

Westport Fuel Systems Inc.**Q2 2023 Conference Call**

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PRESENTATION

Operator

Good morning. My name is Myra (phon), and I will be your conference Operator today.

At this time, I would like to welcome everyone to the Westport Fuel Systems Q2 2023 Conference Call. All lines have been placed on mute to prevent any background noise.

After the speakers' remarks, there will be a question-and-answer session. If you would like to ask a question during this time, simply press *, then the number 1 on your telephone keypad. If you would like to withdraw your question, please press *, then the number 2. Thank you.

Miss Ashley Nuell, you may begin your conference.

Ashley Nuell — Senior Director, Investor Relations, Westport Fuel Systems Inc.

Good morning, everyone. Welcome to Westport Fuel Systems' second quarter conference call for the 2023 fiscal year. This call is being held to coincide with the press release containing Westport's financial results that was issued yesterday.

On today's call, speaking on behalf of Westport is Chief Executive Officer, David Johnson, and Chief Financial Officer, Bill Larkin.

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 on this call and our responses to certain questions may constitute forward-looking statements within the meaning of the US 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 — Chief Executive Officer, Westport Fuel Systems Inc.

Thanks, Ashley. Good day, everyone. I'm pleased to be with you to review our 2023 second quarter results.

Today, Bill and I will walk you through an overview of those Q2 results, also an update regarding our growing LPG business. And finally, I'll speak about our planned HPDI joint venture that we and Volvo announced in July, as this marks an important inflection point for Westport's HPDI business.

On a consolidated basis, Westport delivered record revenue of \$85 million, up 6 percent compared to last year.

In addition, we continue to deliver improving gross margins, both in dollar terms and as a percent of revenue.

This quarter's top-line record result was primarily driven by increased sales volumes in our delayed OEM, electronics and fuel storage businesses, and additional revenues in our independent aftermarket business due to increased sales volumes in Africa, Eastern Europe, and South America. These are partially offset by lower sales to our light-duty OEM customers in India and lower sales volumes in our hydrogen and heavy-duty OEM businesses.

Regarding sales volumes in our heavy-duty business, earlier this year, our European HPDI launch partner, Volvo, announced that they would launch new bio-LNG-fueled trucks with more horsepower, increased efficiency, lower emissions, and an extended driving range.

As is typical with new product introductions, we expected this model change to result in lower sales volumes leading up to the launch and higher volumes following the launch. We saw exactly that in the second quarter, and we're looking forward to the volume ramp starting later this month and continuing into and beyond Q4 of this year.

We've said for some time that we're a leader in the LPG space and that demand for our clean, low-cost LPG solutions continues to grow. Our announcement yesterday morning fully confirms our leadership claim.

As a direct result of our excellent products and technical services, we've added to our previously announced Euro 7 supply agreement and, as a result, we will become the exclusive supplier of Euro 7 LPG fuel systems to our customer, a leading global OEM.

As we announced about a year ago, we'll begin delivering Euro 6 LPG systems to this customer in the fourth quarter of this year, and we'll continue to supply them as Euro 7 comes into effect.

These supply agreements for Euro 6 and Euro 7 LPG systems add materially to our revenue and market share and leverages our existing engineering and production capabilities.

As a reminder, the Euro 6 deliveries begin in Q4 of this year and will generate revenues of €38 million over the following two years. The newly announced supply of Euro 7 LPG systems is forecast to generate revenue of €63 million through 2028. This increases the total revenue generated from LPG fuel system supply agreements for Euro 6 and Euro 7 with this OEM to approximately €255 million.

We look forward to the opportunity to continue supplying our new customers for the longer term, that is, beyond 2028 and in markets around the world.

The ability of our alternative fuel systems to provide customers an affordable way to use cleaner, low-cost fuels is also driving growth in our delayed OEM business. More OEMs are taking notice of our fuel system products and vehicle conversion abilities.

We grew delayed OEM sales volumes again this quarter as compared to Q2 of last year, due to increasing supply of LPG systems to dR Motors.

dR Motors has been growing strongly during the last few years by offering low-cost LPG-fueled vehicles in the Italian market. Recently, they've accelerated their growth by adding sales in Spain and Eastern Europe. As demand for LPG-fueled vehicles increases across Europe, dR Motors has been gaining market share. We're pleased to be the key supplier of LPG fuel systems to dR Motors.

We expect the LPG market to continue growing as the LPG price advantage is substantial in many of our key markets.

As an example, in Europe, we've seen an LPG price advantage that equates to, in US-dollar terms, more than \$6 per gallon for customers who fuel with LPG compared to those who fuel with gasoline. This kind of LPG price advantage is playing a key role in consumers' decision-making, and Westport has the products to respond to this growing customer demand.

OEMs are also taking notice of this increasing demand, which we'll expect will persist in a variety of markets globally for decades to come.

Although our heavy-duty business experienced an expected volume slowdown this quarter, we see a very bright future for HPDI. HPDI is the most affordable and practical product for reducing carbon emissions in long-haul and heavy-duty applications. LNG pricing in Europe has returned to an advantageous position relative to diesel fuel, and this price advantage is a key driver of fleet demand, enabling fleets to run on cleaner fuel with reduced operating costs, that is, lower TCO, the key metric for fleets.

And our planned HPDI joint venture we expect to accelerate the commercialization of HPDI globally.

Following five-plus years of field experience with HPDI, Volvo has given Westport's HPDI a big vote of confidence. The planned joint venture with Volvo is expected to elevate HPDI's market relevance

and enhance our competitive position, expand our reach to a wider customer base, drive growth and innovation by pooling resources and knowledge, and strengthen Westport's financial position.

When the definitive agreements are finalized, Volvo will purchase 45 percent interest in the JV directly from Westport for \$28 million. Following the closing planned for early next year, as the JV meets certain milestones, Volvo will pay Westport an additional earnout of up to \$45 million.

With a lot of work ahead of us, both teams will be working diligently to meet our target launch date in the first half of 2024. In the near term, I do want to highlight that we're pleased with the agreed pricing structure that will drive improved HPDI profitability this year for Westport and the future for our JV.

Volvo has outlined their strategy to focus on three different technologies: battery electric, fuel cell electric, and internal combustion engines with biofuels. Our HPDI joint venture will secure the long-term future of the internal combustion engine with biogas now and hydrogen in the future.

We recognize that our HPDI fuel system offers the most affordable and practical solution to respond to both environmental demands and fleet performance requirements. HPDI enables the internal combustion engine to perform like or better than the diesel engine that the industry has counted on for decades.

Today, almost all trucks on the road depend on the internal combustion engine. And almost all, which means way too many, of those engines run high-carbon diesel fuel. Using HPDI allows diesel engines to use cleaner fuels, delivering environmental benefits with economics we can all afford.

Both Volvo and Westport are committed to attracting new customers globally to adopt HPDI, primarily in long-haul and off-road applications. Since the announcement last month, our conversations with global OEMs have been very positive, including with OEMs in Europe, China, Japan, and North

America. Through this partnership, Volvo is demonstrating their commitment to the future of HPDI, and we're inviting other OEMs to join them.

In addition to the conversations we've had, work on the HPDI development programs currently underway is progressing well. This includes our work with Scania, as well as two other OEMs who are testing and evaluating hydrogen HPDI on their engine platforms with both hydrogen and methane fuels.

Focusing quickly on the near term, as I previously mentioned in this call, HPDI volumes saw an expected decrease in the second quarter, which was mainly attributed to Volvo's model change. We do see orders picking up.

As a reminder, factories in Europe are closed for about four weeks in the July/August period. Therefore, we don't anticipate seeing the full impact of this ramp-up in volumes until the fourth quarter.

Looking ahead, we remain confident that Westport is offering solutions required by heavy-duty OEMs in order to meet future emissions reductions requirements, while delivering the efficiency and performance being demanded by their fleet customers.

As LNG pricing reestablishes a persistent advantage versus diesel, and as the 2025 emissions regulations and associated penalties for OEMs loom, the growing realization is that affordable, low-carbon solutions like HPDI are required to meet emissions targets. HPDI is reducing emissions today, with thousands of trucks already on the road. We're confident that we can continue to grow these volumes.

With that, I'll hand off to Bill to walk you through our financial results.

Bill Larkin — Chief Financial Officer, Westport Fuel Systems Inc.

Good morning, and thank you, David.

In the second quarter of '23, we generated our highest-ever quarterly revenue of \$85 million, a 6 percent increase compared to Q2 2022.

Our core businesses had a strong quarter, including our delayed OEM, electronics, and fuel storage businesses, as well as our aftermarket business, which together, more than made up for an expected but significant decline in HPDI systems sales.

Our gross margin increased to \$14.4 million or 17 percent of revenue for the second quarter of 2023, compared to \$10.5 million or 13 percent of revenue, for the same quarter last year.

This 37 percent improvement in gross margin dollars was mainly due to higher sales volumes across multiple businesses and increased gross margin in our heavy-duty OEM business, driven by higher spare parts sales, unit pricing on HPDI systems, and the engineering services revenue.

However, our gross margin was negatively impacted from higher production costs that continue to impact our business, stemming from global supply chain challenges and inflation, specifically on logistics and labour costs. We are continuously working with our customers to pass through the impacts of cost increases where appropriate.

A couple other important highlights that I wanted to touch on, which some of David has mentioned.

Early in the quarter, we entered into an agreement with Cartesian to terminate the initial financing and consent agreements in exchange for mutual releases of any future obligations. This included the release of security interest in our HPDI 2.0 fuel system intellectual property.

During the second quarter, we paid \$8.7 million, resulting in the settlement of the \$5.8 million minimum royalty payable balance, and we recorded a loss on extinguishment of royalty payable totalling \$2.9 million.

We finalized our share consolidation in June, which led to the regaining of compliance with NASDAQ's minimum bid requirements.

And finally, we signed a nonbinding letter of intent with Volvo to establish a joint venture to reduce CO2 emissions from long-haul transport, utilizing our HPDI technology. This is a transformational event for Westport. It is expected to not only put us on solid financial ground, but the partnership is also expected to create more opportunities to support a brighter global growth outlook for HPDI.

Moving to the next slide. In Q2 2023, adjusted EBITDA was a loss of \$4 million compared to a loss of \$4.3 million in the same period last year. The improvement in adjusted EBITDA loss was primarily due to higher revenues and improvement in our gross margin.

Higher total SG&A expenses partially offset the increase in revenue in gross margin for the quarter, which is primarily driven by increased activity for trade shows and exhibitions where we highlighted our HPDI fuel system technology in North America and Asia.

We also had an increase in our corporate SG&A, driven by increased consulting and legal fees related to ongoing corporate projects, including the activity related to the letter of intent with Volvo. We expect legal and consulting fees to increase in the second half of the year as we move forward with setting up the JV with Volvo.

On the next slide, OEM revenue for the second quarter this year was \$52.4 million, compared to \$54.3 million in the second quarter of last year.

As I mentioned, we highlighted in our first quarter call that we anticipated a decline in HPDI fuel system deliveries, leading into Volvo's updated product release later this year, which is a more powerful option with extended range. We also experienced a decrease in revenue due to lower sales to customers in India and the light-duty OEM business, and lower sales volumes to our hydrogen customers.

These declines in revenue were partially offset by increased sales volumes from our delayed OEM, fuel storage, and electronic businesses compared to the same quarter last year.

Gross margin increased by \$3.7 million to \$8.4 million or 16 percent of revenue in the second quarter this year, as compared to \$4.7 million or 9 percent of revenue in the second quarter of last year.

In addition to the increases in revenue mentioned above, gross margin was positively impacted by improved gross margin in our heavy-duty OEM business from higher spare parts sales, unit pricing on HPDI systems, and engineering services revenue. This is partially offset by higher production input costs.

Gross margin and gross margin percentage from our HPDI fuel system products will vary based on production and sales volumes, level of development work, and successful implementation of initiatives to reduce component costs.

As LNG fuel prices continue to trend positively against diesel, and Volvo releases their HPDI-equipped engine that delivers increased horsepower, improved emissions, and extended range, we anticipate volumes begin improving later in Q3, with Q4 being a full quarter at higher volume levels.

Also, we continue to see a significant improvement or reduction in our warranty claims. And during the second quarter, we do not have any adjustments to our warranty provision outside of our normal warranty estimation process.

On the next slide, Independent Aftermarket. The IAM revenue for the second quarter this year was \$32.6 million compared to \$25.7 million in the second quarter last year. The increase in revenue was driven by higher sales volumes in Africa, Eastern Europe, and South America.

Gross margin increased by \$200,000 to \$6 million or 18 percent of revenue in the second quarter this year, as compared to \$5.8 million or 23 percent of revenue in the second quarter last year. The increase in gross margin dollars is related to higher sales in South America. And the decrease in gross margin percentage is driven by lower-margin sales mix and increased material costs.

Looking ahead, supportive LPG pricing continues to boost the demand trend in Europe. And it's an important area of growth for our company in the years ahead. In the fourth quarter this year, we began production for our previously announced work with a leading global OEM for the supply of LPG fuel systems.

Finally, I'd like to touch on liquidity. Our cash and cash equivalents decreased by \$19.7 million during the second quarter of 2023 to \$52.3 million. The decrease in cash during the second quarter is primarily driven by \$18.5 million net cash used in our financing activities, consisting of the \$8.7 million settlement of the royalty allegation, a reduction in borrowings under our revolving financing facilities, and scheduled principal payments on our term debt.

We did realize a significant improvement in cash use and operating activities in the second quarter, which declined to \$41,000. This is compared to \$16.5 million in the same quarter last year. This improvement was driven by a change in working capital, specifically in accounts receivable and prepaid expenses.

We continue to take actions to monetize existing inventory and optimize inventory levels to further free up cash and net positive for our balance sheet going forward.

Given the large one-time payment in the second quarter, cash use was higher than normal.

Although we believe we have sufficient liquidity to continue as a going concern beyond August '24, long-term financial sustainability of the Company will depend on our ability to generate sufficient positive cash flows from all of our operations, specifically through profitable, sustainable growth and from the ability to finance our long-term strategic objectives and operations.

Our recent HPDI JV announcement with Volvo is an inflection point for Westport financially. Volvo's payment for their 45 percent share of the joint venture includes an initial \$28 million and an

earnout of up to \$45 million, which is a clear signal of their commitment to the future growth of HPDI. This also helps shore up our balance sheet.

The joint venture's focus on driving global adoption of HPDI in the long-term improves efficiencies and scale, while in the short term, we have a partner to share in the required investments, including working capital and capital costs.

We will continue to be prudent in our liquidity management, and multiple steps are being taken to do so. Additional debt remains an option as we look to solidify our balance sheets. We continue to do what is necessary to ensure we are adequately and fully capitalized.

Thank you. And with that, I'll turn it back to David.

David Johnson

Thanks, Bill. I'll close with a few comments, and then we'll take your questions.

Our products are making material impact on the decarbonization of the transportation industry. And the magnitude of this impact will only grow as we get these products into the hands of more customers.

Westport's core business is strengthening. Year to date, our delayed OEM business is achieving growth of almost 100 percent, with more growth on the horizon.

In Q4, we'll launch our Euro 6 LPG systems for our global OEM, and we expect the growth of that business in the next three years will significantly add to our top line and bottom line. The announcement of our expanded scope to be the sole supplier of the Euro 7 LPG systems for this OEM is confirmation of our position as a leading supplier to the industry.

In our Independent Aftermarket business, pricing for LPG is favourable in many markets around the world. However, the impact of inflation is weighing on demand in some areas. Yet, in light of these

complex market conditions, our high-quality, cost-effective direct injection technology continues to be an industry leader and is driving increased market share.

For any start-up or entrepreneur, market validation is a key marker of future success and an event that can be decades in the making, as it has been for us. The planned HPDI joint venture with Volvo is transformational for Westport and is expected to unlock the future of HPDI. With this announcement, we secured the recognition of our customer, Volvo, and the clarity that they want to invest in HPDI and join us on this journey of accelerating growth.

HPDI will be a huge part of the future commercial transportation market. This new era will be one of success with new customers, new projects, more volumes, and lower costs.

Finally, enhancing our financial performance has been the key focus in 2023, included but not limited to driving margin expansion, revenue growth, and technology development. We continue to see improvements as we secure new contracts and adjust our pricing where we can. We also continue to do what is necessary to ensure we are adequately and fully capitalized. The planned HPDI joint venture will go a long way to solidifying our financial viability given we now have a partner in place to share in the development costs.

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

Q&A

Operator

Thank you, sir. Ladies and gentlemen, we will now begin the question-and-answer session. Should you have a question, please press *, followed by the number 1 on your touch-tone phone. Again,

that's *, followed by the number 1. If you would like to withdraw your request, please press *, followed by the number 2.

Your first question comes from the line of Colin Rusch from Oppenheimer. Please go ahead.

Colin Rusch — Oppenheimer

Thanks so much, guys.

With the Cartesian debt retired, can you talk a little bit about some of the incremental flexibility that you have in terms of other instruments around liquidity?

Bill Larkin

Sure. I can deal with that. As part of the Cartesian agreement relationship, the insecurity over our HPDI and other assets, as you're aware, in connection with our path forward on setting up the JV, that we needed to free up that IP, because that's going into the JV itself. Also, so that's one of the reasons behind that.

Second, it does give us flexibility from financing standpoint in terms of freeing up collateral that we could potentially pledge once that gets into the JV, as well as other collateral. So it does give us quite a bit of flexibility by paying that off and evaluating other debt financing opportunities.

Colin Rusch

Excellent. Thanks so much, guys.

And then, with the announcement of the JV, obviously, you were able to make an incremental announcement around the LPG adoption. What can you say about customer engagement, willingness to work with you guys, now that you've got a clear path for folks all the way to zero emissions on the solution perspective?

Are you seeing incremental demand and interest in some of the natural gas solutions as you've gotten that news out into the market?

David Johnson

Yeah. Colin, thanks for the question. It's a super-interesting point, I think, a great time from Westport.

We've been working in HPDI for a long time, but to have Volvo join us in the journey and really put their marker and bet on this technology for the future is a very positive sign to the other players in the industry. And so we've already heard that feedback as we talk with our existing customers and other customer prospects around that role that HPDI will play today with biogas and with LNG, and tomorrow with hydrogen.

And as you know, we've got hydrogen engines running in our test cells and running in other people's test cells around the world. So we see a very, very bright future. And having our customer, after all these years of the work we've done together and the experience they have in the field, come forward and say, we want to form a joint venture with Westport, super, super exciting for us.

Colin Rusch

Thanks so much, guys.

Operator

Thank you. Your next question comes from the line of Amit Dayal from H.C. Wainwright. Please go ahead.

Amit Dayal — H.C. Wainwright

Hey. Good morning, David, Bill. Thank you for taking my questions.

Just on the HPDI JV with Volvo, how should we think about this impacting the sales pipeline for this offering between now and when the JV is operational?

David Johnson

I guess, Amit, I would say that—thanks for your question—I don't expect a huge catalyst in the near term. I really expect a huge catalyst in the long term as we sign up more customers to do the necessary development work to bring product to market.

So the pipeline right now is basically Volvo in terms of production and then Weichai with the launch in the near future. And then customers following that that are working on hydrogen HPDI today.

Amit Dayal

Okay. Understood. And then, just moving on to some of the operational aspects. Looks like some of the higher input costs are not yet being fully transferred to customers. Is this something that will get resolved in the near future?

David Johnson

Yeah. For sure. We see inflation, inflation in energy cost, inflation in labour cost, inflation in material cost. And when we can pass those on to customers, we do.

And I would tell you that's an ongoing process. There's always some lag in terms of what you're able to bring back, the price in the marketplace. And so we have to be very careful about that, too, because our products are really bought for an environmental benefit, but also for an economic benefit. And so if it costs too much to buy the product, it reduces the economic benefit.

So this is something we have to be careful with and manage carefully. And it's our daily work of our sales team with our customers around the world to pass on what we can pass on and to make sure our product is still competitive in the marketplace.

Amit Dayal

Okay. Thank you, David. Just last one from me. In terms of the near-term outlook, it looks like this model transition at Volvo, should we assume that maybe 3Q will be a little bit lower than 2Q sequentially in terms of revenues?

David Johnson

No. I think—go ahead, Bill.

Bill Larkin

Oh, no. I was going to say, when you look at it from a consolidated basis, typically our Q3 is historically lower than Q2, just because of the seasonality of our business—

David Johnson

Yes.

Bill Larkin

—with respect to—so that's one piece of it, which does impact the heavy-duty business and deliveries of systems.

As we mentioned, we do expect Volvo to start delivering the updated version of the truck with our HPDI system on it in Q3. And that will ramp up through the end of that quarter and then start moving full steam ahead in Q4.

Amit Dayal

Okay. All right. Guys. Thank you—

Bill Larkin

And then the other piece too, I think David mentioned, is we've got fair (phon) sales in there, which continue to increase over time as we get more and more trucks on the road. Also, engineering

services, we're getting at a pivotal point where we've got to start talking about Euro 7, hydrogen, and other programs as well with various customers out there, OEM customers. So as we start moving forward with those, that'll have an impact on revenue as well.

Amit Dayal

Okay. Got it. Thank you, guys.

Operator

Thank you. Your next question comes from the line of Rob Brown from Lake Street Capital Markets. Please go ahead.

Rob Brown — Lake Street Capital Markets

Hi. Good morning. My question is on the JV with Volvo.

Can you help us understand kind of what drives the milestone payments and additional investment and sort of the timing window of that?

Bill Larkin

Hey, Rob. This is Bill. Yeah. We haven't disclosed what those milestones consist of in the timing. What we can say is they're strategically aligned with performance of the JV and what are those key items that will drive success and growth of the JV, so. And that'll be over a period of years those milestones are laid out.

Rob Brown

Okay. Great. And then maybe help me understand how the JV kind of drives other customer interest in the HPDI product. Are you now able to kind of invest to develop product?

Are there customers sort of following Volvo with kind of the regs out there and trying to meet the emission standards? I guess just help understand how you see additional customer demand coming into the business.

David Johnson

I think there's a lot of things going on in the marketplace right now, Rob, with respect to which technologies will be the technologies of the future for heavy-duty, long-haul trucking. There's talk on fuel cells, talk on battery electric, and there's biofuels. There's a lot of, I'll say, options, technical options for OEMs to pursue.

And for a long time, we've been touting our HPDI as a key element of the portfolio solutions that will be required. And everyone knows in the industry that this product has been in the marketplace and selling and picking up share. But it's a next step of really understanding and knowing when our customer comes forward and says, yeah, this is a really important part of our portfolio to respond to the regulations to make fleets have trucks that are cleaner and economic to operate. And so really, it's kind of a marker for the industry to have this customer, our customer at Volvo, with all their experience with products say, this is part of the future.

And meanwhile, I'll tell you that the OEMs have been working with fuel cells, they have been working with battery electric, they have been doing this. And there's demos and one vehicle here, ten vehicles there kind of thing. And they're recognizing the cost of these vehicles and the challenge that is for commercial trucking. And so then to have this formation of a joint venture between Volvo and Westport around HPDI and recognizing what we've shown with hydrogen and that being a really important part of the future, I think it's a new ingredient, an added ingredient, and hopefully a catalyst for the market to recognize where HPDI can play in heavy-duty, long-haul trucking.

Rob Brown

Okay. Great. Thank you. And then on China, could you just give us an update on how that market is developing and maybe where that's at?

David Johnson

Yeah. The good news in China is that we continue to work with Weichai on all the necessary steps to achieve launch. They've got certified product at the engine level and at the vehicle level with their customers. And the market is improving. So basically, globally, our LNG prices, natural gas prices, have stabilized at a lower level. And so there's an advantage that's been reestablished versus diesel in Europe, but also in China.

And so this basically is the key ingredient that then catalyzed the market and enable us to bring HPDI to the Chinese market is a fuel price advantage. It gives you a TCO advantage, and a customer with certified product that can bring that product to market. So we're really excited about the potential to have some good news to share with you in the future.

Rob Brown

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

David Johnson

Thanks, Rob.

Operator

Thank you. Your next question comes from the line of Eric Stine from Craig-Hallam. Please go ahead.

Eric Stine — Craig-Hallam

Hi, David. Hi, Bill.

David Johnson

Good morning.

Eric Stine

Good morning. So I know you've talked a lot about HPDI so maybe I'll focus on some other areas.

For OEM, I mean, this is kind of momentum that we haven't seen in quite a while. And I know DR, strong in Italy, taking it to other markets. So curious, thoughts about how early or what that means in terms of going to other markets. But also, I would assume other OEMs are seeing the market share gains, they see the economic benefit of using LPG. So maybe what that also means for your OEM pipeline.

David Johnson

Yeah. So I think this is a really interesting story relative to Westport. We've announced, just yesterday, additional sales and supply agreements for Euro 7, so out into the future with leading OEM. And really, when you look at our Aftermarket business and the LPG business in general, which are highly linked, we're seeing benefits in markets around the world for our LPG systems. And it's a low cost to access technology and it's a low cost to operate.

So that figure I talked about just a little bit ago of \$6 per gallon—I turned it into gallons so it would be easy to understand for all of us in the US—this drives the behaviour of customers. People are looking for lower cost ways to access transportation and access clean transportation. And our systems, whether they're applied on an aftermarket basis or they're applied on a delayed OEM basis where we do the install for our customer or whether they're applied by buying an LPG vehicle that's fitted by an OEM, we see this growing.

And so in places like Italy and Türkiye and Poland, there is a substantial market share of LPG vehicles. And we see that growing in markets around the world because of this economic advantage.

And so it's a real bright spot for us. We're super excited to have secured this new business on the OEM side. And we think the delayed OEM is a quicker way for OEMs to get to market and we're glad to help with that. And the DR story is a great success story for DR but also for Westport Fuel Systems.

Eric Stine

Yep. Absolutely. Okay. And then maybe last one for me. I guess I will go back to HPDI, and you've detailed kind of the change in stance from Volvo. It's certainly big validation and then other OEMs as well. But curious what this means for other markets. Correct me if I'm wrong but I think there's been some penetration, small, in Canada under some waivers.

Just curious, I mean, is this something that in the, call it the next year or two, we should expect that if you were to penetrate North America with HPDI, it would be under those waivers on kind of a case-by-case basis? Or is it possible that Volvo brings it to North America under this JV?

David Johnson

So first of all, thanks for the question. It's a great question because today in the marketplace around the world, the only place you can buy an HPDI-equipped truck is in Europe.

From our perspective, the opportunities in China and North America and really, rest of world are quite significant. And so there's activities going on by our current customer and there's activities going on with prospective customers that are testing engines. And we see application in basically all the markets. So the question is when and how quickly.

And I'm glad you raised the point on Canada. We did some work with partners in Canada that enables Volvo and their customers to bring European trucks into Canada. And so we have the first of those trucks arriving in Canada around now. And we look forward to the validation of those vehicles in the Canadian market because that will then prime the pump, so to speak, for more imports.

It's a really exciting development for us that the European Volvo truck with HPDI can be imported into Canada now. And we look forward to the market understanding how much better an HPDI-equipped truck is versus a spark-emitted natural gas truck in terms of fuel efficiency and performance and truly delivering what fleet customers need in the field with their heavy loads and long-distance travel that is certainly a key part of the market in Canada.

Eric Stine

Okay. That's great. Thanks.

David Johnson

Thank you.

Operator

Thank you. Your next question comes from the line of Chris Dendrinis from RBC Capital Markets. Please go ahead.

Chris Dendrinis — RBC Capital Markets

Yeah. Good morning. Thank you. I guess I kind of wanted to just follow up on the second half of the year and sort of expectations and the cadence.

You mentioned some softness in 3Q just due to natural kind of seasonality. Is there anything, I guess, with 4Q and then that LPG system ramp that we should be kind of thinking about or accounting for? I guess, maybe specifically, any kind of near-term margin pressure just with the volume ramp or anything like that? Thanks.

David Johnson

Yeah. So maybe just to hit on HPDI on that topic first, Chris. We are having, let's say, this lower volume in Q2 because of model change. And the new model, with more horsepower, more efficiency,

longer range, as we talked about earlier, launches after the summer shutdown. So as soon as the summer shutdown, we'll see some ramp of that volume. And we're looking forward to that. Right?

What the numbers are exactly is not perfectly clear to us. But definitely, we see an uptick. And so then we'll have an uptick in volume in Q3 and then more in Q4, is our expectation. And that's with the improved pricing that we've been able to negotiate. So kind of hitting both things, some margin improvement and some volume improvement. So it should be better going forward.

And then, in the broader scope, when we think about Westport fuel systems as we launch our LPG customer, our new LPG customer, in the fourth quarter, that also will add to the equation. And again, I think, in the industry and with these launches, it's not a step function; it is a ramp, for sure. And so as we look into 2024, we have very positive outlook on that for the business.

Chris Dendrinis

Great. Thank you. And then I guess maybe just as my follow up, I guess now that you guys have announced the JV with Volvo, you previously have been kind of, I guess, pretty quiet in regards to maybe any testing that you had been doing with them as far as the hydrogen HPDI goes.

So anything to comment there? I guess, either should we consider this kind of what you're doing with Volvo is maybe more consistent with Scania where it's kind of engine testing right now? Or I guess, where are you kind of at in that development plan or testing environment? Thanks.

David Johnson

Yeah. Thanks. So one of the things we do with our existing customers is work goes on. Right? So we are regularly having our current customers, Volvo's engines, and our test cells, and doing work. And certainly, they're still, even in the case of the JV, as we get to those markers in the first half of next year, Volvo will remain a customer of the JV. And so I would expect that when there's a significant development

contract signed, there'll be an announcement from either us or the JV in the future saying these things are happening.

And so I would expect you'll hear about those in due course. But, let's say, it is a normal course of business for us to be continuously doing development activities and evaluating certain technologies and calibrating and running durability tests. So that's normal business for us that's running right now.

Chris Dendrinis

Got it. All right. Thank you.

David Johnson

Thank you.

Operator

Your next question comes from the line of Mac Whale from Cormark Securities. Please go ahead.

Mac Whale — Cormark Securities

Hi, David. When you look at the new business this fall, you talked about €38 million coming from that. That customer today isn't a customer at all. So that's not like there's revenue that will disappear as the new Euro 6 shipments on the LPG build. Is that correct?

David Johnson

Largely correct. So basically, for us, this new OEM, we sell them product. It's a new customer for us. We do have some parts of what they're currently using in their system that we supply through one of our competitors. So basically, we're a sub-supplier to our competitor, and they're supplying that customer today.

So there is a piece of the revenue that overlaps. But for the most part, that €38 million is largely incremental over the next two years.

Mac Whale

Okay. So then in '25, when you go to the Euro 7, do you expect to continue to make Euro 6 shipments? And I'm wondering if that €63 million comes in, does the €38 million go away? You know what I mean?

David Johnson

Yeah. No. Not exactly. So what we're talking about here is, first of all, on the emission standards, there's still some lack of clarity in the regulations in terms of when Euro 7 is required and when it might launch. And you can also understand that the OEMs, when they launch a new model, independent of the emissions regulations, when they say, here's a new vehicle, here's a new this or that, they want to have the fuel system there and available for LPG. And so these different awards that we've announced are associated with different vehicles. And so we're picking up different vehicles along the way.

And when we get into Euro 7, we become the exclusive supplier. We were doing all the models for this OEM. And so that really is a stepwise increase in our revenues and our market share of LPG systems in the market.

Mac Whale

Okay. Great. And then just lastly, I think you already addressed this with one of the questions on the margin outlook in the second half of the year. Just asked another way, does the Euro 6 LPG, is that business significant enough to put pressure on the margins? Or do you expect to see that continue improvement as these new products launch?

David Johnson

The business that we've secured, we feel quite good about the prices we'll be able to obtain and the margin that we'll yield. And so we see this really as accretive to the income statement and very helpful to our business.

I think there's also an element, I mentioned it earlier, that really this business and LPG system leverages capacity and capability we already have in our Westport Fuel Systems world. So in terms of ability to produce the parts, having the capacity, the engineering capacity to support this customer, we're not adding a lot in order to respond to this need. So it should drive a more favourable bottom line.

Mac Whale

Okay. Great.

David Johnson

That's certainly our goal.

Mac Whale

Okay. Great. That's all my questions. Thank you.

David Johnson

Thanks, Mac.

Operator

Your next question comes from the line of Bill Peterson from JP Morgan. Please go ahead.

Bill Peterson — JP Morgan

Yeah. Hi. Good morning, and thanks for taking the questions.

Wanted to ask a question on the natural gas HPDI a bit differently. You talked about the potential for Weichai coming back. But when we see natural gas prices improve, what's the lag time on when you see that kind of roll through and result in new business opportunities?

And I guess with that in mind, especially in Europe, is there other opportunities? Or you just have to get past this sort of model changeover for the business to be maybe even larger than it was at steady state last year?

David Johnson

Yeah. Thanks, Bill, for your question. Fundamentally, in the marketplace, fleet operators are buying vehicles and using them three to five years before they turn over and get new vehicles and those vehicles become used vehicles. And so they're doing the calculations. And it's their confidence around the ability to deliver freight and do so with an economic advantage, so an environmental advantage and economic advantage.

And so that price differential between natural gas and diesel is something that weighs heavily in the equation. And I do think it takes some time. Right? So we had a price spike primarily in 2022 that lasted more or less the whole year following Russia's invasion of Ukraine. So with that kind of history, there is some hangover, some baggage that comes along. But now that the price of reestablish has gone back to normal and yet that war is ongoing, I think the fleets are getting more comfortable with the fact that they can count on that advantage. And that really is what it takes.

And so you ask, what's the lag time? Well, it depends on which fleet you talk to and what their confidence is and what their outlook is. But I think having Volvo then say, we're betting on this technology for the long term because we see the long-term benefits really helps to have the marketplace see that this is not just a token effort, but actually a fundamental effort by Westport, by Volvo, and by others to bring natural gas trucking and, in the future, hydrogen trucking to the marketplace so that the fleets can access cleaner transportation and low TCO.

Bill Peterson

Thanks for that. Second question on the LPG and the progression from Euro 6 eventually to Euro

7.

How should we think about the margin structure between your wins in Euro 6 and Euro 7? It looks like you have a higher revenue base. Should we expect better fixed cost absorption? I mean, is this going to be higher margin just based off what you designed in? Just try to get a feel for the margins as we look ahead.

David Johnson

Yeah. I think the biggest factor here is good margins on the business itself and then more absorption of the fixed cost on a higher top line that makes the gross profit improve from there. So I think fundamentally, it's a big piece of business that we've secured and will fundamentally improve our P&L accordingly.

Bill Peterson

Thanks for that.

Operator

Thank you. Your next question comes from the line of Jeff Osborne from TD Cowen. Please go ahead.

Jeff Osborne — TD Cowen

Thank you. Good morning. Just a couple of questions on my side.

Back on the joint venture, I was wondering at this point if we've determined sort of the board structure and whether you'd be able to consolidate the financials or not.

Bill Larkin

I'll take that. So the board structure, both partners will have equal members on the board at this point. All the specific details will be laid out in the definitive agreements, which we'll work on over the next few months.

Respect to consolidation, as we are currently looking at it, we are evaluating consolidation. Initially, first looking at it, I don't think we're going to be able to consolidate it. As we go through and look at all the criteria, as you're aware, several years ago, it used to be quantitative analysis. Now it's more qualitative around the decision-making at the board level and how those decisions are made. So as we go through and kind of formalize the structure, the arrangements, we will continue to evaluate consolidation. But as we sit here today, I don't think we're going to be able to consolidate.

However, irrespective of that, we will have expanded disclosure in the footnotes of our financial statement. So you're going to be able to see volumes, revenues, margins for that business, I think very similar to how we disclose the CWI JV.

Jeff Osborne

That's helpful, Bill. And then I was just curious, is there any feedback from non-Volvo OEMs around sort of information sharing with a perceived competitor that's part of the JV? Just wondering what types of information barriers and other sort of blockades you'll be able to put up to give potential future customers assurances because my understanding is pretty much everyone will need to be buying through the JV. Is that correct? Can you just walk us through that process?

Bill Larkin

Yeah. For sure. So this is, in the industry, I'll say, done all the time. So companies, major OEMs work with their suppliers and share information with their suppliers. And the supplier's responsibility is to keep that information from their customers' competitors. It happens all the time. And so our JV will need

to do that too. And that's, I'll say, normal business that every supplier needs to be cognizant of, aware of, and manage. Because if they fail, they'll lose business.

So in the grand scheme of things, I think at first blush, people say, uh-oh, Volvo's in this JV; now they're going to know everything. And that cannot be the case. It will not be the case. And we just have to demonstrate that to our customers over and over again, as we do today.

So we're working with multiple OEMs, Westport is today. And in the future, our JV will be doing that. But I think showing how we do it and reassuring our customers that their confidential information will be protected is our job. And so we'll do that.

Jeff Osborne

Got it. And my last quick one, if I can squeeze it in, just for Bill, is you gave some comments around revenue trajectory for Q3, Q4. Can you just walk us through sort of major sources and needs of cash for the third and fourth quarter?

Bill Larkin

No. I think as we look forward, as I mentioned, Q2, we had higher than normal on debt servicing payments. So I think we're going to go back to normal on just kind of our normal principal payments, as well as our CapEx. As we mentioned, we're going to be in \$12 million-to-\$15 million range. We have about \$7.5 million year to date. I don't expect any major changes in our CapEx.

One of the critical areas that I had in my prepared remarks is really focusing on working capital and trying to drive that down, improve our AR collections. We have to drive inventory down. And I think through those initiatives, we're going to be able to free up some cash and put that on the balance sheet as we go forward. So that's where we're really focusing our efforts right now.

Jeff Osborne

Perfect. That's all I had. Thank you.

Operator

Thank you. There are no further questions at this time.

I'd now like to turn the call back over to David Johnson for any closing remarks.

David Johnson

Yeah. Thanks, everyone, for your time this morning.

I think when I look at our Q2 record revenues and improving gross margin, I think it's a solid quarter and good performance, especially in light of the fact that our volumes on our marquee product HPDI were rather low.

So in that grand scheme of things and now with this additional LPG business, to me, the signs are super positive for our light-duty OEM business, our heavy-duty OEM business, and of course, our hydrogen trajectory that we have with the developing for both fuel cells and internal combustion engines.

So there's a lot of bright signs on the horizon for us, and we're really looking forward to the quarters ahead.

Thanks, again, for your time and interest in Westport Fuel Systems. I look forward to speaking with you again.

Operator

Thank you, sir. Ladies and gentlemen, this concludes your conference call for today. We thank you for participating and ask that you please disconnect your lines. Have a lovely day.