

## FRANKLY INC.

# Management's Discussion & Analysis

*For the Three and Nine Month Periods Ended September 30, 2016 and 2015*

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### INTERIM MANAGEMENT'S DISCUSSION & ANALYSIS

#### Date

This management's discussion and analysis ("MD&A") relates to the financial condition and results of operations of Frankly Inc., together with its owned subsidiaries, as of November 29, 2016 and is intended to supplement and complement the Company's unaudited interim condensed consolidated financial statements for the three and nine month periods ended September 30, 2016 and 2015 and the notes thereto. Readers are encouraged to read the cautionary Forward-Looking Statements included with this MD&A and to consult the Company's audited annual consolidated financial statements for the 2015 financial year and corresponding notes to the financial statements which are available on SEDAR website at [www.sedar.com](http://www.sedar.com). The September 30, 2016 unaudited interim condensed consolidated financial statements and MD&A are presented in U.S. dollars, unless otherwise noted, and have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board.

Where we say "we", "us", "our", the "Company" or "Frankly", we mean Frankly Inc. or Frankly Inc. and/or one or more or all of its subsidiaries, as it may apply.

#### Forward-Looking Statements

*This document contains forward-looking statements relating to the Company's operations or to the environment in which it operates, which are based on the Company's operations, estimates, forecasts and projections. Forward-looking statements include, but are not limited to, statements with respect to the nature of the usage of the Company's software-as-a-service platform, the post-acquisition strategy and capabilities of the Company, changing audience and advertising demand for local news and media, needs for new technology from local news and media industry, the vertical and regional expansion of the Company's market and business opportunities, the expansion of the Company's product offering, and the estimated number of smart device users, local news and media businesses and digital advertisers in the future. These statements are not guarantees of future performance and involve risks and uncertainties that are difficult to predict or are beyond the Company's control. A number of important factors including those set forth in other public filings could cause actual outcomes and results to differ materially from those expressed in these forward looking statements. Consequently, readers should not place undue reliance on such forward-looking statements. In addition, these forward-looking statements relate to the date on which they are made.*

*Forward-looking information reflects the Company's current beliefs and is based on information currently available to the Company and on assumptions it believes to be not unreasonable in light of all of the circumstances.*



*Forward-looking information is subject to known and unknown risks, uncertainties and other factors that may cause the actual results, activities, performance or achievements of the Company to be materially different from that expressed or implied by such forward-looking statements. Such material factors and assumptions include, but are not limited to: Frankly's ability to successfully integrate any acquired businesses; Frankly's overall ability to effectively respond to technology affecting the industry and increasing competition from other technology providers; Frankly's ability to retain existing customers or add new ones, and maintain the level of customer engagement and usage; Frankly's user growth and engagement on mobile devices which will depend upon effective integration with mobile operating systems, networks, and standards which Frankly does not control; Frankly's ability to effectively compete with other content management, social engagement and monetization platform providers serving in the same markets; the recent consolidation and vertical integration within the local news broadcasting industry; the business conditions of Frankly's customers particularly in the local news broadcasting and adjacent industries; Frankly's ability to expand its customer base to global markets; Frankly's ability to protect its intellectual property; Frankly's ability to access capital markets, as well as the additional risks identified in this MD&A under the heading "Risk Factors".*

*Management believes that cash on hand, cash to be generated from future operations and cash available under existing and future credit facilities will be sufficient to meet the Company's needs. However, circumstances such as the Company's ability to achieve sustainable profitable operations, ability to raise additional financing, the loss of significant customers or deterioration in the economy, particularly in the media and advertising industries, could cause these sources of cash and liquidity to be insufficient. There can be no assurances that the Company will be successful in achieving profitable operations or that it will be able to raise additional cash needed to finance operations, if required.*

*Although the Company has attempted to identify important factors that could cause actual actions, events or results to differ materially from those described in forward-looking information, there may be other factors that cause actions, events or results to differ from those anticipated, estimated or intended. Forward-looking information contained herein is made as of the date of this MD&A and, other than as required by law, the Company disclaims any obligation to update any forward-looking information, whether as a result of new information, future events or results or otherwise.*

## **Business Background and Overall Performance**

### **2014 Qualifying Transaction**

Frankly Inc. ("Frankly"), formerly named WB III Acquisition Corp. ("WB III"), was incorporated under the laws of the Province of Ontario on June 7, 2013. WB III was initially classified as a Capital Pool Company (a "CPC"), as defined in Policy 2.4 of the TSX-V Corporate Finance Manual.

On December 23, 2014, WB III Subco Inc., a wholly owned subsidiary of WB III, merged with TicToc Planet Inc. ("TicToc") which was incorporated in the state of Delaware on September 10, 2012 and is located in San Francisco, California. The transaction was structured as a reverse triangular merger under the Delaware General Corporation Law, as a result of which TicToc became a wholly owned subsidiary of WB III. Subsequent to the transaction, WB III changed its name to Frankly Inc. and TicToc's name was changed to Frankly Co.

As a result of the merger, the former shareholders of TicToc acquired control of the Company as they owned the majority of the outstanding shares of the Company upon completion of the merger transaction. This transaction resulted in a reverse merger with TicToc being identified as the acquirer for accounting purposes and the net assets of WB III being recorded at fair value at the date of the transaction. Consequently, the historical results of operations up to the date of the merger are those of TicToc. We refer to these transactions as the "Qualifying Transaction."

### ***2015 Acquisition of Worldnow***

On July 28, 2015, we signed an agreement (the "Unit Purchase Agreement") to purchase the outstanding units of Gannaway Web Holdings, LLC, operating as Worldnow, for total consideration of \$45 million. On August 25, 2015 (the "Closing Date"), the Company completed this acquisition of Worldnow. Subsequent to the acquisition, Worldnow changed its name to Frankly Media LLC.

Under the terms of the Unit Purchase Agreement, on August 25, 2015, we paid \$10 million in cash, \$20 million in Restricted Shares (the "Share Consideration") and executed the Worldnow Promissory Notes for \$15 million, bearing simple interest at a rate of 5% per year and due August 31, 2016. The Worldnow Promissory Notes were refinanced under the Raycom Loan transaction. The number of Restricted Shares comprising the Share Consideration was 9,772,204 shares, of which 3,021,072 shares were issued to GEI (the "GEI Shares") and 6,751,132 shares were issued to Raycom (the "Raycom Share Consideration Shares").

All of the Restricted Shares comprising the Share Consideration were subject to a lock-up agreement. The lock-up period with respect to securities representing 50% of the value of the Share Consideration expired upon the first anniversary of the Closing Date of the transaction in August 2016 and the lock-up period with respect to the remainder of the Share Consideration will expire upon the second anniversary of Closing Date of the transaction in August 2017. The lock-up periods are subject to earlier expiry upon the occurrence of certain events that constitute a change of control of the Company. Further, upon expiry of the lock-up periods, the Restricted Shares will be converted into common shares on a 1:1 basis. In August 2016, all of the Raycom Share Consideration Shares were converted into 6,751,132 common shares, upon waiver by us of the lock-up restriction for the Raycom Restricted Shares and half of the GEI Shares were converted into 1,510,536 common shares for a total of 8,261,668 common shares. The remaining 1,510,536 GEI Shares are subject to lock-up until August 2017.

In connection with the acquisition, additional units of Worldnow were issued to us for the assumption of a \$400,000 liability of Worldnow due to a third-party vendor. We satisfied the liability by issuing 195,446 common shares to the vendor.

### ***Raycom Transaction***

On September 1, 2016, we repaid \$15 million of the Worldnow Promissory Notes with proceeds from the Raycom Loan transaction. The Raycom Loan transaction, as more fully described herein under "Liquidity and Capital Resources" below, provided us with net proceeds of \$500,000 after such repayment, substantially improving our liquidity position.

### ***Goodwill Impairment***

Due to the continued decline of our common share price during the third quarter of 2016, we performed an interim goodwill impairment analysis as of September 30, 2016. As a result, a portion of the goodwill related to the Worldnow acquisition was impaired and we recorded a non-cash goodwill impairment charge of \$12.9 million. See further discussion below "Discussion of Operations."

### ***Description of the Business***

Frankly is headquartered in San Francisco, California, with offices in New York City. Frankly provides a white-labeled, integrated software platform to media companies and brands which use its technology to get their content onto multiscreen devices, increase social interaction on those multiscreen experiences, and enable digital advertising. The platform consists of a content management system, native application and responsive web framework, and digital advertising solutions. It is used by around 140 US local news stations covering approximately 60 million monthly users. The Company also offers digital advertising



services for approximately 200 U.S. digital properties. The Company plans to enhance the platform by providing data analytics, proprietary chatting features and cutting-edge infrastructure technology.

Since its inception, Frankly built its chat offerings and related technology. Until 2014, the Company developed and marketed its legacy instant messaging apps, Frankly Chat and TicToc Plus, both of which are no longer a material part of its business but became the foundation for its chat platform. Since the second quarter of 2014, the Company has increasingly focused its efforts on the marketing and development of its chat platform for brands and businesses to enhance their interaction with fans and customers. It was launched in October 2014 and has served several customers including United Nations Foundation, the Sacramento Kings and Victoria's Secret.

Through the acquisition of Frankly Media during the 3<sup>rd</sup> quarter of 2015, Frankly became a software-as-a-service provider of content management and digital publishing software, also offering related digital advertising services for local media sites on the web and mobile. The SaaS platform enables site owners to design, build, and host content publishing sites, to manage media assets on all digital platforms and to interact with end users. The Company's advertising teams source national and local advertising for its customers to distribute over multiple consumer devices. The chat platform became a meaningful part of the product roadmap for the integrated content platform.

As a combined business, post acquisition, Frankly is now positioned to offer an integrated white-labeled platform for media customers to create, distribute, analyze and monetize their content across all of their digital properties on the web, mobile and TV.

### **Market**

Prior to the acquisition of Frankly Media, the Company primarily operated in the instant messaging application and platform market. The market consists of myriad brands and businesses that are in need of instant messaging solutions for their Internet and mobile properties, as well as end users who used primarily smart phones to communicate over instant messaging apps.

After the acquisition, the Company's market opportunity shifted and expanded to the broader market of integrated technology platforms where content management and over-the-top ("OTT") publishing solutions, instant messaging-based engagement/monetization platforms, and digital advertising converge. In the near term, the primary customers of the Company in this market are local news broadcasters and media groups in the US. In addition, the Company sees opportunity in adjacent verticals such as other local media as well as global customers for future growth.

The US local news and media market has been rapidly adopting OTT publishing and native mobile platforms for reaching end users on new generations of devices. The increasing number of consumers who have abandoned cable and over the air access to television programming in favor of online access may create further opportunities for the Company's products and services.

Especially, the local news and media audience of new, younger generations demand social networking and multiscreen experiences with the content. The Company's capability to provide one-stop shop to meet those needs for media companies and brands will become more valuable.

Digital advertising over local content and mobile devices is the sector to be developed further in terms of both technology and market size. The local media companies are looking for a better solution to run their digital advertising business, and the overall mobile advertising sector is being quickly developed, especially with capabilities to hyper-target local advertising based on data and mobility. The Company believes its broad reach among local media and technology can be benefited from the future development of the digital advertising markets.



In all, the Company believes there are significant opportunities to increase the distribution of its products and services.

### ***Factors Concerning the Company's Financial Performance and Results of Operations***

The Company believes that the most significant factors and trends that affect its financial performance and results of operations are as follows:

#### *Retention and acquisition of the content platform customers*

The Company is currently serving a large number of customers with its content platform, and competing for new customers with other technology providers in the market. While a typical customer contract runs for multiple years, the retention and ongoing acquisition of new customers will have a material impact on the Company's financial performance. Increasing competition may affect the Company's ability to retain existing customers, and acquire new customers.

#### *Development of new products and services*

The Company continues to upgrade the quality and improve the features of its products and services. Given the high level of competition in the market, and ever changing technology needs of its customers, the Company's successful development of new products and services will affect its financial outcome in the mid and long term. The complexity of developing new technology in a rapidly changing marketplace may increase the Company's development costs.

#### *Demand for national and local advertising*

The Company generates a portion of its revenue from the sale of national and local online advertising inventory. Therefore, the Company's available supply of advertising inventory, general demand for the Company's advertising inventory and other marketplace factors have the potential to impact the Company's financial performance.

#### *The Company's ability to improve and optimize advertising technology*

The Company strives to employ the latest technology to monetize its advertising inventory. The success of the Company's efforts to optimize the process by which it sells its advertising inventory may impact the Company's financial performance.

#### *Customer's adoption of native mobile technology and platform*

The local news and general media industries are expected to adopt native mobile technology and platforms to better serve their audience. The Company's ability to provide compelling native mobile offerings to its existing and potential customers and their adoption of mobile platforms will have an impact on Company's financial performance. Mobile software technology is rapidly changing which has the potential to adversely affect the Company's mobile development expenses.

#### *The demand for mobile advertising*

The native mobile digital advertising is still at a developing stage, and therefore the future demand and actual adoption of advertisers are hard to forecast. The volatility in mobile advertising demand may have an adverse impact on the Company's financial performance.

#### *Consolidation and vertical integration of the US local media industry*



The local news and media industry in the United States has been going through industry-wide consolidation led by a handful of large media groups. This consolidation may change the purchasing power of the Company's customers as well as the number of customers. In addition, the consolidation may lead to more vertical integration of technology providers in the market, with the potential to alter the market landscape.

#### *Enhancing user engagement*

The size of Frankly offerings' user base and the users' level of engagement are integral to the Company's success. The Company's financial performance is impacted by its success in adding, retaining, and engaging active users of Frankly's offerings. The Company aims to ensure that Frankly's platform and application offerings are perceived as useful, reliable, and trustworthy in order to attract or retain users and increase the frequency and duration of their engagement.

#### *General supply and demand for integrated technology platform of content management, user engagement and advertising solutions*

The Company plans to offer an integrated platform of content management system ("CMS"), web and mobile publishing, social engagement and monetization. The market for the offering is in flux and is served by a diverse array of technology providers. Therefore, not only customer needs but also competition among suppliers may have a material impact on the mid and long term financial outcome of the Company.

#### *Uncertain competitive conditions*

The Company faces competition in the local news and media market with other technology and SaaS providers, as the market has been adapting to OTT publishing and native mobile platforms for the new generation of audience. Due to the recent industry consolidation and the rapidly changing technology, the future competitive landscape is uncertain. Moreover, many large media companies have the potential to build such technologies in-house given significant growth of digital and multi-screen media services to their audiences.

#### *International expansion*

The Company's primary focus is on the North American market. Also, the content platform would have potential customers outside of the current local market. The Company's ability to successfully expand beyond North America and differentiate itself from its competitors overseas will impact its growth prospects.

#### *Regulatory oversight*

The content platform's primary market is a heavily regulated broadcasting industry. Therefore, regulatory actions and policy changes will have great impact on Frankly's business.

#### *Security and Stability of Platform*

Given the sensitive nature of American news outlets to reach a massive user base, the Company's technology and content platform can be targets of hostile attempts to breach security and integrity of the platform. A coordinated attack on the Company's infrastructure is a risk to the stability of the platform and can be subjected to hostile action by politically or terror motivated foreign and domestic actors.

#### *Hiring and maintaining highly skilled workforce*



The Company intends to hire a significant number of personnel in the coming years, and it expects to face significant competition from other companies in hiring such personnel, particularly in San Francisco Bay Area. As the Company matures, it will need to continue to offer competitive incentives to attract, retain, and motivate employees. The Company's success in attracting, hiring, and integrating excellent personnel, or retaining and motivating existing personnel, will impact its ability to expand effectively. The need for the Company to pay competitive wages and offer competitive incentives may impact its profitability.

## Discussion of Operations

The Company was in the early stage of its business development cycle and had not recorded significant revenues from its operations until it completed the acquisition of Frankly Media on August 25, 2015.

### Selected Financial Information

A summary of selected financial information for the three and nine month periods ended September 30, 2016 and 2015 is as follows:

|                                       | Three month period ended |                       | Nine month period ended |                       |
|---------------------------------------|--------------------------|-----------------------|-------------------------|-----------------------|
|                                       | September 30,<br>2016    | September 30,<br>2015 | September 30,<br>2016   | September 30,<br>2015 |
| Total revenue                         | \$ 6,196,691             | \$ 1,511,930          | \$ 16,664,579           | \$ 1,580,084          |
| Total expenses                        | (20,461,829)             | (5,883,514)           | (33,996,724)            | (11,337,019)          |
| Net loss before tax                   | (14,265,138)             | (4,371,584)           | (17,332,145)            | (9,756,935)           |
| Net loss after tax                    | (14,315,462)             | (4,399,049)           | (17,386,259)            | (9,785,200)           |
| Cash and cash equivalents             | 2,803,013                | 12,412,103            | 2,803,013               | 12,412,103            |
| Total assets                          | 32,592,579               | 59,387,428            | 32,592,579              | 59,387,428            |
| Total liabilities                     | 16,504,786               | 24,468,212            | 16,504,786              | 24,468,212            |
| Shareholders' equity                  | 16,087,793               | 34,919,216            | 16,087,793              | 34,919,216            |
| Net cash used in operating activities | 1,021,948                | (3,282,390)           | 303,524                 | (10,311,102)          |
| Net change in cash                    | (1,529,201)              | (9,399,941)           | (4,751,115)             | (16,427,861)          |
| Loss per share (basic and diluted)    | \$ (0.44)                | \$ (0.17)             | \$ (0.54)               | \$ (0.42)             |

### Non-IFRS Measures

The Company reports earnings before interest, taxes, depreciation and amortization ("EBITDA") and Adjusted EBITDA, which are not financial measures calculated and presented in accordance with IFRS and therefore may not be comparable to similar measures presented by other issuers. EBITDA and Adjusted EBITDA should not be considered in isolation or as a substitute to net income (loss) or any other financial measures of performance or liquidity calculated and presented in accordance with IFRS. The Company defines Adjusted EBITDA as EBITDA, adjusted to exclude certain non-cash charges and other items that we do not believe are reflective of our ongoing operating results. The Company utilizes Adjusted EBITDA internally for purposes of forecasting, determining compensation, and assessing the performance of our business, therefore, we believe this measure provides useful supplemental information that may assist investors in assessing an investment in the Company.



A summary of Net Loss and Adjusted EBITDA for the three and nine month periods ended September 30, 2016 and 2015 is as follows:

|  | Three month period ended |                       | Nine month period ended |                    |
|--|--------------------------|-----------------------|-------------------------|--------------------|
|  | September 30, 2016       | September 30, 2015    | September 30, 2016      | September 30, 2015 |
| <b>Revenue</b>   | \$ 6,196,691             | \$ 1,511,930          | 16,664,579              | 1,580,084          |
| <b>Expenses</b>  |                          |                       |                         |                    |
| Salaries and benefits, net of capitalized software                       | 2,462,016                | 2,364,615             | 8,060,013               | 4,736,106          |
| Technology related costs   | 1,424,577                | 577,050               | 3,896,913               | 1,077,203          |
| Professional fees  | 159,929                  | 269,229               | 539,764                 | 948,981            |
| Consulting fees, net of capitalized software                             | 85,589                   | 381,773               | 452,345                 | 828,727            |
| Advertising and marketing  | 30,829                   | 108,492               | 236,831                 | 454,257            |
| Office and administration  | 699,950                  | 496,018               | 2,148,783               | 1,043,633          |
| Other  | 7,244                    | 37,276                | 20,891                  | 97,440             |
| Revenue sharing expense  | 946,834                  | -                     | 1,030,012               | -                  |
| <b>Total operating expenses, excluding depreciation and amortization</b> | <b>5,816,968</b>         | <b>4,234,453</b>      | <b>16,385,552</b>       | <b>9,186,347</b>   |
| <b>Adjusted EBITDA</b>   | <b>\$ 379,723</b>        | <b>\$ (2,722,523)</b> | <b>279,027</b>          | <b>(7,606,263)</b> |
| Business acquisition related costs                                       | -                        | 968,838               | (3,011)                 | 968,838            |
| Impairment expense   | 12,850,000               | -                     | 12,850,000              | -                  |
| Integration expenses   | -                        | -                     | 163,065                 | -                  |
| Sales tax settlement   | (135,531)                | -                     | 42,616                  | -                  |
| Loss on disposal of assets   | -                        | -                     | 1,093                   | -                  |
| Loss on extinguishment of debt   | 90,573                   | -                     | 90,573                  | -                  |
| Nasdaq uplisting fees  | 410,225                  | -                     | 410,225                 | -                  |
| Stock based compensation   | 276,230                  | 306,681               | 859,799                 | 777,383            |
| Foreign exchange (gain) / loss   | (5,716)                  | (8,637)               | (3,061)                 | (15,484)           |
| <b>EBITDA</b>  | <b>(13,106,058)</b>      | <b>(3,989,405)</b>    | <b>(14,132,272)</b>     | <b>(9,337,000)</b> |
| Depreciation and amortization  | 848,246                  | 305,704               | 2,447,265               | 343,458            |
| Interest expense, net  | 310,834                  | 76,475                | 752,608                 | 76,477             |
| Income taxes   | 50,324                   | 27,465                | 54,114                  | 28,265             |
| <b>Net loss</b>  | <b>\$ (14,315,462)</b>   | <b>\$ (4,399,049)</b> | <b>(17,386,259)</b>     | <b>(9,785,200)</b> |

For purposes of the discussion on the results of operation, reference is made to “former business” and “acquired business.” “Former business” is defined as our operations before the acquisition of Worldnow on August 25, 2015 which consisted solely of the operations in San Francisco, California. “Acquired business” is defined as our operations after the acquisition of Worldnow on August 25, 2015, excluding the former business. The segregation noted above is purely for analytical purposes only to assist in identifying variances pre- and post-acquisition of Worldnow. We do not view our operations as two separate businesses.

### **Results of Operations for the three month periods ended September 30, 2016 and 2015**

The Company incurred a net loss of \$14,315,462 for the three month period ended September 30, 2016 compared to a net loss of \$4,399,049 in the comparable prior year period. Explanations for the material components of this decrease of approximately \$9.9 million are explained below:

The Company had Adjusted EBITDA of \$379,723 for the three month period ended September 30, 2016 compared to \$(2,722,523) in the comparable prior year period. Explanations for the material components of this improvement of approximately \$3.1 million are explained below:

- Total revenue for the three month period ended September 30, 2016 as compared to the comparable prior year period increased by \$4.7 million. On August 25, 2015, Frankly completed its acquisition of Frankly Media, which accounted for the increase in total revenue between the periods noted above, as only one month of Frankly Media revenue was included in the prior year period.

- Total operating expenses, excluding depreciation and amortization for the three month period ended September 30, 2016 as compared to the comparable prior year period increased by approximately \$1.6 million due to the following:
  - Increase in salaries and benefits of \$97,000, of which \$1.1 million related to the acquired business, offset by a decrease of \$960,000 partially attributed to capitalization of \$373,000 of salaries and benefits of the former business for the three month period ended September 30, 2016 compared to \$Nil in the comparable prior year period. Beginning in 2016, Frankly Co. employees began to work on software projects of the Company which met the capitalization criteria as defined by IAS 38 – Intangible Assets. The remaining decrease of \$587,000 was primarily due to \$400,000 decrease in bonus expense;
  - Increase in technology related costs of \$848,000, of which \$991,000 related to the acquired business, offset by a decrease of \$143,000 of technology related costs of the former business due to decrease in costs incurred to support our legacy chat products;
  - Increase in office and administration costs of \$204,000, of which \$324,000 related to the acquired business, offset by a decrease of \$120,000 of office and administration costs of the former business;
  - Increase in revenue sharing expense of \$947,000. Beginning Q2 2016, we began amending certain advertising contracts with our customers to take on additional inventory and credit risk. Revenue recognized under these contracts was historically accounted for on a net basis as we were identified as an agent. Subsequent to the amendments noted above, we are now recognizing revenue on a gross basis (amount billed to advertisers) with amount due to publisher being reflected as a revenue sharing expense.

The above increases in operating expenses were offset by decreases to the following:

- Decrease in professional fees of \$109,000, adjusted to decrease of \$216,000 after excluding \$107,000 related to the acquired business. The decrease of \$216,000 primarily related to \$180,000 legal settlement incurred in Q3 2015;
- Decrease in consulting fees of \$296,000, primarily attributed to decrease in consulting fees incurred to support our legacy chat products.

Other items (below Adjusted EBITDA):

- Decrease in business acquisition related costs of \$969,000 related to acquisition of Worldnow on August 25, 2015. No such costs were incurred in the 2016 period;
- Increase in impairment expense of \$12,850,000 due to goodwill impairment recorded in Q3 2016. Due to the continued decline in our share price during Q3 2016, we tested goodwill for impairment as of September 30, 2016. As a result of the goodwill impairment analysis we concluded there was impairment to our goodwill of \$12,850,000, being the excess of the carrying value over the recoverable amount;
- Increase in Nasdaq uplisting fees of \$410,000 related to professional fees incurred in Q3 2016 in connection with the filing of our S-1 registration statement with the U.S. Securities and Exchange Commission. No such fees were incurred in the 2015 period;

- Increase in depreciation and amortization of \$543,000, of which \$528,000 related to the acquired business;
- Increase in interest expense, net of \$234,000, primarily due to the \$15 million promissory notes issued in connection with the acquisition of Frankly Media and \$14.5 million non-revolving credit facility with Raycom Inc., a related party, which closed on September 1, 2016. The 2015 period included one month interest expense on the \$15 million promissory notes compared to two months in the 2016 period. Further, the 2016 period included one month interest expense on the \$14.5 million non-revolving credit facility.

Cash flows:

- Net change in cash for the three month period ended September 30, 2016 as compared to the comparable prior year period increased by approximately \$7.9 million due to the following: increase in net cash from operating activities of \$4.3 million primarily due to decrease in net loss (adjusted for non-cash items) of \$3.5 million; increase in net cash from investing activities of \$4.0 million primarily due to \$4.5 million net cash used in the acquisition of Worldnow in the 2015 period; offset by decrease in net cash from financing activities of \$728,000 due to \$1.3 million increase in revolving credit facility principal payments partially offset by \$500,000 proceeds from closing of the non-revolving credit facility on September 1, 2016.

***Results of Operations for the nine month periods ended September 30, 2016 and 2015***

The Company incurred a net loss of \$17,386,259 for the nine month period ended September 30, 2016 compared to a net loss of \$9,785,200 in the comparable prior year period. Explanations for the material components of this decrease of approximately \$7.6 million are explained below:

The Company had Adjusted EBITDA of \$279,027 for the nine month period ended September 30, 2016 compared to \$(7,606,263) in the comparable prior year period. Explanations for the material components of this increase of approximately \$7.9 million are explained below:

- Total revenue for the nine month period ended September 30, 2016 as compared to the comparable prior year period increased by \$15.1 million. On August 25, 2015, Frankly completed its acquisition of Frankly Media, which accounted for the increase in total revenue between the periods noted above, as only one month of Frankly Media revenue was included in the prior year period.
- Total operating expenses, excluding depreciation and amortization for the nine month period ended September 30, 2016 as compared to the comparable prior year period increased by approximately \$7.2 million due to the following:
  - Increase in salaries and benefits of \$3.3 million, of which \$5.3 million related to the acquired business, offset by a decrease of \$2.0 million primarily attributed to capitalization of \$1.4 million of salaries and benefits of the former business for the nine month period ended September 30, 2016 compared to \$Nil in the comparable prior year period. Beginning in 2016, Frankly Co. employees began to work on software projects of the Company which met the capitalization criteria as defined by IAS 38 – Intangible Assets. The remaining decrease of \$600,000 was primarily due to approximately \$400,000 decrease in bonus expense;



- Increase in technology related costs of \$2.8 million, of which \$3.3 million related to the acquired business, offset by a decrease of \$484,000 of technology related costs of the former business due to decrease in costs incurred to support our legacy chat products;
- Increase in office and administration costs of \$1.1 million, of which \$1.2 million related to the acquired business;
- Increase in revenue sharing expense of \$1.0 million. Beginning Q2 2016, we began amending certain advertising contracts with our customers to take on additional inventory and credit risk. Revenue recognized under these contracts was historically accounted for on a net basis as we were identified as an agent. Subsequent to the amendments noted above, we are now recognizing revenue on a gross basis (amount billed to advertisers) with amount due to publisher being reflected as a revenue sharing expense.

The above increases in operating expenses were offset by decreases to the following:

- Decrease in professional fees of \$409,000, adjusted to decrease of \$773,000 after excluding \$364,000 related to the acquired business. The decrease of \$773,000 primarily related to legal, audit and accounting fees associated with the Company becoming public at the end of 2014 and the post-closing matters as well as \$180,000 legal settlement incurred in Q3 2015.
- Decrease in consulting fees of \$376,000, adjusted to decrease of \$642,000 after excluding \$266,000 related to the acquired business. The decrease of \$642,000 was partially attributed to capitalization of \$174,000 of consulting fees of the former business for the nine month period ended September 30, 2016 compared to \$Nil in the comparable prior year period. Beginning in 2016, Frankly Co. contractors began to work on software projects of the Company which met the capitalization criteria as defined by IAS 38 – Intangible Assets. The remaining decrease was primarily attributed to decrease in consulting fees incurred to support our legacy chat products.

Other items (below Adjusted EBITDA):

- Decrease in business acquisition related costs of \$972,000 related to acquisition of Worldnow on August 25, 2015. No such costs were incurred in the 2016 period;
- Increase in impairment expense of \$12,850,000 due to goodwill impairment recorded in Q3 2016. Due to the continued decline in our share price during Q3 2016, we tested goodwill for impairment as of September 30, 2016. As a result of the goodwill impairment analysis we concluded there was impairment to our goodwill of \$12,850,000, being the excess of the carrying value over the recoverable amount;
- Increase in integration expenses of \$163,000 related to the integration of the Company's two operating subsidiaries, Frankly Co. and Frankly Media, subsequent to the acquisition of Worldnow. No such expenses were incurred in 2015 period;
- Increase in Nasdaq uplisting fees of \$410,000 related to professional fees incurred in Q3 2016 in connection with the filing of our S-1 registration statement with the U.S. Securities and Exchange Commission. No such fees were incurred in the 2015 period;



- Increase in depreciation and amortization of \$2.1 million, of which \$2.1 million related to the acquired business;
- Increase in interest expense, net of \$676,000, primarily due to the \$15 million promissory notes issued in connection with the acquisition of Frankly Media and \$14.5 million non-revolving credit facility with Raycom Inc., a related party, which closed on September 1, 2016. The 2015 period included one month interest expense on the \$15 million promissory notes compared to eight months in the 2016 period. Further, the 2016 period included one month interest expense on the \$14.5 million non-revolving credit facility.

Cash flows:

- Net change in cash for the nine month period ended September 30, 2016 as compared to the comparable prior year period increased by approximately \$11.7 million due to the following: increase in net cash from operating activities of approximately \$10.6 million primarily due to decrease in net loss (adjusted for non-cash items) of \$7.7 million; increase in net cash from investing activities of \$1.9 million primarily due to \$4.5 million net cash used in the acquisition of Worldnow in the 2015 period offset partially by increase of \$3.2 million of capitalized software costs; offset by decrease in net cash from financing activities of \$871,000 due to \$1.3 million increase in revolving credit facility principal payments partially offset by \$500,000 proceeds from closing of the non-revolving credit facility on September 1, 2016.

## Summary of Quarterly Results

The following table sets out selected consolidated quarterly information for the last eight quarters:

|   | 2014        | 2015        |             |              |              | 2016         |              |              |
|---|-------------|-------------|-------------|--------------|--------------|--------------|--------------|--------------|
|   | Q4          | Q1          | Q2          | Q3           | Q4           | Q1           | Q2           | Q3           |
| Revenue   | \$ 34,565   | \$ 59,261   | \$ 8,893    | \$ 1,511,930 | \$ 5,413,249 | \$ 5,220,270 | \$ 5,247,618 | \$ 6,196,691 |
| Net loss for the period                                     | (6,542,035) | (2,434,640) | (2,951,511) | (4,399,049)  | (3,117,388)  | (1,627,847)  | (1,442,950)  | (14,315,462) |
| Basic and diluted loss per share                            | \$ (0.46)   | \$ (0.11)   | \$ (0.13)   | \$ (0.17)    | \$ (0.10)    | \$ (0.05)    | \$ (0.04)    | \$ (0.44)    |
| <b>Weighted average number of common shares outstanding</b> |             |             |             |              |              |              |              |              |
| Basic and diluted   | 14,202,192  | 22,057,722  | 22,062,949  | 25,996,085   | 32,067,294   | 32,093,331   | 32,093,331   | 32,898,207   |

*This summary of quarterly results should be read in conjunction with the consolidated financial statements and notes included in the Company's annual report.*

Total revenue for the three month period ended September 30, 2016 as compared to the three month period ended June 30, 2016 increased by \$949,000. The sequential increase was primarily due to contractual changes to our advertising program requiring us to recognize gross revenues for select customers on the new program.

## Related Parties Transactions

The following table summarizes related party balances in the statement of financial position as at September 30, 2016 and December 31, 2015:

|  | September 30,<br>2016 | December 31,<br>2015 |
|--|-----------------------|----------------------|
| <b>Statement of financial position</b> |                       |                      |
| Accounts receivable (ii)               | \$ 244,725            | \$ 86,112            |
| Unbilled revenue (ii)                  | 25,000                | -                    |
| Accounts payable (ii)                  | 296,406               | 92,089               |
| Deferred revenue (ii)                  | 19,890                | 79,560               |
| Promissory notes (iii)                 | -                     | 15,000,000           |
| Non-revolving credit facility (iv)     | \$ 11,407,796         | \$ -                 |

The following table summarizes related party transactions for the three and nine month periods ended September 30, 2016 and 2015:

|  | Three month period ended |                       | Nine month period ended |                       |
|--|--------------------------|-----------------------|-------------------------|-----------------------|
|  | September 30,<br>2016    | September 30,<br>2015 | September 30,<br>2016   | September 30,<br>2015 |
| <b>Statement of loss and comprehensive loss</b>            |                          |                       |                         |                       |
| Revenue - Raycom Media (ii)                                | \$ 1,071,999             | \$ 231,809            | \$ 3,262,516            | \$ 231,809            |
| Interest expense, net (Promissory notes) (iii)             | 125,000                  | 62,500                | 500,000                 | 62,500                |
| Interest expense, net (Non-revolving credit facility) (iv) | 165,078                  | -                     | 165,078                 | -                     |
| Consulting fees, net of capitalized software (i)           | \$ -                     | \$ 32,741             | \$ -                    | \$ 108,587            |

- (i) The Company had services agreements with its then ultimate parent company, SK Planet Co. Ltd. ("SK Planet") Korean and U.S. subsidiaries, whereby the affiliated companies provide market research, mobile application development, and support for the Company's back office operations as requested. The agreements provide that all intellectual property interest in all works completed by the affiliated company will be transferred to the Company. Pursuant to the agreements, the Company incurred consulting fees of \$32,741 and \$108,587 for the three and nine month periods ended September 30, 2015, respectively.
- (ii) The Company has various customer service agreements with Raycom Media, Inc., a significant shareholder of the Company.

The Company recorded revenues from Raycom Media, Inc. of \$1,071,999, \$231,809, \$3,262,516 and \$231,809 for the three and nine month periods ended September 30, 2016 and 2015, respectively.

Related party balances with this affiliate in the accompanying statement of financial position as at September 30, 2016 include accounts receivable of \$244,725, unbilled revenue of \$25,000, accounts payable of \$296,406 and deferred revenue of \$19,890. Related party balances with this affiliate in the accompanying statement of financial position as at December 31, 2015 include accounts receivable of \$86,112, accounts payable of \$92,089 and deferred revenue of \$79,560.

- (iii) In connection with the acquisition of Worldnow, the Company executed promissory notes, bearing simple interest at a rate of 5 percent per year, to pay an additional \$15 million in cash on August 31,

2016. The holders of the promissory notes also hold equity in the Company. Interest expense on the promissory notes amounted to \$125,000, \$62,500, \$500,000 and \$62,500 for the three and nine month periods ended September 30, 2016 and 2015, respectively, and is presented within interest expense, net on the interim condensed consolidated statement of loss and comprehensive loss.

- (iv) On September 1, 2016, the Company completed the closing of its financing with Raycom Media Inc. The Company received a non-revolving term line of credit from Raycom in the principal amount of \$14.5 million and, subject to approval of Raycom, an additional available \$1.5 million non-revolving line of credit (collectively, the Loan). The Loan was recorded at fair value of \$11,359,748 with the remaining \$3,140,252 being allocated to the warrants. The carrying value of the Loan at September 30, 2016, net of debt discount, was \$11,407,796. Interest expense on the Loan amounted to \$165,078 for the three and nine month periods ended September 30, 2016, and is presented within interest expense, net on the interim condensed consolidated statement of loss and comprehensive loss.
- (v) Compensation to key management is as follows:

Key management personnel include the directors and corporate officers of the Company who are responsible for planning, directing and controlling business activities. Their compensation for the three and nine month periods ended September 30, 2016 and 2015 is as follows:

|   | Three month period ended |                       | Nine month period ended |                       |
|---|--------------------------|-----------------------|-------------------------|-----------------------|
|   | September 30,<br>2016    | September 30,<br>2015 | September 30,<br>2016   | September 30,<br>2015 |
| Salaries, bonuses and employee benefits       | \$ 334,532               | \$ 477,506            | \$ 1,350,453            | \$ 1,077,504          |
| Stock based compensation (at full fair value) | 269,969                  | -                     | 710,302                 | 2,065,744             |
|   | \$ 604,501               | \$ 477,506            | \$ 2,060,755            | \$ 3,143,248          |

## Disclosure of Outstanding Share Data

As at September 30, 2016, and as of the date of this discussion, the following is a description of the outstanding voting shares (common shares and restricted voting shares), stock options, restricted share units and warrants issued by the Company:

### ***Common shares and restricted voting shares***

The Company's authorized share capital consists of an unlimited number of authorized common shares with no par value and an unlimited number of Class A restricted voting shares with no par value.

The restricted voting shares have the same voting rights as common shares except for voting for the election and removal of directors of the Company. The restricted voting shares participate in dividends and liquidation events in the same manner as common shares. In terms of restrictions on transfer, no restricted voting shares shall be transferred to another party unless an offer to acquire common shares is concurrently made that is identical to the offer for the restricted voting shares in terms of price per share, percentage of outstanding shares to be transferred and in all other material respects.

The following table reflects the continuity of voting shares (both common shares and restricted voting shares) for the nine month period ended September 30, 2016 and the period from September 30, 2016 to November 29, 2016:



|  | Common<br>Shares  | Class A<br>Restricted<br>Voting Shares | Amount               |
|--|-------------------|--|----------------------|
| <b>Balance, January 1, 2016</b>                        | <b>21,998,304</b> | <b>10,095,027</b>                      | <b>\$ 60,376,338</b> |
| Issuance of common shares                              | 2,553,400         | -                                      | 1,000,000            |
| Share issuance costs                                   | -                 | -                                      | (6,040)              |
| Exchange of restricted voting shares for common shares | 8,342,093         | (8,342,093)                            | -                    |
| <b>Balance, September 30, 2016</b>                     | <b>32,893,797</b> | <b>1,752,934</b>                       | <b>\$ 61,370,298</b> |
| Vesting of restricted share units                      | 90,090            | -                                      | 57,685               |
| Exchange of restricted voting shares for common shares | 92,490            | (92,490)                               | -                    |
| <b>Balance, November 29, 2016</b>                      | <b>33,076,377</b> | <b>1,660,444</b>                       | <b>\$ 61,427,983</b> |

### Stock options

On April 1, 2015, the Company adopted an amended and restated equity incentive plan, which amends and restates the equity incentive plan which was previously established as of December 23, 2014.

Under the terms of the Company's Equity Incentive Plan (the "Plan"), the maximum number of shares reserved for issuance under the Plan was 10% of the issued common shares on a rolling basis. On January 22, 2016, the Company and its Board of Directors amended the Plan to have a fixed 5,715,105 shares reserved for issuance of both stock options and restricted share units.

Options may be exercisable over periods of up to 10 years as determined by the Board of Directors of the Company and the exercise price shall not be less than the closing price of the shares on the day preceding the award date, subject to regulatory approval.

The following table reflects the continuity of stock options for the nine month period ended September 30, 2016 and the period from September 30, 2016 to November 29, 2016 (all options are exercisable into one common share):

|  | Number of Shares<br>Issuable under Options | Exercise Price per<br>Share (US\$) | Expiry Date      |
|--|--|------------------------------------|------------------|
| <b>Options outstanding, January 1, 2016</b>    | <b>2,393,755</b> *                         |                                    |                  |
| Issued   | 2,884,500                                  |                                    |                  |
| Exercised                                      | -  |                                    |                  |
| Forfeited or expired                           | (1,002,548)                                |                                    |                  |
| <b>Options outstanding, September 30, 2016</b> | <b>4,275,707</b>                           |                                    |                  |
| Issued - November 1, 2016                      | 8,000                                      | \$ 0.75                            | November 1, 2026 |
| Forfeited or expired                           | (84,713)                                   |                                    |                  |
| <b>Options outstanding, November 29, 2016</b>  | <b>4,198,994</b>                           |                                    |                  |

\* Includes 515,802 options granted to the Company's Agent as a part of Agent's commission on completion of a private placement.

### Restricted share units

On April 1, 2015, the Company adopted an amended and restated equity incentive plan, which amends and restates the equity incentive plan which was previously established as of December 23, 2014.

The restated plan allows the Company to award restricted share units to officers, employees, directors and consultants of Frankly and its subsidiaries upon such conditions as the board may establish, including the attainment of performance goals recommended by the Company's compensation committee. The purchase price for common shares of the company issuable under each Restricted Share Unit ("RSU")



award, if any, shall be established by the board at its discretion. Shares issued pursuant to any RSU award may be made subject to vesting conditions based upon the satisfaction of service requirements, conditions, restrictions, time periods or performance goals established by the board.

The maximum aggregate number of shares that may be issued under the restated plan pursuant to the exercise of RSUs shall not exceed 2,205,772 shares. As previously contemplated pursuant to the equity incentive plan, the maximum number of common shares of Frankly which may be reserved and set aside for issuance upon the grant or exercise of option awards under the restated plan is 10 percent of Frankly's common shares issued and outstanding from time to time on a non-diluted basis.

On January 22, 2016, the Company and its Board of Directors amended the Plan to have a fixed 5,715,105 shares reserved for issuance of both stock options and restricted share units.

The following table reflects the continuity of RSUs for the nine month period ended September 30, 2016 and the period from September 30, 2016 to November 29, 2016:

|                                    | <b>Number<br/>of RSUs</b> |
|------------------------------------|---------------------------|
| <b>Balance, January 1, 2016</b>    | <b>608,036</b>            |
| Issued                             | 962,535                   |
| Cancelled                          | (247,676)                 |
| Vested                             | -                         |
| <b>Balance, September 30, 2016</b> | <b>1,322,895</b>          |
| Issued                             | 71,628                    |
| Cancelled                          | -                         |
| Vested                             | (90,090)                  |
| <b>Balance, November 29, 2016</b>  | <b>1,304,433</b>          |

### ***Warrants***

Pursuant to the Raycom Loan, the Company issued warrants to purchase 14,809,720 common shares at a price per share of CDN\$0.50 and accounted for the balance of warrants outstanding as at September 30, 2016 and November 29, 2016.

## **Financial Condition and Liquidity**

### **Liquidity and Capital Resources**

The purpose of liquidity management is to ensure that there is sufficient cash to meet all the financial commitments and obligations of the Company as they come due. Since inception the Company has financed its cash requirements primarily through the issuance of securities and convertible promissory notes, as well as limited income in connection with advertising revenues generated from TicToc Plus, the business that was disposed of in April 2013. Due to its start-up status and limited revenue generated from operations, the Company has had recurring losses and negative cash flows from operating activities. With the acquisition of Worldnow on August 25, 2015, the Company will now be able to utilize the positive cash flows from operating activities of Worldnow to help finance and support the operations of the Company.

In managing capital, the Company estimates its future cash requirements by preparing a budget and a multi-year plan annually for review and approval by its board. The budget establishes the approved activities for the upcoming year and estimates the costs associated with those activities. The multi-year plan estimates future activity along with the potential cash requirements and is based upon the Company's assessment of its current progress along with the expected results from the coming years'

activity. Budget to actual variances are prepared and reviewed by management and are regularly presented to the board.

The Company's exposure to liquidity risk is dependent on its ability to raise funds to meet purchase commitments and to sustain operations. The Company controls its liquidity risk by managing working capital and cash flows. The Company's approach to managing liquidity risk is to ensure that it will have sufficient liquidity to meet liabilities when due. As at September 30, 2016, the Company had a cash and accounts receivable balance of \$5,617,909 (December 31, 2015 - \$10,668,274) to settle current financial liabilities of \$4,848,392, excluding deferred revenue and revolving credit facility (December 31, 2015 - \$19,363,266). All of the Company's financial liabilities, excluding non-current portion of capital leases and the non-revolving credit facility, have contractual maturities of less than 12 months.

Management believes that cash on hand, cash to be generated from future operations and cash available under existing and future credit facilities will be sufficient to meet the Company's needs. However, circumstances such as the Company's ability to achieve sustainable profitable operations, ability to raise additional financing, the loss of significant customers or deterioration in the economy, particularly in the media and advertising industries, could cause these sources of cash and liquidity to be insufficient.

#### ***Unit Purchase Agreement and Worldnow Promissory Notes***

On July 28, 2015, we entered into the Unit Purchase Agreement, pursuant to which we issued the Worldnow Promissory Notes to Gannaway Entertainment Inc. (GEI) and Raycom Inc. (Raycom) in the aggregate principal amounts of \$11 million and \$4 million, respectively as partial consideration for their respective membership interests in Gannaway Web Holdings, LLC. The Worldnow Promissory Notes bore simple interest at a rate of 5% per year.

#### ***Raycom Loan***

On August 31, 2016, we entered into the Raycom SPA, the Credit Agreement and the related promissory note and fully paid the GEI Promissory Note and \$3 million of the Original Raycom Note. We also converted \$1 million of the Original Raycom Note into 2,553,400 common shares.

#### ***Securities Purchase Agreement***

Pursuant to the Raycom SPA, we issued to Raycom an aggregate of 2,553,400 common shares for a purchase price of CDN\$1,276,700 (or \$1 million based on the exchange rate at August 18, 2016) in repayment of \$1 million of the Original Raycom Note. The common shares are subject to a four month statutory holding period expiring on January 1, 2017. Raycom's 6,751,132 Restricted Shares were also converted into our common shares on a one-for-one basis. Under the Raycom SPA, we agreed to enlarge our Board to seven (7) directors, subject to shareholder approval, within 90 days of August 31, 2016.

#### ***Credit Agreement***

Pursuant to a Credit Agreement, we entered into a Credit Facility with Raycom in the principal amount of \$14.5 million and issued to Raycom Warrants to purchase 14,809,720 common shares at a price per share of CDN\$0.50 (\$0.39 based on the exchange rate at August 18, 2016). The Credit Facility terminates on August 31, 2021. The Warrants have a 5-year term but will expire on the date which is later of (a) August 31, 2017 or (b) 30 days from the date of each principal repayment. Upon each payment of principal, the number of warrants that will expire will equal the product of the (i) then outstanding number of Warrants and (ii) the principal repayment divided by the then outstanding principal balance of the term loan by 100. The exercise price and the number of shares underlying the Warrants will be subject to adjustment as set forth in the Credit Agreement.

Subject to approval of Raycom, at its sole discretion, we may require further loans up to an aggregate amount of \$1.5 million. We will pay interest on each loan outstanding at any time at a rate per annum of 10%. Interest will accrue and be calculated, but not compounded, daily on the principal amount of each loan on the basis of the actual number of days each loan is outstanding and will be compounded and payable monthly in arrears on each interest payment date. To the maximum extent permitted by applicable law, we will pay interest on all overdue amounts, including any overdue interest payments, from the date each of those amounts is due until the date each of those amounts is paid in full. That interest will be calculated daily, compounded monthly and payable on demand of Raycom at a rate per annum of 12%. We have the option to repay all or a portion of loans outstanding under the Credit Facility without premium, penalty or bonus upon prior notice to Raycom and repayment of all interest, fees and other amounts accrued and unpaid under the Credit Facility.

We must also make the following mandatory repayments:

- (a) \$2 million prior to August 31, 2019;
- (b) commencing on November 30, 2019 and on the last day of the month of each three month period thereafter, an amount of \$687,500 per three month period;
- (c) proceeds (less actual costs paid and income taxes) on any asset sales or issuances of debt or equity;
- (d) upon a successful listing of our common shares on Nasdaq with a capital raise of between \$8 million to \$11 million, mandatory repayment in the amount of \$2 million, which will be applied toward the repayment obligation required by (a) above, if completed by March 31, 2017;
- (e) upon a successful listing of our common shares on Nasdaq with a capital raise of more than \$12 million, a mandatory repayment in the amount of \$3 million which will be applied toward the \$2 million repayment obligation required by (a) above, if completed by March 31, 2017; and any amounts raised in excess of \$2 million will be applied pro rata to repayment obligations required by (b) above commencing November 30, 2019; and
- (f) commencing on the financial year ending December 31, 2017, and each financial year ending thereafter, 100% of the current year excess cash flow amount in excess of \$2 million must be paid to Raycom as a mandatory repayment amount no later than May 1 of the following year until a total leverage ratio of not more than 3:1 has been met for such fiscal year, at which point 50% of the current year excess cash amount in excess of \$2 million will be paid to Raycom as mandatory repayment amounts. Such excess cash flow payments will be applied pro rata to reduce other mandatory payments due thereunder.

In addition, we must maintain certain leverage ratios and interest coverage ratios beginning the fiscal quarter ending December 31, 2017. The leverage ratios range from 4:1 to 2.5:1 and 2:1 to 3.5:1 for the interest coverage ratio. We are also subject to the certain covenants relating to, among others, indebtedness, fundamental corporate changes, dispositions, acquisitions and distributions.

Upon an event of default, Raycom may by written notice terminate the facility immediately and declare all obligations under the Credit Agreement and the related loan documents, whether matured or not, to be immediately due and payable. Raycom may also as and by way of collateral security, deposit and retain in an interest bearing account, amounts received by Raycom from us under the Credit Agreement and the related loan documents and realize upon the Security Interest Agreements, Guaranty Agreements and Pledge Agreement as described below. If we fail to perform any of our obligations under the Credit Agreement and the related loan documents, Raycom may upon 10 days' notice, perform such covenant or agreement if capable. Any amount paid by Raycom under such covenant or agreement will be repaid by us on demand and will bear interest at 12% per annum.

### ***Guaranty Agreements, Security Interest Agreements and Pledge Agreement***

In connection with the Credit Agreement, our subsidiaries Frankly Co. and Frankly Media LLC have entered into Guaranty Agreements whereby Frankly Co. and Frankly Media LLC have guaranteed our obligations under the Credit Agreement. In addition, each of Frankly Inc., Frankly Co. and Frankly Media LLC have entered into Security Interest Agreements pursuant to which Raycom has first priority security interests in substantially all of our assets. Under the Security Interest Agreements, we do not have a right to sell or otherwise dispose of all or part of the collateral except in the ordinary course of business that are not material. Frankly Media LLC has also entered into an Intellectual Property Pledge Agreement pursuant to which it has granted a security interest in all of its intellectual property to Raycom. We have also (i) deposited our intellectual property in escrow accounts for the benefit of Raycom, (ii) entered into a control agreement pursuant to which we granted Raycom control of 100% of the equity interest of Frankly Media LLC and (iii) entered into an insurance transfer and consent assigning our rights and payments under insurance policies covering our operations and business naming Raycom as mortgagee, first loss payee and additional named insured.

In addition, we have entered into a Pledge Agreement pursuant to which we granted Raycom a security interest on substantially all the assets and securities of our current and future subsidiaries.

Upon an event of default, we will be required to deposit all interests, income, dividends, distributions and other amounts payable in cash in respect of the pledged interests into a collateral account over which Raycom has the sole control and may apply such amounts in its sole discretion to the secured obligations under the Credit Agreement. Upon the cure or waiver of a default, Raycom will repay to us all cash interest, income, dividends, distributions and other amounts that remain in such collateral account. In addition, upon an event of default, Raycom has the right to (i) transfer in its name or the name of any of its agents or nominees the pledged interests, (ii) to exercise all voting, consensual and other rights and power and any and all rights of conversion, exchange, subscription and other rights, privileges or options pertaining to the pledged interests whether or not transferred into the name of Raycom, and (iii) to sell, resell, assign and deliver all or any of the pledged interests. We have also agreed to use our best efforts to cause a registration under the Securities Act and applicable state securities laws of the pledged interests upon the written request from Raycom.

Raycom may transfer or assign, syndicate, grant a participation interest in or grant a security interest in, all or any part of its rights, remedies and obligations under the Credit Agreement and the related loan documents, without notice or our consent.

### ***Repayment of Bridge Bank Loan***

As a condition to entering into the Credit Agreement, on August 31, 2016, we fully repaid the Bridge Bank Loan.

### ***Western Alliance Bank Letter of Credit***

On August 31, 2016, in lieu of a security deposit under the lease dated October 26, 2010, with Metropolitan Life Insurance Company, for real property located at 27-01 Queens Plaza North, Long Island City, NY, we entered into a standby letter of credit with Western Alliance Bank for an amount of \$500,000 (the "Letter of Credit"). For each advance, interest will accrue at a rate equal to the sum of (i) the Base Rate (as defined below), plus (ii) 3.50%, provided that such interest rate will change from time to time as the Base Rate changes. The "Base Rate" means the rate of interest used as the reference or base rate to establish the actual rates charged on commercial loans and which is publicly announced or reported from



time to time by the Wall Street Journal as the “prime rate”. Interest will accrue from the date of the advance until such advance is paid in full. We have granted Western Alliance Bank a security interest in a USD\$524,115.40 controlled cash deposit account together with (i) all interest, whether now accrued or hereafter accruing; (ii) all additional deposits hereafter made to the account; (iii) any and all proceeds from the account; and (iv) all renewals, replacements and substitutions for any of the foregoing.

### **Equipment financing**

On March 24, 2014, Frankly Media, entered into a finance agreement with Leaf Capital Funding, LLC in the principal amount of \$108,849 with proceeds used to purchase server equipment used in our operations. The term of the agreement is 36 months with the final recurring payment due in March 2017. The loan is secured by the server equipment noted above.

### **Nasdaq uplisting**

We are currently in the process of listing our common shares on the Nasdaq exchange. We filed our S-1 with the U.S. Securities and Exchange Commission on November 14, 2016. We intend to use the net proceeds of the offering as follows:

- to increase sales and marketing investments (including channel partnerships) to increase market share and expand into other verticals;
- for product development on existing and new products including CMS, mobile and TV apps, and video workflow;
- for development of new business lines in big data and digital advertising;
- \$2 million to partially repay amounts outstanding under the Credit Facility; and
- the balance for working capital and general corporate purposes.

### **Commitments and contingencies**

The Company is obligated under several non-cancellable operating leases for office space, expiring in 2017 - 2023. The future aggregate minimum lease payments under these non-cancellable operating leases are as follows:

| <b>Payments Due During the Years Ending September 30,</b> | <b>Total</b>        |
|---|---------------------|
| 2017  | \$ 1,459,608        |
| 2018  | 1,375,908           |
| 2019  | 1,210,908           |
| 2020  | 852,908             |
| 2021  | 852,908             |
| Thereafter  | 1,208,287           |
| <b>Total</b>  | <b>\$ 6,960,527</b> |

### **New Standards and Interpretations**

Information on new standards, amendments and interpretations that have been issued but are not yet effective and may impact the Company's consolidated financial statements are provided below:

IFRS 9, 'Financial instruments', published in July 2014, replaces the existing guidance in IAS 39, 'Financial Instruments: Recognition and Measurement'. IFRS 9 includes revised guidance on the classification and measurement of financial instruments, including a new expected credit loss model for

calculating impairment on financial assets, and the new general hedge accounting requirements. It also carries forward the guidance on recognition and derecognition of financial instruments from IAS 39. IFRS 9 is effective for annual reporting periods beginning on or after January 1, 2018, with early adoption permitted.

IFRS 7, 'Financial Instruments: Disclosures' has been amended by the IASB to require additional disclosures on transition from IAS 39 to IFRS 9. The amendment to IFRS 7 is effective for periods beginning on or after January 1, 2018.

IFRS 15, 'Revenue from Contracts with Customers' establishes a comprehensive framework for determining whether, how much and when revenue is recognized. It replaces existing revenue recognition guidance, including IAS 18, 'Revenue', IAS 11, 'Construction Contracts', and IFRIC 13, 'Customer Loyalty Programmers'. IFRS 15 is effective for annual reporting periods beginning on or after January 1, 2018, with early adoption permitted.

IFRS 16, 'Leases' sets out the principles for the recognition, measurement and disclosure of leases. IFRS 16 provides revised guidance on identifying a lease and for separating lease and non-lease components of a contract. IFRS 16 introduces a single accounting model for all lessees and requires a lessee to recognize right-of-use assets and lease liabilities for leases with terms of more than 12-months, unless the underlying asset is of low value. Under IFRS 16, lessor accounting for operating and finance leases will remain substantially unchanged. IFRS 16 is effective for annual periods beginning on or after January 1, 2019, with earlier application permitted for entities that apply IFRS 15.

Management is currently in the process of evaluating the potential impact of adopting these pronouncements.

There are no other IFRSs or IFRIC interpretations that are not yet effective that would be expected to have a material impact on the Company.

## **Risk Factors**

Due to the nature of the Company's business, the legal and economic climate in which it operates and its present stage of development, we are subject to significant risks. Our future development and operating results may be very different from those expected as at the date of this discussion. Risk factors relating to our business include, but are not limited to, the following:

### **Risks Related to Our Business**

- We have a limited operating history which may make it difficult for investors to evaluate our prospects for success.
- Since our inception, we have experienced losses and we may incur additional losses in the future.
- Our independent registered public accounting firm has expressed in its report on our audited consolidated financial statements a substantial doubt about our ability to continue as a going concern.
- Our revenue and operating results may fluctuate, which may make our results difficult to predict and could cause our results to fall short of expectations.

- If we are unable to retain and acquire new CMS platform customers, our financial performance may be materially and adversely affected.
- If we are unable in the future to generate new customers for our mobile technology products, our financial performance may be materially and adversely affected.
- A significant portion of our projected revenue is generated from the sale of national and local online advertising inventory, which is dependent on available advertising inventory and market demand and prices for such inventory. A decline in available supply of advertising inventory, general demand for advertising inventory and general economic conditions may materially and adversely affect our advertising revenue.
- Some of our customer agreements require us to guarantee certain advertising revenues. If market rates fall below our guaranteed customer agreement rates, we will experience a loss on those advertising inventory units subject to the guarantee.
- If we are unable to respond to the rapid technological changes in our industry or develop new products and services in a cost effective manner, we may be unable to compete successfully in the competitive market in which we operate and our financial results could be adversely affected.
- We may introduce significant changes to our existing products or develop and introduce new and unproven products. If any of our new products or services, including upgrades to our current products or services, do not meet our customers' expectations or fail to generate revenue, we could lose our customers or fail to generate any revenue from such products or services and our business may be harmed.
- A significant percentage of our revenue is generated from two large customers. If we are unable to maintain our relationship with these customers, our business and operations may be materially and adversely affected.
- The loss of one or more of our key personnel, or our failure to attract and retain other highly qualified personnel in the future, could harm our business.
- We determined that a portion of our goodwill and amortizable intangible assets were impaired.
- We may expand our business through acquisitions of, or investments in, other companies or new technologies, or joint ventures or other strategic alliances with other companies, which may divert our management's attention or prove not to be successful or result in equity dilution.
- If we fail to manage our growth effectively, our business, financial condition and results of operations may suffer.
- Our degree of leverage could adversely affect our ability to raise additional capital to fund our operations, limit our ability to react to changes in the economy or our industry and prevent us from meeting operational goals.
- Our debt agreements and those of our subsidiaries contain restrictions that limit our flexibility in operating our business.
- We may not be able to generate sufficient cash to service all of our indebtedness, and may be forced to take other actions to satisfy our obligations under our indebtedness, which may not be successful.



- We cannot be certain that additional financing will be available on reasonable terms when required, or at all.
- If we are unable to protect our intellectual property, the value of our brand and other intangible assets may be diminished, and our business may be adversely affected.
- We are a holding company and our only asset is the direct ownership of Frankly Co. and Frankly Media.
- We may be party to litigation, which can be expensive and time consuming, and, if resolved adversely, could have a significant impact on our business, financial condition, or results of operations.
- Our software is highly technical, and if it contains undetected errors, our business could be adversely affected.
- We rely on third parties to provide the technologies necessary to deliver products and services to our customers, and any change in the licensing terms, costs, availability, or acceptance of these technologies could adversely affect our business.
- Failure to license necessary third party software for use in our products and services, or failure to successfully integrate third party software, could cause delays or reductions in our sales, or errors or failures of our service.
- Computer malware, viruses, hacking and phishing attacks, and spamming could harm our business and results of operations.
- System failures or capacity constraints could harm our business and financial performance.
- Our business depends on continued and unimpeded access to the Internet by us, our customers and their end users. Internet access providers or distributors may be able to block, degrade or charge for access to our content, which could lead to additional expenses to us and our customers and the loss of end users and advertisers.
- We may not maintain acceptable website performance for our platform, which may negatively impact our relationships with our customers and harm our business, financial condition and results of operations.
- We may incur liability as a result of information retrieved from or transmitted over the internet or through our customer websites and claims related to our products.
- We may expand our operations into international markets where we have limited experience and we will be subject to risks associated with international operations.
- We have no operating experience as a publicly traded company in the U.S.
- We cannot be certain that our net operating loss ("NOL") carryforwards will be available to offset future taxable income for tax purposes.
- The preparation of our financial statements will involve the use of estimates, judgments and assumptions, and our financial statements may be materially affected if such estimates, judgments and assumptions prove to be inaccurate.

- If we fail to maintain an effective system of internal control over financial reporting, we may not be able to accurately report our financial results or prevent fraud. As a result, shareholders could lose confidence in our financial and other public reporting, which would likely negatively affect our business and the market price of our common shares.
- We will incur increased costs as a result of being a U.S. public company.
- We are an “emerging growth company,” and we cannot be certain if the reduced SEC reporting requirements applicable to emerging growth companies will make our common shares less attractive to investors, which could have a material and adverse effect on us, including our growth prospects.

### **Risks Related to Our Industry**

- Our business is highly competitive. Competition presents an ongoing threat to the success of our business.
- Recent consolidation within the local news broadcasting industry may materially and adversely affect our ability to expand our customer base.
- Our business may be subject to the adverse effects of Federal Communications Commission (“FCC”) regulations.
- The adoption of ATSC 3.0 has the potential to disrupt the demand for or composition of the products and services we provide to our customers.
- The broadcast industry is subject to changing demographics and user preferences.
- The growth of the market for our services and products depends on the continued growth of the internet and mobile devices as mediums for content, advertising, commerce and communications.
- The growth of the market for our services and products depends on the development and maintenance of the internet infrastructure and the mobile phone services and technology.
- Government regulation of the internet continues to evolve, and new laws and regulations could significantly harm our financial performance.

### **Risks Related to Our Common Shares**

- We do not know whether an active, liquid and orderly trading market for the common shares will be maintained or sustained and what the market price of the common shares will be and as a result it may be difficult for investors to sell their common shares.
- The price of our common shares may fluctuate significantly, which may make it difficult for holders of our common shares to sell their common shares at a time or price they find attractive.
- If research analysts do not publish research about our business or if they issue unfavorable commentary or downgrade our common shares, the price of our common shares and their trading volume could decline.
- Once the listing of our common shares is approved by Nasdaq, our common shares will be traded on more than one market and this may result in price variations.



- We may issue additional equity securities, or engage in other transactions that could dilute our book value or affect the priority of our common shares, which may adversely affect the market price of our common shares.
- The exercise of outstanding options, RSUs, Restricted Shares and warrants may dilute current shareholders.
- We have not paid any cash dividends in the past and have no plans to issue cash dividends in the future, which could cause our common shares to have a lower value than that of similar companies which do pay cash dividends.
- Two large shareholders have substantial control over us, which will limit an investor's ability to influence the outcome of important transactions, including a change in control.

Additional information relating to the Company, including the Company's annual information form for the year ended December 31, 2015 dated as of April 26, 2016, is available under the Company's profile on SEDAR at [www.sedar.com](http://www.sedar.com).