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Tesla remains a compelling short for 2018 (01-04-18)

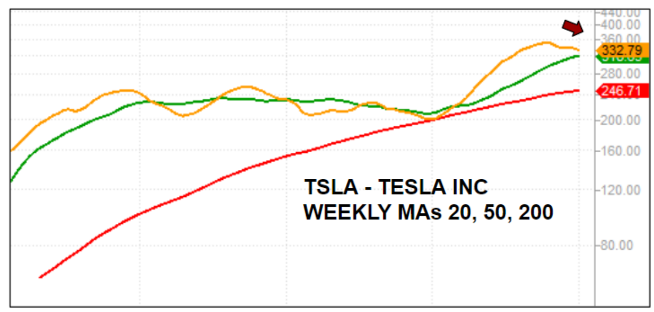
The gist: Tesla remains a compelling short for 2018. TSLA is below its 200 DMA and close to 20% down from its highs. We'll initiate a new moderate sized short position on a break of trend support.

Actions: Will establish a new mid-size short position in TSLA on a ½ ATR (average daily trading range) break of trend support, with risk to 2.5 ATR above the 200 day MA (currently at $331).

Tesla announced another major whiff in Model 3 deliveries for the fourth quarter versus already low expectations.

Last July, Elon Musk predicted a production volume of 20,000 Model 3 vehicles per month by December 2017.

Based on fourth quarter production averages, they did about three percent of that. Three percent!



The idea that Tesla will ramp its production to 500K cars per year anytime soon is beyond fantasy. It is pure fiction at this point. Problems are likely to worsen.

Yet TSLA's market cap remains above $50 billion, bigger than Ford's (who makes more than 6 million cars per year) and not far behind General Motors' (10 million).

Tesla remains a compelling short for 2018. Not only does the valuation make no sense, the evidence of missed targets continues to weigh heavily.

There is an increasing gap between optimism and reality based on hard numbers. Even if one takes Tesla's success as the base case, they will need to raise huge amounts of additional capital to sustain expansion costs. Every new product idea (e.g. pick-up truck) just adds to those costs.

In the current market environment, almost nothing goes down, unless there are severe problems. But TSLA's share price is close to 20% off its highs and below its 200 day MA.

We aren't willing to let a short position run to the upside with no stops, because there is no telling how far hype can push a story. But TSLA remains one of the most compelling cases of valuation detaching from reality we've ever seen. And the price action indicates a wake-up call.

TSLA is also interesting in terms of being a credit bellwether. The company has terrifying levels of cash burn. Interest rates are set to rise around the world in 2018, with easy credit drying up. This could cause a rerating of cash-burning companies with major borrowing needs.

We want the early positioning to build size on later, as the shares could fall 50% and still be overvalued. Were TSLA to become a takeover target, it would be a distress target with huge cash needs – likely scooped up at fire-sale levels 60% or 80% down from current value.