PARTICIPANTS

Corporate Participants

Kristi Cushing – Manager-Investor Relations, Clean Diesel Technologies, Inc.
Robert Craig Breese – President, Chief Executive Officer & Director, Clean Diesel Technologies, Inc.
Nikhil Atul Mehta – Chief Financial Officer & Treasurer, Clean Diesel Technologies, Inc.
Stephen John Golden – Chief Technology Officer & VP-Strategic Growth, Clean Diesel Technologies, Inc.

Other Participants

Philip L. Shen – Analyst, ROTH Capital Partners LLC
Ian T. Gilson – Analyst, Zacks Investment Research, Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Good day, ladies and gentlemen, and welcome to the Clean Diesel Technologies, Incorporated Fourth Quarter and Fiscal Year 2012 Financial Results Conference Call.

At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session and instructions will follow at that time. [Operator Instructions] As a reminder, this conference call is being recorded.

I would now like to introduce your host for today's conference, Ms. Kristi Cushing, Investor Relations Manager. Ma'am, you may begin.

Kristi Cushing, Manager-Investor Relations

Thank you, Kate, and good morning, everyone. Thank you for joining the Clean Diesel Technologies, or CDTi, Conference Call and Webcast to discuss the company's financial results for the fourth quarter and year-ended 2012, which ended on December 31, 2012.

By now, you should have a copy of our results press release, which crossed the wire this morning prior to market open. A copy of the press release, along with other company information, may be found on the Investor Relations page of the company's website at www.cdti.com.

Before I turn the call over to Craig Breese, President and Chief Executive Officer of CDTi, I want to emphasize that some of the information discussed in this call are forward-looking statements, particularly statements about improved demand for and regulatory enforcement of retrofit mandates, changes to customer reimbursement rates for raw materials and any impacts such rates may have on future growth and margins, as well as overall business growth, momentum and margin improvement.

These forward-looking statements speak only as of today and involve risks and uncertainties that are outside of CDTi's control. Accordingly, undue reliance should not be placed on such forward-looking statements as actual results may materially differ.

Risks and uncertainties that may affect such forward-looking statements include, among others, the risk of decreased government spending on emission control projects or decreased regulation of emissions and the risks associated with the receipt of regulatory approvals and continued customer acceptance of our products, as well as the other risk factors previously detailed in our filings with the SEC.

For a complete discussion and understanding of the risks our company faces, you should review the Risk Factors in the Annual Report on Form 10-K, which was filed with the SEC on March 29, 2012.

Call participants are advised that the audio of this conference call is being broadcast live over the Internet and will be available as an archived replay on our website. The archive may not be re-recorded or otherwise reproduced or distributed without prior written permission from CDTi.

I will now turn the call over to Craig Breese, President and Chief Executive Officer of CDTi.

Robert Craig Breese, President, Chief Executive Officer & Director

Thank you, Kristi, and good morning, everyone. Today, it's my pleasure to share with you the CDTi fourth quarter and full year 2012 financial performance, including highlights on our restructuring, program and business repositioning, and to provide a technology update of some of the most exciting new technology in the catalyst field that we are pioneering, and finally to touch on how see 2013 shaping up to-date.

Joining me for this call are Nikhil Mehta, CDTi's Chief Financial Officer; and Dr. Steve Golden, the Head of Business Development for the company as well as our CTO.

So let me begin with the company's total financial results, and then move on to a review of the results for each for our divisions.

The sales performance for the fourth quarter and the full year of 2012 were clearly disappointing, but particularly so on our Heavy Duty Diesel retrofit sales. The pick-up in sales activity related to the California truck and bus mandate, which we had expected in the second half of the year, did not occur. We believe the primary reasons for the lower-than-expected sales results were related to the late and weak enforcement actions by the state regulators, also known as CARB, and the delay in receiving regulatory approval on one of our emission solutions, which we only received in January of this year.

We also faced a difficult comparison in the fourth quarter. As you may recall, our prior-year results included over $6 million in sales into the London Low Emission Zone area, which were not repeated in 2012.

In reviewing the 2012 Manufacturers of Emission Controls Association, known as MECA, the report regarding industry sales of diesel particulate filters, we actually don't believe that our major competitors had a vastly different experience under the mandatory California Truck and Bus Regulation. Because as we look at our performance in the California market, we actually see and we're encouraged to note that our overall market share remain in the range of 17% of the number of units sold. In the remaining 49 states, our share was a healthy 34%, nearly a total third of the market.

With our EGR product now fully CARB-approved, coupled with a more aggressive enforcement plan by CARB and the exit from the retrofit sector of a key competitor, a company known as Cleaire, we are guardedly optimistic that we'll see an improvement in demand in this retrofit sector.

And in fact, early signs of a pick-up in data logging by customers and quotations by our distributors year-to-date are positive signs.

We're also continuing to focus our efforts on expanding our Heavy Duty Diesel sales from non-retrofit sources to represent a more sustainable original equipment manufacturing and aftermarket business for the reduction of exhaust emissions. Given our London and our 2012 California retrofit experience, we believe it is both prudent and necessary to continue diversifying our sales mix, tilting our efforts wherever possible towards these segments.

For the full year, non-retrofit sales, which include off-road and stationary diesel, gasoline and alternative fuel engines, were 37% of our Heavy Duty Diesel sales, compared to 33% in the year 2011. In order to grow the non-retrofit segment faster, we're pursuing relationships with other companies that have well-established global platforms serving the OE customer base.

We've recently hired a key sales executive from Cummins Engine to help us to drive in this direction. Our recently-formed joint venture with a subsidiary of the Pirelli Group to market and sell emission control products for both gasoline and diesel applications in Europe and the CIS countries is also an example of how we plan to grow this segment even further.

The lower Heavy Duty Diesel retrofit sales offset what was a very good performance by our Catalyst division, where sales increased more than 40% year-over-year. The highlight in this division, in addition to the stronger automotive market in North America, was our success as a supplier of catalyst to Honda for the new 2013 model year of its Accord in both the four- and six-cylinder models.

Looking at our Q4 Catalyst sales, we were negatively impacted by a lower gross margin due to an unsatisfactory rate for rare earth metal reimbursement from Honda. We recently finalized a reimbursement agreement though, which is expected to alleviate this issue as we now move forward and go into 2013.

So overall, we're pleased with the improved performance of our Catalyst division and we believe that we do have positive momentum in this business going forward, as evidenced by the Honda press release which was issued back in September 2012 which indicated their intent to use our technology in additional vehicle models beyond the Accord.

I'd now like to turn to our execution strategy, which is a key area. First, we continue to make progress with our restructuring activities that we began last year in order to streamline our operations and take cost out of our business. As we discussed in previous calls, throughout 2012, we implemented numerous cost reduction activities and actions. Total operating expenses including severance and restructuring costs were down by $1.6 million compared to last year. We remain on-track in terms of these costs related to our restructuring programs and the financial benefits as well.

To help us manage costs and drive growth, we've recently added new members to our management team. As mentioned, we hired a new Head of Sales for North America in our Heavy Duty Diesel division, and we've also brought in a new Global Head of R&D as well as a new Manager of our manufacturing facility in Markham, Canada. We're very fortunate to have these high-caliber professionals on our team to help us drive improved performance and execution.

Given some of the challenges we have experienced related to the delays in large government regulated retrofit programs like California and the complexities of working with global OE customers in our Catalysts business, we've also intensified our efforts to strategically reposition the company.

The goal of this repositioning is to better leverage CDTi's unique, core material science technology and unlock greater value for our customers and shareholders. We're focusing our efforts in a number of areas to achieve this goal.

First, we are substantially ramping up our pursuit of intellectual property development and protection, and we will be very active in 2013 with new patent filings. Second, we've demonstrated our technology leadership position by establishing a zero-platinum group metal, or PGM initiative, that will, to the best of our knowledge, be unsurpassed in this industry.

We will continue to aggressively innovate in this area and leverage our leadership position to pursue new activities. And more specifically, we've began to implement processes designed to better manage our technology portfolio and identify ways to both expand the addressable markets and monetarize our materials platform through a variety of approaches, which would include licensing, joint development agreements and joint ventures such as the one that we've recently announced in formation with Pirelli.

We have identified a number of new large vertical markets in addition to our emission control catalyst market that we believe represent opportunity for CDTi. Steve will provide greater detail on these markets during his discussion.

So now, I'll turn over the call to Nikhil for his comments on our financial results and operations. And then, Steve will walk you through our technology portfolio strategy. Over to you, Nikhil.

Nikhil Atul Mehta, Chief Financial Officer & Treasurer

Thanks, Craig, and good morning, everyone. I'm pleased to report our fourth quarter and full year 2012 results.

First, the fourth quarter results. Revenue of $12.4 million was down 41.8% compared to last year. Prior results included over $6 million in sales in the London Low Emission Zone which are not repeated this year. Additionally, the sales – the growth in sales in California in the second half of 2012 did not meet our expectation.

Gross margin was 22%, compared to 27.6% in the prior-year period. Gross margin was negatively impacted primarily by increases in cost of rare earth metals in our Catalyst division which were not fully reimbursed by our customer, Honda.

Through the first half of 2012, Honda was reimbursing substantially all our actual price increases. In the second half of 2012, on the launch of the new 2013 Accord platform, Honda decided to switch the reimbursement mechanism to a formula-driven process. We now have an agreement with Honda under which the cost increases will be reimbursed from January 2013 onwards based on a specific market index-driven formula. The base price for these cost increases is the price as of March 2009.

The revenue mix of our Heavy Duty Diesel business and the Catalyst business is approximately two-thirds Heavy Duty Diesel and one-third Catalyst in the fourth quarter of this year versus approximately 80/20 last year. This mix change also had a negative impact on our margins in the current period when compared to last year.

Loss from operations is $2.4 million compared to a profit of $200,000 last year. Loss per diluted share was $0.39 versus a gain of $0.06 per share in the fourth quarter of 2011.

Business segment highlights for the quarter include the following. Our Heavy Duty Diesel Systems sales of $8.4 million were down over 50% from $17.3 million last year, primarily due to the reduction in retrofit sales in London.

However, gross margins for this business have improved from 26% in the fourth quarter of 2011 to nearly 31% in the fourth quarter of 2012, resulting from a richer product mix sold in California and North America compared to the mix achieved in London last year, as well as due to higher content of Clean Diesel-manufactured low-PGM catalyst content in our Heavy Duty Diesel products. We recorded approximately $3.5 million of sales in California.

Our Catalyst OEM sales were flat compared to last year despite increased volumes from Honda as the rare earth prices and reimbursements were considerably lower than 2011. We continue to implement cost reductions throughout the organization while investing in critical sales and research and engineering resources.

During the quarter, we booked severance and other charges of approximately $0.5 million. Excluding these charges, our operating expenses in the fourth quarter were down – were $4.6 million compared to $5.7 million a year ago. We continue to aggressively look for opportunities to increase efficiency and reduce cost.

Let me now summarize the full year results. For the full year 2012, revenue were $60.5 million, down 1.7% from $61.6 million last year. External sales of Catalyst were up over 40%, from $14.2 million to $19.8 million, as Honda sales continued to perform well. Heavy Duty sales were down 14.3%, from $47.4 million last year to $40.7 million in 2012, with substantially all the reduction attributable to retrofit sales.

Gross margin was 24.3% in 2012 versus 28.5% in 2011, due to the shift in revenue mix on Heavy Duty Diesel to Catalyst, the lower rare earth reimbursement in the Catalyst business, and inventory write-offs relating to the London Low Emission Zone inventory.

Operating expenses were down from $24.1 million in 2011 to $22.5 million in 2012. Excluding severance and other charges of approximately $900,000, operating expenses were down 10% year-over-year.

Looking to the future, we anticipate that Catalyst gross margins will gradually improve during 2013 as our sales volumes increase and as rare earth reimbursement begin reflecting actual cost increases. We also expect Heavy Duty Diesel margins to improve as we incorporate more of our in-house Catalyst technologies and as the California market picks up in 2013.

Lastly, we expect savings of over $2 million in operating expenses per year as a result of restructuring actions taken in 2012. While we will prudently reinvest in strengthening our sales and marketing and other operational resources, we expect to continue to manage operating expenses tightly going forward.

Loss per diluted share was $1.34 for fiscal 2012 versus $1.31 per share for fiscal 2011.

Now, for the balance sheet and cash flow. Net working capital was $7.1 million as of December 31, 2012, versus $11.3 million a year ago. Cash and cash equivalents were $6.9 million as of December 31, 2012, compared to $3.5 million last year.

Cash used in operations was approximately $160,000 in 2012 versus over $14.6 million of cash usage in 2011. This positive swing of nearly $14.5 million was the result of reductions in inventory, as well as strong receivables collection. This will continue to be a critical focus in 2013.

In addition, we are renegotiating key supplier terms to further improve our cash flow.

During 2012, we secured a long-term loan of $3 million from a shareholder. In addition, we recently announced that we have renegotiated the terms of a $1.5 million loan from the same shareholder, whereby the lender has agreed to extend the maturity of the loan by approximately two years.

That concludes my comments on our financial results and operations. I would now like to turn the call over to Steve Golden to walk you through our technology portfolio strategy. Steve?

Stephen John Golden, Chief Technology Officer & VP-Strategic Growth

Thanks, Nikhil. Good morning, everyone. I'm going to talk about our core materials platform and how it has enabled our leadership in low- and zero-PGM high-performance catalyst products and how it drives our opportunity to innovate for new markets, bringing added value to customers and shareholders.

Our focus is on the key steps to establishing a technology leadership and how important it is to underpin this by brand protection. And I'll give you examples of the different markets for our technology and discuss a dominant IP portfolio, how that allows us to develop alternative monetization paths.

So our strategy involves some in-depth analysis of the competitive landscape, coupled with a much stronger investment in IP. We are investing where our Mixed Phase Catalyst or MPC platform can make a difference, where the competitors' position is not so strong.

I'll go into a bit more detail on the emission control space first and how our strengths and technology leadership approach is being applied to three main areas. They all have significant impact on the OEM customer base.

But first is our position in leading low-PGM emission control catalyst, like three-way catalyst, to the gasoline market. The catalysts we launched into mass production for Honda's 2013 Accord are good examples of this, where we still use PGM with much lower amounts.

The other two areas are zero-PGM for diesel applications globally and in gasoline-powered cars and light trucks. The catalyzed filter in our EGR system offering now launched in California is a patented zero-PGM coating that rapidly removes the diesel soots at low temperature.

We also see strong potential to develop a PGM-free three-way catalyst for gasoline vehicles with the same high performance as PGM products in the OEM market that currently spend several billion dollars per year on PGM purchases.

While we are experts in the emissions control industry and in minimizing and removing PGM use, we have identified markets outside of the emission control space that could benefit from our unique materials technology.

Let's talk for a few moments about our materials technology, the MPC platform, and how we can add value to other markets. At its heart, the MPC platform is consists of oxides of base metals and sometimes precious metals that are stabilized in nanostructures with superior stability under prolonged exposure to high temperatures.

This technology enables the oxide catalyst to resist sintering or fusing, thereby maintaining a high catalytic surface area. And as a result, the formulation maintains high levels of performance over time using substantially lower PGM and other technologies which results in cost benefits to the end user. We're also developing a zero-PGM catalyst that allows stabilized nanostructures of base metals, with high activity and surface area.

Catalysts in the petrochemical and refining industry use precious metals or base metals in many different industrial processes. The catalyst reactions involve a high temperature step which can cause a loss of activity in the catalyst and loss of yield of the product. Our unique MPC platform is designed to enhance the stability and the productivity of these types of reactions.

Catalysts in several types of fuel cells that use hydrogen or hydrocarbon feeds to efficiently make electricity are currently dominated by platinum and other precious metals. [ph] You can see the (21:47) amount of these metals commonly used as a major roadblock to fuel cell commercialization in [ph] device power (21:53) distributed electricity generation and automotive fuel cells. The assessment we have made is that our platform materials technology has a great potential to enable to stabilize low-PGM and zero-PGM catalysts in fuel cell applications.

Finally, we see a longer-term opportunity for new families of materials based on mixed metal oxide, materials we currently make for catalyst applications for the emerging thermoelectric market. We believe that we can effectively address these new market opportunities by using our strategy as outlined above, to protect and build our IP portfolio to demonstrate our capability and our leadership and pursue monetization through licensing arrangements, joint development agreements and partnerships.

Back to you, Craig.

Robert Craig Breese, President, Chief Executive Officer & Director

Thanks, Steve. What Steve has just shared with you remains one of the major reasons why I joined CDTi a year ago. I continue to believe in the company's future. Our technology platform is simply unparalleled. Our access to existing markets and, now, new markets are exciting opportunities that we will continue to focus on and drive on forward hard. We're committed to operational excellence and we intend to capture full technology value as we continue to reposition CDTi for success.

So that really concludes our future – excuse me, our formal remarks and comments today. So operator, I'd now like to turn it over to questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Our first question comes from the line of Philip Shen with ROTH Capital. Your line is open.

<Q – Philip Shen – ROTH Capital Partners LLC>: Craig, Nikhil, Steve, good morning.

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Good morning.

<Q – Philip Shen – ROTH Capital Partners LLC>: So my first question is about California. Our channel checks indicate that 2013 retrofit demand may follow a similar seasonal pattern to 2012. Additionally, we're hearing that overall volumes could be down in 2013 versus 2012. Can you give us a sense for what you're seeing in terms of demand and in terms of seasonality and volumes? That would be helpful.

<A – Craig Breese – Clean Diesel Technologies, Inc.>: So, let me start with a little historical perspective. Our data, which is driven right off the MECA numbers, suggest that the California market was stagnant between 2011 and 2012 with respect to the actual number of filters sold in the state, residing at roughly 6,000 each year. With that as a background, the question relative to cyclicality or seasonality in this business, to me, what's different in 2013 from the previous two years is that now most of the fleets are well into the middle of their compliance commitments.

So 2013, in most of the big fleets, they were really segmenting it into three years, 2012, 2013 and 2014. 2013 should be according to the compliance schedules that the fleets have signed up for, the largest of those three years in terms of the actual retrofits installed on the trucks. That's basically coming straight from the CARB organization, that information.

Now, the second aspect to this that I'd mentioned to you is, as you know, there is a segment of the market which is not in the large fleet area but more in the owner-operator independent segment. That segment was very slow to convert and, in fact, our information suggested it really didn't convert hardly at all in the last two years.

And as such, with compliance now kicking in – and if you look on the CARB website, you will see a dramatic spike in citations issued in Q4 of 2012, and that in turn is driving owner-operators and independents into their truck distributors asking, what do I do to get compliant, how do I go above that, what options do I have? And as a result, frankly, through February, as I said in my remarks earlier, we're seeing a dramatic spike, I'm talking about us, in terms of both data logging requests as well as quotations out to these various customers or segments of the customer base.

I would also draw your attention, Philip, to one other thing. We're comparing against a market where Cleaire was clearly a major factor in the California retrofit business a year ago. With the vacancy of that space now, with Cleaire being foreclosed upon by the bank and no longer present in the market, that clearly opens up a wide space which we and, obviously, our competitors are trying to fill as fast as we can.

So, I believe in two things. I believe that 2013 should actually see a larger volume in total aggregate demand in retrofit in California than 2012, and in talking to the CARB people, that certainly is their view. Secondly, I believe that the vacancy of the Cleaire situation bodes well for us as well as the rest of the competitors remaining in the space. And third of all, I believe we've enhanced and upgraded our sales team in California, and we're focusing and driving much harder than we were even in parts of 2012 to secure specific opportunities in the marketplace.

So at an aggregate level, again, I think that demand is probably going to be up year-over-year. And in a more specific vein, I think our performance, with now our EGR approved, product that we did not have in the portfolio a year ago, and Cleaire vacancy in the market, gives us additional opportunities to get a bit more jet-propelled here in the California market.

<Q – Philip Shen – ROTH Capital Partners LLC>: Great. Thanks, Craig. That's definitely helpful. I think it sounds like there's pent-up demand in the past couple of years there. You commented on CARB there, so I have a couple of follow-ups. So, you're definitely starting to see a step-up in enforcements. Do you expect that to continue and perhaps even get stronger? And then, another question I had was, just remind us again what the market share was that Cleaire had in – I think it was pretty large, but just remind us what it was in 2012.

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Okay, Philip. Good questions, both of them. So, actually, I was up in Sacramento with some top CARB officials just two weeks ago. And again, I beat the drum all the time with them relative to the slowness of compliance and enforcement, and they direct me to the CARB website where you can actually go in and look at the specific citations that are being issued, all right. And I think, when you do that, you'll go in and you'll see that continuing swell of citations and what that's a reflection of is that the California Highway Patrol and the enforcement officers that accompany them from CARB are actually out on the highways now, stopping trucks, checking for their paperwork. And if it's in order, they're being given citations on the spot. And as a result, this is clearly driving a lot of concern in the industry to go ahead and get compliant if they're not already.

So, I believe – I think, both CARB's focus and even paranoia about not having done enough early enough last year, I think they're – they can't over-correct in my view, but they're certainly compensating now for a very slow start. I believe that is the case and I think the numbers bear that out.

And I think on the second question with respect to Cleaire, our numbers suggest, and this comes from MECA data in the past, that their market share in California was as high as 40%. So – and that may vary by segment. To some degree, it will. And remember, they were very strong in the school bus retrofit programs in the last decade and the early part of this decade, and they were transitioning that strength into the truck initiative as well.

But with their departure, there are literally thousands of unfulfilled units now that have a temporary fix to them that will have to be pulled back out of the market and retrofit at some point with a new system which wouldn't be a Cleaire system, and I think it creates a lot of potential opportunities certainly for, like I say, all of those that remain in this segment going forward.

<Q – Philip Shen – ROTH Capital Partners LLC>: Yes. So I think you talked about in your prepared remarks of having 17% of the California market share. What – obviously, you would like to get more than 17% of Cleaire's 40%. What degree of confidence do you have in your ability to do that and what gives you that confidence?

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Well, I'd like to have it all, right. Let's be clear. And so, I think what gives me confidence is our EGR product, which was verified and approved in January, fills a critical gap in our product line that we didn't have to fight with last year, which was a sweet spot, frankly, for the CARB – or, excuse me, for the Cleaire product line up, which we just simply didn't have anything to compete with.

Secondly, let's talk about their distributor network for just a minute. They went through, primarily, the Cummins West and the Cal Cummins (sic) [Cummins Cal Pacific] (32:08) distributors in California. Those were their two largest sales outlets. Another one is a company called Iron Man.

So in the case of Cummins, we've now been contacted by the Cummins dealers about potentially selling them our solutions and we're in discussions with them. So I think there's clearly a gap here and the market will fill it, and we'll be one of those market players to fill that gap.

But I also think that the customers are going to be looking at companies that they view to be credible, companies that will support them in the field, and companies that can give them a reliable part of their emission control system which will work and function well.

And I think we're well-positioned through the PACCAR distribution network in California, the Navistar distribution network in California, the Caterpillar distribution network in California, are the three pillars of our distribution networks here in the state, which I think gives me a lot of confidence that we're going to pick up a lot of those folks that have been, if you will, abandoned now by Cleaire and are looking for other solutions. So I'm...

<Q – Philip Shen – ROTH Capital Partners LLC>: I think Iron Man is, if not the largest, one of the largest in the state in terms of retrofits. So, that will be good to try and get in there.

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Absolutely.

<Q – Philip Shen – ROTH Capital Partners LLC>: Also, what happened to Cleaire? It was – I heard that – or I saw that they – that their DPF caused like two forest fires or something?

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Yes, I mean there's a lot of history there, Philip, that you could go back and read. I mean I think it's all in the public domain. But essentially, they used a different solution than many of us in the industry. They used a cordierite material and they used metallic around that cordierite. We use silicon carbide, as you know, which is a more expensive material.

And they got verified by the authorities, so they were fully verified. But unfortunately, some of their products just weren't able to hold up in certain applications in a way that ours, and probably others in the industry, would because we're using different materials at different melt temperatures and what have you in high heat applications.

So I think what happened though is they got bought by a private equity firm. They were highly leveraged. They probably just ran out of gas at some point, because their sales, when they had these recalls in 2012, resulted in them having to go back and put a lot of temporary fixes in place, cost them a lot of money, slowed them down in terms of new sales. And ultimately, the banks call the loans and they couldn't pay the loan.

<Q – Philip Shen – ROTH Capital Partners LLC>: Okay. One last one, I'll jump back in queue. What kind of incremental Honda business can we expect? How close are you and when could we possibly see actual revenue impact?

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Well, you saw the year-over-year improvement, which was huge. Now, we have to temper that by the fact that we're recovering from the tsunami. But even in spite of that, Honda's market share in Accord is up, the U.S. market is up. And certainly, we're seeing that kind of strength if you look at the J.D. Power and Associate data and the R. L. Polk data. We're seeing that same trend continuing here in the first quarter with respect to Honda. So we're pretty optimistic that that will continue as long as the Honda story continues positive.

As far as new platforms, as they said in their press release, they are actively pursuing, putting our technology, our formulation, into new platforms. And we are actually working on a number of new projects there, but I really can't give you a sense of the timing in when those might kick in or any associated volumes with them at this point.

<Q – Philip Shen – ROTH Capital Partners LLC>: Okay. Thanks, Craig.

<A – Craig Breese – Clean Diesel Technologies, Inc.>: You're welcome, Philip.

Operator: Our next question comes from the line of Ian Gilson with Zacks Investment. Your line is open.

<Q – Ian Gilson – Zacks Investment Research, Inc.>: Hi. Good morning, gentlemen. I got a couple of questions. On the repricing mechanism with Honda for the precious metal costs and sales, is that a lag basis or how will you be reimbursed versus the delivery of catalyst systems to Honda?

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: Okay. Thanks for the question, Ian. How are you doing? It's the rare earth elements, it's not the precious metal, just to clarify. And the way it works now going forward from January is that there is what is called an Asian Metal Index, which provides a price index for these six rare earth elements that we use in our catalyst formula. And that is going to be established every quarter. And that – based on that price, we will be reimbursed by Honda.

We have to manage our costs and inventories to match that essentially, okay. So there is going to be some lag if we don't manage inventories properly or correctly. So, there could be lags in that. And depending on when we actually purchase the raw materials. It's a fairly complicated thing and we hope that sometime – over the course of 2013, what we are being reimbursed will start aligning with what is actually costing us on a unit-by-unit basis.

<Q – Ian Gilson – Zacks Investment Research, Inc.>: So it could possibly be a lag?

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: Yes, it could possibly be a lag.

<Q – Ian Gilson – Zacks Investment Research, Inc.>: These are the market prices for rare earth or your costs?

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: They are both the market prices established based on the index and our cost – and by the way, we are working with our suppliers to also – suppliers based on the similar index, okay. But there could be lags based on when we buy the inventory and when we actually get reimbursed for it.

<Q – Ian Gilson – Zacks Investment Research, Inc.>: Okay. In the press release, you state, we will see increased sales momentum driven by more vigorous CARB enforcement. Does that mean you have not yet seen that increased sales momentum?

<A – Craig Breese – Clean Diesel Technologies, Inc.>: So, Ian, I would say that for the purposes of 2012, that is correct. I think if you look at our market share, units sold not just by us but by the entire industry, and the fact that the enforcement activities in CARB really only kicked in in the latter part of 2012, for the purposes of this press release which really referred back to 2012, we didn't see that.

What we're also saying as per the earlier question though is that that enforcement is now stepped up rather significantly. The number of citations being issued in the state is increasing significantly. And as a result, that's driving the truckers and the fleets into asking questions about how do they get complaint so that they avoid any penalties associated with this particular regulation. And as such, that's manifesting itself in more quotations, more data logging requests, and ultimately more sales. That would be the logical outcome of that. So that is the statement and that is definitely what we're seeing.

<Q – Ian Gilson – Zacks Investment Research, Inc.>: Is that also how you're going to drive some of the owner-operators out of business so that that aftermarket sales will actually be translated into OEM sales?

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Well, I mean that's the good point. On the on-road segment, let's stay on that, there is clearly a move by some trucking companies to do a cost-benefit analysis and say, all right, if my new truck costs me so much and my old truck is already, let's say, seven or eight years old and so it's partially depreciated, and I have to install a $15,000 emission control system on it, what's my payback? And though – so that may differ by customer, obviously, or by application, but there is clearly a certain segment of the trucking industry in California that it's opting to buy a new truck rather than expense the retrofitting against the old platform.

Now, that, in turn, means that the estimates on a number of retrofits to be occurring over the life of this initiative would be coming down. We have already stated that back last year, I believe, in a press release, as has CARB. They've already taken that estimate down rather considerably from the original estimate. But I think it's fair to say that that trend would continue and there's probably some truckers, for sure, that are buying new trucks.

<Q – Ian Gilson – Zacks Investment Research, Inc.>: Okay, fine. Thank you very much.

Operator: Our next question comes from a private investor, [ph] Kartik Sergamaswan (41:49). Your line is open.

<Q>: Thank you. I have a few questions that I wanted to ask. I guess, first off, the off-road HDD biz was down significantly year-over-year in the last quarter. Can you just talk a little bit about why that was and just kind of characterize that business in terms of its degree of lumpiness so we just understand the degree of predictability going forward? And I have some follow-up questions.

<A – Craig Breese – Clean Diesel Technologies, Inc.>: [ph] Kartik (42:14), good morning. You're referring to the off-road?

<Q>: Yes.

<A – Craig Breese – Clean Diesel Technologies, Inc.>: I'm not sure we're segmenting off-road with on-road here. What we're talking about for sure is the overall Heavy Duty Diesel segment year-over-year was definitely down, and that is driven by the fact that our London Special Emission Zone (sic) [London Low Emission Zone] (42:38) business, which was around $6 million in Q4 in 2011, did not repeat in 2012, plus a weaker-than-expected California performance in retrofit. And that's, again, in the on-road segment and that's over the two-year period.

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: Yes. [ph] Kartik (42:59), essentially...

<Q>: That doesn't really answer my question, actually. What I'm asking is, if you exclude California and London from last year's number...

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Yes.

<Q>: And you exclude California from this year's number, the number is down, the remainder is down.

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: So, let me...

<Q>: So, I'm trying to understand why that is. If you can explain that, that will be helpful. Thank you.

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: [ph] Kartik (43:18), let me just kind of lay it out for you. The reduction in the fourth quarter and in the full year for our HDD business was pretty much entirely in the on-road retrofit business, okay. Firstly, that's a fact.

The second – the pieces of that, London was by far the biggest piece in the fourth quarter. In addition, if you remember, back in late 2011 and the first half of 2012, we did a significant amount of business in New Jersey, okay? So, while the New Jersey project is still going on, it's nowhere near the levels of where we were in the fourth quarter of 2011. That is also an on-road retrofit program [indiscernible] (43:58). So between London, New Jersey and other parts of the North American on-road retrofit business, our revenue was down in the fourth quarter by close to $9 million.

Okay. The off-road and other, what we call the non-retrofit business, was pretty much flat. And within that flat, there are puts and takes. Europe was slightly weak, but we had stronger performance in North America, et cetera, but those are small in amount.

On a full year basis, our London business was down roughly about $3 million from last year. And New Jersey and some of the other North American retrofits businesses were down maybe another couple of million. We actually had, again, close to a flat kind of performance in the non-retrofit kind of business for the full year. Does that answer your question?

<Q>: No, that's helpful. I'm glad you broke it out at that way, thank you. My next question is related to this issue of PGM reimbursement. And I just want to be clear on this. So you mentioned the possibility of getting a catch-up payment from Honda. Based on your comments earlier, that would pertain mostly to the second half of 2012. Is that no longer the case, or is that just being spread out over the course of 2013? Could you just help me to understand exactly what's going on with that in particular?

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: Okay. Just so you know, we were negotiating a reimbursement mechanism. And again, I got to – please let me clarify it, it's rare earth, not PGM. It maybe just means a lot to us, but PGMs are related to platinum and the platinum group metals. So what we were talking about is rare earth, which has kind of went through a crazy pricing scenario over the last two years.

Anyway, we were negotiating with Honda an overall formula. And what we've so far achieved in the formula that we've agreed to is a formula going forward from January, okay. Talking about anything related to the second half of last year, where we obviously did not get reimbursed, what our costs were, we are still in discussions with Honda and there's just no guarantee at all that they'll agree to anything, but we are in discussions, okay?

<Q>: Okay, fair enough. And then, my next question pertains to Pirelli. [ph] We didn't get to (46:18) talk about it earlier in this call, unfortunately, given what happened in Q4, out could you just talk a little more about exactly how this JV is going to work, what assets you're going to be contributing, what OpEx may be associated with Pirelli, and I guess perhaps, most importantly, what the sales rep is going to be like for that initiative?

<A – Craig Breese – Clean Diesel Technologies, Inc.>: So, let's step back and try to understand a little bit why we did the Pirelli venture to begin with. Our costs in Europe were very high relative to our sales, okay. Coming out the London Emission Zone initiative, we had obviously put in a lot of costs there in terms of supporting that. And what happened is – and we also had a Swedish company, which continues, and we have a person in France that's been helping us on the Renault business.

So when you add all that up, what you see is after we vacate the London initiative, you have quite a bit of SG&A but not enough sales. So at a high level, if you look at the Pirelli situation, they actually have a factory in Romania that make substrates and they have a full-blown emission control business primarily serving the European markets in the Southern part of the continent, primarily Italy, Spain, and they have a pretty extensive network in Germany.

So it turns out, our biggest footprint was in – certainly, in Scandinavia and, to some degree, the U.K. So geographically, the two organizations were complementary. And from a product line standpoint, we don't make substrates but they do, we coat but they don't, so from an operating and an industry standpoint there was also some synergy. But they, like us, didn't have enough sales to justify all of the SG&A and the overhead that they were spending in this business, and they were primarily focused on retrofit as we were.

And so, what we said is, look, this doesn't make any sense, both of us trying to beat our heads against the market by ourselves because our costs are just too high and we can't get any leverage on the sales end. So what if we threw our lot in together on a sales and marketing joint venture, which just the answer to your first question about assets, so virtually no assets are in fact being contributed initially by either party.

What it is, it's a sales and marketing joint venture, a commercial joint venture, that doesn't [ph] preclude (49:00) the fact that in the future, there wouldn't or couldn't be an asset contribution by both parties. But what I'm saying right now is what we're starting to do is by pulling the sales and marketing, if you will, resources, rationalizing them and then getting them focused in three main markets – we're focusing really on OEs both in light-duty vehicle and heavy-duty vehicles, we're focusing on aftermarket, and then we're focusing on fuel-borne catalysts as a specific area of opportunity because we've frankly done very well in the past several years in selling fuel-borne catalysts into the European market.

So that's the initial focus of the business. It's commercial. Like I'd say, assets are really not being contributed. I mean there will be some working capital, but it's – I would deem it not to be material in this instance. But what we're saying is one plus one should equal three in the sense that now we've got a complete solution to offer our OE aftermarket customers, which is a substrate, a coating and a complete system in any of those menu selections or combinations that the customer may want.

So that's the concept, and the hope is that we obviously are going to do better together, leveraging their contacts and their infrastructure in Europe than we would have been able to do on our own. And at the same time, it will be more cost effective.

So I hope that's helpful. I mean we're right at the beginning of this. We're still just assembling the various pieces and getting the key players in place and starting to make our initial sales calls to the customer basis that I touched on a minute ago.

<Q>: Great. Thanks.

Operator: Our next question comes from the line of [ph] Gary Cooper with Pays Capital (51:00). Your line is open.

<Q>: Thanks. So, couple of questions here. If we look at the Catalyst business, it was down in revenue. And I'm wondering if you can tell us, first, what it was in units? And then, second, maybe talk about what else, if anything, is in that division?

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: Okay. Let me just take that, Craig. If you look at the Catalyst business, [ph] Gary (51:28), you really need to look at two things. I presume you're looking at the number which says that our revenue was down in the fourth quarter from $5.8 million to $5.1 million. Is that what you're looking at?

<Q>: Correct.

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: Okay. Now, if you see the next item, which says intercompany revenue, which was down from $1.8 million last year to $1.1 million this year. So if you net those two numbers, because the intercompany revenues is the amount of catalyst we are selling to – from the Catalyst business to their HDD business. Now, that was down because we had a huge push in London last year. So this year, that revenue was down for the Catalyst business by about $700,000.

But now, if you net those out, the overall Catalyst business last year was about $4 million and it is about $4 million this year, it was flat. And that's what I – that's what we said in the press release and what I said earlier, is that volume-wise, we were probably up about 20% because of Honda, or maybe even a little more than that.

But it is this rare earth thing. We were just not reimbursed our full rare earth costs. If we had been reimbursed our full rare earth cost, our revenue might have reflected our volume increases.

<Q>: Yes. So just to understand that, your unit sales to Honda were up roughly 20% in the quarter, because you were not reimbursed on rare earth, you ended up down. Is that accurate?

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: We ended up flat, no, sorry. Our sales – our catalyst sales outside the company ended up flat.

<Q>: Okay.

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: Our catalyst sales within the company were down, yes, were down about $700,000.

<Q>: Okay. So you may have just answered my next question, but let's just walk through it so I'll understand it. Your HDD revenue declined $8.9 million in the quarter and...

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: Right.

<Q>: And [ph] their (53:12) profit declines $1.4 million, right?

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: Right.

<Q>: But now, we go over the Catalyst side, revenue down $700,000 but catalyst profits down $1.2 million. I mean what that suggests to me here is that, overwhelmingly, the profit lever here is with the Catalyst business and really, namely, was the catalyst revenue. But I'm not real sure how the London business or this rare earth reimbursement is impacting that, if you understand my question.

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: Okay. So the Catalyst revenue includes revenue that we sell to our own division. And last year, we had – Catalyst revenue was high because we sold a lot of catalysts for the London business, okay. So, yes, there is a lever there which impacts Catalyst's profitability.

The rare earth element was pretty big. I mean if you figure a 20% volume increase being wiped out because we did not get reimbursed for rare earth, you can kind of do the math. There's a fair amount of rare earth revenue that – if you don't get reimbursed there, it eats your profit right away. It's 100% flow-through to profit.

<Q>: Okay. And again, just to follow up on the previous questions, it doesn't sound to me like you're going to get reimbursed for rare earth in the first half of 2013, but then it may kick in thereafter. Is that accurate?

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: Well, no, no, sorry. I don't know if that's – I didn't mean to make it sound that way.

There is a formula which starts January 1 of 2013 that reimburses us based on a formula we've agreed to with Honda, okay. Now, that formula takes into account all the rare earth elements that we have in our catalyst formulations. So to that extent, we're already narrowing the gap between what it has cost us and what we're going to reimburse.

Now, what matters is that we try to avoid any lags because the prices are going down, okay. So we try to avoid any lags in how we purchase our inventories and turn those around versus how we are reimbursed. So for example, if a price was established at the beginning of every quarter based on the index, we got to make sure that our costs are aligned with that. It takes a lot of execution. So yes, we will be reimbursed more than we were in the second half. It will probably take time for the two are in complete alignment.

<Q>: Okay. And then, just a follow-up on the question I already asked. What else is in this Catalyst segment besides the Honda Accord sales?

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: Okay. So we have sales to – we have service kind of part sales to customers like General Motors, we have sales to Renault.

<A – Craig Breese – Clean Diesel Technologies, Inc.>: It's primarily in HDD.

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: Yes. And then, we have – a very big chunk of it is sales to our own sister company. If you see the intercompany sales, that's the piece of Catalyst that we are selling within the company.

<Q>: Okay, all right. So to change topics here, back to the balance sheet and back to CARB, you've managed working capital pretty well and actually we're almost cash-flat. But I'm wondering given that and given the fact that I think you said that Cleaire had 40% market share in California, do you have enough product in the channel to meet this demand that may or may not show up? And I guess, in answering that, give us some indication of how long it would take from order to you getting the product out to the mechanic or the distributor?

<A – Craig Breese – Clean Diesel Technologies, Inc.>: So, let me try to put some color around that, [ph] Gary (56:43). The difference here with CARB and California versus what we experienced in London is night and day. In London, we had a scenario where we built a lot of inventory, shipped it to the UK based on a certain set of assumptions and forecasts, and found, as the market evolved over there, that we just called it wrong, that it was skewed a lot more to light-duty and mid-range-type applications as opposed to the heavy-duty larger trucks. And as a result, we got caught out with a lot of inventory of the wrong stuff. And as you can appreciate, the supply chain is a pretty extended supply chain when you're shipping across the ocean.

The good news here is we learned a lot from that experience and I think we've corrected rather dramatically and tightened up our supply chain so that, essentially, the [ph] long pull in the tent (57:44) is always substrates, in other words, the ceramics that we buy in, coat, and then build into a system in Canada.

And the good news there is, through our ability now to hold inventory on these substrates – and we have a pretty standard range of substrates which cover virtually a 100% of the California size requirements, and there aren't 100 different sizes, there's probably a half a dozen or so. So, it's high moving at the substrate end.

As you walk through the supply chain, coating, if we have the substrate on hand, which we do, we can coat that substrate in batch in a matter of a day or two. I mean it's that fast if we want to put it through the oven. And then, it's simply a question of getting that canned and turned around and shipped to the customer.

And so, typically, right now, we can get that order turned around in two weeks or so. And based on the forecasts and our ability to supply in the market today, I think that's probably a pretty reasonable timeline to run to. And when we talk to our competitors' distributors and we talk to customers, what we understand is that's pretty good in the marketplace. So our – some competitors out there that are quoting six to eight week turnarounds, and we can clearly beat that at this point in time.

So, I think we're well-positioned there. But at the same time, because we've tightened up the supply chain dramatically and, as I mentioned we got a new team in place, a strong leader now in the Markham site, and a much better forecasting that we're using on this, I don't really see us consuming great – great amounts of cash here in this situation. So, that's why we're pretty – I'd say, we're pretty confident that we're not going to have that kind of consumption of cash in the California initiative that we would have seen maybe in the buildup of inventory with London.

<Q>: Okay, thanks. So here's my last question, I'll get out of here. Cleaire, I might have missed this, I think you said that they had as much as 40% market share in [ph] Cal. (01:00:09) Can you just repeat that so I understand it and maybe even talk about is there any other business opportunity away from the CARB compliance stuff that Cleaire has left open here as well? Thank you.

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Yes, absolutely. So that's their traditional market share. Now, keep in mind, the California situation started with the school bus retrofit back in the late-2000s and early 2010, 2011, and Cleaire was clearly the market leader in school bus retrofits. As it turns out, the school bus retrofit program is not finished and there were a lot of open orders, as it turned out, with Cleaire for school bus retrofits as well as new programs that hadn't yet been started and are funded in the state of California as we speak today. So, with Cleaire exiting that market, that clearly gives us an opportunity to target the school bus market again, all right? And we are, actually. We have quotes out, there is activity in that area. And the fact that Cleaire is not in there is an obvious advantage for us.

By the same token, on the truck side, their exiting the market means that the systems that they have out there that are, we'll call them, exemption systems, and there are roughly 3,000 of them, will have to be brought back in and retrofit with a verified system. So, that opens an opportunity.

And then the new opportunities yet to unfold where Cleaire is no longer a player, so you're pointing out the 40% or so, on a going-forward basis, that's open season on those opportunities for us and the other competitors in the market. So I mean it certainly can't hurt us, it can only help us, but now we just got to get after those opportunities.

<Q>: Okay, thanks.

Operator: Our next question is a follow-up from the line of Philip Shen with ROTH Capital. Your line is open.

<Q – Philip Shen – ROTH Capital Partners LLC>: Hi, just a quick follow up here on the Pirelli discussion. When do you expect you could see the first signs of meaningful sales out of that JV? And then, what could the revenue ramp look like thereafter?

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Well, again, as you appreciate, Philip, I mean we're just getting this off of the road now. I mean, we're going to continue the momentum that we had as our own organization, so I don't expect to see any reduction, if you will, from what we would have previously considered to be a European sale by CDTi. But it should be accretive, it should be additive to that.

I think we'll start to see signs of increased activity and, hopefully, revenue as early as towards the end of the second quarter of this year. But there's different types of customers. The OEs, as you know, the much longer sales cycle there. The aftermarket is a little bit shorter-sales cycle. But my hope is – that we're pushing these guys pretty hard and my hope is that we do start to see some signs of new business blooming, certainly, by the middle of this year or so.

<Q – Philip Shen – ROTH Capital Partners LLC>: Great, that's helpful. Thanks.

Operator: I'm not showing any further questions at this time. I'd like turn the call back over Mr. Craig Breese for closing remarks.

Robert Craig Breese, President, Chief Executive Officer & Director

So, I appreciate all of those questions and the interest on CDTi. I think it's interesting, I didn't get – or we didn't get any questions on the technology portion of the presentation. You will be hearing more about that as time goes on. But I think I understand completely the bend of the questions relative to these earnings reports, because that's essentially what we're talking about today.

Again, I'll just express I am very disappointed, as I know the leadership team is, in these results, but I can tell you that there is a great amount of effort and focus on trying to drive profitability in the business, to try to drive good revenue in the business, and to improve the way that the business processes are working so that some of these one-time issues that we've had to deal with here in the last year or so don't reoccur and really give us the ability then to drive the business forward in an unencumbered fashion.

So again, appreciate everyone's interest in CDTi. I think it's a developing story, remains so, a lot of the good things happening and yet to happen, and we look forward to the next call.

Operator: Ladies and gentlemen, thank you for participating in today's conference. This does conclude the program and you may all disconnect. Everyone have a great day.

