



An Innovative Technology Company Providing
Custom Energy and Emission Reduction Solutions

▶ Second Quarter Report – FY 2009

Period ending November 30, 2008



36 Bentley Avenue, Ottawa, Ontario, Canada. K2E 6T8
Telephone: 613-723-6776, Fax: 613-723-7286
e-mail: investor@thermalenergy.com
www.thermalenergy.com

THERMAL ENERGY INTERNATIONAL INC.
 Incorporated under the Ontario Business Corporations Act

CONSOLIDATED BALANCE SHEETS

As at	(Unaudited)	
	Nov 30 2008	May 31 2008
	\$	\$
ASSETS		
Current assets		
Cash	166,042	84,717
Short-term investments (note 5)	5,378,234	552,773
Accounts receivable (note 6)	1,456,865	627,571
Contracts in progress	-	156,000
Inventories	534,905	-
Net investment in lease (note 8)	249,159	227,034
Prepays and other assets	91,172	31,934
	7,876,377	1,680,029
Property, plant and equipment (note 7)	121,637	65,066
Net investment in lease (note 8)	1,818,536	1,948,906
Goodwill (note 4)	4,804,213	-
	14,620,763	3,694,001
LIABILITIES, CAPITAL STOCK, CONTRIBUTED SURPLUS AND DEFICIT		
Current liabilities		
Bank loans (note 9)	924,966	908,667
Accounts payable	862,798	2,001,801
Accrued liabilities	480,833	459,777
Deferred revenue	70,000	384,908
Due to past President (note 10)	17,937	17,937
	2,356,534	3,773,090
Non-controlling interest (note 4)	10,143	-
Capital stock, contributed surplus and deficit		
Capital stock (note 11)	32,606,553	19,479,079
Contributed surplus (note 11)	2,273,122	1,528,414
Deficit	(22,536,999)	(21,086,582)
Accumulated other comprehensive loss	(68,304)	-
	12,274,372	(79,089)
	14,620,763	3,694,001

Contingency (note 18)

The accompanying notes are an integral part of these consolidated financial statements

On behalf of the Board



President and C.E.O.



Chief Operating Officer & CFO

THERMAL ENERGY INTERNATIONAL INC.

CONSOLIDATED OPERATIONS, COMPREHENSIVE LOSS AND DEFICIT
(Unaudited)

	Three months ended November 30		Six months ended November 30	
	2008 \$	2007 \$	2008 \$	2007 \$
REVENUE				
Sales	1,140,563	618,290	2,198,881	1,666,647
Cost of sales	317,700	637,914	847,915	1,423,319
Gross profit (loss)	822,863	(19,624)	1,350,966	243,328
Expenses				
Administration	644,552	250,894	1,172,131	535,167
Selling, marketing and business development	830,837	480,208	1,351,919	781,317
Legal fees	59,797	5,312	69,382	10,409
Audit fees	46,468	15,744	64,468	30,744
Insurance	34,155	41,563	68,403	71,739
Amortization of property, plant and equipment	15,199	7,918	26,890	15,611
Patent and trademark maintenance	14,730	6,295	17,540	6,295
Research and development	83,407	22,474	155,050	53,154
Interest and bank charges	34,868	1,163	65,762	4,150
Foreign exchange loss (gain)	(12,048)	21,436	21,264	39,943
	1,751,965	853,007	3,012,809	1,548,529
Loss before the following:	(929,102)	(872,631)	(1,661,843)	(1,305,201)
Interest revenue	31,306	9,200	65,327	23,875
Finance revenue	64,465	-	149,517	-
Loss before non-controlling interest	(833,331)	(863,431)	(1,446,999)	(1,281,326)
Non-controlling interest	(1,000)	-	(3,418)	-
Net loss	(834,331)	(863,431)	(1,450,417)	(1,281,326)
Exchange translation adjustment of net investment in self-sustaining foreign operation	40,146	-	68,304	-
Net loss and Other comprehensive loss	(874,477)	(863,431)	(1,518,721)	(1,281,326)
Deficit, beginning of period	(21,730,826)	(19,131,969)	(21,086,582)	(18,714,074)
Deficit, end of period	(22,605,303)	(19,995,400)	(22,605,303)	(19,995,400)
Net loss per share - basic and diluted	(0.005)	(0.009)	(0.009)	(0.014)
Weighted average number of common shares	167,709,197	91,876,821	159,005,606	91,702,425

The accompanying notes are an integral part of these consolidated financial statements

THERMAL ENERGY INTERNATIONAL INC.

CONSOLIDATED STATEMENT OF CASH FLOWS
(Unaudited)

	Three months ended November 30		Six months ended November 30	
	2008	2007	2008	2007
	\$	\$	\$	\$
OPERATING ACTIVITIES				
Net loss for the period	(834,331)	(863,431)	(1,450,417)	(1,281,326)
Add items not involving cash:				
Stock-based compensation charge	56,104	132,034	177,508	285,834
Amortization of property, plant and equipment	15,199	7,918	26,890	15,611
Non-monetary compensation charge	10,808	47,171	17,500	90,921
Changes in non-cash operating working capital				
Accounts receivable	(462,616)	(296,813)	89,427	(201,737)
Contracts in progress	194,000	(192,300)	156,000	(221,300)
Prepays and other assets	5,013	22,023	(5,785)	23,476
Accounts payable	64,412	1,119	(1,506,401)	451,110
Accrued liabilities	26,328	602,333	(218,342)	588,798
Deferred revenue	70,000	77,553	(314,908)	(392,000)
Net cash used in operating activities	(854,934)	(462,393)	(3,028,528)	(640,613)
INVESTING ACTIVITIES				
(Acquisition) reduction in short term investments	763,638	817,052	(4,823,119)	551,639
Acquisition of subsidiary	-	(333,976)	(5,411,394)	(333,976)
Additions to property, plant and equipment	(21,367)	(1,567)	(37,811)	(26,248)
Net cash used in investing activities	742,122	481,509	(10,272,324)	191,415
FINANCING ACTIVITIES				
Increase (decrease) in bank loan	(113,969)	-	(405,506)	-
Net investment in lease (note 8)	44,574	-	108,245	-
Common shares issued (note 11)	-	11,000	14,900,400	176,500
Financing fees	-	-	(1,223,226)	-
Decrease in loan receivable	-	25,000	-	25,000
Net cash provided by financing activities	(69,395)	36,000	13,379,913	201,500
Effect of exchange rate fluctuations on cash and cash equivalents	367	-	2,264	-
Increase (decrease) in cash for the period	(181,840)	55,116	81,325	(247,698)
Cash beginning of period	347,882	246,382	84,717	549,196
Cash end of period	166,042	301,498	166,042	301,498
Interest paid	39,058	697	58,753	3,087
Shareholder loans to acquire shares	65,000	-	212,600	-
Fair value of options exercised transferred to capital stock	35,000	26,041	69,000	133,058
Fair value of warrants issued for financing fees	-	-	636,200	-

The accompanying notes are an integral part of these consolidated financial statements

THERMAL ENERGY INTERNATIONAL INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1 GOVERNING STATUTES AND NATURE OF OPERATIONS

The Company was incorporated under the Ontario Business Corporations Act on May 22, 1991 and is primarily engaged in the development, engineering and supply of pollution control and heat recovery systems.

2 GOING CONCERN

The Company incurred losses from operations in the quarters and six months ended November 30, 2008 and 2007.

The Company's ability to meet its obligations as they fall due is dependent upon any combination of the following: the continued financial support of its shareholders, its ability to arrange long-term financing, its ability to generate sufficient cash from operations and its ability to operate with a gross margin.

The financial statements have been prepared on the going concern basis, which assumes the realization of assets and the satisfaction of liabilities in the normal course of business. These financial statements do not include any adjustments to the carrying value or classification of assets and liabilities, nor to the results of operations, should the Company not continue to operate as a going concern.

3 BASIS OF PRESENTATION AND ACCOUNTING CHANGES

The accompanying interim unaudited consolidated financial statements of Thermal Energy International Inc. have been prepared by management in accordance with Canadian generally accepted accounting principles applicable to interim consolidated financial statements and do not include all the information required for complete financial statements. The interim unaudited consolidated financial statements and accompanying notes should be read in conjunction with the audited consolidated financial statements and accompanying notes for the year ended May 31, 2008. These interim consolidated financial statements are also prepared in accordance with the accounting policies described in the Company's audited consolidated financial statements for the year ended May 31, 2008 except for the changes in accounting policies, and new accounting policies adopted and described below.

Inventories

Inventories are valued at the lower of cost and net realizable value after making due allowance for obsolete and slow-moving items. Cost includes all direct costs and an appropriate proportion of fixed and variable overheads where applicable.

Amortization

Property, plant and equipment is recorded at cost. Amortization is computed using the following annual rates and methods:

Plant and equipment	25% declining balance
---------------------	-----------------------

4 BUSINESS ACQUISITION

On July 1, 2008 the Company acquired the net assets of Gardner Energy Management Limited of Bristol, England, a company engaged in the condensate return solutions business, for a total cash consideration of \$5,411,245, including acquisition costs. An additional payment of up to £1,300,000 sterling may be made in cash and shares over a three-year period based on Gardner Energy Management Limited meeting certain performance targets.

This transaction was accounted for using the purchase method and the results of operations are included in the financial statements from the acquisition date. The purchase price allocation is as follows:

	July 1, 2008
	\$
Net assets acquired	
Current assets	1,649,363
Property, plant and equipment	50,202
Goodwill	4,804,213
	6,503,778
Current liabilities assumed	1,107,210
Non-controlling interest	(14,677)
Net assets acquired	5,411,245

THERMAL ENERGY INTERNATIONAL INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

5 SHORT-TERM INVESTMENTS

Short-term investments consist of excess cash invested in money market funds.

6 ACCOUNTS RECEIVABLE

	Nov 30, 2008	May 31, 2008
	\$	\$
Trade	1,295,832	438,592
Commodity taxes	93,114	145,928
Directors and Officers	46,565	34,500
Other	21,354	8,551
	1,456,865	627,571

7 PROPERTY, PLANT AND EQUIPMENT

	Nov 30, 2008		May 31, 2008	
	Cost	Accumulated Amortization	Cost	Accumulated Amortization
	\$	\$	\$	\$
Plant and equipment	72,209	55,356		
Furniture and fixtures	109,361	94,066	81,671	66,330
Laboratory equipment	52,857	24,122	52,857	21,073
Computers	260,675	213,850	157,861	144,787
Software	33,214	19,285	16,971	14,525
Leasehold improvements	21,401	21,401	21,401	18,980
	549,717	428,080	330,761	265,695
Accumulated amortization	(428,080)		(265,695)	
Net book value	121,637		65,066	

8 NET INVESTMENT IN LEASE

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

	Nov 30, 2008	May 31, 2008
	\$	\$
Total minimum lease payments receivable	3,347,985	3,605,747
Unearned income	1,280,290	1,429,807
	2,067,695	2,175,940
Less: current portion	(249,159)	(227,034)
	1,818,536	1,948,906

Future minimum lease payments receivable under the sales-type lease are as follows:

	\$
2009	358,210
2010	615,972
2011	615,972
2012	615,972
2013	615,972
2014	525,887
	3,347,985

THERMAL ENERGY INTERNATIONAL INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

9 BANK LOAN

At November 30, 2008, the Company had two bank loans aggregating \$924,966. The first loan has an authorized amount of \$2,500,000. At November 30, 2008 this loan, secured by term deposits, accounts receivable and a general security agreement, with interest rate at prime plus 0.25%, amounted to \$658,667 (May 31, 2008 - \$908,667). Prime rate at November 30, 2008 was 4.00%. In accordance with the loan agreement, the Company is subject to certain loan covenants and must meet certain financial ratios. At November 30, 2008 not all financial covenants were met.

At November 30, 2008, the second loan amounted to \$266,299 (May 31, 2008 - \$Nil). It is secured by certain trade debts of a subsidiary and carries a service charge of 0.805% of gross debts subject to a minimum annual charge of approximately \$30,000 and an interest rate of 1.95% over the United Kingdom bank base rate. At November 30, 2008 the United Kingdom bank rate was 3.0%.

10 RELATED PARTY TRANSACTIONS

Related party transactions, in the normal course of operations, are measured at the exchange value which represents the amounts established and agreed upon by both parties.

	November 30, 2008	November 30, 2007
Balances owing to/from directors		
Accounts receivable	\$38,500	-
Loans receivable	\$354,647	\$49,647
Accrued liabilities	\$26,250	\$22,500
Directors share options and warrants outstanding at November 30, 2008		
Issued	3,500,000	4,000,000
Exercisable	2,711,000	3,461,000
Warrants outstanding	37,500	-
Balances owing from officers		
Accounts receivable	\$8,000	-
Loans receivable	\$278,800	-
Officers share options and warrants outstanding at November 30, 2008		
Issued	-	1,993,000
Exercisable	-	1,954,000
Transactions with directors and officers were as follows:		
Directors fees for services	\$31,500	\$36,000
Officers fees for services	\$66,000	\$102,000
Shares issued to Directors	800,000	287,500
Shares issued to officers	-	-

Amounts due to the past President have no fixed repayment terms and are non-interest bearing.

THERMAL ENERGY INTERNATIONAL INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

11 CAPITAL STOCK AND CONTRIBUTED SURPLUS

	Quarter Ended Nov 30, 2008	
	# Shares	\$
Authorized		
Unlimited number of Class A common shares, no par value		
Unlimited number of Series 1 preferred shares, voting only		
In the case of dissolution of the Company at \$0.01 per share and convertible to common shares on a 1 to 1 basis at the rate of 20% of the number originally issued per year.		
Class A Common shares issued		
Balance, beginning of quarter	167,483,922	35,222,330
Fair value of options exercised by loan from contributed surplus (i)	-	35,000
Issued as a result of the exercise of options for loans (ii)	250,000	65,000
	167,733,922	35,322,330
Less: loans outstanding to assist a shareholder in purchasing capital stock (ii)		(856,353)
Share issue costs		(1,859,424)
Balance, end of quarter	167,733,922	32,606,553

	Year to Date Nov 30, 2008		Year Ended May 31, 2008	
	# Shares	\$	# Shares	\$
Class A Common shares issued				
Balance, beginning of period	99,052,104	20,122,830	90,918,419	17,573,323
Issued in settlement of liabilities	50,000	17,500	350,685	104,848
Issued for cash, net of flow through share tax benefit (i)	68,281,818	15,093,000	4,190,000	1,867,359
Issued as a result of the exercise of options for loans (ii)	350,000	89,000	3,593,000	577,300
	167,733,922	35,322,330	99,052,104	20,122,830
Less: loans outstanding to assist shareholders in purchasing capital stock (ii)		(856,353)		(643,751)
Share issue costs		(1,859,424)		-
Balance, end of period	167,733,922	32,606,553	99,052,104	19,479,079

(i) In fiscal 2008, the Company renounced expenditures of \$615,000 (2007 - \$540,000) from 4,190,000 (2007 - 3,484,334) flow-through common shares issued during the respective fiscal years. The resulting future income tax recovery of \$200,000 (2007 - \$195,000) was charged against capital stock as share expenses.

	Quarter ended November 30		Year to date November 30	
	2008	2007	2008	2007
Loans to exercise options				
Directors and officers	65,000	-	89,000	-

Loans were extended to directors and officers to acquire shares of the Company through the exercise of options. These loans are for a two-year period with an interest rate of 5%. The borrower's liability in respect of these loans shall at all times be limited to the value of the underlying shares for which the loan was granted. They can be repaid in part or in full at any time within the two year period at which time the shares with an equivalent value to the repayment will be released to the borrower by the Company.

(iii) Repayments made on these loans during the quarter and six months ended November 30, 2008 and 2007 were \$nil.

	Loans to acquire shares	
	Nov 30, 2008	May 31, 2008
	\$	\$
President	124,647	124,647
Directors and Officers	450,800	361,800
Other shareholders	280,906	157,304
	856,353	643,751

THERMAL ENERGY INTERNATIONAL INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Stock-based compensation on these loans was estimated using the Black-Scholes option pricing model with the following assumptions:

	Loans to exercise options		Loans to acquire shares	
	Quarter ended Nov 30		Quarter ended Nov 30	
	2008	2007	2008	2007
Weighted average assumptions:				
Expected dividend	0%	-	-	-
Expected volatility	79%	-	-	-
Risk-free interest rate	2.50%	-	-	-
Expected option life in years	2.0	-	-	-

	Loans to exercise options		Loans to acquire shares	
	Year to date Nov 30		Year to date Nov 30	
	2008	2007	2008	2007
Weighted average assumptions:				
Expected dividend	0%	-	0%	0%
Expected volatility	81%	-	82%	80%
Risk-free interest rate	2.50%	-	2.50%	4.50%
Expected option life in years	2.0	-	1.0	1.0

The Company has a five-year licensing and purchasing agreement with Mabarex for their Dry-Rex™ system ending September 8, 2011. Under the terms of this agreement, the Company is required to issue 125,000 common shares at \$0.16 each to Mabarex for each of the first two contracts to use the Dry-Rex™ system.

In addition, the Company is committed to issue 539,000 options to directors to purchase common shares at \$0.16 per share, based on Company performance and which will expire on December 20, 2009.

Warrants

(a) In June 2008 the Company completed a private placement. Part of the share issue cost was the issue of non-transferable warrants to the lead broker. Activity in share purchase warrants was as follows:

	Year to date Nov 30, 2008		Year to date Nov 30, 2007	
	# Warrants	Weighted Average Exercise Price	# Warrants	Weighted Average Exercise Price
		\$		\$
Balance, beginning of period	8,788,501	0.40	14,480,390	0.35
Issued	5,236,363	0.22	-	-
Exercised	-	-	(312,828)	0.33
Expired	(1,249,084)	0.30	(3,153,666)	0.35
Balance, end of period	12,775,780	0.34	11,013,896	0.35

(b) The following table summarizes the status of warrants outstanding at November 30, 2008:

Warrants Outstanding	Exercise Price \$	Expiry Date
324,000	0.30	To December 6, 2008
281,250	0.30	To December 29, 2008
4,166,667	0.40	To May 23, 2009
1,250,000	0.40	To May 29, 2009
1,517,500	0.50	To December 7, 2009
5,236,363	0.22	To June 20, 2010
<u>12,775,780</u>		

THERMAL ENERGY INTERNATIONAL INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Contributed surplus

	Quarter Ended Nov 30, 2008 \$	Year to Date Nov 30, 2008 \$	Year Ended May 31, 2008 \$
Balance, beginning of period	2,252,018	1,528,414	1,881,487
Stock-based compensation	56,104	177,508	495,786
Share issue costs	-	636,200	-
	2,308,122	2,342,122	2,377,273
Fair-value of options exercised and transferred to capital stock	35,000	69,000	848,859
Balance, end of period	2,273,122	2,273,122	1,528,414

12 COMMITMENTS

The Company is committed under the terms of operating leases for premises and office equipment contracts with various expiry dates in the following amounts:

	\$
2009	136,800
2010	193,500
2011	92,600
2012	78,600
2013	69,300
Total	570,800

13 SHARE OPTION PLAN

The Company established the Company's Share Option Plan applicable to Directors, Officers and full-time and part-time employees of the Company. In the plan, the aggregate number of options may not exceed 20% of the outstanding shares and the total number of shares to be optioned to any optionee may not exceed 5% of the number of issued and outstanding shares as at the option granting date. The options are granted with an exercise price equal to the market value of the common shares of the Company at the date of grant, less any permissible discounts, and may be exercised at any time after the vesting date, not to exceed five years from the date of granting. Vesting period for options granted is at the discretion of the Board of Directors. Options granted in the quarters and six months ended November 30, 2008 and 2007 had vesting periods ranging from four to twelve months.

(a) Activity in stock options was as follows:

	Quarter Ended Nov 30, 2008		Quarter Ended Nov 30, 2007	
	# Options	Weighted Average \$	# Options	Weighted Average \$
Outstanding, beginning of quarter	5,875,000	0.22	8,643,000	0.19
Granted	250,000	0.25	100,000	0.34
Exercised	(250,000)	0.26	(192,857)	0.21
Forfeited	-	-	-	-
Expired	-	-	-	-
Outstanding, end of quarter	5,875,000	0.22	8,550,143	0.19
	Year to date Nov 30, 2008		Year to date Nov 30, 2007	
	# Options	Weighted Average \$	# Options	Weighted Average \$
Outstanding, beginning of period	5,857,143	0.21	8,368,000	0.17
Granted	625,000	0.30	850,000	0.37
Exercised	(450,000)	0.25	(667,857)	0.16
Forfeited	(57,143)	0.21	-	-
Expired	(100,000)	0.24	-	-
Outstanding, end of period	5,875,000	0.22	8,550,143	0.19
Number of options exercisable as at November 30	4,672,000		7,788,643	

THERMAL ENERGY INTERNATIONAL INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Options exercised during the period were as follows:

	Quarter ended Nov 30, 2008		Quarter ended Nov 30, 2007	
	# shares	\$	# shares	\$
Employees	-	-	142,857	30,000
Directors	250,000	65,000	-	-
Consultants	-	-	50,000	11,000
	250,000	65,000	192,857	41,000

	Year to date Nov 30, 2008		Year to date Nov 30, 2007	
	# shares	\$	# shares	\$
Employees	200,000	48,000	317,857	54,000
Directors	250,000	65,000	250,000	32,500
Consultants	-	-	100,000	21,000
	450,000	113,000	667,857	107,500

In the six months ended November 30, 2008, 350,000 options were exercised in consideration of loans receivable of \$89,000 (2007 – \$Nil) and 100,000 options were exercised for cash of \$24,000 (2007 – 142,857 for debt and 525,000 for cash).

(b) The following options are outstanding and/or exercisable at November 30, 2008:

Number of Options Outstanding	Number of Options Exercisable	Exercise Price Per Share \$	Expiry Date
3,000,000	2,422,000	0.16	December 20, 2009
500,000	500,000	0.20	March 15, 2010
350,000	350,000	0.37	June 11, 2010
300,000	300,000	0.35	June 15, 2010
100,000	100,000	0.43	July 20, 2010
500,000	500,000	0.20	January 25, 2011
250,000	250,000	0.285	April 29, 2011
250,000	250,000	0.27	May 16, 2011
375,000		0.33	August 15, 2011
250,000		0.25	September 9, 2011
5,875,000	4,672,000		

THERMAL ENERGY INTERNATIONAL INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

c) Stock-based compensation

The fair value of options granted was estimated using the Black-Scholes option pricing model with the following weighted average assumptions:

	Quarter ended November 30		Year to date November 30	
	2008	2007	2008	2007
Expected dividend	0.00%	0.00%	0.00%	0.00%
Expected volatility	72%	98%	76%	96%
Risk-free interest rate	2.50%	4.50%	2.50%	4.50%
Expected option life in years	2.4	2.4	2.4	2.4

Stock-based compensation expense included the following amounts:

	Quarter ended November 30		Year to date November 30	
	2008	2007	2008	2007
Employees	56,104	123,020	116,088	257,020
Consultants	-	9,014	5,320	28,814
Shareholders	-	-	56,100	-

14 INFORMATION INCLUDED IN OPERATIONS

	Quarter ended Nov 30		Year to date Nov 30	
	2008	2007	2008	2007
	\$	\$	\$	\$
Interest expense	39,058	697	58,753	3,087

THERMAL ENERGY INTERNATIONAL INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

15 SEGMENTED INFORMATION

In the quarter and six months ended November 30, 2008 the Company operated in the energy conservation and environmental compliance (air) industry in North America and Europe and was also engaged in the start-up phase of similar operations in China. Within this business segment, the Corporation markets, sells, engineers, fabricates, constructs, installs and supports three retrofit technology lines – waste energy recovery solutions, air emission control solutions and condensate return system solutions. Assets are located in Canada and Europe.

The Company operated in three reportable segments in the quarter and six months ended November 30, 2008 (one in 2007). In the waste energy recovery and air emission control business, customers finance these projects entirely from their own resources or through the Company's Thermal-AUD™ system whereby the Company finances the project and leases back the facility to the customer. This gives rise to two reportable segments. The third segment is in the condensate return system solutions business through its acquisition of Gardner Energy Management Limited (GEM™) on July 1, 2008. These three reportable segments are detailed below:

	Quarter Ended November 30, 2008		
	Customer financed contracts and other \$	Thermal-AUD™ contract \$	GEM™ \$
Revenue from external customers	33,198	-	1,107,365
Inter-segment revenues	41,067	-	12,545
Interest and finance revenue	31,302	64,465	4
Interest expense and bank charges	1,849	9,071	23,948
Stock-based compensation charge	56,104	-	-
Amortization of property, plant and equipment	7,538	-	7,661
Segment loss (profit)	988,518	(14,327)	139,840
Expenditures for property, plant and equipment	8,874	-	11,812

	Year to date November 30, 2008		
	Customer financed contracts and other \$	Thermal-AUD™ contract \$	GEM™ \$
Revenue from external customers	535,022	-	556,494
Inter-segment revenues	69,734	-	14,945
Interest and finance revenue	66,309	149,517	18
Interest expense and bank charges	3,708	20,330	41,724
Stock-based compensation charge	177,508	-	-
Amortization of property, plant and equipment	16,131	-	10,759
Segment loss (profit)	1,638,866	(56,953)	(131,496)
Segment assets	13,143,164	2,134,033	1,497,247
Expenditures for property, plant and equipment	25,318	-	11,812

THERMAL ENERGY INTERNATIONAL INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Reconciliation to financial statements	Quarter ended Nov 30, 2008	Year to date Nov 30, 2008
	\$	\$
Revenues		
Total revenues for reporting segments	1,194,175	2,283,560
Elimination of inter-segment revenues	(53,612)	(84,679)
Total company revenues	1,140,563	2,198,881
Loss		
Total loss for reported segments	834,331	1,450,417
Exchange translation adjustment of net Investment in self-sustaining foreign operation	40,146	68,304
Net loss and Other comprehensive loss	874,477	1,518,721
Assets		
Total assets for reported segments		16,774,444
Elimination of inter-segment receivables		(2,153,681)
Total assets		14,620,763

Other significant items	Quarter ended November 30, 2008		
	Segment totals	Adjustments	Company totals
	\$	\$	\$
Interest revenue	31,306	-	31,306
Interest expense and bank charges	34,868	-	34,868
Finance revenue	64,465	-	64,465
Stock-based compensation charge	56,104	-	56,104
Amortization of property, plant and equipment	15,199	-	15,199
Expenditures for property, plant and equipment	20,686	-	20,686
Other significant items			
	Segment totals	Adjustments	Company totals
	\$	\$	\$
Interest revenue	65,327	-	65,327
Interest expense and bank charges	65,762	-	65,762
Finance revenue	149,517	-	149,517
Stock-based compensation charge	177,508	-	177,508
Amortization of property, plant and equipment	26,890	-	26,890
Expenditures for property, plant and equipment	37,130	-	37,130
Goodwill	4,804,213	-	4,804,213

Geographic Segments	Quarter ended	Year to date	As at
	Nov 30, 2008	Nov 30, 2008	Nov 30, 2008
	Revenues	Revenues	Property, plant and equipment
	\$	\$	\$
Canada	26,740	31,629	74,253
United States	33,643	537,896	-
Europe	1,080,180	1,629,356	47,384
Total	1,140,563	2,198,881	121,637

Revenues from outside customers are attributed to the geographic segments based on the location of the project.

THERMAL ENERGY INTERNATIONAL INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

16 FINANCIAL RISKS

Interest rate risk

The Company has contracted a short-term bank loans bearing floating rates of interest. These financial instruments expose the Company to risk in the event market interest rates fluctuate.

Foreign exchange risk

The Company is exposed to foreign exchange risk as follows:

	November 30, 2008			May 31, 2008
	US\$	£	Euros	US\$
Cash	15,767	40,682	886	7,115
Short-term investments	200	-	-	200
Accounts receivable	331,231	258,291	220,316	394,798
Inventories	-	282,102	10,807	-
Bank loans	-	82,633	74,174	-
Accounts payable	276,774	53,556	21,857	824,252
Accrued liabilities	-	128,519	27,653	-

The Company does not enter into arrangements to hedge its foreign exchange risk.

Credit risk

The financial instruments that potentially expose the Company to credit risk are accounts receivable and loans outstanding to assist directors, officers and shareholders in purchasing capital stock.

Liquidity risk

Liquidity risk management serves to maintain a sufficient amount of cash and cash equivalents and to ensure that the Company has financing sources such as bank loans for a sufficient authorized amount. The Company continues to actively seek external financing to ensure it has the necessary funds to fulfill its obligations.

Fair value of financial instruments

Given that they will mature shortly, the fair value of short-term financial assets and liabilities are equivalent to their carrying amount.

17 COMPARATIVE AMOUNTS

Certain 2007 amounts have been reclassified to conform with the current year's presentation.

18 CONTINGENCY

On October 20, 2005 the Company announced that the voluntary mediation between the Company and its past President had ended without resolution. On October 25, 2005 the Company had been served with a statement of claim for \$2.3 million from its past President. On December 2, 2005 the Company had filed its statement of defence and had filed a counterclaim seeking damages from the past President in the amount of \$5.4 million. As the ultimate resolution of the lawsuits cannot be reasonably estimated, no provision has been recorded in the accounts.

19 RECENTLY ISSUED ACCOUNTING STANDARDS NOT YET IMPLEMENTED

Goodwill

Section 3064 establishes standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets by profit-oriented companies. It clarifies the recognition of intangible assets and deals with the recognition of internally generated intangible assets.

The Company will implement these new standards in its first quarter of fiscal year 2010 and is currently evaluating the impact of their adoption on its consolidated financial statements.

THERMAL ENERGY INTERNATIONAL INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS