Bad Karma: How Fisker failed

The company raised $1.4 billion in private and public funds since its founding in 2007, but most of the money is gone. Where did it go?

Danish designer Henrik Fisker knows how to style a sexy car. Among his works is the BMW Z8, driven by James Bond in “The World Is Not Enough,” where the sleek roadster gets sliced in two by a helicopter armed with giant saws.

Fisker’s latest piece of rolling sculpture is the comely Fisker Karma hybrid sports sedan — and it may meet an equally ugly end.

BIG DREAMS: Fisker’s goal was to build a beautiful, “green” car that could rival exclusive European brands like Maserati and Aston Martin.

REUTERS/ALLISON JOYCE
FISKER A CAUTIONARY TALE

The Dane’s startup, Fisker Automotive, hasn’t built a car in nearly a year. It fired most of its workforce, hired bankruptcy advisers and is seeking a buyer. Co-founder Henrik Fisker resigned in mid-March in a dispute with some of the directors. And despite raising $1.4 billion in private and public funds since its founding in 2007, the company is out of cash. For months, key investors have been footing the car maker’s day-to-day expenses to keep it alive in diminished form.

An examination of the company’s rise and fall reveals Fisker’s finances started to unravel as early as June 2011, when the U.S. Department of Energy cut off access to taxpayer-funded loans — a fact that wasn’t publicly acknowledged by Fisker for nine months.

That and other troubling information remained unknown by many of Fisker’s private-sector investors, who put $525 million into the company from May 2011 through August 2012, attracted by rosy sales forecasts and assurances the company valued itself at nearly $2 billion.

“One characteristic of businesses that are in trouble like this is, as the desperation increases, they tend to bend the story a little,” said David Cole, a longtime auto consultant and former head of the Center for Automotive Research in Ann Arbor, Michigan.

Fisker declined to comment. A Fisker executive who spoke on the condition of anonymity said the company accurately presented its finances to both investors and the government. The executive said Fisker disclosed to investors in a December 2011 letter that it was unlikely to meet the financial covenants under the government loan.

“Whatever the Energy Department’s internal assessment or view might have been, we certainly weren’t giving them different information or different forecasts than we were providing to our own investors,” the executive told Reuters in late May.

Fisker’s undoing had numerous causes. Fundamentally, say suppliers and some insiders, executives simply couldn’t orchestrate the complex dance that leads from a design sketch to the production and sale of a profitable car. Spending was lavish; engineering blunders rife. The company also faced...

$35,000

The amount that Fisker lost on each car it built

Source: Internal financial statements and interviews with former executives
Fisker breaks down

Over five years, Fisker Automotive raised more than $1.4 billion in equity and debt financing, from private investors and the U.S. government.

Most of the money is gone.

Fisker’s origins

Fisker Automotive was founded in August 2007 with the goal of building a beautiful, “green” car that could rival exclusive European brands like Maserati and Aston Martin.

Around the same time, Ray Lane, then a senior partner at venture-capital firm Kleiner Perkins Caufield & Byers, was developing a portfolio centered on clean technology. Lane, a onetime IBM executive, made his reputation as president of software giant Oracle. Kleiner Perkins had bankrolled the likes of Google and Amazon. Their backing was a coup for any startup.

Lane threw his support behind Henrik Fisker in early 2008, joined Fisker’s board of directors and ultimately went on to serve as the startup’s lead investor, board chairman and chief cheerleader. Two people close to Lane said he was impressed by Henrik Fisker’s design chops.

Fisker landed an even bigger backer the next year. In September 2009, Fisker...
won a $529 million loan from the Energy Department to develop the Karma and build a second model in the United States. The financing came as part of a broader Obama administration effort to shore up employment in the recession-ravaged auto industry and improve the fuel efficiency of the U.S. auto fleet by extending government loans to so-called green-energy initiatives.

A month later, Fisker agreed to buy an idle General Motors factory in Delaware for about $20 million. The government loan approval was a welcome relief for Fisker, which was hurting for cash by late that summer and eager to raise more money from investors, according to an email from Koehler.

“We are oversubscribed in this equity round with the Energy Department support — and nowhere without it,” Koehler said in an August 2009 email to Energy Department officials.

The announcement triggered a flood of investor interest in Fisker. The company raised some $600 million before it ever sold a car.

**PRODUCTION PROBLEMS**

Despite this influx of cash, Fisker never turned a profit. From 2008 to 2012, the carmaker lost an estimated $1 billion, according to internal financial statements and confidential presentations made to prospective investors.

Fisker built an estimated 2,450 Karmas from 2011 to 2012, but lost at least $35,000 on each car, according to internal financial statements and interviews with former Fisker executives. One former executive said the Karma “cost far more to produce than we could ever charge for it.”

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Fisker eventually delivered about 200 cars to customers in 2011 and another 1,600 in 2012; it originally planned to sell 15,000 Karmas a year, starting in late 2009.

Some of the production delays were caused by last-minute design changes and engineering fixes, insiders said, resulting in additional cost overruns and late shipments of critical components. Fisker also over-ordered and stockpiled other parts. There was no sales revenue to help offset some of those costs until late 2011. A person close to the company’s finances estimated that last-minute tweaks rendered between $50 million and $100 million of Fisker’s parts inventory obsolete.

Another hitch: Pressure on engineers to stay faithful to Henrik Fisker’s original design, even when flaws emerged that undercut the Karma’s performance and potential fixes would add millions in cost.

In mid-2011, engineers found that Fisker’s unusual front-end exhaust design was too noisy and hurt the Karma’s horsepower. This could have been headed off years earlier by putting the exhaust pipe in the back, as is standard, but the idea was struck down.

What emerged was a solution dubbed the “pizza box” that kept the exhaust system in front, but encased it in a very thin steel box. The idea emerged after engineers ordered pizza for lunch one afternoon. The solution addressed some concerns about the sound of the vehicle, as well as CEO Fisker’s aesthetic sensibility — but at an extra cost of millions of dollars, according to two engineers who worked on the redesign program.

Beneath the world-class skin was a rudimentary machine that needed several years of engineering refinement and testing before it could be ready to be released.

Maurice Gunderson
a managing partner at Runway Capital Partners
“Beneath the world-class skin was a rudimentary machine that needed several years of engineering refinement and testing before it could be ready to be released,” said Maurice Gunderson, a managing partner at Runway Capital Partners who had an opportunity to invest in Fisker in early 2010 and passed.

The frayed relations with suppliers didn’t help. By late 2011, Fisker had amassed $200 million in unpaid bills, according to the Energy Department. Fisker acknowledged, in a December 2011 letter to shareholders, that it faced $168 million in “claims arising from liabilities to suppliers and other creditors.”

Henrik Fisker and co-founder Koehler were pulling down handsome salaries — $600,000-$700,000 a year, according to several sources familiar with Fisker’s executive compensation — even after the company began laying off hundreds of employees in late 2011 and early 2012.

Considerable sums were used to burnish the image of the company as well as Henrik himself.

In May 2011, the company co-sponsored a pre-race grand prix party aboard a 146-foot yacht moored in the Monte Carlo harbor. Guests drank glasses of champagne served with flecks of gold. Clad in a dark pinstripe suit and open-neck white shirt, Henrik Fisker navigated a crowd that included Prince Albert of Monaco, whom he described as the inspiration for the Karma. The next day, Fisker took the prince for a ride on the race course in a prototype Karma.

The Monaco weekend, according to several sources familiar with the event, cost Fisker between $80,000 and $100,000. That wasn’t lavish by auto-marketing standards, but by this point every penny mattered. Within weeks, the Energy Department stopped payments on its loan.

The 15-month period from the time the Energy Department held up the loan in June 2011 was critical. As the first Karmas began to arrive at U.S. dealers in late 2011, investors and government representatives weren’t always hearing the same story.

Fisker faced a series of cash crises, telling the Energy Department it was nearly broke in October and December of 2011 and August 2012. Investors in late 2011 heard a different spin — that Fisker pegged its value at nearly $2 billion and envisioned annual sales of more than $12 billion within five years.

In the run-up to the Karma’s launch, the company battled constantly with the Energy Department to renegotiate the terms of its loan agreement, as it regularly missed deadlines, constantly revised downward its projections for production and sales, and suffered from chronic cash shortfalls.

The Energy Department, in a December 2011 internal briefing, said it “halted further funding of the loan” in June 2011 after it received “varied and incomplete explanations” from Fisker about persistent delays in producing and selling the Karma. In a separate internal briefing in December 2011, the Energy Department said it had stopped disbursing loan funds to Fisker after the company had “missed production milestones” while experiencing “performance and execution problems.”

Neither the Energy Department nor Fisker made that news public until February 2012, when Fisker told reporters that it was “renegotiating” terms of the loan. The department that same month said that it “only allows the loan to be disbursed as the company meets certain milestones and demonstrates results.”

Before then, Fisker told the government on Nov. 1, 2011, that it would run out of cash within three days without additional government loan money or an injection of private equity; on Nov. 30, it said a modest investment increase of $37 million at mid-month had nudged its cash pile to a still-thin $20 million.

Just weeks later, in a Dec. 14 letter to shareholders, Fisker told investors that the company had a capitalization “approaching $2 billion.” That included $720 million in private equity, almost all of which had been spent.

The total also included the full $529 million in loans approved by the Energy Department — even though Fisker was able to tap only $192 million before being cut off six months earlier — and an inflated value of up to $700 million for the still-idle Delaware plant, more than 30 times the purchase price. The Energy Department described the plant, in a December 2011 memo, as “just a shell.”

In an internal Energy Department briefing dated Dec. 19, 2011, officials discussed a plan to monitor Fisker’s progress in getting the Delaware plant ready to build cars “by the end of 2013.” In a separate email exchange in late December 2011, Energy Department officials and consultants forecast that Fisker’s second model, the Atlantic, would not be ready for production in Delaware until mid-2014.

In the Dec. 14, 2011, shareholder letter, CEO Henrik Fisker assured investors that the company “will maintain the 2013 launch timing” for the Atlantic. Seven weeks later, on Feb. 7, 2012, the company shut down work at the Delaware plant and laid off all 26 workers there.

As for the critical government loan, Fisker did not tell investors in the December letter that it hadn’t been able to tap the Energy Department funds for six months. The company said the remaining $336 million of the loan “remained available” to help fund the Atlantic and that it had “elected” not to request any further draws while it renegotiated terms with the government.

It admitted missing “certain financial covenants and project milestones,” but said the Energy Department had agreed to delay the effective dates of the covenants for one year.

The Fisker executive told Reuters that
BEIJING, JUNE 16, 2013

as if, ‘that’s all!?’” according to one of the Fisker’s self-estimated value in late 2011. as little as $250 million, about an eighth of he suggested Geely could take control for and cons of taking a majority stake in Fisker. Geely Chairman Li Shufu through the pros and hyundai marketing executive, walked during that time because we weren’t submitting advance requests.”

Privately, the company was trying to renegotiate the loan terms, telling Energy Department overseers in fall 2011 that it needed to raise additional private equity. The Energy Department, in internal briefings, noted that it had granted Fisker a one-year waiver in early December 2011 on meeting certain unspecified milestones and covenants - but it had not restored access to the loan funds.

Fisker told the Energy Department in early 2012 that its dire financial circumstances might force a sale of the company or a move to China or Russia. Fisker also considered a high-yield debt offering of up to $400 million in mid-2012 and an initial public offering in mid-2013. Neither one materialized.

By August 2012, Fisker’s cash was down to $12 million, and the Energy Department recommended to Fisker that it consider an “emergency sale,” according to an internal Energy Department briefing dated Aug. 2, 2012.

Fisker made no mention of the Energy Department’s recommendation or the company’s precarious cash position in an Aug. 22, 2012 investor presentation aimed at raising $150 million in equity by September and another $275 million in mid-2013.

In that August presentation, Fisker noted that the DOE loan remained “an attractive, low-cost source of funding” for the company, but observed that “no future advances are expected.”

CASH DRAINED AGAIN

By spring 2013, with Fisker’s cash drained yet again, Energy officials were pushing for a bankruptcy restructuring, a move that continues to be opposed by several of the company’s largest investors.

To be sure, Fisker still has its backers. Lane, now partner emeritus at Kleiner Perkins Caufield & Byers and a Fisker director until late May, has personally provided funding to the company, a person familiar with the matter said. Neither Lane nor Kleiner Perkins would comment.

Lane’s willingness to invest personally in the company is an unusual step in venture capital. It also comes at a time when Lane has been beset by other issues, including settlement of a long-running, multimillion-dollar tax dispute with the Internal Revenue Service and resigning the chairmanship of Hewlett-Packard in April under investor pressure for his role in the acquisition of Autonomy Plc.

Some Fisker investors also are emboldened by the success of green-car rival Tesla Motors Co, whose stock has more than tripled this year and whose market capitalization briefly topped $12 billion in late May.

For some smaller investors, however, it’s too late to recoup their losses.

“My money is gone forever,” one investor said. “Somebody will have to explain to me why that happened. I still have questions.”

Additional reporting by Ayesha Rascoe in Washington and Norihiko Shirouzu in Beijing; Editing by Claudia Parsons and Leslie Gevirtz

Fisker’s China (dis)connections

BY NORIHIKO SHIROUZU
BEIJING, JUNE 16, 2013

In late January, consultant Joel Ewanick arrived at Geely’s headquarters in eastern China to deliver an impassioned pitch on behalf of Fisker Automotive, the California-based boutique green-car maker that was running out of cash and sliding toward bankruptcy.

Ewanick, a former General Motors Co and Hyundai marketing executive, walked Geely Chairman Li Shufu through the pros and cons of taking a majority stake in Fisker. He suggested Geely could take control for as little as $250 million, about an eighth of Fisker’s self-estimated value in late 2011.

“Chairman Li’s eyes got big, and it was as if, ‘that’s all!!?'” according to one of the people who attended the meeting.

The deal ultimately fell apart for many reasons, including hard-to-meet terms of Fisker’s U.S. government loan. But the outcome was also the result of missteps by Fisker’s top managers, including openly appearing to favor a rival Chinese automaker early on, according to eight individuals with direct knowledge of the effort over the past year.

By betting on the wrong company as its potential white knight, Fisker may have bungled an opportunity to raise hundreds of millions of dollars. Fisker’s board sent out at least two search teams, but proceeded without a clear roadmap or coordination between the teams, those knowledgeable individuals told Reuters.

The events show how Fisker’s last-ditch bid for survival has been just as messy as the mismanagement that led the company to burn through more than $1.4 billion in public and private funds in less than six years.

Now five months later, Fisker continues to stave off bankruptcy, but it is fielding bids a tenth the size of Ewanick’s proposal to Geely. The company also risks making the same errors in judgment and derailing even those smaller offers, people close to the company said.

Fisker’s suitor search began in earnest last August when Joseph Chao was named the head of operations in China, the world’s biggest auto market. One of his main tasks was to lead the search there for new strategic investors — and a potential buyer.

Chinese companies had begun buying up the troubled assets of Western automakers to expand their presence on the global stage and gain access to more advanced technology. In 2010, Zhejiang Geely Holding

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Group acquired Sweden’s Volvo Car from Ford Motor Co. Wanxiang Group bought Fisker’s battery maker, A123, in 2012.

Chao wasn’t the only one looking for a partner or buyer. Fisker also had hired Ewanick as interim chief commercial officer and tasked him with finding a potential suitor, a quest that took him to China and Korea.

While Chao focused on China’s state-owned Dongfeng Motor Group, one of China’s four largest vehicle manufacturers and a partner of Nissan Motor, Honda Motor, Kia Motors and Peugeot-Citroen, Ewanick concentrated on Geely and Beijing Automotive Industry Holding Co.

Joining Chao in pursuing Dongfeng was former General Motors engineer Tony Posawatz, who was named Fisker CEO in August. Posawatz did not return calls seeking comment.

At Geely headquarters in Hangzhou, Ewanick’s meeting segued into a multi-course lunch with bottles of French wine in the company’s executive dining room. Over lunch, Li agreed to consider the deal and promised to move quickly.

Li assembled a team of Chinese executives from Geely, Volvo China and Geely’s main investment bank, who put together a two-fold turnaround plan: Use a former GM plant in Delaware, now owned by Fisker, to produce Volvo and Geely cars, as well as the long-gestating Fisker Atlantic sedan, and use Fisker’s engineering and design expertise to develop plug-in hybrids for Geely and Volvo.

At Fisker’s Anaheim headquarters in February, Geely’s due diligence team was “serious” and “asked smart questions,” people familiar with the matter said. Dongfeng’s due diligence team, in contrast, moved slowly. A Fisker employee in Anaheim who helped host the Dongfeng team said the Chinese didn’t ask many questions: “It felt more like those guys were there on holiday.”

On March 13, Henrik Fisker resigned from the company, citing major disagreements with other executives and board members.

By the end of March, it was clear that neither Chinese company would bid. Within weeks, Fisker fired 75 percent of its U.S. workforce in a last-ditch effort to save cash.

The Chinese government told state-owned Dongfeng not to go alone on the deal, according to a source close to Dongfeng. It also preferred Dongfeng bid jointly with Geely, this person said.

The Chinese government also wanted production of Fisker cars moved to China, but concluded that wouldn’t be possible because of the terms of Fisker’s U.S. Department of Energy loan. The restrictive terms of the DOE loan and the amount of work needed to overhaul the Delaware plant also helped convince Geely not to submit a final offer.

People close to Fisker worry the company is about to repeat the same errors. Investors, led by Hong Kong billionaire Richard Li, are looking to buy out the DOE’s loan for pennies on the dollar. The unusual strategy would allow Fisker to avoid bankruptcy, an outcome favored by other investors. As a result, Fisker has still not acted on a competing offer from Chinese auto parts supplier Wanxiang and VL Automotive, a joint venture between former General Motors executive Bob Lutz and Michigan industrialist Gilbert Villarreal.

Meanwhile, the company’s value is dropping by the day.

Reporting by Norihiko Shirouzu in Beijing; Additional reporting by Deepa Seetharaman in Detroit; Editing by Claudia Parsons and Leslie Gevirtz

FOR MORE INFORMATION
Paul Lienert, Detroit Bureau Chief
paul.lienert@thomsonreuters.com

Claudia Parsons, Editor, Top News
claudia.parsons@thomsonreuters.com

Michael Williams, Global Enterprise Editor
michael.j.williams@thomsonreuters.com

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