

**Action Summary – 9 May 2013**

Analyst Theodore R. O'Neill *is raising his rating to Buy from Hold raising his target to \$100 from \$38*

- Company announced 1Q13 results that were better than we expected by \$0.08
- However, the outlook for the company and management's execution of the business plan is far better than we expected
- As a result of the changes to the near-term results, the financial implications significantly lower the risk factors in our opinion and lead to a forecast that drives our price target to \$100
- Our revenue forecast for growth in 2014 goes from 19% to 57% and because of the increased revenue and earnings in 2014, we project the balance sheet will go from negative net cash of \$0.71 per share to positive \$1.29
- Tesla is clearly taking market share and if I were in Detroit I'd be very concerned if Tesla made an EV truck which it clearly could

Current share price: \$65.10	Market cap: \$7.6 billion	Non-GAAP 2014 P/E: 18	2013 EV/Sales: 2.0
Shares outstanding: 124 million	Insider ownership: 38%	Avg. trading volume: 2 million	Dividend: NA

**Macroeconomic context**

- Slow growth in U.S. GDP unlikely to affect 2013 revenue estimates. Worldwide slowdown could affect EU/Asia rollout.
- High fuel prices over the summer months are likely to help shares trade higher

**Estimates (non-GAAP EPS in dollars – GAAP Revenue in millions)**

Period	EPS	Revenue	Net Margin
1Q12A	(\$0.76)	\$30.2	(298%)
2Q12A	(\$0.89)	\$26.7	(396%)
3Q12A	(\$0.92)	\$50.1	(221%)
4Q12A	<u>(\$0.65)</u>	<u>\$306.3</u>	<u>(29.4%)</u>
FY12A	<u>(\$3.20)</u>	<u>\$413.3</u>	<u>(96%)</u>
1Q13A	\$0.13	\$561.8	2.0%
2Q13E	(\$0.23)	\$412.0	(8.2)%
3Q13E	\$0.20	\$612.0	3.2%
4Q13E	<u>\$0.45</u>	<u>\$663.0</u>	<u>7.8%</u>
FY13E	<u>\$0.55</u>	<u>\$2,249</u>	<u>2.1%</u>
1Q14E	\$0.70	\$767.0	10.7%
2Q14E	\$0.80	\$819.0	11.5%
3Q14E	\$1.05	\$921.0	13.6%
4Q14E	<u>\$1.22</u>	<u>\$1,024</u>	<u>14.3%</u>
FY14E	<u>\$3.76</u>	<u>\$3,531</u>	<u>12.7%</u>

Note: Calculation of full year data may not add up due to rounding. See our full model in the back of this report. Excel versions available.

**Cash balance (in millions)**

• 2012A	• \$221.0
• 2013E	• \$197.7
• 2014E	• \$560.8

**Debt (in millions)**

• 2012A	• \$452
• 2013E	• \$425
• 2014E	• \$425

Debt is owed to the Department of Energy

**EBITDA (in millions)**

• 2012A	• (\$366.5)
• 2013E	• \$89.7
• 2014E	• \$489.4

**Risks/Valuation**

- Share price appears to be rising on short covering hence it may be volatile near-term
- Company's revenue recognition model will be changing in 2Q13 making an unfavorable comparison with 1Q13
- Our \$100 target is derived using a modified dividend discount model, details of which can be found in this report

**Company description**

TSLA designs, develops, manufactures and sells high-performance fully electric vehicles and advanced electric vehicle powertrain components. Headquarters are in Palo Alto, CA.

Figure 1 – Tesla Motors - Trading snapshot



Source: BigCharts.marketwatch.com

#### ViewPoint

- 1) We were wrong in our initial assessment of the company's business and this affected the price target, which at the time was below the current stock price.
- 2) Results show TSLA is continuing to take market share
- 3) Everything points to accelerations of market share gains given:
  - a. There are now leasing opportunities (in some states but will likely grow)
  - b. It is now shipping to new markets in the EU and Asia where fuel prices and pollution issues respectively will likely only increase demand
  - c. It has a pipeline of new products that utilize the same Model S platform which is a proven winner by *Consumer Reports*
  - d. It has a better than world class resale value
- 4) Should Tesla decide to make an EV truck, which we believe it could, it would likely be a significant challenge to GM and Ford and set up a great pairs trade
- 5) We believe that consensus EPS estimates will rise throughout the next 2 years

Stock gapped up on positive preannouncement in April and company followed through with a good outlook

You could wait for a better entry point but The Model S could be the perfect car and the outlook for sales is better than people expect

#### Financial Analysis

We forecast cash balances growing and the company becoming net cash positive in 2014

The critical financial issue for investors is whether the company can reach profitability without diluting current investors. We run a comprehensive cash flow analysis that has an excellent track record of determining if a financing is needed; how much and in what time period. In our analysis, if the company reaches profitability in 2Q13, which is our call, it will be cash flow self-sufficient so long as it remains profitable which it appears it will. This will lead to a positive net cash balance by the end of 2014.

#### Forecasts

Growth will "slow" to 57% in 2014 but production volumes will be sufficient for margins to improve

We are forecasting higher growth for 2013 than 2014 but 2013 growth is compared to small numbers. We believe the company has supplier agreements in place that call for traditional cost savings to kick in as certain volume milestones are met and these savings contribute to improving gross profit margins. We have had to raise our expectation for 2014 and are likely at the very high end of the range of estimates. The margins are improving and we expect them to continue to improve as volumes grow and the company perfects its manufacturing plan.



## Tesla Motors, Inc.

TSLA-Buy-\$100 PT

We assume that a single investor owns all the stock. What is the discounted value of the earnings stream?

### Price Target

Our price target is derived using a modified dividend discount model. Intellectually we assume we just bought 100% of the outstanding stock and the earnings stream flows to a single investor. What is the value of that stream? We assume all the annual earnings are dividends, we grow them as shown in the model at the back of this report and then over the course of the next 10 years we scale the growth back until earnings growth matches GDP. We then discount those “dividends” at 14%. This model probably understates the tax benefits thus could be seen as understating the price target but offsetting this is that the model never shows a decline in earnings and thus we feel the two balance out. Changes we made to the DCF since our last report include: 1) higher earnings and; 2) we lowered the discount rate to 12% from 14% due to the expected improvement in the balance sheet and the clear acceleration of business.

### Quarterly Results

Tesla beat our GAAP 1Q13 expectations by \$0.08 this was due to better than expected revenue, lower expenses and higher other income partially offset by a lower gross margin rate (see our variance analysis in Figure 4. From a purely operational perspective, the company beat our estimates by \$0.2. The remaining \$0.6 beat was due to non-operating factors.

Figure 2 - Tesla Motors, Inc. - Income Statement

(\$ in thousands except per share)

December ending year	2010	2011	2012				2012	2013E				2013E	2014E				2014E
	Year	Year	Q1	Q2	Q3	Q4	Year	Q1	Q2E	Q3E	Q4E	Year	Q1E	Q2E	Q3E	Q4E	Year
Automotive sales	97,078	148,568	19,245	22,054	50,023	294,377	385,699	555,203	407,002	607,002	657,002	2,226,209	760,002	811,002	912,002	1,014,002	3,497,008
Development services	19,666	55,674	10,922	4,599	81	11,955	27,557	6,589	5,000	5,000	6,000	22,589	7,000	8,000	9,000	10,000	34,000
<b>Total revenue</b>	<b>\$116,744</b>	<b>\$204,242</b>	<b>\$30,167</b>	<b>\$26,653</b>	<b>\$50,104</b>	<b>\$306,332</b>	<b>\$413,256</b>	<b>\$561,792</b>	<b>\$412,002</b>	<b>\$612,002</b>	<b>\$663,002</b>	<b>\$2,248,798</b>	<b>\$767,002</b>	<b>\$819,002</b>	<b>\$921,002</b>	<b>\$1,024,002</b>	<b>\$3,531,008</b>
Growth	4%	75%	-38%	-54%	-13%	678%	102%	1762%	1446%	1121%	116%	444%	37%	99%	50%	54%	57%
Cost of auto sales	79,982	115,482	13,932	20,150	58,865	278,710	371,657	461,818	333,742	479,532	492,752	1,767,843	562,401	600,141	665,761	740,221	2,568,526
Cost of services	6,031	27,165	6,025	1,741	0	3,765	11,531	3,654	3,000	3,000	3,600	13,254	4,620	4,800	5,400	6,000	20,820
Cost of Goods	86,013	142,647	19,957	21,891	58,865	282,475	383,188	465,472	336,742	482,532	496,352	1,781,097	567,021	604,941	671,161	746,221	2,589,346
<b>Gross Profit</b>	<b>30,731</b>	<b>61,595</b>	<b>10,210</b>	<b>4,762</b>	<b>(8,761)</b>	<b>23,857</b>	<b>30,068</b>	<b>96,320</b>	<b>75,260</b>	<b>129,470</b>	<b>166,651</b>	<b>467,701</b>	<b>199,981</b>	<b>214,061</b>	<b>249,841</b>	<b>277,781</b>	<b>941,662</b>
<b>Gross Margin</b>	<b>26.3%</b>	<b>30.2%</b>	<b>33.8%</b>	<b>17.9%</b>	<b>-17.5%</b>	<b>7.8%</b>	<b>7.3%</b>	<b>17.1%</b>	<b>18.3%</b>	<b>21.2%</b>	<b>25.1%</b>	<b>20.8%</b>	<b>26.1%</b>	<b>26.1%</b>	<b>27.1%</b>	<b>27.1%</b>	<b>26.7%</b>
Research and development	\$92,996	\$208,982	\$68,391	\$74,854	\$61,901	\$68,832	\$273,978	\$54,859	\$59,000	\$59,000	\$60,000	\$232,859	\$61,000	\$62,000	\$64,000	\$65,000	\$252,000
% of total revenue	79.7%	102.3%	226.7%	280.8%	123.5%	22.5%	66.3%	9.8%	14.3%	9.6%	9.0%	10.4%	8.0%	7.6%	6.9%	6.3%	7.1%
SG&A	\$84,573	\$104,102	\$30,582	\$36,083	\$37,798	\$45,908	\$150,371	\$47,045	\$50,000	\$51,000	\$55,000	\$203,045	\$57,000	\$58,000	\$60,000	\$66,000	\$241,000
% of total revenue	72%	51%	101%	135%	75%	15%	36%	8%	12%	8%	8%	9%	7%	7%	7%	6%	7%
Total Operating Expenses	177,569	313,084	98,973	110,937	99,699	114,740	424,349	101,904	109,000	110,000	115,000	435,904	118,000	120,000	124,000	131,000	493,000
<b>Operating Income</b>	<b>(146,838)</b>	<b>(251,489)</b>	<b>(88,763)</b>	<b>(106,175)</b>	<b>(108,460)</b>	<b>(90,883)</b>	<b>(394,281)</b>	<b>(5,584)</b>	<b>(33,740)</b>	<b>19,470</b>	<b>51,651</b>	<b>31,797</b>	<b>81,981</b>	<b>94,061</b>	<b>125,841</b>	<b>146,781</b>	<b>448,662</b>
<b>Operating Margin</b>	<b>-125.8%</b>	<b>-123.1%</b>	<b>-294.2%</b>	<b>-398.4%</b>	<b>-216.5%</b>	<b>-29.7%</b>	<b>-95.4%</b>	<b>-1.0%</b>	<b>-8.2%</b>	<b>3.2%</b>	<b>7.8%</b>	<b>1.4%</b>	<b>10.7%</b>	<b>11.5%</b>	<b>13.7%</b>	<b>14.3%</b>	<b>12.7%</b>
Total Other Items	(7,317)	(2,433)	(1,051)	681	(2,228)	804	(1,794)	16,983	0	0	0	16,983	0	0	0	0	0
<b>Pre-Tax Income</b>	<b>(154,155)</b>	<b>(253,922)</b>	<b>(89,814)</b>	<b>(105,494)</b>	<b>(110,688)</b>	<b>(90,079)</b>	<b>(396,075)</b>	<b>11,399</b>	<b>(33,740)</b>	<b>19,470</b>	<b>51,651</b>	<b>48,780</b>	<b>81,981</b>	<b>94,061</b>	<b>125,841</b>	<b>146,781</b>	<b>448,662</b>
<b>Pre-Tax Margin</b>	<b>-132.0%</b>	<b>-124.3%</b>	<b>-297.7%</b>	<b>-395.8%</b>	<b>-220.9%</b>	<b>-29.4%</b>	<b>-95.8%</b>	<b>2.0%</b>	<b>-8.2%</b>	<b>3.2%</b>	<b>7.8%</b>	<b>2.2%</b>	<b>10.7%</b>	<b>11.5%</b>	<b>13.7%</b>	<b>14.3%</b>	<b>12.7%</b>
Taxes (benefit)	173	488	59	109	116	(147)	137	150	150	150	150	600	150	150	150	150	600
Tax Rate	-0.1%	-0.2%	-0.1%	-0.1%	-0.1%	0.2%	0.0%	1.3%	-0.4%	0.8%	0.3%	1.2%	0.2%	0.2%	0.1%	0.1%	0.1%
<b>Net Income (loss)</b>	<b>(154,328)</b>	<b>(254,410)</b>	<b>(89,873)</b>	<b>(105,603)</b>	<b>(110,804)</b>	<b>(89,932)</b>	<b>(396,212)</b>	<b>11,249</b>	<b>(33,890)</b>	<b>19,320</b>	<b>51,501</b>	<b>48,180</b>	<b>81,831</b>	<b>93,911</b>	<b>125,691</b>	<b>146,631</b>	<b>448,062</b>
<b>Net Margin</b>	<b>-132.2%</b>	<b>-124.6%</b>	<b>-297.9%</b>	<b>-396.2%</b>	<b>-221.1%</b>	<b>-29.4%</b>	<b>-95.9%</b>	<b>2.0%</b>	<b>-8.2%</b>	<b>3.2%</b>	<b>7.8%</b>	<b>2.1%</b>	<b>10.7%</b>	<b>11.5%</b>	<b>13.6%</b>	<b>14.3%</b>	<b>12.7%</b>
EPS, as reported	(3.04)	(2.53)	(0.86)	(1.00)	(1.05)	(0.79)	(3.69)	0.10	(0.27)	0.16	0.41	0.40	0.66	0.76	1.01	1.18	3.60
non-GAAP EPS	1.71	(2.17)	(0.76)	(0.89)	(0.92)	(0.65)	(3.20)	0.13	(0.23)	0.20	0.45	0.55	0.70	0.80	1.05	1.22	3.76
Diluted Shares Outstanding	50,718	100,389	104,784	105,242	105,556	113,763	107,349	114,712	124,250	124,260	124,270	121,873	124,280	124,290	124,300	124,310	124,295

Sources: Company reports and Litchfield Hills Research, LLC

**Figure 3 - Tesla Motors, Inc. - Balance Sheet**

(\$ in thousands except per share)

December ending year	FY2014E	FY2013E	FY2012	FY2011	FY2010	FY2009
Net cash per share	\$1.29	(\$2.00)	(\$2.16)	\$0.24		
<b>Balance sheet</b>						
<b>Current Assets</b>						
Cash and S.T.I.	\$560,822	\$197,760	\$220,984	\$303,803	\$173,155	\$69,627
Accounts receivable	100,000	75,000	26,842	9,539	6,710	3,488
Inventories	350,000	275,000	268,504	50,082	45,182	23,222
Other assets	<u>30,000</u>	<u>20,000</u>	<u>18,509</u>	<u>21,171</u>	<u>10,839</u>	<u>4,222</u>
<b>Total Current Assets</b>	<b>1,040,822</b>	<b>567,760</b>	<b>534,839</b>	<b>384,595</b>	<b>235,886</b>	<b>100,559</b>
Net PP&E	700,000	650,000	552,229	298,414	114,636	23,535
Other non-current assets	<u>30,000</u>	<u>30,000</u>	<u>27,122</u>	<u>30,439</u>	<u>35,560</u>	<u>6,330</u>
<b>Total Assets</b>	<b><u>\$1,770,822</u></b>	<b><u>\$1,247,760</u></b>	<b><u>\$1,114,190</u></b>	<b><u>\$713,448</u></b>	<b><u>\$386,082</u></b>	<b><u>\$130,424</u></b>
<b>Current Liabilities</b>						
Notes payable and CPLTD	\$500,000	\$400,000	\$343,180	\$88,250	\$49,896	\$15,086
Accounts payable + Acc. Exp.	25,000	100,000	138,817	91,761	30,755	40,580
Other current liabilities	<u>40,000</u>	<u>40,000</u>	<u>29,986</u>	<u>18,226</u>	<u>4,914</u>	<u>1,823</u>
<b>Total current liabilities</b>	<b>565,000</b>	<b>540,000</b>	<b>511,983</b>	<b>198,237</b>	<b>85,565</b>	<b>57,489</b>
Long Term Debt	425,000	425,000	452,337	276,251	71,828	0
Other non-current	<u>50,000</u>	<u>50,000</u>	<u>25,170</u>	<u>14,915</u>	<u>21,641</u>	<u>7,233</u>
<b>Total Liabilities</b>	<b>1,040,000</b>	<b>1,015,000</b>	<b>989,490</b>	<b>489,403</b>	<b>179,034</b>	<b>64,722</b>
<b>Stockholders' Equity</b>						
Preferred stock						
Total stockholders' equity	<u>730,822</u>	<u>232,760</u>	<u>124,700</u>	<u>224,045</u>	<u>207,048</u>	<u>65,702</u>
<b>Total Liabilities and equity</b>	<b><u>\$1,770,822</u></b>	<b><u>\$1,247,760</u></b>	<b><u>\$1,114,190</u></b>	<b><u>\$713,448</u></b>	<b><u>\$386,082</u></b>	<b><u>\$130,424</u></b>

Sources: Company reports and Litchfield Hills Research, LLC

<b>Exhibit 4 - Tesla Motors, Inc. - Quarterly Variance Analysis</b>			
	2013	2013	
<b>Income Statement</b>	<u>Q1E</u>	<u>Q1A</u>	<u>Better/(worse) than forecast</u>
Product revenue	528,000	555,203	27,203
Contract revenue	11,000	6,589	(4,411)
Total Revenue	\$539,000	\$561,792	22,792
Cost of products	432,960	461,818	(28,858)
Cost of contracts	7,260	3,654	3,606
Total cost of revenue	440,220	465,472	(25,252)
Total Gross Profit	98,780	96,320	(2,460)
Operating expenses:			
Research and development	\$58,507	\$54,859	3,648
SG&A	48,000	47,045	955
Amortization of intangibles & other	0	0	0
Total Expenses	106,507	101,904	4,603
Earnings (loss) from Operations	(7,727)	(5,584)	2,143
Total Other income/(expense)	10,000	16,983	6,983
Earnings before taxes	2,273	11,399	9,126
Tax expense/(benefit)	150	150	0
Net income	\$2,123	\$11,249	9,126
EPS	\$ 0.02	\$ 0.10	\$ 0.08
For First Call	\$ 0.06	\$ 0.13	\$ 0.07
Diluted common shares	114,000	114,712	(712)
Source: Company filings and Litchfield Hills Research, LLC			

**Disclosures:**

**Analyst Certification**

I Theodore R. O'Neill, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject company and the underlying securities. I further certify that I have not and will not be receiving direct or indirect compensation in exchange for expressing the specific recommendation(s) in this research report.

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## Tesla Motors, Inc.

## TSLA-Buy-\$100 PT

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