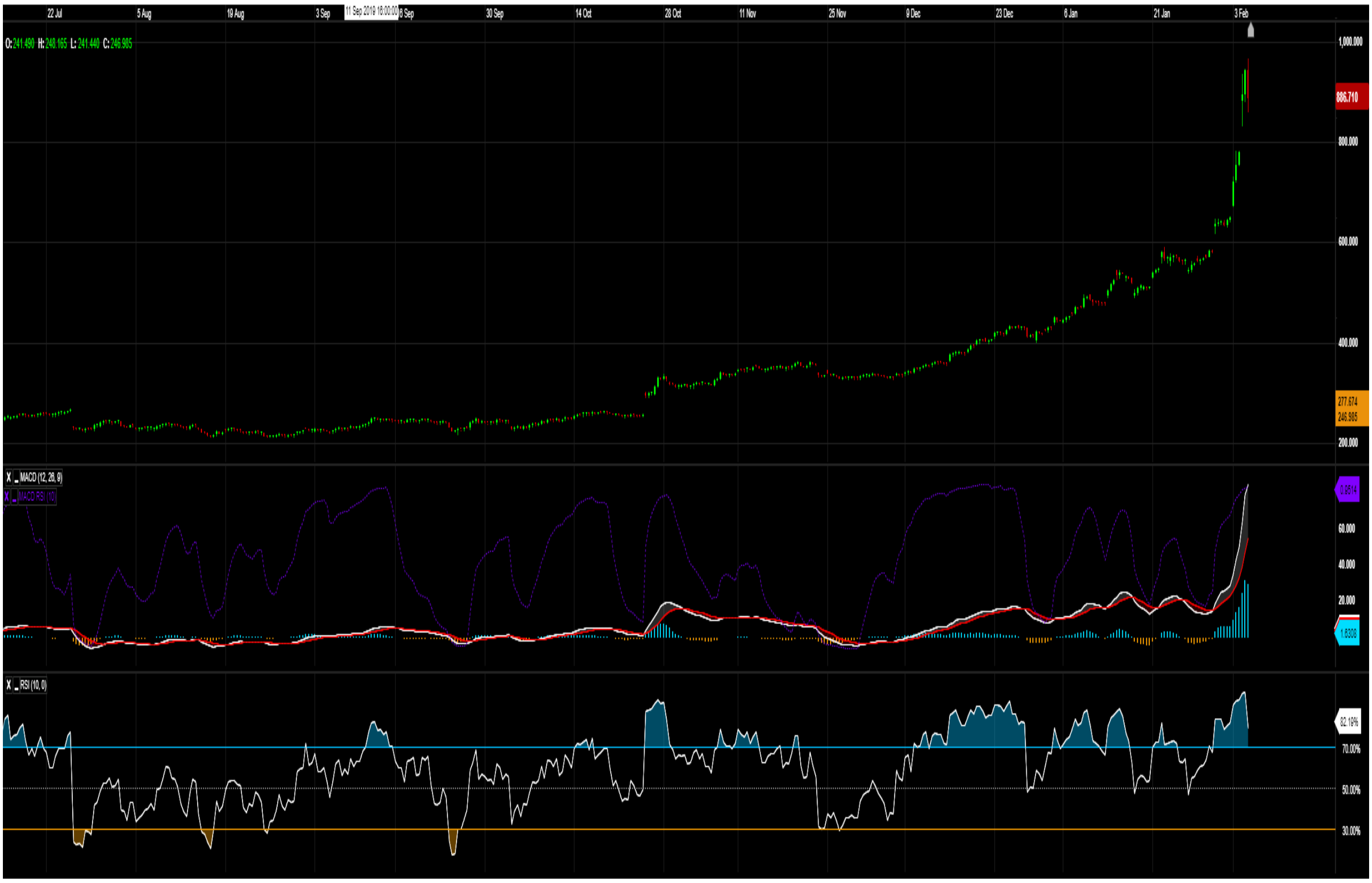
500th Supercharger station in Europe: a milestone in more ways than one

In December 2019 Tesla announced the opening of the 500th Supercharger station in Europe - a significant achievement that now includes more than 4700 individual Superchargers and gives owners the option to be able to travel across 24 countries. This really does give Tesla a huge footprint across Europe. When the first European station was opened in Norway in 2013 driving across multiple countries in a fully electric car was inconceivable and seen as a unique accomplishment. With the Supercharger network, long distance travel has become the new normal.

Key Fundamentals

Key Fundamentals	31-Dec-14	31-Dec-15	31-Dec-16	31-Dec-17	31-Dec-18
Revenue ($ m)	3198.36	4046.02	7000.13	11758.75	21461.27
Pre-Tax ($ m)	-284.64	-875.62	-746.35	-2209.03	-1004.74
EPS	-236.00¢	-693.00¢	-468.00¢	-1183.00¢	-572.00¢
PE	n/a	n/a	n/a	n/a	n/a
PEG	n/a	n/a	n/a	n/a	n/a
EPS Growth	n/a	n/a	n/a	n/a	n/a
Dividend Cover	n/a	n/a	n/a	n/a	n/a
Dividend Yield	n/a	n/a	n/a	n/a	n/a

Technical Chart



Fourth Quarter Update

The recent Full year earnings update was certainly well received with Tesla banging the drum on 2019 being a key turning point for the business. The firm showed strong organic demand for Model 3, returned to GAAP (generally accepted accounting principles) profitability in the second half of the year and generated $1.1B of free cash flow for the year. The firm achieved strong cash generation through persistent cost control across the business.

They have said “The pace of execution has also improved significantly, as we have incorporated many lessons learnt from launching the Model 3 in the United States. As a result, we were able to start Model 3 production in Gigafactory Shanghai in less than 10 months from breaking ground and have already begun the production ramp for Model Y in Fremont.”

The biggest shock (positive) was that this was accomplished without any spend on advertising. As more people drive our cars and as the industry rapidly validates electrification, interest in our products will continue to grow.

Financial Summary - Highlights

Revenue

In 2019, revenue growth was positively impacted by a strong increase in vehicle deliveries. Revenue growth was offset by higher lease mix, Model 3 becoming a larger part of this mix, introduction of the Standard Range trims of Model 3, and adjustments to vehicle pricing.

These changes have resulted in a reduction to the average selling price relative to 2018. The firm has said they do not expect average selling prices to change significantly in the near term, which means volume growth and revenue growth should correlate more closely this year. They have also stated

that the business is positioned to accelerate revenue growth further through increasing build rates in the Gigafactory Shanghai and Model Y production line in Fremont. These production increases will allow for higher total vehicle deliveries and associated revenue.

Profitability GAAP gross profit of $4.1B remained essentially flat in 2019 compared to 2018. Volume growth and successful cost reduction efforts were offset by normalization of the ASP, mix shift towards Model 3 and a higher lease mix.

Sequentially, GAAP gross margin remained relatively flat in Q4 compared to Q3, while they ramped Model 3 production at Gigafactory Shanghai. While there was an increase in operating expenses in Q4 (driven mostly by $72M of non-cash SBC expense related to one more 2018 CEO award operational milestone becoming probable), higher gross profit resulted in a 72bp sequential improvement of GAAP operating margin to 4.9% in Q4.

Cash

Quarter-end cash and cash equivalents increased by $930M QoQ to $6.3B, driven by positive quarterly free cash flow of $1.0B. Capital expenditures increased sequentially due to investments in Gigafactory Shanghai and Model Y preparations in Fremont.

Energy Business

Energy storage deployment reached an all-time high of 530 MWh in Q4, which included the first deployments of Megapack, our new commercial scale 3 MWh integrated storage system that is preassembled at Gigafactory Nevada as a single unit. Since the introduction of this product, the level of interest and orders from various global project developers and utilities has surpassed expectations.

In 2019, we deployed 1.65 GWh of energy storage, more than we deployed in all prior years combined. In Q4, we deployed 54 MW of solar, 26% more than in the prior quarter.

Where offered, subscription solar has grown significantly in Q4. With a monthly subscription that can generate income from the first month of usage, there is no reason not to have solar panels installed.

Solarglass Roof

In Q4, they continued to ramp both Solarglass Roof production as well as installations. In addition to Tesla installers they have also partnered with several roofing companies to support installations to fulfil demand for Solarglass Roof. After organizing several roofing company training days at our training homes in Fremont they have now demonstrated dramatically shorter installation times versus previous versions of this product. Solarglass tiles are made in our Gigafactory New York, and we are hiring hundreds of employees at this facility.

Year ahead outlook

Volume:- For full year 2020, vehicle deliveries should comfortably exceed 500,000 units. Due to ramp of Model 3 in Shanghai and Model Y in Fremont, production will likely outpace deliveries this year. Both solar and storage deployments should grow at least 50% in 2020.

Cash Flow:- We expect positive quarterly free cash flow going forward, with possible temporary exceptions, particularly around the launch and ramp of new products. We continue to believe our business has grown to the point of being self-funding.

Profitability:- We expect positive GAAP net income going forward, with possible temporary exceptions, particularly around the launch and ramp of new products. Continuous volume growth, capacity expansion, and cash generation remain the main focus.

Production:- Production ramp of Model Y in Fremont has begun, ahead of schedule. Model 3 production in Shanghai is continuing to ramp while Model Y production in Shanghai will begin in 2021. We are planning to produce limited volumes of Tesla Semi this year.

Summary. So, should I buy the Shares...?

In a single word at this stage I would say a resounding no,

Firstly, the share scream over bought on pretty much every technical indicator and have gone up nearly 4-fold since May 2019, Whilst a lot of positives came out of the figures about the year ahead they are not exactly stellar numbers. The devil is often in the detail and the devil is certainly there. Competition is growing from china and firms like NIO, as well as most car producers making electric cars, and what was well hidden in a very positive report is that sales growth has been slower.

The recent ramp up in share prices really started after the surprise of a positive EPS for the third quarter 2019 and then the fourth quarter also showed a profit although smaller.

Tesla has an incredibly lofty valuation indicating the market has already priced in very strong future sales growth and healthy margins, YoY revenue growth has shown a lack of consistency, and the past two quarters show signs that revenue growth may already be rolling over. Gross margins are declining as they have been moving downmarket to pick up more volume with their model 3.

Until very recently, Tesla was still raising more cash from selling its own shares and bonds to investors than from selling cars to customers so again not exactly a strong reason to buy. The lack of dividend also shows that there are no plans to return any consistent cash back to investors anytime soon. The share price needs to settle back and clarity sought on the year ahead. I think what we are witnessing at the moment is a classic short squeeze of epic proportions. What I mean by that is Tesla shares have been heavily shorted but as the share price has rallied hard it will force out these short sellers triggering a further run of buys to close the shorts. This in turn has pushed the shares even higher. The sector is also not exclusively owned by Tesla and competition will only increase over time.

Don't get caught up I the hype, the business has a lot to do to prove itself a stable and solid investment and with no dividend to satisfy the income buyers you are soley dependant on capital growth. There are plenty of others moving in this sector and regardless of the recent moves a pullback and consolidation is needed.

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