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Markets Crown Tesla the Big EV Winner, But Won't Pick the Legacy Losers

Tesla's stellar operating results in its most recent quarter followed by a deal with Hertz to deliver 100,000 electric vehicles (EV) by the end of 2022 sent its market cap soaring past \$1 trillion¹ and solidified its place in the minds of analysts and investors as the undisputed and unsurpassable leader in EV and battery technology at least through the end of this decade despite a big push into EV by legacy automakers.

Not bad for an upstart carmaker that will sell just 850,000 vehicles this year in a 90-million-unit global auto market. But markets aren't rewarding Tesla for what it has accomplished, as impressive as that is; they are salivating over what it is widely expected to do over the next 5-10 years. Much of Tesla's market value is attributable to its battery technology and the software revenues to be derived from self-driving vehicles, with analysts ascribing anywhere from 30%-50% of Tesla's current market value to its businesses other than vehicle sales. Still, if "only" \$500 billion of value is attributable to its EV business, Tesla is still the most valuable OEM in the world by far —

with a miniscule 1% market share of global auto sales this year. Going along with this nosebleed valuation are some lofty expectations about Tesla's EV growth and dominance in the years ahead.

You don't have to be an expert in EV technology to recognize that when a disruptive newcomer enters a mature, low-growth industry and is poised to take significant market share from incumbents, there must be losers. The global automotive industry essentially operates as a zero-sum game; that is, one player's gains are another's losses. The size of the pie is barely growing. EVs certainly will change what cars people will

be driving over the balance of the decade but they won't be a pie grower, which is largely a function of population and income growth. (Moreover, ride sharing will likely dampen total auto market growth.) Global auto sales contracted by nearly 18% in 2020 due to the pandemic and chip shortages and will be struggling to get back to pre-pandemic levels over the next several years. UBS estimates that global auto sales will reach 94 million vehicles by 2025, just short of 2017 volumes.² Moreover, while EVs are still considerably more expensive than cars with internal combustion engines, that gap is narrowing, and OEMs, including Tesla, are determined to introduce more affordable EVs over the next several years. Affordability will be a huge determinant of EV growth and market share this decade.

Expectations for EV growth are huge, with the largest OEMs aiming for EVs being 30%-40% of new vehicle sales by 2030, and some ambitious players targeting 50% by the end of the decade. Estimates are that global EV unit sales will grow from 2.5 million vehicles in 2020 to 11.2 million in 2025 and 31.1 million by 2030, a CAGR of 28%, and a 32% market share of total global vehicle sales by the end of the decade compared to 3.0% in 2020.³ Projecting global EV sales and market share is an exercise requiring numerous assumptions and is fraught with error potential, but we've yet to see an EV market share forecast of less than 30% of annual vehicle sales by 2030; several estimates are considerably higher than that. EVs are arguably the most disruptive change ever in the long history of the automotive industry.

Tesla currently enjoys a large market share of a nascent EV market — approximately 27%-30% of global EV unit sales — and an even higher share if we only consider battery electric vehicles (BEV). This dynamic will be changing in the years ahead, as other OEMs roll out more EVs and EV's share of the total auto market accelerates. Over time Tesla will be taking a smaller market share of a much larger EV market, taking it from a niche auto player to a major OEM by 2030. UBS's base-case scenario projects that Tesla will be selling 3 million vehicles by 2026 and 7 million units by 2030, giving it a market share

of global EV sales of approximately 20% and nearly an 8% share of total global auto sales in 2030.⁴ Incredibly, UBS's upside scenario has Tesla vehicle sales of 20 million units in 2030, which would make it the largest OEM in the world. This scenario will largely depend on the timing of autonomous vehicle rollouts as well as Tesla's ability to produce an EV model that's affordable to the masses. Tesla's technological edge over competitors, especially as it pertains to batteries, combined with cost advantages arising from its vertically integrated production relative to other OEMs, make it the most likely OEM to introduce low-cost EVs.

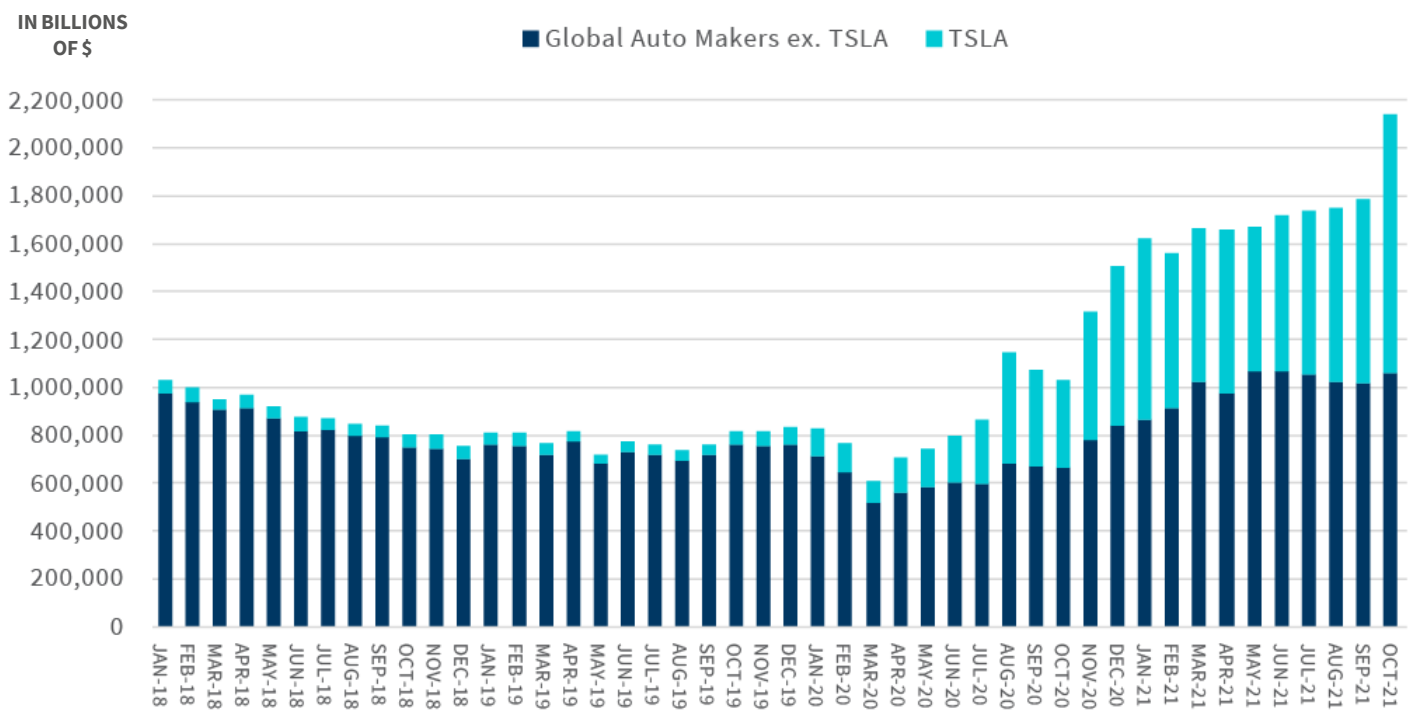
The flip side of this discussion is that Tesla's ongoing success must necessarily come at the expense of incumbent OEMs in a mature (or stagnant) end-market for autos. It's true that Volkswagen, Ford and other major OEMs have invested billions in EV, and they will surely garner significant EV market share gains in short time. But an industry newcomer like Tesla, which is expected to take global auto market share approaching double-digits or more within a decade, will surely be inflicting pain on some legacy OEMs and their suppliers. This argument is hardly a new one. Predictions of upheaval in the global auto supply chain have been made for several years and have yet to materialize in fact or in market valuations. It's more likely that such predictions were premature rather than flat-out wrong.

Equity markets have decided that Tesla is the big winner in the EV battle, judging from its market valuation in 2021 (**Exhibit 1**). Tesla's equity market value is now equal to the value of all other publicly owned global OEM automakers **combined** (more than 25 of them!), up from 10% at the end of 2019, though again, a significant portion of this value is attributable to its non-EV businesses. Assuming its EV business is worth a mere \$500 billion, that would still peg Tesla's market share at more than twice that of Toyota, the world's largest OEM, despite producing one-tenth as many vehicles as Toyota in 2021. Expectations attached to such an astounding valuation are sky high.

Strangely, equity markets have yet to penalize other OEMs (or their suppliers) despite rewarding Tesla richly in what we maintain is essentially a zero-sum automotive industry. Collectively, market valuations of other global OEMs have appreciated significantly since the end of 2019 — up nearly 40% as a group—while Tesla’s value has increased more than ten-fold in that time. The top five global OEMs have appreciated even more than

the composite group compared to their pre-pandemic valuations. Like other inexplicable market anomalies these days, something eventually must give. Either markets are vastly overestimating Tesla’s market share potential or investors are blithely ignoring sizeable market share losses soon to come for some legacy OEMs at the hands of Tesla. But they can’t all be winners. This isn’t a children’s soccer game.

Exhibit 1 - Global Auto Makers: Equity Market Value



Source: S&P Capital IQ and FTI analysis

Endnotes

- 1 <https://www.barrons.com/articles/tesla-market-cap-trillion-dollars-51635189306>
- 2 UBS, *UBS Global Auto Sales Monthly*, September 29, 2021
- 3 <https://www2.deloitte.com/content/dam/Deloitte/tw/Documents/consumer-business/rp210126-2021-electric-vehicles-trends-en.pdf>
- 4 UBS, *Tesla: EV Teardown*, March 2, 2021

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