

Conference Call Transcript

Third Quarter 2022 Results Conference Call: November 8, 2022

Operator

Welcome to the Westport Fuel Systems Third Quarter 2022 Results Conference Call.

As a reminder, the conference is being recorded.

After the presentation, there will be an opportunity to ask questions.

I would now like to turn the conference over to Ashley Neull, Senior Director of Investor Relations. Please go ahead.

Ashley Neull speaking

Investor Relations Representative

Good morning everyone. Welcome to Westport Fuel Systems Third Quarter 2022 Conference Call, which is being held to coincide with the press release containing Westport Fuel Systems' financial results that was distributed yesterday.

On today's call, speaking on behalf of Westport, is Chief Executive Officer, David Johnson, and Chief Financial Officer, Richard Oraziotti. Not speaking today but joining us on our call is Bill Larkin, our incoming CFO, who will assume the role following Richard's departure on November 30.

Attendance on this call is open to the public 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.

With that, I'll turn the call over to you, David.

David Johnson speaking

Chief Executive Officer

Thank you, Ashley, and good morning everyone.

I'm pleased to be with you today to discuss our third quarter. Once again, our team delivered solid results as we continue to execute our strategy and showcase our pioneering hydrogen HPDI technology to a wide audience amid the ongoing challenging macro environment.

We continue to work through the industry felt headwinds and feel both prepared and poised to grow into the future. We believe that strong LPG price advantages, continued expansion into new markets, supportive global emissions reductions requirements, and further OEM conversations about hydrogen HPDI will drive growth and profitability.

We remain committed to our announced \$1 billion revenue and profitability goals but also recognize that, due to the headwinds we've faced so far this decade and which we'll continue to face for at least the near-term future, the time to achieve these goals will be later this decade. The environmental, economic, and regulatory requirements will not stop or wait, and Westport is well-positioned to respond.

Today I'll be walking you through an update from our hydrogen HPDI roadshow where we've been promoting our technology at important industry and government events. I'll also dive into our recently announced Scania test results to clarify the import of what we've achieved. I'll discuss the rise of liquid biomethane, highlighting its growth particularly in Europe and its increasing usage in heavy-duty transport, and why Westport stands to benefit. Finally, I'll walk you through our independent aftermarket business, where we see recovery through this year which is being bolstered by the continued price advantage of LPG in many markets.

In Q3, we delivered revenues of US\$71 million, slightly lower than Q3 last year. As indicated in prior quarters, the Russian market has been historically important for Westport through both our aftermarket and OEM channels. Now with the war in Ukraine, the sanctions on Russia, and in combination with a weakened euro and high natural gas prices in Europe, we've been heavily impacted. If we were able to set these aside, our business would have grown by 15% in the third quarter. Absent changes in foreign exchange, our revenues grew by 10%. We also

Conference Call Transcript

Third Quarter 2022 Results Conference Call:
November 8, 2022

continued to experience the impacts of rising inflation, supply chain constraints, higher utility costs, and fuel price volatility that have weighed heavily on our industry.

As many of you know, we are the only Company with the technology to use diesel type combustion with LNG and biomethane, and there are thousands of trucks on the road today using our technology. Taking this a step further, our fuel system technology paves the path from natural gas and biomethane today to green hydrogen tomorrow. We were thrilled to continue to inform both industry participants and policy makers about our unique capabilities and the advantages of hydrogen HPDI with our Class 9 demonstrator vehicle at multiple industry events in Europe and North America.

It isn't a surprise that as populations grow and economic development continues, we'll need to move more freight. Both the industry participants and the policy makers agree - the numbers of trucks on the road will grow and the performance and cost effectiveness of lower carbon solutions will become increasingly critical. We truly believe that HPDI is the solution today and for the future.

Speaking more broadly about our business, fundamentally, the outlook remains strong. The demand trends for affordable mobility options that reduce emissions are encouraging and we're seeing regulatory and policy support for options that utilize zero carbon fuels like hydrogen and biomethane. We're capitalizing on this now with the advancements we have made with hydrogen HPDI and the further recognition of what HPDI technology can achieve today with natural gas and liquid biomethane in addition to the work we're doing developing fuel systems to respond to future regulations, including the pending Euro 7 standard.

I wanted to quickly take the time to reiterate our three-pronged go-forward strategy as a Company and how we are positioning ourselves for the future. We'll drive sustainable growth in our existing markets through a diversified portfolio of technologies, products, and services. This will be seen across all our business units. Second, we aim to unlock new and emerging markets through the delivery of cleaner, affordable transportation solutions. Third, we'll continue, as we've done in the past, to drive operational excellence and maintain our reputation as a Tier 1 supplier with enhanced quality and reliability.

Historically when the word hydrogen has been used in relation to on-road transportation, only fuel cells come to mind. We're challenging this narrative. The future requires many options, including solutions' best fit for certain applications based on factors like distance, payload,

Conference Call Transcript

Third Quarter 2022 Results Conference Call:
November 8, 2022

durability, and affordability. Our technology is the solution for using zero carbon hydrogen effectively in many applications with the required performance at an affordable price.

We're having these conversations now, including unveiling our hydrogen HPDI fuel system equipped Class 8 demonstrator vehicle at IAA Transportation 2022 in Hanover, Germany, one of the largest commercial vehicle conferences in the world. Further differentiating hydrogen HPDI from other technologies is the ability and opportunity to use existing manufacturing infrastructure, a key factor in the near-term adoption of sustainability solutions and a discussion point with all OEMs at the Hanover show. Minimizing investment, both public and private, on the path towards decarbonization is a key component of our ability to achieve real change quickly.

OEMs are taking notice. We've demonstrated that our technology achieves better performance than diesel engines with near zero CO₂ emissions, all while utilizing existing already paid for manufacturing infrastructure. The interest in our solution continues to grow and IAA was a major stepping point in highlighting our technology to leading industry participants. The recognition and momentum around the product are growing, and so like many others, our excitement is growing.

In our discussions with global OEMs at IAA, it was clear they are beginning to understand that Westport's hydrogen HPDI fuel system solution addresses the portion of the market not addressed by electrification and does so in a more affordable way than a fuel cell. OEMs recognize that total electrification of all applications is not possible and utilizing internal combustion engines is a compelling option.

The tide is turning, and the conversations are shifting. The cost realities and engineering limits for electric solutions for heavy-duty applications are sinking in with OEMs. We remain committed to the idea that there will be a full suite of options in the future, but it's becoming strikingly clear that electric doesn't meet the needs of heavy-duty long-haul transport, while hydrogen HPDI does.

Following IAA, we spent time in Brussels and Washington DC, where we had policy makers and OEMs looking more seriously at internal combustion engines and alternative fuels and recognizing these will play a larger role in the solution for a lower emissions future. In Brussels, we presented our hydrogen HPDI fuel system to key policy makers, highlighting its ability to substantially reduce CO₂ emissions in alignment with EU decarbonization goals. Becoming part of the conversation now is important as work is being done to shift sentiment given that

internal combustion engine technologies weren't being recognized as part of the solution for our future.

It's our hope that the EU Commission and member states prioritize the availability of green hydrogen for the transport sector in the coming years and support engine technology advances that will be key for the development of the whole hydrogen transportation sector. Our message is clear: the lowest cost CO₂ abatement is using internal combustion engines fueled by HPDI technology, representing the most cost-effective pathway to deep decarbonization of long-haul road freight.

In Washington DC, we participated in the Hydrogen Americas Summit, exploring the topic of hydrogen mobility applications. One of the focal parts of the discussion was exploring opportunities for widespread mobility decarbonization through hydrogen combustion, an area in which hydrogen HPDI can take the lead for heavy-duty transport. Every time we get in front of industry participants and policy makers, it's a win as we advance our story and highlight our lower cost solution for using advanced internal combustion engines with hydrogen to make a long-term contribution towards decarbonization.

Engines equipped with our fuel system provide a superior combination of attributes as compared to fuel cell systems, diesel-fueled engines, and spark-ignited IC engines, including greater efficiency, higher power density, as well as lower total cost of operation, TCO. We think we have the solution for hydrogen utilization in heavy-duty transport and remain committed to spreading our message and educating potential OEM customers on the unique and significant potential our technology brings.

As our analysis has made clear and as industry observers have noted, IC engines fueled with hydrogen or biomethane can achieve equal or greater CO₂ reductions as compared to fuel cells while preserving manufacturing and capital investments. Our hydrogen HPDI fuel system offers more power, more torque, and more efficient use of hydrogen and therefore the best opportunity for hydrogen IC engines in real-world usage.

Biomethane and the growth we've seen this year in usage in heavy-duty transport is an area we're excited about as 100% biomethane in HPDI achieves 100% well-to-wheel CO₂ reductions. Let me say that again: HPDI with 100% biomethane achieves 100% well-to-wheel CO₂ reductions. As the share of bio-LNG increases and the size of the deployed fleet increases, the total CO₂ reductions well-to-wheel accumulates rapidly. Continuing this momentum is key to mitigating the full effects of climate change, and the speed of mitigation is paramount.

Conference Call Transcript

Third Quarter 2022 Results Conference Call:
November 8, 2022

With the increasing substitution of renewable fuels like biomethane, our products can further decrease the greenhouse gas impact of transportation, and they do so much more affordably than battery electric vehicles, for example. HPDI with natural gas and renewable natural gas works, and it works well. It's available now and it can help lower operating costs while helping fleets achieve their carbon reduction targets.

Take note of what's happening in Europe right now: support for renewables and biometh continues to increase in the wake of the EU energy crisis. In the third quarter, the European Parliament voted to increase the use of renewable energy from 40% to 45% while a bio-based joint undertaking is estimating to allocate \$2.4 billion of private investment in biometh infrastructure by 2024.

Why all this talk about biomethane, you might ask? Because biomethane is today's hydrogen. It's available, it reduces greenhouse gases, it's affordable, it's scaling right now, and HPDI works today with biomethane and hydrogen tomorrow.

Development and testing of our hydrogen HPDI fuel system solution is a key step to providing our customers with a pathway to significant emissions reductions, and we have projects underway now that I want to provide an update on.

We recently announced impressive test results from our joint demonstration program with Scania. As you know, we applied our hydrogen HPDI fuel system to Scania's 13-liter CBE1 platform, Scania's next generation, best-in-class engine intended for Euro 7 on-highway emission standards. Test results using our hydrogen HPDI solution, which requires a limited redesign of the cylinder head and no redesign of the pistons, external gas exchange system, or crank case ventilation system show performance with peak brake thermal efficiency of 51.5%. This is complemented by a 48.7% brake thermal efficiency at road load conditions.

This is a significant achievement, given that the 50% brake thermal efficiency mark with diesel has been seen as the industry's loftiest goal, and we're able to eclipse this number by 1.5 percentage points, truly validating our technology. In addition, we've demonstrated that hydrogen can be combusted at the same compression ratios as the diesel engine uses without NOC limitations that all SI hydrogen engines are struggling with.

The fact that we've achieved higher BTE over and above best-in-class engines simply by changing the fuel system while retaining the engine architecture and the on-engine HPDI fuel system components demonstrates the tremendous value and best-in-class performance that

Conference Call Transcript

Third Quarter 2022 Results Conference Call:
November 8, 2022

HPDI offers. What further excites us is the strong potential for industrialization and a commercial product launch. This isn't just a laboratory test. Hydrogen HPDI has all the ingredients to be turned into a product appreciated by truck drivers and fleet owners.

The feedback from the announcement has been significant. OEMs have been reaching out to us. We remain very optimistic that the compelling benefits of hydrogen HPDI will lead to commercial availability later this decade. We're proud to partner with Scania for this demonstration program and are looking forward to next steps.

In addition to our work with Scania, we also have a program underway with TUPY and AVL, aimed at combining advanced material and casting technologies with hydrogen HPDI. We anticipate being able to detail the results of this collaboration late in the first quarter of next year.

Just a reminder, Hydrogen HPDI offers low TCO, nearly 20% lower than a fuel cell vehicle just within five years and 580,000 kilometers. For the truck customer, it's a lower upfront acquisition cost with a proven design and durability. For the OEM, it's a familiar product and the ability to reuse substantial investments that have already been made in power train manufacturing and supply chain.

A nearly 20% reduction is a significant number and is steering conversations with more potential OEM partners, as is the opportunity to avoid new investments in fuel cells, batteries, and motors, and to reuse existing engine manufacturing assets. The results from the work we continue to do in these projects are informing our current customers and other industry players, and importantly are bringing us new potential OEM customers.

Now switching focus to the light duty LPG market, despite the headwinds which I discussed earlier, we're seeing strong demand and higher sales in key markets like Poland, Algeria and Peru. The large and increasing price advantage of LPG compared to petrol is driving our results also in the Netherlands, Italy, and Turkey. We're implementing price increases to mitigate the effect of inflation. To date we have achieved some success as margins grew slightly in the quarter. Surely, we have more work ahead of us since there's no sign that inflation is going away.

Fuel and geographic diversities are important core aspects of our overall offering. We can pick up market share in areas where the spread between petrol and alternative fuels is favourable. This includes growth in new markets like Thailand, Peru, and Bolivia, all emerging markets with

regulations emphasizing the need for cleaner transportation. In Peru for example, we're seeing a growth trend emerge. The price of LPG compared to gasoline is nearly \$0.70 a liter cheaper. This is a significant spread in a cost-sensitive market.

In India, despite the recent spread narrowing between CNG and petrol, the overall trend continues to be positive. Currently in the Indian market, the average running cost of a CNG-fueled vehicle has jumped from 1.2 rupees per kilometer to now 2.6 rupees per kilometer, but the running cost of gasoline-fueled vehicles is nearly double that at 5.1 rupees per kilometer. This favorable operating cost advantage for CNG supports our positive outlook for our business in India; in fact, at IAA, we met with several Indian OEMs who expressed interest in many of our solutions, including HPDI with methane and hydrogen.

The CNG filling network in India is expanding quickly with the government committed to have the number of filling stations increased by 10,000 by the end of the decade. Westport is poised to benefit from the impact as products we offer are used in all OEMs.

In summary, despite the macro headwinds that we face, high fuel costs and continued focus on carbon emissions create opportunities for our business as both industry operators and end customers look for lower cost options. What we're seeing in key markets with LPG is a clear example of that.

With that, I'd like to turn it over to Richard to go through our financials.

Richard Orazietti speaking

Chief Financial Officer

Good morning and thank you David.

Despite a challenging macroeconomic and geopolitical environment, I want to start by highlighting that fundamentally, Westport delivered better performance year-over-year in the third quarter of 2022; however, this is not readily apparent due to the negative impact of foreign currency translation from the weakening of the euro against the US dollar.

Total revenues for the third quarter 2022 decreased 4% to \$71.2 million compared to \$74.3 million in the same prior-year period, primarily driven by the weakening euro. Excluding the impact of foreign currency translation, total revenues increased by 10%, mainly due to a

rebound in the performance of our independent aftermarket business and the resilience and growth in the portfolio of OEM businesses, like delayed OEM, electronics, and hydrogen. This is a remarkable achievement given the significant challenges presented by the impact on sales volumes from volatile LNG and CNG fuel prices, sanctions on Russian customers, inflationary pressures on production, and continued supply chain disruption.

Loss from operations of \$10.9 million and a net loss of \$11.9 million for the third quarter of 2022 compared to a net operating loss of \$8.6 million and a net loss of \$5.8 million for the same prior-year period. The increase in operating loss was driven mainly by a \$2.6 million unrealized foreign exchange loss caused by the depreciation of the Canadian dollar and euro to the US dollar.

In our Adjusted EBITDA calculation, we exclude unrealized foreign exchange gains and losses to better reflect the underlying performance of our business. For the quarter, Adjusted EBITDA was negative \$4.5 million compared to negative \$1.4 million in the same prior-year period.

Adjusting for the unrealized FX loss in the prior-year period, the operating loss decreased by \$1.2 million year-over-year due to higher gross margins generated in 2022, driven primarily through increased sales in multiple OEM businesses and a more normalized sales mix of heavy-duty OEM systems parts. However, this better performance was offset by the loss of equity income from the termination and sale of the Cummins-Westport joint venture. The comparative result in 2021 included \$3.8 million in equity income from the joint venture.

Turning to our business segments, OEM revenue for the third quarter of 2022 was \$44.1 million, down 8% compared to the prior-year quarter. The 16% decrease in the average euro rate versus the US dollar for the third quarter was the main driver for the decrease in revenue; however, this was partially offset by higher sales in delayed OEM, fuel storage, hydrogen, and electronics. The impact of Russian sanctions was significant to our light duty OEM business as we generated approximately \$3 million less than the prior-year quarter. The impact from the Russia-Ukraine war on CNG prices also negatively impacted our sales volumes to the European market.

On a positive note, we saw an increase of light duty OEM sales to our Indian OEM customers for the period. In our heavy-duty OEM business, our sales volume to our initial OEM launch partner decreased 16% as compared to the same prior-year period but remains comparable on a year-to-date basis. This is a direct result of the unfavourable pricing differential between LNG and diesel in Europe. Higher LNG prices continue to cause a significant challenge to the demand

for LNG trucks, which is expected to temper our expected volume growth for our OEM launch partner until relative LNG prices return to a more favourable equilibrium.

The operating loss of \$7.3 million for the segment was comparable to the prior year due to better gross margin. Gross margin improved to \$4.7 million or 11% of revenues for the third quarter compared to \$3.1 million or 6% of revenues in the prior year. We saw a strong increase in gross margin driven by increased sales in multiple OEM businesses, as discussed before, and a more normal mix of HPDI systems components along with higher engineering services revenue.

In the third quarter of 2021, we had a higher sales mix of spare parts in our heavy-duty OEM business for warranty purposes that had lower margins. Improvement in gross margin was partially offset by the annual contractual price reduction to our OEM launch partner and a decrease in margin in our light duty OEM businesses due to a higher mix of sales to emerging markets that generate lower margins. Further, we continue to experience higher production input costs from supply chain challenges and inflation in logistics, energy, and other costs, which we have only partially been able to pass through to our OEM customers.

R&D expenses for the third quarter were \$6.5 million, slightly higher year-over-year. Our heavy-duty OEM R&D continues to focus on the development and demonstrations with potential OEM customers of next generation HPDI fuel systems, particularly with the use of hydrogen. Our light duty OEM R&D is focused on the development of new LPG fuel systems to meet upcoming Euro 7 standards.

Now turning to independent aftermarket, our business continues to be resilient in the face of macroeconomic challenges, with some positive encouraging trends. Revenue for the quarter increased by 3% to \$27.1 million compared to the prior-year period. Despite the significant impact of foreign exchange translation discussed previously, higher sales in Eastern Europe as well as in Algeria and Peru generated higher revenues year-over-year. Our focus on entering new markets and better competing in the markets we are currently in has enabled us to offset some of the loss of revenue to the Russian market from sanctions as a result of the Russia-Ukraine conflict, an impact of approximately \$4 million for the nine months to date in 2022.

Gross margin was \$6.6 million or 24% of revenues for the quarter, down slightly compared with the same prior-year period. The decrease in gross margin and gross margin percentage was mainly the result of higher production input costs occurring in material, transportation, and energy costs. Looking ahead, supportive LPG pricing is creating a promising demand trend for

Conference Call Transcript

Third Quarter 2022 Results Conference Call:
November 8, 2022

our business as Westport continues to address and serve markets for customers looking to save money on fuel costs.

Finally, I'd like to touch on liquidity. Our cash position decreased by \$11.7 million during the quarter to \$86.5 million. The decrease was primarily from net cash used in operating activities, modest capital expenditures, and repayment of \$3.6 million of debt. Our net cash flow used in operating activities was \$8.6 million in the third quarter, a decrease of \$5.8 million from net cash used of \$14.4 million compared to the same prior-year period. The decrease in cash used was driven by net changes in working capital, specifically in inventory. Our inventory levels have remained consistent since the second quarter of this year due to lower-than-expected sales volumes in Russia and the timing of delivery of some tenders in the independent aftermarket we anticipated in the third quarter that have been pushed to the fourth quarter, resulting in less of an inventory reduction than expected.

Our net cash used from investing activities in the quarter was \$2.5 million, primarily driven by our investments in capital expenditures for the expected growth in our portfolio of OEM businesses. Net cash flows used in financing activities were \$3.6 million for the third quarter as we continued to pay down our debt. We anticipate that we will pay down an additional \$3.1 million in the fourth quarter of 2022.

We remain focused and disciplined with our capital allocation and resources to execute our strategic and operating plans, and as such, improving profitability and liquidity. Although we saw some improvements in gross margin this quarter, we continued to see pressure on gross margin from inflation, and this is an area we continue to work to improve. Work continues with our customers in both OEM and independent aftermarket to implement price increases and other actions to improve our cost structure.

As David highlighted, we do see positive signals of growth in our business and a path to profitability as sales volumes grow in our heavy-duty and light duty OEM businesses. We are also optimistic about a continued improvement in profitability of our independent aftermarket business from the current tailwind of favourable LPG prices.

With that, I would like to turn it back to David.

David Johnson speaking

Chief Executive Officer

Thank you, Richard.

Before my closing remarks, I'd like to welcome Bill Larkin to the Westport team. Bill joined us in early October and will be stepping into the role of Chief Financial Officer following Richard's resignation. Having previously served as CFO of Westport Innovations and Fuel Systems Solutions, the deep industry expertise and capabilities he brings will be instrumental in realizing our growth and profitability goals.

Finally, as this will be Richard's last earnings call with Westport, I wanted to take this opportunity to thank him. Since he joined Westport, Richard has led us through a critical period and has positioned us for long-term success by strengthening our financial position. Richard has been a valuable member of our Management Team, and we wish him all the success in the future.

Before we close, let me touch on the written notice we received from NASDAQ last week regarding the Company not being compliant with the minimum bid price requirement. As we highlighted in our press release yesterday afternoon, we have 180 calendar days to regain compliance, or until May 2, 2023. Let me be clear - we fully intend to resolve the deficiency and regain compliance with NASDAQ's listing rule. Our operations are not affected by the receipt of the notification nor is there any impact on the listing of our common shares as we continue to trade normally.

Finally, let me close on these few final points. Westport delivers market-ready transportation solutions to OEMs, fleets, and individuals that deliver cleaner technology affordably right now. We remain encouraged by the long-term outlook for our business, and here are just three reasons why: number one, low and zero emissions transportation is our future and HPDI is our story, performance, efficiency, and even better with hydrogen provides an affordable solution to the market; second, the growth of our LPG business, which continues to address and serve markets which can't afford expensive electric and non-electric vehicles but is still looking for clean solutions; and third, the growth we're seeing and we expect to see in our business in India.

Conference Call Transcript

Third Quarter 2022 Results Conference Call:
November 8, 2022

As a supplier of advanced fuel delivery components and systems for clean, low carbon fuels, I'm confident in our ability to capture the additional market opportunities in front of us. All these factors give us optimism in our ability to meet the needs of our customers and advance towards our financial objectives.

With that, I'll turn it over to the Operator to open the call for questions.

Operator

Thank you. We will now begin the question-and-answer session.

Our first question is from Eric Stine with Craig-Hallum. Please go ahead.

Eric Stine speaking Craig-Hallum Capital

Good morning, everyone.

David Johnson speaking Chief Executive Officer

Good morning, Eric.

Eric Stine speaking Craig-Hallum Capital

Hey, so you mentioned obviously some interaction coming out of a number of the demonstrations you've done, conferences with some Indian OEMs on HPDI. I'm wondering if you can provide a little more detail outside of India, I don't know whether it's by number of

OEMs, accelerated talks with OEMs, anything just providing more details, and also how the greater brake thermal efficiency plays into those discussions.

David Johnson speaking

Chief Executive Officer

Yes, gladly, Eric.

I think we had the chance, as you know, to bring our truck to the Long Beach show back in May, ACT Expo, and then we had our truck at the Hanover show in September, and the combination of those events was really fantastic for us. Frankly, what we've been doing with the truck, the roadshow we referenced just a moment ago, has been very effective in terms of getting the truck in the hands of key individuals at OEMs around the world.

As an example, Hanover, I spent time with nine different OEMs at the senior executive level—sometimes CEO, sometimes CTO, and sometimes head of purchasing—so really a great audience. Many times, a large contingent would come from an OEM to our stand to talk to us and review our technology, and every time these were super useful conversations because I think in the grand scheme of things, our technology is not as well-known as it needs to be, and having the truck and going to the shows is really changing things for us as we sell and offer this important technology to the industry.

So those discussions, we mentioned Indian OEMs but also Chinese OEMs, European OEMs, North American OEMs, so we really cover all the main markets of the world. I also had the chance to spend a week in Japan recently meeting with OEMs there, so frankly I think we're covering the bases well and really getting a fantastic response.

Then we pile on, I would say, with our latest results with our project demonstration with the Scania engine. This is just a fantastic result. I can remember in my career many years that the U.S. Department of Energy had hundreds of millions of dollars of funding available for companies to try and show a pathway to get to 50% brake thermal efficiency, so just to kind of put things in perspective, most of the engines on the road today in all markets are on the range of 43% to 45% or 46%, maybe, brake thermal efficiency, and these are an improvement over where we were in prior decades.

The goal that the DOE has held for a long time has been 50% brake thermal efficiency from a diesel engine, and now companies like Scania are achieving that kind of really record performance for a diesel engine. So then for us to put their engine in the test cell, apply our HPDI hydrogen, HPDI system, feed the engine with hydrogen and achieve 51.5% brake thermal efficiency is really a tremendous accomplishment and just kind of sets the stage for what we'll achieve next in terms of the full map and the full capability of the engine as we continue those development projects with customers.

For us, this is a really, really important and exciting time. We've been in production with HPDI using methane as let's say as our molecule for a long time. These trucks are really well-received in the marketplace, but then to show that pathway that goes from fossil natural gas to biomethane and then hydrogen in the future is really compelling for OEMs around the world.

Eric Stine speaking

Craig-Hallum Capital

Yes, that's great, and good segue.

I guess my next question was just going to be how the data points which clearly—I mean, other OEMs are watching closely, how that gets others beyond your launch partner today to look at LNG as that interim solution, people who maybe were saying, "Look, I'm not going to move to HPDI utilizing LNG if I'm going to have to go to hydrogen in five-plus years." Are you seeing that movement, or is that something that you expect to see going forward?

David Johnson speaking

Chief Executive Officer

We're seeing it and we're expecting to see more of it is the short answer but let me just expand a bit.

Fundamentally, I'll tell you in the marketplace, there has been so much pressure from various constituencies around the world getting basically every segment, the media, investors, OEMs, fleets, all focused just on zero, and this idea of electrification being the shiny object that we all

should pursue and fuel cells are the technology that we all need to move to, and this idea even that hydrogen equals fuel cells has pervaded the industry in every market around the world, and so when we show up with hydrogen HPDI and hand people the keys to a truck, they can see that, no, there's another path that's really quite attractive from an economic standpoint.

All of the OEMs that we're talking to around the world have billions of dollars invested in engines, in internal combustion engine manufacturing, in the supply chains for that manufacturing, in the delivery and how that engine fits in the vehicle and then meets their customers, in the servicing of those engines around the world, so we have a massive installed base of capability, and manufacturing capability too, around the internal combustion engine, so when we show you can keep that internal combustion engine and make it run on zero carbon hydrogen and have all the power, actually more power, more torque, and more efficiency than you could have with a diesel engine or with a natural gas engine, that makes it very exciting.

The second step in the thought process is, well, given that there isn't a massive installed base of hydrogen and this technology that Westport provides also works on methane and biomethane, why wouldn't we go there now? Just on that point with respect to methane, we spent a fair amount of our discussion points with customers at Hanover, for example, helping them understand the public data that's out there regarding the efficiency and the capability of our product.

I think there's a significant number of constituents in the universe, in the public domain, again, media, investors, and customers, who think all natural gas engines are the same, that they all involve a spark plug, a reduced compression ratio, a three-way catalyst, and at the end of the day deliver 15% lower torque and dramatically less efficiency, and so we spent time at our events, and continue to spend time, even privately with OEMs of course, helping them understand that the product that we have in the market today with our lead OEM customer, the HPDI product preserves all of the capability of a diesel engine in terms of power, torque, and efficiency, and therefore in real-world applications and real-world testing and usage, it's delivering a 30% lower consumption of natural gas.

So whether it's natural gas or biomethane, reducing that fuel cost by 30% using HPDI as opposed to a spark plug is something that's not as well-known as it really needs to be, and so we're helping customers understand that and pointing to the data in the marketplace, and I think so now that combination of dramatically better fuel consumption figures, all the power

Conference Call Transcript

Third Quarter 2022 Results Conference Call:
November 8, 2022

and all the torque with methane, with biomethane and with a path to zero carbon hydrogen is super compelling for OEMs around the world.

Eric Stine speaking

Craig-Hallum Capital

Okay. Thanks, David.

David Johnson speaking

Chief Executive Officer

My pleasure. Look forward to seeing you soon.

Operator

The next question is from Rob Brown with Lake Street Capital Markets. Please go ahead.

Rob Brown speaking

Lake Street Capital Markets

Good morning.

David Johnson speaking

Chief Executive Officer

Morning, Rob.

Rob Brown speaking

Lake Street Capital Markets

I think you mentioned in your script some hydrogen revenue in the quarter or in the year. Could you kind of elaborate on the revenue you're getting from hydrogen at this point?

David Johnson speaking

Chief Executive Officer

Yes, so we have, let's say, two areas that I would call in the category of hydrogen. We've been talking a lot already this morning about hydrogen HPDI, and I would say our revenues right now with respect to that are really on the demonstration project, and I would say—I would categorize them as low single million-dollar figures with multiple OEMs and really in a cost recovery mode. We're basically partnering with them to demonstrate, like we did with Scania, our technology on their engines.

The other part of our hydrogen business is, I would say, going business. As part of our growth opportunities for the Company, we have been supplying hydrogen fuel system components to connect fuel storage, 700 bar and 350 bar tanks, to fuel cells, and so we've been doing that business through our GFI brand for more than a decade and we're seeing really great growth. We are in this day a leader with that technology, with products available to companies like Plug Power and other fuel cell makers in both North America and China, and increasingly in Europe as the European OEMs get their heads wrapped around how they're going to use fuel cells in their product mix, so that's a really important part of our business, a growing part of our business and keeps us very busy.

Rob Brown speaking

Lake Street Capital Markets

Okay. Great. Thank you.

Then you sort of alluded to a path to profitability. I know you don't give guidance, but what's your view on that trajectory? Can you be profitable in 2023, and what might that depend on?

David Johnson speaking

Chief Executive Officer

Yes, with respect to our profitability trajectory, and it's been, let's say, in evidence for quite some time that our JV with Cummins ended at the end of last year, and so we took this kind of step function reduction in our profitability trajectory, but we see this profitability growth that will get us to profitability, and that's where I talked about what we previously called our mid-decade goals being a little further out fundamentally, and so that kind of billion dollar revenue and 20% gross profit targets, we're fully committed to, but clearly after COVID, supply chain, and now a war in Russia, we've had some setbacks from the timetable, but nonetheless we see that coming.

It's fundamentally driven by growth, Rob, and so we need to see our HPDI volume growing, and the hydrogen story we're telling right now will help with that; but certainly we're also seeing now natural gas prices in global markets coming back down from the extraordinary peaks that they've seen in the follow-on aftermath, if you will, of the initiation of the war in Ukraine by Russia. So that whole dynamic and the change in landscape of flows of natural gas, with increased exports from the U.S., and building new natural gas pipelines, and LNG terminals and so forth, that takes time, and so we are seeing a decrease in natural gas prices and that will help our growth, and the growth is the key to our profitability.

Rob Brown speaking

Lake Street Capital Markets

Great. Thank you. I'll turn it over

David Johnson speaking

Chief Executive Officer

Thank you Rob.

Operator

The next question is from Amit Dayal with HC Wainwright. Please go ahead.

Amit Dayal speaking

HC Wainwright & Co.

Just quickly on the margin strength for the quarter relative to last quarter, is there anything unique this quarter (inaudible 0:43:17.5) last quarter, and then going forward, should we continue to expect the 16% level gross margins?

Richard Oraziotti speaking

Chief Financial Officer

Why don't I handle that one, Amit?

The biggest difference that we had, probably quarter-over-quarter, for sure there was increased performance in the portfolio of our OEM businesses, which are electronics and hydrogen. Our fuel storage did very strong, and delayed OEM. The biggest difference as well, which may carry forward is we had a large amount of a particular HPDI component that actually had a lower margin, and that was because of a replacement of the component, and that has now gotten much better, and so in terms of the performance with regards to margins in heavy-duty, that is somewhat improved, and so that should carry through somewhat. But in terms of modeling out a specific percentage, it does move around a little bit, Amit, but yes, we do expect a little bit of improvement, yes.

Amit Dayal speaking

HC Wainwright & Co.

Understood. Thank you for that, Richard.

(Inaudible 0:44:31.4) and a lot of macro challenges you guys are facing. In that context, what are the drivers (inaudible 0:44:43.4)?

Richard Oraziotti speaking

Chief Financial Officer

Hey Amit. I apologize. Amit, I'm really struggling to hear you. There seem to be a connectivity issue, perhaps with your phone. Is there something you could do on your end, because I can't get your question. I heard macro environment, but...

Amit Dayal speaking

HC Wainwright & Co.

Yes, I was just trying to say if there is any solution to this ForEx pressure.

David Johnson speaking

Chief Executive Officer

Well, I think just talking about foreign exchange, basically as a Company, we are very strongly naturally hedged. The vast majority of our revenues are in euros, the vast majority of our expenses are in euros, and so that does kind of cushion us against the bottom-line impacts of foreign exchange. Unfortunately, it doesn't do anything for the top line because we report in US dollars and so we have all those conversions that we do make, and so that translation of that business, about 70% of our business is in Europe, that translation, it will be what it will be, and

Third Quarter 2022 Results Conference Call:
November 8, 2022

so that's why we call it out when we announce our earnings and our revenues, because fundamentally our business is about 70% in Europe and that's the currency, but it is naturally hedged.

Richard, anything you want to add.

Richard Oraziotti speaking

Chief Financial Officer

No, I think you described it well. Our functional currency more likely than not actually is more the euro. The Canadian dollar is what we have as our main functional currency, and reporting in US dollars is something we do because many and most of our shareholders are U.S.-based, but it does create this distortion here because—and that was my comment in terms of the prepared comments. The performance of the actually underlying business was up 10%, and this was during a period of obviously a lot of turbulence in both the macroeconomic and geopolitical environment, so the Company actually did pretty good in this third quarter.

It's something that we have not decided, if there's no foreign exchange derivatives or instruments that we would use to modify that. It's an unfortunate part of our reporting that we've taken for investor purposes.

Amit Dayal speaking

HC Wainwright & Co.

Understood, that's helpful. (Inaudible 0:47:16.2)

Operator

I'm going to move on to the next caller, if that's all right. We seem to have difficulty hearing Mr. Dayal.

The next question is from Colin Rusch from Oppenheimer. Please go ahead.

Colin Rusch speaking

Oppenheimer & Co.

Thanks so much, guys.

Can you talk a little bit about the progress that you're making on engineering subcomponents for the hydrogen system? Obviously producing a vehicle is a big deal but getting ready for mass production is another level of preparation, so just curious how that's coming along.

David Johnson speaking

Chief Executive Officer

Yes, thanks for the question, Colin.

You're right that demonstrating a vehicle is a big deal. We're very happy about that, and fundamentally to do that, we've used off-the-shelf components that are in production today for our natural gas production products. So from our perspective, those demonstrators work great.

We fully recognize that there is some optimization and some development in validation cycle that we're proceeding with in this time so that we're ready for production hydrogen products. I do think those production hydrogen products are kind of in the '25 to '27 timeframe, and so because the normal cycle for OEMs is going to be a full development and validation of the calibration and the hardware, including both the engine, our fuel system, the fuel storage, the whole integration on the vehicle, and so that's kind of the cycle, but we continue to make progress and make investments which are relatively modest because our hardware is largely the hardware that we already have in production.

We expect some tweaks, as you can imagine. So for example when we develop the injector, we do CFD work to analyze the combustion system with hydrogen and how it's different than natural gas, and then we make modifications to the nozzle, and so we're already testing and developing different nozzle patterns that fit both with our customers' engines as well as with hydrogen fuel, and so that is, I would say, a normal part of our business but now a little bit of uniqueness relative to hydrogen.

Colin Rusch speaking

Oppenheimer & Co.

Okay, that's super helpful.

Then maybe I missed it, but can you just give us an update on how the HPDI 2.0 ramp in China is coming along and any signals that you're getting around inflection points on that in any way?

David Johnson speaking

Chief Executive Officer

Yes, thanks for asking.

Fundamentally we didn't talk much about it in the call so far. There is progress, we do see that, but we're really a bit gun shy about calling any timing on when that product might hit the market. Fundamentally, a good thing that we see globally is what I referenced earlier about natural gas commodity prices coming back down. That will help the equation because fundamentally product in China is going to be sold based only on TCO for the most part, and so we need that fuel price to come back down to make any natural gas product in China commercially attractive, and so that's happening.

Our customer has continued to do work to be ready to launch the product, and so we're anticipating that, but I don't have any timing that I can share with you other than to say there's work going on, and so they wouldn't be doing the work if there wasn't intention to go to market at some future date.

Colin Rusch speaking

Oppenheimer & Co.

Perfect. Thanks guys.

David Johnson speaking

Chief Executive Officer

Maybe I should just add, Colin, we actually are spending also a tremendous amount of our time and energy working with customers broadly in China with respect to the opportunity for hydrogen. Hydrogen in China today is already, I would say, like refueling infrastructure, more developed than the other market that I can see, so they have more than 1,000 hydrogen stations is the information that I've seen and heard about the Chinese market, and so that push towards hydrogen in China is very, very real.

You've seen a number of announcements perhaps of spark-ignited hydrogen engines, demonstrating and low volume and so forth. Of course, we see that with hydrogen HPDI, and this is what we're talking to the OEMs in China as well as other markets, of course, about is the potential to have a much more superior product with hydrogen HPDI: more power, more torque, more efficiency than is possible with a spark-ignited hydrogen product. So we think that's an important part of what we're doing right now that will pay benefits in the future.

Colin Rusch speaking

Oppenheimer & Co.

That's actually quite helpful. I appreciate the additional colour there.

Operator

The next question is from Jeff Rossetti with Cowen & Company. Please go ahead.

Jeffrey Rossetti speaking

Cowen & Co.

Good morning.

David Johnson speaking

Chief Executive Officer

Good morning.

Jeffrey Rossetti speaking

Cowen & Co.

David, you mentioned earlier you expect to release results from your AVL TUPY demonstration at the end of Q1, and I was just wondering if you could provide any findings, you might expect and how it might be differentiated from Scania, and if there was any update with testing with Cummins.

David Johnson speaking

Chief Executive Officer

Yes, sure. Glad to talk about those, Jeff.

First of all on AVL TUPY, we have an engine in test cell with our hardware, their engine, their "an OEM's engine with our hardware in it," and we're starting that development now and we expect to have some results. I would tell you in every case it's up to our partners, in this case AVL and TUPY, to make the decisions on what kind of announcements we can make, when, but we're hopeful to have some colour at least, if not some data, to offer the market in Q1, as we said.

What we expect out of that testing, I would say, is very similar to what we've found with other engines, and that is that basically the application of our HPDI technology in combination with hydrogen on an otherwise formerly diesel engine will offer about a 20% improvement in power, about a 15% improvement in torque, and about a 10% improvement in efficiency, and these are really important numbers. You don't typically get double-digit percentage increases in any of those parameters, let alone all three, but we've done this on a number of engines already,

some you can see on YouTube, some we talked about in our press release about our Scania work.

I would tell you we expect the same kind of increment and hopefully we can demonstrate even more through the contributions that TUPY is making with respect to the engine structure. Having greater engine structure in terms of pressure capability can improve the engine and then get more out of our fuel system as a result, so we're very much looking forward to bringing that development through the cycle and then sharing results when we can.

You asked also about Cummins, and that work is basically completed from our side. We've done the necessary studies that Cummins asked us to perform, and they are now evaluating where does hydrogen HPDI sit in their portfolio, and we look forward to some opportunity to do some more work with them.

Jeffrey Rossetti speaking

Cowen & Co.

Great.

I appreciate the detail you provided on your path to commercialization of hydrogen HPDI. Just wondering, I think you called out '25 through '27 as a potential timeframe for commercialization. Are there any milestones that you are targeting for, say, 2023 to put you on that path?

David Johnson speaking

Chief Executive Officer

I expect in 2023 you'll hear more from us with respect to developments like the kind we've already done—you know, the AVL TUPY news, for example. I expect there'll be more OEMs that will be testing our fuel systems on their engines. I expect with the OEMs that we've already worked with, like Scania and others, there will be next steps that we'll have a chance to announce, so I think you'll hear that kind of news from us in the coming quarters.

Conference Call Transcript

Third Quarter 2022 Results Conference Call:
November 8, 2022

Looking out further, I'm very keen on the opportunity to make some demonstration fleets, so fundamentally you've seen this in the fuel cell world - for example, Hyundai in Switzerland has been demonstrating fuel cells. There's quite a few fuel cell applications that have been announced, and so I think that same kind of activity for us would be quite straightforward.

As you saw with our demonstration vehicle that we showed in Long Beach and also in Hanover, this is a driving prototype. It tows 40 tons, so 80,000 pounds of freight. It drives very, very well and all on hydrogen, zero carbon hydrogen. Actually making demonstrator vehicles, there are some certification and exemptions and things like that, that we need to do, but I think that's the activity that maybe we'll be announcing some of that also in 2023 for deployment in '24, '25, '26, so this is basically the path that we're expecting.

Jeffrey Rossetti speaking

Cowen & Co.

Thanks very much.

David Johnson speaking

Chief Executive Officer

My pleasure.

Operator

The next question is from Chris Dendrinis with RBC Capital Markets. Please go ahead.

Chris Dendrinis speaking

RBC Capital Markets

Hi, thank you.

I just wanted to, I guess, hone in a little bit more on some of your comments around policy here. I think one of the bigger investor concerns out there is that most of the policy and incentive programs right now are focused more on the battery side of technology, so as it relates to your discussions in Brussels and Washington, what's the receptivity of policy makers to the technology that might not be exactly zero emissions, and I guess what's their understanding of the technology today?

David Johnson speaking

Chief Executive Officer

Yes, it's a great question, Chris, and I thank you for asking it.

We feel it's very important for us to carve out the time with the truck and our team to go and speak with and inform and educate policy makers around the world because fundamentally, even just two years ago, there was no idea, no concept, no discussion around internal combustion engines with hydrogen, primarily, I would tell you because most people, 99.9%, were thinking about a spark-ignited product which has tremendous challenges with respect to pre-ignition NOC and so forth because hydrogen is so combustible.

I would tell you that the basic mentality policy makers and much of the public domain is around if it's hydrogen, it must be a fuel cell, and so we're having to—we need to, it's our task to do so, educate people about the opportunity that we've unveiled and demonstrated in our test cells and with our demo trucks, and so that is what we're doing now.

I think in all my experience in the industry, regulators like to write regulations. Regulators write regulations in most cases for technologies that they know can be applied to achieve that regulation. This was the work of the U.S. DOE over decades has been let's go demonstrate this is possible so that the regulators can write a regulation forcing it to happen, and so whether it's a 50% BTE goal that they had for many, many years, and so that's kind of the, I'll call it the modus operandi of regulators is to write regulations for technologies that they know of and they know can be deployed.

Therefore, as we go to DC and Brussels and help policy makers understand this is possible - no, here it is, here are the keys, drive it, here's the data, here's the development path, this is when it will be ready - that will inform future regulatory making. That's our approach to the

marketplace and approach to policy, and fundamentally I believe they're going to be real happy about this and they're going to be willing to make those changes to regulations because the significant opportunity to decarbonize long-haul trucking, which is super, super hard to decarbonizes...

Let's just call it out, right, Tesla has had access to tremendous amounts of capital and yet their truck is still not out, announced four years ago, and why? Fundamentally because it's got a lot of batteries on it, it'll have less payload capability, it's going to be super expensive to acquire, and it's a super challenging application to electrify. It's not Tesla, it's about the physics, the economics and so forth, and so for long-haul heavy-duty trucking—and I'll go a step further, we talk—you know, we're a Canadian Company, there's a lot of mining in Canada.

We talk about mine haul trucks. These are super hard to decarbonize because they use so much energy and they run so many hours, and so they can't stop and recharge, so this is where we play. This is where we play, and helping regulators understand that will allow them to write regulations that then promote and encourage our technology to come to market, so we think it's a really important part of what needs to be done, what we are doing, and we expect it to be effective. It'll take some time, but it will be effective.

Chris Dendrinios speaking

RBC Capital Markets

Got it. Yes, thank you.

I guess maybe just switching gears here really quick, focusing maybe on some of the inventory levels, I think you had previously mentioned that you were looking to monetize some of that or draw it down and I guess have a maybe more efficient use of your working capital. Can you provide any updates on that process, kind of what are you thinking right now and maybe the ease of the ability to monetize some of that?

David Johnson speaking

Chief Executive Officer

Yes, so good question, happy to talk about our inventory.

For sure it's too high. It's not at the level that we wish to have and we expect to sustain, so it is an active effort on our part to move that inventory and reduce our levels.

I would tell you there's two fundamental drivers in that—there's a lot of drivers, of course, but two big elements. One element is on the electronics side. You all recall, I'm sure, how chips were in short supply and still aren't so easy to get, and we had a lot of our chip suppliers come to us and say, "Listen, we need to know exactly what you need and so please place orders now for material 18 months out, and you can't cancel these orders, you can't change these orders. We need to know, and you need to commit to it." And so we're sitting on quite a bit of inventory of chips. Every day we're working to get that last chip that's required to make that ECU or that controller that we need to make.

So moving to a more, let's say, normalized supply chain dynamic with respect to electronics will allow us to unlock on the order of \$6 million, \$8 million of inventory that's on our books right now just in electronics. So that's kind of a, I'll say, a perturbation of the market that's happened right now, whether you call it from COVID or inflation, or whatever those dynamics are that caused the supply chain to do that, we're just dealing with it and we expect to unwind that and monetize that inventory in electronics, as an example, going forward.

The other one is our HPDI inventory. Our HPDI inventory is higher than it should be, and that's because we haven't seen the growth volume in sales that we were forecasting, and so we were building inventory to—not inventory, but we have the pipeline full for a certain kind of volume expectation that was pre the war with Russia and Ukraine, and so as LNG prices have gone up and the volumes have been flattening, we've built an inventory in HPDI that we do expect to monetize, and that includes expectations on our part that we will move product to China with Weichai, and so those things, we still have on our list of things to do, and that will help us to unwind that inventory and turn it from inventory into cash.

Chris Dendrinis speaking

RBC Capital Markets

Got it. Thank you.

David Johnson speaking

Chief Executive Officer

My pleasure.

Operator

The next question is from Bill Peterson with JP Morgan. Please, go ahead.

Bill Peterson speaking

JP Morgan

Yes hi, good morning, guys. Richard, I just want to say it was nice working with you over the last couple of years, so good luck in your next endeavours.

On conventional HDPI—sorry, I can't even say it—last year you had some really nice growth in your lead customer in Europe, so I think you said they have a thousand trucks on the road or thousands of trucks on the road. I wanted to discuss what you're seeing in terms of reliability and uptime relative to diesel. You talked about some of the performance benefits, but I guess was the warranty issue related to that at your lead customer?

I'm trying to understand what the interest in these trucks could look like should nat gas pricing starts to normalize, if you can answer that, and then I guess to that second point about nat gas normalizing, the U.S. still actually is a relatively less expensive place compared to other places and diesel is in short supply, particularly in the northeast, so do you see additional interest maybe stemming from that spread? Thank you.

David Johnson speaking

Chief Executive Officer

Yes, great questions Bill. Thanks for joining us this morning.

With respect to the durability and reliability of our product in Europe, we have been on, let's say, a journey from the launch in 2018 through now and we have had a variety of challenges with the product along the way, but the team has done exceptional work to really stomp out those problems early and minimize the impact, and so right now in the marketplace, I would tell you that people are thrilled with the durability and reliability, and the primary reason for that is because fundamentally we've developed the system, we've solved the early problems, and the basics of the system are based on a diesel engine, so we're not asking the engine itself to do anything that it's not used to doing.

I guess just to contrast that, spark-ignited natural gas engines run hotter. They have challenges that diesel engines with our HPDI system don't have, and so we feel we're in a very good place.

The fleets love the product and really all that's tempering demand at this point in time is the high price of natural gas, and so as we see that commodity price come down, we need to see that commodity price flow through all the way to the pumps so that fleets can say, "Let me buy more HPDI-equipped trucks so I can deliver freight and do it with a lower TCO." So that's really the story there.

With respect to U.S. and natural gas prices, and frankly your point on scarcity of diesel, fundamentally in the marketplace for all of our products, the equation isn't so much about the price of natural gas or the price of LPG or the price of gas or the price of diesel, it's really about the delta between the two. Can I save money by using natural gas versus diesel? Can I save money by using LPG instead of petrol? It's the price differential between the two fuels. So when diesel gets scarce and diesel prices go up, that will help our natural gas and our LPG business as people look for alternatives.

I'll say it even more broadly, fundamentally in every market around the world, when energy gets more expensive, all energy—electric by the way, natural gas, petrol, diesel—when energy gets more expensive, people go looking for alternatives, and it's where there's that price differential that offers our customers a savings by using natural gas, biomethane, hydrogen or LPG, that's where we win because we're the gaseous fuel specialists.

Bill Peterson speaking

JP Morgan

Okay, thanks for that colour.

I think the next one is probably for Richard, and I asked this the last quarter too, but when we think about the cost and use of cash, OpEx, you should be getting advantages, I guess, on OpEx the same way with the USD relative to other currencies, but offsetting that you have inflation, so trying to understand how we should think about OpEx trajectory looking out over the next few quarters.

Then I think in terms of CapEx, I think you talked about maybe around \$15 million. It looks like you're going to be probably ending up a little short of that, but I guess, is this pushed into next year, or I guess any colour on how we should think about capital intensity as we're looking ahead to 2023 in terms of the use of cash? Thanks.

Richard Oraziotti speaking

Chief Financial Officer

Thanks Bill, and thank you very much. Much appreciated your comments before. It's been great working with you as well.

With regards to—yes, for sure on the foreign exchange, because a lot of our engineering is done in Canada, and so we did get the benefit of that. We're in a rationalization moment right now because we're quite well aware of our liquidity and trying to be responsible, we'll call it fiscally disciplined on that. Next year, I mean, we're in the neighbourhood between \$15 million and \$20 million. We're trying—we've got obviously a lot of investments in the future, and hydrogen being one of it, and we're doing some work on LPG for Euro 7, and then there's the natural increase of capacity for HPDI. We're trying to stay in that number, and the purchasing that we're doing is in euros predominantly so there's a little bit of an advantage there, but we are purchasing certain equipment from the U.S.

With regards to OpEx, we spent a little bit more money this year, probably in we're trying to promote HPDI and build awareness, specifically with hydrogen. There is, we'll call it, the sort of

Third Quarter 2022 Results Conference Call:
November 8, 2022

the education process that David referred to, and that's gaining a lot of actual interest within the industry that it didn't just come from us. Everybody, every major OEM is considering hydrogen ICE programs as well as part of their portfolio, and so there was a little bit of extra money that we had to spend there, but generally, our operating expenses will be more or less in line. If anything, we're tightening the belt as well as the year progresses.

Bill Peterson speaking

JP Morgan

Thanks Richard. Thanks for the colour. Good luck.

Richard Oraziotti speaking

Chief Financial Officer

Thank you, Bill.

Operator

This concludes the question-and-answer session. I'd like to turn the conference back over to Mr. David Johnson for any closing remarks.

David Johnson speaking

Chief Executive Officer

Thank you very much, and thanks everyone for joining our call this morning.

I think at the top line for our Company, we've been through a very challenging time and the challenges keep coming, but we keep making progress. Fundamentally, to think about our revenues being up 10% year-over-year on an absent foreign exchange, which is just a translation error, in the context of a place where we've got high natural gas prices, both CNG

Conference Call Transcript

Third Quarter 2022 Results Conference Call:
November 8, 2022

and LNG, a war in Russia, a constrained supply of LNG, I think there's a lot of people out there that can understand in 2025 and 2030 in Europe specifically, we need to make really big improvements in CO₂ of long-haul trucking, 15% by 2025, 30% by 2030, and everybody in Europe is thinking about how do we make those standards tougher.

When you think about a technology like hydrogen HPDI being able to offer a 98% reduction in carbon and do so very affordably that will have a huge impact on the fleet average for those fleets, so we really see a bright future ahead.

I appreciate the chance to speak with all of you today and field your questions, and I look forward to the chance to meet with investors at the Craig-Hallum conference next Thursday in New York City, and then we have an upcoming capital markets day that we'll do in Toronto on December 8, so look forward to continuing the discussion and helping you understand better the future for Westport Fuel Systems.

Thanks again 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.