

Conference Call Transcript

First Quarter 2020 Financial Results:

June 5, 2020

Operator

Welcome to the Westport Fuel Systems' First Quarter 2020 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 Shawn Severson with alphaDIRECT Advisors, Westport's Investor Relations representative. Please go ahead, Mr. Severson.

SHAWN SEVERSON speaking

Investor Relations Representative, alphaDIRECT Advisors

Thank you and good morning, everyone. Welcome to Westport Fuel Systems' first quarter conference call which is being held to coincide with the press release contained Westport Fuel Systems' financial results that was distributed yesterday. On today's call, speaking on behalf of Westport Fuel Systems is Chief Executive Officer David Johnson, and Chief Financial Officer Richard Oraziatti. 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 the U.S and applicable Canadian securities laws, and as 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're 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.

I'll now turn the call over to David. David?

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DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Good morning. Thank you for joining our conference call to review Westport Fuel Systems' Q1 2020 results. I sincerely hope that all of you, your colleagues, friends and family are healthy and well and that you stay healthy and well. I've had a chance to speak with many of you since our 2019 year-end results call on March 17th. It has certainly been a challenging time, but I've also been incredibly impressed with the resiliency and ingenuity of our team in the face of this global crisis.

Our focus has now shifted from COVID-19 response to a safe and efficient post-COVID recovery. As this pandemic made its way around the world, our teams have been following government guidelines, local protocols in each jurisdiction where we operate. Our people have shown tremendous fortitude and have safely and effectively resumed operations at all our locations.

Despite the near-term uncertainty and expected softer demand on the passenger vehicle side of our business, I am confident that the need for affordable clean transportation solutions remains. It's encouraging to see that climate change hasn't fallen to the back burner. Rather, we're seeing signs that the green recovery is on.

Cost consciousness and renewed pragmatism means that CapEx decisions will be heavily scrutinized, and with that scrutiny will come the realization that electric propulsion for long-haul heavy-duty truck applications is, at best, an expensive, distant hope for the far off future. Gaseous fuel solutions are proven, available and affordable right now. While vehicle purchase decisions might be delayed by the post-COVID economy, we believe the compelling fundamentals point directly to solutions from Westport Fuel Systems. And with renewable natural gas, otherwise known as biomethane, the story only becomes more compelling.

Post COVID, the challenges of climate change and urban air quality have not disappeared. The need to efficiently move goods hasn't disappeared. The world needs affordable, clean transportation more than ever.

There have been a number of important developments since our year-end results call and I'll walk through those in a moment, but first I want to share the headline Q1 financial results. On the heels of our successful 2019 results, each of our operating segments was performing in line or ahead of our 2020 expectations prior to the onset of the shutdowns and economic fall out for COVID-19. Our first quarter results reflect the impact of COVID-19, related customer shutdowns which began in China in January and spread to Europe and North America in mid-March. Roughly 75% of our global operations are located in Italy where shutdowns were implemented in the second half of March and then through all of April. In Q1, we mitigated Chinese supply chain disruptions which stemmed from their COVID shutdown, and we were able to increase inventories and ship to meet customer demand in advance of our own shutdown.

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Our headline financial results are as follows.

Consolidated revenues for the quarter decreased 8% or \$6 million to \$67.2 million compared to the same period last year. Adjusted EBITDA of minus \$3.6 million was lower compared to \$7.3 million last year, primarily due to a \$10 million charge for a service campaign to replace pressure release valves in the field. I must note there have been no failures in the field to date. We've been proactively working with our customers to eliminate the remote risk associated with a batch of our components by replacing those components in the field. We expect to recover a significant portion of this charge from our insurer during the second half of the year, but accounting rules do not allow us to book the insurance recovery at this time.

Our efforts to shore up the balance sheet and improve liquidity include the recently announced long-term €5 million loan secured through UniCredit, and we are in the process of securing a \$10 million bridge facility with Export Development Canada. We have been successful in accessing various government support programs in Canada, Italy and the Netherlands, and expect approximately \$4 million in wage subsidies in Q2 2020. We very much appreciate that support at this time.

Now, we're back at work and order flow is returning. We continue to focus on cost reduction, disciplined cash management and supporting our global team and their communities as we navigate this recovery period.

At the same time, we've been able to secure new business opportunities, such as the recently announced deal with GASTEC in Egypt. It's encouraging to see green shoots of optimism in the face of so much uncertainty.

As our customers, partners and suppliers return to production, there have been many questions about the impact of the downturn on our industry. Let's start with China.

Despite COVID-19-related delays, our Weichai/Westport joint venture has completed all the emissions testing with the Chinese Ministry of Ecology and Environment, and with the Chinese Ministry of Industry. We greatly respect the efforts of the Chinese government officials to confirm the tests that were completed to their satisfaction, and we're optimistic that the current administrative proceedings will conclude with the final paperwork for certification in the near future.

While the certification delay affects the timing of the commercial launch and the production and sales ramp that follows, we do not expect it will change the shape of the adoption curve. The long-term potential of HPDI in China, the largest natural gas commercial vehicle market in the world, remains compelling. We have a great partner and a great product, and a large market to serve. We look forward to doing that just when the Chinese government provides the final green light.

Now, let's turn to Europe. The European Union's Green Deal includes measures to increase the supply of low emissions fuels. Biomethane, otherwise known as renewable natural gas or RNG,

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accounts for 17% of all natural gas fuel consumed by road transportation in Europe, and in some countries biomethane already dominates. For example, in the U.K., renewable natural gas, biomethane is nearly 70% of the mix, while in Sweden 94% of CNG fuel is sold as renewable. In Denmark, all CNG stations dispense renewable natural gas exclusively. Production capacity is proven and the infrastructure is in place and rapidly expanding. Royal Dutch Shell has just committed to opening 10 more sites this year in Germany, two more in Belgium, one in Poland, beginning to invest also in Austria. Their liquefaction plants for bioenergy are progressing quickly, expected to come online this year, and a large German liquefaction facility coming online in 2021.

A vehicle fueled with renewable gas is effectively climate neutral. We believe renewable gas is the best solution to accelerate the decarbonization of the transportation sector. In Germany, the authorities have announced the extension of the road toll exemption for CNG and LNG heavy-duty trucks through 2023. While still subject to parliamentary approval, this is an important signal to the marketplace that natural gas trucking is a critical component of Germany's decarbonization plans.

Additional subsidies on the purchase of natural gas vehicles announced in July 2019, that is €12,000 for LNG vehicles, €8,000 for CNG vehicles, and a fuel energy tax on natural gas that is 70% less than diesel adds up to significant savings. These subsidies amount to approximately €70,000 of savings in the first five years of vehicle operation.

We also see signs that warrant optimism for our light-duty and aftermarket products. According to the European Automobile Manufacturers Association's latest report, the demand for cars fuelled with CNG in Europe increased by 68% in the first quarter of 2020. Italy remains Europe's largest market for light-duty vehicles, followed by Spain, Belgium, France, Sweden and Germany.

Like most of you, I've been following closely the commentary about the global economic recovery. As the economy restarts, gaseous fuels including LPG, natural gas, hydrogen and renewable gases have figured prominently in the Green Deal Initiatives of the EU's recovery plan. Commercial demand is strong, though we may not see quite as steep a growth curve as we were projecting for 2020. On the Aftermarket side, we're concerned consumer confidence and we expect to endure some softness in demand. We believe a focus on renewable and decarbonized gases as well as clean and sustainability mobility will offer us an opportunity to boost the economic recovery, retain and create jobs and achieve our critical emissions reduction goals.

As we look out to the remainder of the year, the steady recovery of our OEM and Aftermarket businesses, the growth of HPDI in Europe and the upcoming production launch of HPDI in China are keys to our success. I'm confident that we can weather the current headwinds and our team is committed to delivering on our strategic priorities.

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To recap, we remain focused on the successful commercial launch of HPDI in China, further cost reductions, new light-duty and heavy-duty OEM businesses in key market geographies, and the profitable growth of our light-duty business through both our Aftermarket and OEM channels. Despite the near-term uncertainty, a strong regulatory ecosystem is still there and so is the strong desire for a green recovery.

Now, I'll turn it over to Richard to review our financials. Richard?

RICHARD J. ORAZIETTI speaking **Chief Financial Officer, Westport Fuel Systems**

Thank you, David.

As David described in the financial highlights at the beginning of the call, during the first quarter our revenues were \$67.2 million, which was a year-over-year decrease of \$6 million or 8% compared to the first quarter '19. The decrease was driven mainly by lower sales in March in our light-duty and heavy-duty business, caused by the shutdowns from COVID-19. We had softer sales in our light-duty OEM business to our Russian and German customers, and we had some contracted price concessions to our HPDI launch partner that started in late fourth quarter 2019.

Gross margin of \$4.3 million decreased by \$12.9 million year-over-year, primarily due to the \$10 million charge we took on the field service campaign. On a tax effected basis, the charge was approximately \$7.5 million. As David described, we expect to recover 70% of the replacement costs from insurance recovery, however, we have not recorded the recovery at this time due to the early stage of the insurance claim review. We expect to recognize the insurance recovery once we have official confirmation from the insurance company.

Excluding the charge, margins were also impacted by lower revenues from our OEM businesses by \$3.6 million, partially offset by some improvement in our independent aftermarket business of about \$1 million.

Income from equity investment of \$5.4 million was down 37% year-over-year due to lower CWI earnings driven by a 17% decrease in engine sales and lower parts sales. The decrease in engine sales in the first quarter of 2020 largely reflects the timing of transit orders and build schedules combined with lower refuse market sales.

Net loss of negative \$15.3 million, down \$12.3 million year-over-year resulted mainly from the \$7.5 million charge for the field service campaign, lower OEM margins and an unrealized foreign exchange loss of approximately \$7 million on the translation of our U.S. dollar denominated debt in our Canadian legal entities. The unrealized foreign exchange loss was driven by a 9% devaluation in the Canadian dollar. As most of our revenues are generated in euros, this is

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somewhat less of a concern in paying down our debt and actually realizing a true cash foreign exchange loss and more of an accounting loss.

Turning to EBITDA, year-over-year EBITDA was negative \$11 million, which was \$15.3 million less than positive \$4.2 million in the first quarter of 2019. After adjusting for noncash and nonrecurring items, that is share based compensation and the unrealized foreign exchange loss, year-over-year Adjusted EBITDA decreased by \$10.9 million from positive \$7.3 million to negative \$3.6 million.

Turning to our liquidity and financing, we had a net cash outflow of \$6.9 million during the first quarter and we ended up with \$39 million in cash on-hand. The cash outflow was driven mainly by a buildup of working capital. The CWI dividend was consistent year-over-year, however we expect decreases for the remainder of the year.

Our cashflow from financing activities were lower year-over-year due to a deferral of one principal payment on the Export Development Canada term loan and we drew on our credit facility.

COVID-19 has dealt us new challenges which we have been dealing with since early March, and that we expect to persist through the end of the year. The majority of our businesses have now reopened and we are seeing demand beginning to pick up, albeit modestly.

We have taken several steps to improve our liquidity, and these actions to date have created approximately \$20 million in short-term liquidity to weather the economic impact of COVID-19. We are taking a structured and measured approach to secure liquidity for the short term, but thinking about refinancing for long term to fund our growth of HPDI and our other growth opportunities.

The actions taken to date, many of which we have communicated in press releases or at our AGM include a deferral of \$6 million in principal payments agreed by Export Development Canada, which is effectively a de facto extension of the term loan to 2022, a previously announced €5 million loan to one of our Italian subsidiaries by UniCredit under the Italian government stimulus program known as the Decreto Liquidità, salary and other compensation deferrals and reductions which we expect will reduce expenses by \$2 million during 2020, across the board spending cuts and capital expenditure reductions which are anticipated to reduce cash outflows by \$3 million during 2020. Wage subsidies from several governments in the jurisdictions we operate like Canada, Italy, the Netherlands, Sweden and the United States are expected to provide \$4 million in the second quarter.

In addition to the actions completed, we also expect new debt financing enabled by government programs in Canada and Italy, including a \$10 million bridge facility from Export Development Canada. We are also pursuing additional loans in Italy under the Decreto Liquidità. As discussed at our AGM, we indicated that we were working to secure bridge and long-term financing in the range of \$20 million to \$30 million. With the recent UniCredit loan and the EDC bridge financing, we are comfortable that this range is achievable. We are also in

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discussion with current lenders to potentially extend maturity dates on other loan obligations under mutually agreeable terms.

Over the next year, we will also continue to evaluate our sources and uses of financing to improve our cost of capital and align to the long-term growth needs of the Company. We are confident that our action plans will provide us with the necessary liquidity to meet our obligations as they come due and provide the capital to continue to grow our business.

Westport Fuel Systems is market ready, tested and gaseous fuelled vehicles have achieved scale in many market segments. With the potential of renewable gas to offer net zero carbon solutions, we are ready to be part of the economic recovery.

With that, I'd like to turn it back to the Operator for your 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 Eric Stine with Craig-Hallum Capital Group. Please go ahead.

Eric Stine - Analyst, Craig-Hallum Capital Group

Hi, David. Hi, Richard.

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Hi, Eric.

Eric Stine - Analyst, Craig-Hallum Capital Group

Good morning. Hey, great to hear your confidence in the balance sheet given the steps taken to date and some things you're targeting near term. I was wondering, you're two months into the quarter, about a month beyond where you've started to ramp back up in Italy, and I know that a lot of uncertainty and still the environment is—I mean just a lot of question marks. Anything,

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any details you could share about what you're seeing early days in Italy, markets where you may be seeing some relative strengths, that would be very helpful.

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Eric, glad to answer. Glad to follow up. It has been and continues to be a difficult time, as everyone knows, not just us. But we do see green shoots, and as we mentioned just a moment ago, that there are people coming back to life, consumers and industries also. As you know, going into the COVID crisis, we created a number of scenarios, surely like many companies did, and stress tested our liquidity plans against those scenarios. As we look at that, kind of looking backwards a little bit on what's actually unfolding, we see that we bounded the equation enough. Our worst case that we used is worse than it actually is right now, which maybe sounds not so optimistic, but frankly, we're pleased to see the market coming back and we think the actions being taken by governments have been very helpful, but we're not through this yet, and so that's where we come out saying so far, so good. We're pleased that our factories are open. We're pleased that our customers are reopening. We're pleased to get the orders from our OEM customers and see that order bank building back up, but there's a lot of time still ahead of us and it looks like a long road.

Eric Stine - Analyst, Craig-Hallum Capital Group

Right, right. Okay. I can appreciate that.

Maybe then just on China and Weichai, I mean your commentary here in the call is certainly differently and more optimistic than in the release itself, saying targeting something in 2020. I'm curious, what types of actions have you taken in the market, and I know that it doesn't change what you think that the growth curve looks like, but I mean, how does this set up that if we were to see a—the certification was granted, do you think this is a quarter or two? How do you think about when you may start to see activity and then that activity followed by a ramp in volumes?

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Yes, I totally get where you're coming from on the questions and we're making our efforts to understand as best we can what looks ahead for us in the Chinese market. We're confident in getting that certification. We've done all the things we need to do. The product is ready to

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launch. We need the certification, of course. We need that paperwork and we expect that will come. I don't know at what pace. We're hopeful it's any day now but we're in a wait and see mode.

In terms of the market dynamics though, I'm really encouraged about the opportunity. We have a great partner with Weichai Power. We're the strongest player in the market with natural gas engines already today with spark ignited product. Adding HPDI to the mix, it's a far superior productive spark-ignited product and we think the market is really ready for it.

Having said that, we also recognize like we went through in Europe with our lead customer there, there is a learning cycle for every fleet operator, every truck driver to try it out and get used to the new technology and get comfortable with it. We do think that the evidence, if you will, of the market uptick in Europe will propel the Chinese market even more. We also think that Weichai Power is a supplier of engines in our joint venture, Weichai Westport is a supplier of engines that can serve multiple OEMs and will serve multiple OEMs, and so we have that additional benefit.

Nonetheless, my expectations for this year are modest and my expectations for 2021 are quite significant. I'm looking forward to the launch curve that unfolds in front of us.

Eric Stine - Analyst, Craig-Hallum Capital Group

Got it. Maybe last one for me. Just if you could provide some details on the faulty, the pressure device, and I guess where I'm coming from is that that likely has some bearing on the insurance repayment. I mean, you clearly feel confident about that but also in the timing of getting that reimbursement, I think you're targeting 4Q.

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Absolutely. You never like to have these situations but in our business we have to react. I'm very pleased with the way our team has reacted. We identified the root cause, we fixed the root cause, we got new parts into production and we're working with all our customers around the world to replace those suspect parts that are in the field as quickly as we can.

In terms of the insurance recoveries, it seems pretty clear to us that we're in a good place and we'll have a good result, but necessarily we have to work with our insurer to secure those recoveries and to provide all the evidence and work through that process and that just takes time.

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I've had in my career, unfortunately, a chance to work on a number of actions like this at different OEMs and it always takes longer than you'd like with respect to getting the job done and getting the insurance recoveries, but at the same time this is just a, let's say normal part of business unfortunately that we have to go through from time to time. So, we see our way clear to the insurance recoveries and to providing good product for our customers.

Eric Stine - Analyst, Craig-Hallum Capital Group

That view that it always takes longer than you'd like, you're factoring that in when you talk about 4Q as the target?

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Absolutely. We have the discussion opened up with our insurer but we haven't been able to conclude it at this point in time. It's pretty early in the process. We've just started the process in the field so there's plenty of work to be done, but I don't think this is a multi-year process by any way, shape or form, so I think we can this year is very reasonable.

Eric Stine - Analyst, Craig-Hallum Capital Group

Okay. Thank you.

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Thank you, Eric. Good to hear you.

Operator

Our next question comes from Rob Brown with Lake Street Partners. Please go ahead.

Robert Brown - Analyst, Lake Street Partners

Hi. Good morning.

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DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Good morning.

Robert Brown - Analyst, Lake Street Partners

I just wanted to clarify kind of on the automotive side the OEM versus the Aftermarket recovery expectations. Have you seen order flow start to return from the OEM side, and I guess which one do you sort of see ramping more quickly, and sort of your view on how those two markets recover?

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Yes, I think it's pretty clear from what we've seen already and just thinking about the marketplace that the trucking industry in general around the world has a demand that doesn't fluctuate nearly as much as what consumers do. On the trucking side, we need to move freight and one of the things I was contemplating recently is that typically in an economic downturn like we're certainly having now and we'll have for some time, truck fleets do push off orders and don't buy as many trucks as they were originally planning to conserve some of their capital in kind of tough times. But my expectation is that when they push up those orders, they are pushing orders off of diesel trucks and they're keeping or maybe increasing their order of LNG trucks. With Germany, putting in place or extending the tax exemption for natural gas trucks in Germany, there are big economic incentives and we already know that our trucks provide a lower total cost of operations even absent those road toll incentives and purchase incentives, just based on the fuel price.

So from my perspective, while the market for trucking may decline overall, have some softness that will have some interim, short period of time, hopefully, the demand for our products I think could actually and we expect to grow and we're seeing signs of that.

On the passenger vehicle side, this really gets to family budgets. Basically, people taking their cars to a local workshop and having it changed from gasoline only to a biofuel with natural gas or propane, this is an individual decision of the consumer. The consumers need to see that the economy is coming back, they can go out to dinner again, their job is retained. These are real individual aspects of budgets and so forth.

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At the same time, I think a countervailing force there is that basically our products are purchased in markets around the world because of the money they can save on fuel. We think there is a balance there that will be achieved and we will have a good business going forward, but it's really hard to judge it right now until we truly get into, I'll say the normal range of recovery that is just starting to unfold right now in markets around the world.

Robert Brown - Analyst, Lake Street Partners

Okay, good. Thanks for that clarity. Then on the CWI side, it was down in the quarter, but what's your visibility there of how have those demand trends stabilized here into the most recent months? Have you seen that come back or is that still quite uncertain?

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

We see a little bit of softness, but I think much like the comments I made regarding commercial vehicles in Europe, the same thing plays out in North America. As an example, UPS placed this large order last year talking about their view of natural gas trucking, and from what I understand in the marketplace, people aren't backing away from that. They recognize and done years of work to decide what kind of technologies they want to apply in the marketplace. The Waste Managements in the world and other key customers of ours continue to be keen to have our product in their portfolio and in operation for their fleet.

I do think there is some softness, if you will, in transit buses. As I've mentioned previously, have nothing to do with COVID, where basically, electric buses have made some inroads and so that puts pressure on our transit side of the business. Nonetheless, I think as people try out those technologies, natural gas and transit will continue to be an important part of the mix.

We see some softness just based on the general economy and some delays and so forth, but not so significant in the grand scheme of things, we believe.

Robert Brown - Analyst, Lake Street Partners

Okay. Great. Thank you. I'll turn it over.

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DAVID M. JOHNSON speaking
Chief Executive Officer, Westport Fuel Systems

Thanks, Rob.

Operator

Our next question comes from Colin Rusch with Oppenheimer and Company. Please go ahead.

Colin Rusch - Analyst, Oppenheimer and Company

Thanks so much, guys. Can we talk a little bit more about the details on this EDC facility? Can you talk about any sort of covenants you are anticipating, collateral, including restricted cash, that will be associated with that line?

RICHARD J. ORAZIETTI speaking
Chief Financial Officer, Westport Fuel Systems

Hi Colin, it's Richard. Regarding security and collateral, it's going to the same one that is already in place on the existing term loan, so nothing really changed on that. It's a very friendly loan. It's going to be prime plus 3%, so it comes at a time that's very helpful to us and the EDC has been a big supporter of clean tech and has been in our corner right from the beginning, as can be seen by the deferral or the extension, effectively, of the term loan.

Colin Rusch - Analyst, Oppenheimer and Company

Okay.

RICHARD J. ORAZIETTI speaking
Chief Financial Officer, Westport Fuel Systems

We hope to get it announced shortly. We're just going through the paperwork because of all the security. Just the way the nature of some of our loans that we've done in the past, it's a little bit tricky of where we're attaching security in different jurisdictions, but that's the only thing that's really holding it up right now.

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Colin Rusch - Analyst, Oppenheimer and Company

Okay. Can you use that capital across the organization, or is it really going to be restricted to the China business?

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

It is mainly dedicated towards investing in HPDI and working capital in the Parent. That's where the money is going to be spent. With regards to the rest of the business, we're using debt financing mainly through Italian banks right now, which have been even more lucrative. They're sub 2% cost of borrowing.

Colin Rusch - Analyst, Oppenheimer and Company

Okay, got it. Can you talk a little bit about the dynamics on inventory levels and sell-through for both the aftermarket kits and the DOEM business. I think one of the concerns is really around having to work through the existing components and kits that are out there. Do you have a sense of how many months of inventory are in the channel at this point and kind of the order pattern that you're seeing right now for incremental business?

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Actually, let me talk first about DOEM. I think this is a very interesting kind of dynamic to understand. So, our DOEM business, delayed OEM business as you know, is basically retrofitting zero-kilometre brand new cars that come from OEMs, as they come from the factory before they go to the dealer. They're really a great business for us.

What we see right now is that basically the vehicles that were on ships and in transit from our customers in Asia are still coming. The pause, if you will, and the drop in the market for us and operations for delayed OEM is still in our future. We're running quite strongly. There was a backlog because we shut down for a little bit more than a month in Carasco and as soon as we opened, there were all sorts of vehicles ready for us to retrofit. That's going plus or minus close to full tilt for us on the delayed OEM side.

On the kit side, we're shipping kits out to customers around the world. Basically, I would say inventory levels weren't particularly out of line and but we had this pause of our operations of

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producing kits and we had pause at the workshop and distributors around the world. I would say these were largely coordinated, so we don't see any specific buildup of inventory or drought of inventory. This is what we've been watching very closely because, of course, we're not going to sell more until that are sold, also with the dealers and distributors around the world and workshops around the world. That order flow is starting to come back and giving us some encouragement that the market is reopening and customer is getting back to, let's say, normal behaviour, that will let us have the material flow that is something that is good for our business and that we can manage and keep up with.

Colin Rusch - Analyst, Oppenheimer and Company

Perfect. Then on the supply chain side, you guys have been pretty proactive in terms of getting components. Are you seeing any issues or delays on incremental component supply as you start to ramp up again?

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

This is another area where I think both through our efforts, as you mentioned, kind of when China shut down first and we had supplies from China that we had to find alternatives and accelerate shipments and things like that, we did that. That worked well, kind of leading into our own shutdown.

Then a lot of our supply base for our, especially Italian operations but also our Dutch operations, are local and they're in the area. And so they had the same kind of experience, if you will, with respect to shut down. Overall, we have not had significant supply chain disruptions. There's always something to work on for our supply chain team, but nothing that we haven't been able to mitigate or that caused us any significant, let's say material consequence in our ability to work for our customers.

Colin Rusch - Analyst, Oppenheimer and Company

Okay. Thanks, guys.

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DAVID M. JOHNSON speaking
Chief Executive Officer, Westport Fuel Systems

Thanks, Colin.

Operator

Our next question comes from Sameer Joshi with H.C. Wainwright. Please go ahead.

Sameer Joshi - Analyst, H.C. Wainwright & Co.

Good morning. Thanks for taking my questions. Just a clarification on China. You mentioned that the testing was done, but the certification was pending. Was the tests according to the results that they expected and is the certification delayed because of any technical issues?

DAVID M. JOHNSON speaking
Chief Executive Officer, Westport Fuel Systems

There are no remaining technical issues, Sameer. We passed all the tests. They confirmed we passed all the tests. It really is, as we understand from our side, within the bureaucracy of the Chinese ministries to process the paperwork and get the certifications out. I can't begin to explain what that process looks like and how long it will take. Seems to all of us on the outside it should be quick, but here we stand waiting for their certification. I do expect it to come. I do expect it's just bureaucracy, but it's really hard to put a bead on. Okay, so how long? Is it a week? Is it a month? What is it?

Sameer Joshi - Analyst, H.C. Wainwright & Co.

Right. Understood. Okay, thanks for that. As far as the field service campaign goes, is this just the cost of replacing the units, or is there any associated liabilities that you expect or may already have incurred?

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DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Yes, it's just the cost of the replacements basically. It's a fair bit of labor to make the replacement component in the field. We have to go to the vehicle and make the replacement. That's the primary cost that we see, and frankly, and fortunately we have no field incidents so there is no liabilities in that regard and we're looking to keep that track record.

Sameer Joshi - Analyst, H.C. Wainwright & Co.

Okay, good to know. Then one just last clarification on the SG&A costs, which were lower by \$5.8 million, of which \$1.8 million are related to the one-time costs, but then how are the \$4 million of the remainder distributed between the lower compensation costs and the favourable legal claim settlement? I'm just trying to understand, how much of these is going to be ongoing and what is one-time?

RICHARD ORAZIETTI speaking

Chief Financial Officer, Westport Fuel Systems

Could you repeat your question again?

Sameer Joshi - Analyst, H.C. Wainwright & Co.

Yes. The SG&A costs were lower by \$5.8 million, and around \$4 million of those can be attributed to lower compensation costs and favourable settlement of the legal claim. What was the legal claim amount?

RICHARD ORAZIETTI speaking

Chief Financial Officer, Westport Fuel Systems

The legal claim, it was roughly about \$400,000 and we had accrued more for that historically because we managed to settle for a smaller amount, so that one goes away. Then what was the second one?

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Sameer Joshi - Analyst, H.C. Wainwright & Co.

Yes, so I was trying to understand how much of this lower compensation costs will continue into second quarter and maybe third quarter.

RICHARD ORAZIETTI speaking

Chief Financial Officer, Westport Fuel Systems

The lower compensation costs will definitely probably continue to about August. In terms of the wage subsidies that we get in Italy and Canada, those have been extended until the end of August 31st, so almost there. It really depends on the length of the pandemic, but right now it's almost all of the third quarter.

Sameer Joshi - Analyst, H.C. Wainwright & Co.

Got it, okay. Thanks. I'll turn it over.

RICHARD ORAZIETTI speaking

Chief Financial Officer, Westport Fuel Systems

No problem.

Operator

Our next question comes from Jeffrey Osborne with Cowen and Company. Please go ahead.

Jeffrey Osborne - Analyst, Cowen and Company

Hey, good morning. Most of the questions were asked, but I'm trying to get a better understanding of your dialogue with Weichai. Clearly you're waiting for your certification. You seem frustrated that it's not in. Is Weichai actively marketing the vehicle or the truck engine, etc., expecting an imminent receivable of the certification, or are all wheels not in motion until that is received?

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DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Yes. I would say—Hi, Jeff, good morning. I would say very clearly that Weichai, our joint venture and our joint venture partner Weichai Power are working with our customers, the vehicle OEMs to prepare the field, if you will, because obviously when you prepare the HPDI engine that includes a number of components on the engine, there are quite a few components on the vehicle. As an example, the tests that were run that achieved that lead to the certification include vehicle tests that we've been doing with our customers. I would say that ground is pretty well established and ready. It's just a question of, no one can order until you have a certification, and so we need that certification so we can take the orders from our customers and the joint venture can place those orders with us for the components.

Jeffrey Osborne - Analyst, Cowen and Company

Got it. Then a couple of people asked about different end markets for you in order strength or lack thereof. Is there a way instead of playing the game of asking each one separately? Is there a way you could say, of all the end markets you sell to, which one has recovered the quickest or has the best visibility for you and which one is the worst?

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

What I would tell you is that—let me start with the kind of struggling part. The struggling part is in India. I'm really bullish about that market in general, but they've had a very long shutdown and I think it's really challenging to reopen that business and to get back on our feet there.

But on the other end of the spectrum, on the strength of our business, I'm really encouraged by what's happening in Europe with respect to support by the governments and also order flow from our customers with respect to specifically HPDI. In the end, we won't get the growth that we were hoping for in this year, just because of COVID, but I see significant strength and I'm continuously compelled by the business opportunity. And frankly the need, I think you might have caught it in my opening remarks that my view is as in tough times OEMs, like the ones I've worked for before and like the ones that are our customers today have to dial back on their CapEx investments, just like we are. When they do that, they're going to look for more pragmatic and practical solutions and I think that's us. I think it bodes well for us and we're seeing that already as the fleets place their orders with our lead customer in Europe and as those orders come on to us.

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Jeffrey Osborne - Analyst, Cowen and Company

Got it. Thank you. That's all I had.

DAVID M. JOHNSON speaking Chief Executive Officer, Westport Fuel Systems

Thanks, Jeff.

Operator

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

DAVID M. JOHNSON speaking Chief Executive Officer, Westport Fuel Systems

I want to thank everyone for joining the call and really appreciate your time and questions.

As we look at our business, we recognize clearly this is a tough time and we've been very focused on making sure we could protect our employees and our team members; their health and safety has been paramount. We think overall that has worked well and we're happy to be back at work, and we're looking forward to the economic recovery as it unfolds and we're poised with liquidity we have to get through this period and continue to deliver for our customers and help get the world to a lower carbon transportation that's truly economic, affordable, and available now.

Thanks everyone for your time. Have a good day.

Operator

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