KWESST MICRO SYSTEMS INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Three months ended December 31, 2021

(Expressed in Canadian Dollars)

All references in this management's discussion and analysis (the "MD&A") to "KWESST", "we", "us", "our", and the "Company" refer to KWESST Micro Systems Inc. and its subsidiaries as at December 31, 2021. This MD&A has been prepared with an effective date of February 28, 2022.

This MD&A should be read in conjunction with our unaudited condensed consolidated interim financial statements for the three months ended December 31, 2021 ("Q1 Fiscal 2022 FS") and the annual audited consolidated financial statements and related notes for the year ended September 30, 2021 ("Fiscal 2021 FS"). The financial information presented in this MD&A is derived from these unaudited condensed consolidated interim financial statements prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). This MD&A contains forward-looking statements involves risk, uncertainties and assumptions, including statements regarding anticipated developments in future financial periods and our future plans and objectives. There can be no assurance that such information will prove to be accurate, and readers are cautioned not to place undue reliance on such forward-looking statements. See "Forward-Looking Statements".

All references to $ or dollar amounts in this MD&A are to Canadian currency unless otherwise indicated.

Additional information, including press releases, relating to KWESST is available for view on SEDAR at www.sedar.com.

NON-IFRS MEASURES

In this MD&A, we have presented earnings before interest, taxes, depreciation and amortization ("EBITDA") and EBITDA that has been adjusted for the removal of stock-based compensation, foreign exchange loss (gain) and any one-time, irregular and nonrecurring items ("Adjusted EBITDA") to provide readers with a supplemental measure of our operating performance and thus highlight trends in our core business that may not otherwise be apparent when relying solely on IFRS financial measures. Management also uses non-IFRS measures, in addition to IFRS financial measures, to understand and compare operating results across accounting periods, for financial and operational decision making, for planning and forecasting purposes, and to evaluate our financial performance. We believe that these non-IFRS financial measures enable us to identify underlying trends in our business that could otherwise be hidden by the effect of certain expenses that we exclude in the calculations of the non-IFRS financial measures.

Accordingly, we believe that these non-IFRS financial measures reflect our ongoing business in a manner that allows for meaningful comparisons and analysis in the business and provides useful information to investors and securities analysts, and other interested parties in understanding and evaluating our operating results, enhancing their overall understanding of our past performance and future prospects.

We caution readers that these non-IFRS financial measures do not replace the presentation of our IFRS financial results and should only be used as a supplement to, not as a substitute for, our financial results presented in accordance with IFRS. There are limitations in the use of non-IFRS measures because they do not include all the expenses that must be included under IFRS as well as they involve the exercise of judgment concerning exclusions of items from the comparable non-IFRS financial measure. Furthermore, other peers may use other non-IFRS measures to evaluate their performance, or may calculate non-IFRS measures differently, all of which could reduce the usefulness of our non-IFRS financial measures as tools for comparison.

GOING CONCERN

As an early-stage company, we have incurred significant losses and negative operating cash flows from inception that have primarily been funded from financing activities. KWESST's Q1 Fiscal 2022 FS have been prepared on the "going concern" basis which presumes that KWESST will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future. Refer to Note 2(a) of the Q1 Fiscal 2022 FS.

FORWARD-LOOKING STATEMENTS

Certain statements in this document constitute "forward-looking statements". Such forward-looking statements include, but are not limited to, information with respect to our objectives and our strategies to achieve these objectives, as well as statements with respect to our beliefs, plans, expectations, anticipations, estimates and intentions. These forward-looking statements may be identified by the use of terms and phrases such as "may", "would", "should", "could", "expect", "intend", "estimate", "anticipate", "plan", "foresee", "believe", or "continue", the negative of these terms and similar terminology, including references to assumptions, although not all forward-looking statements contain these terms and phrases. Forward-looking statements are provided for the purposes of assisting the reader in understanding us, our business, operations, prospects and risks at a point in time in the context of historical and possible future developments and therefore the reader is cautioned that such information may not be appropriate for other purposes.

Forward-looking statements relating to us include, among other things, statements relating to:

- our expectations regarding our business, financial condition and results of operations;
- the future state of the legislative and regulatory regimes, both domestic and foreign, in which we conduct business and may conduct business in the future;
- our expansion in domestic and international markets;
- our ability to attract customers and clients;
- our marketing and business plans and short-term objectives;
- our ability to obtain and retain the licences and personnel we require to undertake our business;
- our strategic relationships with third parties;
- our anticipated trends and challenges in the markets in which we operate;
- governance of us as a public company; and
- expectations regarding future developments of products and our ability to bring these products to market.

Forward-looking statements are based upon a number of assumptions and are subject to a number of risks and uncertainties, many of which are beyond our control, which could cause actual results to differ materially from those that are disclosed in or implied by such forward-looking statements. These risks and uncertainties include, but are not limited to, the following risk factors, some of which are discussed in greater detail under the section "*Risk Factors*" in our annual MD&A dated November 23, 2021.

- limited operating history;
- failure to realize growth strategy;
- failure to complete transactions or realize anticipated benefits;
- reliance on key personnel;
- regulatory compliance;
- competition;
- changes in laws, regulations and guidelines;
- demand for our products;
- fluctuating prices of raw materials;
- pricing for products;
- ability to supply sufficient product;
- expansion to other jurisdictions;
- damage to our reputation;
- operating risk and insurance coverage;
- negative operating cash flow;

- management of growth;
- product liability;
- product recalls;
- environmental regulations and risks;
- ownership and protection of intellectual property;
- constraints on marketing products;
- reliance on management;
- fraudulent or illegal activity by our employees, contractors and consultants;
- breaches of security at our facilities or in respect of electronic documents and data storage and risks related to breaches of applicable privacy laws;
- government regulations with regards to COVID-19, employee health and safety regulations;
- the duration and impact of COVID-19, and including variants of COVID-19, on our operations;
- regulatory or agency proceedings, investigations and audits;
- additional capital requirements to support our operations and growth plans, leading to further dilution to shareholders;
- conflicts of interest;
- litigation;
- risks related to United States' and other international activities;
- risks related to security clearances and risks relating to the ownership of KWESST common shares ("Common Shares") such as potential volatility of share price; and
- no assurance of active market for Common Shares.

Although the forward-looking statements contained herein are based upon what we believe are reasonable assumptions, investors are cautioned against placing undue reliance on this information since actual results may vary from the forward-looking statements. Certain assumptions were made in preparing the forward-looking statements concerning availability of capital resources, business performance, market conditions and customer demand.

BUSINESS OVERVIEW

Corporate Information

We are an early commercial-stage defense technology company focused on the development and commercialization of next-generation tactical systems that meet the requirements of security forces and personal defense for overmatch capability against adversaries.

Key market segments and solutions addressed by our technologies are:

(i) breakthrough technology in non-lethal systems with broad application, including law enforcement and personal defense,
(ii) modernized digitization of tactical forces for shared situational awareness and targeting, and
(iii) counter-measures against threats such as drones, lasers and electronic detection.

For more details on KWESST products and markets, refer to the amended Annual Information Form dated April 15, 2021. This document and other information about KWESST are available on SEDAR under the Company's profile at www.sedar.com.

Major Highlights – Q1 Fiscal 2022

The following is a summary of the major highlights that occurred during Q1 Fiscal 2022:

- On October 13, 2021, we announced that we are accelerating the readiness of deployable and man-wearable Battlefield Laser Detection System ("BLDS") for first deliveries available by end of Q1 Fiscal 2022, following military interest from a number of NATO land and Special Operation Forces at the signature European defense show, DESI, which took place in London, UK, on September 13 to 18, 2021. While no deliveries took place in Q1 Fiscal 2022, we are in active discussion for a first order with an overseas NATO country for two vehicle-mounted versions of the BLDS for Special Forces light patrol vehicles.

- On November 12, 2021, we announced that General Dynamics Land Systems ("GDLS") has selected KWESST's Phantom™ electronic battlefield decoy as part of its ongoing efforts to develop a next generation multi-million domain mobile capability at the tactical level. If GLDS wins the contract with their United States military customer, we have estimated the potential value for this contract to KWESST could be more than USD $40 million, depending on the number of Phantom™ units per military vehicle. The United States military customer will announce the winner of the tender for 400-500 next generation military vehicles in calendar 2023.
- On November 15, 2021, we conducted live fire demonstration of our initial non-lethal cartridge-based personal defence products for investors near Toronto, Ontario, including an opportunity for these investors to use the devices. Further, on January 14, 2022, we announced the launching of our non-lethal cartridge-based products under the brand PARA OPS™ at the 2022 SHOT Show in Las Vegas held on January 18th to 21st 2022.

- On November 23, 2021, in connection with an updated capital markets strategy, we submitted our initial application to list on The Nasdaq Stock Market ("Nasdaq"). We believe that, if successful, a Nasdaq listing can broaden investor awareness to the market for KWESST's common shares, with a view to supporting shareholder value.

- On December 2, 2021, we announced that we have engaged the New York-based public relations firm AMW Public Relations to lead our public relations, brand strategy, and media communication initiatives.

- On December 8, 2021, our United States military customer accepted the delivery of the final milestone of the US $0.8 million relating to the integration of our TASCS IFM with 81 mortar system. Final payment was received in January 2022. While we expect follow-on customer orders for this solution during Fiscal 2022, there is no assurance of such orders.

- On December 14 and 16, 2021, we announced that we signed a Master Services Agreement with General Dynamics Mission Systems – Canada ("GDMS") to support the development of digitization solutions for future Canadian land C4ISR programs. We estimated this contract to be up to $1 million over the next 12 months.

- On December 15, 2021, we completed the non-cash acquisition of Police Ordnance Company Inc. – see below "Acquisition" for further details. On January 10, 2022, we announced that Police Ordnance Company Inc. received orders from law enforcement agencies for approximately $0.4 million in ARWEN products, all expected to be delivered by the end of Q2 Fiscal 2022.

Update on COVID-19

While COVID-19 has not had a material impact to our business to date, the following is a summary of what we believe may impact our future business given the persistency of COVID-19: disruptions to business operations resulting from quarantines of employees, customers, manufacturers and other third-party service providers in areas affected by the outbreak; disruptions to business operations resulting from travel restrictions, including travel to industry tradeshows; and uncertainty around the duration of the virus' impact.

Despite the global vaccination efforts underway, the extent to which COVID-19 could impact our operations, financial condition, results of operations, and cash flows is highly uncertain and cannot be predicted. Negative financial results, uncertainties in the market, and a tightening of credit markets, caused by COVID-19, or a recession, could have a material adverse effect on our liquidity and ability to obtain financing in the future.

ACQUISITION

To accelerate our growth plans and respond to market opportunities, we have made the following acquisition during Q1 Fiscal 2022.

Police Ordnance

On December 15, 2021, we acquired 2720178 Ontario Inc., an Ontario (Canada) corporation, which owns all of the issued and outstanding shares of Police Ordnance Company Inc., an Ontario (Canada) corporation (together, "Police Ordnance"), herein referred as the "Police Ordnance Acquisition". Located in Bowmanville, Ontario, with ancillary operations in Florida, Police Ordnance owns all intellectual properties to the ARWEN product line of less-lethal launchers, and a proprietary line of 37 mm less-lethal cartridges designed for riot control and tactical teams. Police Ordnance has law enforcement customers across Canada, the United States, and abroad. The Police Ordnance Acquisition provides us with a strategic opportunity to leverage its law enforcement customer base to accelerate growth within our specialty ordnance business.

The fair value of the purchase consideration was $592,822, which comprised of: (i) 277,576 Common Shares, (ii) 200,000 Common Share purchase warrants exercisable at a price of $1.72 per share and expiring on December 15, 2024; and (ii) 61,264 Common Shares contingent on fulfilment of a financial milestone (refer to Note 4 of the Q1 Fiscal 2022 FS for further financial information). While this acquisition is expected to be accretive annually based on historical results, we do not expect it will have a material impact to our overall consolidated results of operations, financial condition, and/or cash flows over the next twelve months.

RESULTS OF OPERATIONS

The following selected financial data has been extracted from Q1 Fiscal 2022 FS.

	Three months ended December 31,	
(Unaudited)	**2021**	2020
		(Adjusted) (1)
Revenue	**$ 17,465**	$ 146,349
Cost of sales	**(25,479)**	(71,564)
Gross profit	**(8,014)**	74,785
Gross margin %	***-45.9%***	*51.1%*
Operating Expenses		
General and administrative	**1,055,140**	539,631
Selling and marketing	**1,346,391**	534,863
R&D	**794,412**	505,247
Total operating expenses	**3,195,943**	1,579,741
Operating loss	**(3,203,957)**	(1,504,956)
Other income (expenses)		
Net finance costs	**(47,642)**	(17,948)
Foreign exchange gain (loss)	**8,745**	(3,385)
Net loss	**$ (3,242,854)**	**$ (1,526,289)**
EBITDA loss	**$ (3,123,175)**	**$ (1,469,607)**
Adjusted EBITDA loss (2)	**$ (2,204,390)**	**$ (1,192,607)**
Loss per share - basic and diluted	**$ (0.07)**	**$ (0.04)**
Weighted average common shares - basic	**49,022,129**	41,392,149

(2) EBITDA and Adjusted EBITDA are non-IFRS measures. See ''Non-IFRS Measures'''. See below for ''Reconciliation of Non-IFRS Measure''.

In the following table, we have reconciled EBITDA and Adjusted EBITDA to the most comparable IFRS financial measure.

	Three months ended December 31,	
(Unaudited)	**2021**	2020
		(Adjusted) (1)
Net loss as reported under IFRS	**$ (3,242,854)**	$ (1,526,289)
Net finance costs	**47,642**	17,948
Depreciation and amortization	**72,037**	38,734
EBITDA loss	**(3,123,175)**	(1,469,607)
Other adjustments:		
Stock-based compensation	**927,530**	273,615
Foreign exchange gain (loss)	**(8,745)**	3,385
Adjusted EBITDA loss	**$ (2,204,390)**	$ (1,192,607)

For Q1 Fiscal 2022, KWESST's net loss was $3.2 million, an increase of $1.7 million over the comparable period, primarily due to lower revenue and higher operating expenses driven by higher headcount and related share-based awards, investment in promoting and advertising our company and products, and to a lesser extent additional professional fees relating to our Nasdaq listing application and Registration Statement with the United States Securities Exchange Commission ("SEC").

Share-based compensation accounted for most of the adjustments to EBITDA. The significant increase in share-based compensation in Q1 Fiscal 2022 compared to the same quarter in Fiscal 2021 is mainly due to granting a higher volume of options at a higher fair value per option for recruiting and retaining directors, executives and key business consultants.

Revenue and Gross Profit

	Three months ended December 31,		2020 to 2021
(Unaudited)	**2021**	2020	**%**
Digitization and counter threat systems	**$ 16,640**	$ 138,934	-88%
Other	**825**	7,415	-89%
Total revenue	**$ 17,465**	$ 146,349	-88%
Gross profit	**$ (8,014)**	$ 74,785	
Gross margin	***-45.9%***	*51.1%*	

Total revenue declined by 88% during Q1 Fiscal 2022 compared to same quarter in Fiscal 2021 mainly due to the completion of the USD$0.8 million military contract, awarded in December 2020, during the quarter where we recognized the remaining 2.7% of the total revenue. While we won a new contract with GDMS in December 2021 (see Business Overview section of this MD&A), we began delivering on this contract only from Q2 Fiscal 2022. We expect revenue to ramp up over the next few quarters with new military contracts, coupled with the official launch of our PARA OPS™ product line in January 2022 for non-lethal personal defense, with low-rate initial production ("LRIP") shipments expected to commence in April 2022 subject to timely receipt of ATF classification. We anticipate transitioning from LRIP to full production with strategic partners by the end of summer 2022.

The negative gross profit in Q1 Fiscal 2022 is largely due to final adjustment to estimated costs incurred relating to the above contract for the United States military contract. Our gross profit will continue to fluctuate from quarter-to-quarter with the anticipated new product mix and sales volume.

Operating Expenses (OPEX)

	Three months ended December 31,		2020 to 2021
(Unaudited)	**2021**	2020	**%**
		(Adjusted) [(1)]	
General and administrative	**$ 1,055,140**	$ 539,631	96%
Selling and marketing	**1,346,391**	534,863	152%
Research and development	**794,412**	505,247	57%
Total operating expenses	**$ 3,195,943**	$ 1,579,741	102%

Overall, our OPEX increased by 102% or $1.6 million for the current quarter over the comparable prior period, including $0.7 million of additional share-based compensation (non-cash item) or 40 percentage points of the total increase. The increase in OPEX was driven primarily by:

- G&A increased by 96% or $0.5 million primarily due to augmenting the senior management team with two full-time executives and recruiting independent directors and other staff, which led to an increase in total personnel costs including $0.2 million of additional share-based compensation over Q1 Fiscal 2021. Additionally, in the current quarter we incurred $0.2 million in professional fees in connection with our Nasdaq application and the preparation of the Registration Statement filing with the SEC.

- S&M increased by 152% or $0.8 million primarily due to making a significant investment in promoting and increasing awareness about us and our product offerings, including attending two investor conferences in the United States and engaging strategic advisors. This included The Officer Tatum LLC who joined us in July 2021 as our strategic advisor and advocate for our non-lethal PARA OPS™ product line for law enforcement and personal defense in the United States; the STRYK Group in September 2021 to assist us with the commercialization of our PARA OPS™ product line including a new website (www.para-ops.com); and AMW Public Relations in November 2021 to lead our United States public relations, brand strategy and media communications initiatives. The increase in S&M includes $0.3 million of additional share-based compensation in lieu of cash consideration to certain strategic advisors.

- R&D increased by 57% or $0.3 million primarily due to an increase in headcount to accelerate product development. The increase in personnel costs included $0.2 million of additional share-based compensation over Q1 Fiscal 2021.

Net Finance Costs

Total finance costs for Q1 Fiscal 2022 were $47,642, a 165% increase over the comparable prior period primarily due to the accretion cost relating to accrued royalties payable to DEFSEC Corporation for the acquisition of the technology known at the time as the Low Energy Cartridge system, branded as PARA OPS™.

SUMMARY OF QUARTERLY RESULTS

The following tables summarize selected results for the eight most recent completed quarters to December 31, 2021 (unaudited).

($ in thousands, except per share)	March 2021 (Q2 FY21)	June 2021 (Q3 FY21)	September 2021 (Q4 FY21)	December 2021 (Q1 FY22)
Revenue	$ 448	$ 522	$ 160	$ 17
Cost of sales	$ 332	$ 315	$ 80	$ 25
Gross profit	$ 116	$ 207	$ 80	$ (8)
Gross margin %	26.0%	39.6%	49.7%	-45.9%
Operating expenses	$ 2,376	$ 2,798	$ 2,925	$ 3,196
Operating loss	$ (2,260)	$ (2,591)	$ (2,845)	$ (3,204)
Other income (expenses)	$ (17)	$ (37)	$ (38)	$ (39)
Net loss	**$ 2,277**	**$ 2,628**	**$ 2,883**	**$ 3,243**
Net finance costs	$ 15	$ 28	$ 19	$ 48
Depreciation and amortization	$ 35	$ 13	$ 53	$ 72
EBITDA loss	**$ 2,227**	**$ 2,587**	**$ 2,811**	**$ 3,123**
Adjusted EBITDA loss	**$ 1,627**	**$ 2,017**	**$ 1,831**	**$ 2,204**
Loss per share - basic and diluted	**$ (0.05)**	**$ (0.06)**	**$ (0.06)**	**$ (0.07)**
Weighted average common shares - basic	42,141,523	46,016,645	47,745,525	49,022,129

($ in thousands, except per share)	March 2020 (Q2 FY20)	June 2020 (Q3 FY20)	September 2020 (Q4 FY20)	December 2020 (Q1 FY21)
Revenue	$ 49	$ 600	$ 213	$ 146
Cost of sales	$ 8	$ 144	$ 95	$ 72
Gross profit	$ 41	$ 456	$ 118	$ 74
Gross margin %	83.4%	76.1%	55.1%	55.1%
Operating expenses	$ 632	$ 1,048	$ 2,392	$ 1,580
Operating loss	$ (591)	$ (626)	$ (2,274)	$ (1,506)
Other income (expenses)	$ (108)	$ (186)	$ 248	$ (21)
Net loss	**$ 699**	**$ 812**	**$ 2,026**	**$ 1,527**
Net finance costs	$ 25	$ 91	$ (45)	$ 18
Depreciation and amortization	$ 34	$ 69	$ 15	$ 39
EBITDA loss	**$ 640**	**$ 652**	**$ 2,056**	**$ 1,470**
Adjusted EBITDA loss	**$ 539**	**$ 392**	**$ 573**	**$ 1,193**
Loss per share - basic and diluted	**$ (0.02)**	**$ (0.03)**	**$ (0.07)**	**$ (0.04)**
Weighted average common shares - basic	28,695,065	30,393,359	33,024,736	41,392,149

Quarterly Results Trend Analysis

There is no material change to our quarterly results trend from our disclosure in our annual MD&A dated November 23, 2021, except that we expect further volatility with our quarterly revenue during Fiscal 2022 due to the launch of PARA OPS^{TM} products, the Police Ordnance Acquisition, and anticipated new military contracts.

FINANCIAL CONDITION, LIQUIDITY, AND CAPITAL RESOURCES

Financial Condition

The following table summarizes our financial position:

(Unaudited)	**December 31, 2021**	September 30, 2021
Assets		
Current	**$ 2,209,012**	$ 4,055,697
Non-current	**4,944,500**	4,662,149
Total assets	**$ 7,153,512**	$ 8,717,846
Liabilities		
Current	**$ 1,342,153**	$ 1,159,490
Non-current	**1,402,914**	1,434,628
Total liabilities	**2,745,067**	2,594,118
Net assets	**$ 4,408,445**	$ 6,123,728
Working capital (1)	**$ 866,859**	$ 2,896,207

Our working capital was $0.9 million at December 31, 2021, a decrease of $2.0 million from September 30, 2021. This decrease was mainly driven by our net operating loss for the current quarter, which was partially offset by the net assets assumed in the Police Ordnance Acquisition.

Total assets decreased by $1.6 million from September 30, 2021, mainly due to $1.8 million decrease in currents assets driven by the $1.9 million net use of cash to fund our operating activities, net by the assets assumed in the Police Ordnance Acquisition. This was partially offset by an increase of $0.3 million in non-current assets, largely due to the increase in intangible assets from capitalized development costs for our Phantom™ and PARA OPS™ systems and acquired intangible assets from Police Ordnance.

Total liabilities increased by $0.2 million from September 30, 2021, mainly due to additional liabilities from the Police Ordnance Acquisition.

Liquidity and Capital Resources

Overview

Our primary sources of capital to date have been from security offerings, exercise of stock options and warrants, and, to a lesser extent, pre-commercial revenue. At December 31, 2021, our cash position was $0.7 million, a decrease of $2.0 million since September 30, 2021 primarily due to incurring a net operating loss for Q1 Fiscal 2022, offset by an increase in cash of $0.2 million from the Police Ordnance Acquisition.

While we are confident we will be awarded additional customer contracts in Fiscal 2022, we expect additional capital will be required to initially fund these potential contracts, our commercialization efforts in the United States for the launch of the Para OPS™ system, R&D activities and our working capital requirements over the next twelve months. Potential sources of capital may include additional equity and/or debt financings, Canadian ITCs for SR&ED activities, and other government funding such as Innovation Solutions Canada. Based on management's current projection, the minimum additional funding required to remain in business for at least the next 12 months is approximately $8 million. While we are currently in active discussions with current and prospective investors, there can be no assurance that we will be able to obtain the capital sufficient to meet any or all of our needs. In our view, the availability of capital will be affected by, among other things, capital market conditions, the success of our PARA OPS™ system commercialization efforts, timing for winning new customer contracts, potential acquisitions, and other relevant considerations. In the event we raise additional funds by issuing equity securities, our existing shareholders will likely experience dilution, and any additional incurrence of indebtedness would result in increased debt service obligations and could require us to agree to operational and financial covenants that could further restrict our operations. Any failure to raise additional funds on terms favorable to us or at all may require us to significantly change or curtail our current or planned operations in order to conserve cash until such time, if ever, that sufficient proceeds from operations are generated, and could result in us not being in a position to advance our commercialization strategy or take advantage of business opportunities.

Cash Flows

Our approach to managing liquidity is to ensure, to the extent possible, that we always have sufficient liquidity to meet our liabilities as they come due. We regularly perform cash flow forecasts to ensure that we have sufficient cash to meet our operational needs while maintaining sufficient liquidity. At this time, we do not use any derivative financial instruments to hedge our currency risk.

The following table summarizes KWESST's consolidated statements of cash flows for the respective periods:

	Three months ended December 31,	
(Unaudited)	**2021**	2020
Total cash provided by (used in):		
Operating activities	**$ (1,864,760)**	$ (1,229,876)
Investing activities	**(68,960)**	(329,316)
Financing acitivities	**(20,401)**	186,795
Net cash outflows	**$ (1,954,121)**	$ (1,372,397)
Cash, beginning of period	**2,688,105**	3,073,760
Cash, end of period	**$ 733,984**	$ 1,701,363

Cash used by operating activities

With the additional capital raised during Fiscal 2021, we continued to invest significantly across the organization and product development. As an early-stage company with various products in the pipeline (pre-commercialization phase), our revenue remains low and insufficient to cover the increase in our overhead costs, professional fees, advertising and promotion costs, and R&D costs. As a result, cash flow used in operating activities was $1.9 million for Q1 Fiscal 2022, compared to $1.2 million in the comparable prior quarter.

Cash used by investing activities

Cash flow used in investing activities decreased in Q1 Fiscal 2022 compared to Q1 Fiscal 2021 mainly due to $0.2 million net cash acquired from the Police Ordnance Acquisition, coupled with lower capitalized development costs.

Cash provided by financing activities

The $0.2 million decrease in cash provided by financing activities in Q1 Fiscal 2022 over Q1 Fiscal 2021 was primarily driven by no exercise of options in the current quarter.

Capital Management

Our objective in managing our capital is to safeguard KWESST's ability to continue as a going concern and to sustain future development of the business. KWESST senior management is responsible for managing the capital through regular review of financial information to ensure sufficient resources are available to meet operating requirements and investments to support its growth strategy. The Board of Directors is responsible for overseeing this process. From time to time, we could issue new common shares or debt to maintain or adjust our capital structure. We are not subject to any externally imposed capital requirements.

KWESST's capital is composed of the following:

(Unaudited)	**December 31, 2021**	September 30, 2021
Debt:		
Lease obligations	**$ 307,741**	$ 307,909
Borrowings	**80,783**	53,251
Equity:		
Share capital	**17,668,904**	17,215,068
Contingent shares	**83,319**	-
Warrants	**1,920,389**	1,848,389
Contributed surplus	**3,373,241**	2,458,211
Accumulated other comprehensive loss	**(5,605)**	(8,991)
Accumulated deficit	**(18,631,803)**	(15,388,949)
Total capital	**$ 4,796,969**	$ 6,484,888

At December 31, 2021, our contractual obligations and commitments were as follows:

Payment due:	**Total**	**Within 1 Year**	**1 to 3 years**	**3 to 5 years**
Minimum royalty commitments	**$ 2,500,000**	$ -	$ 150,000	$ 2,350,000
Accounts payable and accrued liabilities	**1,180,189**	1,180,189	-	-
Lease obligations	**382,200**	78,000	187,200	117,000
Short-term rental obligations	**25,938**	25,938	-	-
Other commitments	**50,712**	50,712	-	-
Borrowings	**90,000**	30,000	60,000	-
Total contractual obligations	**$ 4,229,039**	**$ 1,364,839**	**$ 397,200**	**$ 2,467,000**

Equity

During Q1 Fiscal 2022, we issued 277,576 common shares and 200,000 warrants exercisable at $1.72 each to the selling shareholders of Police Ordnance. These warrants will expire on December 15, 2024. Additionally, we issued 250,000 common shares in connection with the exercise of 250,000 warrants issued as part of the GhostStep technology acquisition in Fiscal 2020. This was a cashless exercise to settle the annual fee payable on December 31, 2021, to SageGuild LLC (the seller of the GhostStep technology).

OFF-BALANCE SHEET ARRANGEMENTS

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

RELATED PARTY TRANSACTIONS

Refer to Note 9 of Q1 Fiscal 2022 FS for disclosure about KWESST's related party transactions conducted in the normal course of business.

FINANCIAL INSTRUMENTS AND OTHER INSTRUMENTS

We recognize financial assets and liabilities when we become party to the contractual provisions of the instrument. On initial recognition, financial assets and liabilities are measured at fair value plus transaction costs directly attributable to the financial assets and liabilities, except for financial assets or liabilities at fair value through profit and loss, whereby the transactions costs are expensed as incurred.

Refer to Note 9 of the Q1 Fiscal 2022 FS for further disclosure on KWESST's financial instruments.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Refer to Note 2(g) of the Fiscal 2021 audited consolidated financial statements for a discussion of the accounting policies and estimates that are critical to the understanding of our business operations and the results of our operations.

OUTSTANDING SHARE INFORMATION

At December 31, 2021, KWESST's authorized capital consists of an unlimited number of common shares with no stated par value. There were 49,508,997 outstanding and issued common shares as at December 31, 2021.

DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROLS OVER FINANCIAL REPORTING

Disclosure controls and procedures ("DC&P") are intended to provide reasonable assurance that material information is gathered and reported to senior management to permit timely decisions regarding public disclosure. Internal controls over financial reporting ("ICFR") are intended to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with IFRS accounting principles.

TSX Venture-listed companies are not required to provide representations in their annual and interim filings relating to the establishment and maintenance of DC&P and ICFR, as defined in Multinational Instrument MI 52-109. In particular, the CEO and CFO certifying officers do not make any representations relating to the establishment and maintenance of (a) controls and other procedures designed to provide reasonable assurance that information required to be disclosed by the issuer in its annual filings, interim filings or other reports filed or submitted under securities legislation is recorded, processed, summarized and reported within the time periods specified in securities legislation, and (b) processes to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with the issuer's GAAP.