

SANGOMA TECHNOLOGIES CORPORATION
MANAGEMENT DISCUSSION AND ANALYSIS OF FINANCIAL
CONDITION AND RESULTS OF OPERATIONS
SECOND QUARTER FISCAL 2017 ENDED DECEMBER 31, 2016

February 6, 2017

INTRODUCTION

The Management Discussion and Analysis (“MD&A”) provides a detailed analysis of the financial condition and results of operations of Sangoma Technologies Corporation (hereinafter referred to as “Sangoma” or the “Company”). The MD&A compares the financial results for the fiscal second quarter of 2017 with those of the same quarter in the previous year. This MD&A should be read in conjunction with Sangoma’s audited annual consolidated financial statements and related notes for the year ended June 30, 2016 (“Financial Statements”) which are available at www.sedar.com. All amounts are in Canadian Dollars unless otherwise noted.

BASIS OF PRESENTATION

The Company reports in accordance with International Financial Reporting Standards (“IFRS”).

NON-IFRS MEASURES

This MD&A contains references to certain non-IFRS financial measures such as Operating Income and EBITDA. Non-IFRS financial measures are used by management to evaluate the performance of the Company and do not have any meaning prescribed by IFRS and therefore may not be comparable to similar measures presented by other reporting issuers. Non-IFRS financial measures used herein have been applied on a consistent basis. “Operating Income (Loss)” means gross margin less expenses before financing costs and one-time charges. “EBITDA” means earnings before interest, income taxes, depreciation, amortization and one-time charges. EBITDA is a measure used by many investors to compare issuers on the basis of their ability to generate cash from operations. We believe that Operating Income and EBITDA are useful supplemental information as they provide an indication of the results generated by the Company’s main business activities before taking into consideration how they are financed, taxed, depreciated or amortized. Investors are cautioned that non-IFRS measures, such as those presented herein, should not be construed as an alternative to net income or cash flow determined in accordance with IFRS.

FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements, including statements regarding the future success of our business, development strategies and future opportunities.

Forward-looking statements include, but are not limited to, statements concerning estimates of expected expenditures, expected future product development, expected future production, anticipated cash flows, and other statements which are not historical facts. When used in this document, the words such as “could”, “plan”, “estimate”, “expect”, “intend”, “may”, “potential”, “should” and similar expressions indicate forward-looking statements.

Although Sangoma believes that its expectations reflected in these forward-looking statements are reasonable, such statements involve risks and uncertainties and no assurance can be given that actual results will be consistent with these forward-looking statements. Forward-looking statements are based on the opinions and estimates of management at the date that the statements are made, and are subject to a variety of risks and uncertainties and other factors that could cause actual events or results to differ materially from those projected in forward-looking statements. Except as required by law, Sangoma undertakes no obligation to update forward-looking statements if circumstances or management’s estimates or opinions should change.

Readers are cautioned not to place undue reliance on forward-looking statements, as there can be no assurance that the plans, intentions or expectations upon which they are based will occur. By their nature, forward-looking statements involve numerous assumptions, known and unknown risks and uncertainties, both general and specific, that contribute to the possibility that the predictions, forecasts, projections and other events contemplated by the forward-looking statements will not occur. Although Sangoma believes that the expectations represented by such forward-looking statements are reasonable, there can be no assurance that such expectations will prove to be correct as these expectations are inherently subject to business, economic and competitive uncertainties. Some of the risks and other factors which could cause results to differ materially from those expressed in the forward-looking statements contained in the management's discussion and analysis include, but are not limited to, changes in exchange rate between the Canadian dollar and other currencies, changes in technology, changes in the business climate, changes in the regulatory environment, the decline in the importance of the PSTN (see glossary below), the cost and availability of parts used in manufacturing products, impairment of goodwill or intangible assets and new competitive pressures. The forward-looking statements contained in the management's discussion and analysis are expressly qualified by this cautionary statement.

DESCRIPTION OF THE BUSINESS

General (please also refer to the Glossary of Terms at the end of this document)

The communications landscape continues to grow in complexity, with more devices, networks, clouds, and systems needing to interoperate. Sangoma's portfolio of products enables service providers, carriers, enterprises, small and medium-sized businesses (SMBs), and original equipment manufacturers (OEMs) alike to leverage their existing infrastructure for maximum financial return, while still delivering the most advanced applications and services from the latest technologies available.

Sangoma's latest innovations and expanded product portfolio are intended to offer a comprehensive Unified Communications solution to large and small customers and include technology and appliances such as session border controllers (SBCs), IP-PBXs based on FreePBX, a range of IP-phones customized for one stop install and management, VoIP gateways, PBXact UCC service, SIP trunking service, fax-over-IP services, call tapping, call center software, and signaling gateways for enterprise, SMB, carrier, and OEM applications. Sangoma continues to invest and lead the market in VoIP-to-PSTN interface boards.

Session Border Controllers

Anytime two VoIP networks interconnect, issues of security and interoperability arise. SBCs can manage these issues, including provider-to-provider connections, provider-to-enterprise connections, and enterprise-to-enterprise connections. Sangoma's SBCs are available as hardware appliances, as software-only solutions running on a virtual machine in hosted environments, or as a hybrid of both. The hybrid solution is unique to Sangoma and provides all the flexibility expected from virtual machine capability coupled with the scalability that is found in hardware-based solutions.

IP-PBXs

A Private Branch Exchange (PBX) is an enterprise communication system. An IP-PBX is a VoIP-based PBX that uses Internet Protocol. Sangoma offers a feature rich IP-PBX called FreePBX, one of the most widely used software-based PBXs in the world. FreePBX is available free of charge as an open source software download, or in two commercial variants that come pre-loaded on a Sangoma telecom appliance. The first is the FreePBX phone system, which can be enhanced a la carte with the purchase of individual add-on commercial modules (such as call center builder, high-availability, phone configuration management, enhanced reporting, etc.). The second is Sangoma's PBXact UC system, which comes pre-packaged with add-on functionality, tighter release and revision control, and service contracts. Usage of FreePBX by customers also pulls through complementary products such as PSTN interface cards, VoIP gateways, or SBCs.

IP-Phones

Sangoma's recently launched range of IP-Phones are customized to seamlessly integrate with all FreePBX systems to provide zero touch installation, simplified system management and instant access to a wide range of features.

VOIP Gateways

VoIP gateways are needed any time voice traffic moves from a VoIP network to a traditional PSTN telephone network. As the traffic traverses these networks there are issues that need to be resolved regarding both the media (the sound of the caller's voice) and the signaling (the method used to control the media traveling over that connection).

Vega Enterprise Gateways are used by businesses that want to connect their traditional phone systems (PBX or key system) to a VoIP provider. These types of connections are referred to as SIP trunks, and Sangoma's gateways enable users to take advantage of the cost savings and flexibility of SIP trunks, without having to upgrade their entire phone system.

These same gateways can also be used to connect a newer IP-PBX to the PSTN. In addition to providing a backup to the service provided by their VoIP Provider, companies can use VoIP gateways for multi-site transitions from older phone systems to new IP-PBX phone systems.

VoIP Gateways are also needed to connect traditional telephones to an IP-PBX. For large companies, the cost of new IP phones can be higher than replacing the core system, so they keep the older phones and connect them to the new IP-PBX. This allows them to phase in the new phones over time without disrupting normal business operations. There may also be specialized telephones (elevator phones, door entry phones, ruggedized phones for use in hard industrial or outdoor conditions) for which there are no IP replacements. These phones can also be connected to the IP-PBX with a Vega gateway.

In a service provider or carrier network, much larger gateways perform these same tasks. In addition, there are signaling protocols that are only used when carrier networks communicate with other carrier networks that are not included in the enterprise product line. The NetBorder SS7 VoIP Gateway is a carrier-specific product that enables a VoIP carrier to connect their network to the SS7 network.

PBXact UCC Service

PBXact UCC service is a cloud based PBX service specifically designed to meet the needs of SMBs and small enterprise. PBXact UCC uses Sangoma IP phones and delivers simple online signup, unlimited US/Canada calling, number portability and VoIP security.

SIPStation

SIPStation is a hosted, SIP trunking service targeted to users of FreePBX systems. SIP trunking is fast becoming the technology of choice to interconnect an IP-PBX system to a telephone company (in this case an IP telephony service provider or ITSP). The main drivers are cost efficiencies (over fixed lines such as ISDN or analog lines from incumbent telcos) and newer UC features/transparency. Cost efficiencies are realized because SIP Trunking uses already-available broadband connections at customer premises. SIPStation is tightly integrated into the Sangoma FreePBX graphical user interface (GUI); and customers can purchase and enable the service directly from that GUI.

FoIP

Faxing remains an important communications tool. Yet VoIP networks are sometimes unable to

send faxes reliably because fax standards are based on very specific timing that can be interrupted in VoIP systems, especially where there is substantial latency. Sangoma's FoIP (Fax over Internet Protocol) service is a hosted service to remedy this problem. It features a telecom appliance with up to four analog connections for fax machines, and operates in concert with Sangoma's fax server data center to encrypt and package the fax communication to make it fail safe. This is particularly useful for small businesses that rely on fax communications but also for industries with challenging network conditions such as mining, oil rigs, ship-to-shore over satellite.

Call Center Software

Sangoma currently supports two different products used by outbound call centers for call progress analysis (CPA). The NetBorder Call Analyser is targeted at very large call centers and is usually delivered under an OEM arrangement with the company providing the call center solution. Lyra is a "lighter weight" version of the software that has been optimized to work with contact centers that are built on the Asterisk platform.

Sangoma's CPA is based on a proprietary artificial intelligence model that is currently considered to be the most accurate system available, with an accuracy of approximately 95%. CPA customers include many large businesses and Fortune 500 companies. CPA is sold largely through recommendations made by partners such as Genesys, a major supplier of call center applications. Work continues on streamlining the implementation of CPA, with the goal of simplifying the tasks performed by these partners. Sangoma is actively seeking new partners in the call center business to help market and implement the product.

Other Connectivity and Media Processing Products

Tapping Boards

Recording calls has long been a requirement for call-center training purposes, for validating over-the-phone transactions such as stock orders placed with a broker, and a variety of other scenarios. The Sangoma T116 is a specialized, high-density board that can be used as part of large call recording platforms.

Transcoding Boards and Gateways

One of the things that makes VoIP telephony different from traditional telephony is the way in which sound (media) is encoded for transmission. In the traditional telephony network, there is a universally agreed upon standard that has been in place for nearly 100 years. This means that the media can easily be moved across any number of networks or devices. However, there are a variety of methods that can be used to encode media for transmission over a VoIP Network. Transcoding boards and gateways are specially designed to translate media encoded by one method into another. This allows calls to pass between networks, even if they use different methods of encoding the media. Sangoma offers both board and appliance-based products to offer network providers the maximum flexibility when deploying a solution.

Multiplexers

Different standards are used to move information over the physical wires of a network. A multiplexer is a device that works at the physical layer of a network, and is used to translate these standards. For example, the Sangoma STM1Fiber multiplexer can consolidate up to 83 T1s running over copper wire into a single OC-3 fiber connection. Sangoma provides a variety of multiplexers for connecting different types of physical networks.

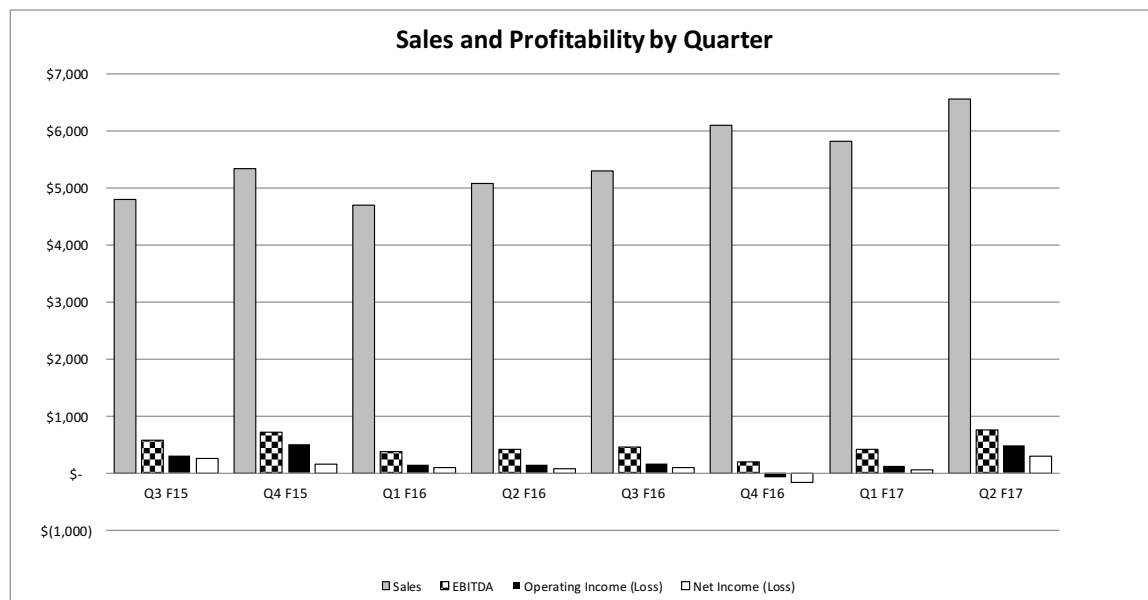
PSTN Interface Boards

This product category is the one responsible for Sangoma's initial rise in market leadership. Sangoma continues to invest in this area and has maintained a leadership position with the sixteen-span board, the highest density TDM interface board on the market. This board can manage up to 480 calls using a single expansion slot in a server. Sangoma also has a complete line of boards that can interface a VoIP system with nearly every kind of telephony network on earth, including digital PRI/PRI, analog and GSM (cellular networks).

The above boards are primarily used in PC-Based VoIP telecommunications systems that connect to the PSTN and perform a very similar task to VoIP gateways, but are installed inside the server rather than being stand-alone devices. By providing customers with the option of using a PSTN interface board or a VoIP gateway, Sangoma maximizes flexibility based on installation requirements – particularly when space and power are at a premium. They may also be used in harsh conditions that require ruggedized servers.

OVERALL PERFORMANCE

Financial



¹ Operating Income (Loss) before undernoted and EBITDA are metrics used by the Company to monitor its performance and the definitions may be found in the section non-IFRS measures above.

For the second quarter of fiscal 2017, sales were a record \$6.57 million, 29% higher than in the same quarter last year making this the eighth quarter in a row that Sangoma has grown significantly and consistently, over the same quarter in the prior year.

Gross profit was \$4.35 million for the second quarter, 19% above that of the same quarter last year, and gross margin was 66% of sales, slightly better than in the first quarter, and in line with our expectations.

Operating expenses were \$3.86 million for the second quarter, 9% higher than in the same quarter of fiscal 2016, but growing at a slower rate than revenue and gross profit.

EBITDA was \$0.76 million for second quarter of fiscal 2017, almost double the \$0.41 million earned in the same quarter last year. Operating income was \$0.49 million, three fold higher than in recent quarters.

Net income for the quarter ended December 31, 2016 was \$0.29 million (\$0.009 per share fully diluted), compared to net income of \$0.08 million (\$0.002 per share fully diluted) for the quarter ended December 31, 2015.

Sangoma finished the quarter with a cash balance of \$2.28 million having generated \$0.46 million from operations and spent \$0.55 million on an acquisition during the quarter. As of December 31, 2016 the company had healthy working capital of \$6.61 million.

Operational

Sangoma is a leading provider of hardware and software components that enable or enhance IP communications systems for both telecom and datacom applications. Enterprises, SMBs and carriers in more than 100 countries rely on Sangoma's technology as part of their mission-critical infrastructures. Through a worldwide network of distribution partners, Sangoma delivers high-quality products, some of which carry the industry's first lifetime warranty.

The Company has been a major player in the open source telephony ("OST") business for many years, is a respected contributor to open source telephony solutions, and contributes back to the OST community regularly. Sangoma has been involved in multiple OST projects (including two of the most common, Asterisk and Freeswitch) and, on January 1, 2015, extended its engagement through the acquisition of Schmooze Com Inc. This resulted in Sangoma taking over the management of the FreePBX project, which supports more than two million installs worldwide.

To protect its future, Sangoma has recognized the critical need to evolve the Company beyond its reliance on PSTN-based products. This started with an operational rebuild, the acquisition of VegaStream, an internal build out of the product portfolio, and competing in new market and customer segments such as SBCs. The acquisitions on January 1, 2015 have added a core PBX product and introduced Sangoma to the service business through SIPStation and FoIP offerings. Sangoma has added to its portfolio to provide full solutions through the March launch of Sangoma IP phones and more recently the launch of cloud PBX service.

Sangoma is now a stronger competitor in the larger, more typical telecom equipment market, which is not generally OST based. With its PSTN interface boards, Vega gateway products, SBCs, Free PBX, various Support Services and others, Sangoma now sells to carriers, service providers, enterprises, SMBs, and OEM customers with several third-party application providers using Sangoma products.

Innovation

Sangoma continues to invest in Research and Development (“R&D”) to develop new products and to improve existing offerings. New additions to the product portfolio over the last few years include:

- T3 Mux Appliance
- Version 4 of NetBorder SS7 Media Gateway
- Vega 50, 400 and 5000 series Gateways
- NetBorder Express Microsoft Lync Certification
- NetBorder SS7 VoIP Gateway Appliance
- W400 GSM Board
- Vega 100 and 200 Gateways
- NetBorder Transcoding Gateway
- NetBorder Lync Express Appliance
- Vega 400 Session Border Controller
- A116 16-Span Digital Telephony Interface Board
- B500 BRI Board
- STM1 Mux Appliance
- Call Progress Analysis for Asterisk Systems
- NetBorder SS7 Gateway Release 5.0
- Full line of Session Border Controllers
- T116 16-Span Tapping Board
- NetBorder VOIP Gateway
- Lync Express 2.0
- SBC 2.0
- Video Multipoint Control Unit (MCU)
- FreePBX
- SIP trunks for FreePBX users through SIPStation
- FoIP service
- Sangoma’s commercial IP-PBX range called PBXact
- IP-phones with instant connect to FreePBX and PBXact
- PBXact UCC Cloud PBX Service

Sales and Marketing

Over the last few years the Company has steadily increased its investment in, and focus on, sales. Sangoma has professional sales teams across all key geographic regions to identify and engage local distributors and resellers to address opportunities with larger customers such as carriers and OEMs. Sangoma continues to use a dual sales path to customers: direct sales to large customers (typically OEMs and carriers) and distribution to others.

Carriers are typically telcos, ISPs, ITSPs, wireless/mobile operators, and service providers who resell services using either their own networks or those of others. All of these organizations are potential customers for Sangoma.

OEM partners are companies that “design in” Sangoma products as a component of their solutions. OEM customers tend to be committed participants in their given markets, and have longer-term focus. It is important to reach these potential customers in the early days of any project to secure design wins and to have sales and marketing programs that will ensure close collaboration during product and sales development cycles that may last as long as three years.

In other cases, Sangoma utilizes an indirect distribution model to reach the full breadth of customers in markets where such partners have established relationships. For enterprise and SMBs, the Company has built a network of distributors and resellers. Distributors typically sell to resellers. These resellers then sell, install, and support end users. Using regional distributors and resellers supported by Sangoma’s sales and marketing efforts has proven very successful. The impact of lower margins from a two-tier distribution model is offset by the net new growth of sales that distributors bring to Sangoma, as well as the cost reduction of handling relatively small orders. Distribution channels require frequent attention to keep Sangoma as the premier supplier in a crowded product marketplace. Sangoma has implemented several incentive programs with its resellers and distributors and has developed a comprehensive set of channel promotion programs to incent and reward its channel partners for performance and behaviours that Sangoma believes will grow its revenues.

Sangoma continues to increase its focus on, and investment in, marketing. The Company has assembled corporate marketing programs to promote its brand and products more aggressively and to convey the message about Sangoma’s full solutions of connectivity products, PBX’s, Phones, and SIP trunks. Sangoma is now using various marketing techniques typical of technology firms to generate greater awareness of the Company and its new products. This includes participation in tradeshows, speaking at selected industry events, attending specialized seminars run by Sangoma’s distribution channel and other partners, investing in electronic marketing strategies (e.g. web presence, social media and blogging, online advertising, search engine campaigns, etc.), conducting lead generation campaigns, and creating thought leadership pieces.

RESULTS OF OPERATIONS

SUMMARY OF RESULTS FOR THE SECOND QUARTER OF FISCAL 2017

Sales

Sales for the quarter ended December 31, 2016 were a record \$6.57 million, up 29% from the \$5.08 million in the second quarter of fiscal 2016 ended December 31, 2015 and 13% higher than the \$5.82 million in the first quarter of fiscal 2017. Revenues were strong in this quarter across all product lines and Sangoma's goal to offer a complete Unified Communications (UC) solution accessible via on-premise or cloud based solutions is now clearly evident. Revenue has now exceeded the same quarter in the prior year for eight consecutive quarters.

Cost of Sales and Gross Margin

The cost of sales for the quarter ended December 31, 2016 was \$2.22 million compared to \$1.41 million for the quarter ended December 31, 2015. Gross profit for the second fiscal quarter of 2017 was \$4.35 million, 19% higher than the \$3.67 million realized in the second quarter of fiscal 2016. Gross margin for the second quarter ended December 31, 2016 was 66% of revenue, compared to 72% recorded in the same period of fiscal 2016. The lower gross margin between years reflects the product mix in particular quarters and also the introduction of phones to round out the portfolio, which are sold at somewhat lower margins than other products in Sangoma's product portfolio.

Operational expense

Under IFRS costs are allocated to the respective departments except for the impact of foreign exchange which can result in material swings between time periods.

Selling and Marketing

Selling and marketing expenses were \$1.16 million for the quarter ended December 31, 2016, 8% lower than for the same quarter last year (\$1.26 million). Sales and marketing expenditure is focused on leveraging the newly integrated portfolio of products that now includes phones and hosted services.

Research and Development

Certain development costs are capitalized each period and amortized on a straight-line basis over three years (see the Notes to the 2016 Annual Audited Consolidated Financial Statements available at www.sedar.com). The engineering expense incurred and the development costs amortized during the quarter ended December 31, 2016 were \$1.28 million, 7% higher than in the same quarter last year (\$1.20 million) reflecting the addition of technical resources in pre-sales engineering and customer support to manage the broader portfolio and the launch of our Cloud offerings.

General and Administration

General and Administration expenses were \$1.39 million for the quarter ended December 31, 2016 an increase of 14% over the same period ended December 31, 2015 (\$1.22 million). While the absolute increase appears high the rate of General and Administrative expense post acquisitions has remained relatively stable at around 23% of sales.

Foreign Exchange

For the quarter ended December 31, 2016, there was a foreign exchange loss of \$0.02 million compared to a \$0.16 million gain in the second quarter of fiscal 2016.

Total operational expense

Operating expense for the second quarter was \$3.86 million, a 9% increase over the same period last year but at less than 60% of revenue was lower in relative terms than that of the last few quarters. This is as planned and should deliver improved operating leverage as the rate of expense increase remains lower than the rate of sales growth.

Operating Income (before interest, tax and one-time acquisition expense)

Operating income for the quarter ended December 31, 2016 was \$0.49 million versus an operating income of \$0.14 million in the second fiscal quarter of 2016 ended December 21, 2015.

Net Income

Net Income for the quarter ended December 31, 2016 was \$0.29 million (\$0.009 per share fully diluted) compared to a net income of \$0.08 million (\$0.002 per share fully diluted) for the same quarter ended December 31, 2015.

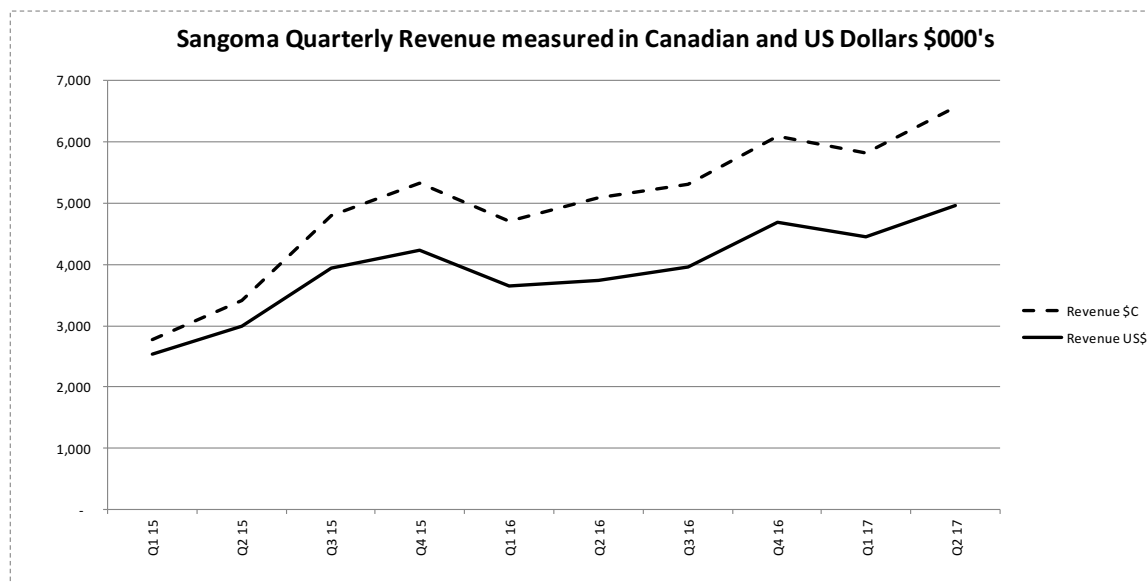
Earnings before Interest, Taxes, Depreciation, Impairment and Amortization (“EBITDA”)

EBITDA for the second quarter of fiscal 2017 ended December 31, 2016 was \$0.76 million considerably higher than the \$0.41 million recorded in the second quarter of fiscal 2016. As indicated above, growing revenue, stable gross margin percentage and expenses growing slower than revenue means that EBITDA for Sangoma is increasing as a ratio of sales, and Sangoma believes this trend can be continued.

\$C Thousands	Three months ended	
	Dec 31, 2016	Dec 31, 2015
Net Income	290	78
Tax	178	35
Interest	0	0
Interest on Operating Line	23	29
Stock Based Compensation	78	46
Amortization of Property, Plant and Equipment	29	30
Amortization of Intangibles	160	190
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EBITDA	758	408

The above table shows the reconciliation of net income and total comprehensive income to EBITDA which is a metric used by the Company to monitor its performance and the definition may be found in the section non-IFRS measures above.

QUARTERLY RESULTS TRENDS



When measured in source currency (predominantly US\$), sales in the quarter ended December 31, 2016 were 33% higher than those of the same quarter in the preceding year. Sangoma's quarterly revenue has exceeded the same period in each of the last eight quarters.

SALES AND NET INCOME BY QUARTER

C\$ thousands	Third quarter 2014-2015	Fourth quarter 2014-2015	First quarter 2015-2016	Second quarter 2015-2016	Third quarter 2015-2016	Fourth quarter 2015-2016	First quarter 2016-2017	Second quarter 2016-2017
Sales	\$ 4,793	\$ 5,337	\$ 4,712	\$ 5,082	\$ 5,301	\$ 6,099	\$ 5,820	\$ 6,570
Gross Margin	\$ 3,407	\$ 3,572	\$ 3,353	\$ 3,669	\$ 3,634	\$ 3,752	\$ 3,765	\$ 4,350
Operating Expense	\$ 3,099	\$ 3,070	\$ 3,203	\$ 3,527	\$ 3,459	\$ 3,829	\$ 3,635	\$ 3,859
Operating Income (Loss)	\$ 308	\$ 502	\$ 150	\$ 142	\$ 175	\$ (77)	\$ 130	\$ 492
Net Income (Loss)	\$ 248	\$ 147	\$ 88	\$ 78	\$ 104	\$ (156)	\$ 64	\$ 290
Net Earnings per Share								
Non-diluted basis	\$0.008	\$0.005	\$0.003	\$0.002	\$0.003	(\$0.005)	\$ 0.002	\$ 0.009
Fully diluted basis	\$0.008	\$0.005	\$0.003	\$0.002	\$0.003	(\$0.005)	\$ 0.002	\$ 0.009
EBITDA	\$ 573	\$ 726	\$ 384	\$ 408	\$ 450	\$ 191	\$ 423	\$ 758

¹ Operating Income (Loss) before undernoted is a metric used by the Company to monitor its performance and the definition may be found in the section non-IFRS measures above.

SUMMARY OF RESULTS FOR THE YEAR TO DATE FISCAL 2017

Sales

Sales for the six months ended December 31, 2016 were \$12.39 million, up 27% from the six months ended December 31, 2015 (\$9.79 million). Compared to fiscal 2016, Sangoma is seeing growth from new products. The work done over the last few years to round out the product line and deliver an end to end Unified Communications solution to multiple customer segments is continuing to deliver consistent growth.

Cost of Sales and Gross Margin

The cost of sales for the six months ended December 31, 2016 was \$4.27 million compared to \$2.77 million for the six months ended December 31, 2015. Gross margin for the six months ended December 31, 2016 was 66% of revenue, 6% lower than that recorded in the same period of fiscal 2016. Gross profit for the six months ended December 31, 2016 was \$8.12 million, 16% higher than the \$7.02 million realized in the same six-month period of fiscal 2016. Gross margin % remains in the mid 60% range as the growth in some lower margin products is offset by continuing improvement in software/services, which have higher margin. Sangoma expects this trend should continue going forward.

Operational expense

Under IFRS costs are allocated to the respective departments except for the impact of foreign exchange which can result in material swings between time periods.

Selling and Marketing

Selling and marketing expenses were \$2.24 million for the six months ended December 31, 2016, 6% lower than for the period last year (\$2.38 million). Investment in sales and marketing is focused on leveraging the newly integrated portfolio of products and continuing to launch new products.

Research and Development

Certain development costs are capitalized each period and amortized on a straight-line basis over three years (see the Notes to the 2016 Annual Audited Consolidated Financial Statements available at www.sedar.com). The engineering expense incurred and the development costs amortized during the six months ended December 31, 2016 were \$2.48 million, 9% higher than in the same period last year (\$2.27 million) reflecting the addition of technical resources in pre-sales engineering customer support and technical staff from the two acquired companies.

General and Administration

General and Administration expenses were \$2.74 million for the six months ended December 31, 2016 an increase of 19% over the same period ended December 31, 2015 (\$2.30 million). The increase is from the addition of staff and other miscellaneous operating expense in the new businesses and the amortization of the Intangible Assets acquired.

Foreign Exchange

For the six months ended December 31, 2016, there was a foreign exchange loss of \$0.04 million. In the first six months of fiscal 2016 there was a foreign exchange gain of \$0.23 million.

Total operational expense

Operating expense for the first six months of fiscal 2016 was \$7.49 million, an 11% increase over the same period last year (\$6.73 million). The rate of increase of operational expense in fiscal 2017 has been held below the rate of revenue and gross profit growth such that the ratio of expense to revenue has now declined from 69% as of December 31, 2015 to 61% as of December 31, 2016.

Operating Income (before interest, taxes, financing and one-time acquisition expense)

Operating income for the six months ended December 31, 2016 was \$0.62 million versus an operating income of \$0.29 million in the same period ended December 31, 2015. The doubling of operating income reflects the operational leverage now being realized as the rate of revenue growth has exceeded the rate of spending growth.

Net Income

Net income for the six months ended December 31, 2016 was \$0.35 million (\$0.011 per share fully diluted) compared to a net income of \$0.17 million (\$0.005 per share fully diluted) for the same period ended December 31, 2015.

Earnings before Interest, Taxes, Depreciation, Impairment and Amortization (“EBITDA”)

EBITDA for the six months ended December 31, 2016 was \$1.18 million versus \$0.79 million for the same period of fiscal 2016. This improvement results from the increase in revenue versus fiscal 2016 and from the trend described above in which expenses grow more slowly than revenue. The improving operating leverage means that Sangoma is generating more EBITDA for each dollar of revenue, as well as benefiting from the revenue growth itself.

\$C Thousands	Six months ended	
	Dec 31, 2016	Dec 31, 2015
Net Income	354	166
Tax	220	71
Interest	0	(2)
Interest on Operating Line	48	56
Stock Based Compensation	149	66
Amortization of Property, Plant and Equipment	64	59
Amortization of Intangibles	346	376
	<hr/>	<hr/>
EBITDA	1,181	792

The above table shows the reconciliation of net income and total comprehensive income to EBITDA which is a metric used by the Company to monitor its performance and the definition may be found in the section non-IFRS measures above.

LIQUIDITY

As of December 31, 2016 Sangoma had current assets of \$10.86 million and current liabilities of \$4.66 million, resulting in working capital of \$6.20 million, as compared to \$6.48 million on June 30, 2016. For the second quarter of fiscal 2017 ended December 31, 2016 the company generated positive cash flow from operations of \$0.46 million, spent \$0.55 million on the initial consideration for an acquisition and closed with cash of \$2.28 million as compared to \$2.09 million as at June 30, 2016.

Accounts Receivable of \$3.31 million on December 31, 2016 were \$0.9 million lower than for June 30, 2016 and \$1.45 million lower than at the same time as last year. The combination of growing revenue and lower accounts receivable is a further indication of the new business model working. On a relative basis the 45 days of receivables as at December 31, 2016 is almost one half of the 84 days as at December 31, 2015. The \$0.80 million of receivables over 90 days is up slightly this quarter but is mostly tied to longer term projects of which \$0.27 million was received in the first week of January 2017.

Inventories were \$4.46 million on December 31, 2016, \$0.57 million higher than for June 30, 2016. As had been previously shared Sangoma expected inventories to grow following the introduction of phones and the general growth in new products for which the supply chain reaches back into Asia. There has been no change in our assessment of excess or obsolete inventory as the growth is all in products with growing demand.

There are no existing or anticipated defaults or arrears on lease payments or interest payments and Sangoma is in full compliance with all debt covenants. Management of the Company believes that the current working capital and expected funds generated from operations will be sufficient to meet the operating and planned capital expenditures of the Company for the foreseeable future and could allow the company to commence paying down of the operating line of credit.

CAPITAL RESOURCES

There are no commitments for capital expenditures at this time.

OFF-BALANCE SHEET ARRANGEMENTS

There are no off-balance sheet arrangements that have, or are reasonably likely to have, a current or future effect on the results of operations or financial condition of Sangoma.

RELATED PARTY TRANSACTIONS

Except as disclosed, the Company is not party to any material transactions with related parties. The Chairman of the Board of Directors, who is also a significant shareholder of the Company, has a contract through Entropy Control Ltd. to provide certain services to Sangoma including input to the preparation of the Company's Scientific Research and Experimental Development tax claim.

PROPOSED TRANSACTIONS

There are no proposed asset or business acquisitions as at the date of this MD&A.

FINANCIAL INSTRUMENTS AND OTHER INSTRUMENTS

Sangoma has determined the estimated fair value of its financial assets and liabilities based on generally accepted valuation methods.

Short-term financial instruments

Cash and equivalents, trade receivables, sales tax receivables, investment tax credits receivable, accounts payable and accrued liabilities and term loan are short-term financial instruments whose fair value approximates their carrying amount on the balance sheet due to their near-term maturities. On December 30, 2014, Sangoma established an operating line of credit for up to \$2.5 million to satisfy any short term cash requirements. As of December 31, 2016, \$1.34 million of this had been drawn down.

OUTSTANDING SHARE DATA

As of February 6, 2017 there were 32,479,809 issued and outstanding common shares of Sangoma, the same as on December 31, 2015. Also as of February 6, 2017 Sangoma has outstanding option grants to acquire 5,969,160 common shares.

SIGNIFICANT EVENTS

None

POST REPORTING EVENTS

Subsequent to December 31, 2016, the Company held its Special and Annual Meeting during which time the following actions were ratified by shareholders:

- (i) an amendment to the Company's stock options plan to increase the amount of shares reserved and set aside for issuance from 5,542,160 to 6,199,160. Following the approval of the Plan increase the 450,000 options conditionally granted on June 22, 2016 were issued.
- (ii) the introduction of the shareholder rights plan and the adoption of the advance notice by-law that were initiated by the Board of Directors on November 25, 2016.

ADDITIONAL INFORMATION

Additional information relating to the Company is filed electronically on SEDAR at www.sedar.com.

GLOSSARY OF TERMS

Analog

Analog telephony is the telephone system that dates back to the original experiments by Alexander Graham Bell. The voice signal is picked up by a microphone and transmitted to the central office. Voice signals from the central office consist of voltages that drive a headset to produce sound. Analog means that the voice pressure signals are represented by voltages levels on the line.

API

Application Program Interface: An API is a purpose-built interface that allows fourth party software to interact with a particular application. A typical API is the user interface for Windows that allow programmers to write programs for Windows that use all its built-in utilities. APIs do not depend on revealing source code, in general. They are usually well documented and include sample programs that make development easy.

Codec

In the telephony context a codec is a mechanism of digitally encoding voice. On the PSTN a voice channel takes up 64kbps in a codec standard called G.711. Cell phones use a codec called GSM that compress the voice further so that a GSM call consumes about 24kbps. Other compressed codecs are used in VoIP to conserve bandwidth. These include standards such as G.729, G.723. Most audio codecs are lossy, in that some of the voice quality is degraded by the compression. On the other hand, as bandwidth becomes cheaper, VoIP allows one to use other codecs that in fact use more bandwidth than the PSTN, the so-called broadband codecs that have DVD-like voice quality.

Digital telephony

In the modern PSTN only the “last mile” line to the customer is still analog, all other internal parts of the network are digital. Digital in this case means that at the central office the analog signal from the subscriber’s telephone is sampled digitally, converting the line voltages to a series of numbers that can be easily transmitted error free over long distances. See T1, E1 below.

Gateway

In the telephony context this is typically a separate unit with its own case and power supply that provides VoIP-to-PSTN services for a VoIP network. Almost all gateway devices use SIP interfaces to the VoIP system over Ethernet and have analog or digital telephony interfaces that connect to the PSTN. VoIP gateways are available from many manufacturers including Audiocodes, Cisco, Grandstream, Patton Electronics and many others.

ISDN

Integrated Services Digital Network (“ISDN”) is a set of communications standards for simultaneous digital transmission of voice, video, data, and other network services over the traditional circuits of the public switched telephone network. Of the many variations of ISDN, Sangoma supports BRI (Basic Rate Interface) which is essentially an all-digital replacement for ordinary analog lines and PRI (Primary Rate Interface) which is used over T1 and E1 lines. BRI is very popular outside of North America. PRI is used worldwide.

IP

The Internet Protocol (“IP”) is the primary protocol in the internet layer of the Internet protocol suite, and delivers data packets from the source host to the destination host solely based on the IP address.

ISP

Internet Service Provider

ITSP

Internet Telephony Service Provider who offer telecommunications service including voice over internet type connections.

IVR

Interactive Voice Response: IVR systems use the phone to navigate a menu, for example those used by banks to allow access to customer’s account information. IVR systems have typically been driven by dial tones as the buttons on your phone are pressed, but increasingly they are using voice recognition for navigation.

Open Source

Open Source software is distributed free subject to certain conditions. Open Source licenses usually stipulate that source code must always be distributed or made available, and any improvements in the code have to be donated back to the community. It is possible to have dual licensing: Open Source to the community and also a closed, commercial license of the same or similar software.

NetBorder

This is the trade name of a Sangoma SIP to PSTN gateway product. It includes several other functions in addition to the PSTN gateway function. The mass marketed version is known as NetBorder Express or NBE.

PBX

Private branch exchange. A PBX is a premises based device to deliver calls from the PSTN or VOIP network to phones in a single or multiple locations.

PSTN

Public Switched Telephone Network: This is the standard telephone network that has been in operation for many decades. A telephone or FAX or PBX or other telephony device is generally connected to an analog line at a wall plug, which is connected by “last mile” cabling to the central office. The analog signal from the device is converted to a digital signal at the Telco central office and is multiplexed, 24 simultaneous voice channels per line (in North America) onto a T1 for onward transmission. At the other end of the line the digital channel is reconverted to analog for transmission over the “last mile” to the receiving phone or other device.

SBC

A Session Border Controller (“SBC”) is a device deployed in Voice over Internet Protocol (“VoIP”) networks to exert control over the signaling and usually also the media streams involved in setting up, conducting, and tearing down telephone calls or other interactive media communications. SBCs are deployed as demarcation points between enterprises and service providers and between service provider networks.

Signalling

Call setup and tear down is remarkably complicated, involving such things as responding to the different tones as well as generating them, caller identification and handling the different features like hook-flash and voicemail properly. There are different signalling mechanisms for different types of circuits. Analog circuits use tones such as out-of-order, busy, ringing as well as the dialling tones. T1 lines often use a data protocol called ISDN PRI, where packets of control data are exchanged on a separate data channel. ISDN PRI is a simplification of the general signalling protocol used internally by the telecommunications networks known as SS7. In all cases signalling has to be exactly compatible with what the Telco expects, so interoperability and standards are important.

SIP

Session Initiation Protocol: SIP is the emerging standard signalling protocol for VoIP, though it has much broader applications. SIP is responsible for setting up and teardown of two party and multiparty calls, as well as a host of management features. To a great and increasing extent, VoIP calls are SIP based. The term SIP Trunk is used to describe the provision of a SIP line to an end customer.

T1, E1

A T1 line is a circuit that carries 24 digital telephone calls simultaneously. At higher densities, 28 T1s are aggregated into a T3 line carrying 672 calls. Larger offices can also connect to the central office via T1 directly, so as to have only one circuit for up to 24 calls. T1 is standard in North America and Japan while E1 is the standard in the rest of the world. E1 carries 30 channels of digitized voice per line.

TDM

Time Division Multiplexing (“TDM”) is used in circuit switched networks to increase the number of calls carried simultaneously on any one circuit and formed the basis for the digital telephony networks.

Unified Communications

Unified communications is a concept in which voice, email, messaging, video and any other type of communication are all considered forms of data that can be combined, manipulated and used in intelligent applications in a seamless way.

VoIP

Voice over IP: The transfer of voice traffic over the Internet Protocol. IP is used universally for all networking including local area networks and private networks, not just the Internet. So VoIP is not necessarily voice over the Internet, but voice over general data networks.