DRONESHIELD

Quarterly Report

For the period ending
31 December 2020

Image: DroneSentry™ US Department of Defense deployment

DroneShield Limited (ASX:DRO)
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DroneShield Ltd (ASX:DRO) ("DroneShield" or the "Company") is pleased to provide the following update on its activities during the three-month period ended 31 December 2020 and its Appendix 4C quarterly cash flow report for the same period.

The quarter's key highlights are as follows.

- ✓ ***All-time record high quarterly customer receipts of $2.1 million, along with $250,000 in grants received, for a total record of $2.4 million in gross cash receipts from operations***
- ✓ ***A break-even cashflow quarter on a normalized basis (excluding investment in inventory for future sales and one-offs associated with growth of the business)***
- ✓ ***Currently, a book of $13 million in firm customer orders placed with, and to be delivered by, the Company***
- ✓ ***The expected changes in the U.S. foreign policy and military posture expected to be a substantial positive for the Company***

Financial Performance and Outlook

The Company's order book has more than doubled from last quarter to approximately $13 million (with approximately $2.7 million in customer deposits received during and prior to the quarter in relation to these orders).

Consistent with the increase in customer orders, DroneShield recorded record customer cash receipts of approximately $2.1 million (and record gross cash receipts from operations of approximately $2.4 million after accounting for additional $250,000 in cash receipts from grants.

The quarter thus demonstrated the Company's accelerating capability to convert substantial order leads into substantial orders.

The Company's high conviction pipeline is estimated at over $90 million[1]. In addition to the high conviction pipeline, there are a number of further tenders and other processes in the *full project pipeline* that DroneShield is participating in, which are not referred to in the *high conviction pipeline*, due to the Company having lesser visibility of the probability of winning the project.

The quarter also demonstrated DroneShield's ability to receive meaningful repeat purchase orders from marquee customers on short notice such as the $400,000 Five Eye country Government Agency repeat order announced on 29 December 2020.

As foreshadowed at the time of the Company's recent $17 million Placement and Share Purchase Plan, during the quarter the Company made a substantial investment in inventory, and undertook one-off expenses such as recruitment fees associated with growing the team, reducing the Company's cash balance by approximately $1 million (to $16.3 million as at 31 December 2020), after these one-off expenses. On a normalised basis, after adjusting for such one-offs, the December 2020 quarter was a break even operating cashflow quarter for the Company. Further, even after the one-off expenses, the Company's net cash outflow for the quarter was less than half that of the previous quarter, reflecting the acceleration in sales.

[1] Necessarily, not all, and there can be no assurance that any, of the Company's sales opportunities will result in sales

Sales

At the macro level, international tensions and greyzone warfare (which C-UAS, EW and related areas are a key part of) continue to rise, driving increases in security and national defence budgets. During the quarter, DroneShield continued to expand the range of its customers and its sales pipeline. The Company currently offers its products in over 100 countries and the diversity of its pipeline is one of its key strengths. Importantly, with a wide distribution network and a history of orders from a variety of customers, DroneShield is not dependent on any one customer or any one existing or potential contract for its success.

The update below does not seek to cover each of the Company's sales opportunities or even each type of Company's sales opportunities, which are numerous. Rather, it highlights a limited number of near-term themes that are some of the main sales drivers for the Company.

Five Eyes Community

As an Australian defence manufacturer with an on the ground presence in the US and the UK, DroneShield is closely aligned with the Five Eyes (a signals intelligence alliance between the US, Canada, Australia, UK and New Zealand). During the quarter, the Company completed a delivery of an $900,000 order for its DroneGun Tactical™ hand-held counter-drone product from a major intelligence Government agency of a Five Eyes country, with a follow up $400,000 order received during the same quarter, on 29 December 2020. This follow up order is expected to be delivered in 1Q21, with payments received across 1Q21 and 2Q21[2].

The United States Department of Defense and other U.S. government agencies

The United States government, through a wide variety of its agencies and departments, is the largest counterdrone customer globally.

During the quarter, DroneShield continued to expand its US operations, moving into a larger US premises (consisting of an office, demo facility and an inventory warehouse) within the same Warrenton precinct in Virginia as its previous office. The precinct has a long defence heritage with a substantial amount of defence facilities and military contractors within its vicinity. The Company has also continued to expand its US team, including hiring of a dedicated Sales Director to service Corrections, Ports and Maritime and Commercial markets within the US.

Image: DroneShield US Government agency demo

[2] All quarters refer to calendar quarters, as DroneShield's financial year end is December

To further accelerate its work in the US market, the Company continues to work with Cassidy & Associates, Inc. ("Cassidy"), a pre-eminent Washington, DC government relations firm, whereby Cassidy advises the Company on contracting with U.S. government agencies, contracts in connection with U.S. federal government budgetary allocations, and other U.S. federal government relations matters.

During the quarter DroneShield continued to undertake product demonstrations and meetings with the U.S. Department of Defense and other Government agencies, including supporting the recent U.S. Army Defense in Depth Exercise (DiDEX 20) with several of its C-UAS solutions for dismounted, mounted, and fixed-site drone detection.

During DiDEX, DroneShield successfully demonstrated its DroneSentry™, DroneSentry-X™, RfPatrol™, and DroneGun™ solutions to support multiple operational scenarios within a densely populated urban environment. DroneGun™ and RfPatrol™ were used to support dismounted operations, providing situational awareness and an intuitive response capability at the tactical edge by an individual operator. DroneSentry-X™, while mounted to a commercial vehicle, provided real-time alerts, stationary and on-the-move through the city, proving a highly effective, portable, and flexible C-UAS solution for mobile operations.

Images: DroneShield's fixed-site DroneSentry™ system being installed in support of Defense in Depth Exercise (DiDEX) and DroneShield's vehicle mounted DroneSentry-X™ operating near the Superdome in New Orleans, LA

DroneSentry™ demonstrated its extended range of Radio Frequency ("RF") detection and triangulation throughout the urban airspace with its RfOne™ sensors. In addition to long-range detections, DroneSentry demonstrated interoperability with the U.S. Army's Forward Area Air Defense Command and Control ("FAAD C2") software. FAAD C2 was selected and approved by the Department of Defense Joint Counter Small-Unmanned Aircraft Systems Office ("JCO") earlier this year. This is a key step towards a more seamless integration between the DroneSentry™ multi-sensor system and FAAD C2.

One of DroneShield's key demonstrated advantages during the evaluation was offering a family of adaptable and interoperable solutions to effectively detect and mitigate the threat, and protect the Warfighter, as opposed to a single "one size fits all" solution. This enables individuals and units to effectively address their C-UAS requirements, leverage existing mission components, and reduce overall cognitive burden. DroneSentry™ and DroneSentry-C2™'s open architecture allows for interoperability of DroneShield solutions across the ecosystem of JCO approved C-UAS systems and solutions including FAAD C2 and others.

DiDEX is facilitated by the U.S. Army's C5ISR Center Unique Mission Cell (UMC), part of the Combat Capabilities Development Command (CCDC). Following DroneShield's participation in DiDEX last month, the company announced MIL-STD-2525 compliance of its DroneSentry-C2™, further demonstrating its commitment to and support of U.S. DoD end users.

Additionally, the Company is currently awaiting on finalisation of internal DoD spectrum approvals to complete the installation of its DroneSentry™ system at a DoD base. This is currently expected to be complete this March 2021 quarter, with installation and payment shortly following.

In addition to the defence work, DroneShield has been selected as a shortlisted tenderer for a major state-wide prison rollout tender in the US, with an expected total value of about $15 million (upfront and ongoing), with DroneShield bidding to act as the primary contractor for the commissioning, deployment and operations of the system.

Further, DroneShield has entered into a Cooperative Research and Development Agreement ("CRADA") with the US Department of Homeland Security ("DHS") as part of its engagement with DHS.

Image: US Government agency DroneGun™ demo

Australian and New Zealand Departments of Defence and other government agencies

Following several orders from the Australian Department of Defence ("DoD") in the recent 12 months, DroneShield continues to actively engage with the DoD and other Australian Government agencies, both directly and as a subcontractor for large defence prime contractors.

The Company won a $630,000 contract with the DoD in November 2020. Further, it is the preferred bidder on a high-profile defence project in Australia as a subcontractor to a major defence prime, and expects to finalise and announce this contract in the current quarter. DroneShield is also working with several other primes, who are including the Company's products and capabilities into their submissions to the Australian DoD as part of the Australian Industrial Capability (AIC) requirement for the primes to do business with the DoD.

As previously reported in October 2020, DroneShield received a Capability Improvement Grant from the Australian Department of Defence via the Centre for Defence Industry Capability ("CDIC"), towards meeting the standards for secret clearance levels required for the Company as the overall business, to engage in more classified work. As DroneShield is in the business of understanding, and minimising defence and Government customer vulnerabilities, secret clearances are important for closer and more productive customer engagements as the Company scales its business. The Company anticipates completing its defence Industry Security Program ("DISP") process and becoming eligible for a defence clearance, this 2021 calendar year.

The Middle East

DroneShield is awaiting a payment of approximately $2.3 million (in addition to the funds previously received by DroneShield under this order) for a shipment of the remaining DroneGun Tactical™ units under a prior Middle Eastern Ministry of Defence order, with the customer confirming successful receipt of the goods and all obligations met on DroneShield's part. The delays resulted from the COVID-19-related disruptions and a recent transfer of the counter-UAS responsibility between the departments within the Ministry of Defence, however an active engagement to process the payment continues and the payment is currently expected in the present quarter.

DroneShield also continues to pursue the $58 million to $71 million[3] potential order, with a fully completed form of contract awaiting execution by the sovereign customer. During the quarter, DroneShield's in-country partner held multiple discussions with the customer and work continues to arrange near term execution of the contract.[4]

Europe

During the quarter, DroneShield delivered and received full payment for a DroneSentry™ system to a European Ministry of Defence. The system will be used for evaluation deployments by the customer, with a view to potential near-term purchases of additional units following the successful deployment.

Further, DroneShield is presently in the process of delivering several large orders to Europe across its product range, including portables, vehicle and fixed site solutions. These orders are expected to be delivered to the customers prior to end of the current March quarter.

Also during the quarter, the Company announced deployment of a DroneSentry™ system at the Altenrhein Airport in Switzerland. The provided system was entirely passive (no emissions) with no interference to other equipment, making it well suited for the airport environment.

Image: DroneSentry-C2™ screen at air traffic control tower of Altenrhein Airport

While the system has been deployed on a no revenue basis, an ability to have a working airport with a DroneShield system that can be referenced and visited by prospective airport and other customers, around Europe and globally, is expected to result in paid deployments, as a number of

[3] Corresponding to US$45-55 million. Movement from previously reported amount due to AUD/USD FX fluctuations
[4] Originally announced on 10 July 2018. Necessarily, there can be no assurance that any of the Company's sales opportunities will result in sales. There is no assurance that the bid referenced in this paragraph will result in a sale

airports in Europe and globally have indicated upcoming deployments of C-UAS systems in 2021.

The Company also continues to progress discussions with the European Union police forces, where it has won the framework agreement, under which DroneGun Tactical™ is expected to be rolled out across a range of police units across the European Union. The first order under the EU police framework agreement was received on 18 January 2021, and is currently in the process of being fulfilled.

The United Kingdom – Partnership with BT

DroneShield continues its partnership with BT on its counterdrone pipeline. UK Ministry of Defence ("UK MOD") is presently the prime focus for the partnership, given the COVID-19 slowdown affecting other customers in the UK, particularly in light of the recent lockdowns. DroneShield and BT have made substantial inroads within the UK MOD in the last nine months, including DroneShield products having been successfully deployed by the UK MOD in actual combat conditions, with highly positive reviews. The DroneShield/BT team is progressing several opportunities ranging from hundreds of thousands to millions of pounds in value each, expecting to close some of these opportunities in the 2021 calendar year, with the timing being substantially dependent on the UK COVID-19 situation[5]. Additionally, BT has demonstrated its confidence in its partnership with the Company and continued to support the partnership in the short term by continuing to purchase DroneShield equipment for demo purposes, including taking sensor deliveries under purchase orders to DroneShield this March quarter.

As part of its joint marketing, BT and DroneShield conducted multiple defence and commercial customer webinars, which were both well attended by key prospective stakeholders of the UK C-UAS industry.

Image: BT DroneShield C-UAS webinar

Importantly, in addition to the C-UAS strategy, BT has been actively growing its civilian Unmanned Traffic Management ("UTM") strategy, including its Future Flight consortium with Altitude Angel (a UK based UTM provider) selected by the UK Research & Innovation to deliver UK's first commercial drone corridor in open and unrestricted airspace, located south of Reading, Berkshire. DroneShield RfOne™ sensors, are ideally suited for the sensor hardware element of the UTM systems, being long range passive sensors not requiring the tracked drones to carry any specialised transponders or cooperate with the sensors in any way.

[5] Necessarily, not all, and there can be no assurance that any, of the Company's sales opportunities will result in sales

Team and Operations

Following the transformative capital raise in 3Q20, DroneShield expanded the team, including additions to its engineering and operations staff in its Australian office, and sales and engineering field support staff in the US office.

In order to assist scale up in operations and increase efficiency, DroneShield has continued onboarding an experienced defence manufacturing contractor in Australia (a fully Australian owned and operated medium size specialised electronics manufacturer), for some of its product lines. DroneShield continues to do own manufacturing for products which continue to be further developed. The outsourced manufacturer works on a per unit cost basis, meaning DroneShield does not take volume associated risks, and orders for manufacture are placed to align with customer and demo requirements.

Image: DroneShield's Australian manufacturing partner operations

Image: RfOne MKII™ units completing manufacturing process

Marketing

While most trade shows continued to be postponed or held virtually due to COVID-19 during the quarter, DroneShield is planning to participate in events which are still going ahead in 2021, directly or via local partners, starting with the International Defence Exhibition and Conference ("IDEX") in Abu Dhabi in February 2021.

Image: DroneGun Tactical™ at a South Korean Army Training and Doctrine Command conference, held during 4Q20

DroneShield continues to be recognised at premier Australian defence awards.

Image: DroneShield's CEO Oleg Vornik, CFO Carla Balanco and Vice President of Design Lawrence Marychurch at the DefenceConnect Australian Defence Industry Awards, where DroneShield was selected as the Finalist in several categories, held December 2020

DroneShield's Guillaume Jounel has been selected as the winner of the Australian Industry and Defence Network (AIDN) NSW Young Achiever of the Year Award, going on to the AIDN National Awards along with winners from the other States, held in Canberra on 3rd February 2021. This continues DroneShield's tradition of winning the AIDN NSW Young Achiever Award, with the previous year winners being its CTO Angus Bean and Vice President of Design Lawrence Marychurch.

Image: Guillaume Jounel, DroneShield Optical AI Lead, receiving the AIDN NSW Young Achiever Award, with DroneShield CEO Oleg Vornik

In November 2020, DroneShield held a launch event together with the University of Technology Sydney (UTS), with whom it has collaborated on the optical Artificial Intelligence technology for UAS detection, under the Australian Government's Defence Innovation Network scheme. Collaboration between defence industry and universities forms an important part of product development in defence. The event was held at the Sydney Science Park in Western Sydney and attended by the UTS Vice Chancellor Professor Attila Brungs and Hon Stuart Ayers, NSW Minister for Jobs and Western Sydney.

Image: DroneShield/UTS showcase event at the Sydney Science Park

Product Development

DroneShield continues to position itself at the cutting edge of solutions for detection and response to a wide variety of asymmetric multi-domain threats, as the greyzone conflict continues to rapidly rise, at both non-State actor level and State-on-State warfare.

This presents several current priorities for 2021 being:

- rapid software advancements including Artificial Intelligence/Machine Learning, at Field-Programmable Gate Array ("FPGA") circuit level up – making sense of a wide amount of received multi-domain information
- Printed Circuit Board ("PCB") design technologies – making our circuits smarter and faster
- waveform technologies – receiving and emitting RF signals better
- ecosystem integration, both as third-party products into DroneShield's ecosystem, and offering the Company's sensors into ecosystems of defence primes and similar integrators. This dual approach maximises the sales opportunities available to the Company. During the 4Q20 quarter, DroneShield has both completed integration of several third party sensors into its C2, with further detail available at https://www.droneshield.com/partner-technologies
- continuous refinement of supply chain, enhancement of build manuals and other required work to maximise scalability and short delivery time for complex products, exceeding defence and security customer expectations in the industry known for excessive delivery timeframes and scope creep. DroneShield positions itself as an industry disruptor not only in the nature of its products, but in transforming customer expectations on responsiveness and order delivery timing.

DroneSentry-C2™

During the December quarter, the Company has released a US DoD MIL-STD-2525 compliant version of its DroneSentry-C2™ command-and-control system, as part of its continued work with the US Department of Defense.

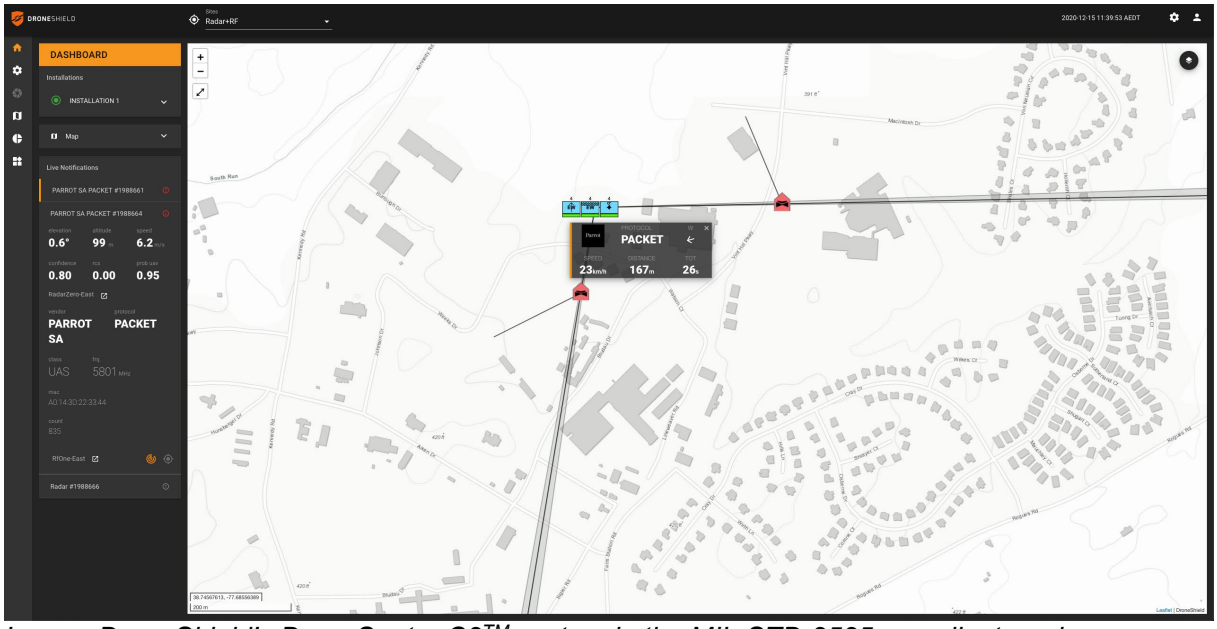

Image: DroneShield's DroneSentry-C2™ system in the MIL-STD-2525 compliant mode

MIL-STD-2525 refers to a standard structured set of symbology for the display of information in command-and-control (C2) systems and applications, by use by the US Department of Defense, and non-DOD entities such as other Federal agencies and NATO partners. DroneSentry-C2™ now provides users with industry leading enterprise features and MIL-STD-2525 compliance.

DroneSentry-C2 ™ is a common operating picture for the Counter-UxS mission. DroneSentry-C2™ enables its users to visualize their operational space, integrate with existing perimeter security and C2 systems, and leverage multi-sensor fusion capabilities unique to DroneSentry-C2™. As a sensor agnostic, open architecture platform, DroneSentry-C2 ™ brings advanced interoperability and flexibility to users.

Press Coverage

DroneShield continued to be reported as being at the cutting edge of the counterdrone industry in the media. Coverage of DroneShield included the following:

- DroneShield received $900K order from major Govt. Agency[6]
- DroneShield, UTS partnership better detects and tracks targets[7]
- Future of warfare: New tech helps better detect drones[8]
- DroneShield, UTS develop technology to better detect and track drone threats[9]
- DroneShield highlights DroneOptID's AI-driven UAS identification capabilities[10]
- DroneShield boosts AI capabilities for C-UAS and beyond[11]
- Common ways counter-drone technology detects drones[12]
- How counter-drone systems defeat and destroy rogue drones[13]
- DroneShield and Squarehead partner in the C-UAS space[14]
- DroneShield releases US Military compliant counter drone system, DroneSentry-C2[15]
- DroneShield deploys counter-drone tech at a Swiss airport[16]
- DroneShield hits record sales, rolls out demo airport system[17]
- DroneShield deploys C-UAS DroneSentry at Swiss airport[18]
- DroneShield receives follow-up order from a Five Eyes government[19]
- A Five Eyes country has upped its recent order for DroneShield's DroneGun[20]
- Counter-Drone Technology Supports U.S. Army Exercise[21]
- DroneShield receives first order under EU Police contract[22]
- DroneShield 'aggressively' investing in growth[23]

DroneShield has appeared on Channel 7 news during the quarter:

[6] https://themarketherald.com.au/droneshield-asxdro-receives-900k-order-from-major-govt-agency-2020-10-01/
[7] https://dronedj-com.cdn.ampproject.org/c/s/dronedj.com/2020/11/11/droneshield-uts-partnership-better-detects-and-tracks-targets/amp/
[8] https://www.miragenews.com/future-of-warfare-new-tech-helps-better-detect-drones/
[9] https://www.thedefensepost.com/2020/11/11/droneshield-uts-drone-threats/
[10] https://www.janes.com/defence-news/news-detail/droneshield-highlights-droneoptids-ai-driven-uas-identification-capabilities
[11] https://asianmilitaryreview.com/2020/11/droneshield-boosts-ai-capabilities-for-c-uas-and-beyond/
[12] https://dronedj.com/2020/12/01/common-ways-counter-drone-technology-detects-drones/
[13] https://dronedj.com/2020/12/03/how-counter-drone-systems-defeat-and-destroy-rogue-drones/
[14] https://www.suasnews.com/2020/12/droneshield-and-squarehead-partner-in-the-c-uas-space/
[15] https://www.unmannedairspace.info/counter-uas-systems-and-policies/droneshield-releases-us-military-compliant-counter-drone-system-dronesentry-c2/
[16] https://dronedj.com/2020/12/15/droneshield-deploys-counter-drone-tech-at-a-swiss-airport/
[17] https://themarketherald.com.au/droneshield-asxdro-hits-record-sales-rolls-out-demo-airport-system-2020-12-15/
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[23] https://www.eurekareport.com.au/investment-news/droneshield-aggressively-investing-in-growth/149238

Video: DroneShield on Channel 7 News

Environment

The end of 2020 saw the US military put emphasis on the development and deployment of C-UAS equipment in 2021, with plans to spend approximately US$500 million on the counter-drone sector, as outlined by the Congressional Research Service. On 7 January 2021, the Pentagon released a new strategy to counter increasingly complex small drone threats, that focuses on establishing a common threat picture, architecture and protocol across the services.

The new strategy also sets up stronger coordination between other federal agencies in the homeland as well as with allies and partners abroad.

At the same time, the US Government has added DJI, a Chinese drone manufacturer that is one of the largest drone sellers in the world, to the US Department of Commerce's Entity List, designating DJI as a national security concern and banning US-based companies from exporting technology to the company, in a similar mechanism for the US Government's ongoing ban on the Huawei products.

The use of small UAS is no longer limited to non-government actors, with militaries such as Iran developing low-cost, payload carrying and surveillance aircraft. The Iranian kamikaze UAS, which are more compact than traditional military UAS, were recently used in a two-day exercise as bombers, interceptors and reconnaissance missions, as tensions in the region increase.

Iran and the regional forces it backs have increasingly relied in recent years on drones in Yemen, Syria, Iraq and the Strait of Hormuz at the mouth of the Gulf.

Image: Iranian drones capable of carrying out swarm kamikaze attacks on display at an Iranian military exercise

As military-grade drones become more common, so do publicly accessible drones. Smaller state groups can quickly support their cause with widely available commercial-off-the-shelf (COTS) and modified (MOTS) drones. The Pakistan/India border experienced several incidents where rebel groups delivered supporting equipment, such as ammunition, arms and communication equipment to frontline fighters, with Punjab Police making two arrests associated with drone smuggling.

Image: One of the drones confiscated by the Punjab Police during the smuggler arrests

BBC has published a report by Conflict Armament Research (CAR) in December 2020 showing ISIS seeking to develop high-speed drones powered by pulse jet engines like those used in V-1 bombs dropped on the UK during World War Two.

The report mentioned a "fully constructed pulse jet engine" measuring more than two metres in length was found at a hospital in west Mosul, Iraq in September 2017. Namir Shabibi, the CAR's head of operations in Iraq, was reported stating "remaining cells in Iraq and Syria have become increasingly active in the past year".

Image: The pulse jet engine (pictured left, with air intake unit at right) was found at a hospital in Mosul, Iraq in September 2017

The Taliban were suspected of using a drone to kill at least four security officers in Afghanistan in November, marking a potentially dangerous upgrade to the insurgents' arsenal, as violence continues throughout the country while peace talks with the government remain stalled. The attack on a government compound in the northern province of Kunduz earlier in January was thought to have been the first use of a weaponised drone by the Islamist group during the 19-year war. One Taliban fighter told The Times (UK newspaper) that the group had a "fun new weapon" at its disposal.

Meanwhile, Kuwaiti military has issued a statement threatening legal action to anyone flying drones without permits from the Directorate General of Civil Aviation (DGCA), and in September 2020, Oman also announced new rules regulating drone usage, requiring users to get permits.

Small UAS continued to cause incidents with commercial aircraft. The reported incidents during the quarter have included:

- A student training aircraft in South Africa was forced to make an emergency landing after striking a small UAS and sustaining wing damage.
- In November in Canada, law enforcement was unable to locate the drone that was interfering with air traffic in the North Bay area. Transport Minister Marc Garneau stated: "Interfering with air traffic near airports with a drone, as was the case in North Bay this weekend, can cause a serious incident. When you fly your drone, you're sharing the skies, remember to always stay away from people, airports, and other aircraft."
- A medical helicopter landing at a Michigan hospital came within meters of colliding with a drone that was flown illegally over the helipad. While the drone was recovered after the incident, the pilot could not be located or prosecuted in the absence of drone detection equipment.
- Authorities arrest a man for crashing a drone into an LAPD helicopter.

Image: A small UAS that was involved in a near miss with a landing Aero Med helicopter at Butterworth Hospital in Michigan

Residents of Coral Gates, a small community in San Ysidro, California have been reporting increasing drone flights from across the border (the location is close to Tijuana, Mexico), which reportedly were carrying drugs.

In January 2021, Cyprus Police reportedly seized a drone carrying 60g of cannabis in Ayios Dhometios, Nicosia.

Prison drug drops have continued to be reported, including a man charged over drone smuggling operation of phones and cocaine at Ireland's maximum security Portlaoise Prison.

Commercial venues have proven to be particularly vulnerable to small UAS, which can discretely circumvent security measures. Even small UAS are capable of causing significant damage in both intentional and negligent scenarios. Allegiant stadium in Las Vegas suffered damage after a UAS was crashed into panels approximately 100 feet above the ground. Whilst the offending drone was captured, its lack of registration meant the pilot could not be found or prosecuted.

The impact of COVID-19 on sporting fixtures resulted in many matches taking place without spectators, causing a spike in UAS incidents as pilots sought to gain exclusive imagery of the games. In all the incidents listed below, authorities were unable to identify or prosecute the pilot.

- Championship match between Rotherham and Sheffield was halted after a UAS was flown into the stadium and hovered above the pitch.
- A Chicago MLB game had to evacuate players and umpires after a drone with filming equipment landed in the outfield.
- An MLB game in New York was delayed after a UAS incursion shortly after the match start.
- A Minneapolis MLB game was halted when an unauthorised UAS flew over the field.

Image: Small UAS that interrupted a Minneapolis Major League Baseball game

Please see https://www.droneshield.com/press-coverage and https://twitter.com/DroneShield for more information.

Payments to related parties of the entity and their associates

During the quarter, DroneShield paid Sort Hub Pty Ltd $10,738 for shipping of inventory globally, on normal commercial terms and conditions no more favourable than those available from other parties in the logistics industry. Director Jethro Marks is a related party of Sort Hub Pty Ltd.

Board fees paid to Non-Executive Directors and salary to CEO amounted to $174,169.

Capital Structure

As of the date of this report, there are 389,880,102 ordinary shares on issue. No other class of securities (other than the options referenced below) exist.

Below table summarises current outstanding options, issued to the Board, management and staff (and in the case of class O and R options, issued to brokers as part of previous capital raisings).

Class	Amount Outstanding	Strike Price	Expiry
E	250,000	30c	29 Mar 2021
F	750,000	30c	22 Jun 2021
G	250,000	30c	29 Mar 2022
J	225,000	50c	22 Jun 2021
K	675,000	50c	22 Jun 2022
M	50,000	20c	22 Jun 2022
N	50,000	20c	22 Jun 2023
O	1,446,066	22c	21 Feb 2021
P	500,000	40c	5 Aug 2022
Q	3,987,500	65c	30 Jun 2023
R	10,000,000	40c	5 Aug 2022
S	2,200,000	25c	31 Dec 2023
Zepos - Tranche 1	21,000,000	Nil (exercise can only take place when the Company achieves $10m in revenue or cash receipts in a 12 month period, or a takeover or a similar transaction occurs)	15 Aug 2021
Zepos - Tranche 1	2,459,384		17 Oct 2021
Zepos - Tranche 2	4,870,000	Nil (exercise can only take place when the Company achieves $20m in revenue or cash receipts in a 12 month period (not counting any revenue applied to Tranche 1 Zepos vesting, or a takeover or a similar transaction occurs)	30 Nov 2022
Total	48,712,950		

Authorised for release by the Board of Directors.

Further Information

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About DroneShield Limited

DroneShield (ASX:DRO) is an Australian publicly listed company with its head office in Sydney and teams in the US and UK, specialising in Electronic Warfare, RF sensing, Artificial Intelligence and Machine Learning, Sensor Fusion, rapid prototyping and MIL-SPEC manufacturing. Our capabilities are used to protect military, Government, law enforcement, critical infrastructure, commercial and VIPs throughout the world.

Through our team of Australian based engineers, we offer customers bespoke solutions and off-the-shelf products designed to suit a variety of terrestrial, maritime or airborne platforms. DroneShield is proudly exporting Australian capability to customers throughout the world and supporting Australia's defence, national security and other organisations protect people, critical infrastructure and vital assets.

END

Appendix 4C

Quarterly cash flow report for entities subject to Listing Rule 4.7B

Name of entity

DRONESHIELD LIMITED

ABN	**Quarter ended ("current quarter")**
26 608 915 859	31 December 2020

Consolidated statement of cash flows		**Current quarter $A**	**Year to date (12 months) $A**
1.	**Cash flows from operating activities**		
1.1	Receipts from customers	2,138,777	3,660,494
1.2	Payments for		
	(a) research and development	(288,047)	(1,015,165)
	(b) product manufacturing and operating costs	(901,439)	(2,346,270)
	(c) advertising and marketing	(129,888)	(614,228)
	(d) leased assets	-	-
	(e) staff costs	(1,173,168)	(4,011,567)
	(f) administration and corporate costs	(717,095)	(1,983,250)
1.3	Dividends received (see note 3)	-	-
1.4	Interest received	5,232	23,657
1.5	Interest and other costs of finance paid	(7,360)	(68,139)
1.6	Income taxes paid	-	-
1.7	Government grants and tax incentives	248,000	1,706,555
1.8	Other (provide details if material)	-	-
1.9	**Net cash from / (used in) operating activities**	**(824,988)**	**(4,647,913)**

2.	**Cash flows from investing activities**		
2.1	Payments to acquire or for:		
	(a) entities	-	-
	(b) businesses	-	-
	(c) property, plant and equipment	(174,585)	(727,840)
	(d) investments	-	-
	(e) intellectual property	-	-

+ See chapter 19 of the ASX Listing Rules for defined terms.

Consolidated statement of cash flows		Current quarter $A	Year to date (12 months) $A
	(f) other non-current assets	(44,318)	(44,318)
2.2	Proceeds from disposal of:		
	(g) entities	-	-
	(h) businesses	-	-
	(i) property, plant and equipment	-	-
	(j) investments	-	-
	(k) intellectual property	-	-
	(l) other non-current assets	-	-
2.3	Cash flows from loans to other entities	-	-
2.4	Dividends received (see note 3)	-	-
2.5	Other (provide details if material)	-	-
2.6	**Net cash from / (used in) investing activities**	**(218,903)**	**(772,158)**

3.	**Cash flows from financing activities**		
3.1	Proceeds from issues of equity securities (excluding convertible debt securities)	-	16,967,000
3.2	Proceeds from issue of convertible debt securities	-	-
3.3	Proceeds from exercise of options	-	-
3.4	Transaction costs related to issues of equity securities or convertible debt securities	-	(876,344)
3.5	Proceeds from borrowings	-	750,368
3.6	Repayment of borrowings	-	(600,000)
3.7	Transaction costs related to loans and borrowings	-	-
3.8	Dividends paid	-	-
3.9	Other (provide details if material)	(6,770)	56,514
3.10	**Net cash from / (used in) financing activities**	**(6,770)**	**16,297,538**

4.	**Net increase / (decrease) in cash and cash equivalents for the period**		
4.1	Cash and cash equivalents at beginning of period	17,348,193	5,485,000
4.2	Net cash from / (used in) operating activities (item 1.9 above)	(824,988)	(4,647,913)
4.3	Net cash from / (used in) investing activities (item 2.6 above)	(218,903)	(772,158)

Consolidated statement of cash flows		Current quarter $A	Year to date (12 months) $A
4.4	Net cash from / (used in) financing activities (item 3.10 above)	(6,770)	16,297,538
4.5	Effect of movement in exchange rates on cash held	(8,760)	(73,695)
4.6	**Cash and cash equivalents at end of period**	**16,288,772**	**16,288,772**

5.	Reconciliation of cash and cash equivalents at the end of the quarter (as shown in the consolidated statement of cash flows) to the related items in the accounts	Current quarter $A	Previous quarter $A
5.1	Bank balances	4,158,819	15,453,706
5.2	Call deposits	12,129,953	1,894,487
5.3	Bank overdrafts	-	-
5.4	Other (provide details)	-	-
5.5	**Cash and cash equivalents at end of quarter (should equal item 4.6 above)**	**16,288,772**	**17,348,193**

6.	Payments to related parties of the entity and their associates	Current quarter $A
6.1	Aggregate amount of payments to related parties and their associates included in item 1 Payments to CEO and Non-Executive Directors of $174,169, and payment of $10,738 for inventory global shipping costs to shipper Sort Hub Pty Ltd, of which the director Jethro Marks is a related party.	(184,907)
6.2	Aggregate amount of payments to related parties and their associates included in item 2	-

Note: if any amounts are shown in items 6.1 or 6.2, your quarterly activity report must include a description of, and an explanation for, such payments.

7.	**Financing facilities** *Note: the term "facility' includes all forms of financing arrangements available to the entity.* *Add notes as necessary for an understanding of the sources of finance available to the entity.*	**Total facility amount at quarter end $A**	**Amount drawn at quarter end $A**
7.1	Loan facilities	150,368	150,368
7.2	Credit standby arrangements	-	-
7.3	Other (please specify)	-	-
7.4	**Total financing facilities**	150,368	150,368

7.5	**Unused financing facilities available at quarter end**	-

7.6 In regards to point 7.1, the Company has received loan proceeds of AU$150,368 (US$99,600) from the US Government, under the Paycheck Protection Program ("PPP"). The loan bears a fixed interest rate of 1% per annum. The loan and accrued interest are forgivable at the end of the loan term if the loan proceeds are used for qualifying expenses. The Company intends to use the proceeds for purposes consistent with the PPP and currently believes that its use of the loan proceeds will meet the conditions for forgiveness of the loan.

8.	**Estimated cash available for future operating activities**	**$A**
8.1	Net cash from / (used in) operating activities (item 1.9)	(824,988)
8.2	Cash and cash equivalents at quarter end (item 4.6)	16,288,772
8.3	Unused finance facilities available at quarter end (item 7.5)	-
8.4	Total available funding (item 8.2 + item 8.3)	16,288,772
8.5	**Estimated quarters of funding available (item 8.4 divided by item 8.1)**	**19.74**

Note: if the entity has reported positive net operating cash flows in item 1.9, answer item 8.5 as "N/A". Otherwise, a figure for the estimated quarters of funding available must be included in item 8.5.

8.6 If item 8.5 is less than 2 quarters, please provide answers to the following questions:

8.6.1 Does the entity expect that it will continue to have the current level of net operating cash flows for the time being and, if not, why not?

Answer: N/A

8.6.2 Has the entity taken any steps, or does it propose to take any steps, to raise further cash to fund its operations and, if so, what are those steps and how likely does it believe that they will be successful?

Answer: N/A

8.6.3 Does the entity expect to be able to continue its operations and to meet its business objectives and, if so, on what basis?

Answer: N/A

Note: where item 8.5 is less than 2 quarters, all of questions 8.6.1, 8.6.2 and 8.6.3 above must be answered.

Compliance statement

1 This statement has been prepared in accordance with accounting standards and policies which comply with Listing Rule 19.11A.

2 This statement gives a true and fair view of the matters disclosed.

Date: 27 January 2021

Authorised by: .....
Carla Balanco, Company Secretary

Notes

1. This quarterly cash flow report and the accompanying activity report provide a basis for informing the market about the entity's activities for the past quarter, how they have been financed and the effect this has had on its cash position. An entity that wishes to disclose additional information over and above the minimum required under the Listing Rules is encouraged to do so.

2. If this quarterly cash flow report has been prepared in accordance with Australian Accounting Standards, the definitions in, and provisions of, *AASB 107: Statement of Cash Flows* apply to this report. If this quarterly cash flow report has been prepared in accordance with other accounting standards agreed by ASX pursuant to Listing Rule 19.11A, the corresponding equivalent standard applies to this report.

3. Dividends received may be classified either as cash flows from operating activities or cash flows from investing activities, depending on the accounting policy of the entity.

4. If this report has been authorised for release to the market by your board of directors, you can insert here: "By the board". If it has been authorised for release to the market by a committee of your board of directors, you can insert here: "By the [*name of board committee – eg Audit and Risk Committee*]". If it has been authorised for release to the market by a disclosure committee, you can insert here: "By the Disclosure Committee".

5. If this report has been authorised for release to the market by your board of directors and you wish to hold yourself out as complying with recommendation 4.2 of the ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations*, the board should have received a declaration from its CEO and CFO that, in their opinion, the financial records of the entity have been properly maintained, that this report complies with the appropriate accounting standards and gives a true and fair view of the cash flows of the entity, and that their opinion has been formed on the basis of a sound system of risk management and internal control which is operating effectively.