

**Omnitek Engineering Corp. (OMTK)**

Neutral

December 5, 2008

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**Developing the International Natural Gas Vehicle Retrofit Market, but Under-Capitalization Limits Opportunity; Initiating at Neutral**

**Key Metrics**

Price:	\$1.00
Rating:	Neutral
52-Week Range:	\$0.25-3.00
Cash (M):	\$0.04
Debt (M):	\$0
Debt/Capital:	0%
Book Value/Share:	\$0.13

**Market Data**

Market Cap (M):	\$16
Enterprise Value (M):	\$16
Shares Out. (M):	16.0
Float (M):	NA
10-Day Avg. Vol.:	1,100
Institutional Ownership:	NA

**Stock Performance**



Source: TSX

**Valuation**

FY08E EV/Sales:	2.7x
FY09E EV/Sales:	1.5x
FY09E P/E	NM

**Company Description**

*Omnitek Engineering Corp. is a leader in the alternative fuels engines industry. Omnitek develops and supplies new natural gas engines, advanced engine management systems for gaseous fuels and is the manufacturer of proprietary technology used to convert old or new diesel engines to operate on natural gas, propane, or hydrogen. Omnitek offers a total system approach and is supplying alternative energy solutions that are affordable and contribute to combat global warming.*

**Investment Conclusion**

As fuel prices rise and government entities continue to put pressure on sources of carbon emissions, we believe the commercial vehicle, diesel gen set and bus markets—all segments being significant producers of greenhouse gases (GHGs)—will likely accelerate its adoption of alternative-fuel and hybrid vehicle platforms across all vehicle sizes. From a technology standpoint, we feel Omnitek is well positioned to grow its base of business within the diesel-to-natural gas conversion markets; however, we believe the company's balance sheet could be a limiting factor to revenue and earnings growth.

**Summary**

• **Omnitek is a leader in engine conversions.** Omnitek's proprietary engine management system has been successfully adapted to work with many different engine designs to meet current and future emissions standards. While Omnitek's core strength is in the conversion of existing gasoline or diesel engines to natural gas, the company also offers complete new natural gas engines which serve as a direct replacement for high-polluting diesel engines in stationary and vehicle applications.

• **Natural gas fueled vehicles are on the rise.** The demand for natural gas vehicles is expected to increase in the foreseeable future primarily due to new legislation and regulations surrounding emissions from the transportation sector. As more stringent emissions standards are adopted, the automotive industry will have no choice but to devote significantly more resources in the development of natural gas vehicles, hybrid vehicles and clean diesel vehicles.

• **Capital is required for growth.** Omnitek's growth outlook is highly dependent on the company's ability to increase its working capital for inventories of key components. As of the end of 3Q08, Omnitek held a cash balance of \$42K and no debt (net cash of \$0.00 per share). Work-in-process inventory amounted to \$1.3M, or just over one quarter's worth of conversion kit production. Given the need for additional capital to fund operations at this time, we are initiating coverage of Omnitek Engineering Corp. with Neutral rating.

**MCF Estimates\***

	FY08E	FY09E	FY10E
SALES (M)			
1Q	\$0.5	\$1.0	
2Q	1.0	1.5	
3Q	1.2A	1.8	
4Q	1.0	1.6	
<b>FY (Dec)</b>	<b>\$3.6</b>	<b>\$5.8</b>	<b>\$10.9</b>
EV/S	5.5x	3.8x	2.4x
EPS			
1Q	(\$0.01)	(\$0.01)	
2Q	(0.00)	0.01	
3Q	0.00A	0.01	
4Q	(0.00)	0.01	
<b>FY (Mar)</b>	<b>(\$0.02)</b>	<b>\$0.02</b>	<b>\$0.10</b>
P/E	NM	15.6x	6.8x

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Please see **Important Disclosures** on the last page of this report



## Company Background

Omnitek, based in San Marcos, California, develops and supplies new natural gas engines, advanced engine management systems for gaseous fuels (natural gas, propane and hydrogen) and technology and components for diesel-to-natural gas engine conversions. Omnitek's products service both stationary applications (diesel gen sets) and the global truck and bus markets, including light commercial vehicles, minibuses, heavy trucks and municipal buses. Currently, Omnitek's sales are predominantly to markets in Thailand, but the company has been expanding into the U.S. market place as well. In addition, Omnitek has been marketing its technology to India, Bangladesh, China, Mexico and Myanmar. Omnitek markets its products to engine manufacturers, system integrators, fleet operators, engine conversion companies and end-users.

*CNG vehicles offer performance comparable with diesels while capitalizing on the economic and environmental benefits associated with natural gas.*

Omnitek's proprietary engine management system has been successfully adapted to work with many different engine designs to meet current and future emissions standards. While Omnitek's core strength is in the conversion of existing gasoline or diesel engines to natural gas, the company also offers complete new natural gas engines which can serve as a direct replacement for high-polluting diesel engines for stationary and transportation applications. The company's electronic control unit senses engine parameters in real time and adjusts to deliver the correct amount of fuel and ignition timing, allowing for optimal engine performance and the lowest emissions.

Omnitek technology enables diesel and gasoline engines to operate on natural gas or propane and provides a cost effective option to any engine manufacturer (OEM) as well as to the retrofit markets and engine converters. Omnitek offers conversion kits, along with engineering support to rebuild engines locally or through partnering companies in other locations across the globe. In addition, the company has the capability of engineering and completing the conversion of diesel engines from start to finish at its headquarters in San Marcos, California. Complete service conversions can be made on new or old diesel engines.

Omnitek designs natural gas conversion kits in two categories: The Carburetion and Ignition Management System (CIMS) which is used for carburetor controlled engines and is priced by the company at approximately \$1,300 per kit, and the Electronic Fuel Injection system (EFI) for fuel injected engines priced at approximately \$2,600 per kit. Omnitek's gross margins have averaged 35% for the first three quarters of FY08.

## Air Quality

Each year, approximately 68% of the oil consumed in the United States is used for transportation. As a result, vehicle emissions have become a leading source of U.S. air pollution. Advances in technology and environmental regulations have decreased aggregate emissions of key air pollutants over the last three decades despite a marked increase in energy consumption.

Nonetheless, fossil fuel-fired power plants, other industrial sources and vehicles remain significant sources of air pollution. These emissions can be associated with significant health problems, including respiratory and cardiopulmonary disease, cancer and birth defects. In addition, these pollutants can be harmful to forests and bodies of water.

***68% of the oil consumed in the U.S. is used for transportation – vehicle emissions have become the leading source of air pollution.***

**Past successes.** The U.S. Environmental Protection Agency's (EPA) Acid Rain Program, enacted as part of the 1990 Clean Air Act Amendment, is the only program directed primarily at reducing air emissions from electric utilities. The EPA program has reduced sulfur dioxide (SO<sub>2</sub>) emissions from utilities faster than required by law for a fraction of the initial cost estimates. By 2010, the EPA expects the program will reduce annual SO<sub>2</sub> emissions by 10 million tons from 1980 levels.

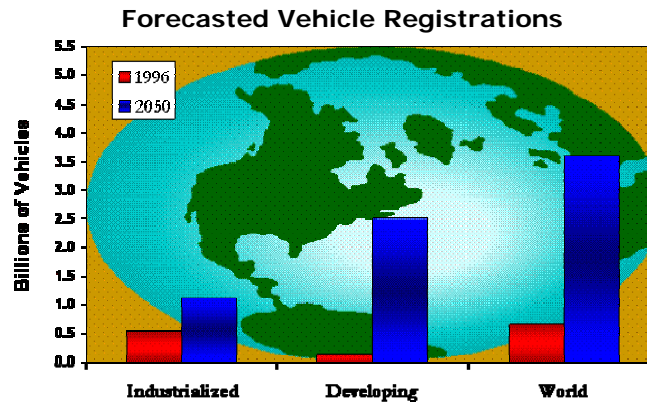
**Eyeing autos.** Cars and trucks are also responsible for significant quantities of pollutants that are emitted every day. Federal and state regulatory programs also limit air pollution directly by restricting emissions from cars and trucks, and indirectly by setting the criteria for the fuel for vehicles. An individual car meeting 2004 federal requirements will emit 95% less carbon monoxide (CO), 94% less nitrogen oxide (NOx), and 98% less hydrocarbons than an average car did before regulation.

**Overall emissions remain constant.** However, despite the fact that individual cars and trucks are far cleaner today than they were in 1970, total emissions from the fleet of highway vehicles have remained relatively constant, because Americans drive twice as many miles today (2.5 trillion miles a year) as they did in 1970. Therefore, it becomes increasingly clear to us that advanced technologies will have to further reduce the production of harmful emissions — or eliminate them altogether — in order to improve air quality as the driving population increases and as each individual driver makes greater use of their personal vehicles each day.

**Estimates from the EPA indicate that motor vehicles in the United States account for:**

- 78% of all carbon monoxide emissions
- 45% of nitrogen oxide emissions
- 37% of volatile organic compounds

The need to reduce emissions from cars and trucks has contributed to technological innovations that have transformed the domestic and global automotive industries. U.S. vehicle emission standards were the primary driving force for the original development of innovative technologies, many of which have become standard design features of today's high-tech vehicles: sophisticated three-way catalysts, onboard computers, oxygen sensors and fuel injection systems for cars and advanced fuel systems for trucks. Technologies such as these have allowed today's vehicles to run more cleanly and efficiently with better performance, reliability and durability compared to their counterparts of the 1960s and 1970s.



*Source: U.S. Department of Energy*

Despite the current overcapacity, the number of worldwide automobile and truck registrations is expected to grow significantly in future years, with the number of vehicles worldwide projected to grow from 800 million today to 3.5 billion in 2050. Industrialized countries could see a doubling of registrations between now and 2050. More importantly, developing nations like China and India are expected to experience an explosion in the number of vehicles; hence the recent moves by major vehicle companies to enter into partnerships with Chinese vehicle makers, or establish new production facilities in countries such as Thailand to serve as hubs for regional operations.

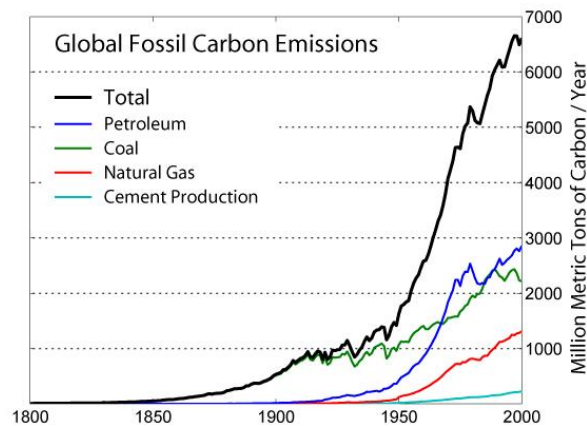
This explosion in the developing regions of the world has major implications not just for the automobile industry's global economic impact, but also for its impact on energy use and emissions. Rapid economic growth generates demand for personal mobility and the transport of goods. This in turn drives the long-term demand for transportation energy (oil for the production of gasoline).

Advances in technology and environmental regulations have decreased aggregate emissions of key air pollutants over the last three decades despite a notable increase in energy consumption. Federal and state regulatory programs limit air pollution directly by restricting emissions from cars and trucks, and indirectly by setting the criteria for the fuel for these vehicles.

Vehicle emissions fall into five main categories:

- **Carbon Dioxide (CO<sub>2</sub>)** - a product of burning a fuel which contains carbon. CO<sub>2</sub> is believed to be a main contributor to global warming.
- **Carbon Monoxide (CO)** - a product resulting from the incomplete burning of a hydrocarbon. In high concentrations it is poisonous.
- **Hydrocarbons (HC)** - also known as "Volatile Organic Compounds" or VOCs, which are essentially unburned fuel. VOCs can cause breathing problems and are a contributor to "Photochemical Smog" in certain climatic conditions.
- **Oxides of Nitrogen (NO<sub>x</sub>)** - a product of heating air in engines. NO<sub>x</sub> is a contributor to both Photochemical Smog and Acid Rain and can be an irritant to the lungs.
- **Particulate Matter (PM)** - very small particles consisting mostly of unburned carbon.

Since the industrial revolution, carbon dioxide emissions have dramatically increased as they are a byproduct in the combustion of hydrocarbon based fuels such as gasoline and coal. As can be seen in the following graph, which illustrates carbon dioxide emissions as a function of time, annual emissions have dramatically increased over the past 150 years.



Source: Department of Energy

### The Growing Natural Gas Opportunity

Natural gas used in the transportation sector is still in its infancy, but natural gas powered vehicles present an enormous opportunity for cleaning emissions from this sector. Demand from the transportation sector currently accounts for only 3% of total U.S. natural gas demand. The demand for natural gas to supply natural gas vehicles is almost negligible compared to the energy requirements of traditionally fueled vehicles (i.e. gasoline and diesel fueled vehicles).

The demand for natural gas vehicles is expected to increase in the foreseeable future primarily due to new legislation and regulation surrounding emissions from the transportation sector. As more stringent emissions standards are adopted, the automotive industry will have no choice but to devote significantly more resources in to the development of natural gas vehicles, hybrid vehicles and clean diesel vehicles.

Natural gas, also known as methane, is a colorless, odorless fuel that burns cleaner than many other traditional fossil fuels. It is one of the most popular forms of energy today for home heating, industrial applications, power plants as well as vehicular transportation. Increasingly, natural gas is being used in combinations with other fuels to improve their environmental performance and decrease air pollution.

Natural gas is produced, sometimes along with oil, by drilling the earth's crust where pockets of natural gas were trapped hundreds of thousands of years ago. Once the gas is brought to the surface, it is processed to remove impurities, like water, other gases and sand. It is then transmitted through large pipelines that span large distances and serve city and county infrastructures.

Rising oil prices and increased environmental awareness have forced diesel-intensive transportation, such as trucks and buses, to increase focus on near-term alternatives, including technology based on natural gas. In our view, Omnitek is well positioned to capitalize on this increased market demand for natural gas engines. Natural gas vehicles are typically five years ahead of most other commercially viable fuels in terms of air pollutant reductions, resulting in a growing demand for natural gas fueled engines. The mass conversion of more than 10,000 diesel busses to compressed natural gas (CNG) in Delhi India has led to a measurable improvement in air quality. This success is being duplicated in Bangkok and other cities throughout Asia.

In Thailand, a number of convergent factors have led to the establishment of natural gas vehicles on a significant commercial scale, including the volatility in price of petroleum imports, the need for improved air quality, a reduction in greenhouse gas emissions and the availability of domestic and renewable fuel sources. Omnitek has successfully penetrated the natural gas engine market in Thailand over the past 24 months.

Benefits of natural gas vehicles:

- Reduction of national demand and oil dependency
- Improve national balance of payments by reducing the need for imported oil
- Improve national security of energy supply
- Improve economic stability (dampen oil prices)
- Make use of renewal energy (bio-methane)

Natural gas engines offer two important advantages over diesel engines: reduced emissions and lower fuel costs.

**Reduced emissions.** The problem of air pollution caused by vehicular exhaust emissions is recognized worldwide as the number one source of air pollution that needs to be addressed in order to prevent major health consequences, especially in third world nations. The following table highlights the advantages of using garbage trucks that use natural gas instead of diesel fuel. Using natural gas allows garbage trucks to produce substantially lower emissions, reduce noise and eliminate organic water pollution. Particulate matter emissions could be reduced by up to 94%.

<b>Benefits of Natural Gas vs. Diesel-Fueled Garbage Trucks</b>		
<i>Impact</i>	<i>Pollutant</i>	<i>Percentage Reduction, Natural Gas Trucks</i>
<b>Air Pollution</b>	•Particulate matter	66-94%
	•Nitrogen oxides	32-73%
	•Non-methane hydrocarbons (NMHC)	69-83%
<b>Noise</b>	•Noise (decibels)	50% (behind truck)
		90% (inside truck)
		98% (beside idling truck)
<b>Water pollution</b>	•Organics	100%

Source: Bus Futures 2006

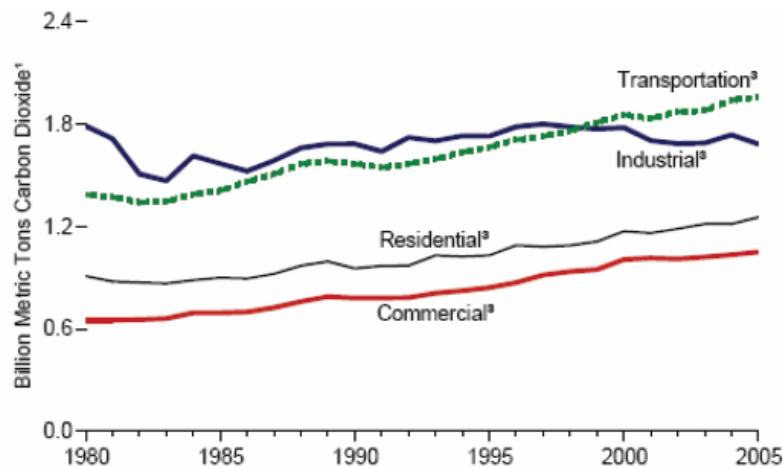
Natural gas vehicles have been shown to be dramatically better for the environment. A case study by the National Renewable Energy Laboratory (NREL) compared buses using CNG to those using diesel and found:

- Average emissions of **NOx** from CNG buses were 54% lower than comparable diesel buses.
- Average **carbon monoxide** emissions were 94% lower than comparable diesel buses.
- Natural gas engines operating in diesel applications offer the opportunity to reduce larger **particulate matter** emissions ten-fold.

*The transportation industry is one of the leading emitters of CO<sub>2</sub> with emissions continuing to grow on an annual basis.*

Natural gas has emerged as a viable solution for high exhaust emission engines. Diesel engine emission standards are getting increasingly difficult to meet and many geographies are beginning major programs to replace diesel fueled engines with natural gas due to its superior emissions profile. Importantly, the transportation sector is increasingly being targeted for emissions reduction technology as a result of the steady growth of CO<sub>2</sub> generation from vehicles of all sizes.

**Annual CO<sub>2</sub> Emissions by Sector in the U.S.**



<sup>1</sup> Metric tons of carbon dioxide can be converted to metric tons of carbon equivalent by multiplying by 12/44.

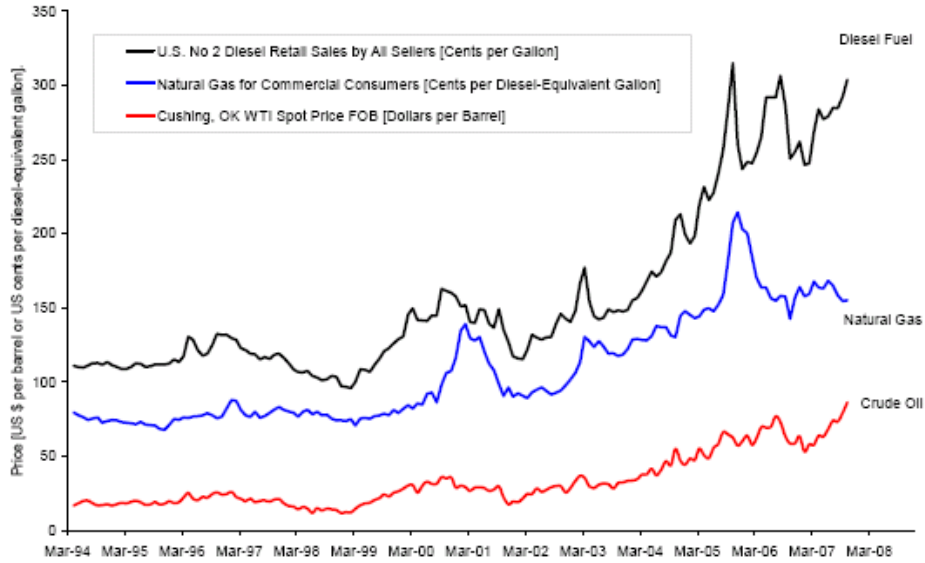
<sup>2</sup> Based on chained (2000) dollars.

Source: The Department of Energy, Energy Information Administration

**Lower operational costs.** A 2006 study noted that the cost of buying and operating a natural gas bus would be below the diesel equivalent provided that oil is above \$31 per gallon (expressed in 2005 dollars). Considering the current oil prices are well over this level and historical spikes above \$100 per barrel, users of diesel engines for stationary and transportation applications would be well served to retrofit these engines with natural gas technology or buy new engines that are natural gas-enabled. The study was prepared by product and technology development firm TIAX LLC for the California Natural Gas Partnership.

Importantly, diesel and natural gas prices are correlated. We note, however, that the correlation is less than one—suggesting that when crude oil prices rise, natural gas prices tend to rise less than diesel prices do. The delta that is created when diesel rises faster is referred to as the “price gap.” The economics for a natural gas fueled vehicle become more attractive as the price gap widens. Currently, the price gap for a gallon of diesel vs. a diesel gallon equivalent of CNG is approximately \$0.85 per gallon.

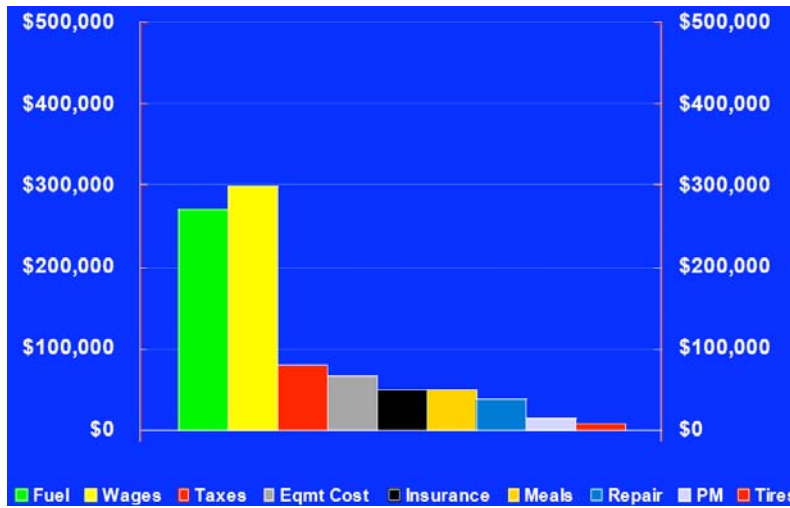
**Price History of Vehicle Fuels (Per Diesel Gallon Equivalent)**



Source: The Department of Energy, Energy Information Administration

As one can see from the following graph, with the exception of wages, fuel costs represent the greatest operating expenditures associated with trucking. As the price gap between diesel and natural gas increases, the payback period becomes shorter and shorter.

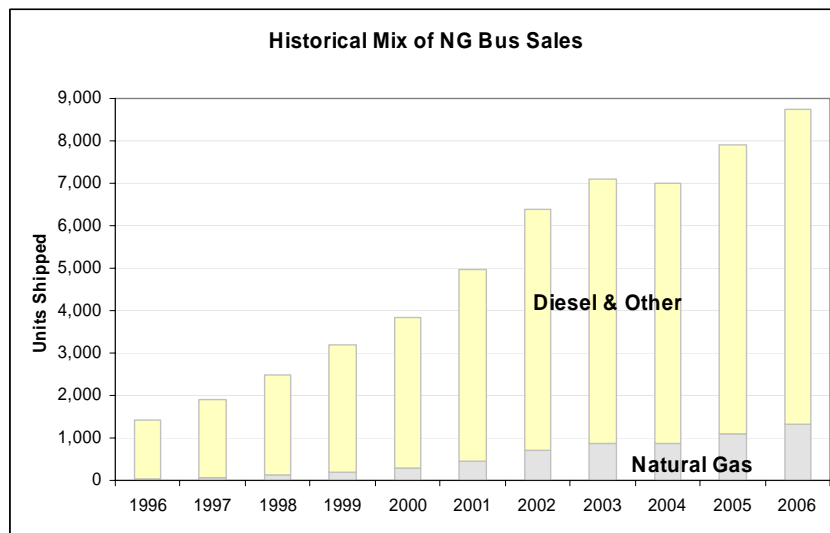
**Truck Company Operating Costs**



Source: Kenworth Truck Company (a subsidiary of PACCAR, Inc.)

### Natural Gas Fueled Vehicle Growth

The 1970 Federal Clean Air Act and its 1990 amendments have targeted the reduction of emissions from diesel and gasoline burning vehicles citing adverse health effects stemming from six “criteria pollutants” including lead, CO, ground-level ozone, particulate matter, S<sub>2</sub>O<sub>4</sub> and nitrogen oxides (NO<sub>x</sub>). However, automotive air pollution remains one of the largest environmental problems facing the United States. As a result, light-, medium- and heavy-duty trucks, in addition to buses, designed to run on CNG are capturing a growing portion of the market for these vehicles. In 2006, CNG-powered transit buses represented 15.2% of all transit buses produced, up from 14.0% in 2005. Omnitek has designed natural gas conversions for over 65 diesel engine models.

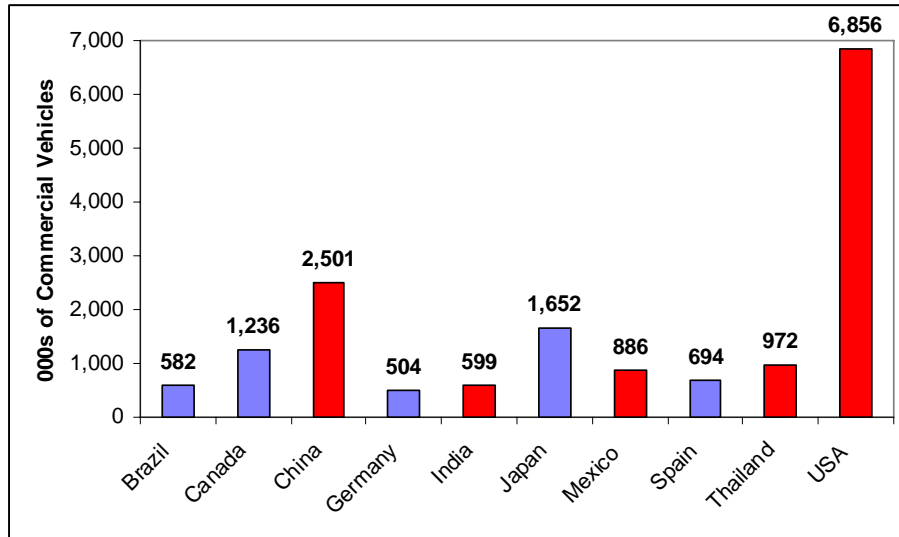


Source: Bus Futures 2006

***Omnitek has designed natural gas conversions for over 65 diesel engine models enabling the company to address a large portion of the engine market.***

Omnitek is currently targeting key geographies where the number of commercial vehicles fueled by natural gas is growing in size. The following graph details countries worldwide which produced more than 500,000 natural gas fueled commercial vehicles in 2007. Omnitek is currently marketing their natural gas engine technologies to those countries labeled in red.

**Natural Gas Commercial Vehicles Produced by Country in 2007**



Source: OICA

**Partnerships**

**CYT Gas Tech Co. Ltd.** In December 2007, Omnitek signed a Business Representative Agreement to appoint CYT Gas Tech (CYT) the exclusive Omnitek natural gas engine warranty and engine parts distribution center for Thailand, as well as a non-exclusive dealer for the company's CNG engines. Purchasers of Omnitek's CNG conversion kits can have their vehicles serviced under warranty at CYT's facilities in Thailand.

**Omnitek Engineering Thailand Co.** In December of 2007, Omnitek entered into a joint venture agreement in Thailand with Omnitek Engineering Thailand Co. Ltd, to sell the company's proprietary diesel-to-natural gas conversion kits and new natural gas engines used to repower existing diesel trucks and buses. Omnitek owns a 15% interest in the joint venture and sells its CIMS and EFI kits to JV.

**Competition**

Omnitek's primary competition comes from manufacturers of new commercial vehicle engines designed for natural gas, whether CNG or LNG. Within this category, Omnitek competes with Westport Innovations, a manufacturer of Class 6, 7 and 8 natural gas engines for garbage trucks, municipal buses, as well as medium and heavy-duty trucks.

Westport controls virtually the entire medium-duty truck market as it relates to natural gas systems. Caterpillar and John Deere had previously made attempts at the technology, but currently Westport's LNG systems, as used in the ISL G and ISX engines, are the dominant platform. Westport intends to maintain its hold on the growing heavy-duty truck market, of which the company already has a substantial market share.

Other competition for Omnitek comes from the emerging diesel-electric hybrid technology platform that targets the heavy-duty truck market. Eaton Corporation and Peterbilt have jointly developed a hybrid technology that is believed to produce fuel savings of more than 5%. Coca-Cola recently launched a fleet of 22 diesel-electric heavy-duty delivery trucks that use 37% less fuel and produce 32% fewer emissions. Coca-Cola

also plans to add an additional 120 vehicles. The Port of Los Angeles is also considering other alternative fuels in addition to natural gas, having recently debuted a heavy-duty electric truck that can pull a 60,000-pound cargo container.

Competitors specific to the natural gas conversion kit marketplace include Iveco (Italy), a manufacturer of a broad range of light, medium and heavy commercial vehicles and intercity buses and coaches, Weichai Power Company, Ltd. (China), a manufacturer of diesel engines for heavy-duty vehicles, coaches, construction machines and power generators, and Woodward Governor Company (U.S.), a manufacturer of energy control solutions for aircraft engines, industrial engines and turbines, and electrical power equipment.

### Investment Risks

**Early commercial stage company.** Omnitek has generated limited revenue from operations. To date, the company's development efforts have been focused primarily on the research, design, development, manufacturing and marketing of its products. A very limited number of Omnitek's products are currently on the market and the time frame necessary to achieve market success is uncertain. There can be no assurance that any of Omnitek's products will prove to meet the anticipated levels of approval or effectiveness, or that the company will be able to obtain and sustain customer as well as distribution approval.

**Fuel prices present a key external influence.** The appeal of natural gas technology is caused in part by the rising cost of oil and the relatively less volatile price of natural gas. Currently, there remains an economic advantage to using natural gas over diesel fuel, however, the delta in pricing among these fuels does fluctuate. If oil retreats to historical prices and if natural gas prices rise significantly, Omnitek's technology solution will likely become less appealing and will affect customer adoption rates.

**Capitalization.** Omnitek's growth outlook is highly dependent on the company's ability to increase its working capital for inventories of key components. As of the end of 3Q08, Omnitek held a cash balance of \$42 thousand and no debt (net cash of \$0.00 per share). The inability to raise additional funds for operations would necessarily impact operating cash flow and revenue growth.

### Management

According to company information:

**Werner Funk** has been a Director and the Chief Executive Officer from Omnitek's formation in May of 2001. Mr. Funk has over 26 years of experience in international business, manufacturing, engineering, marketing and internet commerce. Mr. Funk was educated in Germany where he attended high school and vocational college for automotive technology, receiving a bachelor degree in automotive technology. Mr. Funk worked for Mercedes-Benz in Germany as was assistant crew chief of a Porsche factory sponsored racing team. Mr. Funk is also currently the Chief Executive Officer of Nology Engineering Inc., a manufacturer of automotive products for the performance aftermarket, and PerformanceDepot.com, a leading internet based E-commerce site selling automotive performance parts.

**Janice Quigley** has served as Chief Financial Officer of Omnitek since 2003 and is responsible for the financial reporting and personnel management of the company. Ms. Quigley worked in the electronics industry for 27 years prior to relocating to San Diego in 1992. Ms. Quigley joined Advantage Lift Systems, Inc. a manufacturer of heavy-duty vehicle hoists, in 1993 as controller and was promoted to Chief Financial Officer in 1997 and remained in this position until October 2000 when the company was sold. Ms. Quigley is also the Chief Financial Officer for Nology Engineering, Inc.

**John Reed, MD**, is an outside director of Omnitek and is actively involved in project evaluation and the development of marketing concepts. Dr. Reed's knowledge of engines and engine management systems, as well as his experience in mergers and acquisitions, makes an important contribution to Omnitek's management. Dr. Reed graduated from the University of California and holds dual Bachelors of Science degrees in

Microbiology and Immunology, as well as a Bachelors in degree in Public Health. Dr. Reed received his Doctorate of Medicine from he University of California, San Diego.

**Pete Peterson** is currently the Vice President of Engineering at Omnitek. Mr. Peterson holds a Bachelor of Science degree in Aeronautical Engineering from California Polytechnic State university, San Luis Obispo. Mr. Petersen is an experienced engineering manager and development engineer, having spent 20 years in the field of development, testing and calibration of electronically controlled gaseous fuel injection and metering systems. Mr. Petersen possesses intimate knowledge of fuel systems and engine design, electronic engine control systems and CNG specific control algorithms. Mr. Peterson was a founder of Pensare Inc, which was acquired by Omnitek in November 2006.

### Balance Sheet and Earnings Model

Omnitek finished 3Q08 with \$42 thousand in cash on its balance sheet and no debt. The company's book value per share stood at \$0.13, while net cash per share was \$0.00. Net inventories on hand at the end of the third quarter were \$1.3 million. There are currently 16 million shares outstanding, approximately 55% of which are owned by the Chief Executive Officer, Werner Funk. Insiders currently control 64% of the company's outstanding shares. The following table lists the major insider holdings of Omnitek shares.

#### Current Shareholders of Omnitek Engineering

Name of Shareholder	Shares Owned	Percent
Werner Funk	8,721,132	54.5%
Peter Petersen	1,200,000	7.5%
Jan Quigley	240,000	1.5%
John Reed	79,364	0.5%
<u>Other Shareholders</u>	<u>5,765,902</u>	<u>36.0%</u>
<b>Total</b>	<b>16,006,398</b>	<b>100.0%</b>

Source: Company reports

Our earnings model looks for Omnitek to reach sustained bottom line profitability in 2Q09, however, we believe additional capital will be needed to reach this goal. Our model looks for Omnitek to post FY09 EPS of \$0.02, gross margins of 36% and operating margins of approximately 7% on revenue of \$5.8 million. In FY10, our model looks for Omnitek to post EPS of \$0.10 gross margins of 37% and operating margins of approximately 15% on revenue of \$10.9 million.

Given the need for additional capital to fund operations at this time, we are initiating coverage of Omnitek Engineering Corp. with Neutral rating.

**Omnitek Engineering Corp. (OMTK)**

Neutral

**Other Public Companies Mentioned in this Report:**

Caterpillar Inc. (CAT \$37.52, Not Rated)  
The Coca-Cola Company (KO \$44.75, Not Rated)  
Deere & Co. (DE \$30.98, Not Rated)  
Eaton Corporation (ETN \$41.58, Not Rated)  
Paccar Inc. (PCAR \$25.83, Not Rated)  
Westport Innovations (WPRT \$3.97, Buy)  
Woodward Governor Company (WGOV \$19.64, Not Rated)

**Omnitek Engineering Corp.****Balance Sheet**

(\$ in thousands, except ratios)

	<u>FY06</u>	<u>FY07</u>	<u>3Q08</u>
Current assets:			
Cash and equivalents	18	23	42
Accounts receivable, net	59	72	228
Inventory, net	1,241	1,167	1,325
Deposits	143	70	408
Deferred Tax Assets	131	462	462
<i>Total current assets</i>	<u>1,591</u>	<u>1,795</u>	<u>2,466</u>
Fixed Assets, net	46	33	26
Prepaid expense	0	3	3
Intellectual property, net	473	355	267
<i>Total assets</i>	<u>2,110</u>	<u>2,186</u>	<u>2,762</u>
Accounts payable and accrued expenses	154	76	248
Accrued expenses-related parties	169	242	306
Customer deposits	76	80	174
Shareholder loans	15	15	0
<i>Total current liabilities</i>	<u>414</u>	<u>412</u>	<u>728</u>
<i>Total stockholders' equity</i>	<u>1,696</u>	<u>1,774</u>	<u>2,034</u>
<i>Total liabilities and stockholders' equity</i>	<u>2,110</u>	<u>2,186</u>	<u>2,762</u>
	<u>FY06</u>	<u>FY07</u>	<u>3Q08</u>
Current Ratio	3.8	4.4	3.4
Debt as % Total Capital	0.0%	0.0%	0.0%
Net Cash per Share	\$0.00	\$0.00	\$0.00
Book Value per Share	\$0.12	\$0.11	\$0.13

*Source: company reports*

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Omnitek Engineering Corp. (OMTK)

Neutral

**Omnitek Engineering Corp.**

**Earnings Model**

(\$ in thousands, except per share amounts)

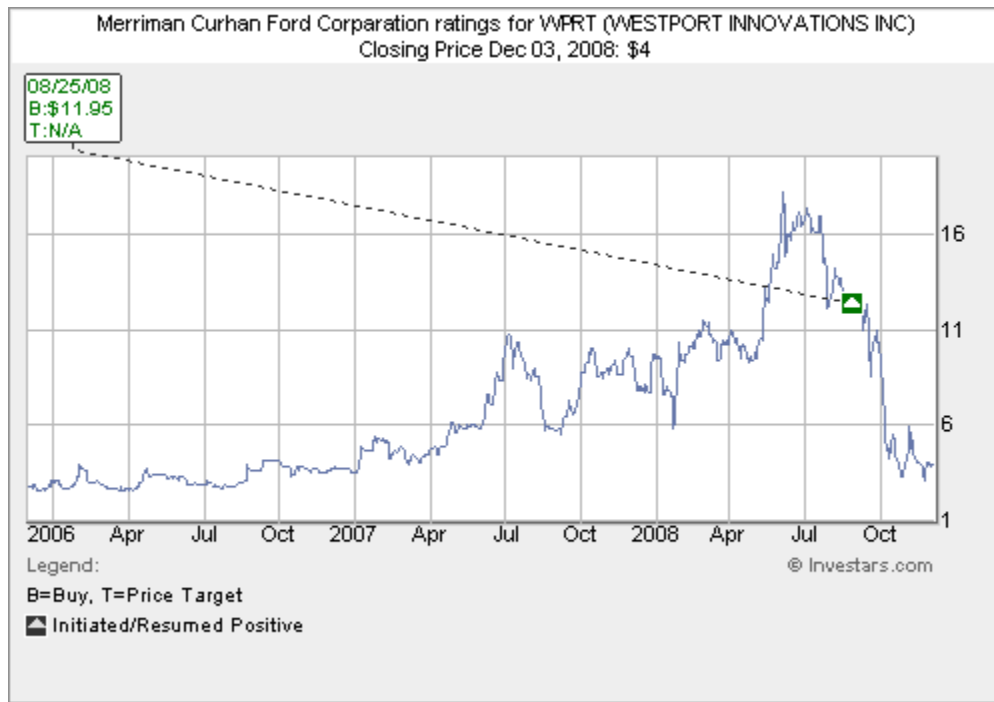
(Fiscal Year ends December)	2008E				2009E				FY10E		
	Q1A	Q2A	Q3A	Q4E	Q1E	Q2E	Q3E	Q4E			
	Mar-08	Jun-08	Sep-08	Dec-08	Mar-09	Jun-09	Sep-09	Dec-09			
<b>Net sales</b>	<b>907</b>	<b>1,017</b>	<b>1,175</b>	<b>950</b>	<b>3,623</b>	<b>1,001</b>	<b>1,450</b>	<b>1,825</b>	<b>1,554</b>	<b>5,830</b>	<b>10,902</b>
Cost of sales	811 #	775	639	737	2,364	668	927	1,150	987	3,731	6,868
<b>Total Gross Profit</b>	<b>96 #</b>	<b>243</b>	<b>323</b>	<b>439</b>	<b>1,260</b>	<b>333</b>	<b>523</b>	<b>675</b>	<b>567</b>	<b>2,099</b>	<b>4,034</b>
General & Administrative	326 #	1,415	292	298	1,159	301	320	340	360	1,321	1,841
Bad Debt Expense	27 #	(5)	2	2	7	2	2	2	2	7	7
Research and Development	168 #	356	32	39	225	83	85	87	90		
Depreciation and amortization	556	1,903	360	409	1,391	420	441	463	486	1,673	2,443
<b>Income (loss) from operations</b>	<b>(460) #</b>	<b>(1,660)</b>	<b>(175)</b>	<b>30</b>	<b>(104)</b>	<b>(87)</b>	<b>82</b>	<b>212</b>	<b>81</b>	<b>426</b>	<b>1,591</b>
Impairment of Investments	(1) #	(0)	0	0	0	0	0	0	0	0	0
Interest Income (expense), net	7 #	1	2	2	7	2	2	2	2	7	7
<i>Total other income (expense)</i>	6	1	2	2	7	2	2	2	2	7	7
Loss before provision for income taxes	(454) #	(1,660)	(173)	32	(262)	(85)	84	214	83	295	1,598
Provision for income taxes	(36) #	(332)	0	0	0	0	0	0	0	0	0
<b>Net loss</b>	<b>(417) #</b>	<b>(1,328)</b>	<b>(173)</b>	<b>32</b>	<b>(262)</b>	<b>(85)</b>	<b>84</b>	<b>214</b>	<b>83</b>	<b>295</b>	<b>1,598</b>
Diluted EPS	<b>(0.03) #</b>	<b>(0.08)</b>	<b>(0.00)</b>	<b>0.00</b>	<b>(0.01)</b>	<b>(0.01)</b>	<b>0.01</b>	<b>0.01</b>	<b>0.01</b>	<b>0.02</b>	<b>0.10</b>
Diluted share count	14,217 #	15,830	16,006	16,006	16,031	16,056	16,081	16,106	16,131	16,094	16,345

Operating Ratios	2008E				2009E				FY10E
	Q1A	Q2A	Q3A	Q4E	Q1E	Q2E	Q3E	Q4E	
	Mar-08	Jun-08	Sep-08	Dec-08	Mar-09	Jun-09	Sep-09	Dec-09	
<b>FY06A</b>	<b>10.6%</b>	<b>23.8%</b>	<b>36.0%</b>	<b>36.0%</b>	<b>33.3%</b>	<b>36.1%</b>	<b>37.0%</b>	<b>36.5%</b>	<b>37.0%</b>
Gross Margin	36.0%	139.1%	54.4%	33.6%	33.3%	36.1%	37.0%	36.5%	36.0%
General and administrative expenses	3.0%	-0.5%	61.3%	27.8%	30.1%	22.1%	18.6%	23.2%	22.7%
R&D Expense	61.3%	187.0%	-50.7%	4.1%	8.3%	5.9%	4.8%	5.8%	0.1%
Total Operating Expense	-46.0%	-130.5%	-50.7%	67.0%	42.0%	30.4%	25.4%	31.3%	28.7%
Operating Margin				-32.5%	-8.7%	5.7%	11.6%	5.2%	7.3%
Net Margin				-32.2%	-8.5%	5.8%	11.7%	5.3%	5.1%
<b>FY07A</b>	<b>12.2%</b>	<b>152.0%</b>	<b>261.0%</b>	<b>218.0%</b>	<b>86.3%</b>	<b>50.9%</b>	<b>55.3%</b>	<b>63.6%</b>	<b>60.9%</b>
Total Revenue	NM	NM	NM	NM	79.9%	62.3%	53.9%	80.9%	66.6%
Gross Profit	NM	NM	NM	NM	-50.1%	-514.4%	608.7%	-177.8%	-426.1%
Operating Income	NM	NM	NM	NM	-50.7%	-568.6%	575.1%	-180.8%	-212.6%
Net Income	NM	NM	NM	NM	-50.8%	-556.5%	570.9%	-180.3%	-212.1%
EPS as Reported (Diluted)	NM	NM	NM	NM					

Source: company reports and Merriman Curhan Ford estimates  
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