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 January 31, 2022

or

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

For the transition period from ___________ to ___________

Commission File Number: 000-31587

Red Cat Holdings, Inc.
(Exact name of Registrant as specified in its charter)

Nevada (State or other jurisdiction of incorporation or organization)	86-0490034 (I.R.S. Employer Identification Number)
370 Harbour Drive Humacao, Puerto Rico (Address of principal executive offices)	00791 (Zip Code)

(833) 373-3228
(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:

Title of Each Class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock	RCAT	Nasdaq Capital Market

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, smaller reporting company, or an emerging growth company. See definition of "large accelerated filer", "accelerated filer" and "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 March 15, 2022, there were53,671,559 shares of the registrant's common stock outstanding.

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RED CAT HOLDINGS
Consolidated Balance Sheets
(Unaudited)

	January 31, 2022	April 30, 2021
ASSETS		
Current Assets		
Cash	$ 7,111,527	$ 277,347
Marketable securities	48,446,302	—
Accounts receivable, net	891,505	321,693
Inventory	2,339,680	362,072
Other	2,234,583	678,898
Due from related party	225,539	—
Total Current Assets	61,249,136	1,640,010
Goodwill	26,029,750	8,017,333
Intangible assets, net	1,983,192	2,032,169
Property and equipment, net	262,859	—
Other	35,907	3,853
Operating lease right-of-use assets	823,838	—
Total Long Term Assets	29,135,546	10,053,355
TOTAL ASSETS	**90,384,682**	**11,693,365**
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities		
Accounts payable	521,139	541,903
Accrued expenses	1,493,691	614,050
Debt obligations - short term	1,127,596	269,045
Due to related party	41,622	390,209
Customer deposits	336,621	46,096
Operating lease liabilities	261,369	—
Warrant derivative liability	1,350,099	2,812,767
Total Current Liabilities	5,132,137	4,674,070
Operating lease liabilities	573,165	—
Debt obligations - long term	1,339,132	—
Note payable to related party	—	1,753,000
Total Long Term Liabilities	1,912,297	1,753,000
Commitments and contingencies		
Stockholders' Equity		
Series A Preferred Stock - shares authorized 2,200,000; outstanding 0 and 158,704	—	1,587
Series B Preferred Stock - shares authorized 4,300,000; outstanding 986,676 and 1,968,676	9,867	19,687
Common stock - shares authorized 500,000,000; outstanding 53,637,971 and 29,431,264	53,638	29,431
Additional paid-in capital	105,947,703	21,025,518
Accumulated deficit	(22,673,118)	(15,809,928)

Accumulated other comprehensive income	2,158	—
Total Stockholders' Equity	83,340,248	5,266,295
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	**90,384,682**	**11,693,365**

See accompanying notes.

RED CAT HOLDINGS
Consolidated Statements Of Operations
(Unaudited)

	Three months ended January 31,		Nine months ended January 31,	
	2022	**2021**	**2022**	**2021**
Revenues	$ 1,856,751	$ 2,145,988	$ 5,116,741	$ 3,122,077
Cost of goods sold	1,516,970	1,576,265	4,521,974	2,351,153
Gross Margin	339,781	569,723	594,767	770,924
Operating Expenses				
Operations	334,278	146,539	794,390	353,295
Research and development	811,288	167,968	1,548,983	341,892
Sales and marketing	238,624	48,719	524,642	97,534
General and administrative	1,337,183	499,155	3,264,071	929,874
Stock based compensation	782,123	854,195	2,066,146	1,068,317
Total operating expenses	3,503,496	1,716,576	8,198,232	2,790,912
Operating loss	(3,163,715)	(1,146,853)	(7,603,465)	(2,019,988)
Other Expense (Income)				
Derivative expense	—	4,481,701	—	4,630,288
Change in fair value of derivative liability	(1,026,466)	3,350,135	(1,299,527)	3,433,938
Investment income, net	363,760	—	402,207	—
Interest expense	46,596	—	109,712	—
Other, net	17,212	5,571	47,333	5,571
Other Expense (Income)	**$ (598,898)**	**$ 7,837,407**	**$ (740,275)**	**$ 8,069,797**
Net loss	**$ (2,564,817)**	**$ (8,984,260)**	**$ (6,863,190)**	**$ (10,089,785)**
Loss per share - basic and diluted	**$ (0.05)**	**$ (0.34)**	**$ (0.15)**	**$ (0.46)**
Weighted average shares outstanding - basic and diluted	**53,592,927**	**26,232,755**	**46,604,898**	**22,161,745**

RED CAT HOLDINGS
Condensed Consolidated Cash Flows Statements
(Unaudited)

	Nine months ended January 31,	
	2022	**2021**
Cash Flows from Operating Activities		
Net loss	$ (6,863,190)	$ (10,089,785)
Stock based compensation	2,066,146	1,068,317
Common stock issued for services	250,400	—
Amortization of intangible assets	48,978	5,571
Depreciation	17,888	—
Change in fair value of derivative	(1,299,527)	3,433,938
Amortization of debt discount	—	79,187
Derivative expense	—	4,630,288
Adjustments to reconcile net loss to net cash from operations:		
Changes in operating assets and liabilities, net of acquisitions		
Accounts receivable	(470,765)	(63,255)
Inventory	(673,297)	(405,987)
Other	(3,492,145)	(118,613)
Operating lease right-of-use assets and liabilities	10,696	—
Customer deposits	227,532	32,967
Accounts payable	(1,673,545)	345,227
Accrued expenses	(190,444)	165,129
Net cash used in operating activities	(12,041,273)	(917,016)
Cash Flows from Investing Activities		
Cash acquired through acquisitions	24,866	—
Payment for acquisition, net of cash acquired	—	(48,368)
Purchases of property and equipment	(92,581)	—
Proceeds from sale of marketable securities	6,250,322	—
Purchases of marketable securities	(54,696,624)	—
Net cash used in investing activities	(48,514,017)	(48,368)
Cash Flows from Financing Activities		

Proceeds from exercise of warrants	99,999	—
Proceeds from related party obligations	—	79,000
Payments under related party obligations	(1,969,193)	(17,140)
Proceeds from debt obligations	—	424,419
Payments under debt obligations	(694,738)	(365,911)
Proceeds from convertible debentures	—	1,080,000
Payments of taxes related to restricted stock vesting	(113,959)	—
Proceeds from issuance of common stock, net	70,065,203	—
Net cash provided by financing activities	67,387,312	1,200,368
Effect of foreign exchange rate changes on cash	2,158	—
Net increase in Cash	6,834,180	234,984
Cash, beginning of period	277,347	236,668
Cash, end of period	**7,111,527**	**471,652**
Cash paid for interest	27,563	—
Cash paid for income taxes	—	—
Non-cash transactions		
Fair value of shares issued in acquisitions	$ 12,727,292	$ 6,351,076
Taxes related to net shares settlement of equity awards	$ 522,628	$ —
Conversion of derivative liability	$ 163,141	$ —
Financed purchases of property and equipment	$ 144,383	$ —
Indirect payment to related party	$ 132,200	$ —
Conversion of preferred stock into common stock	$ 11,407	$ —
Shares withheld as payment of note receivable	$ 5,100	$ —
Issuance of Note Payable - Related Party in acquisition	$ —	$ 1,753,000
Conversion of Notes into common stock	$ —	$ 450,000
Conversion of accrued interest into common stock	$ —	$ 45,024

See accompanying notes.

RED CAT HOLDINGS
Consolidated Stockholders' Equity Statements
(Unaudited)

	Series A Preferred Stock		Series B Preferred Stock		Common Stock		Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total Equity
	Shares	Amount	Shares	Amount	Shares	Amount				
Balances, April 30, 2020	**208,704**	**$ 2,087**	**3,681,623**	**$ 36,816**	**20,011,091**	**$ 20,011**	**$ 4,043,837**	**$ (2,573,753)**	**$ —**	**$ 1,528,998**
Stock based compensation							107,061			107,061
Net Loss		—		—		—	—	(383,244)	—	(383,244)
Balances, July 31, 2020	**208,704**	**$ 2,087**	**3,681,623**	**$ 36,816**	**20,011,091**	**$ 20,011**	**$ 4,150,898**	**$ (2,956,997)**	**$ —**	**$ 1,252,815**
Conversion of debt					710,444	711	494,314			495,025
Stock based compensation							107,061			107,061
Net loss		—		—		—	—	(722,281)	—	(722,281)
Balances, October 31, 2020	**208,704**	**$ 2,087**	**3,681,623**	**$ 36,816**	**20,721,535**	**$ 20,722**	**$ 4,752,273**	**$ (3,679,278)**	**$ —**	**$ 1,132,620**
Acquisition of Fat Shark					5,227,273	5,227	6,345,849			6,351,076
Conversion of preferred stock	(50,000)	(500)	(954,741)	(9,547)	1,212,118	1,212	8,835			—
Stock based compensation							854,195			854,195
Net loss		—		—		—	—	(8,984,260)	—	(8,984,260)
Balances, January 31, 2021	**158,704**	**$ 1,587**	**2,726,882**	**$ 27,269**	**27,160,926**	**$ 27,161**	**$ 11,961,152**	**$ (12,663,538)**	**$ —**	**$ (646,369)**
Balances, April 30, 2021	**158,704**	**$ 1,587**	**1,968,676**	**$ 19,687**	**29,431,264**	**$ 29,431**	**$ 21,025,518**	**$ (15,809,928)**	**$ —**	**$ 5,266,295**
Acquisition of Skypersonic					685,321	685	2,630,955			2,631,640
Public offerings, net of $5,959,800 of issuance costs					17,333,334	17,333	70,022,871			70,040,204
Exercise of warrants					66,666	67	263,073			263,140
Conversion of preferred stock			(982,000)	(9,820)	818,333	818	9,002			—
Stock based compensation					62,500	63	384,023			384,086
Shares issued for services					91,667	92	191,908			192,000
Currency translation adjustments									922	922
Net loss		—		—		—	—	(1,557,772)	—	(1,557,772)
Balances, July 31, 2021	**158,704**	**$ 1,587**	**986,676**	**$ 9,867**	**48,489,085**	**$ 48,489**	**$ 94,527,350**	**$ (17,367,700)**	**$ 922**	**$ 77,220,515**
Acquisition of Skypersonic					21,972	22	84,350			84,372
Acquisition of Teal Drones					3,588,272	3,588	10,007,691			10,011,279

Conversion of preferred stock	(158,704)	(1,587)			1,321,966	1,322	265			—
Stock based compensation					243,615	244	899,693			899,937
Shares issued for services					20,000	20	58,380			58,400
Currency translation adjustments									669	669
Net loss		—		—		—	—	(2,740,601)	—	(2,740,601)
Balances, October 31, 2021	—	$ —	986,676	$ 9,867	53,684,910	$ 53,685	$ 105,577,729	$ (20,108,301)	$ 1,591	$ 85,534,571
Stock based compensation					(46,939)	(47)	369,974			369,927
Currency translation adjustments									567	567
Net loss		—		—		—	—	(2,564,817)	—	(2,564,817)
Balances, January 31, 2022	—	$ —	986,676	$ 9,867	53,637,971	$ 53,638	$ 105,947,703	$ (22,673,118)	$ 2,158	$ 83,340,248

RED CAT HOLDINGS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
January 31, 2022 and 2021
(unaudited)

Our unaudited interim condensed consolidated financial statements and accompanying notes are prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP"). In the opinion of management, the unaudited interim condensed consolidated financial statements reflect all adjustments of a normal recurring nature that are necessary for a fair presentation of the results for the interim periods presented. Interim results are not necessarily indicative of results for a full year. The information included in this Form 10-Q should be read in conjunction with the financial information included in the Annual Report on Form 10-K for the fiscal year ended April 30, 2021 of Red Cat Holdings, Inc. (the "Company"), filed with the Securities and Exchange Commission ("SEC") on August 12, 2021.

Note 1 - The Business

Red Cat Holdings ("Red Cat" or the "Company") was originally incorporated in February 1984. Since April 2016, the Company's primary business has been to provide products, services and solutions to the drone industry which it presently does through its four wholly owned subsidiaries. Teal Drones is a leader in commercial and government Unmanned Aerial Vehicles (UAV) technology. Fat Shark Holdings is a provider of First Person View (FPV) video goggles. Rotor Riot sells FPV drones and equipment, primarily to the consumer marketplace. Skypersonic provides software and hardware solutions that enable drones to complete inspection services in locations where GPS (global positioning systems) are not available, yet still record and transmit data even while being operated from thousands of miles away.

Corporate developments since January 1, 2020 include:

A. <u>Rotor Riot Acquisition</u>

In January 2020, the Company consummated a Merger Agreement under which Rotor Riot Acquisition Corp, a wholly owned subsidiary of the Company, merged with and into Rotor Riot, with Rotor Riot continuing as the surviving entity and a wholly owned subsidiary of the Company. Under the Merger Agreement, each member of Rotor Riot received its pro rata portion of the total number of shares of the Company's common stock issued based on (A)(i) $3,700,000 minus (ii) $915,563 (which included certain debt and other obligations of Rotor Riot and its Chief Executive Officer that the Company agreed to assume (the "Assumed Obligations") divided by (B) the volume weighted average price ("VWAP") of the Company's common stock for the twenty trading days prior to the closing of the Merger. Based on a share issuance value of $2,784,437 and a VWAP of $1.25445, the Company issued an aggregate of 2,219,650 shares of common stock to the members of Rotor Riot.

Following the closing, the Company's management controlled the operating decisions of the combined company. Accordingly, we accounted for the transaction as an acquisition of Rotor Riot by the Company. Based on purchase price accounting, we recognized the assets and liabilities of Rotor Riot at fair value with the excess of the purchase price over the net assets acquired recognized as goodwill. The table below reflects the acquisition date values of the purchase consideration, assets acquired, and liabilities assumed. The shares issued were valued at $1,820,114 (2,219,650 shares issued times $0.82 per share which equaled the closing price of the Company's common stock on the date that the merger agreement was consummated). A summary of the purchase price and its related allocation is as follows:

Shares issued	$	1,820,114
Promissory note issued		175,000
Total Purchase Price	**$**	**1,995,114**
Assets acquired		
Cash		21,623
Accounts receivable		28,500
Other assets		3,853
Inventory		127,411
Trademark		20,000
Brand name		578,000
Customer relationships		39,000
Total assets acquired		**818,387**
Liabilities assumed		
Accounts payable and accrued expenses		171,651
Notes payable		209,799
Due to related party		197,846
Total liabilities assumed		**579,296**
Total fair value of net assets acquired		**239,091**
Goodwill	**$**	**1,756,023**

The final purchase price allocation was determined by an independent valuation services firm. Customer Relationships with a value of $39,000 are being amortized over 7 years. The carrying value of Brand Name is not being amortized but will be reviewed quarterly and formally evaluated at the end of each fiscal year.

B. Fat Shark Acquisition

In November 2020, the Company closed a share purchase agreement ("Share Purchase Agreement") with the sole shareholder of Fat Shark Holdings ("Fat Shark"), to acquire all of the issued and outstanding shares of Fat Shark and its subsidiaries. The transaction was valued at $8,354,076 based on (i) the issuance of 5,227,273 shares of common stock with a value of $6,351,076 on the date of closing (ii) a senior secured promissory note in the original principal amount of $1,753,000, and (iii) a cash payment of $250,000. The Share Purchase Agreement includes indemnification provisions, a two year non-compete agreement, and registration rights for the shares issued in the transaction. A summary of the purchase price and its related allocation is as follows:

Shares issued	$	6,351,076
Promissory note issued		1,753,000
Cash		250,000
Total Purchase Price	**$**	**8,354,076**
Assets acquired		
Cash		201,632
Accounts receivable		249,159
Other assets		384,232
Inventory		223,380
Brand name		1,144,000
Proprietary technology		272,000
Non-compete agreement		16,000
Total assets acquired		**2,490,403**
Liabilities assumed		
Accounts payable and accrued expenses		279,393
Customer deposits		25,194
Total liabilities assumed		**304,587**
Total fair value of net assets acquired		**2,185,816**
Goodwill	**$**	**6,168,260**

The final purchase price allocation was determined by an independent valuation services firm. Intangible assets included proprietary technology and non-compete agreement which are being amortized over 5 and 3 years, respectively. The carrying value of Brand Name is not being amortized but will be reviewed quarterly and formally evaluated at the end of each fiscal year.

C. Skypersonic Acquisition

In February 2021, the Company entered into Share Purchase and Liquidity Event Agreements (the "Skypersonic Agreements") with the founder and majority shareholder of Skypersonic, Inc., ("Skypersonic") and the holders of common stock and equity based agreements representing 97.46% of Skypersonic (the "Sellers"), pursuant to which, subject to the satisfaction of certain closing conditions, the Company would acquire all of the issued and outstanding share capital of Skypersonic for an aggregate of $3,000,000 in shares (the "Share Consideration") of the Company's common stock, based upon the VWAP of the Company's common stock at closing of the transaction (the "Skypersonic Transaction"). Prior to the closing, the Company provided $75,000 to fund operating costs of Skypersonic. This amount was capitalized as part of the purchase price. The transaction closed on May 7, 2021 and was paid through the issuance of 857,124 shares of common stock which had a fair market value of $3,291,356. Fifty (50%) percent of the Share Consideration (the "Escrow Shares") was deposited in an escrow account as security for indemnification obligations and any purchase price adjustments due to working capital deficiencies and any other claims or expenses. Under the Skypersonic Agreements, closing date working capital deficits in excess of $300,000 resulted in a reduction of the Share Consideration on a dollar of dollar basis. In October 2021, the Company and Skypersonic agreed to a reduction in the purchase price of $601,622 which resulted in the cancellation of 149,829 shares held in escrow. A revised summary of the purchase price and its related allocation is as follows:

Shares issued	$	2,716,013
Cash		75,000
Total Purchase Price	**$**	**2,791,013**
Assets acquired		
Cash		13,502
Accounts receivable		51,083
Other assets		12,950
Inventory		50,556
Total assets acquired		**128,091**
Liabilities assumed		
Accounts payable and accrued expenses		1,054,997
Total liabilities assumed		**1,054,997**
Total fair value of net assets acquired		**(926,906)**
Goodwill	**$**	**3,717,919**

The foregoing amounts reflect our current estimates of fair value as of the May 7, 2021 acquisition date. The Company has engaged an independent valuation services firm to complete a formal evaluation of the acquisition. The Company expects to recognize fair values associated with the customer relationships acquired, as well as the Skypersonic brand name. When the valuation project is completed, the Company may make adjustments to the opening balance sheet. The determination of the fair values of the acquired assets and liabilities assumed (and the related determination of estimated lives of depreciable tangible and intangible assets) requires significant judgment.

D. Teal Drones Acquisition

On August 31, 2021, the Company closed the acquisition of Teal Drones Inc., ("Teal") pursuant to an Agreement and Plan of Merger by and among, the Company Teal Acquisition I Corp., ("Acquisition") and wholly-owned subsidiary of the Company, and Teal, (the "Merger Agreement" or "Merger").

Pursuant to the Merger Agreement, we acquired all of the issued and outstanding share capital of Teal in exchange for $14,000,000 of our common stock ("Common Stock") at the Volume Weighted Average Price (VWAP) of our Common Stock for the 20 trading days ended August 31, 2021 of $2.908 per share, reduced by the amount of Teal debt assumed consisting of approximately $1.67 million payable to DA4, and approximately $1,457,000 in working capital deficit, for a net closing date payment of $10,872,753. At closing, we issued 3,738,911 shares of Common Stock (the "Stock Consideration") with a fair market value of $10,431,562. Fifteen (15%) of the Share Consideration (the "Escrow Shares") was deposited in an escrow account for a period of eighteen (18) months as security for indemnification obligations, any purchase price adjustments due to working capital deficiencies and any other claims or expenses. In December 2021, the Company and Teal agreed to a reduction in the purchase price of $438,058 which resulted in the cancellation of 150,639 shares held in escrow. The fair market value of the cancelled shares was $420,283. The Stock Consideration may be increased if Teal attains certain revenue levels in the twenty four (24) month period following the closing. The additional consideration begins at $4 million if sales total at least $18 million and ends at $16 million if sales total $36 million.

A revised summary of the purchase price and its related allocation is set forth below.

Total Purchase Price - shares issued	**$**	**10,011,279**
Assets acquired		
Cash		11,364
Accounts receivable		47,964
Other current assets		15,085
Other assets		48,595
Inventory		1,253,755
Total assets acquired		**1,376,763**
Liabilities assumed		
Accounts payable and accrued expenses		1,143,899
Customer deposits		1,766,993
Notes payable		2,749,091
Total liabilities assumed		**5,659,983**
Total fair value of net assets acquired		**(4,283,220)**
Goodwill	**$**	**14,294,499**

The foregoing amounts reflect our current estimates of fair value as of the August 31, 2021 acquisition date. The Company has engaged an independent valuation services firm to complete a formal evaluation of the acquisition. The Company expects to recognize fair values associated with the customer relationships acquired, as well as the Teal brand name but has not yet accumulated sufficient information to assign such values. When the valuation project is completed, the Company may make adjustments to the opening balance. The determination of the fair values of the acquired assets and liabilities assumed (and the related determination of estimated lives of depreciable tangible and intangible assets) requires significant judgment.

On August 31, 2021, Teal entered into an Amended and Restated Loan and Security Agreement with Decathlon Alpha IV, L.P. ("DA4") (the "Loan Agreement") in the amount of $1,670,294 (the "Loan"), representing the outstanding principal amount previously due and owing by Teal to DA4. Interest on the Loan accrues at a rate of ten (10%) percent per annum. Principal and interest under the term Loan is payable monthly in an amount equal to $49,275 until maturity on December 31, 2024. The Company assumed the Loan Agreement in connection with the acquisition.

Note 2 - Summary of Significant Accounting Policies

Basis of Accounting - The financial statements and accompanying notes are prepared in accordance with generally accepted accounting principles ("GAAP").

Principles of Consolidation - Our condensed consolidated financial statements include the accounts of our operating subsidiaries, Teal Drones, Fat Sharking Holdings, Rotor Riot, and Skypersonic. Intercompany transactions and balances have been eliminated.

Use of Estimates - The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates reflected in these financial statements include those used to (i) determine stock based compensation, (ii) complete purchase price accounting for acquisitions, and (iii) accounting for derivatives.

Cash and Cash Equivalents - At January 31, 2022, we had cash of $7,111,527 in multiple commercial banks and financial services companies. We have not experienced any loss on these accounts and believe they are not exposed to any significant credit risk.

Marketable Securities – Our marketable securities have been classified and accounted for as available-for-sale securities. Our investment manager can sell any of our investment holdings at any time, and therefore, we have classified our marketable securities as short term. Our available-for-sale securities are carried at fair value, with unrealized gains and losses reported within investment income in our consolidated statements of operations.

We have elected to present accrued interest receivable separately from marketable securities on our consolidated balance sheets. Accrued interest receivable was $393,543 as of January 31, 2022 and was included in other current assets. We did not write off any accrued interest receivable during the three months ended January 31, 2022.

Accounts Receivable, net - Accounts receivable are recorded at the invoiced amount less allowances for doubtful accounts. The Company's estimate of the allowance for doubtful accounts is based on a multitude of factors, including historical bad debt levels for its customer base, past experience with a specific customer, the economic environment, and other factors. Accounts receivable balances are written off against the allowance when it is probable that the receivable will not be collected.

Inventories – Inventories, which consist of raw materials, work-in-process, and finished goods, are stated at the lower of cost or net realizable value, with cost being determined by the average-cost method, which approximates the first-in, first-out method. Cost components include direct materials and direct labor, as well as in-bound freight. At each balance sheet date, the Company evaluates ending inventories for excess quantities and obsolescence.

Goodwill - Goodwill represents the excess of the purchase price of an acquisition over the estimated fair value of identifiable net assets acquired. The measurement periods for the valuation of assets acquired and liabilities assumed ends as soon as information on the facts and circumstances that existed as of the acquisition date becomes known, not to exceed 12 months. Adjustments in a purchase price allocation may require a change in the amounts allocated to goodwill during the periods in which the adjustments are determined.

We perform an impairment test at the end of each fiscal year, or more frequently if indications of impairment arise. We have a single reporting unit, and consequently, evaluate goodwill for impairment based on an evaluation of the fair value of the Company as a whole.

Leases - Effective August 1, 2021, the Company adopted Accounting Standards Codification (ASC) 842 titled "Leases" which requires the recognition of assets and liabilities associated with lease agreements. The Company adopted ASC 842 on a modified retrospective transition basis which means that it will not restate financial information for any periods prior to August 1, 2021. Upon adoption, the Company recognized a lease liability obligation of $796,976 and a right-of-use asset for the same amount.

The Company determines if a contract is a lease or contains a lease at inception. Operating lease liabilities are measured, on each reporting date, based on the present value of the future minimum lease payments over the remaining lease term. The Company's leases do not provide an implicit rate. Therefore, the Company uses an effective discount rate of 12% based on its recent debt financings. Operating lease assets are measured by adjusting the lease liability for lease incentives, initial direct costs incurred and asset impairments. Lease expense for minimum lease payments is recognized on a straight line basis over the lease term with the operating lease asset reduced by the amount of the expense. Lease terms may include options to extend or terminate a lease when they are reasonably certain to occur.

Fair Values, Inputs and Valuation Techniques for Financial Assets and Liabilities and Related Disclosures

The fair value measurements and disclosure guidance defines fair value and establishes a framework for measuring fair value. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In accordance with this guidance, the Company has categorized its recurring basis financial assets and liabilities into a three-level fair value hierarchy based on the priority of the inputs to the valuation technique.

The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls has been determined based on the lowest level input that is significant to the fair value measurement in its entirety. The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability.

We disclose and recognize the fair value of our assets and liabilities using a hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in an orderly transaction between market participants at the measurement date. The guidance establishes three levels of the fair value hierarchy as follows:

Level 1: Inputs are unadjusted, quoted prices in active markets for identical assets or liabilities at the measurement date;

Level 2: Inputs are observable, unadjusted quoted prices in active markets for similar assets or liabilities, unadjusted quoted prices for identical or similar assets or liabilities in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the related assets or liabilities; and

Level 3: Unobservable inputs that are significant to the measurement of the fair value of the assets or liabilities that are supported by little or no market data.

Disclosures for Non-Financial Assets Measured at Fair Value on a Non-Recurring Basis

The Company's financial instruments mainly consist of cash, receivables, current assets, accounts payable and accrued expenses and debt. The carrying amounts of its cash, receivables, current assets, accounts payable, accrued expenses and current debt approximates fair value due to the short-term nature of these instruments.

Convertible Securities and Derivatives

When the Company issues convertible debt or equity instruments that contain embedded derivative instruments that are to be bifurcated and accounted for as liabilities, the total proceeds from the convertible host instruments are first allocated to the bifurcated derivative instruments. The remaining proceeds, if any, are then allocated to the convertible instruments themselves, resulting in those instruments being recorded at a discount from their face value but no lower than zero. Any excess amount is recognized as a derivative expense.

Derivative Liabilities

The Company has financial instruments that are considered derivatives or contain embedded features subject to derivative accounting. Embedded derivatives are valued separately from the host instrument and are recognized as derivative liabilities in the Company's balance sheet. The Company measures these instruments at their estimated fair value and recognizes changes in their estimated fair value in results of operations during the period of change.

In October 2020 and January 2021, the Company entered into convertible note agreements which included provisions under which the conversion price was equal to the lesser of an initial stated amount or the conversion price of a future offering. This variable conversion feature was recognized as a derivative. Both financings included the issuance of warrants which contained similar variable conversion features. The Company values these convertible notes and warrants using the multinomial lattice method that values the derivative liability within the notes based on a probability weighted discounted cash flow model. The resulting liability is valued at each reporting date and the change in the liability is reflected as change in derivative liability in the statement of operations.

Revenue Recognition - The Company recognizes revenue in accordance with ASC 606, "Revenue from Contracts with Customers", issued by the Financial Accounting Standards Board ("FASB"). This standard includes a comprehensive evaluation of factors to be considered regarding revenue recognition including (i) identifying the promised goods, (ii) evaluating performance obligations, (iii) measuring the transaction price, (iv) allocating the transaction price to the performance obligations if there are multiple components, and (v) recognizing revenue as each obligation is satisfied. The Company's revenue transactions include a single component, specifically, the shipment of goods to customers as orders are fulfilled. Most customers pay at the time they order and the Company recognizes revenue upon shipment. The timing of the shipment of orders can vary considerably depending upon whether an order is for an item normally maintained in inventory or an order that requires assembly or unique parts. Customer deposits totaled $336,621 and $46,096 at January 31, 2022 and April 30, 2021, respectively.

Research and Development - Research and development expenses include payroll, employee benefits, and other headcount-related expenses associated with product development. Research and development expenses also include third-party development and programming costs, as well as a proportionate share of overhead costs such as rent. Costs related to software development are included in research and development expense until technological feasibility is reached, which for our software products, is generally shortly before the products are released to production. Once technological feasibility is reached, such costs are capitalized and amortized as a cost of revenue over the estimated lives of the products.

Income Taxes - Deferred taxes are provided on the liability method, whereby deferred tax assets are recognized for deductible temporary differences and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

Recent Accounting Pronouncements - Management does not believe that recently issued, but not yet effective accounting pronouncements, if adopted, would have a material effect on the accompanying condensed consolidated financial statements.

Foreign Currency - The functional currency of our international subsidiary is the local currency. For that subsidiary, we translate assets and liabilities to U.S. dollars using period-end exchange rates, and average monthly exchange rates for revenues, costs, and expenses. We record translation gains and losses in accumulated other comprehensive income as a component of stockholders' equity. Net foreign exchange transaction gains and losses resulting from the conversion of the transaction currency to functional currency are recorded in other income, net in the consolidated statements of operations.

Comprehensive Loss - During the three and nine months ended January 31, 2022, differences between net loss and comprehensive loss totaled $567 and $2,158, respectively, relating to foreign currency translation adjustments.

Stock-Based Compensation - We use the estimated grant-date fair value method of accounting in accordance with ASC Topic 718, Compensation - Stock Compensation. Fair value is determined using the Black-Scholes Model using inputs reflecting our estimates of expected volatility, term and future dividends. We recognize forfeitures as they occur. We recognize compensation costs on a straight line basis over the service period which is generally the vesting term.

Basic and Diluted Net Loss per Share - Basic and diluted net loss per share has been calculated by dividing net loss by the weighted average number of shares of common stock outstanding during the period. Common stock equivalents were excluded from the computation of diluted net loss per share of common stock because they were anti-dilutive. The exercise of these common stock equivalents would dilute earnings per share if we become profitable in the future.

Related Parties - Parties are considered to be related to us if they have control or significant influence, directly or indirectly, over us, including key management personnel and members of the Board of Directors. Related Party transactions are disclosed in Note 18.

Note 3 – Marketable Securities

The following tables set forth information related to our marketable securities as of January 31, 2022:

I. Amortized cost, net unrealized gains or losses, and fair values

	Amortized Cost	Net Unrealized Gains (Losses)	Fair Value
Money market funds	$ 1,598,428	$ 1,108	$ 1,599,536
Asset-backed securities	3,113,823	(21,984)	3,091,839
Corporate bonds	44,387,966	(633,039)	43,754,927
Total	$ 49,100,217	$ (653,915)	$ 48,446,302

II. Contractual Maturities

	One Year or Less	One to Five Years	Over Five Years	Total
Money market funds	$ 1,599,536	$ —	$ —	$ 1,599,536
Asset-backed securities	—	3,091,839	—	3,091,839
Corporate bonds	19,808,158	23,366,723	580,046	43,754,927
Total	$ 21,407,694	$ 26,458,562	$ 580,046	$ 48,446,302

III. Fair Value Hierarchy

	Level 1	Level 2	Level 3	Total
Money market funds	$ 1,599,536	$ —	$ —	$ 1,599,536
Asset-backed securities	—	3,091,839	—	3,091,839
Corporate bonds	—	43,754,927	—	43,754,927
Total	$ 1,599,536	$ 46,846,766	$ —	$ 48,446,302

Note 4 – Inventories

Inventories consisted of the following:

	January 2022	**April 2021**
Raw materials	$ 1,370,380	$ —
Work-in-process	39,153	—
Finished goods	930,147	362,072
Total	$ 2,339,680	$ 362,072

Inventory purchase commitments totaled $14,539,895 at January 31, 2022. The global supply chain for materials required to produce our drones is presently experiencing significant delays and disruptions. As a result, we have been required to significantly increase our order lead times for the components of our drones.

Note 5 - Other Current Assets

Other current assets included:

	January 2022	**April 2021**
Prepaid inventory	$ 1,539,479	$ 478,939
Accrued interest income	393,549	—
Prepaid insurance	140,182	—
Prepaid expenses	152,001	115,587
Security deposits	9,372	9,372
Due from related party	—	75,000
Total	$ 2,234,583	$ 678,898

Note 6 – Due From Related Party

In January 2022, the Company determined that an employee had relocated in 2021 but their compensation had not been subject to the required tax withholding by the new jurisdiction. The amount subject to taxation included $155,624 of cash compensation and $1,413,332 of income associated with the vesting of restricted stock ("Stock Compensation"). In March 2022, the Company entered into a note agreement (the "Note") with the employee in the amount of $510,323, representing the estimated taxes owed by the employee related to the Stock Compensation. Under the terms of the Note, 104,166 shares of common stock with a fair value of $280,832, which had vested during calendar 2021, were withheld by the Company and applied against the Note. The employee has agreed not to sell or transfer 110,983 shares of common stock held at the Company's transfer agent until the Note is repaid. In addition, the employee is scheduled to have 20,833 shares of restricted stock vest monthly in calendar 2022, of which 3,000 shares will be withheld with the fair value of those shares applied against the Note. Any shares issued to the employee in 2022 will be held at the transfer agent until the Note is repaid in full. The Note matures on December 31, 2022 and will be repaid by the employee assigning that number of shares, held at the transfer agent, with a fair value required to repay the Note in full. The Company accrued payroll taxes of $596,120 at January 31, 2022 representing $510,323 owed by the employee, $31,604 owed by the Company, and $54,193 of estimated penalties and interest. The note balance totaled $225,539 at January 31, 2022. The shares held at the transfer agent had a fair value of $206,684 at January 31, 2022. The Company filed amended payroll tax returns, which included a payment of $544,057, on March 16, 2022.

Note 7 – Property and Equipment

Property and equipment consist of assets with an estimated useful life greater than one year. Property and equipment are reported net of accumulated depreciation, and the reported values are periodically assessed for impairment. Property and equipment as of January 31, 2022 was as follows:

Original cost	$	423,588
Accumulated depreciation		160,729
Net carrying value	$	262,859

Note 8 – Operating Leases

The Company has the following operating leases for real estate locations where it operates:

Location		Monthly Rent	Expiration
South Salt Lake, Utah	$	22,000	December 2024
Orlando, Florida	$	4,600	May 2024
Cayman Islands	$	3,438	Month to Month
Troy, Michigan	$	2,667	May 2022
Orlando, Florida	$	1,690	September 2022

These lease agreements have remaining terms up to 2.92 years, excluding options to extend certain leases for up to 5 years. The weighted average remaining lease term as of January 31, 2022 was 2.86 years. The Company used a discount rate of 12% to calculate its lease liability at January 31, 2022. Future lease payment obligations at January 31, 2022 were as follows:

Fiscal Year Ended:		
2022	$	98,896
2023		336,257
2024		332,356
2025		230,653
Total	$	998,162

Note 9 – Debt Obligations

A. Decathlon Capital

In connection with the acquisition of Teal, Decathlon Capital agreed to restructure the terms of an existing loan agreement with Teal. Effective August 31, 2021, the principal amount outstanding of $1,670,294 bears interest at 10% annually and is repayable in monthly payments of $49,275 through its December 31, 2024 maturity date. The balance outstanding at January 31, 2022 totaled $1,483,383.

B. Convertible Note

In May 2021, Teal entered into a convertible note agreement totaling $350,000 with one of its equity investors. The note bears interest at the applicable Federal Rate which was approximately 0.13% on the date of issuance. The Company has assumed this obligation which is payable upon demand.

C. Vendor Settlement

In May 2020, Teal entered into a settlement agreement with a vendor that had been providing contract manufacturing services. At August 31, 2021, the Company assumed the outstanding balance of $387,500 which is payable in monthly installments of $37,500 with a final payment of $12,500 due in July 2022. The balance outstanding at January 31, 2022 totaled $200,000.

D. SBA Loan

On February 11, 2021, Teal received a Small Business Administration Paycheck Protection Program ("SBA PPP") loan in the amount of $300,910. The loan was unsecured, non-recourse, and accrued interest at one percent annually. The loan is forgivable if used to fund qualifying payroll, rent and utilities. The principal balance of $300,910 and accrued interest of $3,001 were forgiven on February 16, 2022.

E. Shopify Capital

Shopify Capital is an affiliate of Shopify, Inc. which provides sales software and services to the Company. The Company processes customer transactions ordered on the e-commerce site for Rotor Riot through Shopify. Shopify Capital has entered into multiple agreements with the Company in which it has "purchased receivables" at a discount. Shopify retains a portion of the Company's daily receipts until the purchased receivables have been paid. The Company recognizes the discount as a transaction fee, in full, in the month in which the agreement is executed. The Company assumed an existing agreement when it acquired Rotor Riot in January 2020. This agreement was repaid in May 2020. Since then, the Company has entered into the following agreements with Shopify:

Date of Transaction	Purchased Receivables	Payment to Company	Transaction Fees	Withholding Rate	Fully Repaid In

May 2020	$158,200	$140,000	$18,200	17%	October 2020
September 2020	$209,050	$185,000	$24,050	17%	May 2021
April 2021	$236,500	$215,000	$21,500	17%	January 2022

F. Corporate Equity

In October 2021, Teal entered into an agreement with Corporate Equity to fund $60,000 of leasehold improvements. In January 2022, the agreement was amended to include an additional $60,000 of leasehold improvements funding. The loan bears interest at 8.25% annually and is repayable in monthly payments of $3,595 through its December 2024 maturity date. The balance outstanding at January 31, 2022 totaled $111,180.

G. Revenue Financing Arrangement

In April 2021, Teal entered into an agreement under which it sold future customer payments, at a discount, to Forward Financing. At August 31, 2021, the Company assumed the outstanding balance of $38,758. Repayment of the remaining balance was completed in January 2022.

H. Ascentium Capital

In September 2021, Teal entered into a financing agreement with Ascentium Capital to fund the purchase of a fixed asset totaling $24,383. Monthly payments of $656 are payable through October 2024. The balance outstanding at January 31, 2022 totaled $21,255.

I. PayPal

PayPal is an electronic commerce company that facilitates payments between parties through online funds transfers. The Company processes certain customer payments ordered on its e-commerce site through PayPal. The Company has entered into multiple agreements under which PayPal provides an advance on customer payments, and then retains a portion of customer payments until the advance is repaid. PayPal charges a fee which the Company recognizes in full upon entering an agreement. A November 2019 agreement under which PayPal advanced $100,000 and charged a transaction fee of $6,900 was completed in January 2021. A January 2021 agreement under which PayPal advanced $75,444 and charged a transaction fee of $2,444 was completed in August 2021.

J. Summary

Outstanding principal payments are due as follows:

Balance of fiscal year 2022	$	600,683
2023		680,308
2024		646,287
2025		476,462
2026		62,988
Total	$	2,466,728
Short term – through January 31, 2023	$	1,127,596
Long term – thereafter	$	1,339,132

Note 10 - Due to Related Party

A. Founder of Fat Shark

In connection with the acquisition of Fat Shark in November 2020, the Company issued a secured promissory note in the amount of $1,753,000 to the seller who is now an employee. The note bears interest at 3% annually and matures in full in November 2023. In May 2021, the Company made an initial payment of $132,200 by directing a refund from a vendor based in China to the noteholder who is also based in China. The remaining balance of $1,620,800 plus accrued interest totaling $45,129 was paid in September 2021.

B. BRIT, LLC

In January 2020, in connection with the acquisition of Rotor Riot, the Company issued a promissory note in the amount of $175,000 to the seller, BRIT, LLC. The note bears interest at 4.75% annually. The entire outstanding balance of $85,172 plus accrued interest totaling $12,942 was paid in October 2021.

The Company also assumed a line of credit obligation totaling $47,853 which bears interest at 6.42% annually. The outstanding balance totaled $41,622 and $47,922 at January 31, 2022 and April 30, 2021, respectively.

C. Aerocarve

In 2020, the Company received advances totaling $79,000 from Aerocarve, which is controlled by the Company's Chief Executive Officer. The parties agreed that the funds would bear interest at 5% annually until repaid. The balance owed at April 30, 2021 was $74,000. The balance was repaid in full in May 2021.

Note 11 - Convertible Notes

In November 2019, the Company issued a convertible note in the principal amount of $300,000 to one accredited investor and in December 2019, the Company issued a convertible note in the principal amount of $125,000 to a director and a convertible note in the principal amount of $25,000 to our chief executive officer (collectively, the "2019 Notes"). The Notes had a term of 2 years and accrued interest at an annual rate of 12% through the date of conversion. In September and October 2020, the entire $450,000 of 2019 Notes, plus accrued interest totaling $45,204, was converted into 710,444 shares of common stock.

October 2020 Financing

In October 2020, the Company closed a private offering of convertible promissory notes (the "2020 Notes") in the aggregate principal amount of $600,000. The 2020 Notes accrued interest at 12% annually, had a two year term, and were convertible into common stock at the lower of $1.00 or a 25% discount of the price per share of Common Stock offered in a future, qualified offering. The financing also included the issuance of warrants to purchase 399,998 shares of common stock. The Warrants are exercisable for a period of five years at a price equal to the lower of (1) $1.50 per share, or (2) at a price equal to 75% of the price per share of the common stock offered in a future, qualified offering.

The Company determined that the provision associated with a potential reduction in the conversion price of the notes and the exercise price of the warrant represented an embedded derivative financial liability. The derivative liability was initially valued at $728,587, of which $580,000 of the proceeds were applied as a debt discount to reduce the initial carrying value of the notes to zero with the remaining $20,000 applied against transaction fees. The derivative liability was valued using a multinomial lattice model with $460,588 and $267,999 related to the derivative features of the notes and warrants, respectively.

As of January 31, 2022, (a) the 2020 Notes were fully converted into common stock and the related derivative liability eliminated, and (b) 266,666 of the warrants were outstanding with a derivative liability of $445,709.

__January 2021 Financing__

In January 2021, the Company closed a private offering of convertible promissory notes (the "2021 Notes") in the aggregate principal amount of $500,000. The 2021 Notes accrued interest at 12% annually, had a two year term, and were convertible into shares of the Company's common stock at the lower of $1.00 or a 25% discount of the price per share of Common Stock offered in a future, qualified offering. The financing also included the issuance of warrants to purchase 675,000 shares of common stock. The Warrants are exercisable for a period of five years at a price equal to the lower of (i) $1.50 per share, or (ii) a 25% discount to the price per share of common stock offered in a future qualified offering.

The Company determined that the provision associated with a potential reduction in the conversion price of the notes and the exercise price of the warrant represented an embedded derivative financial liability. The derivative liability was initially valued at $4,981,701, of which $500,000 was applied as a debt discount to reduce the initial carrying value of the notes to zero. The derivative liability was valued using a multinomial lattice model with $2,111,035 and $2,870,666 related to the derivative features of the notes and warrants, respectively.

As of January 31, 2022, (a) the 2021 Notes were fully converted into common stock and the related derivative liability eliminated, and (b) 540,000 of the warrants were outstanding with a derivative liability of $904,390.

Note 12 - Income Taxes

Our operating subsidiary, Red Cat Propware, Inc., is incorporated and based in Puerto Rico which is a commonwealth of the United States. We are not subject to taxation by the United States as Puerto Rico has its own taxing authority which passed the Export Services Act, also known as Act 20, in 2012. Under Act 20, eligible businesses are subject to a special corporate tax rate of 4%. Since inception, we have incurred net losses in each year of operations. Our current provision for the reporting periods presented in these financial statements consisted of a tax benefit against which we applied a full valuation allowance, resulting in no current provision for income taxes. In addition, there was no deferred provision for any of these reporting periods.

At January 31, 2022 and April 30, 2021, we had accumulated deficits of approximately $22,700,000 and $15,800,000, respectively. Deferred tax assets related to the future benefit of these net operating losses for tax purposes totaled approximately $908,000 and $632,000, respectively, based on the Act 20 rate of 4%. Currently, we focus on projected future taxable income in evaluating whether it is more likely than not that these deferred assets will be realized. Based on the fact that we have not generated an operating profit since inception, we have applied a full valuation allowance against our deferred tax assets at January 31, 2022 and April 30, 2021.

Note 13 - Common Stock

Our common stock has a par value of $0.001 per share. We are authorized to issue 500,000,000 shares of common stock. Each share of common stock is entitled to one vote.

On May 4, 2021, the Company closed an offering of 4 million shares of common stock which generated gross proceeds of $16 million and net proceeds of approximately $14.6 million.

On May 4, 2021, the Company issued 50,000 shares of common stock for investor relations services rendered.

On May 7, 2021, the Company issued 685,321 shares of common stock in connection with the acquisition of Skypersonic, as further described in Note 1.

On July 21, 2021, the Company closed an offering of 13,333,334 shares of common stock which generated gross proceeds of $60 million and net proceeds of approximately $55.5 million.

During the three months ended July 31, 2021, 62,500 shares of common stock were issued under the terms of a restricted stock agreement with an officer.

On August 10, 2021, the Company issued 1,321,966 shares of common stock in connection with the conversion of 158,704 shares of Series A Preferred Stock.

On August 15, 2021, the Company issued 20,000 shares of common stock for investor relations services rendered.

On August 31, 2021, the Company issued 3,588,272 shares of common stock in connection with the acquisition of Teal Drones, as further described in Note 1.

During the three months ended October 31, 2021, the Company issued 21,972 shares of common stock in connection with working capital adjustments related to the acquisition of Skypersonic, as further described in Note 1.

During the three months ended October 31, 2021, shares of common stock issued under the terms of restricted stock agreements with officers totaled 62,500.

During the three months ended October 31, 2021, shares of common stock issued due to the exercise of stock options totaled 81,115.

During the three months ended January 31, 2022, shares of common stock issued under restricted stock agreements totaled 45,044. In addition, 62,500 shares which were pending issuance under restricted stock agreements, were instead applied against the Note described in footnote 6 and 29,483 shares were applied toward payroll tax obligations on restricted stock.

Note 14 - Preferred Stock

Series A Preferred Stock outstanding totaled 158,704 at April 30, 2021, and were converted into 1,321,966 shares of common stock on August 10, 2021.

Series B Preferred Stock ("Series B Stock") is convertible into common stock at a ratio of 0.8334 shares of common stock for each share of Series B Stock held and votes together with the common stock on an as-if-converted basis. Shares outstanding at January 31, 2022 totaled 986,676 which are convertible into 822,230 shares of common stock.

Note 15 - Warrants

In October 2020, the Company issued five-year warrants to purchase a total of 399,998 shares in connection with the issuance of $600,000 of convertible notes. The warrants have an initial exercise price of $1.50 which may be reduced to a 25% discount of the price per share of Common Stock offered in a future qualified offering. The warrants were valued at $267,999 using the multinominal lattice model and are considered derivative liabilities under ASC 815-40. The value of the warrants was included in the determination of the initial accounting for the financing including the calculation of the derivative liability and related expense.

In January 2021, the Company issued five-year warrants to purchase a total of 675,000 shares in connection with the issuance of $500,000 of convertible notes. The warrants have an initial exercise price of $1.50 which may be reduced to a 25% discount of the price per share of Common Stock offered in a future qualified offering. The warrants were valued at $2,870,666 using the multinominal lattice model and are considered derivative liabilities under ASC 815-40. The value of the warrants was included in the determination of the initial accounting for the financing including the calculation of the derivative liability and related expense.

In March and April 2021, we received $201,249 in connection with the exercise of 201,666 warrants which had been issued in October 2020 and January 2021 as part of the convertible note financings described in note 10. Since these exercises resulted in the elimination of the derivative liability in the warrants, the derivative liability was reduced by $694,305 with a corresponding increase in additional paid in capital.

In May 2021, the Company issued warrants to purchase 200,000 shares of common stock to the placement agent of its common stock offering. The warrants have a five year term and an exercise price of $5.00.

In June 2021, we received $99,999 in connection with the exercise of 66,666 warrants which had been issued in October 2020 as part of the convertible note financings described in Note 11. Since these exercises resulted in the elimination of the derivative liability in the warrants, the derivative liability was reduced by $163,141 with a corresponding increase in additional paid in capital.

In July 2021, the Company issued warrants to purchase 533,333 shares of common stock to the placement agent of its common stock offering. The warrants have a five year term and an exercise price of $5.625.

The following table summarizes the changes in warrants outstanding since April 30, 2020.

	Number of Shares	Weighted-average Exercise Price per Share	Weighted-average Remaining Contractual Term (in years)	Aggregate Intrinsic Value
Balance as of April 30, 2020	—	—	—	—
Granted	1,074,998	$ 1.50		
Exercised	(201,666)	1.50		
Outstanding as of April 30, 2021	873,332	1.50	4.62	$ 2,218,263
Granted	733,333	5.45		
Exercised	(66,666)	1.50		
Outstanding at January 31, 2022	1,539,999	$ 3.38	4.13	$ 1,371,332

Note 16 - Share Based Awards

The 2019 Equity Incentive Plan (the "Plan") allows us to incentivize key employees, consultants, and directors with long term compensation awards such as stock options, restricted stock, and restricted stock units (collectively, the "Awards"). The number of shares issuable in connection with Awards under the Plan may not exceed 8,750,000.

The aggregate intrinsic value of outstanding options represents the excess of the stock price at January 31, 2022 of $1.70 over the exercise price of each option. As of January 31, 2022 and April 30, 2021, there was $3,762,636 and $914,915 of unrecognized stock-based compensation expense related to unvested stock options which is expected to be recognized over the weighted average period of 1.64 years.

The table below sets forth the assumptions used to calculate the fair value of options granted during the three months ended January 31, 2022:

Exercise price	1.69 - 2.52
Stock price on date of grant	1.69 - 2.33
Volatility	268.51% - 270.18%
Risk-free interest rate	1.50% - 1.74%
Expected term (years)	8.25 – 8.25
Dividend yield	—

A summary of activity under the Plan since April 30, 2020 is as follows:

Options	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding as of April 30, 2020	1,597,475	$ 1.10		
Granted	600,000	3.63		
Exercised	—	—		
Forfeited or expired	—	—		
Outstanding as of April 30, 2021	2,197,475	1.79		

Granted	1,656,000		2.59			
Exercised	(112,500)		0.96			
Forfeited or expired	(26,000)		2.12			
Outstanding as of January 31, 2022	3,714,975		2.17	8.72	$	1,010,178
Exercisable as of January 31, 2022	1,897,142	$	2.13	8.01	$	687,111

Stock compensation expense was as follows:

	Three months ended January 31,				Nine months ended January 31,			
		2022		2021		2022		2021
General and administrative	$	343,549	$	336,301	$	952,899	$	525,559
Research and development		143,279		179,157		284,511		199,047
Operations		182,320		170,612		556,928		175,586
Sales and marketing		112,975		168,125		271,808		168,125
Total	$	782,123	$	854,195	$	2,066,146	$	1,068,317

Note 17 - Derivatives

The Company completed financings in October 2020 and January 2021 which included notes and warrants containing embedded features subject to derivative accounting. See Note 11 for a full description of these financings. Both the notes and the warrants included provisions which provided for a reduction in the conversion and exercise prices, respectively, if the Company completed a future qualified offering at a lower price. These provisions represent embedded derivatives which are valued separately from the host instrument (meaning the notes and warrants) and recognized as derivative liabilities on the Company's balance sheet. The Company initially measures these financial instruments at their estimated fair value and recognizes changes in their estimated fair value in results of operations during the period of change. The Company also measures these financial instruments on the date of settlement (meaning when the note is converted or the warrant is exercised) at their estimated fair value and recognizes changes in their estimated fair value in results of operations. Any discount in the carrying value of the note is fully amortized on the date of settlement and recognized as interest expense. The Company estimated the fair value of these embedded derivatives using a multinomial lattice mode1. The range of underlying assumptions used in the binomial model to determine the fair value of the derivative warrant liability upon settlement of the derivative liability and as of January 31, 2022 are set forth below. In addition, the Company's stock price on each measurement date was used in the model.

Risk-free interest rate	1.39 – 1.39%
Expected dividend yield	—
Expected term (in years)	3.67 – 3.99
Expected volatility	245.10 – 249.99%

As of January 31, 2022, all of the notes had been converted into common stock and 806,666 of the warrants were outstanding. Changes in the derivative liability during the three and nine months ended January 31, 2022 and 2021 were as follows:

	Three months ended January 31,				Nine months ended January 31,			
		2022		2021		2022		2021
Balance, beginning of period	$	2,376,565	$	812,390	$	2,812,767	$	—
Additions				4,981,701				5,710,288
Eliminated upon exercise of warrants		—		—		(163,141)		—
Changes in fair value		(1,026,466)		3,350,135		(1,299,527)		3,433,938
Balance, end of period	$	1,350,099	$	9,144,226	$	1,350,099	$	9,144,226

Changes in fair value primarily related to changes in the Company’s stock price during the period with increases in the stock price increasing the liability and decreases in the stock price reducing the liability.

Note 18 - Related-Party Transactions

In November 2019, the Company issued a convertible note in the principal amount of $300,000 to one accredited investor and in December 2019, the Company issued a convertible note in the principal amount of $125,000 to a director and a convertible note in the principal amount of $25,000 to our chief executive officer (collectively, the "2019 Notes"). The Notes had a term of 2 years and accrued interest at an annual rate of 12% through the date of conversion. In September and October 2020, the entire $450,000 of 2019 Notes, plus accrued interest totaling $45,204, was converted into 710,444 shares of common stock.

In July 2021, the Company entered into a consulting agreement with a director resulting in monthly payments of $6,000. In addition, the Company issued 150,000 options to purchase common stock at $2.51 which vest quarterly over the one-year term of the agreement. In January 2022, the agreement was amended to increase the monthly payments to $10,000.

In January 2022, the Company entered into a note agreement with an employee in the principal amount of $510,323, as further described in Note 6.

Additional related party transactions are disclosed in Note 10.

Note 19 - Subsequent Events

Subsequent events have been evaluated through the date of this filing and there are no subsequent events which require disclosure except as set forth below:

The SBA PPP loan principal balance of $300,910 and accrued interest of $3,001 were forgiven on February 16, 2022.

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

The following discussion should be read in conjunction with our unaudited condensed consolidated financial statements and related notes and other financial data included elsewhere in this Quarterly Report on Form 10-Q.

Management's Discussion and Analysis contains forward-looking statements that involve risks and uncertainties, such as statements relating to our liquidity, and our plans for our business focusing on (i) selling drones and related components, and (ii) cloud-based analytics, storage, and services for drones. Any statements that are not historical fact are forward-looking statements. When used, the words "believe," "plan," "intend," "anticipate," "target," "estimate," "expect," and the like, and/or future-tense or conditional constructions ("will," "may," "could," "should," etc.), or similar expressions, identify certain of these forward-looking statements. These forward-looking statements are subject to risks and uncertainties that could cause actual results or events to differ materially from those expressed or implied by the forward-looking statements in this Quarterly Report on Form 10-Q. The Company's actual results and the timing of events could differ materially from those anticipated in these forward-looking statements as a result of many factors. Investors should also review the risk factors in the Company's Annual Report on Form 10-K filed with the SEC on August 12, 2021.

All forward-looking statements speak only as of the date on which they are made. The Company does not undertake any obligation to update such forward-looking statements to reflect events that occur or circumstances that exist after the date of this Quarterly Report on Form 10-Q except as required by federal securities law.

Recent Developments

Firm Commitment Underwritten Public Offerings

S-1 Offering

On May 4, 2021, the Company closed a firm commitment underwritten public offering (the "S-1 Offering") in which it sold 4,000,000 shares of common stock, at a public offering price of $4.00 per share, to ThinkEquity, a division of Fordham Financial Management, Inc., as representative of the underwriters ("ThinkEquity"), pursuant an underwriting agreement dated April 29, 2021. These shares of common stock were offered to and sold by the Company pursuant to a registration statement on Form S-1, as amended (File No. 333-253491), filed with the SEC, which was declared effective by the Commission on April 29, 2021 (the "S-1 Registration Statement"). The net proceeds to the Company, after deducting the underwriting discount, the underwriters' fees and expenses and the Company's estimated expenses, were approximately $14.6 million.

S-3 Offering

On July 21, 2021, the Company closed on a firm commitment underwritten public offering (the "S-3 Offering") in which it sold an aggregate of 13,333,334 shares of Common Stock at a purchase price of $4.50 per share to ThinkEquity, pursuant to an underwriting agreement dated July 18, 2021. These shares of common stock were offered and sold by the Company pursuant to a registration statement on Form S-3, as amended (File No. 333-256216), filed with the SEC, which was declared effective by the SEC on June 14, 2021 and a Supplement to the Prospectus contained in this registration statement filed with the SEC on July 19, 2021. The net proceeds to the Company, after deducting the underwriting discount, the underwriters' fees and expenses, and the Company's estimated expenses were approximately $55.5 million.

Acquisition of Teal Drones

On August 31, 2021, we closed the acquisition of Teal Drones Inc., ("Teal"). Teal is a leader in commercial and government unmanned aerial vehicle ("UAV") technology and manufactures the Golden Eagle drone, approved by the US Department of Defense for reconnaissance, public safety, and inspection applications.

Pursuant to the Merger Agreement, we acquired all of the issued and outstanding share capital of Teal in exchange for $14,000,000 of our common stock ("Common Stock") at the Volume Weighted Average Price (VWAP) of our Common Stock for the 20 trading days ended August 31, 2021 of $2.908 per share, reduced by the amount of Teal debt assumed consisting of approximately $1.67 million payable to DA4, and approximately $1,457,000 in working capital deficit, for a net closing date payment of $10,872,753. At closing, we issued 3,738,911 shares of Common Stock (the "Stock Consideration") with a fair market value of $10,431,562. Fifteen (15%) of the Share Consideration (the "Escrow Shares") was deposited in an escrow account for a period of eighteen (18) months as security for indemnification obligations, any purchase price adjustments due to working capital deficiencies and any other claims or expenses. In December 2021, the Company and Teal agreed to a reduction in the purchase price of $438,058 which resulted in the cancellation of 150,639 shares held in escrow. The fair market value of the cancelled shares was $420,283. The Stock Consideration may be increased if Teal attains certain revenue levels in the twenty four (24) month period following the closing. The additional consideration begins at $4 million if sales total at least $18 million and ends at $16 million if sales total $36 million.

On August 31, 2021, Teal entered into an Amended and Restated Loan and Security Agreement with DA4 (the "Loan Agreement") in the amount of $1,670,294 (the "Loan"), representing the outstanding principal amount previously due and owed by Teal. Interest accrues at a rate of ten (10%) percent per annum. Principal and interest is payable monthly in an amount equal to $49,275 until maturity on December 31, 2024. Teal may prepay the loan at any time, subject to a prepayment premium of $300,705, less the amount of any prior payments of interest. Under the Loan Agreement, Teal granted DA4 a continuing security interest in substantially all of the assets of Teal. In the event of a default, DA4 may declare the full amount of the Loan immediately due and payable and take additional actions including seeking to foreclose on collateral pledged under the Loan Agreement. The Company agreed to guaranty the obligations of Teal under the Loan pursuant to a Joinder Agreement dated August 31, 2021.

Plan of Operations

Red Cat Holdings ("Red Cat" or the "Company") was originally incorporated in February 1984. Since April 2016, the Company's primary business has been to provide products, services and solutions to the drone industry. Beginning in January 2020, the Company expanded the scope of its drone products and services through a number of acquisitions. Teal Drones is a leader in commercial and government Unmanned Aerial Vehicles (UAV) technology. Fat Shark Holdings is a provider of First Person View (FPV) video goggles. Rotor Riot sells FPV drones and equipment, primarily to the consumer marketplace. Skypersonic provides software and hardware solutions that enable drones to complete inspection services in locations where GPS (global positioning systems) are not available, yet still record and transmit data even while being operated from thousands of miles away. Red Cat Propware is developing drone flight data analytics and storage solutions, as well as diagnostic products and services.

Results of Operations

Three Months Ended January 31, 2022 and January 31, 2021

Revenue

During the three months ended January 31, 2022 (or the "2022 period"), revenues totaled $1,856,751 compared to $2,145,988 during the three months ended January 31, 2021 (or the "2021 period"), representing a decrease of $289,237 or 13%. The decrease in revenues primarily related to lower sales of Fat Shark's products at the end of their lifecycles. This decrease was partially offset by the addition of revenues from Skypersonic and Teal which were not included in the 2021 period.

Cost of Goods Sold

During the three months ended January 31, 2022, we incurred cost of goods sold of $1,516,970 compared to $1,576,265 during the three months ended January 31, 2021, representing a decrease of $59,295 or 4%. The decrease corresponds to the decrease in revenues.

Gross Margin

During the three months ended January 31, 2022, gross margin was $339,781 compared to $569,723 during the three months ended January 31, 2021, representing a decrease of $229,942 or 40%. Gross margin, as a percentage of revenue, decreased from 27% during the 2021 period to 18% during the 2022 period. The lower gross margin during the 2022 period reflects higher product and shipping costs resulting from the impact of global supply chain shortages. Additionally, Fat Shark's gross margin, as a percentage of revenue, decreased from 23% during the 2021 period to 8% during the 2022 period partially due to inventory mark downs for products at the end of their lifecycles.

Operating Expenses

During the three months ended January 31, 2022, operations expense totaled $334,278 compared to $146,539 during the 2021 period, resulting in an increase of $187,739 or greater than 100%. This increase is related to our expanded operations following the acquisitions of Skypersonic in May 2021 and Teal in August 2021. Operations expense for Skypersonic and Teal in the 2021 period collectively represented 40% of the increase.

During the three months ended January 31, 2022, research and development expenses totaled $811,288 compared to $167,968 for the three months ended January 31, 2021 resulting in an increase of $643,320 or greater than 100%. This increase directly related to our expanded operations following the acquisitions of Skypersonic and Teal. Research and development expense for Skypersonic and Teal collectively represented 92% of the increase.

During the three months ended January 31, 2022, sales and marketing expenses totaled $238,624 compared to $48,719 during the three months ended January 31, 2021, resulting in an increase of $189,905 or greater than 100%. This increase is primarily related to higher payroll costs of $144,781 associated with new hires in the 2022 period.

During the three months ended January 31, 2022, general and administrative expenses totaled $1,337,183 compared to $499,155 for the three months ended January 31, 2021, representing an increase of $838,028, or more than 100%. The Company listed on the Nasdaq Capital Market in April 2021 which has resulted in higher "public company" expenses including directors' and officers' insurance, investor relations and other public company expenses which collectively increased by $167,346 in the 2022 period compared to the 2021 period. Additionally, payroll costs increased by $174,265, travel costs increased by $84,208 and office related expenses increased by $33,421. Finally, we incurred general and administrative expenses for Skypersonic and Teal of $127,728 and $171,270, respectively, which were not included in the 2021 period.

During the three months ended January 31, 2022, we incurred stock based compensation costs of $782,123 compared to $854,195 in the 2021 period, resulting in a decrease of $72,072 or 8%. Stock based compensation expense can vary from period to period depending upon the number of options and restricted stock issued in a period, and the related vesting terms. The 2021 period included a significant charge related to restricted stock granted to a newly hired officer.

Other Expense (Income)

Other income, net totaled $598,898 during the three months ended January 31, 2022 compared to Other Expense of $7,837,407 during the three months ended January 31, 2021 representing a change of $8,436,305. Changes in the values of the Company's derivative liabilities accounted for most of the change between periods. During the 2021 period, the Company recorded derivative related expenses totaling $7,831,836 whereas the Company recorded a net benefit related to its derivatives of $1,026,466 during the 2022 period. The net benefit in the 2022 period was partially offset by investment losses of $363,760. The derivative liability is valued using a multinomial lattice model which utilizes the Company's stock price in its calculation. A decrease in the stock price during the 2022 period resulted in the net benefit.

Net Loss

Net Loss during the three months ended January 31, 2022 totaled $2,564,817 compared to a net loss of $8,984,260 during the three months ended January 31, 2021, representing a decrease of $6,419,443, or 71%. This decrease is primarily related to changes in the values of the Company's derivative liabilities. A decrease in the stock price during the 2022 period resulted in the net benefit. The decrease in derivative related expenses is offset by higher operating expenses which increased to $3,503,496 in the 2022 period as compared to $1,716,576 in the 2021 period, representing an increase of $1,786,920. Approximately $1,039,453 of the increase, or 58%, related to Skypersonic and Teal whose acquisitions were completed after the 2021 period.

Results of Operations

Nine Months Ended January 31, 2022 and January 31, 2021

Revenue

During the nine months ended January 31, 2022 (or the "2022 period"), we generated revenues totaling $5,116,741 compared to $3,122,077 during the nine months ended January 31, 2021 (or the "2021 period"), representing an increase of $1,994,664 or 64%. The increase in revenues related to acquisitions, including Teal, that were completed during and after the close of the 2021 period. Revenues for Fat Shark increased to $2,327,025 in the 2022 period compared to $1,538,795 in the 2021 period, representing an increase of $788,230 which represents 40% of the overall increase. Teal revenues of $1,098,532 during the 2022 period represented 55% of the increase.

Costs of Goods Sold

During the nine months ended January 31, 2022, we incurred cost of goods sold of $4,521,974 compared to $2,351,153 during the nine months ended January 31, 2021 representing an increase of $2,170,821 or 92%. The increase related to higher revenues associated with the acquisitions of Fat Shark and Teal which were completed in November 2020 and August 2021, respectively.

Gross Margin

During the nine months ended January 31, 2022, gross margin was $594,767 compared to $770,924 during the nine months ended January 31, 2021, representing a decrease of $176,157 or 23%. Gross margin, as a percentage of revenue, decreased from 25% during the 2021 period to 12% during the 2022 period. The lower gross margin during the 2022 period reflects higher product and shipping costs resulting from the impact of global supply chain shortages. Additionally, Fat Shark's gross margin, as a percentage of revenue, decreased from 23% during the 2021 period to 2% during the 2022 period primarily related to inventory mark downs for products at the end of their lifecycles.

Operating Expenses

During the nine months ended January 31, 2022, operations expense totaled $794,390 compared to $353,295 during the 2021 period, resulting in an increase of $441,095 or greater than 100%. This increase is directly related to our expanded operations following the acquisitions of Fat Shark in November 2020, Skypersonic in May 2021, and Teal in August 2021. Increases in operations expense for Fat Shark and the addition of operations expense for Skypersonic and Teal collectively represented 83% of the increase.

During the nine months ended January 31, 2022, research and development expenses totaled $1,548,983 compared to $341,892 for the nine months ended January 31, 2021 resulting in an increase of $1,207,091 or greater than 100%. This increase is directly related to our expanded operations following the acquisitions of Fat Shark, Skypersonic, and Teal. Increases in research and development expense for Fat Shark, and the addition of research and development expense for Skypersonic and Teal collectively represented 98% of the increase.

During the nine months ended January 31, 2022, sales and marketing expenses totaled $524,642 compared to $97,534 during the nine months ended January 31, 2021, resulting in an increase of $427,108 or greater than 100%. This increase is primarily related to higher payroll costs of $262,899 associated with new hires in the 2022 period. In addition, we incurred branding and marketing event costs of $50,500 and $30,799, respectively, in the 2022 period.

During the nine months ended January 31, 2022, general and administrative expenses totaled $3,264,071 compared to $929,874 for the nine months ended January 31, 2021, representing an increase of $2,334,197, or more than 100%. Much of the increase related to "public company" expenses associated with the Company's listing on the Nasdaq Capital Market in April 2021. This resulted in increased costs associated with Directors' and Officers' insurance, investor relations and other public company expenses which collectively increased by $810,670 in the 2022 period compared to the 2021 period. Additionally, payroll costs increased by $304,810, travel costs increased by $143,730, and office related expenses increased by $47,629. In addition, we incurred general and administrative expenses for Skypersonic and Teal of $367,323 and $304,346, respectively, which was included in the 2022 period.

During the nine months ended January 31, 2022, stock based compensation costs totaled $2,066,146 compared to $1,068,317 in the 2021 period, resulting in an increase of $997,829 or 93%. This increase related to expense associated with the issuance of 775,000 restricted stock units and 1,656,000 options in the 2022 period which were not applicable to the 2021 period.

Other Expense (Income)

Other income, net totaled $740,275 during the nine months ended January 31, 2022, compared to other expense of $8,069,797 during the nine months ended January 31, 2021 representing a change of $8,810,072. Changes in the values of the Company's derivative liabilities accounted for most of the change between periods. During the 2021 period, the Company recorded derivative related expenses totaling $8,064,226 whereas the Company recorded a net benefit related to its derivatives of $1,299,527 during the 2022 period. The net benefit in the 2022 period was partially offset by investment losses of $402,207. The derivative liability is valued using a multinomial lattice model which utilizes the Company's stock price in its calculation. A decrease in the stock price during the 2022 period resulted in the net benefit.

Net Loss

Net Loss during the nine months ended January 31, 2022 totaled $6,863,190 compared to a Net Loss of $10,089,785 during the nine months ended January 31, 2021, representing a decrease of $3,226,595, or 32%. This decrease is primarily related to changes in the values of the Company's derivative liabilities. The derivative liability is valued using a multinomial lattice model which utilizes the Company's stock price in its calculation. A decrease in the stock price during the 2022 period resulted in the net benefit. The decrease in derivative related expenses is offset by higher operating expenses which increased to $8,198,232 in the 2022 period as compared to $2,790,912 in the 2021 period, representing an increase of $5,407,320. Approximately $1,888,475 of the increase, or 35%, related to Skypersonic and Teal whose acquisitions were completed after the 2021 period. Approximately $452,783 of the increase, or 8%, related to increased operating expenses for Fat Shark whose activity in the 2021 period included only 3 months. Higher general and administrative and stock based compensation expense totaling $3,264,071 and $2,066,146 respectively, primarily accounted for the balance of the increase.

Cash Flows

Operating Activities

Net cash used in operating activities was $12,041,273 during the nine months ended January 31, 2022 compared to net cash used in operating activities of $917,016 during the nine months ended January 31, 2021 representing an increase of $11,124,257, or greater than 100%. Net cash used in operations, net of non-cash expenses totaling $1,083,885, equaled $5,779,305 in the 2022 period compared to $872,484 in the 2021 period, resulting in an increase of $4,906,821, or greater than 100%. The higher operating use of cash in the 2022 period reflected the acquisitions of Fat Shark, Skypersonic, and Teal. Net cash used related to changes in operating assets and liabilities totaled $6,261,968 during the nine months ended January 31, 2022 compared to net cash provided through changes in operating assets and liabilities of $44,532 during the nine months ended January 31, 2021, representing an increase of $6,217,436, or greater than 100%. Approximately $2,067,436, or 33%, of the increase related to inventory, both higher balances on hand as well as prepaid purchases not yet delivered. Approximately $2,018,772, or 32%, of the increase related to accounts payable. Changes in operating assets and liabilities can fluctuate significantly from period to period depending upon the timing and level of multiple factors, including inventory purchases and vendor payments.

Investing Activities

Net cash used in investing activities was $48,514,017 during the nine months ended January 31, 2022 compared to $48,368 during the nine months ended January 31, 2021, representing an increase of $48,465,649. The increase primarily related to the purchase of marketable securities during the 2022 period.

Financing Activities

Net cash provided by financing activities totaled $67,387,312 during the nine months ended January 31, 2022 compared to $1,200,368 during the nine months ended January 31, 2021. Financing activities can vary from period to period depending upon market conditions, both at a macro-level and specific to the Company. During the 2022 period, the Company received net proceeds of approximately $70 million in connection with two offerings of common stock.

Liquidity and Capital Resources

As of January 31, 2022, we had current assets totaling $61,249,136, including cash of $7,111,527, marketable securities of $48,446,302, and inventory of $2,339,680. Current liabilities as of January 31, 2022 totaled $5,132,137, including accounts payable of $521,139, accrued expenses of $1,493,691, and short term debt obligations of $1,127,596. Our net working capital as of January 31, 2022 was $56,116,999.

We have reported net losses since inception and only began generating revenues in January 2020. To date, we have primarily funded our operations through offerings of common stock. In May 2021, we completed an offering of common stock which raised gross proceeds of $16 million. In July 2021, we completed an offering of common stock which raised gross proceeds of $60 million.

Underwritten Public Offerings

S-1 Offering

On May 4, 2021, the Company closed a firm commitment underwritten public offering (the "S-1 Offering") in which it sold 4,000,000 shares of common stock, at a public offering price of $4.00 per share, to ThinkEquity, a division of Fordham Financial Management, Inc., as representative of the underwriters ("ThinkEquity"), pursuant an underwriting agreement dated April 29, 2021. These shares of common stock were offered to and sold by the Company pursuant to a registration statement on Form S-1, as amended (File No. 333-253491), filed with the SEC, which was declared effective by the Commission on April 29, 2021 (the "S-1 Registration Statement"). The net proceeds to the Company, after deducting the underwriting discount, the underwriters' fees and expenses and the Company's estimated expenses, were approximately $14.6 million.

S-3 Offering

On July 21, 2021, the Company closed on a firm commitment underwritten public offering (the "S-3 Offering") in which it sold an aggregate of 13,333,334 shares of Common Stock at a purchase price of $4.50 per share to ThinkEquity, pursuant to an underwriting agreement dated July 18, 2021. These shares of common stock were offered and sold by the Company pursuant to a registration statement on Form S-3, as amended (File No. 333-256216), filed with the SEC, which was declared effective by the SEC on June 14, 2021 and a Supplement to the Prospectus contained in this registration statement filed with the SEC on July 19, 2021. The net proceeds to the Company, after deducting the underwriting discount, the underwriters' fees and expenses, and the Company's estimated expenses were approximately $55.5 million.

Until we are able to sustain operations through the sale of products and services, we will continue to fund operations through equity and/or debt transactions. We can provide no assurance that the financings described above will be sufficient to fund our operations until we are able to sustain operations through the sale of products and services. In addition, there can be no assurance that such additional financing, if required, will be available to us on acceptable terms, or at all.

Critical Accounting Policies and Estimates

Our financial statements and accompanying notes have been prepared in accordance with Generally Accepted Accounting Principles ("GAAP") applied on a consistent basis. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting periods.

We regularly evaluate the accounting policies and estimates that we use to prepare our financial statements. A complete summary of these policies is included in the notes to our financial statements. In general, management's estimates are based on historical experience, information from third party professionals, and various other assumptions that are believed to be reasonable under the facts and circumstances. Actual results could differ from those estimates made by management.

Off-Balance Sheet Arrangements

We have no off-balance sheet arrangements.

Recently Issued Accounting Pronouncements

The Company has implemented all new accounting pronouncements that are in effect. These pronouncements did not have any material impact on the financial statements unless otherwise disclosed, and the Company does not believe that there are any other new accounting pronouncements that have been issued that might have a material impact on its financial position or results of operations.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are a smaller reporting company and are not required to provide this information.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Disclosure controls and procedures are designed to ensure that information required to be disclosed in our reports filed under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by our company in the reports that it files or submits under the Exchange Act is accumulated and communicated to our management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. Our management carried out an evaluation under the supervision and with the participation of our Principal Executive Officer and Principal Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rules 13a-15(e) and 15d-15(e) under the Exchange Act. Based upon that evaluation, our Principal Executive Officer and Principal Financial Officer have concluded that our disclosure controls and procedures were effective as of January 31, 2022, except that our disclosure controls and procedures are not effective for the following reasons:

- We did not maintain effective controls regarding the timely financial reporting of accounting transactions. Specifically, certain individuals did not provide reporting on a timely basis regarding certain corporate banking accounts which they managed. The failure to comply with the Company's internal reporting deadlines increases the risk that (i) transactions are not properly accounted for, and (ii) adequate documentation is not obtained. Both risks can adversely impact the accuracy of our financial reporting. The Company is presently evaluating how to remedy this internal control weakness.

Changes in Internal Control over Financial Reporting

During the period covered by this report, there were no changes in our internal controls over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

There are no pending legal proceedings to which the Company is a party or in which any director, officer or affiliate of the Company, any owner of record or beneficially of more than 5% of any class of voting securities of the Company, or security holder is a party adverse to the Company or has a material interest adverse to the Company. The Company's property is not the subject of any pending legal proceedings.

ITEM 1A. RISK FACTORS

We are a smaller reporting company as defined by Rule 12b-2 of the Securities Exchange Act of 1934 (the "Exchange Act") and are not required to provide the information.

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

There were no sales of equity securities sold during the period covered by this Report that were not registered under the Securities Act and were not previously reported in a Current Report on Form 8-K filed by the Company except as set forth below:

During the quarter ended January 31, 2022, pursuant to our 2019 Equity Incentive Plan, we issued options to purchase a total of 737,000 shares of our common stock at prices ranging from $1.69 to $2.52 per share.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

Exhibit	Description
10.1	Promissory Note issued to Allan Evans, dated as of March 11, 2022
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 and accounting 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 Chief 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 Chief 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	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

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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.

Red Cat Holdings, Inc.

Date: March 17, 2022

By: */s/ Jeffrey Thompson*
Jeffrey Thompson
Chief Executive Officer
(Principal Executive Officer)

Date: March 17, 2022

By: */s/ Joseph P. Hernon*

Joseph Hernon
Chief Financial Officer
(Principal Financial and Accounting Officer)

Exhibit 10.1

PROMISSORY NOTE

US $510,323 March 11, 2022

For good and valuable consideration, **Allan Evans**, ("Maker"), hereby makes and delivers this Promissory Note (this "Note") in favor of **Red Cat Holdings, Inc.**, a Nevada corporation ("Holder"), and hereby agree as follows:

1. **Principal Obligation and Interest.** For value received**,** Maker promises to pay to Holder at such place as Holder may designate in writing, in currently available funds of the United States, the principal sum of Five Hundred Ten Thousand Three Hundred Twenty-three Dollars ($510,323). Makers' obligation under this Note shall accrue interest from the date hereof until paid in full at the rate of six percent (6%) per annum.

2. **Payment Terms; Transfer of Maker Shares in the Holder as Payment.** Maker agrees to remit payment in full of all principal and interest due hereunder to Holder on or before December 31, 2022 (the "Maturity Date"). Maker shall have the right to prepay all or any part of the principal under this Note without penalty. In connection with Maker's employment by the Holder as an executive, the Maker has been granted certain awards of common stock in the Holder, some of which have vested and others which are unvested as of the date of this Note. Certain shares of common stock of the Holder owned or to-be-owned by the Maker shall be applied to reduce the balance owing under this Note as follows:

a. Effective as of the date of this Note, 104,166 shares of common stock of the Holder which were scheduled to be issued to the Maker, will be retained by the Holder. The fair value of such shares in the amount of $280,832 shall be deemed applied and credited against the balance of this Note in favor of the Maker.

b. The Maker owns an additional 110,983 shares of common stock in the Holder which are presently held at the Transfer Agent. Such shares, as well as the shares described in section 2.c below, shall not be transferred, sold, assigned, or encumbered by the Maker unless or until all principal and interest due and owing under this Note is paid in full.

c. As part of his compensation as an executive employee, Maker is entitled to receive 20,833 shares of common stock in the Holder each month during calendar year 2022. Holder shall retain 3,000 of these shares each month and, in return, the fair value of such shares as defined under U.S. Generally Accepted Accounting Principles (the "Fair Value") shall be deemed applied and credited against the balance of this Note in favor of the Maker.

d. On or before the Maturity Date, the Maker shall: (i) return to the Holder for cancellation shares of common stock of the Holder having a Fair Value equal to the remaining balance of principal and interest then due under this Note; or (ii) pay the remaining balance of principal and interest then due under this Note in cash; or (iii) pay the remaining balance of principal and interest then due under this Note with a combination of cash payment and return of shares of the Holder for cancellation to be credited at their Fair Value.

3. **Executive Employment Agreement Deemed Amended.** To the extent required to give full effect to the terms of this Note, the Maker's Executive Employment Agreement with the Holder, and any stock award agreement or similar agreement by and between the Maker and the Holder, shall be amended by the terms hereof.

4. **Representations and Warranties of Maker.** Maker hereby represents and warrants the following to Holder:

a. Maker has the full right, power, and authority to execute, deliver and perform his obligations under this Note. This Note has been duly executed and delivered by the Maker and constitutes a valid and legally binding obligation of the Maker enforceable in accordance with its terms.

b. The execution of this Note and Maker's compliance with the terms, conditions and provisions hereof does not conflict with or violate any provision of any agreement, contract, lease, deed of trust, indenture, or instrument to which Maker is a party or by which Maker is bound.

5. **Defaults.** The following events shall be defaults under this Note:

a. Maker's failure to remit any payment under this Note on before the date due, if such failure is not cured in full within five (5) days of written notice of default;

b. Maker's transfer, sale, assignment, or encumbrance of any Maker's shares of common stock in the Holder prior to payment of this Note in full.

c. Maker's failure to perform or breach of any non-monetary obligation or covenant set forth in this Note if such failure is not cured in full within ten (10) days following delivery of written notice thereof from Holder to Maker;

6. **Rights and Remedies of Holder**. Upon the occurrence of an event of default by Maker under this Note, then, in addition to all other rights and remedies at law or in equity, Holder may exercise any one or more of the following rights and remedies:

a. Accelerate the time for payment of all amounts payable under this Note by written notice thereof to Maker, whereupon all such amounts shall be immediately due and payable;

b. By proper direction to the Holder's transfer agent, deem cancelled any and all shares in the Holder owned by the Maker and having a Fair Value equal to or less than the balance of principal and interest then due and owing under this Note; and

c. Pursue any other rights or remedies available to Holder at law or in equity.

7. **Interest To Accrue Upon Default.** Upon the occurrence of an event of default by Makers under this Note, the balance then owing under the terms of this Note shall accrue interest at the rate of eighteen percent (18%) per annum from the date of default until Holder is satisfied in full.

8. **Choice of Laws; Actions.** This Note shall be constructed and construed in accordance with the internal substantive laws of the State of Nevada, without regard to the choice of law principles of said State. Maker acknowledges that this Note has been negotiated in Washoe County, Nevada. Accordingly, the exclusive venue of any action, suit, counterclaim or cross claim arising under, out of, or in connection with this Note shall be the state or federal courts in Washoe County, Nevada. Maker hereby consents to the personal jurisdiction of any court of competent subject matter jurisdiction sitting in Washoe County, Nevada.

9. **Usury Savings Clause.** Maker expressly agrees and acknowledges that Maker and Holder intend and agree that this Note shall not be subject to the usury laws of any state other than the State of Nevada. Notwithstanding anything contained in this Note to the contrary, if collection from Maker of interest at the rate set forth herein would be contrary to applicable laws, then the applicable interest rate upon default shall be the highest interest rate that may be collected from Maker under applicable laws at such time.

10. **Costs of Collection.** Should the indebtedness represented by this Note, or any part hereof, be collected at law, in equity, or in any bankruptcy, receivership or other court proceeding, or this Note be placed in the hands of any attorney for collection after default, Maker agrees to pay, in addition to the principal and interest due hereon, all reasonable attorneys' fees, plus all other costs and expenses of collection and enforcement, including any fees incurred in connection with such proceedings.

11. **Miscellaneous**.

a. This Note shall be binding upon Maker and shall inure to the benefit of Holder and its successors, assigns, heirs, and legal representatives.

b. Any failure or delay by Holder to insist upon the strict performance of any term, condition, covenant or agreement of this Note, or to exercise any right, power or remedy hereunder shall not constitute a waiver of any such term, condition, covenant, agreement, right, power or remedy.

c. Any provision of this Note that is unenforceable shall be severed from this Note to the extent reasonably possible without invalidating or affecting the intent, validity or enforceability of any other provision of this Note.

d. In the event of any action at law or in equity to enforce this Note, the prevailing party shall be entitled to recover its reasonable attorneys' fees and costs from the unsuccessful party.

e. This Note may not be modified or amended in any respect except in a writing executed by the party to be charged.

IN WITNESS WHEREOF, this Note has been executed effective on the date indicated.

"Maker":

____
Allan Evans

Acknowledged by "Holder":

RED CAT HOLDINGS, INC.

By: __________________________________
Joseph Hernon, Chief Financial Officer

EXHIBIT 31.1

CERTIFICATION OF CHIEF EXECUTIVE OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT AND RULE 13A-14(A)
OR 15D-14(A) UNDER THE SECURITIES EXCHANGE ACT OF 1934

I, Jeffrey Thompson, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Red Cat 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. I am 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 my supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to me 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 my 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 my 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 that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. I have disclosed, based on my most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of 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: March 17, 2022

/s/ Jeffrey Thompson
Chief Executive Officer
(Principal Executive Officer)

EXHIBIT 31.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT AND RULE 13A-14(A)
OR 15D-14(A) UNDER THE SECURITIES EXCHANGE ACT OF 1934

I, Joseph Hernon, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Red Cat 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. I am 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 my supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to me 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 my 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 my 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 that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. I have disclosed, based on my most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of 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: March 17, 2022

/s/ Joseph Hernon
Chief Financial Officer
(Principal Financial and Accounting Officer)

EXHIBIT 32.1

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 the Quarterly Report on Form 10-Q of Red Cat Holdings, Inc. (the “Company”), for the quarter ended January 31, 2022, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Jeffrey Thompson, Chief Executive Officer of the Company, certify, 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: March 17, 2022

By: */s/ Jeffrey Thompson*
Name: Jeffrey Thompson
Title: Chief Executive Officer
(Principal Executive Officer)

EXHIBIT 32.2

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 the Quarterly Report on Form 10-Q of Red Cat Holdings, Inc. (the “Company”), for the quarter ended January 31, 2022, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Joseph Hernon, Chief Financial Officer of the Company, certify, 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: March 17, 2022

By: */s/ Joseph Hernon*
Name: Joseph Hernon
Title: Chief Financial Officer
(Principal Financial and Accounting Officer)