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Tesla Forced to Make Tough Choices as Debt Comes Due

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After losing roughly $7 billion in value in late September, Tesla's stock surged recently in response to Elon Musk's settlement with the U.S. Securities and Exchange Commission as well as promising Model 3 production numbers. However, many remain worried about Tesla's ability to pay its debts. Despite Musk's ability to sell equity investors on the future of Tesla, the company's serious debt problem has plummeted Tesla's bond price to a record low.

In its early years, Tesla took on a substantial amount of debt to achieve a sizeable advantage in the electric car space. Tesla was able to successfully seize control of the electric car market and became the most valuable car company in America. Nevertheless, Tesla has yet to turn a profit. Tesla's newest car, the Model 3, was intended to boost profitability as a result of mass production and relative affordability in comparison to the Model S.

Unfortunately, Tesla has failed to meet Model 3 delivery expectations. Meanwhile, more than $9 billion of Tesla's debt is scheduled to mature before 2025, $2.7 billion of which will mature over the next two years. Still, Tesla's cash is rapidly depleting. Tesla has about $2.7 billion on hand and a burn rate of about $6,500 a minute as the company attempts to ramp up production and delivery of the Model 3. Moreover, Tesla is particularly susceptible to financial distress because the electric car business is highly competitive and capital-intensive.

What should the company do? It's unlikely that Model 3 profits will be substantial enough to simultaneously pay off the company's debts, maintain market share, and finance Elon Musk's vision for the future. Given Tesla's current credit rating, leveraging the company would be extremely expensive as a result of hefty interest payments. Instead, Tesla should capitalize on the recent surge in stock price and renewed sense of optimism among equity investors by selling a sizable chunk of the company to pay the company's debts, finance its future, and stave off bankruptcy.