Conference Call Transcript

Second Quarter 2020 Financial Results: August 7, 2020

Operator

Welcome to the Westport Fuel Systems' Second Quarter 2020 Conference Call. As a reminder, all participants are in listen-only mode, and the conference is being recorded. After the presentation, there will be an opportunity to ask questions. To join the question queue, you may press star, then one on your telephone keypad. Should you need assistance during the conference call, you may signal an Operator by pressing star, and zero.

I would now like to turn the conference over to Shawn Severson with alphaDIRECT Advisors, Westport's Investor Relations Representative. Please, go ahead.

SHAWN SEVERSON speaking

Investor Relations Representative, alphaDIRECT Advisors

Thank you and good morning, everyone. Welcome to Westport Fuel Systems' second quarter 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 Fuel Systems is Chief Executive Officer David Johnson, and Chief Financial Officer Richard Orazietti. Attendance on this call is open to the public and to media, but questions will be restricted to the investment community.

You are reminded that certain statements made in this conference call and our responses to various questions may constitute forward-looking statements within the meaning of the U.S and applicable Canadian securities laws, and as such, forward-looking statements are made based on our current expectations and involve certain risks and uncertainties. Actual results may differ materially from those projected in the forward-looking statements, so you're cautioned not to place undue reliance on those statements. Information contained in this conference call is subject to and qualified in its entirety by information contained in the Company's public filings.

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

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Thank you, Shawn. Good morning everyone.

I sincerely hope that all of you and your loved ones are healthy and well and that you're finding some time to enjoy this summer. Since we updated you with our Q1 results in early May, there have been strong signals for our green recovery in multiple jurisdictions around the world and associated stimulus spending to build a better, more resilient, and low-carbon economy. I believe in a green recovery, present about once in a lifetime opportunity to transform our transportation systems so that we can sustainably move people and freight and I'm confident that we have an important role to play.

At Westport Fuel Systems, we've developed, validated, and built solutions that are in production for sale in 70 countries and are being used around the world to enable net zero carbon transportation.

Following our COVID shutdown, our teams have safely and effectively resumed operations at all of our global locations. While revenue was significantly impacted in Q2 due to these shutdowns and those of our customers around the world, I'm pleased to report our net income was positive, an improvement versus the same period last year.

Our team has shown resilience and has been steadfast in their efforts to remain nimble in response to this difficult time. I'm particularly proud of the significant efforts we have made and the results we have achieved to improve liquidity since the start of the year and I'm equally proud of the incredible efforts made by our team members to take care of each other during COVID, safely return to work, and to respond to our customers throughout the shutdown and recovery period.

The COVID-19 global pandemic continues to have far reaching ripple effects. The surge in coronavirus cases in the U.S. and elsewhere has analysts closely watching recovery related indictors, and while a high degree of uncertainty remains, we do see bright spots on the horizon.

Our business is heavily focused in Europe, China, and India and it's in those markets where we're starting to see some promising green shoots of optimism. COVID-19 has put many aspects of our life on hold, but the need for action on climate change remains pressing. As the economy ranks back up, increased online transactions means increased demand for commercial trucking, but government regulators around the world are holding firm on the requirements for reduced CO2 emissions. Air quality improvements during the lockdown brought new focus to the public health discussion and the benefits of deploying cleaner mobility technologies.

I'll talk more about each market shortly, but first I'd like to share some topline financial results. Our second quarter results directly reflect the impact of COVID-19 related customer shutdown which began in China in January, spread to Europe in March, and then North America in April.

Revenue decreased to $36 million from $82.4 million in the same period last year due to the effect of COVID-19 and the various shutdowns in all our business segments. Net income was $3 million compared to a net loss from continuing operations of $2.3 million for the same period in 2019.

This $5.3 million year-over-year improvement resulted from a $7.7 million insurance recovery recorded in the current quarter which was related to the $10 million field service campaign expense we recorded in the first quarter of this year. We also lowered operating expenses and benefited from our foreign exchange gain compared to the second quarter of 2019.

As you've heard, we have been hard at work to shore up our balance sheet, strengthen liquidity, and reduce our cost of capital to weather the difficult market conditions brought on by COVID-19. Since the beginning of the year, we announced over $50 million in liquidity improvements with new debt facilities totaling $32.9 million. We also re-deferred $6 million in principal payments due in 2020, and refinanced our convertible notes with the Cartesian Group, extending the maturity and reducing the coupon rate.

We're also participating in government wage subsidies and other support programs netting a cumulative benefit of $3.8 million in the second quarter.

We continue to focus on cost reduction, disciplined cash management, and supporting our global team and their communities as we navigate this recovery period and respond to ramping customer demand for our products. As our customers, partners, and suppliers return to production, there have been many questions about the impact of the downturn on our industry in various markets.

The European commission is striving for climate neutrality by 2050 which represents both a big challenge and a big opportunity. Carbon neutrality in transportation will only be possible with policies that account for the use of renewable gases like biomethane. Natural gas together with biomethane are a great example of the potential for a circular economy, linking mobility with renewable energy and agriculture.

In Europe, the current uptake of biomethane points to an increasing share of renewable gas in the near term to de-carbonize the transportation sector. Projections are, that by 2030, 40% biomethane will be available to power the entire natural gas sleet, reducing overall greenhouse gas emissions by 55% and delivering up to 1 million jobs.

The timeline for creating the CO2 baseline for commercial vehicle emissions concluded on June 30th of this year. Now the race is on to achieve the goals and avoid the financial penalties which come into effect in 2025.

As a multitude of regulations and policy frameworks have been introduced in the EU national and local levels, keeping on top of a rapidly evolving landscape can be a challenge, but the message is clear. Europe wants a big change and they want it right away.

Stimulus packages may benefit the growing refueling infrastructure for gas's fuels and we see increasing demand for transportation solutions that reduce emissions as much as possible, as quickly as possible. Converting to natural gas can provide much-needed cost relief to operators who are struggling to recover from the impact of COVID-19 on their businesses which in turn, may help keep cost down for consumers.

As of last month, Europe reached a milestone with the installation of its 300th LNG station and CNG stations now numbered nearly 3,900. The LNG refueling infrastructure in Europe has almost doubled in just the last two years. The growth in the market has been driven by the new EU heavy duty CO2 regulations and the increasing availability of LNG in Europe. This has been a multi-year journey and we believe there is more runway.

We need emissions reductions in all sectors to achieve our climate targets. Heavy duty vehicle manufacturers must provide solutions for a range of applications and they currently lack another climate friendly solution that is market ready and suitable for large scale production.

Our products are not a test or an experimental phase. They are mainstream, for sale, and in use around the world today and we believe they're an important part of an economic recovery in many markets. Even modest market share growth of vehicles that use our technologies will make a significant impact on our revenues and profitability.

In Italy, one of the most important alternative fuel markets in Europe, we're seeing encouraging signs of recovery for our light-duty business. For the overall Italian market in June, new vehicle

LPG and CNG registrations are progressing towards pre-COVID levels. In some regions, CNG vehicles make up more than 12% of the total number of light-duty cars on the road.

The Italian government is preparing a new stimulus package targeted in part at the automotive sector. Indications are that this package may include nearly $1 billion to strengthen current incentives to encourage sales of state-of-the-art combustion engine cars. There are few details as to the specifics of these incentives, but we believe this is another positive note for the light-duty business.

On the heavy-duty side of our business, we also see positive support for natural gas vehicles in Europe. Since the start of 2019, natural gas fueled trucks in Germany have been exempt from road toll charges which can save 10,000 euro, per year, per vehicle in operating costs. This incentive structure has now been extended into 2023.

As we reported last quarter, our Weichai Westport joint venture has completed all the emissions testings of the Chinese Ministry of Ecology and the Environment and the Chinese Ministry of Industry. We await the conclusion of the final paperwork for certifications so we can begin commercial sale. The long-term potential of HPDI in China, the largest natural gas commercial vehicle market in the world remains compelling. We have a great partner, a great product, and a large market to serve and we look forward to ramping up sales in this important market in due course.

We're working to grow our business in India. The market fundamentals are strong, with widespread fuel availability, government support and compelling economics. While local shutdowns continue in affected areas and the impact to operations of some of our OEMs, our operations in India are open for business. We already have a leadership position in India's natural gas passenger car market, with the strong base of OEM customers including Tata Motors, Mahindra and Mahindra, Maruti Suzuki, Piaggio, and others.

We have completed more than 20 engine development projects to bring our customers CNG engines up to the new Bharat Standard-6 which were adopted on April 1st of this year. The Bharat Standard-6 emissions standards which affect all vehicles from motorcycles to heavy trucks, culminated a massive effort over the past four years to upgrade vehicles to meet these standards. Prior to this, India adhered to BS-4 regulations which were equivalent to the Euro 4 standards that were in place in 2005 in Europe. India skipped the whole BS-5 generation and now at BS-6 is equivalent to European standards, a dramatic reduction in NOx and particular matter emissions that will improve air quality in the Indian subcontinent.

We're seeing strong growth for CNG vehicles and even a burgeoning interest in RNG resources to fuel this market. CNG vehicles are attractive in the Indian market with most OEMs offering multiple vehicles powered by CNG because of the fuel price difference versus gasoline and diesel. CNG fueling infrastructure is growing with over 1,700 stations in place today and expected to double 3,500 stations by 2023 and then onto 10,000 stations by 2030.

We're pleased with the progress we've made on the new BS-6 products in India and believe there's strong growth potential for us there.

There continues to be much interest around hydrogen vehicles in recent months and I wanted to share a few of my thoughts. While hydrogen faces many of the same challenges that natural gas vehicles faced 10 to 15 years ago, the appeal of a net zero emissions technology is undeniable and presents a compelling, long-term option for our future.

We, along with others like Iveco and Scania, have spent the better part of a decade successfully tackling similar heavy-duty vehicle obstacles as what we see in the hydrogen market today, a lack of fueling infrastructure, the challenge to efficiently produce hydrogen, a substantial incremental vehicle cost, and scaling up of vehicle production. Hydrogen fuel-cell vehicle sales remain low in volume, expensive to produce and restricted to sales in a few countries or regions that have built hydrogen fueling stations. That said, progress has been steady. As I said earlier, this story is familiar to many of us who have been around this industry for a while. We already participate in the hydrogen market across all transportation applications and we continue to make investments in this opportunity. We sell hydrogen components engineered in Canada and manufactured at our facility in Italy, to customers like Plug Power, Ballard, and OEMs and their Tier 1 suppliers.

Hydrogen is a modest fraction of our revenues today, but that's because the global use of fuel cells is relatively small. We believe hydrogen fuel cells have a place in the market. When predicted growth in adoption happens, we're poised to take advantage of that potential. While we support efforts for innovative technologies to reach marketability and critical industrial scale production, we must take advantage of today's solutions or risk higher cost to our global environment, and that solution is HPDI.

In Q2, we prepared our 2019 Environmental Social Governance Report. Our Company has evolved through the combination of several environmental start-ups and we've always been committed to ensuring the way we do business has a positive impact on our people, the environment and the communities in which we work and live.

I want to share just a few highlights from our report. All of our Italian facilities are certified as having met the International Standards ISO 14001 for environmental management systems, as has our technology centre in Vancouver. This certificate is evidence of our commitment to develop, design, test, assemble engines and fuel system components that meet or exceed the expectations of our OEM partners and customers and formalizes the effective environmental practice that processes at our facilities.

We also launched a new Code of Conduct in support of our ongoing efforts to ensure our global diverse workforce is empowered to do the right thing for the right reason and in the right way. Over 95% of our employees completed the training on our new Code of Conduct. And this year, we achieved gender parity on our Board of Directors.

We continue to be committed to delivering financial results and care just as much about the way in which we achieve those results, so I encourage you to read more about our efforts and report on our website when it's published on August 11th.

As we look out to the remainder of the year, the steady recovery of our OEM and aftermarket businesses, the growth of HPDI in Europe and the upcoming production launch of HPDI in China, are keys to our success.

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

RICHARD ORAZIETTI speaking

Chief Financial Officer, Westport Fuel Systems

Thank you, David.

As David described in the financial highlights at the beginning of the call, during the second quarter, our revenue was $36 million, which was a year-over-year decrease of $46.4 million. The decrease was mainly driven by COVID-19-related factory closures and reduced customer demand. As we discussed in our first quarter results call, our facilities in Italy were closed in April and reopened in early May. We were also impacted by the temporary closure of our HPDI and launch partners' facilities in April. As most of our businesses have now reopened, we are seeing improvements in demand and are expecting moderate recovery through the remainder of the year. Perhaps most encouraging is that we are seeing stronger HPDI orders than previously expected.

Consolidated gross margin for the quarter decreased by $7.1 million or 37%, to $12.2 million compared to $19.3 million for the comparative period in 2019. Gross margin decreased due to lower overall sales during the quarter and contractual HPDI price reduction. Offsetting the sales decline was a $7.7 million insurance recovery recorded in the current quarter which related to the $10 million charge we took in the first quarter for our field service campaign for the replacement of Pressure Release Devices.

Consolidated operating expenses for the quarter ended decreased by $14.7 million to $10.5 million or 58%. Operating expenses were lower due to government wage subsidies, compensation reductions and reduced spending in the current quarter. In addition, we had an unrealized foreign exchange gain of $3.6 million due to appreciation of the Canadian dollar.

Net income of $3 million increased by $5.3 million compared to the second quarter in 2019, as a result of a $7.7 million insurance recovery that I spoke of, while lower operating expenses due to government wage subsidies, salary reduction and the higher foreign exchange gains. And, this was partially offset by lower gross margins and lower earnings from our CWI joint venture.

We saw a similar improvement in EBITDA. Compared to the prior year quarter, EBITDA increased by $5.2 million, from $4 million to $9.2 million. After adjusting for non-cash and nonrecurring items, year-over-year Adjusted EBITDA decreased by $1.9 million, from $8.1 million to $6.2 million.

Excluding the insurance recovery, Adjusted EBITDA would have been negative $1.5 million for the quarter.

Turning to our business unit performance, OEM revenue was $19.1 million during the current quarter, which decreased by $25.6 million year-over-year, mainly due to facility shutdowns and the HPDI price reductions. We expect to see a recovery in sales during the second half of 2020, as HPDI sales volumes return to pre-COVID-19 level and continue to grow. The OEM business segment generated operating income of $1.1 million during the quarter, and this was mainly due to the $7.7 million insurance recovery.

The Independent Aftermarket generated revenue of $16.9 million during the quarter, a decrease of $20.7 million year-over-year, mainly due to the shutdown of our plants in Carasco and Albinea in Italy, during the pandemic. On an optimistic note, customer demand has been recovering steadily over the past three months. Due to austerity measures taken by management and wage subsidies, the operating loss in the Independent Aftermarket business segment was $1.2 million and not a larger deficit.

CWI's operating income decreased by 32% year-over-year due to lower sales driven by OEM factory shutdowns and reduced customer demand due to COVID-19. The equity income from the joint venture was $4.1 million, which was down 31% year-over-year due to lower CWI earnings driven by a 21% decrease in sales.

Now turning to liquidity. During the quarter, we had a net cash outflow of $10.2 million. Our operational cash flows were impacted by reduced sales volumes from factory shutdowns caused by the pandemic and a buildup of inventory as a precautionary measure to secure our supply chain. Further, we were also impacted by lower dividends from CWI. During the quarter, we also made our annual royalty payment to the Cartesian Group, which was partially offset by a new financing secured from UniCredit under the Italian Government Liquidity Decree.

In response to the financial impacts of the pandemic, we have also taken actions to reduce costs, obtain wage subsidies from governments and other support programs and delay noncritical projects and capital expenditures. We executed against our plans to refinance the Company to improve liquidity and our ability to finance the growth of the Company. Over the past several months, we have successfully completed over $50 million in new financing and refinancing, which has significantly improved our liquidity.

Over the next year, we will continue to evaluate our financing needs to ensure alignment for the long-term growth plans of our businesses. We are confident that our action plan will provide us with the necessary liquidity to meet our obligations as they come due and provide the capital to continue to grow our business.

With that, I turn it back to you, David.

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Thank you, Richard. To recap, we remain focused on a few key priorities for the second half of the year; the successful launch of HPDI in China, continued cost reduction, new light-duty and heavy-duty OEM businesses in key market categories, profitable growth of our light-duty business for both aftermarket and OEM channels. Despite the near-term uncertainty, a stronger regulatory ecosystem is still there and so is the strong desire for a green recovery. I'm confident in our team and we're committed to delivering.

Westport Fuel Systems is market-ready, tested in gaseous fueled vehicles to achieve scale in many market segments. With the potential of renewable gas to offer a net zero carbon solution, we're ready to be part of the economic recovery.

With that, I'd like to turn it back to the Operator to take your questions.

Operator

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

Our first question comes from Eric Stine of Craig-Hallum. Please go ahead.

Eric Stine - Analyst, Craig-Hallum Capital Group

Hi David, Hi Richard.

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Morning.

Eric Stine - Analyst, Craig-Hallum Capital Group

Morning. So, I appreciate all the colour. I was just wondering, maybe by end market, take it a little further, would love to just hear some discussion about trends you're seeing by segment early here in third quarter.

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

So, just to get started today, thanks for your question, Eric. Generally, we're seeing the recovery that we were hoping for. Of course, steeper would have been better, but month-over-month, we do see the markets coming back, and so that's encouraging. I think this speaks more than anything else to the fundamental need we have as society for transportation, whether it's of people or freight, we need our vehicles and then we need them to be clean, and so, I think overall, we're happy to see the market coming back, and that's looking good.

We do see a stronger recovery on the commercial side, so on commercial trucking and with our HPDI product than we do on the consumer side, but we think that's just a timing thing more than anything else. People can defer their purchases, and I would say people were harmed by the COVID-crisis around the world in a significant way, and it takes some time for that to come back.

But overall, the green recovery that we see and the actions that governments are taking are really supportive of our mission to help clean transportation. And so, on a long-term basis, we feel good. In the near-term, we're pushing very hard to see that recovery come back across all the segments.

Eric Stine - Analyst, Craig-Hallum Capital Group

Yes. Good, and maybe just digging in on HPDI a little bit. I know you've always had the issue where you're a step removed from the ultimate fleet customer. But, I would love to just get your thoughts on the confidence there. I mean, you're clearly more confident there than in the other parts of their business. I mean, do you attribute that to that there's some pent-up demand and so you took a quarter or quarter and a half off because of COVID, and now things resume? Or is there something else to that dynamic?

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Well, I would say it's really important in the commercial trucking industry around the world just to think about some of the fundaments. So, you know, fleet goes to buy trucks, fleets using trucks. And when you have what we have happening in Europe with, in a sense, it's like Germany has to basically exempt natural gas trucks and extend that to 2023, I mean, that is a huge economic impact. We have to understand that in the world of trucking, these are businesses that are working to move freight for their customers and make money doing it. And so when you have an advantage like a road toll tax exemption and then you look at the fundamental advantage that our technology offers in all markets around the world of saving money on fuel, which is such a substantial portion of the cost, if we go back 12 or 18 months, where you're talking about the product's new and people are testing it out, they're trying to buy one or two, and we're moving beyond that phase, which is really what we've anticipated and looking forward to, where basically fleets are saying, no, I've heard from the other place, I've seen and I heard about this road toll tax, and all these factors are coming together to drive demand.

In previous calls, I've mentioned the fact that we were coming up on the conclusion of the baseline measurement period for the CO2 standard for commercial truck companies in Europe. And, that deadline came and went at the end of Q2, and so, the baseline is now established. And, if you dig into any of those reports, you can see that long-haul trucking has an absolutely fundamental weighting of on the order of 70%, 80%, depending on what exactly you categorize as long haul.

But it's really the factor in having OEM be able to achieve their targets in 2025 and 2030. And so now, as I mentioned in my comments, the race is on to meet those targets. And so, I think all those factors are coming together to be really supportive of our business and the growth of that business. So overall, we're pleased about that dynamic playing out in the market right now.

Eric Stine - Analyst, Craig-Hallum Capital Group

Yes. And then my last question, and you kind of read my mind there, but on the baseline now being set, so it sounds like part of that is your current partner, now is really incentivized to push on HPDI. But curious how that's starting to impact or continuing to impact conversations with new potential partners.

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

I think the most important thing here that I was worried about in the COVID period and has not come to fruition is that no one is backing down from the requirements in 2025 and 2030, with respect to CO2 emissions from commercial trucking or for passenger cars, for that matter. And so, like it is on your mirror, objects are closer than they appear. It's coming, right? We have this deadline. As an industry, we have these penalties that are looming and we have this need in the world to clean up transportation, reduce CO2. And I think the markets and our customers and prospective customers are increasingly recognizing that we can help them meet those requirements. And certainly, our lead customer is showing the way.

Eric Stine - Analyst, Craig-Hallum Capital Group

Okay, thank you.

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Thank you, Eric.

Operator

Our next question comes from Colin Rusch of Oppenheimer. Please go ahead.

Colin Rusch - Analyst, Oppenheimer and Company

Thanks so much. Can you provide us with any sort of visibility on when you expect orders to begin in China and how that cadence might be? Obviously, you're very close with your partner there, but want to get a sense of if you're getting any indications around timing on that at all.

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Yes, so thanks for the question, Colin. Good to hear you this morning. Fundamentally, we've received orders and filled orders. So as the—filling the pipeline of product. So, we know the actual commercial launch of engines and then vehicles is on the horizon, it's coming, but the acceleration of those orders is pending the actual certification release from the Chinese authorities.

And so that is, as you know, it's been kind of a—first there was COVID, and then there was this, let's say bureaucratic challenge and so, we have had, I would say a significant delay in that regard that we don't appreciate and had to work through, and hopefully the last step we're working through will happen. But we've already received orders and will fill those orders to basically fill the pipeline so that we can start production, or so our customer can start production, their customers can start production. But yes, we're missing a piece, as you can appreciate.

Colin Rusch - Analyst, Oppenheimer and Company

Yes. Got it. Okay. And then just shifting gears to the hydrogen. I appreciate the commentary around that and the gas expertise. I guess, can you speak to the opportunity near term as folks go through the early stages of vehicle development, how engaged you are with those folks and what that opportunity might look like over the next couple of years? And then how you start to think about content per vehicle as we get into some real viable solutions in 2022, '23?

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Absolutely. I think, for us, it kind of seems like just another, if you will, right, because we're in the gaseous fuels business, that's our specialization, and as I mentioned in my opening comments, there's a beauty and an elegance to the circular economy that hydrogen potentially has.

But we're already a leader in that market, primarily in off-road applications materially with our customer Plug Power and supporting customers like Ballard. But as I think about how that unfolds, to the point of your question, we're working heavily with customers around the world that are pursuing this technology, you know, China, Japan and North America and so forth. So, we have a very good engagement with customers that are developing product and we're supporting them strongly. And yes, we're exciting about the opportunity.

But I do have to be cautionary in my kind of outlook, because there's a lot of work to be done to go from prototypes to production to volume on all these on-road applications. I think you're aware that in North America, we have some fuel cell vehicles that are already in the marketplace, but it's a small world and only a few refueling stations. And in places like Europe, we have very little so far.

So, there's a fair runway to go, but we do think it's an important technology to support and a very big opportunity for our industry and transportation in general to decarbonize and so, while governments are supporting it and industry is supporting it, we're there also to support it with the kind of components that they need to go along with the fuel cell and provide a system in total for delivering the fuel from the tank to the fuel cell.

Colin Rusch - Analyst, Oppenheimer and Company

Thanks so much.

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Pleasure.

Operator

Our next question comes from Rob Brown of Lake Street Capital Markets. Please go ahead.

Robert Brown - Analyst, Lake Street Capital Markets

Good morning.

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Good morning.

Robert Brown - Analyst, Lake Street Capital Markets

Just wanted to follow up on the HPDI business. I think you talked about stronger order activity you expected in the second half, and could you just maybe clarify that a little bit in terms of do you see pre-pandemic levels, kind of getting back to there or do you see growth beyond that? And sort of how fast is that ramp looking to you at this point?

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Yes. Thanks for the question, Rob. Good to hear you this morning. So fundamentally, as you know, from 2018 when we launched to 2019, we saw significant growth. And we forecast going into 2020 that growth would continue and that we would see further increases as the product gains traction and LNG infrastructure builds out, and so that was kind of our plan. Clearly, the COVID crisis, pandemic, there were actions around the world, the shutdowns of our customers, the shutdowns of our plants, just punched a big hole in our plan. But what we see actually is that with the order that we're receiving in Q3 and Q4, we have an opportunity to make up for those losses in total and perhaps do better than our original plan. So, there's lots of work to be done and nothing's done until it's done, but overall, the outlook is quite positive for the next two quarters.

Robert Brown - Analyst, Lake Street Capital Markets

Okay. Great. Great, and then, I think you touched on it a little bit, but just wanted to get a little more detail on the activity by the industry in responding to these environmental regulations. How much are other partners, potential partners looking at LNG versus hydrogen? And, is it a both kind of discussion or are they picking one technology versus the other?

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Yes. I think one of the things that's clear to all the companies that we work with around the world to explore, develop and bring to production our technology is that our technology is ready, it's validated, it's well known, it works, it has a low total cost of operation, the refueling infrastructure's there and their customers are seeking it.

So, this is mounting day-by-day, quarter-by-quarter and we took, of course, a big pause because of COVID in terms of that ground swell and that activity as customers and us, we all constrained our working hours and focused on keeping our companies going in the COVID period. So, we're seeing that come back and now time has passed and the requirements of 2025 and 2030 are closer than they were before the pandemic and so, I think we're a known quantity.

There's been a lot of discussion, as you know, in Europe around hydrogen's right there or electrification's right there, we should do that, and we could just skip LNG. I think there is a growing realization, in fact, that those products aren't available right now and that 2025 is closer than you thought and that our product is something that's ready, it can be deployed in response to that. So, I'm overall bullish and don't have any announcements to make today but look forward to the chance to make those announcements in the future.

Robert Brown - Analyst, Lake Street Capital Markets

Okay, great thank you. I'll turn it over.

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Thanks, Rob.

Operator

Our next question comes from Amit Dayal of H.C. Wainwright. Please go ahead.

Amit Dayal - Analyst, H.C. Wainwright

Thank you. Good morning David. Good morning Richard. With respect to, you know, your China efforts, you said you've received orders but not shipped them. Is that correct?

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

So, we received and shipped some and we've got some still to build, so this is the normal process, I would say, of filling the pipeline of the preproduction parts and then production-ready parts and then regular order flow. We are not into the regular order flow at this point in time, but we do have an order that's not yet filled that we'll fill likely in Q3.

Amit Dayal - Analyst, H.C. Wainwright

Understood. So, these are just like in the 10s, not the 100s? I mean, is that the way to look at it?

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Yes. I can't go into the quantities, but they're meaningful to us and they are representative of the launch similar to what we did with our launch partner in Europe two years ago.

Amit Dayal - Analyst, H.C. Wainwright

Okay. Understood. That's good to hear. With these loans and grants, etc. that you've taken on in the past few months, are there any particularly restrictive terms or comments associated with any of that, that you know, we should be aware of?

RICHARD ORAZIETTI speaking

Chief Financial Officer, Westport Fuel Systems

Hi, Amit. No, there's no—we're just regular commercial terms, nothing restrictive.

Amit Dayal - Analyst, H.C. Wainwright

Okay. Understood.

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Yes. Frankly, a lot of the loans we've gotten have really improved our cost of capital and extended our maturities and so, the government-supported financing has been really, I would say friendly to industry. And so, we were pleased with what was on offer and glad to have been able to secure it with our team in Europe, for example, and as part of UBC also.

Amit Dayal - Analyst, H.C. Wainwright

Understood. And then with respect to sort of the recovery you're seeing, you know, you're back and sort of all your locations are open again, you're functioning, I guess at somewhat normal levels probably. From here do we see some sequential improvements for the remainder of 2020 compared to what we did in the second quarter?

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Yes, so the crystal ball, of course, is never perfectly clear, but what we are seeing, as Richard mentioned, is kind of month-by-month improvements back towards “normal levels”. There's a lot of uncertainty in the market still. You know, we have the daily reports of new outbreaks and new lockdowns and second waves and all these things, which really does weigh heavily on the marketplace. And of course, I think people also look at all the spending done by governments and think about the general economy and unemployment, so there's a lot of anxiety and uncertainty still to play out.

But so far, you know, we're seeing step-by-step increases. To have a 56% revenue drop in Q2, typically our best quarter, is a huge blow to our Company. I'm very, very proud of the work we've done to endure it and get through it with the liquidity measures and support of our governments and partners around the world. But, we do see that recovery step-by-step, and we're hopeful that by the end of this year we can say that 2021 will be not just a normal year, but an up year for us.

Amit Dayal - Analyst, H.C. Wainwright

Understood. That’s all I have guys. I’ll take my other questions of line. Thank you.

RICHARD ORAZIETTI speaking

Chief Financial Officer, Westport Fuel Systems

Thank you.

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Thanks, Amit.

Operator

Once again, if you have a question, please press star, then one.

Our next question comes from Jeff Osborne of Cowen and Company. Please go ahead.

Jeffrey Osborne - Analyst, Cowen and Company

Hey good morning guys. Most of them have been asked, but a couple on my end. I think you mentioned in the prepared remarks about a reduction in price with HPDI. Did I hear that correct? And can you just expand on that if I did?

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Sure. As a part of our long-term supply agreement with Volvo, we did have—excuse me, with our European supply customer, we did have some price reductions that were structural. The way you can think about that is low volume, higher-priced, higher volume, lower-priced. It's pretty normal in the business and we've been seeing those and having to explain those, if you will, as the quarter-over-quarter margins have been decreasing. The fix to that, of course, is to continue the volume up curve and get the cost down and bring the margin back. And so, that's certainly in our plans and you'll see that unfold in the quarters ahead.

Jeffrey Osborne - Analyst, Cowen and Company

I guess maybe I would have thought the opposite would have happened, if the volumes are down, the price went down as well, but as the volumes rebound—I just want to make sure I understand that. Was it just a cadence of time or straight volume? Is there like break points like every six months the price goes down regardless of volume? Or if they buy 100 units it's one price, if it's 500 units it's a different price?

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Yes, I can't go into the details of the contract, obviously. But clearly what we have had is pricing at the start of production that's higher than pricing we have now and that will stabilize and then we're doing the work to bring the cost down. So, it was more a time-based contract than a volume-based contract, but the fundamental was built on the volume, saying that the early units would have higher prices.

Jeffrey Osborne - Analyst, Cowen and Company

Got it. Okay. And then you mentioned Italy on the passenger car side was starting to do better. Are there any other markets that you're seeing as green shoots?

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Yes. I think, you know, we didn't talk a lot about—we talked a little bit about it, but India's a very important market for us, and they're, I would say, still struggling to come out of the crisis and the pandemic. But at the same time, the standards there that changed the game in India played out without a change to the schedule. So, that is the change to Bharat Standard-6. And this is a story really where basically the advent of Euro 6 brought—and 6 means the cost of diesel engines, are going up quite dramatically because the after-treatment that has to be added to meet that standard. And those costs being very high, people look for alternatives, and natural gas vehicles are an excellent alternative and they already have a significant infrastructure in place.

So, as a result of that, we're seeing strong demand for our product in that marketplace, and contacts from additional customers saying we need to offer the product, can you help us? And so, it's really a very positive sign for us that the Bharat Standard-6 was not delayed but came into effect right in the middle of the COVID recovery on April 1st of this year. And so, we're excited about the opportunities in that market and we already have a very strong position working with really almost every single manufacturer in India to help them bring their natural gas products to the marketplace. In that market, for example, there are—some of our customers have dropped diesel and gasoline entirely and all they're offering is natural gas and LPG vehicles. And so those kinds of changes are really significant and really bode well for our business.

Jeffrey Osborne - Analyst, Cowen and Company

Makes sense. It's great to hear. And then the last question I had is, you made reference to a possible subsidy or support around green initiatives for transportation in Italy, and I think you even said details are limited. But to my understanding, some of the other countries in Europe that have had COVID-related support for transportation was more around electrification. Is there anything in the public domain out of Italy that would suggest that LPG or any other gaseous fuel would be supported?

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Yes, so our understanding of what's being developed, I do believe that I referenced in the opening comments, was a support structure for all sorts of technologies, including ours, which would also include the electrification, hybridization, you know, if there's a fuel cell vehicle, whatever. So, I think they're taking an agnostic approach or even a comprehensive approach to those technologies that support their environmental goals and incentivizing the recovery of those disproportionately, which obviously works in our favour.

A key ingredient is the government can put in, any government without anybody else, can put in a structure that says, here's an incentive for clean technology. And then, it's really about what customers want to buy, what they can use and what's available for manufacturers. So, if you incentivise something that's not available, then nothing's going to happen. But our products are available on the marketplace and doing very well, so as an example, earlier this year, pre-COVID, there was some huge increase in the number of natural gas vehicles registered in Italy. I forget the number. It was above 50% increase in the registrations year-over-year. Again, that was a pre-COVID metric, but I think we quoted it in our Q1 call, actually. But so, the market's moving in that direction and the kind of support we get from the government then applies to many technologies, including ours is what we expect.

Jeffrey Osborne - Analyst, Cowen and Company

Perfect. That's all I had. Thank you so much for the detail.

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Pleasure, Jeff. Good to talk to you.

Operator

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

DAVID M. JOHNSON speaking

Chief Executive Officer, Westport Fuel Systems

Yes. Thank you very much. I appreciate everybody joining the call. As you can well understand, not just us, but around the world, COVID has been an absolute challenge for business and we're amongst that. I am very pleased with the work that we've done to get through it to take care of our team members, to support our customers as they close and reopen and their changing demand. And now we're seeing the recovery that gives us hope that the future is a greener future that we can support and grow into.

So overall, I think we're through this crisis to a large degree. There's still some uncertainty in the future, but overall, we're on a good path and I think we're well positioned to grow and prosper in the coming future. Thanks again for your time and support.

Operator

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