Draganfly Inc. (formerly Drone Acquisition Corp.)

Management's Discussion and Analysis

For the year ended December 31, 2019

Special Note Regarding Forward Looking Information

This Management Discussion & Analysis ("MD&A") is intended to provide readers with the information that management believes is required to gain an understanding of the current results of Draganfly Inc. (the "Company" or "Draganfly") and to assess the Company's future prospects. Accordingly, certain sections of this report contain forward-looking statements that are based on current plans and expectations. These forward-looking statements are affected by risks and uncertainties that are discussed in this document and that could have a material impact on future prospects. Readers are cautioned that actual events and results will vary.

In this MD&A we describe certain income and expense items that are unusual or non-recurring. There are terms not defined by International Financial Reporting Standards (IFRS). Our usage of these terms may vary from the usage adopted by other companies. Specifically, *Gross profit, Gross margin* and *Cash flow from operations* are undefined terms by IFRS. We provide this detail so that readers have a better understanding of the significant events and transactions that have had an impact on our results.

Certain statements in the MD&A, other than statements of historical fact, may include forward-looking information that involves various risks and uncertainties. These include, without limitation, the Company's current and planned operations in the technology sector and the expected results of new operations and new clients. These statements are based on current expectations involving a number of risks and uncertainties related to all aspects of the technology sector. These risks and uncertainties include, but are not restricted to, continued increased demand for the Company's products, the Company's ability to maintain its technological and competitive advantages, the Company's ability to attract and retain key employees, the ability of the Company to take advantage of its intellectual property, the Company's ability to raise capital on acceptable terms when needed and the availability of key suppliers and contractors. These uncertainties may cause actual results to differ from information contained herein. There can be no assurance that such statements will prove to be accurate. Actual results and future events could differ materially from those anticipated in such statements. These forward-looking statements are based on the estimates and opinions of Management on the dates they are made and are expressly qualified in their entirety by this notice. The reader is cautioned not to rely on these forward-looking statements. The Company assumes no obligation to update forward-looking statements should circumstances or Management's estimates or opinions change except as required by securities laws.

The following MD&A is presented and dated as of April 24, 2020 and should be read in conjunction with the audited consolidated financial statements and related notes for the year ended December 31, 2019. The Company's audited consolidated financial statements have been prepared on the "going concern" basis, which presumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future.

The operations of the Company have been primarily funded through internally generated cashflow and private placements of equity and convertible debentures. The continued operations of the Company are dependent on the Company's ability to generate profitable operations in the future, develop and execute a sufficient financing plan for future operations and receive continued financial support from shareholders and other providers of finance.

The consolidated financial statements do not reflect the adjustments, if any, or changes in presentation that may be necessary should the Company not be able to continue on a going concern basis.

All currency amounts in the accompanying financial statements and this management discussion and analysis are in Canadian dollars unless otherwise noted.

The recent outbreak of the coronavirus, also known as "COVID-19", has spread across the globe and is impacting worldwide economic activity. Conditions surrounding the coronavirus continue to rapidly evolve and government authorities have implemented emergency measures to mitigate the spread of the virus. These measures, which include the implementation of travel bans, self-imposed quarantine periods, and social distancing, have caused material disruption to business globally resulting in an economic slowdown. Global equity markets have experienced significant volatility and weakness. Governments and central banks have reacted with significant monetary and fiscal interventions designed to stabilize economic conditions.

There are significant uncertainties with respect to future developments and impact to the Company related to the COVID-19 pandemic, including the duration, severity, and scope of the outbreak and the measures taken by governments and businesses to contain the pandemic. While the impact of COVID-19 is expected to be temporary, the current circumstances are dynamic and the impacts of COVID-19 on our business operations cannot be reasonably estimated at this time. At the date of this MD&A, the outbreak and the related mitigation measures have had the following impacts on the Company's operations, among others: temporary closure of business locations, supply chain issues, and decrease in sales. The extent to which these events may impact the Company's business activities will depend on future developments, such as the ultimate geographic spread of the disease, the duration of the outbreak, travel restrictions, business disruptions, and the effectiveness of actions taken in Canada and other countries to contain and treat the disease. These events are highly uncertain and as such, the Company cannot determine the ultimate financial impacts at this time. Any deterioration in the current situation could have an adverse impact on our business, results of operations, financial position, and cash flows in 2020.

Non-GAAP Measures and Additional GAAP Measures

Throughout this document, reference is made to "gross margin" and "working capital", which are non-IFRS measures. Management believes that gross margin, defined as revenue less operating expenses, is a useful supplemental measure of operations. Management believes that working capital, defined as current assets less current liabilities, is an indicator of the Corporation's liquidity and its ability to meet its current obligations. Readers are cautioned that these non-IFRS measures may not be comparable to similar measures used by other companies. Readers are also cautioned not to view these non-IFRS financial measures as an alternative to financial measures calculated in accordance with International Financial Reporting Standards ("IFRS").

Core Business and Strategy

Draganfly creates quality, cutting-edge unmanned vehicle systems and software that revolutionize the way people do business. The Company is incorporated under the British Columbia Business Corporations Act and has its head office at 2108 St. George Avenue, Saskatoon, SK, S7M 0K7 and its registered office is located at 2300 – 550 Burrard Street, Vancouver, BC, V6C 2B5.

Recognized as being at the forefront of technology for two decades, Draganfly is an award-winning, industry-leading manufacturer, contract engineering, and product development company within the commercial UAV (unmanned aerial vehicles) space, serving the public safety, agriculture, industrial inspections, and mapping and surveying markets. Draganfly is a company driven by passion, ingenuity, and the need to provide efficient solutions and first-class services to its customers around the world with the goal of saving time, money, and lives.

Founded in 1998, Draganfly is recognized as the first commercial multi-rotor manufacturer and has a legacy for its innovation and superior customer service. The company has sold products and services to over 50 countries.

Draganfly can provide its customers with an entire suite of products and services that include: quad-copters, fixed-wing aircrafts, ground based robots, hand held controllers, flight training, and software used for tracking, live streaming, and data collection. The integrated UAV system is equipped for automated take-offs and landings with altitude and return to home functions as well as in-house created survey software. Draganfly's standard features combined with custom fit camera payloads ranging from multi-spectral, hyper-spectral, LIDAR, thermal, and infrared allows Draganfly to offer a truly unique solution to clients. Draganfly has also partnered with companies such as Waterloo based, Dejero, who provide a live streaming solution that the Company can offer to its customers and share in monthly usage fees.

With 18 fundamental UAV patents in the portfolio, Draganfly will continue to expand and grow their intellectual property docket.

Historically, the main business of the Company was to operate as a manufacturing company offering commercial UAVs directly to its customer base across various industry verticals. The Company is now doing more engineering procurement for certain customers in a vertical that is not currently served, such as military applications. The rationale is three-fold: engage in long term contracts that tend to be recurring in nature, gain exposure to an industry that the Company otherwise did not have access to, and leverage our innovation learnings into other products that can be sold in other industries.

Draganfly works with its customers to customize a product or platform from idea research and development (R&D) to completion and testing. A work plan is created with timelines and budget which includes materials, travel, testing, and engineering time. This plan is signed off on by the customer before work begins. To date, the majority of this work is considered proprietary and secret in nature.

The Company had done very little outbound sales and marketing promotional activities and yet customers around the world were reaching out to the Company through its website which is still is primary method of selling. It became evident to Management that resources needed to be raised to execute a carefully designed sales and marketing strategy to capitalize on industry demand for its product and services.

Management determined in mid-2018 the best course of action to secure additional capital, grow its brand and expand its reach was to secure a public listing on a reputable exchange. On January 31, 2019, the Company and PrivCo entered into a Business Combination Agreement (the "BCA") providing for a three-cornered amalgamation (the "Amalgamation") among the Company, PrivCo, and a wholly-owned subsidiary of the Company (the "Subco"). As of August 15, 2019, the Amalgamation closed and the Company acquired all of the issued and outstanding common shares of the PrivCo (the "PrivCo Shares"). It was a condition of closing that the Company complete a private placement of 10,000,000 units (a "Unit") at a price of $0.50 per Unit, with each Unit consisting of one common share and one common share purchase warrant (a "Warrant"). Each Warrant will be exercisable into one common share of the resulting issuer at a price of $0.50 for 12 months. The Company completed a private placement of 14,051,499 units raising $7,025,749.50. It is a post-closing covenant of the BCA that the resulting issuer from the Amalgamation obtains a listing for its common shares (the "Listing") on the Canadian Securities Exchange (the "CSE"). The Company has changed its name from Drone Acquisition Corp. to Draganfly Inc. and is the parent company of the wholly owned subsidiary, Draganfly Innovations Inc., which is the amalgamated company with Subco.

Under the Amalgamation, PrivCo Shares were exchanged for ordinary shares of the Company ("Company Shares") on the basis of 1.794 Company Shares for each PrivCo Share held resulting in approximately 42,638,356 PrivCo Shares to be issued. Upon completion of the Amalgamation, holders of PrivCo warrants ("PrivCo Warrants") will be entitled to receive Company Shares in lieu of shares otherwise issuable prior to the effective date of the Amalgamation (the "Effective Date"), adjusted in accordance with the terms of the various agreements and certificates representing the said warrants.

Following the Amalgamation and pursuant to completion of certain conditions precedent, including receipt of all necessary director, shareholder, regulatory and Canadian Stock Exchange (CSE) approvals, the Company was listed on the CSE on November 5, 2019. The Company has incurred significant listing expenses to complete the process but will be well positioned to execute on its business plan.

Additional information relating to the Company may be found at the Company's website, www.draganfly.com.

2019 Highlights

- **2019 Total Revenues at $1,380,427 with contract engineering revenue of $1,131,488**

2019 was another milestone year for Draganfly. The company solidified its engineering services business to not only offset a reduction in manufactured goods due to industry pricing shifts created by Chinese competition but to make this its primary business. Although, the Company's products are still well regarded in the industry, the commercial UAV space as a whole has been impacted by lower priced consumer drones that can now offer similar functionality. The Company recognized their opportunity of engineering procurement for those customers that either choose not to buy Chinese UAVs or are restricted from doing so due to information sensitivity concerns. 2019 revenues were flat year over coming in at $1,380,427 versus $1,387,013 in the previous year. $1,131,488 represents engineering services work while the balance of revenue is from hardware sales.

- **Gross Margins Improve Due to Shift In Business Mix**

With the Company transitioned from being a pure play manufacturer to offering services, the gross margins improved 25.0%. The Company's total gross margin for 2019 was 84.1% vs 67.4% in 2018. Engineering services tends to have a much higher gross margin over manufacturing given lower material costs.

- **Company Focus Shifted from Pure Play Manufacturer To Offering Customized Solutions**

Given the Company's impressive history and deep engineering talent, a natural evolution was to outsource in-house capabilities to customers. Doing this leverages the Company's core skill set of innovation that tends to lead to future projects, bringing in more consistent revenue.

- **Company secures Engineering Procurement from clients in Canada and US**

Securing clients in this business line was key to its consistent revenue achieved by the Company in 2019. These clients were important for revenue and continued validation of the technology, but more importantly they demonstrate that the Company's customized product designs have global applicability.

- **Risks related to operations**

The Company's UAVs are sold in rapidly evolving markets. The commercial UAV market is in early stages of customer adoption. Accordingly, the Company's business and future prospects may be difficult to evaluate. The Company cannot accurately predict the extent to which demand for its products and services will increase, if at all. The challenges, risks and uncertainties frequently encountered by companies in rapidly evolving markets could impact the Company's ability to do the following:

- generate sufficient revenue to maintain profitability;
- acquire and maintain market share;
- achieve or manage growth in operations;
- develop and renew contracts;
- attract and retain additional engineers and other highly qualified personnel;
- successfully develop and commercially market new products;
- adapt to new or changing policies and spending priorities of governments and government agencies; and
- access additional capital when required and on reasonable terms.

Outlook and Guidance

This Outlook and Guidance contains forward-looking statements that the Corporation does not intend, and does not assume any obligation, to update, except as required by law. The forward-looking information and statements include:

- The current economic climate and its effect on the Company's client base business;
- The Company's ability to successfully acquire new customers;
- The Company's ability to successfully implement its technology;
- Management's assumptions regarding the sustainability of recurring revenue streams and the Company's expected profitability; and
- Management's outlook and guidance contains forward looking statements of the Company's ability to penetrate the US and international client base with its products and services and continue its penetration in the Canadian market.

Selected Annual Financial Information

The following selected financial data has been extracted from the audited consolidated financial statements, prepared in accordance with International Financial Reporting Standards, for the fiscal years indicated and should be read in conjunction with those audited financial statements.

For the year ended December 31,	**2019**	2018	2017
Total revenues	**$ 1,380,427**	$ 1,387,013	$ 829,394
Gross Profit (as a % of revenues)	**84.1%**	67.4%	47.9%
Net loss and comprehensive loss	**(11,095,057)**	(601,729)	(932,019)
Net loss per share ($)			
- Basic	**(0.23)**	(0.03)	(0.04)
- Diluted	**(0.23)**	(0.03)	(0.04)
Change in cash and cash equivalents	**2,349,954**	(27,547)	(71,466)
Total assets	**3,221,783**	504,825	626,307
Working capital	**2,037,906**	(4,353,261)	(3,788,207)
Total non-current liabilities	**93,073**	-	-
Shareholder's equity (deficiency)	**$ 2,191,353**	$ (4,132,609)	$ (3,531,280)
Number of shares outstanding	**69,670,613**	39,346,822	39,332,470

Results of Operations

Revenue

For the year ended December 31,	**2019**	2018
Product sales	**$ 248,939**	$ 423,705
Engineering services	**1,131,488**	963,308
Total revenue	**$ 1,380,427**	$ 1,387,013

Total revenue for the year ended December 31, 2019 decreased by $6,586 or 0.5% as compared to 2018. The decrease in revenue is due to the Company's shrinking product sales business partially offset by the continued increase in engineering services.

Cost of Goods Sold / Gross Margin

For the year ended December 31,		2019		2018
Cost of goods sold	$	(218,800)	$	(452,399)
Gross profit	$	1,161,627	$	934,614
Gross margin (%)		84.1%		67.4%

Gross profit is the difference between the revenue received and the direct cost of that revenue. Gross margin is gross profit divided by revenue and is often presented as a percent. As a result of reduced product sales, the Company's Gross Profit increased by $227,013 or 24.3%. As a percentage of sales, gross margin increased from 67.4% in 2018 to 84.1% in 2019. Again, the higher gross margins realized in 2019 was the result of a major shift to engineering service work which has a higher gross margin than the legacy manufacturing gross margin.

Selling, General, and Administrative (SG&A)

For the year ended December 31,		2019		2018
Office and Miscellaneous	$	2,127,632	$	328,292
Professional Fees		524,101		131,028
Research and Development		16,883		16,158
Share-based compensation		761,559		-
Travel		30,896		17,817
Wages and salaries		989,083		984,179
Total	$	4,450,154	$	1,477,474

Selling, General and Administrative expenses in 2019 increased by 201.2%, from $1,477,474 in 2018 to $4,450,154 in 2019. The largest contributor to the increase is marketing and investor relations expenses.

Share-Based Compensation

For the year ended December 31,		2019		2018
Share-based compensation	$	761,559	$	-

Stock options

The Company has adopted an incentive share compensation plan, which provides that the Board of Directors of the Company may from time to time, in its discretion, and in accordance with the CSE requirements, grant to directors, officers, employees and technical consultants to the Company, non-transferable stock options to purchase common shares. The total number of common shares reserved and available for grant and issuance pursuant to this plan shall not exceed 20% (in the aggregate) of the issued and outstanding common shares from time to time. The number of options awarded and underlying vesting conditions are determined by the Board of Directors in its discretion. Such options will be exercisable for a period of up to 10 years from the date of grant. The aggregate sales price (meaning the sum of all cash, property, notes, cancellation of debt, or other consideration received or to be received by the Company for the sale of the securities) or amount of common shares issued during any consecutive 12-month period will not exceed the greatest of the following: (i) U.S.$1,000,000; (ii) 15% of the total assets of the Company, measured at the Company's most recent balance sheet date; or (iii) 15% of the outstanding amount of the common shares of the Company, measured at the Company's most recent balance sheet date; and The number of common shares issuable pursuant to the exercise of options under the plan within a 12 month period to all eligible persons retained to provide investor relations activities (together with those common shares that are issued pursuant to any other share compensation arrangement) shall not, at any time, exceed 1% of the issued and outstanding common shares.

Authorized share capital

Unlimited number of common shares without par value.

Issued share capital

For the year ended December 31, 2019,

- Prior to the closing of the Amalgamation (Note 3), Draganfly Innovations issued 719,927 (pre-consolidation) common shares to a company controlled by a director of the Company for settlement of $799,341 in accounts payable and application of $153,566 in subscription receivable (Note 4).
- Prior to the closing of the Amalgamation (Note 3), Draganfly Innovations issued 1,114,827 (pre-consolidation) common shares with a value of $1,000,000 as transaction fees for the Amalgamation to related parties.
- On August 15, 2019, the Amalgamation (Note 3) was completed and the Company acquired, on a 1.794 for 1 basis, all issued and outstanding shares of Draganfly Innovations in exchange for 42,638,356 common shares of the Company.
- On August 15, 2019, the Company issued 45,325 common shares for settlement of $22,662 in trades payables at a value of $0.50 per share.
- On August 15, 2019, the Company issued 2,118,492 common shares for settlement of $740,000 in convertible debentures and interest. As a result of the settlement, the Company recognized loss on settlement of debt of $319,246 in the statement of loss and comprehensive loss.
- On August 23, 2019, the Company issued 316,940 common shares for exercise of share purchase warrants of the Company for proceeds of $8,833. As a result of the exercise, $212,909 from reserve was reclassification to share capital.
- On October 25, 2019, the Company issued 14,051,499 units per the private placement (Note 3). Each unit consists of one common share and one warrant. These warrants have an exercise price of $0.50 per warrant, each convert to one common share, and have a life of one year, expiring on October 25, 2020.

For the year ended December 31, 2018,

- The Company issued 8,000 shares for proceeds of $400 for exercise of warrants. In relation, $10,000 in equity reserve was reclassified to share capital.

Net and Comprehensive Loss

For the year ended December 31,		**2019**		2018
Loss from operations	**$**	**(3,338,163)**	$	(580,915)
Finance and other costs		**(171,905)**		(145,271)
Foreign exchange loss		**5,803**		2,971
Gain on disposal of assets		**28,651**		-
Gain on settlement of debt		**198,976**		-
Listing expense		**(7,804,859)**		-
Loss on write-off loan receivable		**(13,560)**		-
Other income		**-**		8,130
Scientific research and development tax credit		**-**		113,356
Net and comprehensive loss	**$**	**(11,095,057)**	$	(601,729)

For the year ended December 31, 2019, the Company recorded a comprehensive loss of $11,095,057 compared to a comprehensive loss of $601,729 in 2018. The increased loss was largely the result of a listing expense resulting from the amalgamation as well as increased marketing and investor relations expenses to create awareness of the Company. The Company received Scientific Research and Experimental Development tax credit in 2018.

Selected Quarterly Information

The following selected quarterly financial data has been extracted from the financial statements, prepared in accordance with International Financial Reporting Standards.

In Q4 2019, the Company recorded revenues of $491,520, an increase of $217,358 or 79.3% as compared to the equivalent quarter in 2018. Most of the increase can be attributed to higher billings on the contract engineering business which also greatly improved the gross margin at 91.4% vs 53.7% in Q4 2018. Although operating expenses increased significantly during Q4 2019 ($2,983,115) compared to $477,889 for the same period last year), operating costs for the previous other three 2018 quarters were much more in line with the three quarters in 2018. The increase in operating costs were primarily due to increased marketing and investor relations expenses.

	2019 Q4	2019 Q3	2019 Q2	2019 Q1
Revenue	**$ 491,520**	$ 450,943	$ 289,735	$ 148,229
Cost of goods sold	**$ (42,401)**	$ (71,043)	$ (49,147)	$ (56,209)
Gross profit	**$ 449,119**	$ 379,900	$ 240,588	$ 92,020
Gross margin – percentage	**91.4%**	84.2%	83.0%	62.1%
Operating expenses	**$ (2,983,115)**	$ (683,777)	$ (484,155)	$ (348,743)
Net loss	**$ (2,533,996)**	$ (303,877)	$ (243,567)	$ (256,723)
Other income (expense)	**$ 506,080**	$ (8,133,663)	$ (46,220)	$ (83,091)
Comprehensive loss	**$ (2,027,916)**	$ (8,437,540)	$ (289,787)	$ (339,814)

	2018 Q4	2018 Q3	2018 Q2	2018 Q1
Revenue	$ 274,162	$ 270,127	$ 440,346	$ 402,378
Cost of goods sold	$ (127,014)	$ (77,535)	$ (92,586)	$ (155,264)
Gross profit	$ 147,148	$ 192,592	$ 347,760	$ 247,114
Gross margin – percentage	53.7%	71.3%	79.0%	61.4%
Operating expenses	$ (477,886)	$ (329,744)	$ (374,274)	$ (333,625)
Net loss	$ (330,738)	$ (137,152)	$ (26,514)	$ (86,511)
Other income (expense)	$ (39,197)	$ 58,467	$ (47,521)	$ 7,437
Comprehensive income (loss)	$ (369,935)	$ (78,685)	$ (74,035)	$ (79,074)

Liquidity and Capital Resources

The Company's liquidity risk is on its loans, accounts payable and accrued liabilities, as it may encounter difficulty discharging its obligations. The Company attempts to mitigate this risk by managing its debt holders as well as ensuring there is capital coming into the company for its operations. As at December 31, 2019, the Company has a working capital of $2,037,906 (December 31, 2018 had a deficit of $4,353,261).

The Company considers the items included in capital to include shareholders' equity. The Company manages its capital structure and makes adjustments to it in light of changes in economic and business conditions, financing environment and the risk characteristics of the underlying assets. A $500,000 cash payment will be paid from the Company's available funds to close the Dronelogics share purchase agreement, noted below in Subsequent Events. Aside from this transaction and the regular business operations of managing its liabilities, the Company does not have any contracted or committed capital expenditures as of the date of these financial statements. The Company utilizes its credit card facilities from time to time to make various purchases for their operations. The Company will need to raise additional capital during the next twelve months and beyond to support current operations and planned development. Management intends to finance operating costs over the next twelve months with cash on hand and with the issuance of securities such as the private placement of common shares and convertible debentures. Further, in order to maintain or adjust its capital structure, the Company may issue new shares, new debt, or scale back the size and nature of its operations. The Company is not subject to externally imposed capital requirements. As at December 31, 2019, shareholders' equity was $2,191,353 and at December 31, 2018, shareholder's deficit was $4,132,609.

Subsequent Events

The following reportable events occurred subsequent to the year ended December 31, 2019:

- On January 31, 2020, the Company executed a share purchase agreement with the shareholders of Dronelogics Systems Inc. ("Dronelogics"), whereby the Company has agreed to acquire all of the issued and outstanding shares in the capital of Dronelogics, excluding the cinematography division, for a consideration of $2,000,000, plus the amount, if any, by which the estimated closing date working capital exceeds the target closing working capital (the "Transaction"). The consideration will be paid as follows:
    - $500,000 in cash, subject to working capital adjustment; and
    - 3,000,000 common shares in the capital of the Company at a deemed price of $0.50 per share.

  The shareholders of Dronelogics will enter into executive employment agreements with the Company. In addition, they will receive a nomination right to appoint one person to the board of directors of the Company for a period of two years from the Closing. The Transaction has been approved by the board of directors of the Company and Dronelogics. In connection with the Transaction, the Company will pay fees of $160,000 to certain advisors; consisting of $100,000 by way of 200,000 in shares at a deemed price of $0.50 per share and as to $60,000 in cash or shares at a deemed price of $0.50 per share. At Closing, the Company will issue: (i) additional shares to the shareholders, at a deemed price of $0.50 per share, in satisfaction of accrued management bonuses in connection with their services to Dronelogics; (ii) grant 445,000 incentive stock options to certain employees of Dronelogics pursuant to the Company's share compensation plan, exercisable at a price equal to closing price of the shares on the CSE on January 31, 2020. The options shall have a term of 10 years and vest in three equal tranches, on the first, second and third anniversaries of the date of grant, and (iii) award 375,000 RSUs to certain directors and officers of Dronelogics. RSUs were awarded to certain directors and officers of Dronelogics pursuant to the Company's share compensation plan. The RSUs shall vest in three equal tranches, on the first, second and third anniversaries of the date of award.

  Completion of the Transaction is subject to a number of closing conditions customary for a transaction of this nature, including the filing of required forms with the CSE.

- The recent outbreak of the coronavirus, also known as "COVID-19", has spread across the globe and is impacting worldwide economic activity. Conditions surrounding the coronavirus continue to rapidly evolve and government authorities have implemented emergency measures to mitigate the spread of the virus. These measures, which include the implementation of travel bans, self-imposed quarantine periods and social distancing, have caused material disruption to business globally resulting in an economic slowdown. Global equity markets have experienced significant volatility and weakness. Governments and central banks have reacted with significant monetary and fiscal interventions designed to stabilize economic conditions. There are significant uncertainties with respect to future developments and impact to the Company related to the COVID-19 pandemic, including the duration, severity and scope of the outbreak and the measures taken by governments and businesses to contain the pandemic. While the impact of COVID-19 is expected to be temporary, the current circumstances are dynamic and the impacts of COVID-19 on the Company's business operations cannot be reasonably estimated at this time. As at the financial statement approval date, the outbreak and the related mitigation measures have had the following impacts on the Company's operations, among others: temporary closure of business locations, supply chain issues, and decrease in sales. The extent to which these events may impact the Company's business activities will depend on future developments, such as the ultimate geographic spread of the disease, the duration of the outbreak, travel restrictions, business disruptions, and the effectiveness of actions taken in Canada and other countries to contain and treat the disease. These events are highly uncertain and as such, the Company cannot determine the ultimate financial impacts at this time. Any deterioration in the current situation could have an adverse impact on our business, results of operations, financial position and cash flows in 2020.

Off-Balance Sheet Arrangements

The Company has no material undisclosed off-balance sheet arrangements that have or are reasonably likely to have, a current or future effect on our results of operations, financial condition, revenues or expenses, liquidity, capital expenditures or capital resources.

Contractual Obligations

As of December 31, 2019, and as of the date of this MD&A, and in the normal course of business, the following is a summary of the Company's material obligations to make future payments, representing contracts, and other commitments that are known and committed.

On December 1, 2019, the Company entered into a lease agreement with a related party. The lease agreement is for a period of two years from December 1, 2019 to December 1, 2021 with the option to make six one-year extensions. Management believes that the Company will be at the current location for four years. The lease agreement is for $43,000 per annum or $3,583.33 on a monthly basis. Per IFRS 16, a right of use asset and a lease liability were established.

The Company's right-of-use asset relates to the lease of office space.

On adoption of IFRS 16, the group recognized lease liability which had previously been classified as 'operating leases' under IAS 17 Leases. These liabilities were measured at the present value of the remaining lease payments and discounted using the lessee's incremental borrowing rate as of January 1, 2019. The weighted average lessee's incremental borrowing rate applied to the lease liabilities on January 1, 2019 was 12%.

On December 1, 2019, the Company entered into an amendment for the lease agreement, where the lease was amended with a change in annual payments. As there was no change to the underlying asset, the modification was not accounted for as a separate lease.

The right-of-use asset was calculated as follows:

		Total
Cost		
Balance at January 1, 2019, on adoption of IFRS 16	$	131,634
Lease modification		27,905
Balance at December 31, 2019	**$**	**159,539**
Accumulated depreciation		
Balance at January 1, 2019, on adoption of IFRS 16	$	-
Charge for the period		29,545
Balance at December 31, 2019	**$**	**29,545**
Net book value:		
January 1, 2019, on adoption of IFRS 16	**$**	**131,634**
December 31, 2019	**$**	**129,994**

The lease liability was calculated as follows:

		Total
Balance at January 1, 2019, on adoption of IFRS 16	$	131,634
Interest expense		14,534
Lease payments		(38,000)
Lease modification		27,905
Balance at December 31, 2019	**$**	**136,073**
Which consists of:		
Current lease liability	$	43,000
Non-current lease liability		93,073
Balance at December 31, 2019	**$**	**136,073**

During the year ended December 31, 2019, the Company incurred rent and property tax expenses of $49,018 with a company controlled by the former owner of the Company.

Related Party Transactions

Key management personnel include those persons having authority and responsibility for planning, directing, and controlling the activities of the Company as a whole. The Company has determined that key management personnel consist of members of the Company's Board of Directors and corporate officers. During the years ended December 31, 2019 and 2018, there was no remuneration paid to key management personnel.

***Loans*:**

a) On July 17, 2015, the Company issued a note payable for $600,000 with the former owner of the Company. The note payable bears interest at 5% per annum, was due on December 1, 2015 and is secured against the intellectual property as at the effective date.

   During the year ended December 31, 2019, the Company repaid $378,770 (2018 - $nil). As at December 31, 2019, $nil (2018 - $364,655) in notes payable plus accrued interest is outstanding and in default. For the year ended December 31, 2019, the Company recognized interest expense of $15,153 (2018 - $17,748).

b) On December 17, 2015, the Company issued a $160,000 note payable to a company controlled by a director of the Company. During the year ended December 31, 2017, the balance outstanding of $160,000 was applied against a subscription receivable (note 3). This subscription receivable was settled in the year ended December 31, 2019.

c) During the year ended December 31, 2018, the Company issued into various promissory notes of $273,500 with a company controlled by a director of the Company. The promissory notes are interest bearing at 12% per annum, unsecured and due within 60 days from the date of advance.

   During the year ended December 31, 2019, the company repaid $290,973 (2018 - $37,086). As at December 31, 2019, $nil in promissory notes plus accrued interest is outstanding and is in default (2018 - $253,995). For the year ended December 31, 2019, the Company recorded interest expense of $13,860 (2018 - $17,581).

Key management compensation

Key management includes the Company's directors and members of the executive management team. Compensation awarded to key management for the year ended December 31, 2019 and 2018 included:

	December 31, 2019	December 31, 2018
Contract work	**$ 48,039**	$ -
Management fees to a company controlled by a former Director	**195,000**	-
Management fees to a company controlled by a Director	**177,000**	-
Salaries	**289,450**	280,000
Share-based payments	**480,158**	-
Total	**$ 1,189,647**	$ 280,000

Share Capital

Shares outstanding and dilutive instruments as at the date hereof are as follows:

Stock Options

The following is the summary of the Company's stock option activity:

	Number of Options	Weighted Average Exercise Price
Outstanding, December 31, 2017	300,000	$ 1.25
Expired	(300,000)	1.25
Outstanding, December 31, 2018	-	-
Granted	**3,725,000**	**0.50**
Outstanding, December 31, 2019	**3,725,000**	**$ 0.50**

During the year ended December 31, 2019,

- The Company granted 2,925,000 options to employees. Each option is exercisable at $0.50 per share for a period of 10 years from the grant date.
- The Company issued 800,000 options to consultants. Each option is exercisable at $0.50 per share for a period of 10 years from the grant date.

During the year ended December 31, 2018, the fair value of 300,000 expired options of $323,026 was reclassified from reserves to deficit.

As at December 31, 2019 the Company had the following options outstanding and exercisable:

Grant Date	Expiry Date	Exercise Price	Remaining Contractual Life (years)	Number of Options Outstanding	Number of Options Exercisable
October 30, 2019	October 30, 2029	$ 0.50	9.84	3,075,000	1,024,992
November 19, 2019	November 19, 2029	$ 0.50	9.89	650,000	83,333
				3,725,000	**1,108,325**

Restricted Share Units (RSUs)

The following is a summary of the Company's RSU activity:

	Number of RSUs
Outstanding, December 31, 2017 and 2018	-
Granted	**3,175,000**
Outstanding, December 31, 2019	**3,175,000**

During the year ended December 31, 2019,

- The Company issued 2,925,000 RSUs to employees
- The Company issued 250,000 RSUs to consultants

As at December 31, 2019 the Company had the following RSUs outstanding:

Grant Date	Number of RSUs Outstanding
October 30, 2019	2,925,000
November 19, 2019	250,000
	3,175,000

Warrants

The following is the summary of the Company's warrant activity:

	Number of Warrants		Weighted Average Exercise Price
Outstanding, December 31, 2017	784,232	$	0.30
Exercised	(14,352)		0.03
Outstanding, December 31, 2018	770,030	$	0.27
Warrants of the Company at time of Amalgamation (Note 3)	**4,000,000**		**0.10**
Expired	**(453,090)**		**0.03**
Exercised	**(316,940)**		**0.03**
Granted	**14,051,499**		**0.50**
Outstanding, December 31, 2019	**18,051,499**	**$**	**0.41**

As at December 31, 2019, the Company had the following warrants outstanding:

Date Issued	Expiry Date	Exercise Price	Number of Warrants Outstanding
February 4, 2019	February 4, 2021	$0.10	4,000,000
November 5, 2019	November 5, 2020	$0.50	14,051,499
			18,051,499

The weighted average remaining contractual life of warrants outstanding as of December 31, 2019 was 0.90 years (December 31, 2018 - 0.84 years).

Critical Accounting Policies and Estimates

Measurement Uncertainty (Use of Estimates)

The preparation of the financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and contingent liabilities at the date of the consolidated financial statements and reported amounts of revenues and expenses during the reporting period. Estimates and judgments are continuously evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. However, actual outcomes can differ from these estimates.

The key sources of estimation uncertainty that have a significant risk of causing material adjustment to the amounts recognized in the financial statements are:

a. SR&ED tax credits

The determination of the amount of the Alberta SR&ED tax credit receivable requires management to make calculations based on its interpretation of eligible expenditures in accordance with the terms of the programs. The reimbursement claims submitted by the Company are subject to review by the relevant government agencies. Although the Company has used its best judgment and understanding of the related program agreements in determining the receivable amount, it is possible that the amounts could increase or decrease by a material amount in the near-term dependent on the review and audit by the government agency.

b. Allowance for uncollectible trade and other receivables

The Company makes use of estimates when making allowances for uncollectible trade and other receivables. The Company evaluates each receivable at year end using factors such as age of receivable, payment history, and credit risk to estimate when determining if an allowance is required, and the amount of the allowance.

c. Share-based payment transactions

The Company measures the cost of share-based payment transactions with employees by reference to the fair value of the equity instruments. Estimating fair value for share-based payment transactions requires determining the most appropriate valuation model, which is dependent on the terms and conditions of the grant. This estimate also requires determining and making assumptions about the most appropriate inputs to the valuation model including the expected lives and forfeiture rates of the share options and volatility of the market value of the underlying shares.

Significant estimates and assumptions

The preparation of financial statements in accordance with IFRS requires the Company to use judgment in applying its accounting policies and make estimates and assumptions about reported amounts at the date of the financial statements and in the future. The Company's management reviews these estimates and underlying assumptions on an ongoing basis, based on experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Revisions to estimates are adjusted for prospectively in the period in which the estimates are revised.

Share-based payments

The cost of share-based payment transactions with directors, officers and employees are measured by reference to the fair value of the equity instruments. Estimating fair value for share-based payment transactions requires determining the most appropriate valuation model, which is dependent on the terms and conditions of the grant. This estimate also requires determining and making assumptions about the most appropriate inputs to the valuation model including the expected life, volatility, risk-free interest rate, expected forfeiture rate and dividend yield of the stock option.

Income taxes

Provisions for income taxes are made using the best estimate of the amount expected to be paid based on a qualitative assessment of all relevant factors. The Company reviews the adequacy of these income tax provisions at the end of each reporting period. However, it is possible that at some future date an additional liability could result from audits by tax authorities. Where the final outcome of these tax-related matters is different from the amounts that were initially recorded, such differences will affect the tax provisions in the period in which such determination is made. Deferred tax assets are recognized when it is determined that the company is likely to recognize their recovery from the generation of taxable income.

Inventories

Inventory is valued at the lower of cost and net realizable value. Net realizable value is determined with reference to the estimated selling price. The Company estimates selling price based upon assumptions about future demand and current and anticipated retail market conditions.

Contingencies

The assessment of contingencies involves the exercise of significant judgment and estimates of the outcome of future events. In assessing loss contingencies related to legal proceedings that are pending against the Company and that may result in regulatory or government actions that may negatively impact the Company's business or operations, the Company and its legal counsel evaluate the perceived merits of the legal proceeding or unasserted claim or action as well as the perceived merits of the nature and amount of relief sought or expected to be sought, when determining the amount, if any, to recognize as a contingent liability or when assessing the impact on the carrying value of the Company's assets. Contingent assets are not recognized in the annual financial statements.

Useful lives of equipment and intangible assets

Estimates of the useful lives of equipment and intangible assets are based on the period over which the assets are expected to be available for use. The estimated useful lives are reviewed annually and are updated if expectations differ from previous estimates due to physical wear and tear, technical or commercial obsolescence, and legal or other limits on the use of the relevant assets. In addition, the estimation of the useful lives of the relevant assets may be based on internal technical evaluation and experience with similar assets. It is possible, however, that future results of operations could be materially affected by changes in the estimates brought about by changes in the factors mentioned above. The amounts and timing of recorded expenses for any period would be affected by changes in these factors and circumstances. A reduction in the estimated useful lives of the equipment would increase the recorded expenses and decrease the non-current assets.

Other Significant judgments

The preparation of consolidated financial statements in accordance with IFRS requires the Company to make judgments, apart from those involving estimates, in applying accounting policies. The most significant judgments in applying the Company's consolidated financial statements include:

- The assessment of the Company's ability to continue as a going concern and whether there are events or conditions that may give rise to significant uncertainty;
- the classification of financial instruments;
- the assessment of revenue recognition using the five-step approach under IFRS 15 and the collectability of amounts receivable;
- the determination of whether a set of assets acquired and liabilities assumed constitute a business; and
- the determination of the functional currency of the company.

Foreign currency translation

The functional currency of each entity is measured using the currency of the primary economic environment in which that entity operates. The consolidated financial statements are presented in Canadian dollars which is the functional and presentation currency of the Company and its subsidiary.

Transactions and balances:

Foreign currency transactions are translated into functional currency using the exchange rates prevailing at the date of the transaction. Foreign currency monetary items are translated at the period-end exchange rate. Non-monetary items measured at historical cost continue to be carried at the exchange rate at the date of the transaction. Non-monetary items measured at fair value are reported at the exchange rate at the date when fair values were determined.

Exchange differences arising on the translation of monetary items or on settlement of monetary items are recognized in the statement of comprehensive loss in the period in which they arise, except where deferred in equity as a qualifying cash flow or net investment hedge.

Exchange differences arising on the translation of non-monetary items are recognized in other comprehensive income to the extent that gains and losses arising on those non-monetary items are also recognized in other comprehensive income. Where the non-monetary gain or loss is recognized in profit or loss, the exchange component is also recognized in profit or loss.

Share-based payments

The Company operates a stock option plan. Share-based payments to employees are measured at the fair value of the instruments issued and amortized over the vesting periods. Share-based payments to non-employees are measured at the fair value of goods or services received or the fair value of the equity instruments issued, if it is determined the fair value of the goods or services cannot be reliably measured, and are recorded at the date the goods or services are received. The corresponding amount is recorded to the option reserve. The fair value of options is determined using a Black–Scholes Option Pricing Model. The number of shares and options expected to vest is reviewed and adjusted at the end of each reporting period such that the amount recognized for services received as consideration for the equity instruments granted shall be based on the number of equity instruments that eventually vest. Amounts recorded for forfeited or expired unexercised options are transferred to deficit in the year of forfeiture or expiry. Amounts recorded for forfeited unvested options are reversed in the period the forfeiture occurs.

Share-based payment expense relating to cash-settled awards, including restricted share units is accrued over the vesting period of the units based on the quoted market value of Company's common shares. As these awards will be settled in cash, the expense and liability are adjusted each reporting period for changes in the underlying share price.

Restricted Share Units

The restricted share units ("RSUs") entitle employees, directors, or officers to cash payments payable upon vesting based on vesting terms determined by the Company's Board of Directors at the time of the grant. A liability for outstanding RSUs is measured at fair value on the grant date and is subsequently adjusted for changes in fair value at each reporting date until settlement. The liability is recognized on a graded vesting basis over the vesting period, with a corresponding charge to profit or loss.

Loss per share

Basic loss per share is calculated by dividing the loss attributable to common shareholders by the weighted average number of common shares outstanding in the period. For all periods presented, the loss attributable to common shareholders equals the reported loss attributable to owners of the Company. Diluted loss per share is calculated by the treasury stock method. Under the treasury stock method, the weighted average number of common shares outstanding for the calculation of diluted loss per share assumes that the proceeds to be received on the exercise of dilutive share options and warrants are used to repurchase common shares at the average market price during the period.

Financial instruments

All financial assets are initially recorded at fair value and classified into one of four categories: fair value through profit or loss ("FVTPL"), fair value through other comprehensive income ("FVTOCI") and at amortized costs. All financial liabilities are initially recorded at fair value and classified as either FVTPL or other financial liabilities. Financial instruments comprise cash and accounts payable and accrued liabilities.

a) Financial assets

<u>Classification and measurement</u>

The Company classifies its financial assets in the following categories: at fair value through profit or loss ("FVTPL"), at fair value through other comprehensive income ("FVTOCI") or at amortized cost. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

The classification of debt instruments is driven by the business model for managing the financial assets and their contractual cash flow characteristics. Debt instruments are measured at amortized cost if the business model is to hold the instrument for collection of contractual cash flows and those cash flows are solely principal and interest. If the business model is not to hold the debt instrument, it is classified as FVTPL. Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payments of principal and interest.

Equity instruments that are held for trading (including all equity derivative instruments) are classified as FVTPL, for other equity instruments, on the day of acquisition the Company can make an irrevocable election (on an instrument by-instrument basis) to designate them as at FVTOCI.

<u>Financial assets at FVTPL</u>
Financial assets carried at FVTPL are initially recorded at fair value and transaction costs are expensed in the income statement. Realized and unrealized gains and losses arising from changes in the fair value of the financial asset held at FVTPL are included in the income statement in the period in which they arise. Derivatives are also categorized as FVTPL unless they are designated as hedges.

Financial assets at FVTOCI
Investments in equity instruments at FVTOCI are initially recognized at fair value plus transaction costs. Subsequently they are measured at fair value, with gains and losses arising from changes in fair value recognized in other comprehensive income. There is no subsequent reclassification of fair value gains and losses to profit or loss following the derecognition of the investment.

Financial assets at amortized cost
Financial assets at amortized cost are initially recognized at fair value and subsequently carried at amortized cost less any impairment. They are classified as current assets or non-current assets based on their maturity date.

Impairment of financial assets at amortized cost
The Company recognizes a loss allowance for expected credit losses on financial assets that are measured at amortized cost. At each reporting date, the loss allowance for the financial asset is measured at an amount equal to the lifetime expected credit losses if the credit risk on the financial asset has increased significantly since initial recognition. If at the reporting date, the financial asset has not increased significantly since initial recognition, the loss allowance is measured for the financial asset at an amount equal to twelve month expected credit losses. For trade receivables the Company applies the simplified approach to providing for expected credit losses, which allows the use of a lifetime expected loss provision.

Impairment losses on financial assets carried at amortized cost are reversed in subsequent periods if the amount of the loss decreases and the decrease can be objectively related to an event occurring after the impairment was recognized.

Derecognition of financial assets
Financial assets are derecognized when they mature or are sold, and substantially all the risks and rewards of ownership have been transferred. Gains and losses on derecognition of financial assets classified as FVTPL or amortized cost are recognized in the income statement. Gains or losses on financial assets classified as FVTOCI remain within accumulated other comprehensive income.

b) Financial liabilities

The Company classifies its financial liabilities into one of two categories as follows:

Fair value through profit or loss (FVTPL) - This category comprises derivatives and financial liabilities incurred principally for the purpose of selling or repurchasing in the near term. They are carried at fair value with changes in fair value recognized in profit or loss.

Other financial liabilities - This category consists of liabilities carried at amortized cost using the effective interest method. Accounts payable and accrued liabilities, and convertible debentures, are included in this category. The Company derecognizes a financial liability when its contractual obligations are discharged, cancelled or expire.

Derecognition of financial liabilities
Financial liabilities are derecognized when its contractual obligations are discharged or cancelled, or expire. The Company also derecognizes a financial liability when the terms of the liability are modified such that the terms and/or cash flows of the modified instrument are substantially different, in which case a new financial liability based on the modified terms is recognized at fair value. Gains and losses on derecognition are generally recognized in profit or loss.

Impairment of assets

The carrying amount of the Company's non-financial assets (which include equipment and intangible assets) is reviewed at each reporting date to determine whether there is any indication of impairment. If such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss. An impairment loss is recognized whenever the carrying amount of an asset or its cash generating unit exceeds its recoverable amount. Impairment losses are recognized in the statement of comprehensive loss.

The recoverable amount of assets is the greater of an asset's fair value less cost to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects the current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

An impairment loss is only reversed if there is an indication that the impairment loss may no longer exist and there has been a change in the estimates used to determine the recoverable amount. Any reversal of impairment cannot increase the carrying value of the asset to an amount higher than the carrying amount that would have been determined had no impairment loss been recognized in previous years. Assets that have an indefinite useful life are not subject to amortization and are tested annually for impairment.

Income taxes

Current income tax:
Current income tax assets and liabilities for the current period are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted, at the reporting date, in the countries where the Company operates and generates taxable income.

Current income tax relating to items recognized directly in other comprehensive income or equity is recognized in other comprehensive income or equity and not in profit or loss. Management periodically evaluates positions taken in the tax returns with respect to situations in which applicable tax regulations are subject to interpretation and establishes provisions where appropriate.

Deferred income tax:
Deferred income tax is recognized, using the asset and liability method, on temporary differences at the reporting date arising between the tax bases of assets and li abilities and their carrying amounts for financial reporting. The carrying amount of deferred income tax assets is reviewed at the end of each reporting period and recognized only to the extent that it is probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilized. Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period. Deferred income tax assets and deferred income tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current income tax liabilities and the deferred income taxes relate to the same taxable entity and the same taxation authority.

Inventory

Inventory consists of raw materials for manufacturing of multi-rotor helicopters, industrial areal video systems, civilian small unmanned aerial systems or vehicles, and wireless video systems. Inventory is initially valued at cost and subsequently at the lower of cost and net realizable value. Net realizable value is determined as the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale. Cost is determined using the weighted average cost basis. The Company reviews inventory for obsolete and slow-moving goods and any such inventory is written-down to net realizable value.

Convertible debentures

The components of the compound financial instrument (convertible debenture) issued by the Company are classified separately as financial liabilities and equity in accordance with the substance of the contractual arrangement and the definitions of a financial liability and an equity instrument. The conversion option that will be settled by the exchange of a fixed amount in cash for a fixed number of equity instruments of the Company is classified as an equity instrument. At the issue date, the liability component is recognized at fair value, which is estimated using the effective interest rate on the market for similar nonconvertible instruments. Subsequently, the liability component is measured at amortized cost using the effective interest rate until it is extinguished on conversion or maturity. Upon maturity, the equity portion of the expired unexercised conversion option is reclassified to deficit.

The value of the conversion option classified as equity is determined at the issue date, by deducting the amount of the liability component from the fair value of the compound instrument as a whole. This amount is recognized in equity, net of tax effects, and is not revised subsequently. When the conversion option is exercised, the equity component of the convertible debentures will be transferred to share capital. No profit or gain is recognized to the conversion or expiration of the conversion option.

Transaction costs related to the issuance of the convertible debentures are allocated to the liability and equity components in proportion to the initial carrying amounts. Transaction costs related to the equity component are recognized directly in equity. Transaction costs relating to the liability component are included in the carrying value of the liability component and amortized over the estimated useful life of the debentures using the effective interest rate method.

Revenue recognition

Revenue comprises the fair value of consideration received or receivable for the sale of goods and consulting services in the ordinary course of the Company's business. Revenue is shown net of return allowances and discounts.

Sales of goods
The Company manufactures and sells a range of multi-rotor helicopters, industrial aerial video systems, and civilian small unmanned aerial systems or vehicles. Sales are recognized when control of the products has transferred, being when the products are delivered to the customer and there is no unfulfilled obligation that could affect the customer's acceptance of the products. Delivery occurs when the products have been shipped to the specific location or picked up by the customer, the risks of obsolescence and loss have been transferred to the customer.

Revenue from these sales is recognized based on the price specified in the contract, net of the estimated discounts and returns. Accumulated experience is used to estimate and provide for the discounts and returns, using the expected value method, and revenue is only recognized to the extent that it is highly probable that a significant reversal will not occur. To date, returns have not been significant. No element of financing is deemed present as the sales are made with a credit term of 30 days, which is consistent with market practice.

Some contracts include multiple deliverables, such as the manufacturing of hardware and support. Support is performed by another party and does not include an integration service. It is therefore accounted for as a separate performance obligation. In this case, the transaction price will be allocated to each performance obligation based on the stand-alone selling prices. Where these are not directly observable, they are estimated based on expect cost plus margin.

A receivable is recognized when the goods are delivered as this is the point in time that the consideration is unconditional because only the passage of time is required before the payment is due.

Consulting services

The Company provides consulting, custom engineering and investigating and solving on a project by project basis under fixed-price and variable price contracts. Revenue from providing services is recognized in the accounting period in which the services are rendered. For fixed-price contracts, revenue is recognized based on the actual service provided to the end of the reporting period as a proportion of the total services to be provided. This is determined based on the actual labour hours spend relative to the total expected labour hours. If contracts include the manufacturing of hardware, revenue for the hardware is recognized at a point in time when the hardware is delivered, the legal title has passed and the customer has accepted the hardware.

Estimates of revenues, costs or extent of progress toward completion are revised if circumstances change. Any resulting increases or decreases in estimated revenues or costs are reflected in profit or loss in the period in which the circumstances that give rise to the revision become known by management.

In case of fixed-price contracts, the customer pays the fixed amount based on a payment schedule. If the services rendered by the Company exceed the payment, a contract asset is recognized. If the payments exceed the services rendered, a contract liability is recognized. If the contract includes an hourly fee, revenue is recognized in the amount to which the Company has a right to invoice. Customers are invoiced on a monthly basis and consideration is payable when invoiced.

Cost of Goods Sold

Cost of sales includes the expenses incurred to acquire and produce inventory for sale, including product costs, freight costs, as well as provisions for reserves related to product shrinkage, excess or obsolete inventory, or lower of cost and net realizable value adjustments as required.

Intangible Assets

An intangible asset is an identifiable asset without physical substance. An asset is identifiable if it is separable, or arises from contractual or legal rights, regardless of whether those rights are transferrable or separable from the Company or from other rights and obligations. Intangible assets includes intellectual property, which consists of patent and trademark applications.

Intangible assets acquired externally are measured at cost less accumulated amortization and impairment losses. The cost of a group of intangible assets acquired is allocated to the individual intangible assets based on their relative fair values. The cost of intangible assets acquired externally comprises its purchase price and any directly attributable cost of preparing the asset for its intended use. Research and development costs incurred subsequent to the acquisition of externally acquired intangible assets and on internally generated intangible assets are accounted for as research and development costs.

Intangible assets with finite useful lives are amortized straight-line over their estimated useful lives from the date they are available for use. The amortization period of the Company's intellectual property is 5 years.

Equipment

Equipment is stated at historical cost less accumulated depreciation and accumulated impairment losses.

Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognized. All other repairs and maintenance are charged to the statement of comprehensive loss during the financial period in which they are incurred.

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognized in the statement of comprehensive loss.

Depreciation is calculated on a straight-line method to write off the cost of the assets to their residual values over their estimated useful lives. The depreciation rates applicable to each category of equipment are as follows:

Class of equipment	Depreciation rate
Computer equipment	30%
Furniture and equipment	20%
Software	30%

Research and development expenditures

Expenditures on research are expensed as incurred. Research activities include formulation, design, evaluation and final selection of possible alternatives, products, processes, systems or services. Development expenditures are expensed as incurred unless the Company can demonstrate all of the following: (i) the technical feasibility of completing the intangible asset so that it will be available for use or sale; (ii) its intention to complete the intangible asset and use or sell it; (iii) its ability to use or sell the intangible asset; (iv) how the intangible asset will generate probable future economic benefits. Among other things, the Company can demonstrate the existence of a market for the output of the intangible asset or the intangible asset itself or, if it is to be used internally, the usefulness of the intangible asset; (v) the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset; and (vi) its ability to measure reliably the expenditure attributable to the intangible asset during its development.

Government Assistance

Government grants are recognized when there is reasonable assurance that the grant will be received and all attached conditions will be complied with. When the grant relates to an expense item, it is recognized as income on a systematic basis over the period that the related costs, for which it is intended to compensate, are expensed. When the grant relates to an asset, the cost of the asset is reduced by the amount of the grant and the grant is recognized as income in equal amounts over the expected useful life of the asset.

SR&ED Investment tax credits

The Company claims federal investment tax credits as a result of incurring scientific research and experimental development ("SR&ED") expenditures. Federal investment tax credits are recognized when the related expenditures are incurred and there is reasonable assurance of their realization. Federal investment tax credits are accounted for as a reduction of research and development expense for items of a period expense nature or as a reduction of property and equipment for items of a capital nature. Management has made a number of estimates and assumptions in determining the expenditures eligible for the federal investment tax credit claim. It is possible that the allowed amount of the federal investment tax credit claim could be materially different from the recorded amount upon assessment by Canada Revenue Agency.

The Company claims provincial (Alberta) investment tax credits as a result of incurring SR&ED expenditures. Provincial investment tax credits are recognized when the related expenditures are incurred and there is reasonable assurance of their realization. Management has made a number of estimates and assumptions in determining the expenditures eligible for the provincial investment tax credit claim. The provincial investment tax credits are refundable and have been recorded as Alberta SR&ED tax credit receivable, and as a reduction in research and development expenses on the statement of comprehensive loss. It is possible that the allowed amount of the provincial investment tax credit claim could be materially different from the recorded amount upon assessment by Canada Revenue Agency and the Alberta Tax and Revenue Administration.

Leases

A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. At the commencement date, the lease liability is recognized at the present value of the future lease payments and discounted using the interest rate implicit in the lease or the Company's incremental borrowing rate. A corresponding right-of-use ("ROU") asset will be recognized at the amount of the lease liability, adjusted for any lease incentives received and initial direct costs incurred. Over the term of the lease, financing expense is recognized on the lease liability using the effective interest rate method and charged to net income, lease payments are applied against the lease liability and depreciation on the ROU asset is recorded by class of underlying asset.

The lease term is the non-cancellable period of a lease and includes periods covered by an optional lease extension option if reasonably certain the Company will exercise the option to extend. Conversely, periods covered by an option to terminate are included if the Company does not expect to end the lease during that time frame. Leases with a term of less than twelve months or leases for underlying low value assets are recognized as an expense in net income on a straight-line basis over the lease term.

A lease modification will be accounted for as a separate lease if it materially changes the scope of the lease. For a modification that is not a separate lease, on the effective date of the lease modification, the Company will remeasure the lease liability and corresponding ROU asset using the interest rate implicit in the lease or the Company's incremental borrowing rate. Any variance between the remeasured ROU asset and lease liability will be recognized as a gain or loss in net income to reflect the change in scope.

Accounting pronouncements

The Company adopted the requirements of IFRS 16 effective January 1, 2019. This new standard replaces IAS 17 Leases and the related interpretative guidance. IFRS 16 applies a control model to the identification of leases, distinguishing between a lease and a service contract on the basis of whether the customer controls the asset being leased.

For those assets determined to meet the definition of a lease, IFRS 16 introduces significant changes to the accounting by lessees, introducing a single, on-balance sheet accounting model that is similar to the current accounting for finance leases, with limited exceptions for short-term leases or leases of low value assets. Lessor accounting is substantially changed.

On adoption, the Company's lease consisted of an office lease. The Company transitioned to the new standard using the modified retrospective approach and:

- Measured the lease liability based on the present value of the remaining lease payments discounted using the Company's incremental borrowing rate at January 1, 2019;
- Measured the right-of-use asset as if IFRS 16 had been applied since the commencement date, but discounted using the Company's incremental borrowing rate at January 1, 2019; and
- Recording the cumulative difference to deficit.

The following is a reconciliation of total operating lease commitments at December 31, 2018 to the lease liabilities recognized at January 1, 2019:

Lease liability before discounting	$	38,000
Renewal options		133,000
Discounted using incremental borrowing rate		(39,366)
Lease liability	$	131,634

The following is a reconciliation of lease liabilities to right of use lease asset at January 1, 2019:

Lease liability at January 1, 2019	$	131,634
Right of use lease asset at January 1, 2019	$	131,634

For any new contracts entered into on or after January 1, 2019, the Company considers whether a contract is, or contains a lease. A lease is defined as 'a contract, or part of a contract, that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration'. To apply this definition the Company assesses whether the contract meets three key evaluations which are whether:

i. the contract contains an identified asset, which is either explicitly identified in the contract or implicitly specified by being identified at the time the asset is made available to the Company
ii. the Company has the right to obtain substantially all of the economic benefits from use of the identified asset throughout the period of use, considering its rights within the defined scope of the contract
iii. the Company has the right to direct the use of the identified asset throughout the period of use. The Company assess whether it has the right to direct 'how and for what purpose' the asset is used throughout the period of use.

included under non-current assets and lease liabilities have been included under current and non-current liabilities.

Business Risks

In the normal course of business, the Company's operations are influenced by a number of internal and external factors and are exposed to risks and uncertainties that can affect its business, financial condition and operating results. The activities of the Company are subject to ongoing operational risks including the performance of key suppliers, product performance, and government and other industry regulations and reliance on information systems, all of which may affect the ability of the Company to meet its obligations. While management believes its innovation and technology make it a leader in the industry, revenue and results may be affected if products are not accepted in the market place, are not approved by regulatory authorities, or if products are not brought to market in a timely manner.
The Company will be affected by a number of operational risks and the Company may not be adequately insured for certain risks, including: labour disputes; catastrophic accidents; fires; blockades or other acts of social activism; changes in the regulatory environment; impact of non-compliance with laws and regulations; natural phenomena, such as inclement weather conditions, floods, earthquakes and ground movements. There is no assurance that the foregoing risks and hazards will not result in damage to, or destruction of, the Company's technologies, personal injury or death, environmental damage, adverse impacts on the Company's operation, costs, monetary losses, potential legal liability and adverse governmental action, any of which could have an adverse impact on the Company's future cash flows, earnings and financial condition. Also, the Company may be subject to or affected by liability or sustain loss for certain risks and hazards against which the Company cannot insure or which the Company may elect not to insure because of the cost. This lack of insurance coverage could have an adverse impact on the Company's future cash flows, earnings, results of operations and financial condition.

Resale of Shares

There can be no assurance that the publicly-traded market price of the Company Shares will be high enough to create a positive return for the existing investors. Further, there can be no assurance that the Company Shares will be sufficiently liquid so as to permit investors to sell their position in the Company without adversely affecting the stock price. In such event, the probability of resale of the Company Shares would be diminished.

As well, the continued operation of the Company will be dependent upon its ability to procure additional financing in the short term and to generate operating revenues in the longer term. There can be no assurance that any such financing can be obtained or that revenues can be generated. If the Company is unable to obtain such additional financing or generate such revenues, investors may be unable to sell their Company Shares and any investment in the Company may be lost.

Ability to Manage Future Growth

Future growth, if any, may cause a significant strain on the Company's management and its operational, financial, human and other resources. The Company's ability to manage growth effectively will require it to implement and improve operational, financial, software development and management information systems and to expand, train, manage and motivate employees. These demands may require the addition of management and other personnel and the development of additional expertise. Any increase in resources devoted to research, product development and marketing and sales efforts without a corresponding increase in operational, financial, product development and management information systems could have a material adverse effect on the Company's business, financial condition and results of operations. There can be no assurance that the Company will be able to manage such growth effectively, that its management, personnel or systems will be adequate to support the Company's operations or that the Company will be able to achieve the increased levels of revenue commensurate with the increased levels of operating expenses associated with this growth. The Company is exposed to a variety of financial risks by virtue of its activities, including currency risk, credit risk, and liquidity risk. The overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on financial performance.

Market for Securities

In recent years, the securities markets in the United States and Canada have experienced a high level of price and volume volatility, and the market prices of securities of many companies have experienced wide fluctuations in price which have not necessarily been related to the operating performance, underlying asset values or prospects of such companies. There can be no assurance that continuing fluctuations in price will not occur. It may be anticipated that any quoted market for the Company Shares will be subject to market trends generally, notwithstanding any potential success of the Company in creating revenues, cash flows or earnings. The value of the Company Shares will be affected by such volatility.

History of Losses

The Company cannot assure that it can become profitable or avoid net losses in the future or that there will not be any earnings or revenue declines for any future quarterly or other periods. The Company expects that its operating expenses will increase as it grows its business, including expending substantial resources for research and development and marketing. As a result, any decrease or delay in generating revenues could result in material operating losses.

Reliance on Management and Key Employees

The Company's future success depends substantially on the continued services of its executive officers and its key development personnel. If one or more of its executive officers or key development personnel were unable or unwilling to continue in their present positions, the Company might not be able to replace them easily or at all. In addition, if any of its executive officers or key employees joins a competitor or forms a competing company, the Company may lose know-how, key professionals and staff members as well as partners. These executive officers and key employees could develop drone technologies that could compete with and take customers and market share away from the Company.

Risks Associated with Acquisitions

As part of the Company's overall business strategy, after the completion of the Listing, the Company may pursue select strategic acquisitions that would provide additional product or service offerings, additional industry expertise, and a stronger industry presence in both existing and new jurisdictions. Future acquisitions may expose it to potential risks, including risks associated with: (a) the integration of new operations, services and personnel; (b) unforeseen or hidden liabilities; (c) the diversion of resources from the Company's existing business and technology; (d) potential inability to generate sufficient revenue to offset new costs; (e) the expenses of acquisitions; or (f) the potential loss of or harm to relationships with both employees and existing users resulting from its integration of new businesses. In addition, any proposed acquisitions may be subject to regulatory approval.

Credit risk

Credit and liquidity risk associated with cash and the marketable security is managed by ensuring assets are placed with major financial institutions with strong investment grade ratings.

Credit risk on trade and other receivables reflects the risk that the Company may be unable to recover them. The Company manages its credit risk by closely monitoring the granting of credit. Trade and other receivables that are greater than 30 days are considered past due. Based on the status of trade and other receivables, no allowance for doubtful accounts has been recorded as at December 31, 2019 (December 31, 2018 - $nil).

Interest rate risk

Interest rate risk is the risk that the value of a financial instrument might be adversely affected by a change in the interest rates. In seeking to minimize the risks from interest rate fluctuations, the Company manages exposure through its normal operating and financing activities. The Company is exposed to minimal interest rate risk on its cash balances as they carry a floating rate of interest.

Foreign currency risk

The Company does engage in significant transactions and activities in currencies other than its functional currency. Depending on the timing of the transactions and the applicable currency exchange rates such conversions may positively or negatively impact the Company.

Other Information

Additional information about the Company is available at www.draganfly.com

Approval

This MD&A is authorized for issue by the Board on April 24, 2020.