Clean Diesel Technologies, Inc.	CDTI	Q1 2012 Earnings Call	May 10, 2012
Company▲	*Ticker▲*	*Event Type▲*	*Date▲*

PARTICIPANTS

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Robert Craig Breese – President, Chief Executive Officer & Director
Nikhil Atul Mehta – Treasurer, Chief Financial & Accounting Officer

Other Participants

Philip Shen – Analyst, ROTH Capital Partners LLC

MANAGEMENT DISCUSSION SECTION

Operator: Good day, ladies and gentlemen, and welcome to the Clean Diesel First Quarter 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 be given at that time. [Operator Instructions] As a reminder, this conference is being recorded.

I would like to introduce our host for today, Ms. Kristi Cushing, Investor Relations Manager. Ma'am, please go ahead.

Kristi Cushing, Manager-Investor Relations

Thank you, Karen, and good morning, everyone. Thank you for joining the Clean Diesel Technologies conference call and webcast to discuss the company's financial results for the first quarter and fiscal year 2012, which ended on March 31, 2012. By now you should have a copy of our 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.cdci.com.

Before I turn the call over to Craig Breese, President and Chief Executive Office of Clean Diesel, I want to emphasize that some of the information discussed in this call are forward-looking statements, particularly statements about market share targets, margin improvement and overall business growth and momentum as well as the growth of intercompany catalyst sales, expected sales under the California mandate, introduction and timing of new products and expected receipt of regulatory product approval.

These forward-looking statements speak only as of today and involve risks and uncertainties that are outside of Clean Diesel'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 approval and continued customer acceptance of our products as well as 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.

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

Robert Craig Breese, President, Chief Executive Officer & Director

Thank you, Kristi. And welcome to everyone on the call for the CDTI first quarter conference call results. Joining me today is Nikhil Mehta, who is our Chief Financial Officer. I'm actually in Paris, France today calling you after meeting with one of our key customers, the Renault organization. I will be talking a lot today about a lot of the opportunities that we are looking at going forward and the remainder of 2012 and beyond. But before I get to the growth story that's inherent in the CDT business, I think it's very important to just take a quick review of the key milestones that were achieved in our first quarter.

Clearly, this quarter was marked by success in substantially growing our revenues which is a continuation of trends that we saw in 2011. While it is important and remains a top priority, we did not perform up to our expectations in both gross margin terms as well as in driving additional profitability. Nikhil will discuss the results in more detail, but I'll give you a few highlights right away.

Our total revenues grew by over 23% in the first quarter and we're pleased to start off the year with a very solid top line performance. I'll start with a review of the results for our Heavy Duty Diesel Systems division and then we'll talk on some of the key points relative to our catalyst business.

Heavy Duty Diesel Systems reported solid growth of 33% for the quarter. The largest revenue contributor of course was the London Low Emission Zone which is a continuation as well of the strong fourth quarter performance that we noted in the London Emission Zone business for 2011. And it's also starting to see in Q1 in the initial sales that we are now seeing in the mandatory California Truck and Bus Regulations.

Although we booked and shared the majority of the revenue for the London program in Q4 last year, we did report significant earnings in sales in the first quarter as well. And that was largely a result of a decision in early January by the Transport for London, the executive agency responsible for the regulation and administration of the program to proceed with their customary 28-day grace period for non-complaint operators of certain diesel engine vehicles. This gave operators additional time to gain compliance and in fact was good news for us because it resulted in over $4 million of revenue that we recorded in Q1.

With these additional sales in the quarter, we believe we achieved our market share targets which we had spoken about previously. While this program was an overall success, we also had some challenges. Although we achieved good sales in London, it was an extremely competitive market with some 14 competitors vying for competitive – for competition in this project. And so perhaps given the challenging economic conditions in the UK, everyone was really counting on business from this initiative. It was dominated by a product mix that was in fact skewed to the low end of the retrofit market, which was not what we had expected when we were starting this project and in the middle of this project, and that is the product mix was skewing to lighter duty type vehicles.

And so as we discussed in last quarter's conference call, this type of product mix will probably end up resulting in some margin compression in the quarter in Q1, and that's exactly what happened. In fact, in addition to the impact from product mix on gross margins, we also made a decision, I believe a very prudent one, to write-down excess inventories of certain components related to this program given the mix change which of course occurred during the course of the project.

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With this write-down and our planned steps to scale back our presence in London, given that the program has now been largely completed, we expect our gross margins will now start improving going forward. We also believe that the sales under the California program will positively impact our gross margins, particularly as we move into the second half of 2012.

While London was an important contributor to our top-line, I am pleased to announce that we also saw initial revenues from the California program of over $2 million in Q1 which actually exceeded our expectation.

As I mentioned earlier, our expectation is that sales under this program will be weighted to the back half of 2012, as operators make their decisions regarding retrofit options and perform their operational review and planning for installation on their fleets.

Customers we're speaking with or speaking to, many many in the large fleet owners are already making plans and starting to structure their truck fleets to start the retrofit programs and this is good news and we believe that that indicates that there will be good momentum going forward in the project.

As I think all of you on this call know, California really is a home game for us, we're a California-based company. So our turnkey evaluation and installation process coupled with our California-based engineering resources really gives us a leg up and gives us competitive advantage in terms of providing both verified products and immediate customer support to ensure their compliance in government – with government regulations.

In fact, we have dedicated – we've dedicated a substantial amount of service, marketing and engineering resources to ensure that we are in fact the – one of the most dominant providers of emission control products in this market and the feedback we are getting from customers since we rolled out our infrastructure of this focused initiative, has been extremely positive.

We believe that we offer the industry's most comprehensive portfolio of evaluating an environmental protection agency, California Air Research Board verified systems which is [indiscernible] (8:43) retrofit programs and I think another really key point is we also have now over 50 distributors throughout California with added experience/expertise to actually do the installation of the retrofit systems on vehicles that will be coming to them for the systems, which is a huge growth opportunity for Clean Diesel in and of itself.

Additionally, when you have orders in other states, such as New Jersey, are becoming mandatory compliance progressed. In Texas where we just issued a press release, calling your attention to over $1 million in orders from a school bus program there as well as other states. And in fact, as always innovation continues to be a top priority for Clean Diesel. And we are pleased with the results we realized from our investments in R&D over the years and we continue to be so today.

We've received several key product approvals from EPA as well as the California Air Research Board and we expect to continue to see additional regulatory approvals throughout 2012, which only enhances and extends our product portfolio. These product approvals give us access to a wide variety of engine – vehicle engines and were approved to [indiscernible] (9:59) will provide additional opportunities of often beyond our retro business from all the initiatives underway.

And now segueing over to our Catalyst division, let's talk a bit about how that business has performed. Our revenue was flat year-over-year in the first quarter. That was really a positive thing because what we're seeing is we're experiencing continued strength in our intercompany catalyst sales going into heavy diesel applications where we now are using our catalyst in virtually all of the systems that we are selling at the heavy duty application. All the systems in fact that we sold in

London, we're using our own imported catalyst and we would expect that to go on a forward basis certainly in the California initiatives.

In addition, it is positive impact on total gross margins we now because of the customer feedback we're getting that this vertical integration in quality and systems control provides us with a huge competitive advantage. In fact, our catalyst technology always has been virtually unmatched in terms of both its performance and its cost in the market. And that's largely due to the importance we placed on innovation as I said a moment ago.

We're excited to report that the Catalyst division has in fact developed two breakthrough catalysts. The first is a high-performance catalyst which is designed to meet the stringent California Air Resource Board Super Ultra Low Emission Vehicle emission standards, and the second is a palladium-only catalyst that significantly reduces precious metal content when compared to competitive products, which of course is a huge element of the cost, which typically means that the more expensive and price volatile metals, such as Platinum and Rhodium that are being used. So we expect to introduce both of these products into vehicles launched two OEMs later in 2012. We intend to share more details about this as it is a forward looking statement as this development continues to evolve in the remainder of this year.

So in closing, we had good first quarter from a revenue growth standpoint, particularly in our Heavy Duty Diesels systems as you would have expected from previous comments we've given you relative to the London finishing project and the ramp up of the California initiative. And we also believe that we have significant momentum going forward as we progress throughout this year.

Although we anticipated some downward pressure on gross margins, we of course were disappointed with our performance on this and in terms of the bottom line and we have taken steps already to increase gross margins going forward and we expect to see additional, sequential improvement as we move through the year.

Our catalyst business is very stable and we believe there are probably opportunities in the future to expand our sales to both existing and new OEM customers. And that frankly is one of the big reasons that I and some of our team leaders have been in Europe this week talking to a number of potential new accounts.

We're very excited about our growth prospects globally for the Heavy Duty Diesel Systems division and as we ramp up our business for the California initiatives, we will intend to continue selectively targeting no emission zones throughout Europe and elsewhere while we can see the opportunity to provide high value retrofit product and make the kind of profitable margin business that we would expect in this arena.

So, our expectation for revenue growth continues to be positive for 2012 and we need to simply make sure that we can leverage our fixed cost base as our sales expand so that we ensure profitable growth to our shareholders.

I'd also like to take this opportunity to remind the shareholders that we will be holding our 2012 annual shareholder meeting at 10 AM Pacific Daylight Time on Wednesday May 23 in our Oxnard, California facility.

Shareholders will in fact be asked to vote on a number of proposals including the election of seven directors and our application of the appointment of KPMG as our public accounting firm for 2012 and amendments to our 1994 incentive plan and actually an increase to the number of authorized shares of our common stock from 12 million to 24 million shares.

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The increase in the authorized shares of the common stock primarily gives us the flexibility to issue shares for future corporate needs such as future acquisitions, capital raising, forward financial transactions, stock spreads, stock dividends and current and future equity compensation plans. Currently, however, we have no commitments or understandings to issue any of the additional shares of common stock that will be authorized by the proposed amendment.

We have, however, previously disclosed that we are pursuing a growth strategy focused on emissions reduction in the on-road heavy duty diesel retrofit market and the authorization market as well as continued growth of our catalyst business.

So, we continue to accomplish this growth organically and as opportunities present themselves through some reviews of selected acquisition opportunities as well. So, in either case, we may need to raise additional capital to fund such growth. So, our board of directors recommends about four major proposals. We hope that shareholders will review these proposals carefully and support the board in this recommendation and vote in favor of the proposals in proxy.

So with those comments, I'll now turn it over to Nikhil, so that he can give you a bit more detail on the operational results that we are announcing for Q1. Nikhil, over to you.

Nikhil Atul Mehta, Treasurer, Chief Financial & Accounting Officer

Thanks, Craig, and good morning, everyone. I am pleased to report our first quarter fiscal year 2012 results. Revenue of $17 million, up 23% compared to last year. Gross margin was 23.2% compared to 29.1% in the prior-year period. Gross margin, as Craig has pointed out, was negatively impacted by discounting and a shift in product mix in London to the lower end as reported in the fourth quarter of 2011 and also as anticipated for this quarter.

In addition, the shift in product mix in London resulted in the write-down of excess inventories of certain components totaling approximately $600,000 pre-tax and $500,000 after-tax. We anticipate that gross margins will gradually improve as a result of improved product mix driven by the expected reduction in sales in London, the reduction of our footprint in our London operations during the second quarter and growth in our California sales that are anticipated in the second half of the year.

Loss from operations was $2.4 million compared to $1.9 million last year. Loss per diluted share of $0.39 which includes, as I just mentioned, the $600,000 pre-tax inventory write-down versus a loss of $0.54 per share in 2011.

Just a quick highlight on our business segments. Our Heavy Duty Diesel Systems business had another strong quarter, increasing revenues over 33% compared to last year. The London Low Emission Zone program generated about $4.3 million of sale. In addition, we recorded $2.1 million of sales in California, up 58% year-over-year.

The year-over-year sales growth driven by London and California was partially offset by lower sales in the rest of North America and Europe. Our catalyst OEM sales are flat compared to last year though intercompany sales did increase by 300% as we continue to increase the penetration of our in-house catalyst in our Diesel Systems products. We continue to control expenses while investing strategically in opportunities for near-term and longer-term revenue generation.

Operating expenses for the quarter were $6.4 million compared to $5.9 million a year ago. The increase is primarily a result of expenses for new product verifications to broaden our product offerings in California and the rest of North America and executive recruiting and relocation

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expenses incurred in filling two key positions during the quarter. We recorded an income tax benefit of $300,000 in the first quarter.

On a final note, results for the first quarter included approximately a $100,000 and $400,000 of non-cash stock-based compensation expense and depreciation and amortization of intangible assets compared to $300,000 and $400,000 in the first quarter of 2011.

Results for the first quarter also included a non-cash charge of a $100,000 due to the change in fair value of our liability classified stock warrants compared to a gain of $400,000 in the first quarter of 2011.

A summary of the balance sheet: our net working capital was $9.2 million as of March 31, 2012 compared to $11.4 million a year ago. Cash and cash equivalents were $4.4 million.

That concludes our formal comments. Operator, we are now ready for questions.

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QUESTION AND ANSWER SECTION

Operator: Thank you sir. [Operator Instructions] Our first next question comes from the line of Philip Shen from ROTH Capital Partners.

<Q – Philip Shen – ROTH Capital Partners LLC>: Hi, Craig and Nikhil. Thanks for taking my questions.

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

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Hey, Phil, how are you?

<Q – Philip Shen – ROTH Capital Partners LLC>: Doing well, thanks Craig. Craig, the first question is to you, now that you've been at CDTI for a bit of time, a few months, can you share what you've learned, what is your current thinking in terms of how and where you would like to take the company and perhaps you might be able to contrast that with the company's prior strategy, so basically we're trying to figure out what we should be expecting over the next 12 months?

<A – Craig Breese – Clean Diesel Technologies, Inc.>: I mean it's a very good question. And I'll try to be brief and summarize it. There is really three buckets to our business at CDTI and I believe there is good opportunity growing all three buckets that I'm going to define. So, let's talk about each one. The traditional CSI business, the catalytic business as you know, Phil, is dominated today by our OE; we supply to a couple of key customers, primarily the Honda business in North America. And what I believe is really clear to me now is that without really filling up and absorbing the fixed cost that exist in that business and that's primarily in our Oxnard, California site, if you will, the production site. It will be very difficult for us to say that there is a growing path and a really strong and profitable business if we can't on an ongoing basis absorb the fixed cost and really leveraged in volumes to make that business both sustainable and very profitable.

I will say the good news here on the observations, as you say, after 60 days is that as we visit a number of OEs, I've had the chance to go to Asia, our aim in Europe is revisiting additional OEs and also the North American OEs that we do not sell to. The reception is always very positive and the technology is always greatly appreciated. And so the good news there is I think we have a door, Phil, that is definitely cracked open for us. What we just have to do is trying the compelling proposition for the OE to engage with us to define some concrete opportunities in the near to medium term that we can work, execute against and then convert into actual business.

So, leg one on the stool, if you will, is just knocking on all of the OE doors, selectively going after the ones where we the opportunity in the near-term to convert into business, and thereby leveraging the assets that we already have in the ground and then in the organization today.

The second bucket that we don't talk about probably as much as we should is in the heavy diesel area and that business we – I think we tended on the calls over the years and probably in the press releases to focus a lot on the retrofit business. And that's good because these are big opportunities and obviously like California and London are I mean the real needle movers in both revenue and profit potential for the business. But the bucket I want to talk about is what I call as sustainable heavy duty diesel business. What is....

<Q – Philip Shen – ROTH Capital Partners LLC>: I am sorry, Craig, can you repeat that?

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Yeah. The sustainable heavy-duty emissions business.

<Q – Philip Shen – ROTH Capital Partners LLC>: Great. [indiscernible] (23:23).

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Can you hear me?

<Q – Philip Shen – ROTH Capital Partners LLC>: Yes, go ahead.

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Okay. So, what is that exactly, Phil? That is a combination of businesses with OEs and we already have a number of OEs such as John Deere, Atlas Copco, Sandvik and others that are buying OE systems from us and those – that is a repeatable business that goes on year after year after year and once you're, as you know, stepped into a unit or a vehicle that business is a constant business and typically grows. But there are also other opportunities in areas such as underground mining, stationary generator setups, marine applications and materials handling. Traditional businesses by the way that the Engine Control Systems group, the business we acquired four years ago in Toronto has always done very well. But I think what has happened over the last several years is the focus was rightfully so primarily on getting the vertical integration between CSI and ECS put together. And then as Nikhil said, taking that vertical integration and driving it hard into the retrofit business which as you see we're now doing.

But at the end of the day, almost half of the business that we sell Heavy Duty Diesel Systems in isn't really in – isn't retrofit, it's in these more sustainable applications. So, that's an area as I travel and meet people and they say to me, Craig, but if we can only maybe focus more on this, we believe that we can drive more sales. And I agree with them. And so that's going to be a focus and I believe that's very, very attractive upside definitely in the wheelhouse of this company.

And then of course, the third bucket is the one I think you do know a lot about and the other folks on the call, which is the retrofit business which we talked a lot about. And we're still extremely optimistic about the California initiative, the New Jersey initiative has come through, you just saw the Texas announcement. I mean we are working on lot of things and you know what, we won't get every single one we want because it's a competitive world out there. But candidly, I think we're getting more than our fair share right now because we are executing against these very, very [indiscernible] (25:45).

My conclusion with those spikes, Phil, is that, there is a lot of opportunity and growth potential. We got to be extremely focused on them and we got to execute flawlessly to get after them. And I think the organization is responding very positively. I would say the leadership team is an excellent leadership team and they've pooled together in my view very well. And so, they are much focused on this business and we see the profits really going forward for the business.

I hope that gives you a good sense of what I'm seeing.

<Q – Philip Shen – ROTH Capital Partners LLC>: That's very helpful, it does very much so. In fact, I have a few follow-up questions. You started off the conversation with the catalytic business. And historically you've had one, maybe two kind of key OEMs. As you expand it in more auto manufacturers, can you give us a sense for how long the business development cycle is to secure or when you expect to secure a new OEM in the Catalyst business, I mean can we look to 2012 as a year where you might strike a new relationship and even generate some revenue?

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Well, I should – in that particular question, I definitely want to under-promise and over-deliver if you know what I mean. You know how these are, they are typically long-cycle journeys with an OE, journeys that depending on the OE can go sometimes between three and five years. But I will also tell you we are not starting from scratch in a number of areas. So we have ongoing platforms, new launches that we are in the process of doing right now with Honda for example. And, I mean, the discussions I've had over

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here in Europe this week are about real business that already exists and how to ramp that business up, or extend that business in sister platforms or similar platforms.

I also will tell you that most OEs are expanding their business as they downsize in North America and Europe in some cases, they are building new factories in developing countries such as Mexico, Brazil, China, India. And therefore they don't have a mature group of suppliers yet in these markets, and I see those opportunities candidly, Phil, as areas where there is a vacuum right now and one that we can probably fill pretty quickly and potentially get on to platforms quicker than that three to five cycle that I just mentioned. But I believe you will see a combination of both. I think you will see – you will see partly an extension of existing relationships in business we already have with certain OEs and some new business, hopefully that comes from OEs that we've not even done business with, but need our solutions and our capabilities that fits inside their footprint expansions and their product needs as well.

<Q – Philip Shen – ROTH Capital Partners LLC>: Thanks for the color on that. And one other one on Catalyst if I may, in your Q you talked about part of the margin kind of challenge in Q1 for the Catalyst business was due to rare earth pricing. Can you give us – can you tell us which rare earths you guys use and how much does it represent in terms of your COGS cost structure typically?

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Yeah. I mean, we use – there is at least three major rare earth components that we use. In terms of the total COGS, it's material, but not significant in the total COGS I would say, but it is material. But again, this is depending on the actual specification of a given platform or a given OE utilization. Because remember we are working with different formulations and coatings for each and every OE or application that we face. So, the COGS will vary by the applications. Right now, because our business tends to be primarily with one OE, the OE is absorbing, the good news is in that case the OE is absorbing the rare earth cost volatility. But I'm not going to expect that that would happen forever or with that OE, so it remains a concern.

<Q – Philip Shen – ROTH Capital Partners LLC>: I was a bit surprised to read that, rare earths contribute to margin challenges because rare earth pricing I understand across the board has come down from their peaks of – from 2011, and with some even more downside risk ahead in cerium and a bunch of the...

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: Philip is out, what's going on there?

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Well, so cerium – so, Phil, one thing that you want to think about of us is we have the active programs underway to replace the cerium and other rare earth based elements with other solutions that a) won't have the volatility, and b) won't have the costs, all right. So, that's one of the advantages that we have I think as a technology leader is that as time moves on, we're certainly working in that area very, very hard. But you are right, those rare earth costs have definitely come down from their peaks from last year.

<Q – Philip Shen – ROTH Capital Partners LLC>: Great. So let's move on to California. How many retrofits do you think were conducted in California in Q1?

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Well, what I would say to you, there is no market share data that's yet available quite this quickly unfortunately in the public domain. But to the best of our abilities, we triangulate the information that we have. I think I've said that we've traditionally had a market share in California, traditionally, in and around 20%, maybe a bit higher.

We believe that we're getting at least that kind of market share currently in the California retrofit opportunity. But keep in mind that the numbers are very low right now because if you go back to that 20% – I would say $2 million number that we provided you in the report and you take an average retrofit cost of between $12,000 and $14,000. I think you can make the number yourself as to – more like how many kits were installed in Q1.

<Q – Philip Shen – ROTH Capital Partners LLC>: Good. And given what happened with the London market and lower product mix contributing to weaker margins, do you see that kind of risk in the California market at all where you could get some weak product mix or because it's Class 7 and 8 trucks, the standard retrofit is going to be a standard price and you don't see this in kind of downside margin risk?

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Yeah. I mean it's obviously early days. Couple of things that are quite different about California as you know are, number one, there is really four of us in this game in a big way instead of 14. Secondly, California Air Research Board has been incredibly stringent in terms of specifying exactly what can or can't be done here. So there is not a lot of leeway or I would say opportunistic creativity that any of four key suppliers are going to be able to exercise.

So, this compliance, and we believe compliance is going to be virtual and incomplete because of the way the California Air Research Board operates, what you could probably see maybe is the mix may vary from what we would anticipate quarter-by-quarter. But I think there is a finite amount of trucks in the space as has already been defined. We know exactly what those sizes are, what the ages are, what engines are on those trucks.

And the only thing that could probably shift dramatically would be the fleet owners would make a decision to buy new trucks maybe on more an accelerated pace than to retrofit their existing fleets or sell trucks outside of the State of California and then buy new trucks. That is an unknown for sure. We're not good at the crystal ball there. But I think we've made some pretty conservative assumptions to be honest with you Phil that kind of cover us from a contingency basis on how we look at that.

<Q – Philip Shen – ROTH Capital Partners LLC>: Great. And that's helpful. And one last one and maybe I will just – I will jump back in queue. In terms of the equity line of credit, did you use any of it in Q1? I didn't see it in the 10-Q and just wanted to confirm.

<A – Craig Breese – Clean Diesel Technologies, Inc.>: No, absolutely not. Nikhil, I think it might be appropriate for you to comment further on that.

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: No. We've not used any of the line of credit in Q1 and as of today we haven't used it, no.

<Q – Philip Shen – ROTH Capital Partners LLC>: Great. Thanks very much. And we'll talk later.

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Sure, thanks for your support. And, let's definitely reconnect here soon.

Operator: [Operator Instructions] We do have a follow-up from Mr. Shen.

<Q – Philip Shen – ROTH Capital Partners LLC>: It looks like I might be the only one in queue here. So, can you help us out with SG&A, and then give us a sense for what to expect as we trend through the year?

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Nikhil knows probably – go ahead.

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<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: Yeah, we don't give guidance, Phil, but what we have said is that, we said in the fourth quarter last year what are – what we expected our run-rate to be. There was a little bit of a blip in the first quarter because of some of the recruitment and the location expenses. We do expect that to come back down to normal in the second quarter and going forward.

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

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

<Q – Philip Shen – ROTH Capital Partners LLC>: And then one quick follow-up on California. In terms of – we are about a month, maybe a month-and-a-half into Q2, you talked about an acceleration in sales in California as we go through the year. Have you seen that already? I know the majority of the sale is going to be in the back half of the year, but have you started to see a pickup in Q2 relative to Q1?

<A – Craig Breese – Clean Diesel Technologies, Inc.>: Yeah, I mean, it is – let's put it this way, it is sequentially growing. As we get into 2012, we always expected that the curve would get steeper throughout the year. I think we've been pretty consistent in saying that and I think we're seeing exactly what we were expecting. So I don't see any surprises here or anything abnormal in terms of the growth trends at this point. I will tell you that we will be getting additional approvals for products or extensions as the year moves on and that is a part of our accelerated growth. And so, if you couple that with the compliance pressures that the truck owners and fleets are now starting to experience from CARB, I think it's a pretty clear path to starting to see this accelerate as expected.

<A – Nikhil Mehta – Clean Diesel Technologies, Inc.>: Okay. Hey, Phil, just a follow up on your rare earths question, we did some research while this call was going on. If you look at the rare earths, we use cerium oxide, lanthanum oxide and neodymium oxide, none of those prices have come down in this last one year and we did have a secured supply. And, what the OEM does is basically give us dollar for dollar on any price increase. So that covers our cost but it impacts our gross margin percentage.

<Q – Philip Shen – ROTH Capital Partners LLC>: Okay. That's helpful.

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

<Q – Philip Shen – ROTH Capital Partners LLC>: Thanks, Nikhil and thank you, Craig.

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

Operator: Thank you. And I see no additional questions from the phone line.

Robert Craig Breese, President, Chief Executive Officer & Director

Very good. If there are no other questions, I would very much like to thank everyone for joining us on the call today and for your interest in Clean Diesel Technologies. We will certainly look-forward to updating you again here as we move through the Q2 period. And later in the summer I am very, very excited about the potential opportunities that we discussed today again on the growth side and so we'll be looking forward to sharing those results with you at the conclusion of Q2. Thank you very much.

Operator: Ladies and gentlemen, thank you for your participation in today's conference. This does conclude the program and you may now disconnect. Everyone, have a good day.

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