



## **MANAGEMENT'S DISCUSSION AND ANALYSIS OF THE FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

For the three months ended March 31, 2016

May 26, 2016

The following Management Discussion and Analysis ("MD&A") of Annidis Corporation ("Annidis" or the "Company") provides the consolidated financial position and consolidated results from operations for the three months ended March 31, 2016 and 2015. This MD&A has been prepared by management of the Company and is derived from, and should be read in conjunction with, Annidis Corporation's unaudited condensed interim consolidated financial statements (the "Interim Financial Statements") for the three months ended March 31, 2016 and 2015, including the accompanying notes.

By their nature, the Interim Financial Statements do not include all the information required for full annual financial statements, and so should be read in conjunction with the Company's audited annual financial statements as at, and for the years ended, December 31, 2015 and December 31, 2014, prepared in accordance with IFRS.

Continuous disclosure documents, including the Company's press releases and quarterly reports, are available through its filings with the securities regulatory authorities in Canada at [www.sedar.com](http://www.sedar.com).

Annidis reports its financial results under International Financial Reporting Standards ("IFRS") in Canadian dollars. Per share amounts are calculated using the weighted average number of shares outstanding for the applicable periods.

All amounts are expressed in Canadian dollars unless otherwise stated.

### **FORWARD-LOOKING STATEMENTS**

This MD&A contains "forward-looking statements" which may include, but are not limited to, statements with respect to the future financial or operating performance of the Company. Often, but not always, forward-looking statements can be identified by the use of words such as "plans", "expects", "is expected", "budget", "scheduled", "estimates", "forecasts", "intends", "anticipates" or "believes" or variation (including negative variations) of such words and phrases, or statements that certain actions, events or results "may", "could", "would", "might" or "will" be taken, occur or to achieved. Forward-looking statements are based on the reasonable assumptions, estimates, analysis and opinions of management made in light of its experience and perception of trends, current conditions and expected developments, as well as other factors that management believes to be relevant and reasonable at the date that such statements are made. Forward-looking statements involve known and unknown risks, uncertainties, assumptions and other factors that may cause actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. Such factors include, but are not limited to, the factors discussed in the section entitled "Risk Factors". Although the Company has attempted to identify important factors that could cause actions, events or results to differ materially from those described in the forward-looking statements, there may be other factors that cause actions, events or results to differ from those anticipated, estimated or intended. Forward-looking statements contained herein are made as at the date of the MD&A. There can be no assurance that forward-looking statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Accordingly, readers should

not place undue reliance on the forward-looking statements. The Company does not undertake to update any forward-looking statements except as required by applicable securities laws.

## **THE COMPANY**

**Annidis Corporation** (TSXV:RHA) develops and markets imaging technologies to eye care professionals.

It is a North American based company founded on scientific concepts emerging from a decade of research and development by the Annidis team in consultation with respected eye care professionals in Canada and the United States. The Annidis RHA™ has evolved into an ocular pathology management system to aid in early detection and management of age related macular degeneration, diabetic retinopathy and glaucoma.

## **RECENT DEVELOPMENTS**

### **Highlights**

Beginning in 2015 and continuing into early 2016, the Company has made significant changes to its senior management team with the skills and experience required to reposition the business and products in the marketplace. The new management team will use a staged process to align the business with a customer focused product development and marketing strategy. In recent months the Company has performed several comparative clinical studies in leading clinics which validate the specific clinical utility that the RHA product brings to optometric practices. The RHA's advantage in early detection of vision impacting eye disease proven by these comparative studies will be a fundamental component of the next stage of the Company's marketing initiatives as the RHA advances into a broader market acceptance. The Company believes that the new executive leadership's approach to marketing the instrument through focus on clinical validation, economic benefit to optometric practices and satisfied customer referrals will be an effective strategy to gain market share and to continue to build on relationships with key participants in the industry.

There will be costs associated with required changes as the Company eliminates some activities and initiates others as part of an overall plan to repair strained relationships in the marketplace and implement some foundational product design improvements.

The Company and its distribution partner in China, Yimai Technology International Company ("Yimai"), are optimistic about the opportunities in China and anticipate significant demand for its technology in the country, with an estimated addressable market of 5,000 imaging systems. Yimai is currently conducting several clinical studies in several luminary hospitals across China. A number of key opinion leaders in the Chinese ophthalmology market have been hosted at the Annidis offices in Ottawa to participate in demonstrations and educational seminars focusing on the RHA's clinical capabilities. The Company shipped a total of 19 units to China in fiscal 2015 compared to 16 units in fiscal 2014 and expects this sales volume to increase in fiscal 2016. Furthermore, the Company received an order from Yimai for 30 additional units that are scheduled for delivery by the end of fiscal 2016 for which full payment was received in the third quarter of fiscal 2015. The anticipated increase in sales volume is expected to reduce the cost of inventory by taking advantage of favourable payment terms and discounts from key vendors, and to leverage the Company's presence in China.

In March 2015, the National Space Biomedical Research Institute (NSBRI) Industry Forum launched the 'Vision for Mars' Challenge to identify and advance critical medical technologies for ocular health selecting and funding three companies, one of which was Annidis. Their goal is to further develop unique technologies that address visual problems in space as well as on Earth. Astronauts are susceptible to increased intracranial hypertension. A similar condition called idiopathic intracranial hypertension can be easily seen in RHA images. The expectation is that the RHA will help detect and monitor this condition in astronauts. Furthermore, retinal pigment epithelial disruptions with melanin clumping in macular degeneration and retinal dystrophies are much more easily identified using the

RHA, as indicated in peer reviewed papers which have been published in recent scientific journals. These developments are additional validation that the Annidis RHA is innovative and adds clinical value.

The Company's sales efforts are focused on:

- repairing and building relationships with large US buying groups. This provides a forum to present the Annidis product to large audiences and leverage the sales effort,
- increasing customer service, education and support to ensure the installed units achieve maximum utilization,
- supporting our distribution partner's expansion in the Chinese market through presentations of the RHA at major trade and scientific events.

In the first quarter of fiscal 2016, the Company completed the private placement of six convertible promissory notes with Yimai totaling \$840,000. The convertible promissory notes are scheduled to mature one year from the respective dates of issuance, and bear compounding interest at a rate of 10% per annum, compounded annually, and payable at maturity. At Yimai's option, the convertible promissory notes may be converted into common shares of Annidis at conversion prices ranging from \$0.05 to \$0.09 per common share.

On March 8, 2016, Yimai elected to convert five convertible promissory notes totaling \$670,000, plus all outstanding interest, into common shares, which resulted in the issuance of 9,197,382 shares. Two of these convertible promissory notes, totaling \$280,000, were outstanding at December 31, 2015, while the remaining three convertible promissory notes converted into common shares were issued subsequent to December 31, 2015 as described above.

On April 14, 2016, the Company completed the private placement of a \$1,300,000 grid promissory note (the "Grid Note") with Yimai pursuant to which the Company may draw upon for general working capital purposes. The Grid Note matures and becomes due and payable on the earlier of December 31, 2016 and the completion by the Company of an equity financing of not less than \$5,000,000. The Grid Note bears interest at rate of 10% per annum payable at maturity. The Corporation may prepay the outstanding principal amount of the Grid Note together with all accrued and unpaid interest, without penalty, at any time prior to the maturity date of the Grid Note.

As at the date of this MD&A, \$842,500 has been drawn on the Grid Note.

## Key Financial Metrics

			Three months ended March 31
<i>As at March 31</i>	2016	2015	% Change
Installed Base (units in clinics)	111	84	32.1
	\$	\$	%
Revenue	372,382	564,132	(34.0)
Net loss	(1,206,405)	(1,354,318)	(10.9)
Net loss per share	(0.01)	(0.02)	(50.0)

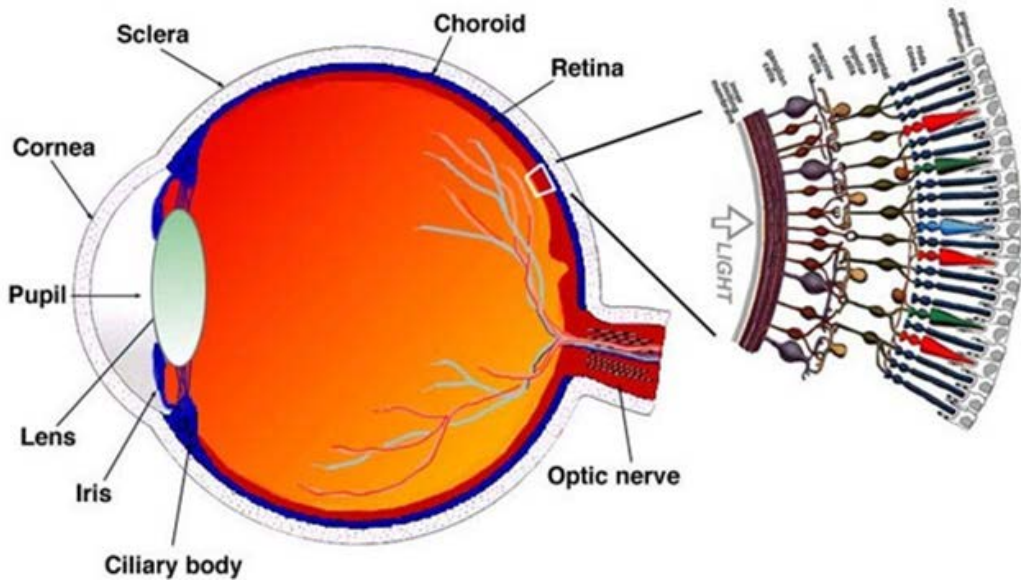
## BUSINESS OVERVIEW

### Company Background

Annidis was founded in 2007 to develop technology for early stage diagnosis of eye diseases. The Company saw the opportunity to improve eye healthcare by providing eye-care professionals with a device to screen, detect, diagnose, treat and manage ocular diseases. Annidis has achieved this by developing a multi-spectral imaging system for retinal and choroidal assessment (the "RHA™").

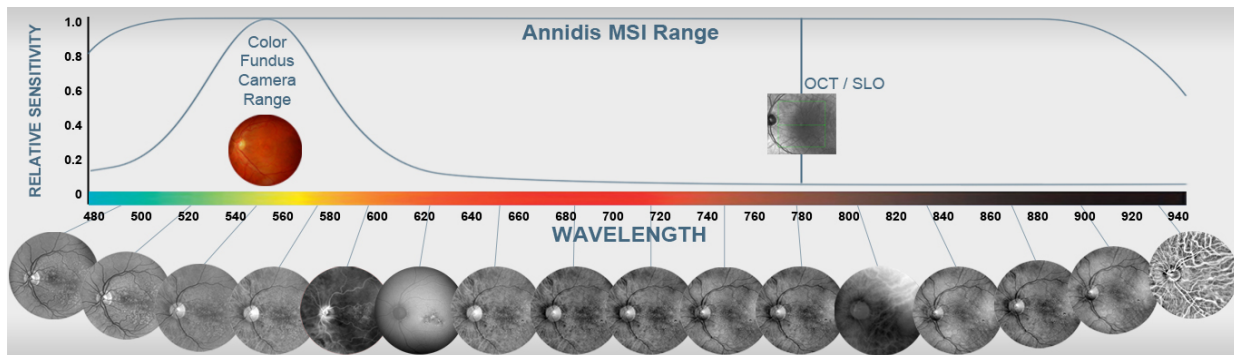
The RHA™ provides eye-care professionals with a broadly based screening tool for early detection and diagnosis of a variety of pathologies in a manner that is currently unavailable in the market. Early detection requires identifying initial metabolic changes, and the RHA™ addresses this need through collecting and combining multi-spectral information. The RHA™ is an ocular pathology management system that integrates advanced multi-spectral imaging with analytic software for early detection and management of ocular pathologies such as glaucoma, age-related macular degeneration ("AMD"), and diabetic retinopathy ("DR").

The RHA™ is a non-invasive instrument that uses multi-spectral imaging ("MSI") to take pictures of the retinal layers of your eye. The images are then processed using the RHA Report™ software to reveal the various layers in the back of the eye, allowing eye care professional to assess their patients' eye health.



**Multi-Spectral Imaging (MSI)**

The RHA™ system adds a new set of capabilities for fundus imaging through the expansion of the range of wavelengths used and the flexibility to use tuned spectral windows for specific probing - together known as multi-spectral imaging. The instrument has been designed to operate across the wavelength range of 500 to 940 nm which is over twice that available with traditional fundus photography. This wide range allows for the progressive examination of different depths in the retina and choroid. Deep retinal imaging is made possible by the use of longer wavelengths which penetrate deeper into the structures of the eye (as shown schematically in the figure below.)



The capability of capturing images at a number of wavelengths allows additional information to be extracted by comparing these images by visual inspection or automation. As one moves from the green through the amber to the red wavelengths, intraretinal hemorrhages are highlighted differently. The green wavelength highlights the nerve fiber layers while the red wavelength highlights the deep layers.

MSI enables improved visual discrimination of retinal and sub-retinal structures through spectral and depth-enhanced differential visibility, using manual and automated processing to highlight targeted features for examination.

### *Products*

The Company's existing RHA Gold, used by eye care professionals as a broad based tool for detecting early-onset of eye related diseases such as Dry AMD, has a potential market of over 20,000 optometric clinics in North America. Further opportunities exist in China, where the Company has entered into a distribution agreement.

The RHA Platinum, which is currently in development with beta units in clinical testing, will further strengthen the value proposition for the ophthalmology market, allowing doctors to visualize choroidal and retinal vasculature non-invasively.

### *Revenue*

The Company derives revenue from the sale of its devices directly to customers, through pay-per-use agreements based on the customers' volume of transactions and maintenance and support fees.

Revenue derived from the use of the eye health technology owned by the Company and provided to the customer under multi-year rental arrangements for the purpose of performing retinal examinations on their patients is recognized as the services are rendered by the customer to its patients. The fee is based on the actual number of billable patients imaged in accordance with the terms of the agreement with the customer.

## QUARTERLY INFORMATION

	Revenue	Net loss	Basic and diluted loss per share
	\$	\$	\$
<b>Quarterly Results</b>			
<b>Fiscal 2016</b>			
Three months ended March 31	372,382	(1,206,405)	(0.01)
<b>Fiscal 2015</b>			
Three months ended March 31	564,132	(1,354,318)	(0.02)
Three months ended June 30	381,893	(1,527,058)	(0.02)
Three months ended September 30	645,309	(1,231,290)	(0.01)
Three months ended December 31	307,325	(1,842,876)	(0.02)
<b>Fiscal 2014</b>			
Three months ended March 31	797,989	(1,242,265)	(0.01)
Three months ended June 30	532,982	(1,362,492)	(0.02)
Three months ended September 30	480,218	(1,240,943)	(0.01)
Three months ended December 31	552,838	(1,827,056)	(0.02)
<b>Cumulative Quarterly Results</b>			
<b>Fiscal 2016</b>			
Three months ended March 31	372,382	(1,206,405)	(0.01)
<b>Fiscal 2015</b>			
Three months ended March 31	564,132	(1,354,318)	(0.02)
Six months ended June 30	946,025	(2,881,376)	(0.03)
Nine months ended September 30	1,591,334	(4,112,666)	(0.04)
Twelve months ended December 31	1,898,659	(5,955,540)	(0.06)
<b>Fiscal 2014</b>			
Three months ended March 31	797,989	(1,242,265)	(0.01)
Six months ended June 30	1,330,971	(2,604,757)	(0.03)
Nine months ended September 30	1,811,189	(3,845,700)	(0.04)
Twelve months ended December 31	2,364,027	(5,672,756)	(0.06)

## DISCUSSION OF OPERATIONS

### REVENUE AND OPERATING EXPENSE ANALYSIS

	Three months ended 2016	March 31 2015
	\$	\$
<b>Revenues</b>	372,382	564,132
Cost of sales	148,201	360,641
	224,181	203,491
<b>Expenses</b>		
Manufacturing and operations	207,334	131,554
Research and development	315,428	270,832
General and administration	254,668	275,563
Sales and marketing	258,455	546,845
	1,035,885	1,224,794
Loss from operations	(811,704)	(1,021,303)
<b>Other expenses</b>		
Interest expense and financing charges	244,368	199,597
Accretion on promissory notes and convertible notes	132,769	127,173
Share-based compensation expense	10,588	-
Amortization of debt issue costs	6,976	6,245
	394,701	333,015
Net loss and total comprehensive loss	(1,206,405)	(1,354,318)
Net loss per share		
Basic and diluted	(0.01)	(0.02)
Weighted average number of common shares		
Basic and diluted	103,076,435	88,735,155

For the three month period ended March 31, 2016, the Company incurred a net loss of \$1,206,405 or (\$0.01) per share, compared to a loss of \$1,354,318, or (\$0.02) per share, for the same period in 2015.

Factors affecting results include:

*Three months ended March 31*

- Revenue decreased by 34% from \$564,132 in the first quarter of 2015 to \$372,382 in the first quarter of 2016 as the Company sold 5 units in 2016 compared to 9 units in 2015.
- The gross margin was higher in 2016 than 2015 as a result of significantly lower inventory costs achieved via cost-savings initiatives. The gross margin percentage increased from 36% to 60%.
- Operating expenses declined by 15% in the first quarter of 2016 over the prior year, resulting in a decrease in the operating expenses from \$1,224,794 to \$1,035,885. This decrease resulted from a reduction in sales and marketing expense in the current year of \$288,390 that was partially offset by an increase in manufacturing and operations expenses and an increase in research and development expenses. The decrease in sales and marketing expenses was largely attributed to the restructuring of the Company's US sales department that occurred in the second half of 2015 and continued up until the end of the first quarter of 2016. Manufacturing and operations expenses were higher in fiscal 2016 due to a low amount of manufacturing labour costs having been capitalized to inventory as a result of low activity in the manufacturing of new instruments, and research and development expenses were higher as a result of an increase in the number of employees working towards further product development.
- Interest expense and related financing charges increased from \$199,597 to \$244,368 as a result of new debt issued by the Company over the course of the last 12 months. Accretion on promissory notes and convertible notes similarly increased from \$127,173 to \$132,769.

**Revenue**

The Company earns revenues from the sale of its devices directly to customers with a recurring fee charged for services rendered, sales to its distributor where there are no recurring revenues and from rental income for devices deployed at clinic offices through pay-per-use agreements based on the number of customer patients imaged.

	Three months ended March 31	
	2016	2015
	\$	\$
<hr/>		
Revenue by Source		
Sales	261,539	481,649
Rentals, support and maintenance fees	110,843	82,483
	<hr/>	<hr/>
	372,382	561,132
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Revenue by Geography		
United States	179,028	292,157
China	180,000	252,240
Canada	13,354	19,735
	<hr/>	<hr/>
	372,382	564,132
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For the three month period ended March 31, 2016, the Company recorded the sale of 1 unit in the United States, 4 in China, and nil in Canada. This is in comparison to the 3, 6, and nil units sold in the corresponding geographies in the three month period ended March 31, 2015.

## Cost of sales

Cost of sales represents the material and subcontract components incurred by the Company in the production and manufacture of the devices, amortization of rental units and royalties.

For the three month period ended March 31, 2016, the Company incurred \$148,201 of cost of sales compared to \$360,641 for the same period in 2015. The decrease in cost of sales reflects the lower number of units sold in the current period fiscal year (2016 – 5 units; 2015 – 9 units) combined with other cost-savings initiatives that were implemented to reduce the costs of the devices.

## Gross margin

	Three months ended March 31	
	2016	2015
	\$	\$
Revenue	372,382	564,132
Cost of sales	148,201	360,641
Gross profit - \$	224,181	203,491
Gross profit - %	60.2%	36.1%

The gross margin percentage for the three month period ended March 31, 2016 increased to 60.2% from 36.1% in the comparative period in the prior year. This increase was driven by cost-savings initiatives that were implemented to significantly reduce the cost of inventory, but was offset in part by a higher proportion of sales having been made to Yimai at the lower distributor price in comparison to the three months ended March 31, 2015.

## Expenses

### Manufacturing and operations

Manufacturing and operations expenses represent the personnel and other costs incurred by the Company in the production and manufacture of the devices, net of labour and overhead allocated to inventory.

For the three months ended March 31, 2016, the Company incurred \$207,334 in manufacturing and operations expenses compared to \$131,554 for the comparable period in 2015. The net increase of \$75,780 is primarily due to a lower capitalization of manufacturing costs as a result of a comparatively unproductive first quarter in the manufacturing of inventory.

### Research and development

Research and development expenses represent the costs incurred by the Company in the research activities undertaken in the development of retinal imaging technology. Reported research and development expenses are net of government assistance for research programs.

For the three month period ended March 31, 2016, the Company incurred \$315,428 in research and development expenses compared to \$270,832 for the same period in 2015. The net increase in costs of \$44,596 was due primarily to increases in labour costs as the Company hired several engineers to continue to enhance the quality of the product and to develop new features.

### **General and administration**

General and administration expenses for the three months ended March 31, 2016 were \$254,668 compared to \$275,563 in 2015, a decrease of \$20,895, stemming from lower discretionary spending, reduction in payroll costs, and various other cost-savings initiatives.

### **Sales and marketing**

Sales and marketing expenses for the three month period ended March 31, 2016 were \$258,455 compared to \$546,845 for the corresponding period in 2015. The decrease of \$288,390 is the result of the reduced spending on trade shows, conferences, conventions, and travel, along with a downsizing of the US sales force beginning in the second quarter of 2015 and continuing into the first quarter of 2016..

### **Interest expense and financing charges**

This expense category consists of the interest expense incurred on the convertible notes, promissory note advances, promissory notes, secured promissory note and financing related expenses.

The Company incurred interest and financing charges for the three month period ended March 31, 2016 of \$244,368 compared to \$199,597 in the prior year. The increase in financing costs reflects additional interest costs incurred on the higher debt levels resulting from the issuance of the new promissory notes and convertible promissory notes in 2015, and the issuance of further convertible promissory notes in 2016.

### **Accretion on promissory notes and convertible notes**

In accordance with the Company's accounting policy, the carrying value of the debt component of the convertible notes and promissory notes are accreted to the original face value of the debt instrument over their corresponding terms using the effective interest rate method.

The amount of accretion recorded for the three month period ended March 31, 2016 was \$132,769 compared to \$127,173 in 2015. The accretion recorded in the three month period ended March 31, 2016 reflects the recording of the accretion on the promissory notes issued in May 2014, the convertible promissory notes, and the secured promissory note. The increase is driven by higher levels of debt that have an equity component.

### **Amortization of debt issue costs**

The amount of amortization of debt issue costs recorded in the three month period ended March 31, 2016 was \$6,976 compared to \$6,245 for the comparative 2015 periods. The amortization relates to costs incurred to obtain and issue the promissory notes in June 2013.

### **Share-based compensation**

Share-based compensation expense for the three month period ended March 31, 2016 was \$10,588 compared to \$NIL for the comparative 2015 period. The change comes as a result of 2,850,000 new options having been granted in the fourth quarter of 2015.

On April 18, 2016, the Company granted incentive stock options to certain directors, officers and employees of the Company for the purchase up to an aggregate of 3,000,000 common shares in the capital stock of Annidis, 1,500,000 of which vested immediately and the remainder of which vest on December 31, 2016. The options are exercisable at a price of \$0.05 per common share and expire on April 18, 2021.

## ASSET, LIABILITY AND SHARE CAPITAL ACTIVITIES

	March 31 2016 \$	December 31 2015 \$
Assets	2,527,603	2,865,300
Liabilities	12,344,776	12,171,944
Deficiency	(9,817,173)	(9,306,644)
Common shares outstanding	109,949,204	100,751,822
Options and warrants outstanding	18,902,085	18,902,085
Shares held in escrow	7,132,046	7,132,046

### *Assets*

Total assets of the Company as at March 31, 2016 and December 31, 2015 were comprised of cash, restricted short-term investments, trade accounts receivable, inventories, prepaids and other receivables, and property and equipment.

Trade accounts receivable decreased from \$179,928 at December 31, 2015 to \$74,785 at March 31, 2016 due to ordinary invoicing and collection activities, which included the collection of a significant receivable outstanding at December 31, 2015 in the amount of \$99,584.

Inventories, which consist of finished goods, work-in-process and raw materials were \$1,748,985 at March 31, 2016 compared to \$1,775,828 at December 31, 2015. During the three month period ended March 31, 2016, the Company's finished goods inventory increased from \$441,472 at December 31, 2015 to \$649,188 at March 31, 2016. This increase came as a result of disappointing first quarter sales results, where forecasted demand was not realized. Work in process decreased from \$494,595 as at December 31, 2015 to \$241,531 as at March 31, 2016 as a result of the completion of 9 units that were previously classified under work in process at December 31, 2015. Raw materials increased from \$839,760 at the end of 2015 to \$858,266 as at March 31, 2016 due to the delivery of raw material purchases to be used in the production of new units, a significant amount of which were long lead-time items that were ordered well in advance of March 31, 2016 in anticipation of high demand and the underlying production requirements.

Prepaids and other receivables decreased from \$242,650 as at December 31, 2015 to \$198,415 at March 31, 2016. This decrease is not considered to be significant, and comes as a result of the Company's ordinary business operations, but stems from the delivery of prepaid inventory that was delivered in the first quarter of 2016.

Property and equipment, net of accumulated amortization, decreased from \$450,465 as at December 31, 2014 to \$317,635 at March 31, 2016. This decrease came as a result of amortization of \$52,532 and the transfer of 3 demonstration units from property and equipment to inventory with a total net book value of \$80,298.

### *Liabilities*

As at March 31, 2016, the Company's liabilities totalled \$12,344,776 of which current liabilities represented \$7,608,813 and long term liabilities representing the remaining \$4,735,963. As at December 31, 2015, the Company's liabilities totalled \$12,171,944 of which current liabilities represented \$7,590,210 and long term liabilities representing the remaining \$4,581,734. A significant portion of the Company's liabilities relate to the convertible and promissory notes (March 31, 2016 promissory notes including convertible and secured notes - \$9,064,049; December 31, 2015 promissory notes including convertible and secured notes - \$8,581,811).

On May 22, 2014, the Company completed a private placement of a secured promissory note in the amount of \$1,000,000 with Yimai. The note has a three-year term and bears interest at a rate of 10% per annum compounded monthly and payable at maturity. The Company may prepay the outstanding principal amount of the note together with all accrued and unpaid interest, without penalty, at any time after the first anniversary of the issuance date of the note. The note is secured by a general security agreement over the assets of the Company but is subordinated to all existing charges against the assets of the Company.

The Company reached an agreement with the note holder whereby the convertible note in the principal amount of \$1,000,000 which matured on June 7, 2014 was cancelled and replaced with a new \$1,000,000 secured promissory note. In connection with the surrender of the convertible note for cancellation, the Company paid to the lender in December 2013 all accrued and outstanding interest on the convertible note up to and including November 30, 2013, along with a one-time note replacement fee of \$50,000. The new secured promissory note matures on January 31, 2017 and bears interest beginning December 1, 2013 at a rate of 12% per annum compounded monthly and payable at maturity. The Company may prepay the outstanding principal amount of the new secured promissory note together with all accrued and unpaid interest, without penalty, at any time after the first anniversary of the issuance date of the new secured promissory note. This note will be secured by a general security agreement over the assets of the Company.

In November 2014, the Company completed the private placement of a \$2,003,589 convertible promissory note with Yimai including the note payable of \$500,000 and accrued but unpaid interest on the note payable of \$3,589. The convertible promissory note was scheduled to mature six months from the date of issuance and bear interest at a rate of 10% per annum, compounded monthly, payable at maturity. On April 15, 2015, the Company and Yimai agreed to extend the term of the convertible promissory note by an additional 24 months to May 2017. At Yimai's option, the convertible promissory note may be converted into common shares in the capital of Annidis at a conversion price of \$0.35 per common share. The Company may prepay the outstanding principal amount of the convertible promissory note together with all accrued and unpaid interest, without penalty, at any time prior to the maturity date of the note. This agreement to extend the term of the note resulted in a reclassification of this liability from current to non-current and required a revaluation of the conversion option.

In 2015 the Company also issued two promissory notes totaling \$329,244. One of these notes was in the amount of \$150,000 to Yimai, and the other was issued to a third party to settle amounts payable in the amount of \$179,244 for past services that were previously included in accounts payable and accrued liabilities. The amount due to the third party was fully settled by March 31, 2016. The promissory note to Yimai was issued in November 2015 with a one year term. The note bears non-compounding interest at a rate of 10% per annum and is payable upon maturity.

In the first quarter of fiscal 2016, the Company completed the private placement of six convertible promissory notes with Yimai totaling \$840,000. The convertible promissory notes are scheduled to mature one year from the respective dates of issuance, and bear compounding interest at a rate of 10% per annum, compounded annually, and payable at maturity. At Yimai's option, the convertible promissory notes may be converted into common shares of Annidis at conversion prices ranging from \$0.05 to \$0.09 per common share.

On March 8, 2016, Yimai elected to convert five convertible promissory notes totaling \$670,000, plus all outstanding interest, into common shares, which resulted in the issuance of 9,197,382 shares. Two of these convertible promissory notes, totaling \$280,000, were outstanding at December 31, 2015, while the remaining three convertible promissory notes converted into common shares were issued in the first quarter of 2016 as described above.

In September 2015, the Company received a purchase order from Yimai for 30 units to be delivered in 2016, and received payment in full for these units. This payment has been recorded in deferred revenue, and will be recognized into revenue by the Company as the units are shipped. Only five of these units were delivered at March 31, 2016.

### ***Deficiency***

As at March 31, 2016 the Company's deficiency was \$9,817,173 compared to a deficiency of \$9,306,644 as at December 31, 2015. This increase in the deficiency is due primarily to a cumulative loss of \$1,206,405 for the three months ended March 31, 2016, offset by the issuance of shares to Yimai to settle the amount outstanding on various convertible notes upon conversion, for net proceeds of \$615,377, as well as the increase of the shared-based reserve of \$69,911 as a result of the convertible notes issued in the first quarter of 2016. The Company also recorded \$10,588 in share-based compensation expenses in the three months ended March 31, 2016.

As at May 26, 2016, the Company had 109,949,204 common shares issued and outstanding; 7,132,046 shares held in escrow; 10,304,585 warrants outstanding, exercisable at prices ranging from \$0.30 to \$0.80; and 11,597,500 options outstanding (8,452,500 exercisable), exercisable at prices ranging from \$0.05 to \$0.40.

### **LIQUIDITY, FINANCING ACTIVITY AND CAPITAL RESOURCES**

The Company is subject to risks including, but not limited to, the potential to raise additional funds through debt and/or equity financing to support the Company's development and continued operations and to meet the Company's liabilities and commitments as they come due. Specifically, the Company has a history of losses with an accumulated deficit of \$36,369,889, shareholders' deficiency of \$9,817,173 and negative cash flow from operations of \$844,829 for the three months ended March 31, 2016.

During 2012, the Company obtained promissory note advances of \$1,292,985 and, in the first quarter of 2013, the Company obtained additional advances of \$636,712. These advances were converted in June 2013 into promissory notes with a term of three years from the date of issuance bearing interest at 10% per annum compounded monthly and payable at maturity or such earlier date upon which the notes are repaid. Yimai subscribed for \$1,000,000 of promissory notes to complete the \$3,000,000 offering.

On October 4, 2013, the Company closed a private placement with the issuance of an aggregate of 27,965,379 common shares to Yimai for total consideration of \$5,000,000. Of these 27,965,379 common shares, 7,132,046 are held in escrow by Annidis and will be released to Yimai on the basis of one escrowed share for each (approximately) 3.26 common shares which are issued upon exercise of certain of the Company's other outstanding convertible securities on or before December 31, 2016. After such date, any escrowed shares not already released to Yimai will be cancelled.

On May 22, 2014, the Company completed a private placement of a secured promissory note in the amount of \$1,000,000 with Yimai. The note has a three-year term and bears interest at a rate of 10% per annum compounded monthly and payable at maturity.

In July 2014, the Company received TSVX approval of an agreement with the convertible note holder whereby the convertible note in the principal amount of \$1,000,000 which matured on June 7, 2014 was cancelled and replaced with a new \$1,000,000 secured promissory note. The new secured promissory note matures on January 31, 2017 and bears interest beginning December 1, 2013 at a rate of 12% per annum compounded monthly and payable at maturity.

In September 2014, the Company entered into an agreement with Yimai whereby Yimai lent the Company the principal amount of \$500,000

In November 2014, the Company completed the private placement of a \$2,003,589 convertible promissory note with Yimai including the note payable of \$500,000 and accrued but unpaid interest on the note payable of \$3,549. In April 2015, this note's maturity date was extended from May 2015 to May 2017 as previously described.

On April 15, 2015, the Company completed a private placement of an unsecured promissory note in the amount of \$500,000 with Yimai. The note was scheduled to mature upon the earlier of six months from the date of issuance or upon the closing by the Corporation of an equity financing of not less than \$3,000,000. The note bore interest at a rate of 10% per annum compounded monthly and was payable at maturity. The Company also held the option to prepay the outstanding principal amount of the note together with all accrued and unpaid interest, without penalty, at any time prior to the maturity date.

On June 9, 2015 the Company completed a non-brokered private placement of common shares whereby Yimai acquired 10,000,000 common shares of Annidis. The shares were issued at a share price of \$0.25 per share, resulting in gross proceeds of \$2,500,000. Concurrently, the Company completed a shares-for-debt transaction with Yimai and settled the \$500,000 amount due – plus the applicable interest – on the unsecured promissory note issued on April 15, 2015. This shares-for-debt transaction resulted in the issuance of an additional 2,016,667 common shares with an implicit share price of \$0.25 per share.

In the fourth quarter of 2015, the Company completed the private placement of convertible notes totalling \$280,000 to Yimai scheduled to mature one year from the date of issuance and bear non-compounding interest at a rate of 10% per annum, payable at maturity, convertible into common shares at a price of \$0.09 per common share. The Company also completed the private placement of six additional convertible promissory notes in the first quarter of 2016 with the same terms, with conversion prices ranging from \$0.05 to \$0.09 per common share. As previously described in the liabilities section of this MD&A, on March 8, 2016, Yimai elected to convert five convertible promissory notes totaling \$670,000, plus all outstanding interest, into common shares, which resulted in the issuance of 9,197,382 shares

As a result of the financing and excluding the escrowed shares, Yimai owns 32,850,000 common shares, resulting in an approximate 38.2% ownership interest in the Company.

The Company's principal capital needs include funds for the production of devices, to support sales and marketing activities, to support the continuing research and development activities of the medical device as well as for general working capital requirements. Since its formation, the Company has financed its cash requirements primarily through the issuance of securities, promissory notes, convertible debentures, short term debt instruments and government incentives. Management believes that over the short-term, there will be an increase in revenues as additional medical devices are deployed in clinics.

#### ***Cash used in operating activities***

During the three month period ended March 31, 2016, the Company used cash of \$844,829 for operating activities as compared to \$57,461 for the corresponding period of 2015. Cash consumption for the first quarter of 2016 was driven most significantly by losses of \$1,206,405 (2015 - \$1,354,318) offset by various non-cash items such as interest accruals, accretion, and amortization. The Company also noted an increase in the amount of non-cash working capital of \$69,201 (2015 - a decrease of \$908,909) which correspondingly impacted the net cash used in operating activities. This increase in non-cash working capital was primarily driven by decrease in deferred revenue resulting from the delivery of four prepaid units to Yimai in the first quarter of 2016. This was offset by significant decreases in inventory and accounts receivable as a result of, respectively, manufacturing activities and the collection of a significant receivable balance that was outstanding at December 31, 2015.

### ***Cash generated through financing activities***

The Company generated cash through financing activities of \$817,537 in the three month period ended March 31, 2016 (2015 – used \$18,682). The activity for the three month period related to the financing received from Yimai of \$840,000 in connection with working capital requirements, offset by share issuance costs of \$19,083, as well as repayment of financing leases of \$3,380 (2015 - \$18,682). In the comparative period in 2015, the only financing activities related to the repayment of financing leases.

### **OFF-BALANCE SHEET ARRANGEMENTS**

The Company has no off-balance sheet arrangements that would require disclosure.

### **FINANCIAL INSTRUMENTS AND OTHER INSTRUMENTS**

The carrying amounts of cash, restricted short-term investments, trade accounts receivable, other receivables, accounts payable and accrued liabilities, and deferred revenue, approximate their fair values due to the short-term nature of these instruments.

Financial instruments that potentially subject the Company to credit risk consist of trade accounts receivable. As at March 31, 2016, three customer accounts for 40% (December 31, 2015 - one customers accounted for 59%) of the Company's accounts receivable with the remaining customers individually accounting for less than 7% of the total accounts receivable. As at March 31, 2016, the Company's aging of receivables was approximately 54% under sixty days (December 31, 2015 - 77% under sixty days).

As at March 31, 2016, the Company had recorded a provision for doubtful accounts of \$11,408 (December 31, 2015 - \$11,408) to reflect the estimated collectability of the overdue accounts.

As at March 31, 2016, the Company's debt consisted of:

- Convertible promissory notes of \$2,708,420 consisting of the following:
  - A convertible promissory issued in November 2014 and extended in April 2015 of \$2,292,153 consisting of a principal amount of \$2,101,550 and accrued and unpaid interest of \$190,603 The convertible promissory note will mature in May 2017 and bears interest at a rate of 10% per annum compounded monthly. The financier holds the option to convert the note into common shares in the capital of Annidis at a conversion price of \$0.35 per common share.
  - Convertible promissory notes issued in the first quarter of 2016 in the amount of \$416,267 consisting of a principal amount of \$450,000 and accrued and unpaid interest of \$2,055 less unamortized accretion in the carrying value of the notes of \$35,788 The convertible promissory notes bear non-compounding interest at 10% per annum and is due in March 2017. The financier holds the option to convert the notes into common shares in the capital of Annidis at conversion prices ranging from \$0.05 to \$0.06 per common share.
- Promissory notes of \$5,108,582 consisting of the following:
  - Promissory notes issued in June 2013 in the amount of \$3,877,609 consisting of a principal amount of \$3,000,000 and accrued and unpaid interest of \$958,325 less unamortized accretion in the carrying value of the notes of \$74,594 and unamortized debt issue costs of \$6,122. The promissory notes bear interest at 10% per annum compounded monthly and is due in June 2016.

- A promissory note issued in May 2014 in the amount of \$1,083,905 consisting of a principal amount of \$1,000,000 and accrued and unpaid interest of \$201,523 less unamortized accretion in the carrying value of the notes of \$117,618. The promissory note bears interest at 10% per annum compounded monthly and is due in May 2017.
- A promissory note issued in November 2015 in the amount of \$147,068 consisting of a principal amount of \$150,000 and accrued and unpaid interest of \$5,219 less the unamortized gain on issuance of the note of \$8,151 as the note was issued under terms more favourable than the market rate. The promissory note bears non-compounding interest at 10% per annum and is due in November 2016.
- A secured promissory note of \$1,247,047 consisting of the principal amount of \$1,000,000, accrued and unpaid interest of \$321,433 less unamortized accretion in the carrying value of the notes of \$74,386. In July 2014, the convertible note in the principal amount of \$1,000,000 which matured on June 7, 2014 was cancelled and replaced with a new \$1,000,000 secured promissory note. The new secured promissory note matures on January 31, 2017 and bears interest beginning December 1, 2013 at a rate of 12% per annum compounded monthly and payable at maturity.
- A financing lease of \$4,693 bearing interest at a rate of 12.8% and maturing in 2016.

## **CONTRACTUAL OBLIGATIONS**

At the end of April 2014, the Company moved its offices and entered into a new five year lease commencing May 1, 2014. Under the terms of the new lease, the Company received a lease inducement of seven months of free rent.

## **RISK FACTORS**

### ***Financial***

The Company recently commenced commercial operations, has no history of profits and is not expected to generate earnings in the short term. There is no assurance that the Company will earn any profits in the future or that profitability, if achieved, will be sustained. Annidis will require additional equity or debt financing, and there is no assurance that the Company will be able to obtain additional financial resources on favourable commercial terms or at all.

### ***Competitors***

There are companies already selling similar solutions which are larger and have a longer operating history than Annidis. Many of these companies are better financed, with larger sales staffs and marketing budgets than Annidis. There can be no guarantee that the Company will be able to effectively compete in the marketplace with such competition.

### ***Slow Acceptance of Annidis' Solutions***

The marketplace may be slow to accept or understand the significance of Annidis' product due to its unique nature and the competitive landscape. Market confusion may slow sales and acceptance of Annidis' product. If the Company is unable to promote, market and sell its products and secure relationships with optometrists and ophthalmologists, the Company's business and financial condition would be adversely affected.

### ***Technological Advancements***

The medical devices industry is subject to significant technological advancements, changing industry standards, market trends, customer preferences and competitive pressures which can, among other things, necessitate revisions in pricing strategies, price reductions and reduced profit margins. The

success of Annidis will depend on its ability to secure technological superiority in its services and maintain such superiority in the face of new technologies. No assurance can be given that further modification of product offerings of the Company will not be required in order to meet demands or to remain competitive.

### ***Intellectual Property***

The success of Annidis will depend, in part, on its ability to maintain proprietary protection over its technology and operate without infringing the proprietary rights of third parties. Despite precautions, it may be possible for a third party to copy or otherwise obtain and use the Company's technology without authorization. There can be no assurance that any steps taken by Annidis will prevent misappropriation of its technology.

### ***Government Regulation and Regulatory Approvals***

Future changes in government regulation could adversely affect the medical devices industry in jurisdictions in which Annidis operates or intends to operate.

As with any medical device company, the Company is dependent on regulatory approvals and the legal systems in the markets in which it operates, such as the U.S. Federal Food and Drug Administration ("FDA"), China Food and Drug Administration ("CFDA") and Health Canada. The Company currently has the necessary regulatory approvals in Canada, United States and China to market and sell the Annidis RHA™ device. Regulators could, even after granting such approvals, be stringent on non-compliance with regulatory requirements or change such requirements, which could have a material adverse effect on the Company's business and result in adverse publicity.

### ***Customer Adoption***

The Company's revenues are highly dependent on the willingness of eye care professionals to market the Annidis products and on public awareness levels of the benefits of preventative or primary level eye and health care. The diverse nature of eye care professionals between different markets will require local adaptation of the Company's strategy and will likely lead to slower adoption of the Annidis products.

## **CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

The preparation of these financial statements requires management to select appropriate accounting policies and to make judgments, estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses and the disclosure of contingent assets and liabilities at the end of the reporting period. The estimates and related assumptions are based on previous experience and other factors considered reasonable under the circumstances, the results of which form the basis of making assumptions about carrying values of assets and liabilities that are not readily apparent from other sources.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period or in the period of revision and future periods if the revision affects both current and future periods.

Significant assumptions about the future that management has made and that could result in a material adjustment to the carrying amounts of assets and liabilities, in the event that actual results differ from assumptions made, relate to, but are not limited to, the following:

- [a] The determination of whether leased assets constitute an operating lease or a financing lease;
- [b] The inputs used in measurement for warrants in the consolidated statements of financial position;
- [c] The inputs used in measurement for share-based compensation expense in the consolidated statements of comprehensive loss;
- [d] The estimated borrowing cost to the Company with no warrants or conversion feature in determining the allocation of a compound instrument between debt and equity;
- [e] The depreciation method and useful lives of property and equipment and intangible assets including assumptions and judgements used in the determination of impairment, if any;
- [f] The \$NIL provision for income taxes which is included in the consolidated statements of comprehensive loss and no recognition of deferred income tax assets and liabilities included in the consolidated statements of financial position at December 31, 2014.

## **ACCOUNTING POLICY CHANGES**

New and amended standards adopted by the Company

*New and revised IFRS in issue but not effective*

The following is a list of standards and amendments that have been issued but are not yet effective and have not yet been adopted by the Company:

### IFRS 9 Financial Instruments (IFRS 9)

IFRS 9 was issued by the IASB in November 2009 and October 2010 and will replace IAS 39. IFRS 9 uses a single approach to determine whether a financial asset is measured at amortized cost or fair value, replacing the multiple rules in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. IFRS 9 is effective January 1, 2018.

### IFRS 15 - Revenue from Contracts with Customers (IFRS 15)

IFRS 15 is effective for annual periods beginning on or after January 1, 2018. IFRS 15 specifies how and when to recognize revenue as well as requires entities to provide users of financial statements with more informative, relevant disclosures. The standard supersedes IAS 18, Revenue, IAS 11, Construction Contracts, and a number of revenue-related interpretations. The new standard will apply to nearly all contracts with customers: the main exceptions being leases, financial instruments and insurance contracts.

### IFRS 16 Leases (IFRS 16)

The IASB issued a new standard, IFRS 16 on January 13, 2016, which supersedes IAS 17 *Leases*. The new standard brings most leases on the balance sheet for lessees under a single model and eliminates the distinction between operating and finance leases. Lessor accounting remains largely unchanged. The new standard will come into effect for periods beginning on or after January 1, 2019.

The impact of these standards and amendments has not yet been determined.