

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended: **March 31, 2025**

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission File No. **001-40222**

Airship AI Holdings, Inc.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

93-4974766

(I.R.S. Employer Identification No.)

8210 154th Ave NE, Redmond, WA

(Address of principal executive offices)

98052

(Zip Code)

(877) 462-4250

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

Securities registered pursuant to Section 12(b) of the Act:

<u>Title of each class</u>	<u>Trading Symbol(s)</u>	<u>Name of each exchange on which registered</u>
Common Stock	AISP	The Nasdaq Stock Market LLC
Warrant	AISPW	The Nasdaq Stock Market LLC

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

As of May 15, 2025, there were a total of 31,844,471 shares of the registrant's common stock issued and outstanding.

Airship AI Holdings, Inc.

Quarterly Report on Form 10-Q
Quarterly Period Ended March 31, 2025

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PART I

ITEM 1. FINANCIAL STATEMENTS.

AIRSHIP AI HOLDINGS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
As of March 31, 2025 and December 31, 2024

	March 31, 2025	December 31, 2024 (1)
ASSETS	Unaudited	
CURRENT ASSETS:		
Cash and cash equivalents	\$ 8,812,178	\$ 11,414,830
Accounts receivable, net of allowance for credit losses of \$0	2,782,650	1,226,757
Prepaid expenses and other	67,311	17,883
Total current assets	11,662,139	12,659,470
OTHER ASSETS		
Other assets	165,960	165,960
Operating lease right of use asset	1,102,967	882,024
TOTAL ASSETS	\$ 12,931,066	\$ 13,707,454
LIABILITIES AND STOCKHOLDERS' DEFICIT		
CURRENT LIABILITIES:		
Accounts payable - trade	\$ 2,179,847	\$ 759,480
Advances from founders	700,000	1,300,000
Accrued expenses	60,551	51,649
Current portion of operating lease liability	405,916	305,178
Deferred revenue- current portion	2,948,695	3,238,483
Total current liabilities	6,295,009	5,654,790
NON-CURRENT LIABILITIES:		
Operating lease liability, net of current portion	758,376	638,525
Warrant liability	18,659,435	34,180,618
Earnout liability	8,199,079	23,304,808
Deferred revenue- non-current	2,528,716	2,951,850
Total liabilities	36,440,615	66,730,591
COMMITMENTS AND CONTINGENCIES (Note 9)		
STOCKHOLDERS' DEFICIT:		
Preferred stock - no par value, 5,000,000 shares authorized, 0 shares issued and outstanding as of March 31, 2025 and December 31, 2024	-	-
Common stock - \$0.0001 par value, 200,000,000 shares authorized, 31,844,471 and 30,588,413 shares issued and outstanding as of March 31, 2025 and December 31, 2024	3,182	3,056
Additional paid in capital	27,731,753	21,918,867
Accumulated deficit	(51,233,605)	(74,941,590)
Accumulated other comprehensive loss	(10,879)	(3,470)
Total stockholders' deficit	(23,509,549)	(53,023,137)
TOTAL LIABILITIES AND STOCKHOLDERS' DEFICIT	\$ 12,931,066	\$ 13,707,454

(1) Derived from the audited consolidated balance sheet.

The accompanying notes are an integral part of these condensed consolidated financial statements.

AIRSHIP AI HOLDINGS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)
For the three months ended March 31, 2025 and 2024
(Unaudited)

	Three Months Ended	
	March 31, 2025 Unaudited	March 31, 2024 Unaudited
NET REVENUES:		
Product	\$ 4,497,240	\$ 9,398,776
Post contract support	998,051	1,176,239
Other services	7,737	-
	<u>5,503,028</u>	<u>10,575,015</u>
COST OF NET REVENUES:		
Cost of Sales	2,923,087	7,789,409
Post contract support	312,021	157,479
Other services	32,916	-
	<u>3,268,024</u>	<u>7,946,888</u>
GROSS PROFIT	<u>2,235,004</u>	<u>2,628,127</u>
RESEARCH AND DEVELOPMENT EXPENSES	719,382	695,366
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	3,229,979	3,335,294
TOTAL OPERATING EXPENSES	<u>3,949,361</u>	<u>4,030,660</u>
OPERATING LOSS	<u>(1,714,357)</u>	<u>(1,402,533)</u>
OTHER INCOME (EXPENSE) :		
Gain (loss) from change in fair value of earnout liability	9,823,605	(21,484,850)
Gain (loss) from change in fair value of warrant liability	15,521,183	(6,847,091)
Loss from change in fair value of convertible debt	-	(2,039,377)
Loss on note conversion	-	(158,794)
Interest income (expense), net	77,554	(31,824)
Total other income (expense), net	<u>25,422,342</u>	<u>(30,561,936)</u>
INCOME (LOSS) BEFORE PROVISION FOR INCOME TAXES	<u>23,707,985</u>	<u>(31,964,469)</u>
Provision for income taxes	-	-
NET INCOME (LOSS)	<u>23,707,985</u>	<u>(31,964,469)</u>
OTHER COMPREHENSIVE (LOSS) INCOME		
Foreign currency translation (loss) income, net	(7,409)	3,239
TOTAL COMPREHENSIVE INCOME (LOSS)	<u>\$ 23,700,576</u>	<u>\$ (31,961,230)</u>
NET INCOME (LOSS) PER SHARE:		
Basic	<u>\$ 0.75</u>	<u>\$ (1.40)</u>
Diluted	<u>\$ 0.61</u>	<u>\$ (1.40)</u>
Weighted average shares of common stock outstanding		
Basic	31,704,117	22,898,487
Diluted	38,820,839	22,898,487

The accompanying notes are an integral part of these condensed consolidated financial statements.

AIRSHIP AI HOLDINGS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' DEFICIT
(Unaudited)

	Common Stock	Common Stock \$	Additional Paid in Capital	Accumulated Deficit	Other Comprehensive Income (Loss)	Total Stockholders' Deficit
Balance as of January 1, 2024	22,812,048	\$ 2,281	\$ -	\$ (17,476,700)	\$ (12,808)	\$ (17,487,227)
Stock-based compensation	-	-	268,989	-	-	268,989
Issuance of common stock for prior period services	15,000	-	-	-	-	-
Issuance of common stock for conversion of debt	169,204	17	835,593	-	-	835,610
Issuance of common stock for exercise of warrants	162,867	16	293,233	-	-	293,249
Foreign currency translation gain	-	-	-	-	3,239	3,239
Net loss	-	-	-	(31,964,469)	-	(31,964,469)
Balance as of March 31, 2024	<u>23,159,119</u>	<u>2,314</u>	<u>1,397,815</u>	<u>(49,441,169)</u>	<u>(9,569)</u>	<u>(48,050,609)</u>
Balance as of January 1, 2025	30,588,413	3,056	21,918,867	(74,941,590)	(3,470)	(53,023,137)
Stock-based compensation	-	-	428,286	-	-	428,286
Issuance of common stock for exercise of warrants	13,200	1	59,399	-	-	59,400
Issuance of common stock for stock options exercise	81,952	8	43,193	-	-	43,201
Issuance of common stock for earnout shares	1,160,906	117	5,282,008	-	-	5,282,125
Foreign currency translation loss	-	-	-	-	(7,409)	(7,409)
Net income	-	-	-	23,707,985	-	23,707,985
Balance as of March 31, 2025	<u>31,844,471</u>	<u>3,182</u>	<u>27,731,753</u>	<u>(51,233,605)</u>	<u>(10,879)</u>	<u>(23,509,549)</u>

The accompanying notes are an integral part of these condensed consolidated financial statements.

AIRSHIP AI HOLDINGS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
For the three months ended March 31, 2025 and 2024
(Unaudited)

	Three Months Ended	
	March 31, 2025	March 31, 2024
	Unaudited	Unaudited
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss)	\$ 23,707,985	\$ (31,964,469)
Adjustments to reconcile net income (loss) to net cash used in operating activities		
Depreciation and amortization	-	1,861
Stock-based compensation	428,286	268,989
Amortization of operating lease right of use asset	83,396	80,291
(Gain) loss from change in fair value of warrant liability	(15,521,183)	6,847,091
(Gain) loss from change in fair value of earnout liability	(9,823,605)	21,484,850
Loss from change in fair value of convertible note	-	2,039,377
Loss on note conversion	-	158,794
Changes in operating assets and liabilities:		
Accounts receivable	(1,555,893)	(55,525)
Prepaid expenses and other	(49,428)	2,010
Other assets	-	1,901
Operating lease liability	(83,750)	(67,211)
Payroll and income tax receivable	-	(2,410)
Accounts payable - trade and accrued expenses	1,429,270	433,415
Deferred revenue	(712,922)	(924,048)
NET CASH USED IN OPERATING ACTIVITIES	(2,097,844)	(1,695,084)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from warrant exercise, net	59,400	293,249
Repayment of advances from founders	(600,000)	-
Proceeds from stock option exercises	43,201	-
NET CASH (USED IN) PROVIDED BY FINANCING ACTIVITIES	(497,399)	293,249
NET DECREASE IN CASH AND CASH EQUIVALENTS	(2,595,243)	(1,401,835)
Effect from exchange rate on cash	(7,409)	3,239
CASH AND CASH EQUIVALENTS, beginning of period	11,414,830	3,124,413
CASH AND CASH EQUIVALENTS, end of period	\$ 8,812,178	\$ 1,725,817
Supplemental disclosures of cash flow information:		
Interest paid	\$ -	\$ -
Taxes paid	\$ -	\$ 2,410
Noncash investing and financing		
Issuance of common stock for debt conversion	\$ -	\$ 835,610
Issuance of common stock for earnout shares	\$ 5,282,125	\$ -
Recognition of operating right-of-use asset	\$ 304,339	\$ -
Recognition of operating lease liability	\$ 304,339	\$ -

The accompanying notes are an integral part of these condensed consolidated financial statements.

AIRSHIP AI HOLDINGS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Organization

Airship AI Holdings, Inc. (the “Company” or “Airship”) is a holding company incorporated in Delaware that executes business through its wholly owned subsidiary, Airship AI, Inc. (“Airship AI”). Prior to the formation of Super Simple AI, Inc. in 2022, the Company operated as Airship AI, Inc. (formerly known as JDL Digital Systems, Inc.). On March 7, 2023, Super Simple AI, Inc. changed its name to Airship AI Holdings, Inc. Super Simple AI, Inc. was formed in January 2022 through a share exchange with JDL Digital Systems, Inc. JDL Digital Systems, Inc. was incorporated under the laws of the State of Washington on June 30, 2003.

On December 21, 2023, the Company completed the merger (“the Merger”) contemplated by the merger agreement (the “Merger Agreement”) dated as of June 27, 2023 and amended on September 22, 2023, by and among BYTE Acquisition Corp. (“BYTS”), BYTE Merger Sub, Inc., a Washington corporation and a direct, wholly-owned subsidiary of BYTS (“Merger Sub”), and Airship AI.

Effective December 21, 2023, Merger Sub merged with and into Airship AI with Airship AI as the surviving corporation. Thus, Airship AI became a wholly-owned subsidiary of the Company. In connection with the Merger, Airship AI changed its name from “Airship AI Holdings, Inc.” to “Airship AI, Inc.”

Fair Value Transactions in Connection with Merger

As a result of the Merger, the Company entered into the following transactions that were measured at fair value and vary quarterly with the share price and other items. Any change is non-cash and is recorded as a gain or loss in other income (expense). See Note 13– Fair Value Measurements for more information.

	Liability as of March 31, 2025	Liability as of December 31, 2024
Earnout liability	\$ 8,199,079	\$ 23,304,808
Warrant liability (Public Warrants)	18,082,635	33,124,868
Warrant liability (Private Warrants)	576,800	1,055,750
Total liabilities measured at fair value	<u>\$ 26,858,514</u>	<u>\$ 57,485,426</u>
Other income (expense) related to instruments recorded at fair value during the three months ended March 31, 2025 and 2024	<u>\$ 25,344,788</u>	<u>\$ (30,371,318)</u>

Business

The Company is a robust AI-driven data management platform that solves complex data challenges for large institutions operating in dynamic and mission-critical environments with rapidly increasing volumes of data being ingested from a similarly rapidly growing number of data sources.

The Company solves these challenges by structuring “dark” or unstructured data at the edge, the location at which the data is generated and collected, and leveraging purpose-built AI models. Unstructured, or “dark” data, which is typically categorized as qualitative data, cannot be processed and analyzed via conventional data tools and methods. Conversely, structured data, typically categorized as quantitative data, is highly organized and easily decipherable by machine learning algorithms.

Structuring and then analyzing data using AI models at the edge, versus transmitting the data from the edge back to a central processing location for structuring and analysis, enables real-time decision making and data-driven operational efficiency.

The Company specializes in ingesting all available metadata from edge-based sensors used by government and law enforcement agencies around the world, including surveillance cameras (video), audio, telemetry, acoustic, seismic, and autonomous devices, along with large commercial corporations with fundamentally similar capabilities and requirements.

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Data generated by these edge-based sensors, including video, can then be run through the Company's trained AI models to detect objects present within the video frame. Once an object is detected, for example an automobile, additional identifying characteristics of the object can be extracted from the image including the license plate characters and the make, model, and color of the automobile. This process of analyzing, logging and categorizing ingested data is referred to as "structuring" the data.

Airship AI's software allows customers to view structured data both in real-time as well as to conduct searches on the structured data at a later point in time. Real-time structured data use includes, for example, alarms on a specific license plate or a specific make, model or color of automobile. Non-real-time structured data use includes, for example, searching a database of video data that has been previously ingested and stored to find instances of a particular license plate being visible, along with other logged vehicle characteristics such as make, model and color of an automobile.

Additional edge deployed AI models enable similar object detection and recognition of common and custom trained objects, such as an aircraft, boat, person, animal, bag, or weapon. Airship AI's models provide similar data points for these object types allowing analysts the ability to be notified in real-time of the detection of a specified object and similarly search for historically detected objects. Examples include detecting aircrafts and boats along with their respective tail numbers and hull registration numbers.

The Company's AI modelling process starts with pre-trained AI models from its technology ecosystem partners which the Company then customizes using proprietary datasets tailored towards its customers' unique workflow requirements. Where customers have pre-existing AI models or engines, the Company integrates those models or engines into its edge platform allowing customers to leverage proprietary models within the Airship AI software ecosystem.

The Company's primary offerings include Outpost AI, Acropolis, and Airship Command. Its offerings allow customers to manage their data across the full data lifecycle, when and where they need it, using a highly secure permissioned based architecture.

The Company employed fifty two employees as of March 31, 2025. The employees are headquartered in Redmond, WA and are supported by a growing team at its Customer Center of Excellence located in Charlotte, NC. The Company employed eight research and development personnel in Taiwan as of March 31, 2025.

2. Summary of Significant Accounting Policies

Basis of Presentation and Consolidation

The accompanying consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. Intercompany accounts and transactions have been eliminated.

The Company has prepared the condensed consolidated financial statements included herein pursuant to the rules and regulations of the U.S. Securities and Exchange Commission ("SEC"). Certain information and footnote disclosures normally included in financial statements prepared in accordance U.S. generally accepted accounting principles ("GAAP") have been condensed or omitted pursuant to such rules and regulations. However, the Company believes that the disclosures herein are adequate to ensure the information presented is not misleading. These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2024.

The Company believes that all necessary adjustments, which consisted only of normal recurring items, have been included in the accompanying financial statements to present fairly the results of the interim periods. The results of operations for the interim periods presented are not necessarily indicative of the operating results to be expected for any subsequent interim period or for the fiscal year ending December 31, 2025.

Functional Currency

The Company's reporting currency is the U.S. Dollar. The Company's functional currency for U.S. operations is the U.S. Dollar. The operations of Zeppelin Worldwide, Inc. and its subsidiary, Zeppelin Taiwan, Ltd. (together "Zeppelin") use the Taiwan Dollar as its functional currency. At each period end, Zeppelin's balance sheet is translated into U.S. Dollars based upon the period end exchange rate, while their statements of operations and comprehensive income (loss) and statements of cash flows are translated into U.S. Dollars based upon an average exchange rate during the period.

Cash and Cash Equivalents

The Company classifies highly liquid temporary investments with an original maturity of three months or less when purchased as cash equivalents. The Company maintains cash balances at various financial institutions. Balances at US banks are insured by the Federal Deposit Insurance Corporation up to \$250,000. The Company has not experienced any losses in such accounts and believes it is not exposed to any significant risk for cash on deposit.

Revenue Recognition and Deferred Revenue

The Company primarily generates revenue from sales of systems and products and the related post contract support to customers. The Company's primary systems and products include Outpost AI, Acropolis and Airship Command. To date, the majority of the Company's product revenue that has been recognized consists primarily of a bundled offering of hardware and software which delivers on premise solutions to its customers. Separate limited software subscription services have been delivered to customers including those customers that are able to operate in a cloud-based environment. The transaction price recognized as revenue represents the amount the Company expects to be entitled to and is primarily comprised of product revenue, net of returns and variable consideration, including sales incentives provided to customers. Payment is typically due within 30 to 90 calendar days of the invoice date.

The Company recognizes revenue when promised goods or services are transferred to customers in an amount that reflects the consideration to which the Company expects to be entitled in exchange for those goods or services by following a five-step process: (1) identify the contract with a customer, (2) identify the performance obligations in the contract, (3) determine the transaction price, (4) allocate the transaction price, and (5) recognize revenue when or as the Company satisfies a performance obligation, as further described below. The Company generally provides a warranty to its customers for its software products and services. In the event that there is a failure of warranties in such agreements, the Company is generally obligated to correct the product or service to conform to the warranty provision as set forth in the applicable agreement, or, if the Company is unable to do so, the customer is entitled to seek a refund of the purchase price of the product and service (generally prorated over the contract term). For the three months ended March 31, 2025 and 2024, the Company did not incur any significant warranty expenses and as such a warranty reserve was not considered necessary as of March 31, 2025 and December 31, 2024.

Product Revenue

Product revenue is derived primarily from sales of the Company's system offerings, Outpost AI, Acropolis and Airship Command. The Company recognizes product revenue at a point in time when title transfers, when the products are shipped, or when control of the system is transferred to the customer, which usually is upon delivery of the system and when contractual performance obligations have been satisfied.

Post Contract Support Revenue

Post Contract Support ("PCS") revenue is derived primarily from the Company's support and software maintenance agreements ("SMA"). The Company's PCS includes the right to receive, on a when and if available basis, future unspecified firmware upgrades and features as well as bug fixes, and email and telephone support. The Company allocates a portion of the transaction price to the PCS performance obligation based on a cost-plus methodology and recognizes the associated revenue on a straight-line basis over the estimated term of the support period. The Company's support contracts are typically one to five years with an average of four years; payment is due within 30 to 90 calendar days of the invoice date and may include options to renew. For the three months ended March 31, 2025 and 2024, the Company recognized revenue of \$101,599 and \$59,361, respectively, related to one-year support contracts. For the three months ended March 31, 2025 and 2024, the Company recognized revenue of \$896,452 and \$1,116,893 respectively, related to multi-year support contracts.

Other Services

The Company earns other service revenues from installation services, training and licensing which are short-term in nature and revenue for these services are recognized at the time of performance when the service is provided. For the three months ended March 31, 2025 and 2024, the Company recognized revenue of \$7,737 and \$0, respectively, related to other services.

Contracts with Multiple Performance Obligations

The Company's contracts with customers often contain multiple performance obligations that can include three separate obligations: (i) a hardware component (which may be bundled with hardware accessories) and the embedded firmware essential to the functionality of the hardware component delivered at the time of sale; (ii) the right to the Company's downloadable free application and software solutions, and (iii) the right for the customer to receive post contract support ("PCS") after the initial sale. The Company's products and PCS offerings have significant standalone functionalities and capabilities. Accordingly, the products are distinct from the Company's PCS services as customers can benefit from the products without the PCS services and such PCS services are separately identifiable within the contracts. The Company accounts for multiple agreements with a single customer as a single contract if the contractual terms and/or substance of those agreements indicate that they may be so closely related that they are, in effect, parts of a single contract. The amount of consideration the Company expects to receive in exchange for delivering on the contract is allocated to each performance obligation based on its relative standalone selling price.

The Company establishes the standalone selling price using the prices charged for a deliverable when sold separately. If the standalone selling price is not observable through past transactions, the Company estimates the standalone selling price based on its pricing model and offering type (products or PCS services).

The Company has elected the practical expedient to not assess whether a contract has a significant financing component as the Company's standard payment terms are less than one year.

The Company sells its products primarily through a direct sales force. The Company considers revenue to be earned when all of the following criteria are met:

- The Company has a contract with a customer that creates enforceable rights and obligations,
- Promised performance obligations are identified,
- The transaction price, or the amount the Company expects to receive, is determinable and
- The Company has satisfied the performance obligations to the customer.

Transfer of control is evidenced upon passage of title and risk of loss to the customer unless the Company is required to provide additional services.

The Company's short-term and long-term deferred revenue balances totaled \$2,948,695 and \$2,528,716 as of March 31, 2025. The Company's short-term and long-term deferred revenue balances totaled \$3,238,483 and \$2,951,850 as of December 31, 2024. Of the deferred revenue balance of \$6,190,333 and \$8,970,780 as of January 1, 2025 and 2024, the Company recognized approximately \$985,548 and \$1,176,239 during the three months ended March 31, 2025 and 2024, respectively.

Accounts Receivable and Provision for Credit Losses

The Company generally sells its products to large governmental entities and large corporations in the United States. Accounts receivable are recorded at invoiced amounts and are non-interest bearing.

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The Company determines estimates of uncollectible accounts receivable based primarily on actual historical bad debt and sales return trends, customers financial condition and general economic conditions. The Company's historical credit loss experience provides the basis for the estimation of expected credit losses, as well as current economic and business conditions, and anticipated future economic events that may impact collectability. In developing its expected credit loss estimate, the Company evaluated the appropriate grouping of financial assets based upon its evaluation of risk characteristics, including consideration of the types of products and services sold. Account balances are written off against the allowance for expected credit losses after all means of collection have been exhausted and the potential for recovery is considered remote.

Occasionally certain long-standing customers, who routinely place large orders, will have unusually large receivables balances relative to the total gross receivables. Management monitors the payments for these large balances closely and very often requires payment of existing invoices before shipping new sales orders. As of March 31, 2025 and December 31, 2024, the Company did not have a reserve for credit losses as all accounts receivable are considered collectible. Accounts receivable balances as of March 31, 2025, December 31, 2024 and January 1, 2024 were \$2,782,650, \$1,226,757 and \$1,648,904, respectively.

Concentration of Credit and Sales Risk

The Company sells its product to commercial and government customers under agreements that are normally paid within 30 days of contract completion.

For the three months ended March 31, 2025, the Company had revenue from twenty customers and three customer represented 83% of total revenue. The primary reason for the high level of customer concentration for the three months ended March 31, 2025 was due to reliance on these three customers for the three months ended March 31, 2024. As of March 31, 2025, two customers represent approximately 81% and 13% of outstanding account receivables. Due to the nature of the customers and timely payment history, customer concentration and credit risk in account receivables is estimated to be minimal.

For the three months ended March 31, 2024, the Company had revenue from seventeen customers and one customer represented 78% of total revenue, although such a high level of customer concentration is not typical. The primary reason for the increase in reliance on a single customer for the three months ended March 31, 2024 was due to one large order received in late 2023 which was fulfilled in the three months ended March 31, 2024. As of March 31, 2024, two customers represent approximately 52% and 27% of outstanding account receivables. Due to the nature of the customers and timely payment history, customer concentration and credit risk in account receivables is estimated to be minimal.

Inventory

The Company's purchase of inventory, primarily computer servers, is undertaken to match purchase orders received from customers. Upon receipt of inventory, the Company generally configures the servers and loads proprietary software onto the servers before shipping out. The Company holds inventory for a short period of time and as of March 31, 2025 and December 31, 2024, it had no inventory in stock. Inventory value is primarily material costs and is valued at the lower of cost (first in, first out method) or net realizable value.

Long-Lived Assets

The Company reviews its long-lived assets for impairment annually or when changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Long-lived assets under certain circumstances are reported at the lower of carrying amount or fair value. Assets to be disposed of and assets not expected to provide any future service potential to the Company are recorded at the lower of carrying amount or fair value (less the projected cost associated with selling the asset). To the extent carrying values exceed fair values, an impairment loss is recognized in operating results. The Company recorded no impairment losses for the three months ended March 31, 2025 and 2024.

Research and Development Expenses

Research and development expenses consist of the cost of employees, consultants and contractors who design, engineer and develop new products and processes as well as materials, supplies and facilities used in producing prototypes.

The Company's current research and development efforts are primarily focused on improving the Company's products. The Company is also actively involved in identifying new applications. The Company's current internal team along with outside consultants has considerable experience working with the application of the Company's technologies and their applications. The Company engages third party experts as required to supplement the Company's internal team. The Company believes that continued development of new and enhanced technologies is essential to the Company's future success. The Company incurred research and development expenses of \$719,382 and \$695,366 for the three months ended March 31, 2025 and 2024, respectively, on development activities.

Software Development Costs

Costs incurred in the development of software programs for the Company's products are charged to operations as incurred until technological feasibility of the software has been established. Generally, technological feasibility is established when the software module performs its primary functions described in its original specifications, contains features required for it to be usable in a production environment, is completely documented and the related hardware portion of the product is complete. After technological feasibility is established, any additional costs are capitalized. Capitalization of software costs ceases when the software is substantially complete and is ready for its intended use. No software development costs have been capitalized as of March 31, 2025 and December 31, 2024.

Cost of Net Revenues

Cost of net revenues for products includes components and freight. Cost of net revenues for post contract support and other services includes primarily the cost of personnel and personnel-related expenses to conduct implementations and ongoing client support.

Advertising and Marketing

Advertising costs are charged to selling, general and administrative expenses as incurred. Advertising and marketing costs for the three months ended March 31, 2025 and 2024 were \$169,221 and \$22,458, respectively.

Shipping and Handling of Products

Amounts billed to customers for shipping and handling of products are included in net revenues. Costs incurred related to shipping and handling of products are included in cost of revenues.

Fair Value Measurements

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. This topic also establishes a fair value hierarchy, which requires classification based on observable and unobservable inputs when measuring fair value. The fair value hierarchy distinguishes between assumptions based on market data (observable inputs) and an entity's own assumptions (unobservable inputs). The hierarchy consists of three levels:

Level 1 — Quoted prices in active markets for identical assets and liabilities;

Level 2 — Inputs other than level one inputs that are either directly or indirectly observable; and

Level 3 — Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The Company initially recorded its senior secured convertible promissory notes, earnout liability (unvested earnout shares), and the warrants that were issued with the notes at fair value, remeasured on a recurring basis and considered them as Level 3 instruments. The public and private warrants were considered Level 1 and 2 instruments, respectively. The senior secured convertible promissory notes were converted to equity during the year ended December 31, 2024. The recorded value of other financial assets and liabilities, which consist primarily of cash and cash equivalents, accounts receivable, other current assets, accounts payable and accrued expenses approximate the fair value of the respective assets and liabilities as of March 31, 2025 and December 31, 2024 are based upon the short-term nature of the assets and liabilities.

The Company classifies as liabilities any contracts that (i) require net-cash settlement (including a requirement to net-cash settle the contract if an event occurs and if that event is outside the control of the Company) or (ii) give the counterparty a choice of net-cash settlement or settlement in shares (physical settlement or net-share settlement).

Derivative Liabilities and Earnout Liabilities

The Company does not use derivative instruments to hedge exposures to cash flow, market, or foreign currency risks. The Company evaluates all of its financial instruments, including issued share purchase warrants and earnout shares to determine if such instruments are derivatives or contain features that qualify as embedded derivatives, pursuant to ASC 480 and FASB ASC Topic 815, "Derivatives and Hedging" ("ASC 815"). The classification of derivative instruments, including whether such instruments should be recorded as liabilities or as equity, is re-assessed at the end of each reporting period. The Company classifies as liabilities any contracts that (i) require net-cash settlement (including a requirement to net-cash settle the contract if an event occurs and if that event is outside the control of the Company) or (ii) give the counterparty a choice of net-cash settlement or settlement in shares (physical settlement or net-share settlement).

At the Merger closing, the Company assumed 515,000 private placement warrants and 16,184,612 public warrants. As of March 31, 2025, there were 515,000 private placement warrants and 16,145,210 public warrants outstanding.

Upon consummation of the Merger, the Company evaluated the warrants and concluded that they did not meet the criteria to be classified within the stockholders' deficit. Accordingly, the Company recognizes the warrant instruments as liabilities at fair value and adjusts the instruments to fair value at each reporting period. The initial estimated fair value of the warrants was measured using a Monte Carlo simulation. The subsequent estimated fair value of the public warrants is based on the listed price in an active market for such warrants while the fair value of the private placement warrants continues to be measured using a Monte Carlo simulation with the key inputs being directly or indirectly observable public warrants listed price.

At the closing of the Merger, the Airship AI securityholders that hold shares of common stock of Airship AI, Airship AI options, Airship AI earnout warrants or Airship AI SARs had the contingent right to receive up to 5.0 million additional shares of common stock, subject to certain contingencies. These earnout shares have been categorized into two components: (i) the vested shares that are associated with stockholders with vested equity at the closing of the Merger that will be earned upon achievement of the earnout milestones and (ii) the unvested shares associated with stockholders with unvested equity at the closing of the Merger that will be earned over the remaining service period with the Company on their unvested equity shares and upon achievement of the earnout milestones.

The earnout shares associated with vested shares are recognized as derivative liabilities in accordance with ASC 815-40, as the events that determine the number of earnout shares required to be released or issued, as the case may be, include events that were not solely indexed to the fair value of common stock of the Company. The earnout shares were measured at the Merger closing and subsequently measured at each reporting date until settled or when they met the criteria for equity classification. Accordingly, the Company recognizes the earnout shares as liabilities at fair value and adjusts the instruments to fair value at each reporting period. The earnout shares were valued using a Monte Carlo analysis.

At the closing of the Merger, the earnout shares associated with unvested underlying shares were considered to be equity instruments and valued at approximately \$3,675,000.

During the three months ended March 31, 2025 and 2024, the Company stock-based compensation expense for the vesting of earnout shares was \$133,761. As of March 31, 2025, unrecognized compensation cost related to unvested earnout shares totaled \$2,006,419. The weighted average period over which this remaining compensation cost is expected to be recognized is 3.75 years.

Derivative warrant and earnout shares liabilities are classified as non-current liabilities as their liquidation is not reasonably expected to require the use of significant current assets or require the creation of current liabilities.

Stock-Based Compensation

The Company has share-based compensation plans under which employees, consultants, suppliers and directors may be granted restricted stock, stock appreciation rights, incentive stock options, nonqualified stock options, unvested earnout shares and warrants to purchase shares of common stock at the fair market value at the time of grant. Stock-based compensation cost is measured by the Company at the grant date and the fair value of the award is recognized as an expense, over the requisite service period which is generally the vesting period. The Company adjusts stock-based compensation for changes to the estimate of expected equity award forfeitures based on actual forfeiture experience. The effect of adjusting the forfeiture rate is recognized in the period the forfeiture estimate is changed.

Income Taxes

Income taxes are accounted for using the liability method. Deferred tax assets and liabilities are recognized for future tax consequences attributable to differences between financial statement carrying amounts of existing assets and liabilities and their respective tax bases and net operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the year in which those temporary differences are expected to be recovered or settled. The Company's ability to realize deferred tax assets depends upon future taxable income, as well as the limitations discussed below. For financial reporting purposes, a deferred tax asset must be reduced by a valuation allowance if it is more likely than not that some portion or all of the deferred tax assets will not be realized prior to expiration. The Company considers historical and future taxable income, future reversals of existing taxable temporary differences, taxable income in prior carryback years, and ongoing tax planning strategies in assessing the need for valuation.

Comprehensive (Loss) Gain

Comprehensive (loss) gain is defined as the change in equity of a business during a period from non-owner sources. There was other comprehensive (loss) gain of (\$,409) and \$3,239, respectively, related to foreign exchange translation for the three months ended March 31, 2025 and 2024, respectively.

Going Concern Assessment

The Company applies Accounting Standards Codification 205-40 ("ASC 205-40"), *Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern*, which the Financial Accounting Standards Board ("FASB") issued to provide guidance on determining when and how reporting companies must disclose going concern uncertainties in their consolidated financial statements. ASC 205-40 requires management to perform assessments of an entity's ability to continue as a going concern within one year of the date of issuance of the entity's consolidated financial statements (or within one year after the date on which the consolidated financial statements are available to be issued, when applicable). Further, a company must provide certain disclosures if there is "substantial doubt about the entity's ability to continue as a going concern" and management plans to alleviate the going concern. In May 2025, the Company analyzed its cash requirements and operations at least through May 2026 and has determined that, based upon the Company's current available cash and operations, the Company has no substantial doubt about its ability to continue as a going concern.

Use of Estimates

In preparing these consolidated financial statements in conformity with GAAP, management is required to make estimates and assumptions that may affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the consolidated financial statements and the reported amount of revenues and expenses during the reporting periods. Actual results could differ from those estimates. Significant estimates and assumptions included in the Company's consolidated financial statements relate to the calculation of revenue recognition, stock-based compensation, valuation of common stock, valuation of senior secured convertible notes, warrant liability, earnout share liabilities, accruals for potential liabilities including income taxes, valuation of deferred tax assets and valuation assumptions related to share-based compensation.

Income (Loss) Per Share

Basic income (loss) per share is based upon the net income (loss) for the three months ended March 31, 2025 and 2024 divided by the weighted average shares of common stock outstanding. Diluted net income per share is determined using the weighted average number of common shares and potential common shares (representing the dilutive effect of stock options, warrants and stock appreciation rights) outstanding during the period using the treasury stock method for the three months ended March 31, 2025. Common stock equivalents for the three months ended March 31, 2024 are not included in the calculation of diluted earnings (loss) per share given the Company incurred a loss and they are anti-dilutive. See Note 14—Earnings per share.

Reportable Segments

The Financial Accounting Standards Board, or FASB, Accounting Standard Codification, or ASC, Topic 280, *Segment Reporting*, requires that an enterprise report selected information about reportable segments in its financial reports issued to its stockholders. Operating segments are defined as components of an entity for which separate financial information is available and that is regularly reviewed by the Chief Operating Decision Maker (“CODM”) in deciding how to allocate resources to an individual segment and in assessing performance. The Chief Executive Officer, Chief Financial Officer and President are the Company’s CODM. The CODM monitors the revenue and expense components of the various products and services the Company offers, but operations are managed and financial performance is evaluated on a corporation-wide basis in comparison to a business plan which is developed each year. Accordingly, all operations are considered by the CODM to be one operating segment and one reportable segment as contained in the Consolidated Statements of Operations and Comprehensive Loss to the consolidated financial statements. The CODM uses consolidated net income (loss) as its required measure of segment profit/loss, as such measure is determined in accordance with the measurement principles most consistent with the consolidated financial statements.

Recent Accounting Pronouncements

All recent accounting pronouncements issued by the FASB, its Emerging Issues Task Force, the American Institute of Certified Public Accountants, and the SEC did not or are not believed by management to have a material impact on the Company’s present or future financial statements.

3. Advances due to and from Founders

Advances due to Founders

During 2024, Mr. Huang and Mr. Xu advanced Airship AI \$ 2,100,000 and were repaid \$2,550,000, with \$1,300,000 recorded as advances from founders as of December 31, 2024. During 2025, Mr. Huang and Mr. Xu were repaid \$ 300,000 each, with \$700,000 recorded as advances from founders as of March 31, 2025. The outstanding advances as of March 31, 2025 are non-interest bearing and the Company expects to pay the balance off within a one year period.

Master Loan Agreement

On September 27, 2024, the Company entered into a Master Loan Agreement with Mr. Huang, whereby he may provide additional funding of up to \$1,500,000 under certain terms and conditions. The agreement provides for interest of 6%. The Company agreed to pay interest for the 2024 advances (described under Advances to Founders above) of \$11,913 and issued warrants to purchase up to 220,000 shares of common stock. The warrants have an exercise price of \$2.36 per share, are exercisable immediately upon issuance and will expire in five years following the date of issuance. The \$284,478 fair value of the warrant is recorded in permanent equity in the consolidated balance sheets and was fully expensed on the date of grant. There are no outstanding advances under this Master Loan Agreement as of March 31, 2025 and December 31, 2024.

4. Revenues

Disaggregation of Revenue

The Company's net revenues for the three months ended March 31, 2025 and 2024 consisted of approximately \$4.5 million and \$9.4 million, respectively, of hardware and software bundled systems for which revenue is transferred at a point in time. The Company's remaining net revenue of approximately \$1.0 million and \$1.2 million relates to PCS revenue and other services which are transferred over time. Within each product category, contract terms, conditions and economic factors affecting the nature, amount, timing, and uncertainty around revenue recognition and cash flow are substantially similar.

Contract Balances

A receivable is recognized in the period the Company delivers goods or provides services or when the Company's right to consideration is unconditional. The Company usually does not record contract assets because the Company has an unconditional right to payment upon satisfaction of the performance obligation, and therefore, a receivable is more commonly recorded than a contract asset. Receivables are generally paid within thirty days and there is no financing element to the customer contracts. As of March 31, 2025 and December 31, 2024, there are no unbilled receivable balances.

The Company's short-term and long-term deferred revenue balances totaled \$2,948,695 and \$2,528,716 as of March 31, 2025. The Company's short-term and long-term deferred revenue balances totaled \$3,238,483 and \$2,951,850 as of December 31, 2024. Of the deferred revenue balance of \$6,190,333 and \$8,970,780 as of January 1, 2025 and 2024, the Company recognized approximately \$985,548 and \$1,176,239 during the three months ended March 31, 2025 and 2024, respectively.

Remaining Performance Obligations

As of March 31, 2025 and December 31, 2024, the Company had approximately \$5.5 million and \$6.2 million of remaining performance obligations, which were comprised of deferred service contracts not yet delivered. The Company expects to recognize approximately 43% of its remaining performance obligations as revenue in fiscal 2025 and the remaining 57% in fiscal 2026 and years thereafter.

Costs to Obtain or Fulfill a Contract

The Company does not pay any material variable compensation to obtain a customer contract. Additionally, the majority of the Company's cost of fulfillment as a seller of products is classified as inventory and then cost of revenue when the product is sold. Other costs of contract fulfillment such as software maintenance are expensed in the period incurred and align with when the revenue is amortized.

5. Notes Payable and Convertible Notes Payable

On June 22, 2023, the Company issued a \$2,000,000 senior secured convertible promissory note to Platinum Capital Partners, Inc. During the year ended December 31, 2024, the Company issued 879,051 shares of common stock related to the conversion of \$2,000,000 of the senior secured convertible promissory note.

On October 3, 2023, the Company issued senior secured convertible promissory notes for \$600,000 to two private investors. At the option of the holders, the notes were convertible into cash, common stock or a combination of cash and stock. On March 5, 2024, the two private investors converted the notes with a face value of \$600,000 and interest into 169,204 shares of the Company's common stock valued at \$835,610. On September 13, 2024, the Company issued an additional 86,198 shares of common stock related to the conversion of notes at \$2.65 per share.

During the three months ended March 31, 2024, the Company recorded an unrealized loss due to the increase in the fair value of the convertible notes payable totaling \$2,039,377.

6. Stockholders' Deficit

Authorized and Outstanding Stock

The Company is a Delaware company and its affairs are governed by its certificate of incorporation, its bylaws and the Delaware General Corporation Law and the common law of the State of Delaware. The Company's charter authorizes the issuance of 205,000,000 shares, consisting of 200,000,000 shares of common stock and 5,000,000 shares of preferred stock, par value \$0.0001 per share.

Details on the common stock, preferred stock and equity incentive plans were disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2024 and filed with the SEC on February 28, 2025.

Common Stock

As of March 31, 2025 and December 31, 2024, there were 31,844,471 and 30,588,413 shares of common stock outstanding, respectively.

Three Months Ended March 31, 2025

During the three months ended March 31, 2025, the Company had the following issuances of equity securities:

As of September 30, 2024, the Company determined the First Operating Performance Milestone of the earnout shares was achieved resulting in the vesting of 1,250,000 shares, of which 1,160,906 shares of the Company's common stock were issued to applicable personnel on January 7, 2025.

During the three months ended March 31, 2025, investors exercised warrants for 13,200 shares of the Company's common stock at \$4.50 per share, and the Company received proceeds of \$59,400.

During the three months ended March 31, 2025, the Company issued an aggregate of 81,952 shares of common stock and received \$43,201 upon the exercise of stock options at exercise prices ranging from \$0.12 to \$1.64 per share.

2023 Equity Incentive Plan

The Company has adopted the 2023 Equity Incentive Plan (the "2023 Plan"), which plan was approved by stockholders at the extraordinary general meeting held in December 2023. Details on the equity incentive plan were disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2023 and filed with the SEC on April 1, 2024. The 2022 Combined Incentive and Non-Qualified Stock Option Plan (the "2022 Plan") is no longer available for use for the grant of future awards. The 2022 Plan will continue to govern the terms of awards that have been granted under the 2022 Plan before, and that are still outstanding following the Merger.

The aggregate number of shares of common stock initially reserved and available for grant and issuance under the 2023 Plan is 4,000,000. Such aggregate number of shares of stock will automatically increase on January 1 of each year for a period of ten years commencing on January 1, 2024 and ending on January 1, 2033, in an amount equal to 2.0% of the total number of shares of common stock outstanding on December 31 of the preceding year. The aggregate number of shares of common stock reserved for grant and issuance under the 2023 Plan is 3,334,721 as of March 31, 2025. The Company measures the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. The cost is recognized over the period which an employee is required to provide service in exchange for the award—the requisite service period.

The Company had the following stock option activity during the three months ended March 31, 2025:

During the three months ended March 31, 2025, the Company granted stock options to 3 employees to purchase an aggregate of 55,000 shares of common stock with an exercise price of \$3.34 and which vest primarily quarterly over four years and expire on during 2035.

During the three months ended March 31, 2025, the Company issued an aggregate of 81,952 shares of common stock and received \$43,201 upon the exercise of stock options at exercise prices ranging from \$0.12 to \$1.64 per share.

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Stock option activity for the three months ended March 31, 2025 was as follows:

	Shares	Exercise Price
Outstanding as of January 1, 2025	5,527,559	\$ 1.04
Granted	455,000	3.34
Exercised	(81,952)	(0.53)
Forfeited	-	-
Outstanding as of March 31, 2025	<u>5,900,607</u>	<u>\$ 1.22</u>

The following table summarizes information about stock options outstanding and exercisable as of March 31, 2025:

Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Life In Years	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price Exercisable	Weighted Average Remaining Life In Years - Vested and Exercisable
\$ 0.12	2,367,033	3.79	\$ 0.12	2,367,033	\$ 0.12	3.79
0.57	922,963	3.27	0.57	922,963	0.57	3.27
1.49-1.65	1,040,798	7.19	1.64	560,642	1.64	7.19
1.90	49,813	2.73	1.90	15,567	1.90	2.73
2.86-2.95	1,065,000	9.54	2.91	130,938	2.91	9.54
3.27-4.47	455,000	9.91	3.34	100,000	3.34	9.91
	<u>5,900,607</u>	<u>6.34</u>	<u>\$ 1.22</u>	<u>4,097,143</u>	<u>\$ 0.60</u>	<u>6.34</u>

There were 5,900,607 options to purchase common stock at an average exercise price of \$1.22 per share outstanding as of March 31, 2025 under the 2023 and 2022 Plans. The Company recorded \$294,525 and \$135,227 of compensation expense, net of related tax effects, relative to stock options for the three months ended March 31, 2025 and 2024, respectively, in accordance with ASC 718. As of March 31, 2025, there was \$ 2,777,071 of total unrecognized costs related to employee granted stock options that were not vested. These costs are expected to be recognized over a period of approximately 3.5 years.

The significant weighted-average assumptions relating to the valuation of the Company's stock option grants were as follows for the three months ended March 31, 2025:

Assumptions	3/31/2025
Estimated stock price	\$3.27-4.47
Exercise price	\$3.27-4.47
Dividend yield	0%
Expected life	4 years
Expected volatility	57.1%
Risk free interest rate	3.48%-3.81%

There were stock incentive plan awards outstanding at March 31, 2025 totaling 5,900,607 shares with an aggregate intrinsic value of \$15,552,307.

Stock Appreciation Rights Plan

Related to the Share Exchange Agreement with Super Simple AI, Inc., on February 17, 2022, the Company's Board of Directors approved the 2022 Stock Appreciation Rights Plan (the "SAR Plan") to issue a maximum of 1,500,000, which was later adjusted to 2,637,150 stock appreciation rights ("SARs") after the Merger.

As of March 31, 2025 and December 31, 2024, there were 1,758,000 SARs outstanding with a base value of \$0.12 and January 2028 expiration. There were no SAR grants during the three months ended March 31, 2025 or the year ended December 31, 2024.

Warrants to Purchase Common Stock

See Note 11 for public and private placement warrants assumed after the merger.

The Company had the following warrant activity during the three months ended March 31, 2025:

During the three months ended March 31, 2025, investors exercised warrants for 13,200 shares of the Company's common stock at \$4.50 per share, and the Company received proceeds of \$59,400.

Warrant activity for the three months ended March 31, 2025 was as follows:

	Warrants	Weighted Average Exercise Price
Outstanding January 1, 2025	21,961,690	4.13
Issued	-	-
Exercised	(13,200)	(4.50)
Forfeited	-	-
Outstanding at March 31, 2025	<u>21,948,490</u>	<u>\$ 4.13</u>

A summary of the warrants outstanding as of March 31, 2025 were as follows:

Number of Warrants	March 31, 2025			
	Weighted Average Remaining Life (In Years)	Weighted Average Exercise Price	Shares Exercisable	Weighted Average Exercise Price
2,689,902	3.20	\$ 1.77	2,689,902	\$ 1.77
220,000	4.50	2.36	220,000	2.36
216,216	4.38	3.47	216,216	3.47
18,822,372	3.84	4.50	18,822,372	3.84
<u>21,948,490</u>	<u>3.81</u>	<u>\$ 4.13</u>	<u>21,948,490</u>	<u>\$ 4.13</u>

Earnout Liability

See Note 12 for common stock shares related to earnout liability.

7. Employee 401(k) Plan

The Company has a 401(k) plan for its employees. The plan provides for a 3.5% match on up to 6% of deferred salary. The Company expensed \$50,978 and \$50,102 of contributions during the three months ended March 31, 2025 and 2024, respectively.

8. Related Party Transactions

Advances due to Founders

During 2024, Mr. Huang and Mr. Xu advanced Airship AI \$ 2,100,000 and were repaid \$2,550,000, with \$1,300,000 recorded as advances from founders as of December 31, 2024. During 2025, Mr. Huang and Mr. Xu were repaid \$ 300,000 each, with \$700,000 recorded as advances from founders as of March 31, 2025. The outstanding advances as of March 31, 2025 and December 31, 2024 are non-interest bearing and the Company expects to pay the balance off within a one year period.

Master Loan Agreement

On September 27, 2024, the Company entered into a Master Loan Agreement with Mr. Huang, whereby he may provide additional funding of up to \$1,500,000 under certain terms and conditions. The agreement provides for interest of 6%. The Company agreed to pay interest for the 2024 advances (described under Advances to Founders above) of \$11,913 and the Company issued warrants to purchase up to 220,000 shares of the Company's common stock. The warrants have an exercise price of \$2.36 per share, are exercisable immediately upon issuance and will expire in five years following the date of issuance. The \$284,478 fair value of the warrant is recorded in permanent equity in the consolidated balance sheets and was fully expensed on the date of grant. There are no outstanding advances under this Master Loan Agreement as of March 31, 2025 and December 31, 2024.

9. Commitments, Contingencies and Legal Proceedings

Legal Proceedings

The Company may from time to time become a party to various legal proceedings arising in the ordinary course of its business. The Company is currently not a party to any pending legal proceeding that is not ordinary routine litigation incidental to its business.

Properties and Operating Leases-Right of Use Asset and Lease Liability

Lease agreements are evaluated to determine whether an arrangement is or contains a lease in accordance with ASC 842, *Leases*. Right of use lease assets and lease liabilities are recognized based on the present value of the future minimum lease payments over the lease term at the commencement date. The incremental borrowing taking into consideration the Company's credit quality and borrowing rate for similar assets is used in determining the present value of future payments. Lease expense is recorded as general and administrative expenses on the Company's consolidated statements of operations and comprehensive income (loss). The Company elected the package of transitional practical expedients, under which (1) the Company did not reassess whether any expired or existing contracts are or contain leases, (2) the Company did not reassess the lease classification for any expired or existing leases and (3) the Company did not reassess initial direct costs for any existing leases. Additionally, the Company elected the short-term lease recognition exemption for all leases that qualify, meaning it does not recognize right-of use assets or lease liabilities for those leases. The Company also elected the practical expedient to not separate lease and non-lease components for all asset classes.

On July 13, 2023, the Company entered into a lease in Redmond, WA for 15,567 square feet of office and warehouse space which started October 1, 2023. The monthly payment is \$25,000 per month. The lease expires October 31, 2027 and the monthly payment increases 3% on July 31, 2024 and each year thereafter. There is a one three year option to extend the lease based on the fair market rate on October 31, 2027, which the Company expects to exercise.

On February 29, 2024, the Company extended an office lease in Mooresville, North Carolina. The Company leases 3,621 square feet and the net monthly payment is \$6,488. On August 27, 2024, the Company extended the lease, which expired on February 28, 2025.

On February 1, 2025, the Company entered into an office lease in Mooresville, North Carolina. The Company leases 5,240 square feet and the net monthly payment is \$9,105. The lease expires January 31, 2028 and the monthly payment increases 3% on February 1, 2026 and each year thereafter. There is no option to extend the lease.

The Company has entered into operating leases for office and development facilities for three to four years and may include an option to renew. The Company determines whether an arrangement is or contains a lease based upon the unique facts and circumstances at the inception of the lease. Operating lease liabilities and their corresponding right-of-use assets are recorded based upon the present value of the lease payments over the expected lease term. As of March 31, 2025 and December 31, 2024, total operating lease liabilities were \$1,164,292 and \$943,703, respectively. Right of use assets was \$1,102,967 and \$882,024 at March 31, 2025 and December 31, 2024, respectively. Current lease liabilities were \$405,917 and \$305,178 at March 31, 2025 and December 31, 2024, respectively. In the three months ended March 31, 2025 and 2024, the Company recognized \$102,417 and \$98,943 in total lease costs for the leases, respectively. Because the rate implicit in each lease is not readily determinable, the Company uses its estimated incremental borrowing rate to determine the present value of the lease payments.

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The weighted average remaining lease term for the operating leases was thirty two months at March 31, 2025 and the weighted average discount rate was 7%.

The minimum future lease payments as of March 31, 2025 are as follows:

Years Ended March 31,	
2026	\$ 471,901
2027	486,075
2028	<u>323,661</u>
Total remaining payments	1,281,637
Less Imputed Interest	<u>(117,345)</u>
Total lease liability	<u>\$ 1,164,292</u>

Employment Agreement

On March 4, 2025, the Company entered into an employment agreement with Paul Allen to serve as President. The employment agreement provides for a base salary of \$350,000. The term of the employment agreement is for a period of three years, which will be automatically extended for additional one-year periods unless either party gives the other party written notice of such party's decision not to renew the term at least 90 days prior to the end of the initial three-year term or any renewal term. Mr. Allen is also eligible to participate in annual performance-based bonus programs established from time to time by the Company's Board, subject to the achievement by Mr. Allen and the Company of the applicable performance criteria set forth in the employment agreement and established for Mr. Allen by the Board. The employment agreement is terminable by either party at any time. In the event of termination by us without cause or by Mr. Allen for good reason, as those terms are defined in the employment agreement, he is entitled to three months' severance.

In connection with entering into the employment agreement, Mr. Allen was granted ten-year options under our 2023 Plan to purchase 100,000 shares of common stock, which options vest immediately, at an exercise price equal to \$3.27, being the fair market value on the date of grant. The total stock compensation expense related to this grant was approximately \$131,000. Mr. Allen was also granted ten-year options under the Plan to purchase 300,000 shares of common stock, which options vest quarterly over four years, at an exercise price equal to \$3.27, being the fair market value on the date of grant.

10. Income Taxes

The Company recorded a provision for income taxes of \$0 for the three months ended March 31, 2025 and 2024.

The Company's effective tax rate was 0% for the three months ended March 31, 2025 and 2024. The difference between the effective tax rate and the federal statutory tax rate for the three months ended March 31, 2025 and 2024 primarily related to the valuation allowance on the Company's deferred tax assets.

For interim periods, the Company estimates its annual effective income tax rate and applies the estimated rate to the year-to-date income or loss before income taxes. The Company also computes the tax provision or benefit related to items reported separately and recognizes the items net of their related tax effect in the interim periods in which they occur. The Company also recognizes the effect of changes in enacted tax laws or rates in the interim periods in which the changes occur.

As of March 31, 2025 and December 31, 2024, the Company retains a full valuation allowance on its deferred tax assets. The realization of the Company's deferred tax assets depends primarily on its ability to generate taxable income in future periods. The amount of deferred tax assets considered realizable in future periods may change as management continues to reassess the underlying factors it uses in estimating future taxable income.

11. Warrant Liability

At the Merger closing, the Company assumed 515,000 private placement warrants and 16,184,612 public warrants. On June 3, 2024, the Company permanently reduced the exercise price of such warrants from \$11.50 per share to an exercise price of \$7.80 per share. On November 20, 2024, the Company further reduced the exercise price of the outstanding public warrants and private warrants to an exercise price of \$4.50 per share. The purpose of this reduced exercise price was to potentially raise proceeds received from the exercise of such warrants, if any, for working capital and general corporate purposes.

Details on the warrant liability were disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2024 and filed with the SEC on February 28, 2025. The public warrants will expire on December 21, 2028.

The following table is a summary of the number of shares of the Company's common stock issuable upon exercise of the public and private warrants outstanding as of March 31, 2025 and December 31, 2024:

March 31, 2025				
	Number of Shares	Exercise Price	Expiration Date	Fair Value
Public Warrants	16,145,210	\$ 4.50	December 21, 2028	\$ 18,082,635
Private Warrants	515,000	\$ 4.50	December 21, 2028	\$ 576,800
December 31, 2024				
	Number of Shares	Exercise Price	Expiration Date	Fair Value
Public Warrants	16,158,410	\$ 4.50	December 21, 2028	\$ 33,124,868
Private Warrants	515,000	\$ 4.50	December 21, 2028	\$ 1,055,750

12. Earnout Liability

At the closing of the Merger, the Airship AI securityholders that hold shares of common stock of Airship AI, Airship AI options, Airship AI earnout warrants or Airship AI SARs had the contingent right to receive up to 5,000,000 earnout shares of the Company's common stock if certain earnout milestones are met. Refer to the Company's annual report on Form 10-K filed with the SEC on February 28, 2025 for more information.

As of March 31, 2025, the estimated fair value of the earnout liability decreased to \$1,199,079 primarily due to the common stock issued to settle approximately \$3 million of earnout liability that was previously achieved plus the decrease in the Company's share price, which resulted in a gain due to the change in fair value of the earnout liability during the three months ended March 31, 2025 of approximately \$9.8 million and is recorded on the consolidated statements of operations and comprehensive income (loss).

In addition, a portion of the earnout shares may be issued to individuals with unvested equity awards. While the payout of these shares requires the achievement of the earnout milestones, the individuals must complete the remaining service period associated with these unvested equity awards to be eligible to receive the earnout shares. As a result, these unvested earn-out shares are equity-classified awards and have an aggregated grant date fair value of \$2,675,223 (or \$5.96 per share).

As of September 30, 2024, the Company determined the first operating performance milestone was achieved resulting in the vesting of 1,250,000 earnout shares, of which 1,160,906 shares of the Company's common stock were issued to applicable personnel on January 7, 2025. The fair value of the 1,160,906 vested shares on the issuance date of \$5,282,008 was determined using the Company's closing trading price on January 7, 2025 and was reclassified from earnout liability to equity as additional paid in capital on the consolidated balance sheet. The remaining 89,094 shares that vested as of September 30, 2024 will continue to be valued on a recurring basis as a Level 1 instrument until issued. The remaining unvested earnout shares continue to be accounted for as liabilities until their respective triggering event occurs.

13. Fair Value Measurements

The following table sets forth by level within the ASC 820, Fair Value Measurement, fair value hierarchy of the Company's liabilities that are measured at fair value on a recurring basis as of March 31, 2025:

	March 31, 2025			Total
	Level 1	Level 2	Level 3	
Liabilities-				
Earnout liability	\$ 343,901	\$ -	\$ 7,855,178	\$ 8,199,079
Warrant liability (Public Warrants)	18,082,635	-	-	18,082,635
Warrant liability (Private Warrants)	-	576,800	-	576,800
Total liabilities measured at fair value	\$ 18,426,536	\$ 576,800	\$ 7,855,178	\$ 26,858,514

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The following table sets forth by level within the ASC 820, Fair Value Measurement, fair value hierarchy of the Company's liabilities that are measured at fair value on a recurring basis as of December 31, 2024:

	December 31, 2024			Total
	Level 1	Level 2	Level 3	
Liabilities-				
Earnout liability	\$ 7,825,000	\$ -	\$ 15,479,808	\$ 23,304,808
Warrant liability (Public Warrants)	33,124,868	-	-	33,124,868
Warrant liability (Private Warrants)	-	1,055,750	-	1,055,750
Total liabilities measured at fair value	<u>\$ 40,949,868</u>	<u>\$ 1,055,750</u>	<u>\$ 15,479,808</u>	<u>\$ 57,485,426</u>

The estimated fair value of the earnout liability was determined using a Monte Carlo Model. The assumptions utilized in the calculation are based on the achievement of certain milestones including projected stock price, volatility, probability of meeting the federal law enforcement agency growth and risk-free rate. The following assumptions were used in the simulation at each valuation date:

	March 31, 2025	March 31, 2024
Stock price	\$ 3.86	\$ 6.59
Risk-free interest rate	3.88%	4.23%
Expected term (in years)	3.8	4.8
Expected volatility	60.2%	69.3%
Dividend yield	0%	0

The fair value of the 1,250,000 vested shares as of December 31, 2024 of \$7,825,000 was determined using the Company's closing trading price on December 31, 2024. On January 7, 2025, 1,160,906 shares were issued with a fair value of \$5,282,125 to applicable personnel and were reclassified to equity as additional paid in capital. The fair value of the remaining 89,094 shares that vested as of September 30, 2024 was determined using the Company's closing stock price on March 31, 2025.

The initial estimated fair value of the private warrants was measured using a Monte Carlo simulation. The estimated fair value of the public warrants is based on the listed price in an active market for such warrants and the fair value of the private placement warrants continues to be measured based on the public warrants listed price.

There were no transfers of financial instruments between valuation levels during the three months ended March 31, 2025 and 2024.

14. Earnings per Share

The following table sets forth the computation of basic and diluted net income (loss) per share attributable to common stockholders:

	March 31, 2025	March 31, 2024
Net income (loss)	<u>\$ 23,707,985</u>	<u>\$ (31,964,469)</u>
Weighted average shares outstanding-		
Basic	31,704,117	22,898,487
Add: dilutive effect of stock options, SARs, vested earnout shares and Airship warrants	7,116,722	-
Diluted	<u>38,820,839</u>	<u>22,898,487</u>
Income (loss) per share-		
Basic	\$ 0.75	\$ (1.40)
Diluted	\$ 0.61	\$ (1.40)

The following potentially dilutive shares were not included in the calculation of diluted shares outstanding for the periods presented as the effect would have been anti-dilutive:

	March 31, 2025	March 31, 2024
Public Warrants	16,145,210	16,159,112
Private Warrants	515,000	515,000
Warrants	2,162,162	-
Outstanding stock options	25,000	-
	<u>18,847,372</u>	<u>16,674,112</u>

The 3,750,000 remaining unvested earnout shares as of March 31, 2025 are excluded from basic and diluted net loss per share as such shares are contingently issuable until the Company exceeds certain milestone thresholds that have not been achieved.

15. Subsequent Events

The Company evaluated subsequent events, for the purpose of adjustment or disclosure, up through the date the financial statements were issued. Subsequent to March 31, 2025, there were no material transaction that occurred that would require recognition or disclosure in the financial statements.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The following discussion and analysis summarizes the significant factors affecting our operating results, financial condition, liquidity and cash flows as of and for the periods presented below. The following discussion and analysis should be read in conjunction with our financial statements and the related notes thereto included elsewhere in this report. The discussion contains forward-looking statements that are based on the beliefs of management, as well as assumptions made by, and information currently available to, management. Actual results could differ materially from those discussed in or implied by forward-looking statements as a result of various factors, including those discussed below and elsewhere in this report, particularly in the sections titled "Risk Factors" and "Special Note Regarding Forward-Looking Statements."

Overview

We are a robust AI-driven data management platform that solves complex data challenges for large institutions operating in dynamic and mission-critical environments with rapidly increasing volumes of data being ingested from a similarly rapidly growing number of data sources.

We solve these challenges by structuring "dark" or unstructured data at the edge, the location at which the data is generated and collected, and leveraging purpose-built AI models. Unstructured, or "dark" data, which is typically categorized as qualitative data, cannot be processed and analyzed via conventional data tools and methods. Conversely, structured data, typically categorized as quantitative data, is highly organized and easily decipherable by machine learning algorithms.

Structuring and then analyzing data using AI models at the edge, versus transmitting the data from the edge back to a central processing location for structuring and analysis, enables real-time decision making and data-driven operational efficiency.

We specialize in ingesting all available metadata from edge-based sensors used by government and law enforcement agencies around the world, including surveillance cameras (video), audio, telemetry, acoustic, seismic, and autonomous devices, along with large commercial corporations with fundamentally similar capabilities and requirements.

Data generated by these edge-based sensors, including video, can then be run through our trained AI models to detect objects present within the video frame. Once an object is detected, for example an automobile, additional identifying characteristics of the object can be extracted from the image including the license plate characters and the make, model, and color of the automobile. This process of analyzing, logging and categorizing ingested data is referred to as "structuring" the data.

Airship AI's software allows customers to view structured data both in real-time as well as to conduct searches on the structured data at a later point in time. Real-time structured data use includes, for example, alarms on a specific license plate or a specific make, model or color of automobile. Non-real-time structured data use includes, for example, searching a database of video data that has been previously ingested and stored to find instances of a particular license plate being visible, along with other logged vehicle characteristics such as make, model and color of an automobile.

Additional edge deployed AI models enable similar object detection and recognition of common and custom trained objects, such as an aircraft, boat, person, animal, bag, or weapon. Airship AI's models provide similar data points for these object types allowing analysts the ability to be notified in real-time of the detection of a specified object and similarly search for historically detected objects. Examples include detecting aircrafts and boats along with their respective tail numbers and hull registration numbers.

Our AI modelling process starts with pre-trained AI models from our technology ecosystem partners which we then customize using proprietary datasets tailored towards our customers unique workflow requirements. Where customers have pre-existing AI models or engines, we integrate those models or engines into our edge platform allowing customers to leverage proprietary models within the Airship AI software ecosystem.

Our primary offerings include Outpost AI, Acropolis, and Airship Command. Our offerings allow customers to manage their data across the full data lifecycle, when and where they need it, using a highly secure permissioned based architecture.

Recent Developments

As of September 30, 2024, we determined the first operating performance milestone of the earnout shares was achieved resulting in the vesting of 1,250,000 earnout shares, of which 1,160,906 shares of our common stock were issued to applicable personnel on January 7, 2025.

Fair Value Transactions in Connection with Merger

As a result of the merger, we entered into the following transactions that were measured at fair value and vary quarterly with the share price and other items. Any change is non-cash and is recorded as a gain or loss in other income (expense). See Note 13– Fair Value Measurements for more information.

	Liability as of March 31, 2025	Liability as of December 31, 2024
Earnout liability	\$ 8,199,079	\$ 23,304,808
Warrant liability (Public Warrants)	18,082,635	33,124,868
Warrant liability (Private Warrants)	576,800	1,055,750
Total liabilities measured at fair value	<u>\$ 26,858,514</u>	<u>\$ 57,485,426</u>
Other income (expense) related to instruments recorded at fair value during the three months ended March 31, 2025 and 2024	<u>\$ 25,344,788</u>	<u>\$ (30,371,318)</u>

Private Placement and Public Warrants in Connection with Merger

At the merger closing, we assumed 515,000 private placement warrants and 16,184,612 public warrants. On June 3, 2024, we permanently reduced the exercise price of such warrants from \$11.50 per share to an exercise price of \$7.80 per share. On November 20, 2024, the Company further reduced the exercise price of the outstanding public warrants and private warrants to an exercise price of \$4.50 per share. The purpose of this reduced exercise price was to potentially raise proceeds received from the exercise of such warrants, if any, for working capital and general corporate purposes. As of March 31, 2025, there were 515,000 private placement warrants and 16,145,210 public warrants outstanding.

Key Performance Indicators

Historically, a majority of our product revenue has consisted primarily of a bundled hardware and software product and to date we have sold or licensed a minimal amount of standalone software. In the future, we expect to see more delivery of our products using a cloud-based software solution which will allow us to create additional subscription revenue.

We have historically evaluated our business solely based on revenue generated from customers and we have not tracked any other customer-related metrics. As we grow and increase our product offerings and customer base, we intend to modify and develop more advanced performance indicators. We believe the following key performance indicators apply to us in the future:

- *Growth within existing government customers.* While we currently have a strong footprint across multiple large U.S. government agencies, growing our business within these agencies outside of the investigation focused departments is a fundamental area of our projected growth. Our ability to expand our footprint by implementing AI based solutions that leverage our core existing competencies within the agencies will be a critical indicator of the success of this strategy. We will measure progress against this objective through the disclosure of awards for new business within these agencies during the affected timeframe, providing tangible evidence of the success of our strategy to both management and investors alike.
- *Greater penetration into the commercial marketplace.* While we have several existing customers in the commercial marketplace, our ability to build on the solutions we provide those customers and expand that base will be critical to our projected growth objectives. We will measure progress against this objective through the disclosure of the number of new commercial customers added during the affected timeframe, providing tangible evidence of the success of our strategy to both management and investors alike.
- *Expansion of our edge AI based solutions.* We began to sell AI based solutions in late 2022. Our current strategy is highly focused on the transition of data management and analysis workloads to the edge, driving efficiency and cost savings for our customers. This strategy also includes new models being trained to extract data at the edge which enables real-time intelligent decision making for our customers. We will measure progress against this objective through the disclosure of the numbers of edge AI hardware devices we are selling as well as the growth of our edge AI analytic capabilities, providing tangible evidence of the success of our strategy to both management and investors alike.

Principal Factors Affecting Our Financial Performance

We believe the following factors and trends may cause previously reported financial information not to be necessarily indicative of future operating results or future financial conditions:

- *Increase in the sales of lower margin solutions as we expand our operational footprint.* While our current focus remains on expanding our AI driven software application portfolio, opportunities will continue to present themselves to provide those software-based solutions as part of a larger hardware-based turn-key solutions where Airship AI can provide a unique value-add to the customer. While these solutions will positively affect revenue we anticipate our operating profits in future periods may be adversely affected as compared to previous years due to the lower operating margin for hardware versus software applications.
- *Challenges due to geo-political driven supply-chain constraints.* While many of the COVID-19 driven supply chain issues have been resolved, challenges to the timely production and delivery of Taiwan based products we utilize for our edge AI platform due to geo-political factors is a concern looking forward. In the event that our suppliers are unable to provide timely delivery of those supplies it will significantly impact our ability to meet delivery schedules for existing and anticipated edge AI hardware-based solutions.
- *Near-term impacts due to merger and acquisition activity.* If Airship AI merges with or acquires another company, it is reasonably expected that there will be increased operating expenses and costs associated with the merger that could negatively impact operating profits in the future periods immediately following the M&A event. The extent and longevity of those impacts is not possible to quantify.
- *Potential tariffs may impact financial performance.* Changes in international trade policies, including the imposition of new tariffs, quotas, trade restrictions, or other government-imposed barriers to trade, could have a material adverse effect on our business, financial condition, and results of operations. We rely on Taiwan and Canada for certain raw materials, components, and finished goods. For example, if the U.S. government were to impose additional tariffs on goods imported from countries where we source key inputs—such as Taiwan and Canada—or if retaliatory tariffs were imposed on U.S. exports, the cost of our products could increase, potentially reducing demand, compressing margins, or requiring us to adjust our pricing structure.

Segment Reporting

The Financial Accounting Standards Board, or FASB, Accounting Standard Codification, or ASC, Topic 280, Segment Reporting, requires that an enterprise report selected information about reportable segments in its financial reports issued to its stockholders. Operating segments are defined as components of an entity for which separate financial information is available and that is regularly reviewed by the Chief Operating Decision Maker (“CODM”) in deciding how to allocate resources to an individual segment and in assessing performance. The Chief Executive Officer, Chief Financial Officer and President are the Company’s CODM. The CODM monitors the revenue and expense components of the various products and services we offer, but operations are managed and financial performance is evaluated on a corporation-wide basis in comparison to a business plan which is developed each year. Accordingly, all operations are considered by the CODM to be one operating segment and one reportable segment as contained in the Consolidated Statements of Operations and Comprehensive Loss to the consolidated financial statements. The CODM uses consolidated net income (loss) as its required measure of segment profit/loss, as such measure is determined in accordance with the measurement principles most consistent with the consolidated financial statements.

Results of Operations

The following table sets forth key components of our results of operations during the three months ended March 31, 2025 and 2024.

(dollars in thousands)

	Three Months Ended March 31,			
	2025	2024	\$ Variance	% Variance
Net revenues	\$ 5,503	\$ 10,575	\$ (5,072)	-48.0%
Cost of net revenues	3,268	7,947	4,679	58.9%
Gross profit	2,235	2,628	(393)	-15.0%
Research and development expenses	719	695	(24)	-3.5%
Selling, general and administrative expenses	3,230	3,335	105	3.1%
Total operating expenses	3,949	4,030	81	2.0%
Operating loss	(1,714)	(1,402)	(312)	-22.3%
Other income (expense):				
Gain (loss) from change in fair value of earnout liability	9,824	(21,485)	31,309	145.7%
Gain (loss) change in fair value of warrant liability	15,521	(6,847)	22,368	326.7%
Loss from change in fair value of convertible debt	-	(2,039)	2,039	100.0%
Loss on note conversion	-	(159)	159	100.0%
Interest income (expense), net	77	(32)	109	340.6%
Total income (other expense), net	25,422	(30,562)	55,984	183.2%
Income (loss) before income taxes	23,708	(31,964)	55,672	174.2%
Provision for income taxes	-	-	-	-
Net income (loss)	\$ 23,708	\$ (31,964)	\$ 55,672	174.2%

Net Revenues — Net revenues for the three months ended March 31, 2025 decreased \$5,072,000 to \$5,503,000 as compared to \$10,575,000 for the three months ended March 31, 2024, as a result of purchase orders from various federal government agency customers totaling over \$13 million which we primarily shipped in the three months ended March 31, 2024.

On January 20, 2025, President Trump signed an executive order creating an advisory commission, the Department of Government Efficiency to reform federal government processes and reduce expenditures. Pressures on and uncertainty surrounding the U.S. federal government's budget, and potential changes in budgetary priorities and spending levels, could adversely affect staffing levels and the funding for government projects. Disruptions in how the government agencies operate due to these policies are materially affecting our business.

Cost of Net Revenues — Cost of net revenues primarily consists of product costs and post customer support. For the three months ended March 31, 2025, cost of sales decreased \$4,679,000 to \$3,268,000 as compared to \$7,947,000 for the three months ended March 31, 2024. The decrease was due to lower sales, offset by product mix with decreased equipment purchases during the three months ended March 31, 2025.

Research and Development Expenses — Research and development expenses for the three months ended March 31, 2025 increased \$24,000 to \$719,000 as compared to \$695,000 for the three months ended March 31, 2024. The increase was due to increased expenses for product development.

Selling, General and Administrative Expenses — Selling, general and administrative expenses for the three months ended March 31, 2025 decreased \$105,000 to \$3,230,000 as compared to \$3,335,000 for the three months ended March 31, 2024. The decrease was due to (i) reduced professional service expenses of \$211,000; (ii) reduced insurance expenses of \$154,000; (iii) offset increased stock based compensation of \$159,000; (iv) increased sales and marketing expenses of \$147,000 related to expanded trade shows; and other reduced operating expenses of \$46,000.

Other Income (Expense) — Other income for the three months ended March 31, 2025 was \$25,422,000 as compared to other expense of \$30,562,000 for the three months ended March 31, 2024. Other income for the three months ended March 31, 2025 consisted of (i) gain from change in fair value of earnout liability of \$9,824,000; (ii) gain from change in fair value of warrant liability of \$15,521,000; (iii) other income of \$77,000. The gain from change in fair value of various financial instruments was primarily the result of a decrease in our stock price.

Other expense for the three months ended March 31, 2024 consisted of (i) loss from change in fair value of warrant liability of \$6,847,000; (ii) loss from change in fair value of earnout liability of \$21,485,000; (iii) loss from change in fair value of convertible debt of \$2,039,000; (iv) loss on note conversion of \$159,000; and (v) noncash interest of \$32,000.

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Net Income (Loss) — Net income for the three months ended March 31, 2025 was \$23,708,000 as compared to a net loss of \$31,964,000 for the three months ended March 31, 2024. The net income primarily related to noncash items of \$24,833,000. Noncash items included (i) gain from change in warrant liability of \$15,521,000; and (ii) gain from change in earnout liability of \$9,823,000; and offset by (iii) stock based compensation of \$428,000; and (iv) net amortization of operating lease right of use asset of \$83,000.

The net loss for the three months ended March 31, 2024 primarily related to noncash charges of \$30,881,000. Noncash charges include (i) depreciation of \$2,000; (ii) stock based compensation of \$269,000; (iii) net amortization of operating lease right of use asset of \$81,000; (iv) loss from change in warrant liability of \$6,847,000; (v) loss from change in earnout liability of \$21,485,000; (vi) loss from change in fair value of convertible note of \$2,039,000; and (vii) loss on note conversions of \$159,000.

Liquidity and Capital Resources as of March 31, 2025 and 2024

Liquidity is our ability to generate funds to support its current and future operations, satisfy its obligations, and otherwise operate on an ongoing basis. Significant factors in the management of liquidity are funds generated by operations, levels of accounts receivable and accounts payable and capital expenditures. We have incurred losses from operations in the past few years and had an accumulated deficit of \$8.8 million as of March 31, 2025. In September 2024, we closed an \$8 million public offering with approximately \$7.3 million in net proceeds. In December 2024, we received net proceeds of approximately \$7.4 million from the exercise of warrants related to an inducement offer agreement. We formally evaluated our liquidity and cash position in May 2025 when preparing the March 31, 2025 Form 10-Q consolidated financial statements. During this process, we analyzed our cash requirements and operations at least through May 2026 and determined that, based upon our current available cash and operations, we have no substantial doubt about our ability to continue as a going concern. Our assessment of the period of time through which our financial resources will be adequate to support our operations is a forward-looking statement and involves risks and uncertainties. Our actual results could vary as a result of our near and long-term future capital requirements that will depend on many factors.

Operating Activities

Net cash used in operating activities for the three months ended March 31, 2025 was \$2,098,000. This amount was primarily related to (i) net income of \$23,708,000; and offset by (ii) net working capital reductions of \$973,000 (including a \$713,000 reduction in deferred revenues); and (iii) noncash items of \$24,833,000. Noncash items included (iv) gain from change in warrant liability of \$15,521,000; and (v) gain from change in earnout liability of \$9,823,000; and offset by (vi) stock based compensation of \$428,000; and (vii) net amortization of operating lease right of use asset of \$83,000.

Net cash used in operating activities for the three months ended March 31, 2024 was \$1,695,000. This amount was primarily related to (i) net loss of \$31,964,000; and (ii) net working capital reductions of \$611,000; offset by (iii) noncash charges of \$30,881,000. Noncash charges include (iv) depreciation of \$2,000; (v) stock based compensation of \$269,000; (vi) net amortization of operating lease right of use asset of \$81,000; (vii) loss from change in warrant liability of \$6,847,000; (viii) loss from change in earnout liability of \$21,485,000; (ix) loss from change in fair value of convertible note of \$2,039,000; and (x) loss on note conversions of \$159,000.

Financing Activities

Net cash used in financing activities for the three months ended March 31, 2025 was \$497,000 and consisted of (i) repayment of advances by founders of \$600,000; and offset by (ii) net proceeds from exercise of warrants of \$60,000; and (iii) proceeds from stock option exercises of \$43,000.

Net cash provided by financing activities for the three months ended March 31, 2024 was \$293,000 and consisted proceeds from warrant exercise.

Contractual Obligations and Commitments

Contractual Cash Obligations	Total	Less Than 1 Year	1-3 Years	4-5 Years
Operating lease cash payments	\$ 1,281,638	\$ 471,901	\$ 486,075	\$ 323,661

On July 13, 2023, we entered into a lease in Redmond, WA for 15,567 square feet of office and warehouse space which started October 1, 2023. The monthly payment is \$25,000 per month. The lease expires October 31, 2027 and the monthly payment increases 3% on July 31, 2024 and each year thereafter. There is a one three year option to extend the lease based on the fair market rate on October 31, 2027, which we expect to exercise.

On February 29, 2024, we extended an office lease in Moorestown, North Carolina. We leased 3,621 square feet and the net monthly payment is \$6,488. On August 27, 2024, we extended the lease, which expired on February 28, 2025.

On February 1, 2025, we entered into an office lease in Mooresville, North Carolina. We lease 5,240 square feet and the net monthly payment is \$9,105. The lease expires January 31, 2028 and the monthly payment increases 3% on February 1, 2026 and each year thereafter. There is no option to extend the lease.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements (as that term is defined in Item 303 of Regulation S-K) that are reasonably likely to have a current or future material effect on our financial condition, revenue or expenses, results of operations, liquidity, capital expenditures or capital resources.

Critical Accounting Policies and Estimates

Our consolidated financial statements have been prepared in accordance with U.S. GAAP. The preparation of these consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, expenses, and related disclosures. We base our estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances. We evaluate our estimates and assumptions on an ongoing basis. Actual results could differ materially from those estimates due to risks and uncertainties, including uncertainty in the current economic environment. To the extent that there are material differences between these estimates and our actual results, our future consolidated financial statements will be affected.

We believe that the significant accounting policies described in "Note 2, Summary of Significant Accounting Policies" to our audited consolidated financial statements are accurate and complete. The critical accounting estimates and policies during the three months ended March 31, 2025 have not materially changed to those discussed in our Annual Report on Form 10-K for the year ended December 31, 2024.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Not applicable to smaller reporting companies.

ITEM 4. CONTROLS AND PROCEDURES.

a) Evaluation of Disclosure Controls and Procedures

We conducted an evaluation, under the supervision and with the participation of our management, of the effectiveness of the design and operation of our disclosure controls and procedures. The term “disclosure controls and procedures,” as defined in Rules 13a-15(e) and 15d-15(e) under the Securities and Exchange Act of 1934, as amended (“Exchange Act”), means controls and other procedures of a company that are designed to ensure that information required to be disclosed by the company in the reports it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission’s rules and forms. Disclosure controls and procedures also include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company’s management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate, to allow timely decisions regarding required disclosure. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of March 31, 2025, our disclosure controls and procedures are effective at the reasonable assurance level.

b) Inherent Limitations on Internal controls

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate. A control system, no matter how well designed and operated can provide only reasonable, but not absolute, assurance that the control system’s objectives will be met. The design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their cost.

c) Changes in Internal Control over Financial Reporting

During the three months ended March 31, 2025, there were no other changes in our internal controls over financial reporting, which were identified in connection with our management’s evaluation required by paragraph (d) of rules 13a-15 and 15d-15 under the Exchange Act, that materially affected, or is reasonably likely to have a material effect on our internal control over financial reporting.

PART II

ITEM 1. LEGAL PROCEEDINGS.

From time to time, we may become involved in actions, claims, litigation, and other legal proceedings occurring in the ordinary course of its business from time to time, including assertions by third parties relating to intellectual property infringement, contract or warranty breaches, or employment-related matters. We are not currently a party to any actions, claims, suits, or other legal procedures whose conclusion, if not determined in our favor, would have a major adverse effect on our business, financial condition, or results of operations, either individually or in the aggregate.

ITEM 1A. RISK FACTORS.

We are a smaller reporting company as defined by Rule 12b-2 of the Securities Exchange Act of 1934 and are not required to provide the information under this item. Our market risks are similar to those disclosed under the caption “Risk Factors” in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2024, and our other filings with the SEC.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

During the three months ended March 31, 2025, we issued no unregistered equity securities:

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

None.

ITEM 5. OTHER INFORMATION.

None.

ITEM 6. EXHIBITS.

Exhibit No.	Description
10.1	Master Loan Agreement dated September 27, 2024 by and between Airship AI Holdings, Inc. and Victor Huang (attached herewith)
10.2	Employment Agreement dated March 4, 2025 by between Airship AI Holdings, Inc. and Paul Allen (attached herewith)
31.1	Certification of Principal Executive Officer pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Principal Financial Officer pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Principal Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Principal Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	Inline XBRL Instance Document (the instance document does not appear in the Interactive Data File because iXBRL tags are embedded within the Inline XBRL document).
101.SCH	Inline XBRL Taxonomy Extension Schema Document.
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB	Inline XBRL Taxonomy Extension Labels Linkbase Document.
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase Document.
104	The Cover Page Interactive Data File, formatted in Inline XBRL (included within the Exhibit 101 attachments).

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: May 15, 2025

Airship AI Holdings, Inc.

/s/ Victor Huang

Name: Victor Huang

Title: Chief Executive Officer

(Principal Executive Officer)

/s/ Mark E. Scott

Name: Mark E. Scott

Title: Chief Financial Officer

(Principal Financial and Accounting Officer)

**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO
EXCHANGE ACT RULES 13a-14(a) and 15d-14(a),
AS ADOPTED PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Victor Huang, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Airship AI Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 15, 2025

/s/ Victor Huang

Victor Huang
Chief Executive Officer
(Principal Executive Officer)

**CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO
EXCHANGE ACT RULES 13a-14(a) and 15d-14(a),
AS ADOPTED PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Mark E. Scott, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Airship AI Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 15, 2025

/s/ Mark E. Scott
Mark E. Scott
Chief Financial Officer
(Principal Financial and Accounting Officer)

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED
PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with Quarterly Report of Airship AI Holdings, Inc. (the "Company") on Form 10-Q for the quarterly period ended March 31, 2025 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned Victor Huang, Chief Executive Officer (Principal Executive Officer) of the Company, certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 15, 2025

/s/ Victor Huang

Victor Huang
Chief Executive Officer
(Principal Executive Officer)

A signed original of this written statement required by Section 906 has been provided to Airship AI Holdings, Inc. and will be retained by Airship AI Holdings, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.

The forgoing certification is being furnished to the Securities and Exchange Commission pursuant to § 18 U.S.C. Section 1350. It is not being filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and is not to be incorporated by reference into any filing of the Company, whether made before or after the date hereof, regardless of any general incorporation language in such filing.

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED
PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with Quarterly Report of Airship AI Holdings, Inc. (the "Company") on Form 10-Q for the quarterly period ended March 31, 2025 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned Mark E. Scott, Chief Financial Officer (Principal Financial and Accounting Officer) of the Company, certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 15, 2025

/s/ Mark E. Scott

Mark E. Scott
Chief Financial Officer
(Principal Financial and Accounting Officer)

A signed original of this written statement required by Section 906 has been provided to Airship AI Holdings, Inc. and will be retained by Airship AI Holdings, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.

The forgoing certification is being furnished to the Securities and Exchange Commission pursuant to § 18 U.S.C. Section 1350. It is not being filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and is not to be incorporated by reference into any filing of the Company, whether made before or after the date hereof, regardless of any general incorporation language in such filing.