

***SANGOMA TECHNOLOGIES CORPORATION***  
***MANAGEMENT DISCUSSION AND ANALYSIS OF FINANCIAL***  
***CONDITION AND RESULTS OF OPERATIONS***  
***THIRD QUARTER FISCAL 2018 ENDED MARCH 31, 2018***

May 15, 2018

## **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 third quarter of 2018 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, 2017 (“Financial Statements”) which are available at [www.sedar.com](http://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, EBITDA and Adjusted Cash Flow. 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 profit 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. “Adjusted Cash Flow” means cash flow from operations as defined by IFRS less the capitalized development costs that Sangoma incurred during the period. We believe that Operating Income, EBITDA and Adjusted Cash Flow 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), impairment of goodwill 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)*

Sangoma's portfolio of products deliver complete, Unified Communications (UC) Solutions. As 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 product portfolio includes a complete line of UC and PBX platforms, IP-Phones and UC Communicators, Cloud-based Services and Network Interconnection Products.

Sangoma's latest innovations and expanded product portfolio include technology and appliances such as IP-PBXs based on FreePBX and PBXact, a range of IP-Phones and integration tools to enable automated configuration and management, a Unified Communication Server and Client with Zulu UC, Session Border controllers (SBCs) to provide VoIP Security, Network bridging and fail-safe VoIP gateways, Hosted IP-PBX service with PBXact Cloud, SIP trunking service with SIPStation, fax-over-IP service with FaxStation and signalling gateways for enterprise, SMB, carrier, and OEM applications. Sangoma continues to invest and lead the market in VoIP-to-PSTN interface boards.

### ***Unified Communications and PBX platforms***

A Private Branch Exchange (PBX) is an enterprise communication system. An IP-PBX is a VoIP-based PBX that uses Internet Protocol. Sangoma offers feature rich FreePBX and PBXact, the most widely used software-based PBXs in the world. FreePBX is available free of charge as an open source software download, or in three commercial variants. The first is the FreePBX phone system pre-installed on a telecom appliance, 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 systems, which comes pre-packaged with add-on functionality, tighter release and revision control, and service contracts. The third one is PBXact SaaS, which offers flexible virtualization and licensing for OEMs and Service providers to run their own hosted UC/PBX services. Usage of FreePBX and PBXact by customers also pulls through complementary products such as IP-phones, PSTN interface cards, VoIP gateways, or SBCs.

### ***IP-Phones and UC Communicators***

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

Sangoma has also recently launched Zulu UC, a set of server, desktop and smartphone software integrated with FreePBX and PBXact that delivers unified communications features (presence, contacts, chat, calling, screen sharing, audio and video conferencing, etc.) from a single application)

## ***Cloud-Based Services***

### **PBXact Cloud**

PBXact Cloud service is a cloud based PBX service specifically designed to meet the needs of SMBs and small enterprise. PBXact Cloud 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 and PBXact 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 end to end 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.

### **Fax over IP (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.

## ***Network Interconnection Products***

### **Session Border Controllers (SBCs)**

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.

Sangoma's SBCs have interoperability certifications for Microsoft Skype for Business and Broadsoft (now part of Cisco), as well as hundreds of installations in other networks along with such vendors as Telefonica, BT, ATT, Verizon, Genesys Call Centers, Cisco Call Manager, Avaya Call Manager, etc.

## **Customer Premise 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 Series 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 addition to the Vega Series, Sangoma markets the Dialogic DMG series of Enterprise gateways. The DMG series provides very specific features for the enterprise: Value Added Services Integration to a PBX such as speech recognition enabled IVRs and high-speed v.34 media processing for integration with IP Fax Server technologies.

Sangoma's Vega Gateways hold certifications for Microsoft Skype for Business, Cisco Call Manager and Broadsoft, as well as hundreds of installations in other networks alongside Genesys Call Centers, Avaya DevConnect, ATT, Verizon, Telefonica, BT, Orange, DT, etc.

## **Carrier and Core VoIP Gateways**

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 for up to 960 channels.

The NetBorder SS7 gateways hold certifications and proven interoperability with Orange, BT, MTN, TATA, Telefonica, Telmex, MTT, etc.

In addition to the NetBorder product family, Sangoma markets the Dialogic IMG2020 Gateways. The Dialogic IMG2020 gateways perform similar functions as the NetBorder family with higher port densities – from 1 unit with support for 2016 channels and the ability to pool 6 units for over 12,000 ports. The IMG2020 also comes with a management system to configure, monitor, update systems from a central location.

## **PSTN Interface Boards**

This product category labelled the A-Series and the B-Series 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 ISDN PRI and BRI, and analog FXO / FXS.

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.

In addition to the A and B series, Sangoma has recently added the Dialogic Media and Network Interface product line which consist in the JCT, DNI, CG and Diva Series. These boards differ from the traditional A or B series boards in that they come with high end DSP media processing on board and with extensive programmable interfaces (APIs) for developers and integrators to design advanced telecom applications: IoT and modem banks, speech recognition systems, IVRs, call centers, et.c

## **Tapping Boards**

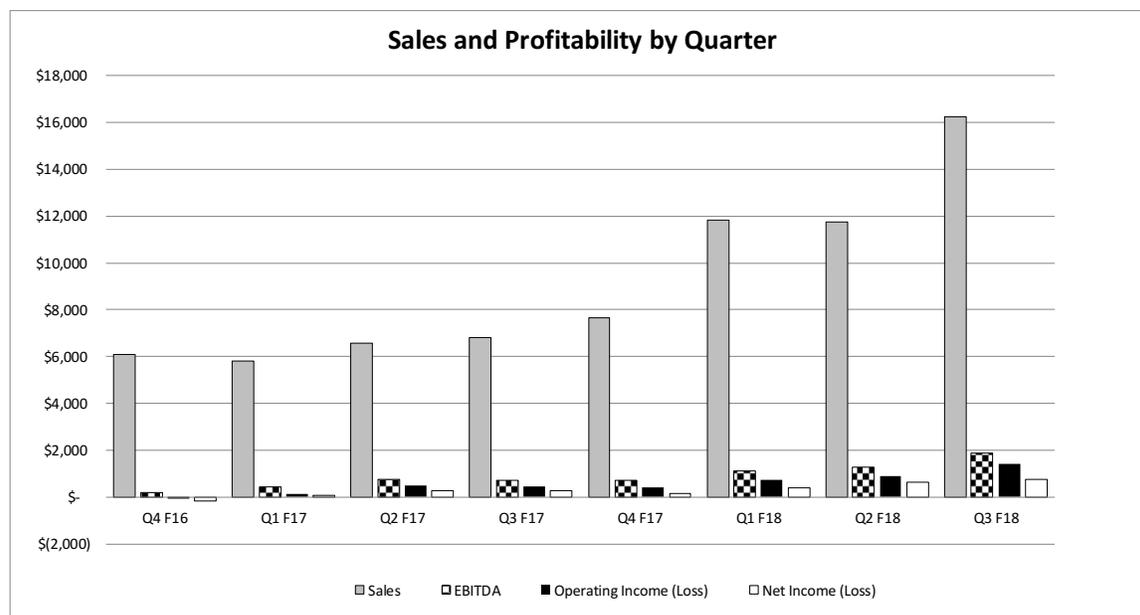
Recording calls has long been a requirement for call-center training purposes, for validating over-the-phone transactions such as stock orders placed with a broker, and a variety of other scenarios. The Sangoma T116 is a specialized, high-density board that can be used as part of large call recording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

## **Transcoding Boards**

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.

# OVERALL PERFORMANCE

## Financial



<sup>1</sup> Operating Income (Loss) 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 third quarter of fiscal 2018, sales were \$16.24 million, 138% more than in the same quarter last year and the thirteenth quarter in row of higher revenue versus the prior year.

Gross profit of \$8.90 million for the third quarter was double that of the third quarter of fiscal 2017, with gross margin percent at 55% of sales reflecting the addition of the newly acquired customer sales.

Operating expenses were \$7.56 million in the third quarter, up 88% from the same quarter in fiscal 2017, reflecting the addition of the two acquisitions and their associated staffs.

EBITDA was \$1.90 million for the quarter ended March 31, 2018 up 160% from the \$0.73 million in the same quarter of fiscal 2017 and at over 10% of revenue, was above our fiscal 2018 target.

Sangoma generated almost \$2 million in cash from operations in the quarter, boosting an already healthy balance sheet that was also strengthened by the approximately \$12 million from the recent private placement. The company finished the quarter with a cash balance of \$14.03 million and working capital of \$16.40 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 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 to compete in new market and customer segments such as SBCs, the addition of a core PBX product and introduction of cloud services with SIPStation, FoIP and cloud PBX offerings together with a range of IP phones.

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, IP phones, 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.

In the first quarter of fiscal 2018, Sangoma acquired all of the membership interests in VoIP Supply providing Sangoma with an industry leading on-line presence, a large customer base to cross sell into, cloud PBX client experience, and enhanced scale.

In the third quarter of fiscal 2018, Sangoma acquired the assets of Dialogic CCD (Converged Communications Division) adding new products and revenues, strong new customers and channels relationships, improved supply chain and over 40 key experienced individuals in sales, support, operations and R&D.

## **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
- Zulu softphone client

## **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.

VoIP Supply LLC adds new unique marketing and sales strength to Sangoma, including an efficient ecommerce transaction business, backed by a professional inside sales organization, and tailored marketing programs to attract and drive traffic to the website.

# **RESULTS OF OPERATIONS**

## **SUMMARY OF RESULTS FOR THE THIRD QUARTER OF FISCAL 2018**

### **Sales**

Sales for the quarter ended March 31, 2018 were \$16.24 million, up 138% from the \$6.81 million in the third quarter of fiscal 2017 ended March 31, 2017. The increase in sales came from the intrinsic product sales growth at Sangoma, the compounding of services revenue, the addition of VoIP Supply LLC sales from July of 2017 and the incorporation of the CCD business acquired on January 9 of this year from Dialogic.

### **Cost of Sales and Gross Margin**

The cost of sales for the quarter ended March 31, 2018 was \$7.27 million compared to \$2.33 million for the quarter ended March 31, 2017. Gross profit for the third fiscal quarter of 2018 was \$8.97 million, double the \$4.45 million realized in the third quarter of fiscal 2017. Gross margin for the third quarter was 55% of revenue, up 4% from last quarter as a result of the CCD revenue having a higher margin, but down from margins in the sixty-percent range during fiscal 2017 due to general pricing pressures in the marketplace, regional economies around the globe requiring localized pricing, Sangoma's expanded product mix that includes the successful introduction of products that have inherently lower margin, and the addition of VoIP Supply LLC which comes with lower gross margin percentage but with lower operating expense percentage as well.

### **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 \$2.19 million for the quarter ended March 31, 2018, 63% higher than for the same quarter last year (\$1.34 million). The higher absolute spend reflects the impact of the addition of the VoIP Supply LLC team and the staff acquired from Dialogic in January but as a percentage of revenue selling and marketing expense for fiscal 2018 are lower than in fiscal 2017.

### **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 2017 Annual Audited Consolidated Financial Statements available at [www.sedar.com](http://www.sedar.com)). The engineering expense incurred and the development costs amortized during the quarter ended March 31, 2018 were \$2.42 million, 86% higher than in the same quarter last year (\$1.30 million) following the addition of the team acquired from Dialogic.

### **General and Administration**

General and Administration expenses were \$2.87 million for the quarter ended March 31, 2018 an increase of 104% over the same period ended March 31, 2017 (\$1.41 million). The higher spend primarily results from the addition of the VoIP Supply LLC team and staff transitioned from Dialogic together with additional charges associated with intangible amortization post the two acquisitions. While the absolute dollar spending is higher compared to fiscal 2017 the general and administration expenses comprise a lower percentage of total sales.

### Foreign Exchange

For the quarter ended March 31, 2018, there was a foreign exchange loss of \$0.08 million compared to a \$0.03 million gain in the third quarter of fiscal 2017.

### Total operational expense

Operating expense for the third quarter was \$7.56 million, an 88% increase over the same period last year (\$4.03 million), reflecting continuing investment to drive Sangoma's top line growth and the additional costs resulting from the incorporation of the VoIP Supply LLC and CCD teams.

### **Business acquisition costs**

In the third quarter of fiscal 2018 Sangoma recorded \$0.28 million of costs directly associated with the legal, financing and closing of the acquisition of a division of Dialogic on January 9, 2018. This is expected to be close to the final total and the specifics of the transaction and associated costs are detailed in the third quarter financial statements.

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

Operating profit for the quarter ended March 31, 2018 was \$1.41 million versus an operating income of \$0.45 million in the third fiscal quarter of 2017.

### **Net Income**

Net Income for the quarter ended March 31, 2018 was \$0.75 million (\$0.015 per share fully diluted) compared to a net income of \$0.27 million (\$0.008 per share fully diluted) for the equivalent quarter ended March 31, 2017.

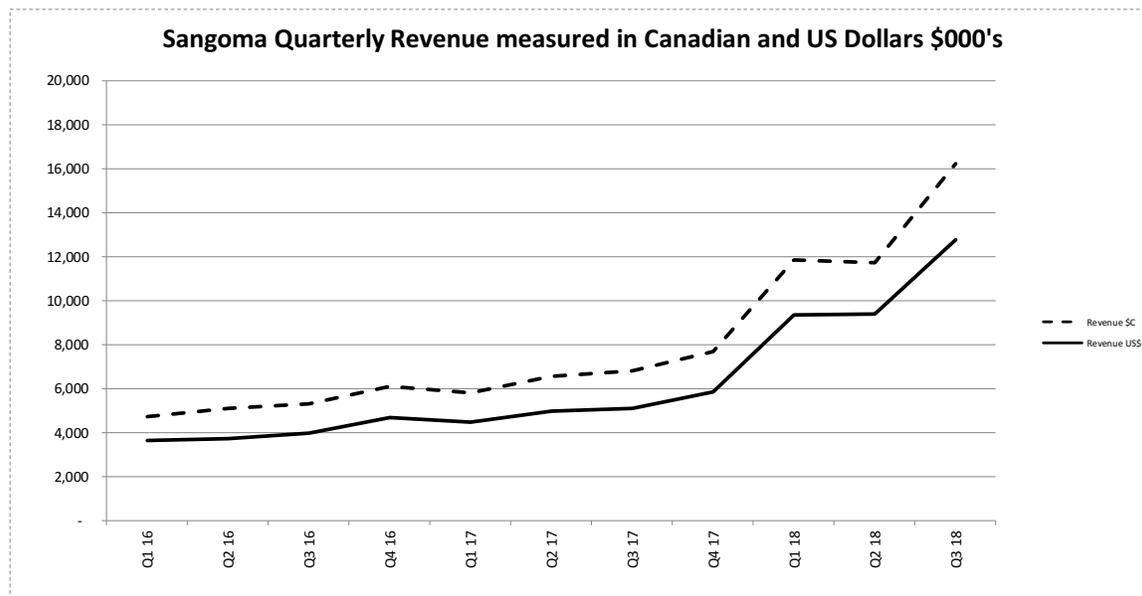
### **EBITDA (Earnings before Interest, Depreciation, Amortization and One Time Items)**

EBITDA in the third quarter was 16.1% of sales, as derived below.

\$C Thousands	Three months ended	
	Mar 31, 2018	Mar 31, 2017
Net Income	750	281
Tax	295	145
Interest	-1	-
Interest on Operating Line	86	27
Stock Based Compensation	62	39
Amortization of Property, Plant and Equipment	84	30
Amortization of Intangibles	337	207
One time acquisition related expense	282	-
EBITDA	1,895	729
% of revenue	11.7%	10.7%

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 March 31, 2018 were 36% higher than in the second quarter of fiscal 2018 and 150% higher than in the same quarter of fiscal 2017. Sangoma's quarterly revenue has now exceeded the same period in the prior year for each of the last thirteen quarters.

## SALES AND NET INCOME BY QUARTER

C\$ thousands	Fourth quarter 2015-2016	First quarter 2016-2017	Second quarter 2016-2017	Third quarter 2016-2017	Fourth quarter 2016-2017	First quarter 2017-2018	Second quarter 2017-2018	Third quarter 2017-2018
Sales	\$ 6,099	\$ 5,820	\$ 6,570	\$ 6,812	\$ 7,678	\$ 11,846	\$ 11,736	\$ 16,244
Gross Margin	\$ 3,752	\$ 3,765	\$ 4,350	\$ 4,478	\$ 4,933	\$ 6,120	\$ 5,991	\$ 8,970
Operating Expense	\$ 3,829	\$ 3,635	\$ 3,859	\$ 4,025	\$ 4,519	\$ 5,374	\$ 5,083	\$ 7,558
Operating Income (Loss)	\$ (77)	\$ 130	\$ 492	\$ 453	\$ 414	\$ 746	\$ 908	\$ 1,412
Net Income (Loss)	\$ (156)	\$ 64	\$ 290	\$ 281	\$ 166	\$ 390	\$ 614	\$ 750
Net Earnings per Share								
Non-diluted basis	(\$0.005)	\$0.002	\$0.009	\$0.009	\$0.005	\$ 0.012	\$ 0.018	\$ 0.016
Fully diluted basis	(\$0.005)	\$0.002	\$0.009	\$0.008	\$0.005	\$ 0.011	\$ 0.017	\$ 0.015
EBITDA	\$ 191	\$ 423	\$ 758	\$ 729	\$ 702	\$ 1,102	\$ 1,274	\$ 1,895

<sup>1</sup> Operating Income (Loss) and EBITDA are metrics 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 YEAR TO DATE FISCAL 2018**

### **Sales**

Sales for the first nine months of fiscal 2018 ended March 31, 2018 were \$39.82 million, 107% up from the \$19.20 million in the first nine months of fiscal 2017 ended March 31, 2017 fuelled by a mixture of intrinsic growth at Sangoma (helped by a single one-time large order in the first quarter), the compounding services revenue, the addition of VoIP Supply LLC and the contribution of sales from CCD purchased in January.

### **Cost of Sales and Gross Margin**

The cost of sales for the first nine months of fiscal 2018 ended March 31, 2018 was \$18.74 million compared to \$6.61 million for first nine months of fiscal 2017 ended March 31, 2017. Gross profit for the first nine months of fiscal 2018 was \$21.08 million, 67% higher than the \$12.59 million realized in the first nine months of fiscal 2017. Gross margin for the nine months to date was 53% of revenue, down from margins in the sixty-percent range in fiscal 2017 primarily due to general pricing pressures in the marketplace, regional economies around the globe requiring localized pricing, Sangoma's expanded product mix that includes the successful introduction of products that have inherently lower margin, the addition of VoIP Supply LLC which comes with lower gross margin percentage but with lower operating expense percentage as well partially offset by higher margins in the most recently acquired division from Dialogic.

### **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 \$5.64 million for the first nine months of fiscal 2018 ended March 31, 2018, 58% higher than for the same period last year (\$3.58 million).

### 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 2017 Annual Audited Consolidated Financial Statements available at [www.sedar.com](http://www.sedar.com)). The engineering expense incurred and the development costs amortized during the first half nine months of fiscal 2018 ended March 31, 2018 were \$5.17 million, 37% higher than in the same period of fiscal 2017 (\$3.78 million).

### General and Administration

General and Administration expenses were \$7.28 million for the first nine months of fiscal 2018 ended March 31, 2018 an increase of 76% over the same period ended March 31, 2017 (\$4.14 million).

### Foreign Exchange

For the first nine months year of fiscal 2017 ended March 31, 2018, there was a foreign exchange gain of \$0.08 million compared to a \$.01 million loss in the first nine months of fiscal 2017.

### Total operational expense

Operating expense for the first nine months of fiscal 2018 quarter was \$18.02 million, a 56% increase over the same period last year (\$11.52 million), reflecting continuing investment to drive Sangoma's top line growth and the additional costs attributable to the VoIP Supply LLC and CCD acquisitions. While absolute spending is higher with spending to drive growth and the addition of the recent acquisitions, expense as a percentage of revenue is lower across all spending categories.

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

Operating profit for the first nine months of fiscal 2018 ended March 31, 2018 was \$3.07 million versus an operating income of \$1.07 million in the first nine months of 2017.

**Business acquisition costs**

In the third quarter of fiscal 2018 Sangoma recorded \$0.28 million of costs directly associated with the legal, financing and closing of the acquisition of a division of Dialogic on January 9, 2018. This is expected to be close to the final total and the specifics of the transaction and associated costs are detailed in the third quarter financial statements.

**Net Income**

Net Income for the first nine months of fiscal 2018 ended March 31, 2018 was \$1.75 million (\$0.035 per share fully diluted) compared to a net income of \$0.63 million (\$0.019 per share fully diluted) for the first nine months of fiscal 2017 ended March 31, 2017.

**EBITDA (Earnings before Interest, Depreciation, Amortization and One Time Items)**

EBITDA for the first nine months of fiscal 2018 was 15.4% of sales, as derived below.

\$C Thousands	Nine Months Ended	
	Mar 31, 2018	Mar 31, 2017
Net Income	1,754	634
Tax	761	366
Interest	-1	0
Interest on Operating Line	170	75
Stock Based Compensation	136	188
Amortization of Property, Plant and Equipment	171	94
Amortization of Intangibles	900	554
One time acquisition related expense	382	-
EBITDA	4,273	1,911
% of revenue	10.7%	10.0%

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 March 31, 2018 Sangoma had current assets of \$29.30 million and current liabilities of 12.90 million, resulting in working capital of \$16.40 million. This compares to \$7.29 million on June 30, 2017 reflecting the share issuance on March 15 contributing \$11.90 million of cash and the acquisitions of VoIP Supply LLC during early July 2017 and the CCD division on January 9, 2018.

	<b>F2018</b>	F2017	<b>F2018</b>	F2017
\$k	Q3	Q3	YTD	YTD
Operating activities cash per financial statements	2,569	586	5,308	2,942
Less capitalization of development costs	-515	-564	-1,365	-1,182
Acquisition of VoIP Supply working capital	0	0	-79	0
Acquisition of Dialogic CCD division working capital	-124	0	-124	0
Adjusted cash flow from operations	<u>1,930</u>	<u>22</u>	<u>3,740</u>	<u>1,760</u>

For the first nine months of fiscal 2018 Sangoma generated \$3.74 million of adjusted cash flow from operations and in the third quarter used the nearly \$2 million in cash flow to pay off the operating line of credit reducing total debt to \$4.82 million.

Accounts Receivable of \$7.16 million on March 31, 2018 were \$4.16 million higher than as at June 30, 2017 (\$3.00 million), reflecting the increased revenue and incorporation of VoIP Supply and CCD businesses.

Inventories were \$6.78 million on March 31, 2018, \$2.23 million higher than for June 30, 2017 of which approximately \$1.20 million was related to inventory purchased as part of the VoIP Supply LLC acquisition and further \$0.40 million from the CCD addition. As has been previously shared Sangoma expects inventories to have somewhat larger swings between quarters as orders for phones and other new products are filled from a supply chain that more regularly 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 in the interim financial statements, the Company is not party to any material transactions with related parties.

## **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. During June 2017, Sangoma established a term loan of \$1.0 million and extended its operating line of credit from \$2.50 million to \$3.50 million to finance the cash component of the VoIP Supply LLC acquisition that closed on July 5, 2017. On January 9, 2018 the Company added a new term loan of \$4.00 million to fund the acquisition of the CCD business. During the quarter the Company paid down all of the operating line such that as of March 31, 2018 the only debt remaining was the outstanding balance of the two term loans totalling \$4.82 million.

## **OUTSTANDING SHARE DATA**

As of May 15, 2018 there were 47,140,190 issued and outstanding common shares of Sangoma and as of the same date there were outstanding options to acquire 5,779,341 common shares. The increase in the number of outstanding shares from June 30, 2017 resulted from exercise of options, the issuance of 993,627 shares as part of the acquisition of VoIP Supply LLC and the issuance of 13,138,000 shares through a private placement that closed on March 15, 2018.

## **SIGNIFICANT EVENTS**

None

## **POST REPORTING EVENTS**

None

## **ADDITIONAL INFORMATION**

Additional information relating to the Company is filed electronically on SEDAR at [www.sedar.com](http://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 premised basis 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.