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# Rivian's Lifeline Is a $5 Billion Gamble for Volkswagen

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Rivian gets the thing it needs most out of its deal with Volkswagen: cash. What Volkswagen VOW3 -0.05%decrease; red down pointing triangle▼ receives in exchange is less clear.

The carmakers late on Tuesday unveiled a tie-up aimed at leveraging their different strengths to fix their respective weaknesses in an industry upended by the rise of electric vehicles.

Rivian's problems are financial and operational: It has well-reviewed EVs but still loses money to make them, setting it on a road to ruin. Volkswagen is a master of scale manufacturing and still generates huge operating cash flows—the analyst consensus is for roughly $38 billion this year—but hasn't nailed the complex software necessary to create cutting-edge EVs.

Overlay these two skill sets and you get a win-win situation, or that is the theory. The reality will depend partly on how well they work together in a proposed joint venture that neither side will control.

In Volkswagen's case, there is also the crucial question of capital efficiency that has long weighed on the stock. It could end up putting $5 billion into Rivian and the JV. If this simply comes on top of internal investments, it will add complexity and cost to an organization in desperate need of simplification.

The JV, to be run by co-chief executives supplied by each company, will focus on the so-called electrical architecture of EVs. This is the system that connects and controls vehicle electronics, increasingly via a “software stack” that can deliver over-the-air updates. Getting it right makes EVs smart as well as electric. The technology is tougher for old-school automakers than just replacing gas engines with batteries and motors because it requires a different kind of engineering.

Volkswagen EVs such as the ID.4 have been praised for their hardware but criticized for their infotainment system, particularly in China. Last year the company invested in Chinese EV maker Xpeng to get access to its software for the local market, and the Rivian deal follows a similar pattern.

Volkswagen will start by giving Rivian $1 billion through a convertible note, with an additional $2 billion for further tranches of equity next year and in 2026, subject to conditions. In addition, the German company will put $1 billion into the JV later this year, including to secure Rivian’s current electrical architecture. A $1 billion loan to the JV may follow in 2026.

Rivian’s stock soared 36% in premarket trading. While the gains are exaggerated by short-covering and may ebb, they reflect the much-reduced risk that investors face now that the company has a strategic backer. Rivian, which is expected to burn through $4.1 billion of cash this year, is holding an investor day Thursday. The deal has come in time to give it better answers to questions about its financial viability.

Volkswagen's preference shares—the instrument that most institutional investors in Europe trade—were down 2% in midday trading Wednesday. That is despite a roughly 50% paper gain on half of its initial Rivian investment, which will convert into stock at a price based on levels before the deal was unveiled. Investors have been burned before by Volkswagen's habit of throwing money at problems.

The German company invests much more of the cash it generates than its peers. The Rivian deal forced it to cut its guidance for automotive free cash flow after acquisitions to just 3.5 billion euros at the midpoint, equivalent to $3.7 billion. General Motors expects to generate $9.5 billion at the midpoint by selling only two-thirds as many vehicles.

If partnerships with Rivian in the U.S. and Xpeng in China can deliver top-notch vehicles, it will be a win for Volkswagen. To turn that into a win for its investors, though, the German company will also need to limit software investments at home to avoid the usual waste and duplication. For a company with a big state shareholding and an unusually dominant union, that may be the harder part.

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