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Risk Analysis of Faraday Future Intelligent Electric Inc.

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Abstract: The challenges Faraday Future Intelligent Electric Inc (FF), a Los Angeles-based automaker founded in 2014 with the goal of transforming the automotive industry with connected smart electric vehicles. This paper first explores the company's troubled history, from its ambitious $500 million project to build a manufacturing plant in North Las Vegas, which was eventually abandoned due to financial difficulties, to the current struggle to deliver its flagship car model, the FF91. This article delves into the effects of FF's financial mismanagement, deglobalization caused by the pandemic, and over-reliance on the success of FF91, all of which contributed to a decline in brand reputation and market confidence. It also discusses the challenges posed by the competitive EV industry and FF's questionable pricing strategy. Despite these uncertainties, the company still managed to list on Nasdaq in July 2021. This article considers the potential outcomes of the reverse split plan FF announced to avoid delisting. Through this analysis, the article attempts to provide insight into the broader implications and applications of the company's struggles and future prospects in the context of the electric vehicle market.

Keywords: faraday future, financial risk, operational risk, management risk

1. Introduction

Faraday Future Intelligent Electric Inc (referred to as FF) was established in 2014. Situated in Los Angeles, California, Faraday Future aims to disrupt the automotive industry by designing a new generation of Internet-enabled smart electric vehicles. At the beginning of the company, the founder of the company, Jia Yueting, wanted to create a new era of electric vehicles with the Internet as the core and intelligent driving as an aid. This concept was very novel in 2014, when electric cars and intelligent driving were not yet popular and Tesla-based electric cars were just starting. At that time, Jia Yueting's LeTV Group could combine its Internet ecology to let LeTV Group complete the ecological closed loop from home smart devices to smart electric cars, so at that time everyone thought it was a very cutting-edge idea. In December 2015, it announced a $500 million project to construct its first manufacturing facility in North Las Vegas. In July 2017, the company announced that it would no longer build a manufacturing facility in North Las Vegas due to financial difficulties. In August 2017, FF declared the construction of a facility in California. FF proclaimed its initial production model, the FF91, in January 2018. FF completed the pilot production of the first FF91 in August 2018 and plans to begin mass production in California by the end of 2020. In 2018, the company will encounter financial difficulties, and 2019, the company was restructured.

The founder of the company filed for personal bankruptcy and announced a delay in the delivery of FF91. In 2020, it will plan to secure investor financing through a reverse merger through the acquisition of property solutions Acquisition Corp. And proclaimed FF91 delivery in Q3 2022. In July 2021, FF completed a reverse merger and was successfully listed on Nasdaq [1]. After it went public, it was struck with a class-action lawsuit over false information that inflated its stock price, which then fell. The special committee completed its investigation into FF in February 2022, stating that there was no proof to support the allegation that FF had sent incorrect information [2]. The California facility was expected to be completed in May and the first FF91 was announced for delivery in the third quarter. The FF91 delivery delay was announced in July, and the company was embroiled in a power struggle at the top, leading to frequent changes at the top. The company's share price fell below one in September, and in November it announced plans at a shareholder meeting for a 2:1 or even 10:1 reverse split to avoid being obliged to delist. In December, FFIE announced that it had only $22.5 million in cash left to support the first batch of $150 million in cash urgently needed for production, and that it would deliver the first production vehicles in April 2023 if funds were available in time. At the end of the month, FFIE announced a reorganization of its board of directors received another delisting warning from Nasdaq, the second time since November 2022 [3]. On January 17, FFIE reached a strategic agreement with Huanggang City, Hunan Province, China to move FFIE China headquarters to Huanggang City in the future, and FFIE stock rose 200% within a week after the announcement [4]. In February, FFIE reached $135 million in financing and announced again that FF91 Futurist will be delivered by the end of April. In mid-February, FFIE will be quasi-production car. In mid-February, FFIE shipped the FF Futurist to China for final testing and validation. At the end of Februray, FFIE announced the launch of its employee incentive program [5].

2. Risk Analysis

2.1. Operational Risk

The business is unitary, heavily dependent on the FF91, which has not yet been delivered, and has no means of making a profit until the first production cars are delivered to customers. International oil prices have gone up because of the war, thanks to strong government support for the electric vehicle industry in recent years. The market demand for electric vehicles is increasing year by year. Under the environment of the carbon cycle, more and more enterprises are trying to join the electric vehicle industry. The main competitiveness of electric vehicles comes from supplying chain, technology and brand.

In the deglobalization environment caused by the global pandemic, FF has had to face the failure of suppliers to provide the necessary components for FF products in a timely manner, which has affected FF's operations and business. Internet and autonomous driving technologies that seemed competition a few years ago will no longer seem competitive when products are being produce. The FF will no longer have a first-mover advantage due to continued delays in delivering FF91 initial production vehicles. In terms of the brand, due to supply chain and financial problems, FF continued to delay the delivery of the first batch of FF91, eroding the brand's reputation among consumers. FF was unable to build brand awareness to customers without the car being delivered, and thus was unable to capture a brand premium. On these bases, and without delivering the key vehicles and without access to market feedback, it is doubtful that the pricing strategy of several years ago is still beneficial to the company's sales. In the international automobile enterprises continue to change the product direction from the internal combustion engine to motor, in the current market environment, the overall competitive advantage is not outstanding. Under the environment of the explosion of motor technology, it is doubtful whether FF91 can stand out from the increasingly fierce competition in the electric vehicle [6].

2.2. Financial Risk

FF's financial management was in doubt when it did not have enough cash flow to sustain production. After multiple rounds of investment, it consistently declared that it did not have sufficient money to mass produce and deliver its first production car. The financial statements disclosed from November 2020 show that the majority of the company's net loss from February to September 2020 stemmed from operating costs, and that $23,572,119 was obtained in July 2020 from the sale of 23,572,119 shares sold at $10 a share including the public offering and private placement, but the statement does not clearly indicate future funding movements. the annual consolidated statement of operations and comprehensive loss for 2020, of the $147,850,000 net loss, development and research expenses accounted for only $20,186,000. General and administrative expenses were twice as high as R&D expenses at $41,071,000. This statement reveals the company's financial misapplication of resources in the company's operations before the first production vehicles are delivered. It is not reasonable that administrative expenses are much larger than R&D expenses. Although this is mitigated in the 2021 statement, administrative expenses and loss on disposal of property and equipment remain at par with R&D expenses.

The Company's financial standards have been in question, and in the May 2021 financial disclosure, both CFOs responded to the company's material weaknesses in both the internal design and operation of its financial reporting, an issue that continued in the August financial disclosure. The problem continued until the company was unable to file its annual report for the year ended December 31, 2021 with Nasdaq within the required time frame, leading Nasdaq to send the company a letter notifying it that the company would be ordered to delist if it failed to file its annual report by May 6, 2022. In that annual report, FF announced that it had identified a material weakness in its internal controls over financial reporting and that it had issued a plan to rectify it. However, the problem persisted in the May and August 2022 financial reports [7].

2.3. Management Risk

The board has a conflict of benefit from the company. The long-term power struggle at the top of the company led to confusion in the management of the company, which resulted in the inability to effectively integrate the company's resources to provide the first batch of production vehicles as soon as possible. Power struggles among board members and a lack of broad capacity are among the most important reasons FF has failed to deliver its first production vehicles on schedule after spending $3 billion over eight years. Unable to reach an agreement on the rights and obligations of the shareholders represented by the board members through internal coordination, a long-standing power struggle at the top of the company led to a degree of management disruption. In October 2021, in response to a shorting report by J Capital Research, a special committee of FF's board of directors launched a "suicidal" internal investigation, which directly led to FF's financial report delay and delisting crisis, causing the company's stock to fall [8]. This power struggle began in January 2022, when Susan Swenson was designated as the new chairman and David Wang, who served as the company's executive chairman and vice president of global capital markets, was suspended. In February of the same year, the board of directors led by Swenson launched an internal investigation into the company's founder and CEO.

In March, FF announced that McBride, who had been on the job for only six months, had resigned as chief financial officer for health reasons, and Becky Rove was appointed as the new chief financial officer. In April, the investigation committee concluded that Jia had misled and profited from investors, and Jia was removed as chief executive officer, but would continue as the company's chief product officer. In June, independent director and former board chairman Krolicki was expelled from the board by majority shareholder FFTOP and Li Han was nominated to replace Krolicki. FFTOP, which

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had already filed with the SEC in February and ordered FF to remove Krolicki from the board under a shareholder agreement. The FF board did not implement the order until June. The company's stock price then rose 132 percent in four business days, but the incident caused FF to miss an opportunity to secure financing from Citigroup, leading the company to announce in July that the first FF91 deliveries would be postponed for financial reasons. Being the announcement, the company's stock began a months-long streak of declines, and in August, an internal letter from more than 140 FF employees was released calling for the removal of Executive Chairman Svensson [9].

The employees argued that Svensson, as the first person in charge of the company after the IPO, should be held responsible for the serious waste of funds and the failure to deliver the first production vehicles due to internal management chaos within one year of the company's IPO. In September, FFTOP demanded the resignation of Svensson, the company's executive chairman, and Vogel, an independent director, and appointed Adam as the company's new chairman in accordance with a shareholder agreement. In October, Svensson, the company's former chairman, and independent directors Jordan Vogel and Scott Vogel all resigned, citing death threats. Roof, the company's chief financial officer, resigned and Yun Han was appointed as the new chief financial officer and Chad Chen as a new board member. This completed the reorganization of FF's board of directors. However, the company's stock price has remained below $1 for two months in a long power struggle and the company is in danger of bankruptcy and restructuring if not the reverse stock split immediately [10]. For example, when the CFO is replaced, the new CFO should take the lead in revising the company's major deficiencies in financial reporting to reduce the waste of the company's assets. However, every CFO has failed to play this role, and the frequent replacement of CFOs reflects this problem. The company did not give the CFO enough time to improve the company's financial problems and was in a hurry to do so, but the new CFO was not able to solve the company's long-standing financial problems in a short period of time.

3. Current Risky Event

FF faces multiple risks that threaten its long-term sustainability. One of the primary risks is financial difficulties, which have plagued the company since 2018. The misapplication of resources and doubts about the company's financial management have led to questions about FF's ability to remain operational. Moreover, the COVID-19 pandemic has negatively impacted FF's operations and business due to delays in the supply of necessary components.

Another significant risk for FF is its heavy reliance on the delivery of the FF91, its first production car model. However, the company has been unable to deliver the FF91 to customers, leading to a decline in brand reputation. The company's pricing strategy is also doubtful in the current market environment, where the competition in the electric vehicle industry is becoming increasingly fierce. Additionally, the company's share price fell below one in September, and in November, FF announced plans for a 2:1 or even 10:1 reverse split to avoid being obliged to delist. The company received another delisting warning from Nasdaq in December, the second time since November 2022.

Moreover, the power struggle at the top has led to frequent changes in leadership, which can create instability within the company. FF's business model, which is unitary and heavily dependent on the delivery of the FF91, is also a significant operating risk. Without the car being delivered, the company has been unable to capture a brand premium. This situation makes FF vulnerable to market conditions and other external factors.

Additionally, FF is the intense competition in the electric vehicle industry. Competitors such as Tesla, Ford, and General Motors have already established themselves in the market, making it challenging for a new entrant like FF to gain market share. Furthermore, the global deglobalization environment has made it difficult for FF to operate efficiently, leading to delays in the supply of necessary components.

In conclusion, FF faces multiple risks that threaten its long-term sustainability. Financial difficulties, delays in delivering the FF91, pricing strategy, competition, and operating risks are all significant concerns for the company. While the company has announced plans to address some of these issues, such as the recent announcement of financing and employee incentives, it remains to be seen if these efforts will be enough to secure FF's long-term success.

4. Conclusion

FF is a Los Angeles-based automaker founded in 2014 with the aim of designing Internet-enabled, smart electric vehicles to revolutionize the automotive industry. However, the company has faced several challenges, including financial difficulties, delivery delays of its first car model, the FF91, doubts about its financial management, and legal issues. The pandemic has also impacted its operations, causing delays in the supply of necessary components. FF's unitary business model heavily relies on the delivery of the FF91, which has negatively impacted its reputation, making it unable to capture a brand premium. Moreover, the company's pricing strategy is doubtful in the current market environment, where competition in the electric vehicle industry is increasingly intense. FF's financial management has also come into question due to its misapplication of resources and the founder's personal bankruptcy filing in 2019. FF secured investor financing through a reverse merger in July 2021 but received a delisting warning from Nasdaq in November and December 2022.

Furthermore, FF faces market risks due to fierce competition in the electric vehicle industry, and it is also subject to legal risks from a class-action lawsuit over false information that inflated its stock price. FF's future success depends on its ability to deliver the FF91 by the end of April 2023 and capture a brand premium in the highly competitive electric vehicle market. While the company has announced plans to deliver the FF91 and secured financing, it still faces significant challenges.

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