

BASIS OF PRESENTATION

This Management's Discussion and Analysis ("MD&A") of the financial results of Westport Innovations Inc. ("Westport", "the Company", "we") should be read in conjunction with, and is qualified by, Westport's Consolidated Financial Statements and related notes for the year ended March 31, 2007 (the "Financial Statements"), which have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). All of the information presented herein is expressed in Canadian dollars, unless otherwise stated. Certain prior year amounts have been reclassified to conform to the current year presentation.

This MD&A contains forward-looking statements, including statements regarding the future success of our business and technology strategies and future market opportunities. These statements are neither promises nor guarantees, but involve known and unknown risks and uncertainties that may cause our actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activities, performance or achievements expressed in or implied by these forward looking statements. These risks include risks related to our revenue growth, operating results, industry and products as well as other factors discussed below and elsewhere in this report. Readers should not place undue reliance on any such forward-looking statements, which speak only as of the date they were made. We disclaim any obligation to publicly update or revise such statements to reflect any change in our expectations or in events, conditions or circumstances on which any such statements may be based, or that may affect the likelihood that actual results will differ from those set forth in the forward looking statements.

Additional information relating to Westport, including our Annual Information Form, is on SEDAR at www.sedar.com.

This MD&A is dated May 31, 2007.

BUSINESS OVERVIEW

Westport is engaged in the research, development and marketing of high performance, low-emission engines and fuel systems which use gaseous fuels such as natural gas, propane or hydrogen. We expect strong demand for these products for transportation, power generation and industrial applications because of the performance, emissions characteristics and life-cycle costs when compared to alternatives now available or known to be under development for these applications. We believe that growing public concern over the environment, high oil prices and national energy security issues in the United States, China and Europe will drive demand for our products and services.

To encourage customers to adopt natural gas solutions for their transportation requirements, our strategy is to provide integrated solutions from fuel supply and storage through to service and support. To do so, we develop

our technologies and products in cooperation with the world's leading engine, component and vehicle manufacturers and fuel infrastructure providers. We target markets where there are lifecycle cost advantages arising from favourable fuel pricing differentials between natural gas and diesel and/or where there are government incentives or mandates for lower emissions. We currently have one operating segment, which involves the research, development, and related commercialization of engines and fuel systems operating on gaseous fuels such as natural gas and hydrogen for the on-road commercial vehicle sector. Within that operating segment, we break down our focus into four strategic pillars: profitably growing Cummins Westport Inc ("CWI"), our 50:50 commercial joint venture with Cummins Inc ("Cummins"); launching our liquefied natural gas ("LNG") systems for heavy duty (Class 8) trucks in North America and Australia; developing new alliances and enabling new market segments; and maintaining our technology leadership with innovative ideas and collaborative research.

Our first pillar, CWI, is focused on the development, marketing and sale of mid-range, spark-ignited natural gas or liquefied petroleum gas ("LPG") engines for transit bus, shuttle and urban specialty vehicles such as refuse trucks. Geographically, CWI's revenues are derived primarily from North America with strong interest and markets developing in Asia, Europe and South America. CWI manufactures its engines in the United States, India and China through facilities owned and operated by Cummins and its affiliates. CWI's strategy is to grow profitably by leveraging its parents – Cummins for its global manufacturing, distribution and service support network, and Westport for its worldwide natural gas focus and expertise, industry relations and technology leadership. Since January 1, 2004, CWI revenues, expressed in US dollars to exclude foreign exchange distortions, have grown at more than 30% annually. In fiscal 2007, CWI contributed \$4.4 million to Westport on a pre-tax basis, more than double the fiscal 2006 contribution of \$1.6 million. Our share of the assets, liabilities, revenue and expenses of CWI are disclosed separately in note 17 of our Financial Statements.

Our second pillar focuses on the introduction of high-performance LNG systems for heavy duty trucks. This product line incorporates our proprietary direct injection technologies which allow us to deliver a natural gas-fueled version of the latest original equipment manufacturer ("OEM") diesel engines and match the base engine's efficiency and performance without changing the base engine design, thereby minimizing the disruptions to the manufacturer and to the customer in switching fuels. In order to deliver LNG to our engines, we have developed proprietary integrated LNG fuel pumps and storage tanks to form a complete system and to support the adoption of LNG systems, we also work with engine, truck, component and fuel providers as necessary to provide integrated solutions for customers.

Our third and fourth pillars focus on developing new OEM and supply relationships and new innovative technologies. We cooperate or have cooperated on fuel delivery system development programs with a number of

companies including Beijing Tianhai Industry Co. Ltd ("BTIC"), Cryostar SAS ("Cryostar"), Ford, BMW, Isuzu, and Cummins and are in various stages of negotiations to develop and commercialize our technologies with other global leaders.

As at March 31, 2007, we also held an approximate 6% investment interest in Clean Energy Fuels Corp. ("Clean Energy"), North America's largest provider of natural gas fuel and service infrastructure for vehicles.

FISCAL 2007 DEVELOPMENTS

In our fiscal year ended March 31, 2007, we closed two significant financial transactions. On June 12, 2006, we agreed to issue up to \$22.1 million in 5-year secured, subordinated, convertible notes with a coupon rate of 8% to Perseus LLC ("Perseus"), a private equity fund management group. The notes were issued in two tranches of \$13.8 million and \$8.3 million, respectively, with the first tranche completed in July, 2006 and the second tranche completed in January, 2007. Interest is payable semi-annually in arrears, on June 30 and December 31, in additional notes or shares at our option, for the first two years.

After the first two years, interest will be calculated at a rate of 8% on the outstanding principal amount of the notes only for the number of trading days in the period on which the share price is below \$3.00 and is payable semi-annually in cash, additional convertible notes or shares at our option. The first tranche is convertible to common shares at a conversion price of \$1.30 at any time during the term of the notes and the second tranche is convertible to common shares at a conversion price equal to \$1.40. At the time of issuance of the notes, the noteholders also received warrants to acquire, at an exercise price equal to the conversion price of the accompanying notes, common shares of Westport equal to 25% of the number of common shares into which the notes are convertible. The warrants expire four years from the date of issuance and include a cashless exercise provision which allows the noteholder to receive the number of common shares having a value equal to the net gain that would be realised by the noteholder had the warrant been exercised for cash and the related shares sold at the market price on the date the option is exercised. Any warrants converted under the cashless exercise provision will be cancelled. For so long as Perseus continues to hold notes and warrants convertible into a specified percentage of Westport's issued and outstanding shares, Perseus also has the right to nominate two of seven board seats. The notes are secured with a second charge on all of our assets.

	Issuance Date	Principal - CDN	Conversion Price	No. of shares	No of warrants
Tranche 1					
Initial Closing	12-Jun-06	5,523,000	1.30	4,248,462	1,062,115
Interim Closing	14-Jul-06	8,284,500	1.30	6,372,692	1,593,173
		13,807,500	1.30	10,621,154	2,655,288
Tranche 2					
	16-Jan-07	8,284,500	1.40	5,917,500	1,479,375
Total of Tranche 1 and 2		22,092,000		16,538,654	4,134,663

We accounted for the \$22.1 million in convertible notes as follows: \$7.6 million assigned to conversion options, \$1.4 million assigned to the warrants and \$13.1 million assigned to long-term debt. During the year, we recognised \$1.7 million in interest and amortization of discount, paid interest of \$0.5 million, net of withholding tax, through the issuance of 401,520 shares and accrued \$0.4 million in interest as at March 31, 2007.

On June 13, 2006, we entered into an agreement with Matco Capital Ltd. ("Matco"), an unrelated party, to reorganize Westport Research Inc. ("WRI"), at the time, a wholly owned subsidiary of Westport. As part of the reorganization, we substantially transferred all of the assets, liabilities and operations of WRI to another wholly owned Westport company, Westport Power Inc., which carries on the business previously carried on by WRI. On closing and post-reorganization, we sold 45% of WRI to Matco for \$4.2 million in cash consideration and recognised a gain of \$3.9 million net of related transaction costs. In addition, Matco facilitated access to a limited recourse credit facility for \$9.7 million secured only by a pledge by us of 4% of the total shares in WRI and other Matco collateral. Under the terms of our original investment agreement with Matco, the full amount was only drawable under the limited recourse credit facility if a previously identified transaction was completed before December 31, 2006. However, as this transaction did not occur, drawings under this credit facility were limited to \$7.3 million. Proceeds from the sale of our remaining shares in WRI are to be first applied to repay the loan. During the year, we drew the full amount available to us under this credit facility of \$7.3 million. We paid interest of prime plus 1% on amounts drawn until December 31, 2006, after which time Matco is responsible for bearing such interest costs.

In February, 2007, WRI, renamed "Wild River Resources Ltd" ("WRRL"), completed a \$25.5 million private placement by issuing additional shares, thereby diluting our ownership percentage from 55% to approximately 17.5%. This dilution resulted in a net dilution gain of approximately \$4.0 million. As part of that transaction, we also recognised a gain of \$0.2 million on the disposition of an additional 1.5% interest in WRRL reducing our investment to approximately 16% as at March 31, 2007. Other than \$0.6 million received from the sale of this

interest used to pay down our limited recourse credit facility, there were no cash inflows or outflows to Westport as a result of this transaction other than associated legal costs. As a result of our change in ownership percentage and resulting loss of control, we no longer consolidate WRRL and we account for our remaining investment in WRRL on a cost basis.

During the year, we saw increased interest globally in our products and technologies amidst growing public awareness and concerns over climate change and the environment, as well as continued instability in several oil-producing regions. In the United States, in January 2007, President Bush announced a long-term goal for alternative fuel deliveries of 35 billion gallons (gasoline gallon equivalents) per year to reduce US dependence on imported oil. Westport and its partners believe that natural gas will form a large part of this move to alternative fuels.

As the first step in a comprehensive five year Clean Air Action Plan, the San Pedro Bay Ports (Los Angeles and Long Beach, California) announced US\$22 million in financial incentives to assist fleets serving the Ports of Los Angeles and Long Beach to replace older trucks with new ones powered by Westport LNG engines. The Port plans to announce funding recipients mid-2007 with deliveries starting soon after. In all, the Ports' action plan calls for the replacement of 5,300 older diesel trucks with new trucks fueled with LNG by 2011.

In Australia, our near term focus has shifted from off-road to on-road applications as we were awarded AUD\$1.4 million from the Australian government to demonstrate and evaluate the use of LNG as a fuel for heavy duty highway trucks in Australia, where natural gas enjoys a significant price advantage over diesel. We expect to be able to adapt our North American product to Australian engines and operating conditions by increasing horsepower and torque and adjusting emissions to meet Australian standards.

In Asia, in July, 2006, we signed a joint venture agreement with BTIC, a Chinese-Korean company with its headquarters and manufacturing facilities in Beijing, China. The joint venture, BTIC Westport Inc. ("BWI"), will leverage BTIC's manufacturing expertise and Westport's LNG tank design to sell and market LNG tanks for natural gas fuelled vehicles globally. Through the 50:50 joint venture agreement and related license and supply agreements, BTIC and Westport will share equally in the profits on products developed and sold by the joint venture. BTIC and Westport will each contribute US\$0.4 million to the formation of the venture. Initiation of formal joint venture business operations is subject to customary government approvals which were received in April, 2007. In the interim, BTIC has established LNG tank manufacturing facilities and has been producing LNG tanks to our design.

In July, 2006, we also announced the completion of a License and Supply Agreement with Cryostar SAS, a division of the BOC Group and a global leader in cryogenic pump products, for the development, manufacture and

supply of cryogenic LNG fuel pumps, based on Westport's cryogenic technology. The off-engine LNG fuel system, consisting of the LNG fuel pump and LNG tank, is a critical component of the overall high pressure direct injection ("HPDI") vehicle solution.

These agreements with BTIC and Cryostar form an integral part of Westport's strategy to secure long-term business alliances that will ensure a reliable supply of leading-edge, top quality components for our LNG transportation solutions, including our heavy duty LNG truck program.

We also completed the December 2005 CNG-DI development contract with Isuzu of Japan as planned. As we and Isuzu do not yet have a mutually agreed plan for commercial production of CNG-DI Isuzu vehicles, we have agreed to conclude the cooperative development program at this point. Technical resources allocated to the Isuzu Elf program were reassigned to other strategic programs during the fourth quarter of fiscal 2007.

On the government funding side, the work phase of our Contribution Agreement with the government of Canada's Technology Partnerships Canada programme ("TPC") ended March 31, 2006 pursuant to the existing terms and schedules in the agreement. However, we continued to work with TPC, now renamed the Industrial Technologies Office, to extend the work phase of that agreement to fund continued development of our vehicle technologies on a retroactive basis from April 1, 2006 and we continued to make progress claims to TPC. For the first three quarters of fiscal 2007, we did not reflect these claims in our financial results as we had not received approval from TPC. After reaching agreement with TPC on a two year extension, we accrued \$2.2 million in claims and reversed approximately \$1.0 million in royalty payments in the fourth quarter of fiscal 2007. To March 31, 2007, we have claimed or accrued approximately \$17.7 million of the \$18.9 million under our TPC agreement.

SELECTED ANNUAL FINANCIAL INFORMATION

	Fiscal Year ended March 31		
	2007	2006	2005
<i>Expressed in thousands of Canadian dollars, except for per share amounts, shares outstanding and units shipped</i>			
Units shipped	2,001	1,327	1,277
Total revenue	60,480	43,552	34,436
Gross margin	22,099	14,910	10,674
GM %	37%	34%	31%
Net loss	(11,307)	(16,860)	(26,209)
Net loss per share – basic and diluted ⁽¹⁾	(0.15)	(0.23)	(0.38)
Weighted average shares outstanding	75,174,826	74,228,495	69,381,968
Cash and short-term investments	23,081	7,832	20,291
Total assets	59,633	29,500	44,442
Long-term financial liabilities ⁽²⁾	22,648	3,497	4,609
Cash used in operations before changes in non-cash working capital	(11,325)	(8,661)	(13,571)
CWI income for the year after taxes	12,115	3,186	186
JV Partner's share of CWI income	6,057	1,593	69
⁽¹⁾ Fully diluted loss per share is not materially different as the effect of conversion of stock options, warrants and performance share units would be anti-dilutive. ⁽²⁾ Excluding current portions of warranty liability and long-term debt obligations, and Joint Venture Partner's share of income from joint venture			

Our revenues from fiscal year 2005 to fiscal year 2007 grew from \$34.4 million to \$60.5 million, or 33% per year, and margins have increased by 44% per year from \$10.7 million to \$22.1 million in the same period on increased revenues and better field experience resulting in lower warranty accruals. Net loss in fiscal 2007 improved to \$11.3 million from \$16.9 million in fiscal 2006 and \$26.2 million in fiscal 2005. Cash used in operations before changes in non-cash working capital increased in fiscal 2007 to \$11.3 million compared to \$8.7 million in fiscal 2006 primarily as the result of reduced government funding of \$3.5 million and increased expenditures associated with development activities around the launch of CWI's new ISL-G engine and our LNG systems for heavy duty trucks and with business development activities in China.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Financial statement preparation requires that we use estimates and assumptions that affect the reported amount of assets and liabilities as well as revenues and expenses. Our accounting policies are described in note 2 to our Financial Statements. The following policies have a significant impact on the consolidated Financial Statements or are impacted significantly by judgments, assumptions and estimates used in the preparation of our consolidated Financial Statements.

Variable Interest Entity Accounting

A variable interest entity ("VIE") is any type of legal structure not controlled by voting equity, but rather by contractual and/or other financial arrangements. Interests in VIE's are consolidated by the company that is the primary beneficiary. Westport has identified CWI as a VIE, determined that we are the primary beneficiary, and accordingly consolidate CWI, reflecting 100% of CWI's assets, liabilities, revenues and expenses in our consolidated financial statements and showing the 50% interest held by Cummins as "Joint Venture Partner's share of net income from joint venture".

Warranty Liability

Estimated warranty costs are recognised at the time we sell our products and included in cost of revenues. We use historical failure rates, and costs to repair product defects during the warranty period, together with information on known products to estimate the warranty liability. The ultimate amount payable and the timing will depend on actual failure rates and the actual cost to repair. Since many of our products are new to the market, historical data may not necessarily reflect actual costs to be incurred and exposes us to the potential for significant positive or negative fluctuations in the warranty liability. We review our warranty provision quarterly and make adjustments to our assumptions based on the latest information available at that time. Adjustments to the warranty provision are recorded in cost of revenues.

Revenue Recognition

Product revenue is recognised, net of estimated costs of returns, allowances, and sales incentives, when the products are shipped and title passes to the customers. Revenue also includes fees earned from performing research and development activities for third parties and revenues earned from licensing our technologies to third parties. Revenue from research and development activities is recognised as the services are performed. Amounts received in advance of revenue recognition are recorded as deferred revenue. Parts revenue is recognised as the parts are sold.

Inventory Valuation

Inventory consists of fuel systems, component parts, work-in-progress and CWI engine products. In establishing

whether or not a provision is required for inventory obsolescence, we estimate the likelihood that inventory carrying values will be affected by changes in market demand for our products and by changes in technology, which could make inventory on hand obsolete. We perform regular reviews to assess the impact of changes in technology, sales trends and other changes on the carrying value of inventory. If and when we determine that such changes have occurred and that they would have a negative impact on the carrying value of inventory on hand, adequate provisions would be made. Unforeseen changes in these factors could result in the recognition of additional inventory provisions.

Long-term Investments

We account for long-term investments in non-consolidated entities using the equity method to the extent that we have significant influence over the investee's strategic operating, financing and investing policies. All other long-term investments are accounted for using the cost method. Long-term investments are reduced to market value only to the extent that the loss in value is other than temporary. In determining market value for our long-term investments in privately held companies, we use assumptions around future cashflows from the investments, recent equity transactions involving its investees and the current financial performance of the investees to determine fair value. All our long-term investments are currently carried at cost.

Equipment, Furniture, and Leasehold Improvements and Intellectual Property

Generally accepted accounting principles in Canada require that we consider whether or not there has been an impairment in our long-lived assets, such as equipment, furniture and leasehold improvements and intellectual property, whenever events or changes in circumstances indicate that the carrying value of the assets may not be recoverable. If such costs are not recoverable, we are required to write down the assets to fair value. When quoted market values are not available, we use the expected future cash flows discounted at a rate commensurate with the risks associated with the recovery of the asset, as an estimate of fair value to determine whether or not a write down is required.

CHANGES IN ACCOUNTING POLICY

Our accounting policies are substantially unchanged from the prior fiscal year ended March 31, 2006. However, as we have started to launch our LNG fuel systems for heavy duty trucks, for clarity, our accounting policies for items such as inventory, have been broadened to include non-CWI activities as applicable.

Financial Instruments

In April, 2005, the Canadian Institute of Chartered Accountants ("CICA") issued Section 3855 Financial Instruments – Recognition and Measurement, applicable to interim and annual financial statements relating to fiscal years beginning on or after October 1, 2006.

Under Section 3855, financial assets and liabilities, including derivative instruments, are initially recognised and subsequently measured based on their classification as held-for-trading, available for sale financial assets, held-to-maturity loans and receivables, or other financial liabilities as follows:

- Held for trading financial instruments are measured at their fair value with changes in fair value recognised in net income for the period.
- Available for sale financial assets are measured at their fair value and changes in fair value are included in other comprehensive income until the asset is removed from the balance sheet.
- Held-to-maturity investments, loans and receivables and other financial liabilities are measured at amortized cost using the effective interest rate method.
- Derivative instruments, including embedded derivatives, are measured at their fair value with changes in fair value recognised in net income for the period unless the instrument is a cash flow hedge and hedge accounting applies in which case changes in fair values are recognised in other comprehensive income.

We will adopt this section effective April 1, 2007. Short-term and long-term investments will be classified as "available for sale" and, except where fair value is not determinable, will be measured at fair value with changes in fair value included in other comprehensive income until the asset is removed from the balance sheet. Deferred transaction costs related to the Perseus convertible note will be netted against the long-term debt and will be amortized using the effective interest method. We continue to review our accounting in this area including a review of all significant contracts to identify further financial instruments, derivatives and embedded derivatives and there may be other changes required. Note 19(a) of our Financial Statements highlights the fair values of our material financial assets and liabilities.

Comprehensive Income

CICA Section 1530 introduced new standards for the reporting and presentation of comprehensive income, which is the change in equity, or net assets, of an enterprise during a reporting period from transactions and other events and circumstances from non-owner sources. It includes all changes in equity during a period except those resulting from investments by, and distributions to, owners. We will be adopting Section 1530 effective April 1, 2007.

DISCLOSURE CONTROLS AND INTERNAL CONTROLS OVER FINANCIAL REPORTING

Our disclosure controls and procedures are designed to provide reasonable assurance that material information is disclosed on a timely basis. We have also designed internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP. Under the supervision of the CEO and CFO, management evaluated the effectiveness of the design and operation of the company's disclosure controls and procedures and assessed the design of the company's internal control over financial reporting as of March 31, 2007, in accordance with the Canadian Securities Administrators' Multilateral Instrument 52-109. Based on this evaluation, we have concluded that disclosure controls and procedures were effective and internal controls over financial reporting have been adequately designed to provide reasonable assurance regarding the reliability of our financial statements and reports.

We have designed additional controls over financial reporting in the fourth quarter relating to the commercialization of our products. We expect that our financial reporting policies, processes and systems will continue to evolve in our fiscal year 2008 as we continue our shift from primarily a research and development company to a commercial one shipping product at increasing volume levels. In particular, our inventory and warranty processes and systems are expected to change over the next few quarters.

FINANCIAL OVERVIEW

For the years ended March 31, 2007 and 2006, net loss decreased to \$11.3 million, or \$0.15 per share, from \$16.9 million, or \$0.23 per share primarily as the result of an \$8.1 million gain on the partial disposition and dilution of our interest in WRI and the recognition of CWI's \$3.5 million future tax benefit (\$1.7 million after taking into account our joint venture partner's share of CWI). Offsetting the gain was \$1.7 million in interest and amortization of discount on the convertible notes issued to Perseus, \$2.0 million increase in general and administrative expenses, \$1.2 million increase in sales and marketing costs and decreased government funding of \$3.5 million year over year as we substantially completed significant government funded projects in 2006.

For the years ended March 31, 2007 and 2006, total revenues were \$60.5 million and \$43.6 million respectively. The 39% increase in revenues was primarily due to increased CWI engine shipments (up 50%) and the delivery of our first LNG systems for heavy-duty trucks offset by a 5% decrease in the US dollar exchange rate. In US dollar terms, revenue growth was 44%. Our products and parts are priced in US dollars and are accordingly affected by fluctuations in the US dollar exchange rate. Cost of goods sold, including warranty, is also primarily US dollar denominated.

For the year ended March 31, 2007, CWI's revenues increased by 37% to \$58.0 million from \$42.3 million with 1993 units shipped compared to 1327 units shipped in the prior year. CWI gross margins increased by \$6.9 million year over year with most of that increasing CWI's net income. By leveraging Cummins' manufacturing and distribution facilities, CWI is able to scale its business without incurring significant additional costs. CWI earned \$8.9 million in income before taxes and recognised a \$3.5 million future income tax benefit for total income for the year of \$12.1 million. After taking into account Cummins share of CWI's net income after taxes, CWI contributed \$6.1 million to our consolidated results in the year.

RESULTS FROM OPERATIONS

Product revenue was \$47.2 million for the year ended March 31, 2007, up 58% from fiscal 2006 revenues of \$29.9 million on 2001 units shipped compared to 1327 units in the prior year. Increased revenues reflected strong CWI sales activities in North America and Asia with revenues from Asia accounting for 13% of revenues. Our geographical and product mix will vary from year to year depending on where our customers are in their order cycles and their locations. CWI also recognised approximately \$1.9 million in B-Gas production kits and components shipped to China and India for local assembly and sale in those countries.

Non-CWI revenues increased to \$2.4 million in 2007 compared to \$1.3 million in 2006 with the first 8 shipments of LNG systems for heavy duty trucks resulting in approximately \$0.8 million in revenues. In both 2007 and 2006, the balance of the non-CWI revenues related to prototype vehicle work performed by Westport for Isuzu and other OEM partners. Our development program with Isuzu ended December 31, 2006 and no further revenue is contemplated at this time.

	Year ended March 31	
	2007	2006
Total units shipped	2,001	1,327
Product	47,195	29,932
Parts revenue	13,285	13,620
	<u>60,480</u>	<u>43,552</u>

Expressed in \$000s except for units

	Year ended March 31	
	2007	2006
	(unaudited)	(unaudited)
North America	72%	82%
Asia	13%	4%
Rest of the world	15%	14%

As a percentage of revenue dollars

Parts revenue for the year ended March 31, 2007 compared to 2006 was down \$0.3 million to \$13.3 million from \$13.6 million reflecting the weaker US dollar. In US dollar terms, parts revenue increased slightly year over year. Parts revenue is a function of engine population, failure rates and price.

Cost of revenue for the years ended March 31, 2007 and 2006 was \$38.4 million and \$28.6 million respectively. The \$9.8 million increase in cost of revenues is consistent with the \$16.9 million increase in revenues. Cost of revenue includes production costs and the associated warranty. Estimated warranty costs are recognised at the time we sell our products and included in cost of revenues. We use historical failure rates, and costs to repair product defects during the warranty period, together with information on known products to estimate the warranty liability. The ultimate amount payable and the timing will depend on actual failure rates and the actual cost to repair. Historical data may not necessarily reflect actual costs to be incurred and could result in significant positive or negative fluctuations in the warranty liability. We review our warranty provision quarterly and make adjustments based on the latest information available at that time. Adjustments to the warranty provision are recorded in cost of revenues. In the years ended March 31, 2007 and 2006, CWI made changes in estimates to its warranty balance, reducing the balance by \$1.4 million and \$1.8 million in the respective years as actual claims experience has been better than the expected experience at time of sale.

Gross margin was \$22.1 million for the year ended March 31, 2007 compared to \$14.9 million for the year ended March 31, 2006 on higher product revenues and higher gross margins. Gross margin percentages were 37% and 34% respectively.

Research and development expenses, net of program funding, were \$21.9 million and \$16.9 million for the years ended March 31, 2007 and 2006 respectively. The \$5.0 million increase in research and development costs year over year was primarily the result of the following:

- Reduced government funding of \$3.5 million with major government funded projects such as the US government funded 1.2 gram project and our Canadian government funded 401 demonstration project substantially completed in 2006;
- Increased CWI research and development activities (\$1.5 million) related primarily to the ISLG engine which is being launched in the calendar year 2007; and
- Increased engineering and development work associated with our on and off-engine LNG systems and increased investment in our patent portfolio as we prepared to commercialize product.

These items were offset by a decrease of \$1.3 million in stock-based compensation in 2007 compared to 2006 reflecting a special grant of options to all employees in 2006.

	Year ended March 31		Year over year	
			% change	
	2007	2006	2007	2006
<i>Expressed in thousands of Canadian dollars</i>				
Research and development expenses	27,041	25,628	6%	5%
Program funding	(5,150)	(8,689)	-41%	45%
Net research and development expenses	21,891	16,939	29%	-8%

General and administrative expenses for the year ended March 31, 2007 and 2006 were \$6.9 million and \$4.9 million respectively with \$0.8 million related to higher bonus and stock-based compensation expense in the year with certain milestones associated with performance share units granted in fiscal years 2005 and 2006 triggering in the year. The balance related primarily due to higher public company costs, including investor relations and the establishment of an internal audit function, and increased legal and finance support activities related to commercialization of our HPDI system.

Sales and marketing expenses increased to \$7.1 million from \$5.8 million in the year ended March 31, 2007 compared to 2006 primarily because of increased business development costs in China (\$1.0 million), and costs associated with sales and marketing activities related to LNG systems offset by lower stock-based compensation expense in the year.

Foreign exchange gains primarily reflect the realised net gains and losses on foreign currency transactions and the net unrealised gains and losses on our net US dollar denominated assets and liabilities, which are mainly comprised of short-term investments, accounts receivable, and warranty liability. The Canadian dollar was relatively unchanged as at March 31, 2007 compared to March 31, 2006.

Depreciation and amortization for the year ended March 31, 2007 compared to 2006 decreased by \$1.3 million to \$1.4 million from \$2.7 million primarily as the result of certain intellectual property, equipment and furniture becoming fully amortized in the year ended March 31, 2006 and because we changed the estimated remaining useful life of our research and development machinery and equipment from five to eight years in the second quarter of fiscal 2006.

Interest on long-term debt and amortization of discount of \$1.7 million in the year ended March 31, 2007 relates to the interest and the accretion on the convertible notes issued to funds managed by Perseus. Interest is being accrued at 8% per annum and is payable in notes or in common shares on June 30 and December 31 of

each year for the first two years, after which time, the interest may be payable in notes, common shares, or in cash. Canadian GAAP requires us to separately value the debt and equity components of convertible debt as well as the warrants issued in connection with the financing. Accordingly, the value of the warrants (\$1.4 million) and the value of the conversion feature (\$7.6 million) as calculated using the Black-Scholes option pricing model are shown on the balance sheet under "Other equity instruments" and the amount allocated to the debt of \$13.1 million is included in "Long-term debt" and is being accreted to its face value using the effective interest rate method. As at March 31, 2007, the long-term debt amount, including accretion to date, was \$13.7 million.

Gain on sale of interest in subsidiary of \$8.1 million relates to the gain, net of expenses, on the sale of 45% of our interest in WRI in the second quarter of this fiscal year and the dilution gain recognised in the fourth quarter of 2007 when our interest in WRI was diluted from 55% to 16% and we changed our accounting for WRI from the consolidation method to the cost method.

Joint Venture Partner's share of income from joint venture reflects Cummins' 50% share of CWI net operating contribution. For the year ended March 31, 2007, Cummins' share of CWI was \$6.1 million representing 50% of CWI's pre-tax income of \$8.9 million (2006 - \$3.2 million) and 50% of CWI's net tax recovery of \$3.3 million (2006 - nil). For the year ended March 31, 2006, Cummins' share of CWI was \$1.6 million, representing 50% of CWI's net income for the year.

Income tax recovery was \$3.1 million in the year ended March 31, 2007. The income tax recovery arose on recognition of \$3.5 million of future tax assets consisting primarily of loss carryforwards from CWI offset by current taxes payable. In prior years, these losses were fully offset by a valuation allowance but as CWI has generated taxable income for two consecutive tax years and we expect that CWI will generate taxable income in the future, a portion of its loss carryforwards has been recognised.

CAPITAL REQUIREMENTS, RESOURCES AND LIQUIDITY

As at March 31, 2007, our cash, cash equivalents and short-term investment position was \$23.1 million. During the year end March 31, 2007, we issued \$22.1 million in convertible notes, borrowed an additional \$7.3 million through a limited recourse facility established under our agreement with Matco, and sold 45% of WRI for \$4.2 million, raising over \$33.0 million. We used \$11.3 million in operations excluding working capital, \$0.9 million for loan repayments, and \$1.2 million for the purchase of equipment, furniture and leasehold improvements. Non-cash working capital requirements in the year totaled \$3.1 million with accounts receivable consuming \$4.7 million and inventory \$2.0 million offset by increases in accounts payable of \$2.4 million and warranty liability of \$1.2 million. The increase in accounts receivable relates to CWI's strong fourth quarter and TPC claims and accruals totaling \$2.2 million. The increase in accounts payable relates primarily to the increase in trade payables for

inventory and other materials and accruals for bonuses. Deferred revenue as at March 31, 2007 related primarily to amounts received from Cryostar that are being recognised over the term of the agreement. Deferred revenue at March 31, 2006 consisted primarily of amounts related to funds received by Cummins but where the engines had not yet been shipped to the end customer. As at March 31, 2007, we had recognised approximately \$0.9 million in net deferred transaction costs related to our transactions with Perseus and Matco and which are being expensed over the term of the Perseus convertible notes or in the periods we dispose of our shares in WRI, as applicable. At March 31, 2007, Cummins share of CWI was \$7.7 million, including its \$1.7 million share of CWI's future income tax recovery, a non-cash item.

In addition to our convertible note with Perseus and the limited recourse loan facilitated by Matco, we have a \$13 million credit facility with our bank, which has been drawn down by our demand instalment loan of \$1.6 million, capital leases of \$0.1 million, and a \$0.6 million letter of credit. Perseus also has a right of first refusal on an additional US\$10 million in financing. Historically, we have relied on public and private sources of equity financing to fund our operations and growth and bank financing to fund working capital and requirements and capital expenditures. Since our incorporation in 1995, we have raised over \$230 million in common share equity primarily from a number of private and public offerings.

As at March 31, 2007, our capital resources consisted primarily of cash, cash equivalents and short-term investments of \$23.1 million, a bank operating line of \$13 million as described above, and our investment in Clean Energy. On May 25, 2007, Clean Energy raised US\$120 million through an initial public offering (IPO) and its shares now freely trade on NASDAQ under the symbol CLNE. As of the date of the IPO, we held 2.1 million shares in Clean Energy with a market price of US\$12. We are restricted from trading our shares for a period of six months from the date of the public offering. We believe that at current valuation levels for Clean Energy and with commercial orders expected in the current fiscal year, we have sufficient capital to fund our existing business activities through the commercialization of LNG systems for heavy duty trucks.

However, Westport's capital requirements will vary depending on a number of factors, including the timing and volume of orders for our LNG systems, our ability to successfully launch product on time, our success in executing our business plan, relationships with current and potential strategic partners, commercial sales and margins, product reliability, progress on research and development activities, capital expenditures and working capital requirements.

We expect our working capital requirements to increase for inventory purposes as we commercialize our products and solutions. We also review investment and acquisition opportunities on a regular basis for technologies, businesses and markets that would complement our own products or assist us in our commercialization plans. Significant new or expanded engine programs, acquisitions or investments could require additional funding. If

such additional funding is not available to us, or if we have significant overspending in our programs, we may be required to delay, reduce or eliminate certain research and development activities and possibly forego new program, acquisition or investment opportunities. Any of those circumstances could potentially result in a delay of the commercialization of our products in development.

This "Capital Requirements, Resources and Liquidity" section contains certain forward looking statements. By their nature, forward-looking statements require us to make assumptions and are subject to inherent risks and uncertainties. Readers are encouraged to read the "Basis of Presentation" section of this MD&A which discusses forward-looking statements and the "Risks and Uncertainties" section of this MD&A for a discussion of the factors that could affect our future performance.

SHARES OUTSTANDING

For the years ended March 31, 2007 and 2006, the weighted average number of shares used in calculating the loss per share was 75,174,826 and 74,228,495, respectively. As of March 31, 2007, actual shares outstanding was 75,686,085 (2006 – 74,391,779). There were also 2,655,288 warrants with an exercise price of \$1.30 and 1,479,375 warrants with an exercise price of \$1.40 outstanding. Of the 5,228,993 share options outstanding, 1,479,465 were exercisable at a weighted average price of \$2.98 and of the 2,063,159 performance share units outstanding 1,763,162 were exercisable. The share options and performance share units are subject to various vesting conditions. We also had convertible notes of \$13.8 million outstanding with a conversion price of \$1.30 and \$8.3 million in convertible notes outstanding with a conversion price of \$1.40. As of May 31, 2007, there were 5,248,505 share options outstanding, 2,001,810 of which were exercisable at a weighted average price of \$2.59, and 2,063,159 performance share units outstanding, of which 1,863,161 were exercisable.

SUMMARY OF QUARTERLY RESULTS AND DISCUSSION OF FOURTH QUARTER 2007

The following table provides summary unaudited financial data for our last eight quarters:

Selected Quarterly Operations Data (Unaudited)

Three months ended	30-Jun-05	30-Sep-05	31-Dec-05	31-Mar-06	30-Jun-06	30-Sep-06	31-Dec-06	31-Mar-07
Units shipped	310	384	245	388	341	414	629	617
Average foreign exchange rate (C\$:US\$)	\$ 1.24	\$ 1.19	\$ 1.17	\$ 1.15	\$ 1.11	\$ 1.12	\$ 1.14	\$ 1.17
<i>(Expressed in thousands of Canadian dollars except per share)</i>								
Product revenue	\$ 7,006	\$ 9,095	\$ 5,147	\$ 8,684	\$ 7,644	\$ 10,327	\$ 13,568	\$ 15,656
Parts revenue	\$ 3,508	\$ 3,134	\$ 3,466	\$ 3,512	\$ 2,978	\$ 3,401	\$ 3,248	\$ 3,658
Total revenue	\$ 10,514	\$ 12,229	\$ 8,613	\$ 12,196	\$ 10,622	\$ 13,728	\$ 16,816	\$ 19,314
Gross margin	\$ 2,710	\$ 4,295	\$ 3,680	\$ 4,225	\$ 4,037	\$ 4,776	\$ 5,398	\$ 7,888
	26%	35%	43%	35%	38%	35%	32%	41%
Net income (loss) for the period	\$ (6,213)	\$ (3,329)	\$ (3,607)	\$ (3,711)	\$ (5,420)	\$ (1,840)	\$ (5,778)	\$ 1,731
Basic and diluted earnings (loss) per share ⁽¹⁾	\$ (0.08)	\$ (0.05)	\$ (0.05)	\$ (0.05)	\$ (0.07)	\$ (0.02)	\$ (0.08)	\$ 0.02
Cash from (used in) operations before change in non-cash operating working capital	\$ (3,019)	\$ (1,463)	\$ (2,225)	\$ (1,954)	\$ (3,685)	\$ (3,760)	\$ (4,448)	\$ 568
Company's 100% share of CWI net income	\$ 133	\$ 1,516	\$ 502	\$ 1,035	\$ 1,528	\$ 1,392	\$ 806	\$ 8,389
Joint Venture Partner's share of CWI net income	\$ 66	\$ 758	\$ 251	\$ 518	\$ 764	\$ 696	\$ 403	\$ 4,194

⁽¹⁾ Fully diluted loss per share is not materially different as the effect of stock options, warrants and performance share units would be anti-dilutive.

Our revenues and operating results can vary significantly from quarter to quarter depending on the timing of customer orders and deliveries, product mix in the quarter, new product launch dates, research and development project cycles, timing of related government funding and foreign exchange impacts. There has been an overall trend of increasing revenues in the last eight quarters with revenues per quarter on average 39% higher than in the prior fiscal year. We expect overall revenue growth to continue through fiscal year 2008 although on a quarterly basis, revenues will continue to fluctuate. Net loss has and can vary significantly from one quarter to another depending on operating results, gains and losses from investing activities, timing of stock-based compensation awards and other similar transactions.

Net loss for the three months ended June 30, 2005 included \$1.8 million in stock-based compensation reflecting a special grant of 1.7 million share options to all employees. Starting in the second quarter of fiscal 2007, we have also been recognizing approximately \$0.4 million per quarter in interest and amortization of discount related to the Perseus convertible notes. This amount increased to \$0.8 million per quarter in the fourth quarter of fiscal 2007 with the issuance of the second tranche of the convertible notes. As we are using the effective interest method to amortize the discount, we expect this expense to increase over time. In the three months ended September 30, 2006, we also recognised a net gain of \$3.9 million on the sale of 45% of WRI and a further gain of \$4.2 million on the partial sale and dilution of our interest in WRI from 55% to 16% was recognised in the three months ended March 31, 2007.

The initial work phase of our TPC agreement was scheduled to end March 31, 2006. Funding claims averaging approximately \$0.5 million per quarter were submitted to TPC but were not accrued in the first three quarters of

fiscal year 2007 pending confirmation that the work phase would be extended and royalty payments of \$0.3 million per quarter were accrued. In the fourth quarter of fiscal 2004, TPC substantially completed its review of our proposed amended statement of work and we have received confirmation of their approval for a two year extension of the work phase of our agreement, allowing us to claim eligible costs through fiscal years 2007 and 2008 and starting royalties two years later. Accordingly, in the fourth quarter, we accrued \$2.2 million in claims and reversed \$1.0 million in royalty accruals recognised in the first three quarters of fiscal 2007 for a total \$3.2 million reduction to research and development expenditures in the quarter.

In the fourth quarter of fiscal 2007, we also recognised \$0.8 million in stock-based compensation with certain vesting milestones relating to prior year performance share unit grants under our long-term incentive plan having been met in the quarter. We also accrued \$1.2 million in annual bonuses. In the three months ended March 31, 2007, revenues increased by 37% to \$19.3 million from \$12.2 million from the fourth quarter of the prior year as the result of higher CWI engine shipments and the first eight shipments of Westport's LNG systems for heavy-duty trucks which contributed approximately \$0.8 million in revenues. Gross margins improved to 41% in the fourth quarter of 2007 compared to 35% in the prior year primarily because of a \$0.8 million warranty adjustment taken by CWI in 2007. As a result of the items discussed above, Westport had its first profitable quarter with net income for the fourth quarter of 2007 of \$1.7 million compared to a net loss of \$3.7 million in the fourth quarter of 2006. Included in net income for the fourth quarter was the \$4.2 million gain described previously on the dilution of our interest in WRI and the recognition of \$3.5 million in future income tax recoveries recognised by CWI. Both of these items are non-cash items. Excluding these items, we would have had a net loss of \$4.3 million after taking into account Cummins' 50% share of the future income tax recovery.

CONTRACTUAL OBLIGATIONS AND COMMITMENTS

<i>Minimum Annual Payments due by Period</i>					
<i>(in thousands of dollars)</i>	Less than 1 year	1 to 3 years	4 to 5 years	After 5 years	Total
Capital lease obligations	75	59	4	-	138
Operating leases	1,078	1,080	199	219	2,576
Total contractual commitments	1,153	1,139	203	219	2,714

Contractual Commitments

Capital lease obligations related primarily to office equipment, have terms of two to five years and have interest rates ranging from 1% to 6.2%. Operating lease commitments represent our future minimum lease payments under leases related primarily to our operating premises and office equipment. We also have an outstanding letter of credit for \$0.6 million.

Demand Instalment Loan

As of March 31, 2007, we had \$1.6 million in a demand instalment loan outstanding, down \$0.9 million from \$2.5 million as at March 31, 2006. The loan is drawn against our line of credit of \$13 million and bears interest at prime. The loan is being repaid over five years.

BTIC

Under our signed joint venture agreement with BTIC, we are committed to contributing US\$0.4 million to the formation of the joint venture. Initiation of formal business operations is subject to customary government approvals which were received subsequent to March 31, 2007.

CONTINGENT OFF-BALANCE SHEET ARRANGEMENTS
Government Funding

We are continually exploring strategic opportunities to work with governments to provide them with alternative fuel solutions. As the result of our government partnerships, we recognised \$5.2 million in government funding in 2007 and \$8.7 million in funding in 2006. Under certain repayment terms, we are obligated to repay royalties as follows:

AGREEMENT	DESCRIPTION	ROYALTIES	TERM
INDUSTRIAL TECHNOLOGIES OFFICE (FORMERLY TECHNOLOGY PARTNERSHIPS CANADA)	Fund 30% of the eligible costs of, among other research projects, the adaptation of Westport's technology to diesel engines, up to \$18.9 million.	Annual royalties equal to the greater of \$1,350,000 or 0.33% of annual gross revenues from all sources, provided that gross revenues exceed \$13.5 million. Share purchase warrants valued at \$4 million under Black-Scholes.	Fiscal 2009 to fiscal 2015, inclusive; royalty period may be extended until the earlier of March 31, 2018 or until cumulative royalties total \$28,189,000. To be issued no earlier than September 30, 2008.

AGREEMENT	DESCRIPTION	ROYALTIES	TERM
DEPARTMENT OF NATURAL RESOURCES CANADA	Funded \$1 million for demonstration of a low emissions natural gas power generator in Grande Prairie, Alberta.	1% of revenues from future sales of natural gas engines for power generators.	Earlier of 10 years from project completion date (August 30, 2004), or when cumulative royalties total \$1 million.
GREEN ECONOMY DEVELOPMENT FUND (Province of British Columbia)	\$0.6 million for low-emission, natural gas power generation demonstration project.	0.75% from gross revenue received by Westport on certain natural gas fuel systems.	Earlier of the seventh anniversary of the funding contribution date (April 10, 2001) or when the cumulative royalties paid by Westport equal \$0.8 million.

As at March 31, 2007 and 2006, no royalties have been paid or were payable under these agreements.

BUSINESS RISKS AND UNCERTAINTIES

An investment in our business involves risk and readers should carefully consider the risks described below and in our Annual Information Form and other filings on www.sedar.com. Our ability to generate revenue and profit from our technologies is dependent on a number of factors, and the risks identified below, if they were to occur, could have a material impact on our business, financial condition, results of operation or prospects. While we have attempted to identify the primary known risks that are material to our business, the risks and uncertainties described below may not be the only ones we face. Additional risks and uncertainties, including those that we do not know about now or that we currently believe are immaterial may also adversely affect our business, financial condition, results of operation or prospects.

We have incurred and continue to incur losses

We have incurred substantial losses since our inception in 1996, and continue to incur losses. We cannot predict if and when we will operate profitably or if we will be able to implement our business strategy successfully. Pursuing our strategy requires us to incur significant expenditures for research and product development, marketing and general administrative activities. As a result, we need to continue to grow our revenues and gross margins to achieve and sustain profitability and positive operating cash flows.

Potential fluctuations in our financial results make financial forecasting difficult

We expect our revenues and results of operation to continue to vary significantly from quarter to quarter. Sales and margins may be lower than anticipated due to timing of customer orders and deliveries, unexpected delays in our supply chain, general economic and market-related factors, product quality, performance and safety issues and competitive factors. In addition, the continuance and timing of government funding of our R&D programs is difficult

to predict, and may cause quarter to quarter variations in financial results. In addition, due to our early stage of development, we cannot accurately predict our future revenues or results of operations. We are also subject to normal operating risks such as credit risks and foreign currency risks. As a result, quarter-to-quarter comparisons of our revenues and results of operation may not be meaningful. It is likely that in one or more future quarters our results of operation will fall below the expectations of securities analysts and investors. If this happens, the trading price of our shares might be materially and adversely affected.

We have foreign currency risk

While CWI's revenues, expenses and warranty balances are all denominated in US dollars, the majority of our revenue is in US dollars while many of our operating expenses, other than cost of sales, are in Canadian dollars. Foreign exchange gains and losses are included in results from operations. A large decline in the value of the US dollar relative to the Canadian dollar could impair revenues, margins and other financial results. We have not entered into foreign exchange contracts to hedge against gains and losses from foreign currency fluctuations.

We may be unable to raise additional capital

Execution of our business plan and our commercial viability could be jeopardised if we are unable to raise additional funds for our research and development projects, sales, marketing and product development activities and other business opportunities. We attempt to mitigate this risk by generating funds from a variety of sources including: through the sale of our commercial products, through the sale of non-core assets including long-term investments, through funding from government agencies, industry and business partners, and through the issuance of shares or debt in the public equity markets or through strategic investors. In addition, we try to maintain reserves of cash and short-term investments and seek to obtain funding commitments before we take on any significant incremental initiatives. There can, however, be no assurance that we will be able to secure additional funding, or funding on terms acceptable to us, to pursue our commercialization plans. In particular, there can be no assurance that we will continue to receive funding from government agencies at the same levels we have received in the past or at all. Funding agreements with government agencies are also subject to audit, which could result in certain funding being denied or monies received from such agencies having to be repaid.

A market for engines with our fuel systems may never develop or may take longer to develop than we anticipate

Engines with our fuel systems represent an emerging market, and we do not know whether end-users will ultimately want to use them or pay for their initial incremental cost. The development of a mass market for our fuel systems may be affected by many factors, some of which are beyond our control, including: the emergence of newer, more competitive technologies and products; the future cost of natural gas and other fuels used by our systems; regulatory requirements; customer perceptions of the safety of our products; and customer reluctance to

try a new product.

In addition, while some of our customers and potential customers have made successful applications for government funding to assist them in converting their vehicles to natural gas engines, there is no guarantee that such funds will continue to be available. If incentive programs are discontinued or are no longer available to our customers and potential customers, it may have a detrimental effect on our sales.

If a market fails to develop or develops more slowly than we anticipate, we may be unable to recover the losses we will have incurred in the development of our products and may never achieve profitability.

We are dependent on fuel price differentials that are hard to predict

The acceptance of natural gas-fuelled engines by customers depends in part on the price differential between natural gas and diesel fuel. Natural gas has generally been, and currently is, less expensive than diesel fuel in many jurisdictions. This price differential is affected by many factors, including changes in the resource base for natural gas compared with crude oil, pipeline transportation capacity for natural gas, refining capacity for crude oil and government excise and fuel tax policies. There can be no assurance that natural gas will remain less expensive than diesel fuel.

We are dependent on growth in natural gas refueling infrastructure that may not take place

For motor vehicles, natural gas must be carried on board in liquefied or compressed form and there are few public or private refuelling stations available in most jurisdictions. We are involved in developing such infrastructure through our minority ownership interest in Clean Energy, the largest natural gas refuelling company for vehicles in North America, and are seeking further involvement with other natural gas refuelling companies. However, there can be no assurance that Clean Energy will continue to be successful in expanding the availability of natural gas as a vehicle fuel, or that other companies will develop refuelling stations to meet projected demand. If customers are unable to obtain fuel conveniently and affordably, a mass market for vehicles powered by our technology is unlikely to develop.

Changes in environmental and regulatory policies could hurt the market for our products

We currently benefit from, and hope to continue to benefit from, certain government environmental policies, mandates and regulations around the world, most significantly in the automotive markets and in the United States. Examples of such regulations include those that provide economic incentives, subsidies, tax credits and other benefits to purchasers of low emission vehicles, restrict the sale of engines that don't meet emission standards, fine the sellers of non-compliant engines, tax the operators of diesel engines and require the use of more expensive ultra-low sulphur diesel fuel. There can be no assurance that these policies, mandates and regulations will be continued. If they are discontinued or if current requirements are relaxed, this may have a material impact on our competitive position.

We currently face and will continue to face significant competition

Our products face and will continue to face significant competition. New developments in technology may negatively affect the development or sale of some or all of our products or make our products uncompetitive or obsolete. Other companies, many of which have substantially greater customer bases, businesses and other resources than us, are currently engaged in the development of products and technologies that are similar to, or may be competitive with, certain of our products and technologies.

Competition for our products may come from current power technologies, from improvements to current power technologies and from new alternative power technologies, including other fuel systems. Each of our target markets is currently serviced by existing manufacturers with existing customers and suppliers using proven and widely accepted technologies. Additionally, there are competitors working on developing technologies such as fuel cells, advanced batteries and hybrid battery/internal combustion engines in each of our targeted markets. Each of these competitors has the potential to capture market share in various markets, which could have a material adverse effect on our position in the industry and our financial results. For our products to be successful against competing technologies, especially diesel engines, they must offer advantages in one or more of these areas: emissions performance, fuel economy, engine performance, power density, engine and fuel system weight, and engine and fuel system price. There can be no assurance that our products will be able to offer advantages in all or any of these areas.

Our products may not be commercially viable

Our direct injection technology has been demonstrated in heavy duty trucks light duty vehicles and high horsepower applications. However, we do not know when or whether we will successfully complete development of commercially viable fuel systems for any of our target markets. There can be no assurance that engines using our fuel systems will perform as well as we expect, or that prototypes and commercial systems will be developed and sold in commercially viable numbers.

Our HPDI fuel systems presently have higher initial capital costs than many established competing technologies, and manufacturing costs of some of our products at a commercial level have not yet been confirmed. If we are unable to produce fuel systems that are economically competitive, on a life cycle costs basis, in terms of price, reliability and longevity, operators of commercial vehicle fleets and power generators will be unlikely to buy products containing our fuel systems.

We are dependent on relationships with strategic partners

Execution of our current strategy is dependent on cooperation with strategic partners for technology development, component supplies, manufacturing and distribution. To be commercially viable, our fuel systems must be integrated into engines and our engines must be integrated into chassis manufactured by OEMs. We can offer no

guarantee that existing technology agreements will be renewed or advanced into commercialization agreements, or that OEMs will manufacture engines with our fuel systems or chassis for our engines, or, if they do manufacture such products, that customers will choose to purchase them. Any integration, design, manufacturing or marketing problems encountered by OEMs could adversely affect the market for our products and our financial results. In addition, there can be no assurance of the commercial success of any joint ventures in which we are, or will become, involved.

While we have negotiated supply agreements with various manufacturers, certain manufacturers may be the sole supplier of certain key components for our products. An inability to obtain adequate supplies of certain components could harm our ability to manufacture certain products or subject us to cancellation of orders or penalties for failed or late deliveries, which could have a material adverse on our business and financial results. The prices at which those supplies are available fluctuate and may increase significantly. Competitive pressure, however, may not allow us to increase the sales price of our products. Any such increases may therefore negatively affect our margins and financial condition.

Any change in our relationships with our strategic partners, whether as a result of economic or competitive pressures or otherwise, including any decision by our strategic partners to reduce their commitment to our products and technology in favour of competing products or technologies, or to bring to an end our various alliances, could have a material adverse effect on our business and financial results.

We are dependent on our relationship with Cummins for CWI revenues and profits

The majority of our revenues are currently derived from the operations of CWI, which, in turn, purchases all of its current and foreseeable engine products from Cummins-affiliated plants and distributors. Although the factories operate with modern technology and experienced management, there can be no assurance that the factory and distribution systems will always be able to perform on a timely and cost-effective basis. Any reduction in the manufacturing and distribution capabilities of Cummins-affiliated plants and distributors could have a material adverse effect on our business and financial results.

Our limited production trials and field tests could encounter problems

We are currently conducting, and plan to continue to conduct, limited production trials and field tests on a number of our products as part of our product development cycle. These trials and field tests may encounter problems and delays for a number of reasons, including the failure of our technology, the failure of the technology of others, the failure to combine these technologies properly and the failure to maintain and service the test prototypes properly. Some of these potential problems and delays are beyond our control. Any problem or perceived problem with our limited production trials and field tests could hurt our reputation and the reputation of our products and delay their commercial launch.

Warranty claims could diminish our margins

There is a risk that the warranty accrual included in our cost of product revenue is not sufficient and that we may recognise additional expenses as a result of warranty claims in excess of our current expectations. Such warranty claims may necessitate a redesign, re-specification or recall of our products, which, in turn, may have an adverse impact on our finances and on existing or future sales. Although we attempt to mitigate against these risks through our sales and marketing initiatives and our product development, quality assurance, support and service programs, there can be no assurance that such initiatives and programs are adequate or that sales of our commercial products will continue to grow and contribute financially.

We may have difficulty managing the expansion of our operations

To support the launch, and increase sales and service, of our fuel system products, we may be required to expand the scope of our operations rapidly. This may include a need for a significant increase in employees and an increase in the size, or relocation, of our premises. Such rapid expansion may place a significant strain on our senior management team and other resources. In addition, we may be required to place more reliance on our strategic partners and suppliers, some of whom may not be capable of meeting our production demands in terms of quantity, quality or cost. Difficulties in effectively managing the budgeting, forecasting and other process control issues presented by such a rapid expansion could harm our business, prospects, results of operations or financial condition.

We could lose or fail to attract the personnel necessary to run our business

Our success depends in large part on our ability, and that of our affiliates, to attract and retain key management, engineering, scientific, manufacturing and operating personnel. As we develop additional capabilities we may require more skilled personnel. Recruiting personnel for the alternative fuel industry is highly competitive. Although to date we have been successful in recruiting and retaining qualified personnel, there can be no assurance that we will continue to attract and retain the personnel needed for our business. The failure to attract or retain qualified personnel could have a material adverse effect on our business.

If we do not properly manage foreign sales and operations, our business could suffer

We expect that a substantial portion of our future revenues will be derived from sales outside of Canada, and we operate in jurisdictions where we may lack sufficient expertise, local knowledge or contacts. Establishment of an international market for our products may take longer and cost more to develop than we anticipate, and is subject to inherent risks, including unexpected changes in government policies, trade barriers, difficulty in staffing and managing foreign operations, longer payment cycles, and foreign exchange controls that restrict or prohibit repatriation of funds. As a result, if we do not properly manage foreign sales and operations, our business could suffer.

We may not realise the anticipated benefits from joint ventures, investments or acquisitions

Our joint ventures, and any future joint venture, investment or acquisition could expose us to certain liabilities, including those that we fail or are unable to identify during the acquisition process. In addition, joint ventures and acquisitions often result in difficulties in integration, and, if such difficulties were to occur, they could adversely affect our results. The integration process may also divert the attention of, and place significant demands on, our managerial resources, which may disrupt our current business operations. As a result, we may fail to meet our current product development and commercialization schedules.

We depend on our intellectual property and our failure to protect that intellectual property could adversely affect our future growth and success

Failure to protect our existing and future intellectual property rights could seriously harm our business and prospects, and may result in the loss of our ability to exclude others from practicing our technology or our own right to practice our technologies. If we do not adequately ensure our freedom to use certain technology, we may have to pay others for rights to use their intellectual property, pay damages for infringement or misappropriation and/or be enjoined from using such intellectual property. Our patents do not guarantee us the right to practice our technologies if other parties own intellectual property rights that we need in order to practice such technologies. Our patent position is subject to complex factual and legal issues that may give rise to uncertainty as to the validity, scope and enforceability of a particular patent. There can be no assurance that:

- any of the rights we have under U.S. or foreign patents owned by us or other patents that third parties license to us will not be curtailed, for example through invalidation, circumvention, challenge, being rendered unenforceable or by license to others;
- we were the first inventors of inventions covered by our issued patents or pending applications or that we were the first to file patent applications for such inventions;
- any of our pending or future patent applications will be issued with the breadth of claim coverage sought by us, or be issued at all;
- our competitors will not independently develop or patent technologies that are substantially equivalent or superior to our technologies; or
- any of our trade secrets will not be learned independently by our competitors; or
- the steps we take to protect our intellectual property will be adequate.

In addition, effective patent, trademark, copyright and trade secret protection may be unavailable, limited or not applied for in certain foreign countries.

We also seek to protect our proprietary intellectual property, including intellectual property that may not be patented

or patentable, in part by confidentiality agreements and, if applicable, inventors' rights agreements with our strategic partners and employees. There can be no assurance that these agreements will not be breached, that we will have adequate remedies for any breach or that such persons or institutions will not assert rights to intellectual property arising out of these relationships.

Certain intellectual property has been licensed to us on a non-exclusive basis from third parties who may also license such intellectual property to others, including our competitors. If necessary or desirable, we may seek further licenses under the patents or other intellectual property rights of others. However, we can give no assurances that we will obtain such licenses or that the terms of any offered licenses will be acceptable to us. The failure to obtain or renew a license from a third party for intellectual property we use at present could cause us to incur substantial liabilities and to suspend the manufacture, shipment of products or our use of processes requiring such intellectual property.

We could become engaged in intellectual property litigation that may negatively affect our business

While we are not currently engaged in any intellectual property litigation, we could become subject to lawsuits in which it is alleged that we have infringed the intellectual property rights of others or in which the scope, validity and enforceability of our intellectual property rights is challenged. In addition, we may commence lawsuits against others who we believe are infringing upon our rights. Our involvement in intellectual property litigation could be time consuming and result in significant expense to us, diversion of resources, and delays or stoppages in the development, production and sales of products or intellectual property, whether or not any claims have merit or such litigation is resolved in our favour. In the event of an adverse outcome as a defendant in any such litigation, we may, among other things, be required to:

- pay substantial damages;
- cease the development, manufacture, use, sale or importation of products that infringe upon other patented intellectual property;
- expend significant resources to develop or acquire non-infringing intellectual property;
- discontinue processes incorporating infringing technology; or
- obtain licenses to the infringing intellectual property.

Any such result could require the expenditure of substantial time and other resources and could have a material adverse effect on our business and financial results.

We could become liable for environmental damages resulting from our research, development or manufacturing activities

The nature of our business and products exposes us to potential claims and liability for environmental damage,

personal injury, loss of life, and damage to or destruction of property. Our business is subject to numerous laws and regulations that govern environmental protection and human health and safety. These laws and regulations have changed frequently in the past and it is reasonable to expect additional and more stringent changes in the future. Our operations may not comply with future laws and regulations, and we may be required to make significant unanticipated capital and operating expenditures. If we fail to comply with applicable environmental laws and regulations, governmental authorities may seek to impose fines and penalties on us or to revoke or deny the issuance or renewal of operating permits, and private parties may seek damages from us. Under those circumstances, we might be required to curtail or cease operations, conduct site remediation or other corrective action, or pay substantial damage claims. In addition, depending on the nature of the claim, our current insurance policies may not provide sufficient or any coverage for such claims.

We could become subject to product liability claims

Our business exposes us to potential product liability claims that are inherent in natural gas, propane, and hydrogen and products that use these gases. Natural gas, propane, and hydrogen are flammable gases and therefore potentially dangerous products. We also produce fuel processors that generate hydrogen from certain raw fuels, which are also flammable. Any accidents involving our products or other natural gas, propane, or hydrogen-based products could materially impede widespread market acceptance and demand for our engines and fuel systems. In addition, we may be subject to a claim by end-users or others alleging that they have suffered property damage, personal injury or death because our products did not perform adequately. Such a claim could be made whether or not our products perform adequately under the circumstances. From time to time, we may be subject to product liability claims in the ordinary course of business and we carry a limited amount of product liability insurance for this purpose. However, our current insurance policies may not provide sufficient or any coverage for such claims, and we cannot predict whether we will be able to maintain our insurance coverage on commercially acceptable terms.

Our share price may fluctuate

The stock market in general, and the market prices of securities of technology companies in particular, can be extremely volatile, and fluctuations in our share price may be unrelated to our operating performance. Our share price could be subject to significant fluctuations in response to many factors, including: actual or anticipated variations in our results of operations; the addition or loss of customers; announcements of technological innovations, new products or services by us or our competitors; changes in financial estimates or recommendations by securities analysts; conditions or trends in our industry; our announcements of significant acquisitions, strategic relationships, joint ventures or capital commitments; additions or departures of key personnel; general market conditions; and other events or factors, many of which may be beyond our control.