
Operator

Welcome to the Westport Fuel Systems Second Quarter 2018 Financial Results Conference Call. As a reminder, all participants are in listen-only mode and the conference is being recorded. After the presentation, there will be an opportunity to ask questions. To join the question queue, you may press star, then one on your telephone keypad. Should you need assistance during the conference call, you may signal an Operator by pressing star and zero.

I would now like to turn the conference over to Ms. Caroline Sawamoto, Senior Manager of Investor Relations and Communications for Westport Fuel Systems. Please go ahead.

CAROLINE SAWAMOTO speaking Senior Manager, Investor Relations and Communications, Westport Fuel Systems

Thank you and good morning. Welcome to Westport Fuel Systems Second Quarter 2018 Conference Call, which is being held to coincide with the press release containing Westport Fuel Systems financial results that went out yesterday. On today's call, speaking on behalf of Westport Fuel Systems is Chief Executive Officer, Nancy Gougarty, and Chief Financial Officer, Mike Willis. Attendance at this call is open to the public and to media, but questions will be restricted to the investment community.

You are reminded that certain statements made in this conference call and our responses to various questions may constitute forward-looking statements within the meaning of U.S. and applicable Canadian securities law, and such forward-looking statements are made based on our current expectations and involve certain risks and uncertainties. Actual results may differ materially from those projected in the forward-looking statements, so you are cautioned not to place undue reliance on these statements. Information contained in this conference call is subject to and qualified in its entirety by information contained in the Company's public filings, in particular, references made to the ongoing SEC investigation and related costs as described in Westport Fuel Systems financial statements and Management's discussion and analysis.

I will now turn over the call over to Nancy.

NANCY GOUGARTY speaking Chief Executive Officer, Westport Fuel Systems

Good morning and thank you for joining us for Westport Fuel Systems Second Quarter Results Conference Call.

For the last two years we have been relentlessly focused on transforming the Company into a profitable, sustainable organization. I am pleased that we have made considerable progress towards this goal. The culmination of our efforts in aligning our cost with revenue, optimizing our product portfolio, divesting of our non-core assets, implementing manufacturing excellence initiatives, and launching Westport HPDI 2.0 has led to this moment.

In the past we have guided that we would achieve positive Adjusted EBITDA during second quarter of 2018. We have delivered and this is a huge milestone for us. Furthermore, with the launch of HPDI 2.0 in 2017, our R&D and capital expenditures have decreased significantly, further improving the Company's cash flow profile.

We ended Q2 with a healthy cash position of \$51.2 million, which has been further strengthened by the recent completion of our Compressor business sale for gross proceeds of €12.3 million.

With increasingly urgent demands for clean vehicles, we are well-positioned to deliver market-ready alternative fuel solutions across all segments of the global transportation market today. We have a complete product offering that addresses a broad range of alternative fuels, including LPG or propane, natural gas, and hydrogen. Our suite of products are quickly taking advantage of the changing market trends, such as higher oil prices, stricter emission regulations, and customer demanding clean vehicles.

In the recent discussions with OEM partners, they said that they have seen a significant increase in CNG car registrations. In Germany, for example, they saw over a 600% increase year-over-year. Although it is still a relatively small market compared to diesel and gasoline car sales, they believe CNG could potentially reach 5% to 10% of the total fleet in Europe.

We have come a long way and we are ready for the next stage of growth. We can now seize evolving opportunities with our valued industry partners. We are doing this by advancing our existing technologies and deepening engagements with industry partners which will further strengthen our market position. For example, for the Aftermarket business we are investing in targeted R&D to stay paced with new technologies introduced by automotive OEMs. We are also investing in high-pressure fuel systems. As OEMs move from 350 to 700 bar hydrogen storage systems, we are developing higher pressure fuel systems components to fit their needs. This higher pressure hydrogen product family is planned for 2019 and it will complement our portfolio of low-pressure components in order to offer a complete hydrogen fuel cell systems.

Another example is on our HPDI system. With higher performance of OEM engine platforms, Westport Fuel Systems is advancing high higher pressure systems to support the powertrain efficiency improvements, specifically, higher peak cylinder pressure. Furthermore, with this shifting landscape, the OEM market is primed for our ready now solutions, especially with the increased anti-diesel sentiment, as well as the heightened renewable energy mandates.

In particular, we are seeing growth in our OEM business, which is typically a leading indicator of growing demands for alternative fuel OEM products. With this growing OEM interest, we have recently hired an experienced leader to lead our OEM activities so we can best build on this momentum and accelerate the pace of adoption, particularly in the alternative fuel markets.

While we are really excited about the prospects of our existing business, we also need to make sure that we keep our eye on the future. This is about growing profitably. Our R&D activity will be much more targeted in nature. We anticipate our customers will fund these initiatives in partnership with us. We are carefully evaluating new opportunities and technologies that we expect to underpin future growth of Westport Fuel Systems, but we will do this in a very sustainable manner.

I'm going to conclude with three key takeaways today. We are delivering on the targets we set out for ourselves and we expect to sustain our positive performance. We have reached an inflection point through our strong operational results with a suite of products that are quickly taking advantage of changing market trends. Finally, we are in a prime position to seize evolving opportunities with our valued industry partners by advancing existing technology and strengthening engagement with industry partners.

With that, I will turn the call over to Mike to provide our Q2 financial details.

MIKE WILLIS speaking

Chief Financial Officer, Westport Fuel Systems

Thank you, Nancy. As you know, this is my first quarterly call since starting with Westport Fuel Systems in early June. I'm really pleased to be joining the Company as it hits this milestone of turning Adjusted EBITDA positive. I've been immediately impressed by the talent of the Westport Fuel Systems team and the passion they have for what the Company is trying to accomplish. I'm very optimistic about our prospects and believe that we are well-positioned to become a profitable company, providing market-ready products to support alternative fuel usage across all segments of the transportation sector. I've had the chance to speak with all of our analysts and with many of our shareholders, and look forward to meeting with more of you in the near future.

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I'll start with Slide 5 that provides a summary of our second quarter results. Note that the current and comparative periods have been adjusted to exclude the Compressor business for which we completed the sale in July. Cash on hand at the end of the quarter was \$51.2 million and excluded the proceeds from this sale.

As a side note, as a newcomer to Westport Fuel Systems I've been really impressed by the Company's ability to drive significant value from its assets since the 2016 merger with Fuel Systems, generating meaningful cash proceeds from the sale of the Industrial, APU, and Compressor businesses while also developing a streamlined and profitable portfolio of transportation-focused businesses.

Now onto our financials, we closed the quarter with sales of \$80.5 million, a net loss of \$5.7 million, and Adjusted EBITDA of \$8.6 million. Operating expenses increased due to unrealized foreign exchange losses of \$5.2 million and legal expenses related to the previously disclosed SEC investigation. But these were partially offset by a significant reduction in R&D expenses.

As already noted, we achieved positive Adjusted EBITDA in Q2 2018, delivering on our prior guidance for the quarter. This is a credit to Nancy and the entire Westport Fuel Systems team for focusing the Company and its product portfolio on the transportation sector and by rightsizing in the Company's cost structure to increase cash margins.

Turning to Slide 6, we look at our Transportation business segment. Revenues for the second quarter improved by 37% to \$80.5 million as compared to the same quarter in 2017. Sales also improved by 26% from the first quarter. This was the result of stronger sales in almost all of our businesses, including the Aftermarket, OEM, Light- and Medium-Duty OEM businesses, as well as from HPDI 2.0. Gross margins improved to \$21.7 million in the second quarter of 2018 from \$15.3 million in Q2 2017, and \$14.6 million in Q1 2018. We are seeing improvement in gross margin as our sales increase and we leveraged a fixed cost basis of several of our businesses. The Company is also seeing efficiencies through the consolidation of its manufacturing facilities globally.

R&D expenses decreased 47% in Q2 2018 compared to the prior year from \$13.6 million to \$7.2 million, in line with what we have previously mentioned publicly. We expected this decrease in R&D spend as we transitioned HPDI 2.0 from a product development activity to a commercial sales and marketing support activity.

Going forward, our R&D efforts will now be more focused on supporting sales of our products in the marketplace and we'll look to have customers support new R&D initiatives in partnership with us. As a result of our higher sales and tightening R&D spend, Adjusted EBITDA improved significantly to a positive \$7.4 million in Q2 2018 within the Transportation segment from a loss of \$5.8 million in Q2 2017 and a loss of \$0.7 million in Q1 2018.

Now turning to Slide 7, we will review the results of the Cummins Westport joint venture. CWI recorded revenues of \$86.9 million in Q2 2018, an increase of \$34.7 million over Q1 2018 and an increase of \$7.4 million over Q2 2017. As we noted, in the Q1 earnings call, CWI revenues were negatively impacted by pre-buy activities that occurred in Q4 2017 in advance of the 2018 requirement for on-board diagnostic compliant engines. It's great to see revenues bounce back so well in Q2.

As anticipated, R&D expenses are trending lower and we expect these expenses to remain at historic lows going forward as the JV isn't anticipating any new major R&D projects going forward. Also, the reduction in corporate tax rates that was recently enacted in the U.S. should increase the after-tax income for CWI. These should translate into higher cash dividends to bulk (phon 13:11) partners in the future.

In Q2, CWI recorded net income of \$15.5 million or 18% of sales, and during the quarter Westport Fuel Systems received cash dividend of \$7.1 million.

Turning to Slide 8, we look at our Corporate segment. As mentioned previously, R&D costs in the Corporate segment are now only associated with protecting our intellectual property, including maintaining our patent and trademark portfolios. SG&A costs remained relatively consistent with prior periods with the exception of legal expenses relating to the SEC investigation which were a net \$2.5 million in the quarter.

Turning to Slide 9, we show our cash walk. We started the quarter at \$55.2 million and ended with \$51.2 million. It's important to note that our ending cash balance does not include the proceeds from the Compressor business as it was completed after quarter end. The reason for the cash decrease is primarily due to legal expenses relating to the SEC

investigation and the buildup of working capital as revenue and production increased during the quarter. Other significant sources and uses of cash were: dividends from CWI were \$7.1 million; capital expenditures were \$1.7 million this quarter, a significant decrease compared to prior quarters; and principal and interest payments were \$2 million.

For the full-year 2018, we are maintaining our revenue guidance from continuing operations to be between \$235 million and \$255 million. For the balance of 2018, we anticipate our financial performance to continue to be positive as compared to what we achieved in 2017. However, it's important to note that we did benefit from some positive market dynamics and some seasonal trend in Q2 that may not be as strong throughout the balance of the year. As the year progresses, we expect to provide additional colour to our shareholders on how we see the year turning up from a financial perspective.

With that, I would like to turn it over to the Operator for questions.

Operator

Thank you. We will now begin the question-and-answer session. Analysts who wish to join the question queue may press star, then one on your telephone keypad. You will hear a tone acknowledging your request. If you are using a speakerphone, please pick up your handset before pressing any keys. To withdraw your question, please press star, then two. We will pause for a moment as callers join the queue.

Our first question comes from Colin Rusch of Oppenheimer & Company.

Colin Rusch - Oppenheimer & Co., Inc.

Thanks so much, guys. Given the benefit that you had in the second quarter and thinking about the guidance for the back half of the year, I guess, we'd like to really get some more granular information around the revenue breakeven level. Should we be thinking about you guys being able to breakeven with the revenue in a range of the \$55 million to \$60 million level? What other levers can you pull to keep this streak alive on the cash flow?

MIKE WILLIS speaking Chief Financial Officer, Westport Fuel Systems

Colin, thanks for the question. I don't think we've done the analysis per se in terms of a specific revenue run rate that gets us to cash flow or at least, I guess Adjusted EBITDA breakeven. I would say that it would probably be higher than, call it, the \$60 million level because we've seen that level for, call it, the last five quarters, plus or minus, so it's probably something higher than \$60 million, definitely obviously lower than \$80 million. But, again, I haven't done the analysis to give you a specific number at this stage.

Key to that also, as you know, is things like product mix. It would probably be the number one thing that I can think of in terms of what would dictate kind of a range as it relates to that number.

Colin Rusch - Oppenheimer & Co., Inc.

Okay. Then just a longer-term strategic question because I know a lot of folks are going to ask about HPDI 2.0. Have you guys looked at moving into adjacent markets in terms of other fuel sources, obviously with the core competence around design and managing supply chain? It seems that you could move into the EV space or another fuel source without too much difficulty. Is that something that you guys are looking at considering at some point?

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NANCY GOUGARTY speaking

Chief Executive Officer, Westport Fuel Systems

Colin, again, thanks for the question. I think that you can see that as we have really looked at our portfolio that as we looked at divesting, we ended up keeping the Hydrogen business. We think that that's very synergistic with our current Gas business. We always are looking at opportunities. We see ourselves as an alternative fuel company, so we don't see ourselves totally boxed in, though we have very, very strong competencies, I'll say, on gaseous fuels.

Colin Rusch - Oppenheimer & Co., Inc.

Great. Thanks so much, guys.

MIKE WILLIS speaking

Chief Financial Officer, Westport Fuel Systems

Thanks, Colin.

Operator

Our next question comes from Eric Stine of Craig-Hallum Capital Group.

Eric Stine - Craig-Hallum Capital Group

Hi, Nancy. Hi, Mike.

MIKE WILLIS speaking

Chief Financial Officer, Westport Fuel Systems

Hey, Eric.

NANCY GOUGARTY speaking

Chief Executive Officer, Westport Fuel Systems

Good morning.

Eric Stine - Craig-Hallum Capital Group

Good morning and congrats on the quarter and getting to your milestone. Maybe just on the transportation segment, is there—I mean, I know that it's all in one bucket, but maybe if you could just talk about the trends in that business? I mean, I would assume that in OEM, DOEM, and Aftermarket it's pretty broad-based, but, I mean, this was a really big quarter so just wondering were there other things in there as well, you know, you had the Algeria contract or a development payment? Then maybe just some commentary on the contribution from HPDI.

MIKE WILLIS speaking Chief Financial Officer, Westport Fuel Systems

Well, I'll answer kind of from a financial perspective, which is we saw upticks in sales pretty much across the board, Eric. It wasn't one thing dominating this uptick. I would say probably the segment that showed the biggest increase quarter-over-quarter was the DOEM business and maybe, Nancy, you can comment, like you described within your prepared comments how DOEM leads potentially into the OEM business.

NANCY GOUGARTY speaking Chief Executive Officer, Westport Fuel Systems

Yes, Eric, good morning. I would say that from what we see, as we have seen this anti-diesel sentiment, there's a lot of, I'll say, pull at this point in time to get vehicles into the showroom. By being able to offer a DOEM solution, which gives products that can get to the showroom on a pretty fast order, we have seen that that market has been quite brisk. I would indicate to you, though, that as we have seen across all our products, oil prices and other things have obviously boosted some of our revenues. We're quite pleased where we are relative to the launch of HPDI. We think that we have gotten good driver feedback. It's now in the hands of real consumers and that's really a test of the product and we think that the feedback and the order book there is pretty much what we expect, and we are continuing to see that as we move through the calendar year and we get country incentives and those kind of things understood that would benefit from HPDI product portfolio and they would qualify, that we are quite pleased with where we are in the launch.

Again, I think, as Mike said, very good for us in terms of this particular quarter that we saw really opportunity of increased revenue across all different sectors. I think, from our perspective, we're finding that this anti-diesel sentiment and that kind of thing, consumers are just really looking for alternatives and, because of the ability of our product and I'll say the nature of it and the cost of it, it seems to be one of the ones that is benefiting most.

Eric Stine - Craig-Hallum Capital Group

Right. It sounds like there really wasn't the benefit a large—whether it's that Algeria contract or something else, I mean, it was really broad-based.

NANCY GOUGARTY speaking

Chief Executive Officer, Westport Fuel Systems

Right.

MIKE WILLIS speaking Chief Financial Officer, Westport Fuel Systems

Including geographies, so pretty much across the board, barring maybe a couple of exceptions, every country seemed to be having a positive quarter for us, which is obviously great.

Eric Stine - Craig-Hallum Capital Group

Right. Absolutely. Okay. Then maybe just turning to I guess a follow-up on the previous question about how we think about the rest of the year. So guidance unchanged, which I know at this time of the year is something that you typically do; you did last year, but, I mean, you're also positive about year-over-year growth. So just, I mean, just kind of think about that because those two things don't necessarily match up. I mean, it's still fair to say, right, that third quarter you're going to have your typical stepdown because of heavy mix towards Europe?

MIKE WILLIS speaking Chief Financial Officer, Westport Fuel Systems

Correct. Yes. The reason why we haven't updated guidance is we still are forecasting out the balance of the year and, really, still taking a view on a variety of things, and I would say everything from currency. As you know, currency has an impact our revenues and I know this is a number that folks are often looking for, so, sequentially, from Q1 to Q2, the euro dropped I think 3% versus the U.S. dollar and that impacted negatively our revenues in Q2 by about \$4 million. Obviously we can't predict currencies, but we can at least take a view on them.

The other one that's kind of, I guess, a new one for us is given all the kind of political activity, international political activity, sanctions and tariffs and all those types of things seem to be high on the list of people's minds that questions. Again, we don't see anything near term that is impacting us significantly, but, again, we need to take a view in terms of how that may impact us for the balance of the year. Seasonality, as you point out, Europe obviously kind of shuts down a little bit in August, so that's going to be impactful to Q3.

Then there are other trends. We mentioned OEM has had a very strong quarter. However, as we have model year change outs towards the tail-end of the year, we need to figure out what are OEMs going to be doing; are they going to continue to work with us on a OEM basis or do they transition more to an OEM business line?

All those things taken in combination just mean that we haven't actually been able to truly forecast out the balance of the year. I think next quarter we will be able to provide a little bit more granularity in terms of what we're thinking about revenues for the full-year.

Eric Stine - Craig-Hallum Capital Group

Got it. I can appreciate that. Okay. Maybe last one for me, just China. I mean, I'd love to hear kind of the WWI volumes or whatever you can share there year-to-date, kind of your expectations for '18; and then maybe just an update on that market and HPDI, how you see that market playing out and also your potential there.

NANCY GOUGARTY speaking Chief Executive Officer, Westport Fuel Systems

Well, Eric, certainly we still see China as one of most significant markets relative to natural gas, and especially relative to the usage of LNG in the trucking sector. I would say that China continues to run strong, and we don't have specific figures for you relative to WWI at the moment, but I would tell you that our discussions continue to understand how we're going to tap that market and being able to utilize HPDI in that market. We continue to work forward on that, and as we get that culminated, certainly, we'll make sure that the market understands exactly where we are on that. Again, as we look, I think that China is an important market for us and we're putting our energy there.

Eric Stine - Craig-Hallum Capital Group

Okay. Thanks a lot.

MIKE WILLIS speaking Chief Financial Officer, Westport Fuel Systems

Thanks, Eric.

Operator

Our next question comes from Rob Brown of Lake Street Partners.

Rob Brown - Lake Street Capital Markets

Good morning.

NANCY GOUGARTY speaking Chief Executive Officer, Westport Fuel Systems

Good morning.

Rob Brown - Lake Street Capital Markets

Hi. Given kind of the dynamics in the market now, what's the latest on other OEM interest in HPDI? I know you've always worked with other OEMs but maybe you can just characterize where that's at and if there's been any uptick in the interest level or attraction for new programs.

NANCY GOUGARTY speaking Chief Executive Officer, Westport Fuel Systems

I'm so glad you'd asked that. I think that, Rob, the interesting thing is I think that back in mid-May the European Commission has outlined a proposal relative to the new standards and targets for the CO₂ reductions for heavy duty trucks. I would tell you that, just to give you some colour on that, the proposed reduction is 15% what they call tank-to-wheel, a reduction in CO₂ by 2025, and 30% CO₂ by 2030, and they're going to baseline the OEMs here coming up in calendar year '19 in order to strike the line of what 15% looks like.

I think that as we have, over the last several weeks, as this regulation has gotten clearer and understood in the market, we have seen and have had quite depth discussions with many of the OEMs. I think that at this point in time, as you look at these regulations, their options are quite narrow. HPDI happens to be one of the products that is in that narrow option base for them, and, so, as you can imagine, for the heavy-duty trucking, that is an area, especially in the Europe with these new regulations, is quite important dialogues going on and I think that you can probably sense that the Leadership Team is spending a significant portion of our time in Europe having these critical discussions.

As you know, in mid-September we have the Hanover Truck Show and that's also a great opportunity for us to be able to push forward these discussions as well with many of the OEMs.

Rob Brown - Lake Street Capital Markets

Okay. Great. Thank you. That's a good overview. Then maybe on the light-duty automotive side, you talked about Europe CNGs seeming to uptick in interest, but maybe just give a sense of what's going on there. I know diesel's a big part of the market there; is diesel sort of, in your thoughts, shifting to natural gas at this point in the light-duty, or maybe just some colour on what's been driving that market shift.

NANCY GOUGARTY speaking Chief Executive Officer, Westport Fuel Systems

I think it's several different things. First of all, we are seeing consumer views relative to buying diesel vehicles. They're not so keen on it. They're not sure that they're going to be able to recoup their cost out of it as they try to resell it and that kind of thing. I think also, they just, in many cases, as being, all say, environmentally, I'll say, conscious a society, they don't really want to take on diesel vehicles. Then in addition to that, we are seeing inner cities ban diesel products. Again, as you look at the options that folks have, when you do that, natural gas and propane fall right into an area that are very acceptable for these inner-city bans. So, that allows them to take these vehicles into the inner-city where the diesel vehicles can't.

Consumers, I think, don't like the restrictions of buying a vehicle that then they can't utilize fully, so that is one of the things that's uplifting of the demand. Most of it is just raw consumer pull. Obviously, having come out of Europe just a couple of

days ago, the prices are quite good for CNG and LPG in that market, significantly lower than that of petrol as well as diesel. That also, from a consumer payback standpoint, as they get the vehicle either in OEM or in what we call our aftermarket modifications, their paybacks are quite good on this. We think that that's really uplifting, at least in our opinion at this point in time, what's uplifting the European demand.

Rob Brown - Lake Street Capital Markets

Okay. Good. Then I have a question on CWI; it had a strong quarter. What's sort of your view on the sustainability of that and in the profit contribution as well; do you see that continuing to increase or is this a level that we should think about going forward?

MIKE WILLIS speaking Chief Financial Officer, Westport Fuel Systems

I think, again, we don't really guide on revenue for CWI for obvious reasons, but I think if you look at Q1, for all the reasons we've discussed in the past, it was obviously a low quarter. Q2 was a great rebound quarter so I think going forward revenues in Q2 are more reflective of the ongoing reality versus Q1. Then per my prepared statements, I think based off of the dynamics of lower R&D cost and lower tax rates, that more of the revenue dollars should be dropping to the bottom line going forward for that business.

NANCY GOUGARTY speaking Chief Executive Officer, Westport Fuel Systems

I guess one other thing to add there is I think that you've seen publicly that there has been some announcements of sizable orders that are coming through with major fleets—UPS, etc.—and we believe that a good portion of that will take place here in calendar '18.

MIKE WILLIS speaking Chief Financial Officer, Westport Fuel Systems

One of the things that we should point out is you may have seen that Cummins had a recent recall, a pretty significant one. Natural gas engines were not part of that recall. So, CWI joint venture is not impacted by that.

Rob Brown - Lake Street Capital Markets

Okay. Good. That's good to know. Thank you. I'll turn it over.

Operator

Once again, if you have a question, please press star, then one. Our next question comes from Jeff Osborne of Cowen & Company.

Jeff Osborne - Cowen & Company

Hey, good morning, guys. Just a couple of quick ones here; maybe following up on Rob's question, many of the CWI announcements have been for replacements of fleets from 2014 and 2015; A) can you confirm that; and then B) are you seeing any new fleets just given the oil diesel pricing environment that we are in, looking to adopt the technology?

NANCY GOUGARTY speaking Chief Executive Officer, Westport Fuel Systems

I guess we would say that certainly we have a lot of interest. We've been a bit helped by the folks at Clean Energy putting in their refuel stations. We believe that in certain geographies, particularly California, that this is quite acceptable and so you'll see it in big distribution companies but we're also, from my understanding, we're seeing it in other applications and other fleet buyers. So I think it's a broad-based, I'll say, pulse to the market. From that perspective, I think that as we have a full fleet of products, especially that run on renewable natural gas that have zero emissions, we stack right up there with the electric and a very, very reliable product. I think that you can see through the change over the last year's relative to the warrantee numbers that we have been talking about and that kind of thing, we've got a good product, CWI, and we've got good market support and, like I said, with the fueling infrastructure that's in place, we're picking up and the winds are favourable in this direction.

Jeff Osborne - Cowen & Company

It makes sense. Just a couple of other quick ones. Mike, for you, the \$2.5 million of expense for the SEC investigation, I imagine that ticked up since the February subpoena. Was there any kind of surge spending this quarter or is that sort of the new normal of what the expense rate should be for the duration of the investigation?

MIKE WILLIS speaking Chief Financial Officer, Westport Fuel Systems

For obvious reasons, we probably shouldn't be predicting specific costs associated with that. I would say that there was obviously a pick up in activity, which obviously spoke to the increase in that cost. But, again, going forward, it's very dependent on how the investigation goes.

Jeff Osborne - Cowen & Company

Got it. But just as we think about you hitting EBITDA positive in the second half, are you backing out any expenses associated with that or are you putting that in the model?

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MIKE WILLIS speaking
Chief Financial Officer, Westport Fuel Systems

You'll see the table as it relates to our Adjusted EBITDA that we do include that as an adjustment because we obviously don't believe that this is going to be a recurring cost over the long term for the Company. The other thing actually to note is some of the costs associated with the investigation—legal and other—we do expect to be able to recoup some of those costs through our DNO insurance, so there is kind of a leveler, if you will, as it relates to that. Obviously we can't predict exactly what those recoup levels are going to be, but there should be some ability to get some dollars through our insurance.

Jeff Osborne - Cowen & Company

It makes sense. Switching gears a little bit, I was intrigued by your comment that the delayed OEM business was the one that was up the most sequentially. I would've thought HPDI 2.0 was just given the minimal volume.

MIKE WILLIS speaking
Chief Financial Officer, Westport Fuel Systems

Well, it was up as well. I mean, it was up, but it was amazing how up our OEM business—Nancy and I were just in Chresco last week, and we see the activity in the parking lot in terms of cars coming in and cars coming out on a daily basis. Nancy sits there and counts the number of cars. So, that's not a reflection that HPDI is not growing.

NANCY GOUGARTY speaking
Chief Executive Officer, Westport Fuel Systems

Year-over-year HPDI probably is higher because we went from zero to where we are now.

MIKE WILLIS speaking
Chief Financial Officer, Westport Fuel Systems

I think in my answer I did describe sequentially. But, anyway, so that's not a reflection that HPDI is not performing well. It's the fact that OEM had such a stellar quarter.

Jeff Osborne - Cowen & Company

Got it. Then can you just remind me, maybe putting 2017 in perspective, the mix of the legacy Fuel Systems business, what percent was OEM versus delayed OEM?



MIKE WILLIS speaking
Chief Financial Officer, Westport Fuel Systems

I don't think we provide that kind of granularity.

Jeff Osborne - Cowen & Company

Okay. Fuel Systems did as a public company, but I wasn't sure.

NANCY GOUGARTY speaking
Chief Executive Officer, Westport Fuel Systems

Yes. Because 2017 we were blended, I don't remember making that split.

Jeff Osborne - Cowen & Company

Okay. Fair to say that OEM is more than half the business?

NANCY GOUGARTY speaking
Chief Executive Officer, Westport Fuel Systems

No. No.

MIKE WILLIS speaking
Chief Financial Officer, Westport Fuel Systems

No. No. The largest segment of our revenues still come from the Aftermarket business.

Jeff Osborne - Cowen & Company

Got it. Then is there meaningful—you talk about the delayed OEM transitioning to OEM, is there a margin implication of that? Obviously it's more strategic with the OEM itself, but how does that impact profitability, either positively or negatively?

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NANCY GOUGARTY speaking

Chief Executive Officer, Westport Fuel Systems

I don't think it has a major impact on it. I think that when you go to the OEM environment, one of the good things is that we have a more predictable schedule and that kind of thing, so we are able to, I'll say, predict and schedule suppliers and those kinds of things. So it has, I'll say, a 26-week framing relative to what they are doing and that kind of thing. I think also on the OEM side, once you get it in they can cross with one engine any vehicle that uses that particular engine. We can get increased volumes in a quite quick way.

I think the other benefit that we've had on the OEM side is we've had really significant increase in terms of the content on the vehicle because they see Westport as the go-to company across all systems. On the OEM side we gain the benefit from volume but we also gain the benefit for more content per vehicle.

Jeff Osborne - Cowen & Company

Makes sense. The last one I had for you, Nancy, is just you talked about Hydrogen uptick and greater interest there. Can you just be a little bit more granular as to what specifically you're providing into that ecosystem? That'd be helpful to understand that. Thank you.

NANCY GOUGARTY speaking

Chief Executive Officer, Westport Fuel Systems

Well, I would say currently the products that we currently provide are on what we call the low-pressure side of the fueling system, and as we get closer into and take the outtake of the tank, that's where the higher-pressure products are really required. We have great position with a variety of different fuel cell folks that use our products, and as they are demanding the 700 bar products, we're right aligned with them. So this will allow us to not only have the low-pressure side but also the high-pressure side of the system, and so we can continue to partner with them as their business grows. I think it's interesting. The Hydrogen, as we look at it, that is one of the alternative fuels, like I said, that's quite synergistic with us because it has tanks and all kinds of things that we are very used to doing, so this is a good reapplication of our skill set.

Jeff Osborne - Cowen & Company

Perfect. Appreciate the detail. Thank you.

MIKE WILLIS speaking

Chief Financial Officer, Westport Fuel Systems

Thanks, Jeff.

Operator

Once again, any analyst who wishes to ask a question may press star, then one.

This concludes the question-and-answer session. I would like to turn the conference back over to Caroline Sawamoto for closing remarks.

CAROLINE SAWAMOTO speaking Manager, Investor Relations and Communications, Westport Fuel Systems

Thank you, everyone, for joining us today. If you have any follow-up questions, feel free to reach out to the Westport Fuel Systems Investor Relations Team. Thanks again.

Operator

This concludes today's conference call. You may disconnect your lines. Thank you for participating and have a pleasant day.