MANAGEMENT'S DISCUSSION & ANALYSIS

For the Quarter Ended August 31, 2016

Introduction

This Management Discussion and Analysis (MD&A) explains the material changes in Thermal Energy International Inc.'s ("Thermal Energy" or the "Company") financial condition and results of operations for the first quarter of Fiscal Year 2017, ended August 31, 2016. The unaudited condensed consolidated interim financial statements and accompanying notes constitute an integral part of the discussion and should be read in conjunction with this MD&A. During the period ended August 31, 2016, the Company's critical accounting estimates, significant accounting policies and risk factors have remained substantially unchanged. Additional information relating to the Company is available on SEDAR at www.sedar.com.

Currency

All financial information in this report is stated in Canadian Dollars, which is both the presentation and functional currency of the Company. Approximately 55% of our operations, assets and liabilities are denominated in British Pound Sterling. As such, foreign currency fluctuations affect the reported values of individual lines on our statement of financial position and income statement. When the Canadian dollar strengthens, the reported values decrease and the opposite occurs when the Canadian dollar weakens.

Review and Approval by the Board of Directors

The Board of Directors, on recommendation of the Audit Committee, approved the content of this MD&A on October 18, 2016. Disclosure contained in this document is current to this date, unless otherwise stated.

Forward-Looking Statements

This MD&A may include statements that are forward-looking. These statements are not guarantees of future performance and are subject to risks and uncertainties that could cause actual results to differ materially from those in the forward-looking statements. We discuss the principal risks of our business in Section 7 of this MD&A. We cannot provide any assurance that forecasted financial or operational performance will actually be achieved. If it is achieved, we cannot provide assurance that it will result in an increase in our share price. See Section 8 entitled "Forward-Looking Information".

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1. Our Business

1.1 Company Overview

Thermal Energy, established in 1991, is an innovative cleantech company and a global provider of proprietary and proven energy and water efficiency and emission reduction products and solutions to the industrial, commercial and institutional markets. The Company is headquartered in Ottawa, Canada, with offices in the U.K., Italy, U.S., China and sales worldwide.

Thermal Energy engages clients through a unique mix of process, energy, environmental and financial expertise to save our customers money and improve their bottom lines by reducing their fuel use and carbon emissions. The Company's award winning products have an excellent track record of longevity, proven reliability and performance and have been shown to provide: significant energy savings; improved water efficiency; reduced greenhouse gas emissions; lower maintenance costs; improved product quality; and increased production efficiency. Thermal Energy's products are effective in a wide range of industries and applications.

More information on Thermal Energy can be found at www.thermalenergy.com. **GEM™, FLU-ACE®, THERMALONOx™**, and **DRY-REX™** are trademarks of Thermal Energy.

1.2 Core Businesses

The Company operates in the energy efficiency industry in North America, Europe, China and the rest of the world. The Company markets, sells, engineers, fabricates, constructs, installs and supports two technology lines – heat recovery solutions (**FLU-ACE®**) and condensate return system solutions (GEM™ steam traps). The Company is also developing a third technology line - low temperature biomass drying systems (**DRY-REX™)**.

Before 2007, the Company concentrated mainly on the selling of heat recovery systems but had begun selling GEM™ product through a distribution agreement with Gardner Energy Management Limited, based in the U.K. In 2008, the Company acquired Gardner Energy Management Limited, which sells the GEM™ product throughout the world. As part of this transaction, the Company also acquired the 67% share of GEMchem Ltd, a UK-based water treatment company providing services within the UK only.

The acquisition of Gardner Energy Management Limited resulted in the Company having two primary operational bases, one in Ottawa, Canada covering North America and China ("Thermal Energy Ottawa") and the other in Bristol, United Kingdom, covering Europe and the rest of the world ("Thermal Energy Bristol") . Although the Ottawa base is deemed to be the center of excellence for the heat recovery side of the business, and Bristol the center of excellence for condensate return system solutions, continuous cross-training means that both bases have expertise across both major product lines.

Although the Company markets its products throughout the world, the majority of sales are from within North America and Europe, due to the proximity to the Company's bases. While this continues to be the key focus, the Company also continues to look for new distributors in regions deemed to have potential.

1.3 Strategy

The Company's mission is to be a best-in-class provider of return on investment-driven thermal energy efficiency technology and solutions to the industrial, institutional, and commercial sectors, helping our clients around the world improve their bottom line, move towards sustainable operations and reduce their environmental and carbon foot print. The Company's products and services are "best-in-class" with world-wide application in a broad range of sectors.

The Company has representation in 28 countries around the world but our current focus is on the key markets of North America, Europe and the Middle East. Despite significant growth over the last few years, Thermal Energy's penetration in these markets remains low and therefore the Company plans to continue growing our sales and distribution capabilities in these markets while at the same time begin to build our business in other energy-intensive markets around the world.

We have sold our proprietary and proven products to hundreds of companies and institutions, including approximately 50 large multinational companies in the pharmaceutical, food and beverage, pulp and paper, chemical and petrochemical sectors. So far the Company has only partially penetrated 100 of the more than 2,000 global sites of these multi-national companies. Thermal Energy has executed a corporate-wide global roll-out of our product with two of these multi-national companies and is currently working with additional companies with the goal of executing similar corporate roll-outs.

With a global sales and distribution network the Company also has the opportunity to introduce new synergistic products and services, and acquire complementary products and businesses that can be distributed through our existing network.

Finally, the Company is also developing a number of recurring revenue streams such as rental and shared savings programs as well as service and maintenance programs.

2. Performance Measures

The Company believes the following performance measures provide useful information to both management and investors to better understand the financial performance and financial position of the Company.

2.1 Adjusted Operating Cash Flow

Adjusted operating cash flow (defined as income (loss) for the period, plus items not involving cash but excluding any changes in working capital items, plus finance lease payments received) is a performance measure used to gauge the cash generating capability of the Company. The impact changes in working capital items has on cash balances is excluded from the calculation of operating cash flow because changes in working capital items are usually only temporary and can fluctuate significantly from period to period and therefore are not a good indicator of the Company's longer term cash generating capabilities.

It is important to note that cash flow is not the same as net income, which includes transactions that did not involve actual cash outflows and excludes some transactions that did involve actual cash inflows. The calculation of adjusted operating cash flow starts with net income as identified in the Consolidated Statements of Comprehensive Income and then adds or subtracts a number of items identified in the Statement of Cash Flows. Adjusted operating cash flow does not have a standardized meaning prescribed by International Financial Reporting Standards and therefore may not be comparable to similar measures presented by other companies. The most directly comparable measure calculated in accordance with generally accepted accounting principles within the financial statements is net cash provided (used) in operating activities, as disclosed in the statement of cash flows.

2.2 EBITDAS

Management believes that EBITDAS (earnings before interest, taxation, depreciation, amortization, impairment of goodwill and other intangible assets, share-based compensation expense and net write down of lease) is a useful performance measure as it approximates cash generated from operations, before tax, capital expenditures and changes in working capital and excludes non-operating items. EBITDAS also assists comparison among companies as it eliminates the differences in earnings due to how a company is financed. EBITDAS does not have a standardized meaning prescribed by International Financial Reporting Standards and therefore may not be comparable to similar measures presented by other companies. The most directly comparable measure calculated in accordance with generally accepted accounting principles within the financial statements is income (loss) before income taxes, as disclosed in the statements of comprehensive income.

2.3 Order Backlog

Order backlog is a useful performance measure that Management uses as an indicator of the short term future revenue of our Company resulting from already recognized orders. The Company includes in "order backlog" any purchase orders that have been received by the Company but have not yet been reflected as revenue in the Company's published financial statements. It is important to note that once an order or partial order is recorded as revenue, the order backlog is reduced by the amount of the newly reported revenue. Order backlog does not have a standardized meaning prescribed by International Financial Reporting Standards and therefore may not be comparable to similar measures presented by other companies.

3. Performance

3.1 Summary of First Quarter Results

	Q1 2017	Q1 2016
	$	$
Revenue	**2,134,753**	2,556,614
Cost of Sales	**(679,068)**	(1,456,844)
Gross Profit	**1,455,685**	1,099,770
Administration, selling, marketing and business development expenses	**(1,456,689)**	(1,487,899)
Research and development expenses	**(34,279)**	(79,521)
Operating loss	**(35,283)**	(467,650)
Finance Revenue	**3,786**	7,821
Loss before income taxes	**(31,497)**	(459,829)
Income taxes (expense) recovery	**(48,233)**	7,232
Net loss for the period	**(79,730)**	(452,597)
Exchange differences on translation of overseas operations	**(256,006)**	144,941
Total comprehensive loss for the period	**(335,736)**	(307,656)

Revenues and Gross Profits

Revenues were $2,134,753 in the quarter ended August 31, 2016, representing a decrease of $421,861, or 16.5%, from the $2,556,614 recognized in the quarter ended August 31, 2015. Sales of heat recovery systems decreased by $923,471 (55.9%) from the same period of the previous year, while sales of GEM™ condensate return systems increased by $501,610 (55.5%).

Whereas the first quarter of FY 2016 included heat recovery revenues from a project at a packaged food business, as announced December 1, 2014, an installation at a Fortune 500 food and beverage leader, as announced April 29, 2015, a project at a leading dairy supplier, as announced March 4, 2015, and an installation at a major hospital, as announced January 29, 2015, the current quarter included just the closing stages of an installation at a major hospital, as announced October 29, 2015 plus an installation at a major food producer, as announced May 3, 2016.

GEM™ condensate return system sales in the quarter ended August 31, 2016 included the partial conversion of the same Fortune 500 food and beverage company as mentioned above, as well as revenues from the various orders mentioned in the press release dated September 20, 2016.

The gross profit of $1,455,685 in the quarter ended August 31, 2016 represented an increase of $355,915, or 32.4%, from the $1,099,770 achieved in the quarter ended August 31, 2015, despite a decrease in revenue. The increase in gross profit resulted from the product split, with the current quarter seeing a higher proportion of revenue from the sale of GEM™ product. These results expressed as a percentage of sales were 68.2% in the first quarter of FY 2017 compared with 43.0% in the first quarter of FY 2016.

Expenses

Administration, selling, marketing and business development expenses in the quarter ended August 31, 2016 totaled $1,456,689 compared to $1,487,899 in the quarter ended August 31, 2015, a decrease of $31,210, or 2.1%. Increases in commission payable due to the increased GEM revenues and training costs resulting from the bi-annual global sales conference were mostly offset by a reduction in stock based compensation plus foreign exchange gains. The weakening of the pound sterling against the Canadian dollar also contributed to the lower cost in the current period.

Research and development **costs** in the first quarter of FY 2017 of $34,279 compared to $79,521 in the first quarter of FY 2016. The first quarter of the prior year included some staff costs which were subsequently reclassified to general salaries.

Finance revenue in the quarter ended August 31, 2016 of $3,786 compared to $7,821 recognized in the quarter ended August 31, 2015. The interest rate implicit in the lease of 14.3% is applied against the reducing finance lease receivable balance, hence lower finance revenues as the term of the agreement progresses.

Loss before income taxes for the quarter ended August 31, 2016 was $31,497 compared to $459,829 in the same quarter of the previous year. The improvement was the result of the product split in the quarter plus the strengthening of the Canadian dollar against U.K. sterling.

Income tax charge in the first quarter of FY 2017 was $48,233, compared to a credit of $7,232 in the first quarter of FY 2016. Both the U.K. and U.S entities are subject to tax charges and fluctuations in the tax charge are the result of changing profitability in those entities.

Net loss for the quarter ended August 31, 2016 was $79,730 compared to a net loss of $452,597 in the same quarter of the previous year.

Comprehensive loss was $335,736 for the first quarter of FY 2017 compared to a loss of $307,656 for the first quarter of FY 2016. The weakening of the pound sterling against the Canadian dollar during the quarter was the main contributor to the exchange difference in the current period of $256,006.

Liquidity & Capital Resources

The working capital was $898,286 at August 31, 2016 compared to working capital of $976,374 at May 31, 2016 – a decrease of $78,088, with the Company's net cash position (Cash and cash equivalents less Bank loans) decreasing by $307,134 from $1,143,148 at May 31, 2016 to $836,014 as at August 31, 2016.

The Company's working capital position over the last eight quarters can be summarized as follows:

	Nov 30, 2014 $	Feb 28, 2015 $	May 31, 2015 $	Aug 31, 2015 $	Nov 30, 2015 $	Feb 29, 2016 $	May 31, 2016 $	Aug 31, 2016 $
Current Assets	3,722,822	3,768,369	3,650,605	2,641,290	3,747,206	4,018,307	3,834,124	3,400,711
Current Liabilities	2,193,708	2,848,970	3,162,216	2,512,531	3,528,790	3,317,835	2,857,750	2,502,425
Working Capital	1,529,114	919,399	488,389	128,759	218,416	700,472	976,374	898,286

Q1 FY 2017 Changes

Current assets decreased in the first quarter of FY 2017 by $433,413 to $3,400,711, the main decrease being to the cash balance which dropped by $307,134, as a number of accounts payable invoices relating to heat recovery projects were settled after year end, plus income taxes relating to the U.S. entity were paid. Other assets combined fell by $126,279.

Current liabilities decreased by $355,325 to $2,502,425. Accounts payable decreased by $306,230, and current tax liabilities decreased by $61,371 for the reasons mentioned above, while deferred revenue decreased by $72,426. Other net liabilities increased by $84,702, due to the timing of invoices issued late relating to the quarter.

As at August 31, 2016, $2,483 (0.2%) of the Company's trade receivables balance was over 90 days past due. None of the overdue balance is considered impaired as at August 31, 2016.

At August 31, 2016, the Company has operating lease commitments as shown below. The Company had no purchase obligations:

	Total $	Less than 1 year $	1-5 years $	More than 5 years $
Operating Leases	320,425	136,411	184,014	nil

Net cash used in operating activities in the quarter ended August 31, 2016 was $312,847 compared to $56,572 in the quarter ended August 31, 2015, mainly due to settling accounts payable balances and U.S. income tax payments.

Net cash provided by investing activities for the quarter ended August 31, 2016 of $30,874 comprised $32,214 finance lease principal payments received less $1,340 paid for additions to property, plant and equipment. This compared to $28,179 finance lease principal payments received less $1,348 paid for additions to property, plant and equipment for the quarter ended August 31, 2015.

After allowing negative $25,161 for the effect of exchange rate fluctuations on cash and cash equivalents, the net result of the above activities was a decrease in cash balance of $307,134 over the first three months of FY 2017, compared to a decrease of $55,902 over the first three months of FY 2016.

Adjusted operating cash outflow (defined as net income or loss, plus items not involving cash, after net tax and interest cash inflows or outflows, plus finance lease payments received) for the quarter ended August 31, 2016 was $78,748 compared to $336,088 for the quarter ended August 31, 2015.

In addition to its net cash balance of $836,014 as at August 31, 2016 the Company also had an estimated $369,000 of unused borrowing capacity under its bank loans. With cash balances and unused borrowing capacity of approximately $1,205,014, management believes that it has sufficient capital resources to fund existing operations and anticipated capital requirements in FY 2017. Order backlog as at August 31, 2016 was approximately $4.7 million compared to $3.1 million at the same time last year. As at October 18, 2016, the Company had $7.8 million in purchase orders that had not yet been reflected as revenue in the Company's published quarterly financial statements.

The Company's ability to realize its assets and discharge its liabilities depends on its ability to arrange debt or equity financing and its ability to generate sufficient cash from operations. No assurance can be given that any such additional funding will be available or that, if available, it can be obtained on terms favorable to the Company.

Management is of the opinion that sufficient working capital will be obtained from future cash flows by achieving profitable operations through continuing to manage expenditures and concentrating on building upon the revenue level experienced in 2016. The Company cannot be certain that cash generated from its operations will be sufficient to satisfy its liquidity requirements and it may need to raise capital by obtaining financing.

A reconciliation of Net cash provided (used) in operating activities to adjusted operating cash flow is shown below:

	Quarter ended	
	Aug 2016 $	Aug 2015 $
Net cash provided (used) in operating activities	(312,847)	(56,572)
Changes in working capital	201,885	(307,695)
Finance lease principal payments received	32,214	28,179
Adjusted operating cash flow	(78,748)	(336,088)

Net Investment in Lease

The Company's net investment in lease includes the following:

	August 31, 2016 $	May 31, 2016 $
Total estimated minimum lease payments receivable	89,054	125,054
Less: unearned income	(4,708)	(8,494)
	84,346	116,560
Less: current portion	(84,346)	(116,560)
	-	-

Finance lease receivable relates to one arrangement. The estimated minimum lease payments receivable in this lease represent the estimated monthly energy outputs of the leased asset and are based on assumptions regarding the efficiency of the asset, the operations of the plant in which it is located and penalty payments resulting from temporary plant shut-downs. On December 31, 2012, the lease with Fortress Specialty Cellulose, as signed on June 29, 2010, expired. On November 27, 2012, an agreement was signed whereby the customer agreed to purchase the recovered energy for a further two years, after which the customer has the option to renew for an additional 24 months on substantially the same terms or purchase the asset from the Company.

On December 22, 2013, the site commenced a market downtime for a period of ten weeks, following the imposition of an interim duty in China on the import of Canadian dissolving pulp, further to which on April 11, 2014, an agreement was made to further extend the existing lease by five months to mid-May 2015.

On May 1, 2015, the customer signed a further extension for 24 months to May 1, 2017. Pursuant to this new extension, the customer has agreed to pay up to $12,000 per month over two years, at the end of which the customer has the option to purchase the asset from the Company.

As part of calculating the impact of the new lease extension, the existing net residual value of the equipment was re-assessed. The estimated value of any re-sale value or scrap value of the equipment less removal and re-sale costs was assessed as $nil and so a write-down of the $139,530 net residual value was taken. This write-down, combined with the write-down of the May 2015 expected payment under the terms of the previous lease, which was expected to expire in mid-May 2015, reduced the net revenue recognized on renewal of the lease by $69,791.

Until the expiry of the new lease on May 1, 2017, finance revenue will be recognized within the income statement at the interest rate implicit in the lease.

The estimated minimum lease payments receivable in this lease represent the estimated monthly energy outputs of the leased asset and are based on assumptions regarding the efficiency of the asset and the operations of the plant in which it is located.

Future estimated minimum lease payments receivable, and expected residual value of equipment at the end of the lease, under the sales-type lease are as follows:

	$
Less than one year	89,054
Residual value of equipment	-
	89,054

Related Party Transactions

Options outstanding for Directors (excluding the CEO) as at August 31, 2016 were 1,250,000 of which 1,083,333 were exercisable. There were no warrants outstanding for Directors.

Options outstanding for Senior Management (including the CEO) as at August 31, 2016 were 9,708,720 of which 6,123,697 were exercisable. There were no warrants outstanding for Senior Management.

Directors and Senior Management Compensation

During the quarter ended August 31, 2016 compensation arrangements for directors was as follows:

$15,000 per annum per Director plus an additional $9,000 per annum payable to the Chairman of the Board, $6,000 per annum payable to the chairperson of the Audit Committee, $6,000 per annum payable to the chairperson of the Ethics, Governance and Compliance Committee and $1,000 payable for each in-person meeting.

During the quarter ended August 31, 2016, Directors fees paid were $22,500. Fees to the Chairperson of the Audit Committee and to the Chairperson of the Ethics, Governance and Compliance Committee were $1,500 each; fees paid to the Chairman were $2,250. One in-person meeting was held during the period.

Compensation payable to directors and officers during the period ended August 31, (inclusive of the amounts described above but excluding stock based compensation) was as follows:

	Salaries and fees		Incentives		Other short-term benefits		Total	
	2016	2015	**2016**	2015	**2016**	2015	**2016**	2015
	$	$	**$**	$	**$**	$	**$**	$
Directors								
M. Williams	**6,250**	6,250	**-**	-	**-**	-	**6,250**	6,250
J. Kelly	**7,000**	7,000	**-**	-	**-**	-	**7,000**	7,000
W. Ollerhead	**4,750**	4,750	**-**	-	**-**	-	**4,750**	4,750
B. Linton	**3,750**	6,250	**-**	-	**-**	-	**3,750**	6,250
J. Schoenmakers	**6,250**	4,750	**-**	-	**-**	-	**6,250**	4,750
D. Spagnolo	**4,750**	4,750	**-**	-	**-**	-	**4,750**	4,750
Total	**32,750**	33,750	**-**	-	**-**	-	**32,750**	33,750
Senior Management								
W. Crossland	**60,000**	60,000	-	-	**-**	-	**60,000**	60,000
J. Flynn[(1)]	**37,283**	42,440	-	-	**5,774**	6,572	**43,057**	49,012
R. Triebe	**38,425**	38,425	-	-	**817**	954	**39,242**	39,379
S. Mawby[(1) (2)]	**36,607**	11,199	-	-	**5,589**	2,271	**42,196**	13,470
Total	**172,315**	152,064	**-**	-	**12,180**	9,797	**184,495**	161,861
Total Related Party Transactions	**205,065**	185,814	**-**	-	**12,180**	9,797	**217,245**	195,611

Other short-term benefits include cash payments for social security costs, employee benefits, and payments made into defined contribution pension plans of the Company's UK based subsidiaries.

(1) Ms. Flynn and Mr. Mawby are compensated in UK Pound sterling. Average exchange rate to Canadian dollar was 1.7497 and 1.9917 in the first quarter of FY 2017, and the first quarter of FY 2016 respectively.

(2) Mr. Mawby was on parental leave between June 15, 2015 and August 31, 2015.

Normal Course Issuer Bid

On February 17, 2016, the Company announced its intent to re-launch the Normal Course Issuer Bid ("NCIB") for a further period of twelve months. The NCIB was approved by the TSX Venture Exchange on February 12, 2016. During the 12-month period commencing February 15, 2016 and ending February 15, 2017, the Company is able to purchase on the TSX up to 12,758,701 common shares, representing approximately 8% of the then issued and outstanding common shares. The actual number of common shares purchased, if any, and the timing of such purchases will be determined by the Company by considering market conditions, share prices, its cash position, and other factors.

The previously announced NCIB was approved by TSX Venture Exchange on November 3, 2014 and expired on November 3, 2015.

In the quarter ended August 31, 2016 the Company did not purchase any common shares (2015: nil).

Segmented Information

In the quarters ended August 31, 2016 and August 31, 2015, the Company operated in the energy efficiency industry in North America, Europe, China and the rest of the world. The Company markets, sells, engineers, fabricates, constructs, installs and supports two technology lines – heat recovery solutions and condensate return system solutions. The Company is also developing a third technology line - low temperature biomass drying systems. Assets are located in Canada, Europe and China.

Management reporting comprises analysis of revenue and gross profit by product segment within two distinct geographical areas. All other items of revenue and expenses are considered on a geographical and/or global basis in making strategic decisions regarding the Company's future. The Company has two operational bases ("reporting units"), one in Canada covering North America and China ("Thermal Energy Ottawa"), and the other in Bristol, United Kingdom, covering Europe and the rest of the world ("Thermal Energy Bristol"). These areas are determined by proximity of the region to the reporting unit, plus the location of the contracts in existence with agents and distributors in the respective areas and the historical relationships with those agents and distributors. Corporate costs that cannot easily be attributed to either of the two reporting units are included in reconciling items. The chief operating decision maker focuses on revenues and costs by geographical segments, but manages assets and liabilities on a global basis.

Segment information for the quarter ended August 31, 2016 and the comparative period are detailed in the table below.

	North America & China		Europe & Rest of World		Reconciling items		Total	
	2016	2015	**2016**	2015	**2016**	2015	**2016**	2015
	$	$	**$**	$	**$**	$	**$**	$
Total revenue	**681,375**	1,253,030	**1,453,378**	1,303,584	**-**	-	**2,134,753**	2,556,614
Cost of sales	**(198,626)**	(886,549)	**(480,442)**	(570,295)	**-**	-	**(679,068)**	(1,456,844)
Gross profit	**482,749**	366,481	**972,936**	733,289	**-**	-	**1,455,685**	1,099,770
Other expenses	**(593,349)**	(593,588)	**(661,612)**	(646,692)	**(236,007)**	(327,140)	**(1,490,968)**	(1,567,420)
Finance revenue	**3,786**	7,821	**-**	-		-	**3,786**	7,821
Profit (loss) before taxation	**(106,814)**	(219,286)	**311,324**	86,597	**(236,007)**	(327,140)	**(31,497)**	(459,829)
Taxation	**24**	493	**(51,461)**	(249)	**3,204**	6,988	**(48,233)**	7,232
Profit (loss) after taxation	**(106,790)**	(218,793)	**259,863**	86,348	**(232,803)**	(320,152)	**(79,730)**	(452,597)
Attributable to:								
Owners of the parent	**(101,259)**	(216,794)	**251,044**	80,325	**(232,803)**	(320,152)	**(83,018)**	(456,621)
Non-controlling interest	**(5,531)**	(1,999)	**8,819**	6,023	**-**	-	**3,288**	4,024

Other expenses within reconciling items comprise the following:

	Quarter ended Aug 31 **2016** **$**	2015 $
Corporate admin costs	**194,869**	188,025
Stock-based compensation	**25,855**	50,828
Professional fees	**95,502**	91,936
Depreciation of property, plant and equipment	**7,862**	7,566
Bank charges and interest	**8,373**	8,654
Foreign exchange differences	**(96,454)**	(19,869)
Total	**236,007**	327,140

Corporate administration costs include directors' fees, all costs relating to both the CEO and CFO, directors and officers insurance, corporate legal costs, public relations costs, professional fees relating to group tax planning and corporate filing costs.

During the quarter ended August 31, 2016 the company had one customer within Europe and the rest of the world that accounted for 20% of total revenue for the period.

During the quarter ended August 31, 2015 the company had two customers within North America and China that accounted for 21% and 12%, and two customers within Europe and the rest of the world that accounted for 14% and 11% of total revenue respectively.

Further geographical analysis:

	Revenue for the three months ended		Property, Plant and Equipment as at		Goodwill and other Intangible assets as at	
	August 31, 2016 $	August 31, 2015 $	**August 31, 2016 $**	May 31, 2016 $	**August 31, 2016 $**	May 31, 2016 $
Canada	**55,031**	47,944	**46,161**	50,380	**-**	-
U.S.A.	**626,344**	1,205,086	**-**	-	**-**	-
U.K.	**1,149,757**	1,153,790	**23,189**	28,057	**1,856,849**	2,047,246
Italy	**166,350**	32,418	**-**	-	**-**	-
Netherlands	**14,896**	25,206	**-**	-	**-**	-
Ireland	**26,836**	-	**-**	-	**-**	-
Germany	**46,562**	82,420	**-**	-	**-**	-
Rest of Europe	**7,438**	273	**-**	-	**-**	-
India	**18,308**	2,754	**-**	-	**-**	-
China	**-**	-	**-**	-	**-**	-
Kenya	**23,231**	-	**-**	-	**-**	-
Rest of world	**-**	6,723	**-**	-	**-**	-
Total	**2,134,753**	2,556,614	**69,350**	78,437	**1,856,849**	2,047,246

Material Segmentation Variances

Revenue

North America and China: revenue for the quarter ended August 31, 2016 was $681,375 compared to $1,253,030 for the quarter ended August 31, 2015. Heat recovery revenue decreased by $833,518, with the current period seeing the very final stages of two projects which were significantly completed in the previous quarter. This compared to two projects in progress in the same period of the prior year. Revenue from sales of GEM™ products meanwhile increased by $261,863 with a number of orders being converted during the current period.

Europe and rest of the world: revenue for the quarter ended August 31, 2016 was $1,453,378 compared to $1,303,584 for the same period of the previous year, an increase of $149,794. Heat recovery revenue decreased by $89,953, with two projects in progress in the first quarter of last year being replaced with one in the current quarter. Revenue from sales of GEM[TM] products increased by $239,747, with one hospital conversion in the current period, compared to none in the comparative period, plus a general increase elsewhere.

Segment Income (loss) Before Tax

North America and China gross profit increased by $116,268 in the quarter ended August 31, 2016 over the same quarter of the preceding year despite the fall in revenue, due to the majority of the current quarter's revenue coming from the sale of GEM[TM] products. Other expenses were at a similar level to the same quarter of the previous year and, combined with a decrease in finance revenue as the lease progresses of $4,035, served to decrease the loss before tax by $112,472.

Europe and rest of the world gross profit increased by $239,647 in the quarter ended August 31, 2016 over the same quarter of the preceding year, again as a result of the product split. Other net costs increased by $14,920, despite the weakening of the pound sterling, the main contributors to the increase being commissions and travel costs related to the global sales meeting. This resulted in a net income before tax of $311,324 for the first quarter of FY 2017 compared to $86,597 for the first quarter of FY 2016.

Other expenses within Reconciling items, which incorporates all costs not specifically attributable to the either regional operational center, amounted to $236,007 in the first quarter of FY 2017 compared to $327,140 in the first quarter of FY 2016, the main variances being a reduction in stock based compensation and favorable exchange rate fluctuations in the current quarter over the same period of the previous year.

Quarterly financial information (unaudited)
For the eight quarters ended August 31, 2016

Quarter ended	31-Aug-16 $	31-May-16 $	29-Feb-16 $	30-Nov-15 $
Revenue	2,134,753	4,123,246	3,220,621	2,501,595
Gross Profit	1,455,685	2,047,713	2,029,240	1,617,282
Gross Profit Percentage	68.2%	49.7%	63.0%	64.6%
EBITDAS(1)	3,302	376,858	504,654	83,538
Total net income (loss)	(79,730)	268,113	417,722	25,630
Income (loss) per share, basic and diluted	(0.001)	0.001	0.003	0.000

Quarter ended	31-Aug-15 $	31-May-15 $	28-Feb-15 $	30-Nov-14 $
Revenue	2,556,614	2,525,061	1,440,985	1,662,805
Gross Profit	1,099,770	1,193,821	711,906	1,019,426
Gross Profit Percentage	43.0%	47.3%	49.4%	61.3%
EBITDAS(1)	(400,871)	(256,642)	(647,245)	(486,557)
Total net income (loss)	(452,597)	(337,642)	(657,592)	(491,164)
Income (loss) per share, basic and diluted	(0.003)	(0.002)	(0.004)	(0.003)

(1) EBITDAS represents earnings before interest, taxation, depreciation, amortization, share-based compensation expense and net write down of lease.

4. Business Outlook

- In June 2012, the Company received an order for approximately $562,000 from a publicly owned hospital for a heat recovery solution. This order was partially completed in FY 2013 and the customer is currently deciding on changes it may wish to be made before the project is continued. It is not yet known when this project may be completed.

- In May 2016, the Company announced that it had received an order for approximately $1,015,000 from a leading food products business for the supply and installation of a FLU-ACE® heat recovery solution at one of its sites. This order was 43% complete as at August 31, 2016, with the balance expected to be fulfilled and revenue earned over the next three months.

- In July 2016, the Company announced that it had received an order for approximately $840,000 from a multi-site hospital group for the extension of a heat recovery system previously installed by Thermal Energy. This order is expected to be fulfilled and revenue earned over the next six months.

- In August 2016, the Company announced that it had received two orders from a hospital trust: the first valued at approximately $868,000 for the supply and installation of a heat recovery system at one of its sites; and the second for the supply and installation of GEM™ steam traps at another site, worth approximately $280,000. The heat recovery order is expected to be fulfilled and revenue earned over the next six months, whilst the GEM™ order has been partially fulfilled by August 31, 2016, as the traps have been despatched but not yet installed.

- Also in August 2016, the Company announced that it had received an order for approximately $750,000 from a global brewing company for the supply and installation of a FLU-ACE® heat recovery solution at one of its sites. This order is expected to be fulfilled and revenue earned over the next six months.

- In September 2016, the Company announced that it had received an order for approximately $500,000 for the supply and installation of GEM™ steam traps at a hospital. This order is expected to be fulfilled and revenue earned over the next six months.

- Also in September 2016, the Company announced that it had received an order for approximately $1,700,000 from a leading producer of industrial and fuel alcohols for the supply and installation of a FLU-ACE® heat recovery solution at one of its ethanol plants. This order is expected to be fulfilled and revenue earned over the next twelve months.

- The Company's order backlog as at August 31, 2016 was approximately $4.7 million. As at October 18, 2016, the Company had an order backlog of approximately $7.8 million, of which approximately $0.3 million is related to long term contracts and is not expected to be reflected in revenue within the next 12 months.

5. Summary of Outstanding Shares and Dilutive Instruments

The Company currently has the following shares and dilutive instruments outstanding:

Shares

157,834,616 class A common shares.

Options

Number of Options outstanding	Number of Options Exercisable	Exercise Price Per Share $	Expiry Date
3,860,000	**3,860,000**	**0.10**	**01-Dec-2016**
4,340,000	**4,340,000**	**0.10**	**22-Nov-2017**
2,924,000	**1,949,334**	**0.05**	**18-Nov-2018**
3,149,360	**2,099,574**	**0.10**	**28-May-2019**
250,000	**83,333**	**0.09**	**01-Dec-2019**
4,076,360	**1,358,787**	**0.08**	**29-May-2020**
3,425,000	**-**	**0.05**	**30-May-2021**
22,024,720	**13,691,028**		

6. Critical Accounting Estimates and Changes in Accounting Standards

Critical Accounting Estimates

The preparation of financial statements in accordance with IFRS necessitates the use of management estimates, assumptions and judgment that affect reported amounts of assets, liabilities, revenues and expenses and disclosure of contingent assets and liabilities at the date of the financial statements. Although management reviews its estimates on an ongoing basis, actual results may differ from these estimates as confirming events occur. The following components of the financial statements depend most heavily on such management estimates, assumptions and judgment, any changes in which may have a material impact on the Company's financial condition or results of operations. For more information about certain assumptions and risks that may affect these estimates, assumptions and judgments, please see the "Forward Looking Information" section of this MD&A.

Valuation of goodwill and intangible assets and asset impairment

Goodwill and intangible assets are tested annually for impairment, or earlier if circumstances indicate an impairment.

An impairment loss is recognized for the amount by which an asset's or cash-generating unit's carrying amount exceeds its recoverable amount. To determine the recoverable amount, management estimates expected future cash flows from each asset or cash-generating unit and determines a suitable interest rate in order to calculate the present value of those cash flows. In the process of measuring expected future cash flows management makes assumptions about future operating results. These assumptions relate to future events and circumstances. The actual results may vary, and may cause significant adjustments to the Company's assets within the next financial year.

In most cases, determining the applicable discount rate involves estimating the appropriate adjustment to market risk and the appropriate adjustment to asset-specific risk factors.

Future production outputs relating to the finance lease

When a new finance lease or amendment is signed, in determining minimum lease payments receivable, management makes estimates regarding monthly energy outputs of the leased asset based on assumptions regarding the efficiency of the asset, the operations of the plant in which it is located, penalty payments resulting from temporary plant shut-downs and residual value of the equipment. These assumptions relate to future events and circumstances.

Assumptions used in the Black-Scholes fair value calculations

The estimation of share-based payment expense requires the selection of an appropriate valuation model and consideration as to the inputs necessary for the valuation model chosen. In calculating the share-based payment expense, key estimates such as the rate of forfeiture of options granted, the expected life of the option, the volatility of the Company's stock price and the risk free interest rate are used.

Revenue Recognition relating to contracts for heat recovery solutions

The stage of completion of any heat recovery solutions contract is assessed by management by taking into consideration all information available at the reporting date. In this process, management exercises significant estimate about milestones, actual work performed and the estimated costs to complete work.

Deferred tax assets

Deferred tax assets are recognized for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable income will be available against which they can be utilized. These estimates are reviewed at every reporting date. Significant management judgment is required to determine the amount of deferred tax assets that can be recognized, based upon the likely timing and the level of the reversal of existing differences, future taxable income and future tax planning strategies.

Changes in Accounting Standards

The Company has adopted the following new or amended accounting standards.

Amendments to IFRS 2, “Share-based Payments”

In December 2013, the IASB issued amendments to IFRS 2 Share-based payments, which clarify vesting conditions by separately defining a performance condition and a service condition, both of which were previously incorporated within the definition of a vesting condition. These amendments became effective for annual periods beginning on or after July 1, 2014 and interim periods within those annual periods. The Company adopted the amendments on June 1, 2015. The adoption of the amendments to IFRS 2 did not have a material impact on the consolidated financial statements.

Amendments to IFRS 13, “Fair Value Measurements”

In December 2013, the IASB issued amendments to IFRS 13 Fair Value Measurements, which relate to the measurement of short-term receivables and payables, and the scope of the portfolio exemption. Short-term receivables and payables with no stated interest rate can still be measured at the invoice amount without discounting if the effect of discounting is immaterial. The portfolio exemption permits an entity to measure the fair value of a group of financial assets and financial liabilities on a net basis. The amendment clarifies that the portfolio exemption applies to all contracts within the scope of IAS 39 Financial Instruments: Recognition and Measurement (or IFRS 9 Financial Instruments if this has been adopted early), regardless of whether the meet the definition of financial assets or financial liabilities within IAS 32 Financial Instruments: Presentation. These amendments became effective for annual periods beginning on or after July 1, 2014. The Company adopted the amendments on June 1, 2015. The adoption of the amendments to IFRS 13 did not have a material impact on the consolidated financial statements.

Amendments to IAS 16 “Property, Plant and Equipment” and IAS 38 “Intangible Assets”

In May 2014, the IASB issued amendments to IAS 16 Property, Plant and Equipment and IAS 38 Intangible Assets. These amendments prohibit entities from using a revenue-based depreciation method for items of property, plant and equipment. They also introduce a rebuttable presumption that revenue is not an appropriate basis for amortization of an intangible asset. The amendments explain that an expected future reduction in selling prices could be indicative of a reduction of the future economic benefits embodied in an asset. These amendments are to be applied prospectively for annual periods beginning on or after January 1, 2016. The Company adopted the amendments on June 1, 2016. The adoption of the amendments to IAS 16 and IAS 38 did not have a material impact on the consolidated financial statements.

At the date of approval of the accompanying consolidated financial statements, certain new standards, amendments and interpretations to existing standards have been published but are not yet effective, and have not been adopted early by the Company. These standards will be adopted at the effective date.

Management anticipates that all of the pronouncements will be adopted in the Company’s accounting policy for the first period beginning after the effective date of the pronouncement. Information on new standards, amendments and interpretations that are expected to be relevant to the Company’s consolidated financial statements is provided below. Certain other new standards and interpretations have been issued, but are not expected to have an impact on the Company’s consolidated financial statements.

IFRS 9, “Financial Instruments”

In July 2014, the IASB issued the final version of IFRS 9, bringing together the classification and measurement, impairment and hedge accounting phases of the project to replace IAS 39, “Financial Instruments: Recognition and Measurement. This standard simplifies the classification of a financial asset as either at amortized cost or at fair value as opposed to the multiple classifications which were permitted under IAS 39. This standard also requires the use of a single impairment method as opposed to the multiple methods in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. The standard also adds guidance on the classification and measurement of financial liabilities. IFRS 9 is to be applied retrospectively for annual periods beginning on or after January 1, 2018. Early application is permitted. The Company does not intend to adopt this standard early and is currently evaluating the impact of adopting this standard on the consolidated financial statements.

IFRS 15, “Revenue from Contracts with Customers”

In May 2014, the IASB issued IFRS 15, Revenue from Contracts with Customers, which provides a single, principles-based five-step model for revenue recognition to be applied to all customer contracts, and requires enhanced disclosures. The IASB recently confirmed a one year deferral of the effective date of IFRS 15 to January 1, 2018. Earlier application of IFRS 15 continues to be permitted. The Company does not intend to adopt this standard early and is currently evaluating the impact of adopting this standard on the consolidated financial statements.

IFRS 16, “Leases”

In January 2016, the IASB issued IFRS 16, Leases, which specifies how to recognize, measure present and disclose leases. The standard provides a single lessee accounting model, requiring lessees to recognize all assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value. Consistent with its predecessor, IAS 17, the new lease standard continues to require lessors to classify leases as operating or finance. IFRS 16 is to be applied retrospectively for annual periods beginning on or after January 1, 2019. Earlier application is permitted if IFRS 15 Revenue from Contracts with Customers has also been applied. The Company does not intend to adopt this standard early and is currently evaluating the impact of adopting this standard on the consolidated financial statements.

7. Risk Factors and Risk Management

Management is confident about our long-term prospects, but does recognize that the company is exposed to a number of risks in the normal course of business that could negatively impact the financial condition of the Company.

Operational risks of the company include the ability to continue to secure and implement sales contracts for its GEM™ and FLU-ACE® technology solutions.

Financial risks and uncertainties of the Company include:

- The Company’s history of operating losses and uncertainty of future profitability;
- The ability to grow sales through the establishment of new cooperative partnerships and strategic alliances;
- The ability to grow sales through the licensing of the corporation’s technologies;
- The ability to secure and maintain the required outside working capital financing;
- The ability to achieve profitable operations through increased sales,
- Reliance on third party collaborations and license arrangements;
- Reliance on proprietary technology;
- Competition in the energy conservation and environmental compliance solutions;
- Product liability claims and insurance;
- Reliance on key personnel;
- The ongoing litigation with its former President & CEO;
- The ability to control costs and achieve a positive gross margin on projects; and,
- The effect of a continuing prolonged recession in Canada, USA and Europe to the financial markets in securing project financing and in particular to industrial and commercial customers in committing capital to projects.
- The impact of the pending departure from the European Union by the U.K.

Management's addressing of the risks:

FY 2012 saw the Company's first ever net profit, which was the result of increased revenues and strict cost control. FY 2013, however, produced an operating loss of $844,328, resulting from diminished revenues and increasing costs. Despite further cost increases as management continue to build the sales force, FY 2014 produced the company's best ever post-tax income of $634,023 as well as an increase in cash balance of $742,022, but this was again followed by a net loss of $2,154,817, accompanied by a cash decrease of $1,331,074 in FY 2015. FY 2016 year saw a return to profitability and an increase in cash balances of $427,805 and although the first quarter of FY 2017 produced a small loss, it was significantly better than previous first quarters and was accompanied by a healthier order backlog than in the previous year.

The Company actively protects its proprietary technology through registered trademarks and confidentiality agreements.

The Company maintains adequate forms of general liability insurance including product liability and errors and omission coverage.

Management still believes that competition against its core technology of GEM™, FLU-ACE® and DRY-REX™ is limited at this time and believes that the market place is sufficiently large to mitigate the risk of stronger competition in the future.

On June 23, 2016 a referendum was held in the U.K., resulting in the decision to leave the European Union. One immediate effect was a significant fall in the value of U.K. Pound Sterling against most other major currencies. Negotiations regarding how trade will continue after the U.K. leaves are ongoing, the outcome of which is difficult to predict. Management continues to monitor the situation, but at this point cannot comment on how the eventual break will impact the Company. In the meantime, business continues as normal.

Management continues to focus on strengthening relationships with key customers, as well as securing new relationships with multi-site organizations, which is anticipated to provide repeat business into the foreseeable future. Management continually monitors costs and cash flow to ensure that the Company has sufficient funds for operations while providing for future growth.

8. Forward-Looking Information

This MD&A contains certain "forward-looking statements." All statements, other than statements of historical fact, that address activities, events or developments that the Company believes, expects or anticipates will or may occur in the future (including, without limitation, statements regarding financial and business prospects and financial outlook) are forward looking statements. These forward-looking statements reflect the current expectations or beliefs of Management, based on information currently available to the Company. Forward-looking statements are subject to a number of risks, uncertainties and assumptions that may cause the actual results of the Company to differ materially from those discussed in the forward-looking statements and, even if such actual results are realized or substantially realized, there can be no assurance that they will have the expected consequences to, or effects on the Company. Factors that could cause actual results or events to differ materially from current expectations include, among other things, changes in general economic and market conditions, changes to regulations affecting the Company's activities, and uncertainties relating to the availability and costs of financing needed in the future. Any forward-looking statement speaks only as at the date on which it is made and, except as may be required by applicable securities laws, the Company disclaims any intent or obligation to update any forward-looking statement, whether as a result of new information, future events or results or otherwise. Although Management believes that the assumptions inherent in the forward-looking statements are reasonable, forward-looking statements are not guarantees of future performance and, accordingly, undue reliance should not be put on such statements due to the inherent uncertainty therein.

9. Management's Responsibility for Financial Reporting

In compliance with the Canadian Securities Administrators' National Instrument 52-109 ("NI 52-109"), the Company has filed with applicable Canadian securities regulatory authorities, certificates signed by its Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") that, among other things, report on the design and effectiveness of disclosure controls and procedures and the design of internal controls over financial reporting.

Under the supervision of the CEO and CFO, the Company maintains systems of internal accounting and administrative controls to provide reasonable assurance that the financial information is relevant, reliable and accurate and that transactions are authorized, assets are safeguarded and proper records are maintained. Internal controls over financial reporting, no matter how well designed, have inherent limitations and may not prevent or detect all misstatements. There were no changes to the Company's internal control over financial reporting during the quarter ended August 31, 2016 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

The Board of Directors is responsible for ensuring that management fulfills its responsibility principally through its Audit Committee.