Unusual Machines Inc.

NYSE American - UMAC

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Fourth Strategic Investment Deepens Vertical Integration; Structure Creates Multiple Upside Pathways

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- **UMAC invested $25M for a potential 34% stake in XTI Aerospace**, gaining exposure to both a long-range VTOL developer and the largest U.S. drone distributor through XTIA's acquisition of Drone Nerds.
- **A new legal interpretation reduces prior 40 Act concerns**, enabling UMAC to treat its holdings as strategic and pursue an SEC No-Action Letter once the government reopens.
- **Drone Nerds' $100M+ profitable operation strengthens UMAC's ecosystem**, while its shift from DJI/Autel to U.S.-made platforms aligns with tightening federal restrictions on Chinese drones.
- **UMAC's 12% senior preferred shares position provides both upside and downside protection,** including potential control of XTIA if outside capital becomes scarce and effective ownership of Drone Nerds in a failure scenario.
- **The structure includes a pricing condition restricting XTIA from raising equity below $2.50 before conversion**, protecting UMAC's economics and supporting its targeted 34% pro forma stake.

Rating	Buy	
Target Price	$25.00	
Ticker Symbol	UMAC	
Market	NYSE	
Stock Price	$10.73	
52 wk High	$23.62	
52 wk Low	$2.34	
Shares Outstanding:	36.8	M
Public Market Float:	34.1	M
Avg. Daily Volume	3,708,513	
Market Capitalization:	$395.7	M
Institutional Holdings:	10.7%	
Dividend Yield:	0.0%	

Earnings Per Share	**Normalized to exclude unusual items**		
FYE - December	**2024**	**2025E**	**2026E**
1Q - March	($0.11)	($0.21) A	($0.07)
2Q - June	($0.15)	($0.32) A	($0.04)
3Q - September	($0.10)	$0.05 A	($0.04)
4Q - December	($2.27)	($0.05)	($0.01)
Year	**($3.84)**	**($0.40)**	**($0.16)**
Revenue ($mm)	**5.6**	**9.8**	**20.9**
EV/Rev	46.5X	26.5X	12.4X
EBITDA ($mm)	**NM**	**NM**	**NM**

Risks/Valuation

- **Execution Risk:** The primary risk for Unusual Machines centers on the execution of its growth strategy. The company is focused on introducing key drone components, such as motors and circuit boards, to supply other drone manufacturers. Success hinges on its ability to effectively develop, market, and sell these components to a growing customer base. Any delays or challenges in production, distribution, or customer adoption could negatively impact its growth trajectory.
- **Valuation Premium:** We currently value UMAC shares at approximately two times the average multiple of its industry peers, reflecting the company's strong growth prospects and strategic positioning within the defense and drone sectors. However, this premium is based on the assumption that execution risks are managed effectively and that acquisitions contribute to long-term growth.

Company description: Unusual Machines operates primarily as a retail drone business under the Rotor Riot brand, catering to the $100 million enthusiast market. The company's strategic growth focus is on expanding into the multi-billion-dollar drone component market. Introducing new products.

Fourth Strategic Investment Deepens Vertical Integration; Structure Creates Multiple Upside Pathways

Yesterday, Unusual Machines (UMAC) announced its fourth strategic investment, committing $25 million for a potential 34% stake in XTI Aerospace (NASDAQ: XTIA). The investment takes the form of 12% Series 10 Convertible Preferred Stock, issued in conjunction with XTIA's acquisition of Drone Nerds for $40 million. Functionally, this transaction provides UMAC exposure to both a next-generation VTOL developer and the largest drone retailer/distributor in the United States—a combination we believe the market has not yet fully appreciated.

Following the announcement, we spoke with CEO Allan Evans, who provided important context regarding the structure, regulatory considerations, and strategic rationale behind the deal. Below we summarize the key takeaways that, in our view, help illuminate why this investment is significantly more attractive than initial headlines imply.

40 Act Considerations: New Interpretation Expands Strategic Flexibility

Prior to this announcement, we were not expecting UMAC to pursue additional minority investments, given the potential risk of inadvertently becoming an "investment company" under the Investment Company Act of 1940. However, UMAC's legal counsel has provided a new interpretation:

- Because each investment is strategic,
- Occurs within the same industry (drones/VTOL), and
- Integrates into UMAC's core manufacturing and distribution ecosystem,

UMAC does not expect to be treated as an investment company.

Once the federal government reopens, UMAC plans to request an SEC No-Action Letter to formalize this view. If granted, this could reopen the door to additional strategic transactions. In a downside scenario, UMAC could register as an investment company or divest an asset—either of which would still preserve the significant gains already embedded in the first three investments.

XTI Aerospace Overview: A Targeted Long-Range VTOL Platform

XTI Aerospace is a Colorado-based developer of a manned, long-range vertical takeoff and landing (VTOL) aircraft. While Joby, Archer, and others focus primarily on short-range urban air mobility, XTI's TriFan 600 targets an underserved segment requiring:

- Longer range,
- Higher payload, and
- Hybrid-electric propulsion.

The aircraft is currently in Preliminary Design Review (PDR) with Critical Design Review (CDR), flight testing, and FAA Type Certification targeted for 2027. Some sources estimate that approximately $200 million of additional capital will be needed to reach certification—a funding gap that could provide UMAC an opportunity to increase its stake or secure a controlling position if external capital becomes scarce.

Drone Nerds: Largest U.S. Drone Retailer, Now Pivoting to U.S.-Made Platforms

Drone Nerds, based in Miami, is the largest drone retailer and distributor in the United States, historically anchored in Chinese platforms such as DJI and Autel. With accelerating U.S. and allied-nation restrictions on Chinese drone imports, the company is rapidly transitioning to American brands, including:

- Anzu Robotics, and
- Teal Drones (a Red Cat subsidiary).

Drone Nerds generates over $100 million in annual revenue and is profitable, providing XTI with an important source of operating cash flow and channel strength. UMAC already had a supplier relationship with Drone Nerds—sourcing DJI drones through the distributor—so this transaction meaningfully deepens vertical integration across manufacturing, components, and distribution.

Strategic Benefits to UMAC

We see several compelling advantages:

1. **Immediate Positioning as the Largest Shareholder of the Largest U.S. Drone Distributor.** UMAC now holds a major stake in Drone Nerds via its XTIA preferred position. This creates a powerful channel for U.S.-made drones incorporating UMAC components—particularly as demand shifts sharply away from Chinese platforms.
2. **Embedded Option on a VTOL Manufacturer in a Rapidly Expanding Sector.** Should the TriFan 600 succeed, UMAC holds a significant equity stake in a next-generation VTOL platform. This provides upside exposure to a sector expected to "take off" over the next several years.
3. **Pathway to Control.** If XTI struggles to raise capital at or above $2.50/share, UMAC—with a strong cash balance and protective covenants—could step in and effectively take control of both a VTOL developer and a major drone distributor at an attractive valuation.
4. **Downside Protection.** UMAC's 12% convertible preferred stock sits at the top of XTI's capital structure. In a failure scenario (e.g., TriFan 600 cannot be certified and XTI files for bankruptcy), UMAC would effectively acquire Drone Nerds for just $25 million, a highly attractive valuation for a profitable company generating over $100 million in revenue.
5. **Anti-Dilution Protection Via the $2.50 Minimum Issuance Price.** The SPA contains a covenant prohibiting XTIA from issuing equity or equity-linked securities below $2.50 per share until after both shareholder approval and registration effectiveness. This protects UMAC from dilution prior to conversion, and opportunistic capital raises that could impair its intended 34% stake.

Scenario Framework

We outline the potential outcomes in order of favorability:

1. **Certification Success (Best Case)**
   - XTI successfully certifies and begins deliveries of the TriFan 600.
   - XTIA's equity would likely re-rate substantially.
   - UMAC would recognize gains and maintain a strategic stake.
   - Some dilution is possible in future rounds, though UMAC could participate.

2. **Capital-Raise Challenge (Strategic Control Case)**

   - XTI makes solid technical progress but struggles to raise outside capital at ≥$2.50/share (triggering the covenant).
   - UMAC could fund the gap and acquire de facto control of the combined VTOL + Drone Nerds platform.

3. **Program Failure (Downside Case)**

   - TriFan 600 cannot be certified; XTI enters restructuring.
   - UMAC's preferred position enables it to acquire Drone Nerds for $25M, creating substantial downside protection and potentially positive IRR even in failure.

Balance Sheet Impact and Funding Philosophy

Post-transaction, UMAC's cash balance declines to approximately $110 million.
Management has consistently indicated a desire to maintain at least $100 million to support:

- A "fortress" balance sheet,
- Vendor reliability for defense-prime customers, and
- Execution capacity as DoD budgets advance.

Accordingly, this investment may mark the end of incremental deal-making unless a high-conviction, transformative opportunity emerges.

UMAC continues to evolve from a drone components manufacturer into a central node in the emerging American drone and VTOL ecosystem. This investment enhances strategic optionality, deepens vertical integration, and offers a uniquely asymmetric risk-reward profile.

We reiterate our Buy rating and $25 price target. Even without strategic investments, UMAC's core business, positioned for a surge in U.S. drone demand, would justify our valuation. Yesterday's announcement simply underscores that UMAC is becoming far more than "just" a components supplier—it is rapidly positioning itself as a key consolidator in a once-in-a-generation industry shift.

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Unusual Machines Income Forecast

	2025E					2026E					2027E				
Fiscal years ended December 31	1QA	2QA	3QA	4Q	YEAR	1Q	2Q	3Q	4Q	YEAR	1Q	2Q	3Q	4Q	YEAR
Revenue															
Retail	1,735,955	1,465,539	1,067,294	1,958,926	6,227,714	1,909,551	1,612,093	1,174,023	2,154,818	6,850,485	2,100,506	1,773,303	1,291,426	2,370,300	7,535,534
percent of total	85.0%	69.0%	50.0%	56.6%	63.8%	48.8%	35.0%	22.7%	30.1%	32.9%	20.8%	18.1%	13.9%	19.2%	18.1%
YoY growth	180.5%	3.9%	-30.3%	15.0%	18.3%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%
Enterprise	306,345	658,431	1,067,294	1,500,000	3,532,070	2,000,000	3,000,000	4,000,000	5,000,000	14,000,000	8,000,000	8,000,000	8,000,000	10,000,000	34,000,000
percent of total	15.0%	31.0%	50.0%	43.4%	36.2%	51.2%	65.0%	77.3%	69.9%	67.1%	79.2%	81.9%	86.1%	80.8%	81.9%
YoY growth				399.0%	1075.0%	552.9%	355.6%	274.8%	233.3%	296.4%	300.0%	166.7%	100.0%	100.0%	142.9%
	2,042,300	**2,123,970**	**2,134,588**	**3,458,926**	**9,759,784**	**3,909,551**	**4,612,093**	**5,174,023**	**7,154,818**	**20,850,485**	**10,100,506**	**9,773,303**	**9,291,426**	**12,370,300**	**41,535,534**
Year-over-year growth	230.0%	50.5%	39.4%	72.6%	75.4%	91.4%	117.1%	142.4%	106.9%	113.6%	158.4%	111.9%	79.6%	72.9%	99.2%
Sequential growth	1.9%	-61.8%	0.5%	62.0%		13.0%	18.0%	12.2%	38.3%		41.2%	-3.2%	-4.9%	33.1%	
Total cost of revenue	1,545,493	1,329,291	1,294,200	2,144,534	6,313,518	2,423,921	2,859,498	3,104,414	3,935,150	12,322,983	5,454,273	5,179,850	4,831,541	6,308,853	21,774,518
As a percent of revenue	75.7%	62.6%	60.6%	62.0%	64.7%	62.0%	62.0%	60.0%	55.0%	59.1%	54.0%	53.0%	52.0%	51.0%	52.4%
Gross margin	496,807	794,679	840,388	1,314,392	3,446,266	1,485,629	1,752,595	2,069,609	3,219,668	8,527,502	4,646,233	4,593,452	4,459,884	6,061,447	19,761,016
As a percent of revenue	24.3%	37.4%	39.4%	38.0%	35.3%	38.0%	38.0%	40.0%	45.0%	40.9%	46.0%	47.0%	48.0%	49.0%	47.6%
Operations	302,602	404,277	636,705	207,536	1,551,120	781,910	461,209	517,402	357,741	2,118,263	505,025	488,665	464,571	618,515	2,076,777
As a percent of revenue	14.8%	19.0%	29.8%	6.0%	15.9%	20.0%	10.0%	10.0%	5.0%	10.2%	5.0%	5.0%	5.0%	5.0%	5.0%
Research and development	7,903	62,731	39,369	34,589	144,592	39,096	46,121	51,740	71,548	208,505	101,005	97,733	92,914	123,703	415,355
As a percent of revenue	0.4%	3.0%	1.8%	1.0%	1.5%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%
Selling and marketing	207,616	302,358	373,539	518,839	1,402,352	781,910	553,451	620,883	858,578	2,814,822	1,212,061	1,172,796	1,114,971	1,484,436	4,984,264
As a percent of revenue	10.2%	14.2%	17.5%	15.0%	14.4%	20.0%	12.0%	12.0%	12.0%	13.5%	12.0%	12.0%	12.0%	12.0%	12.0%
General and administrative	3,225,904	7,195,193	4,730,063	3,000,000	18,151,160	3,000,000	3,000,000	3,000,000	3,000,000	12,000,000	2,200,000	2,200,000	2,200,000	2,200,000	8,800,000
As a percent of revenue	158.0%	338.8%	221.6%	86.7%	186.0%	76.7%	65.0%	58.0%	41.9%	57.6%	21.8%	22.5%	23.7%	17.8%	21.2%
Depreciation and amortization	20,593	20,593	22,449	30,000	93,635	65,000	65,000	65,000	65,000	260,000	75,000	75,000	75,000	75,000	300,000
Loss on impairment of goodwill															
Operating Income	**(3,267,811)**	**(7,190,473)**	**(4,961,737)**	**(2,476,572)**	**(17,896,593)**	**(3,182,287)**	**(2,373,186)**	**(2,185,416)**	**(1,133,199)**	**(8,874,088)**	**553,142**	**559,258**	**512,428**	**1,559,793**	**3,184,620**
Operating margin	-160.0%	-338.5%	-232.4%	-71.6%	-183.4%	-81.4%	-51.5%	-42.2%	-15.8%	-42.6%	5.5%	5.7%	5.5%	12.6%	7.7%
Interest income	1,532	225,734	715,489	800,000	1,742,755	800,000	800,000	800,000	800,000	3,200,000	800,000	800,000	800,000	800,000	3,200,000
Interest expense	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Loss on extinguishment of debt	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Unrealized gain	-	-	5,849,713		5,849,713										
Change in fair value	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Pretax Income	(3,266,279)	(6,964,739)	1,603,465	(1,676,572)	(10,304,125)	(2,382,287)	(1,573,186)	(1,385,416)	(333,199)	(5,674,088)	1,353,142	1,359,258	1,312,428	2,359,793	6,384,620
Taxes				-	-	-	-	-	-	-	-	-	-	-	-
Tax rate	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Net income to common	**(3,266,279)**	**(6,964,739)**	**1,603,465**	**(1,676,572)**	**(10,304,125)**	**(2,382,287)**	**(1,573,186)**	**(1,385,416)**	**(333,199)**	**(5,674,088)**	**1,353,142**	**1,359,258**	**1,312,428**	**2,359,793**	**6,384,620**
Net income margin	-159.9%	-327.9%	75.1%	-48.5%	-105.6%	-60.9%	-34.1%	-26.8%	-4.7%	-27.2%	13.4%	13.9%	14.1%	19.1%	15.4%
Diluted shares outstanding	15,902,473	21,771,954	30,002,179	35,002,179	25,669,696	35,102,179	35,202,179	35,302,179	35,402,179	35,252,179	35,502,179	35,602,179	35,702,179	35,802,179	35,652,179
Seq change	15,902,473	5,869,481	8,230,225	5,000,000		100,000	100,000	100,000	100,000		100,000	100,000	100,000	100,000	
EPS diluted - continuing	**($0.21)**	**($0.32)**	**$0.05**	**($0.05)**	**($0.40)**	**($0.07)**	**($0.04)**	**($0.04)**	**($0.01)**	**($0.16)**	**$0.04**	**$0.04**	**$0.04**	**$0.07**	**$0.18**
EBITDA															
Operating income	(3,267,811)	(7,190,473)	(4,961,737)	(2,476,572)	(17,896,593)	(3,182,287)	(2,373,186)	(2,185,416)	(1,133,199)	(8,874,088)	553,142	559,258	512,428	1,559,793	3,184,620
Addback:					-					-					-
Depreciation and amortization	20,593	20,593	22,449	30,000	93,635	65,000	65,000	65,000	65,000	260,000	75,000	75,000	75,000	75,000	300,000
Share-based compensation	1,906,373	5,513,328	2,102,560	1,000,000	10,522,261	1,000,000	1,000,000	1,000,000	1,000,000	4,000,000	1,000,000	1,000,000	1,000,000	1,000,000	4,000,000
Other	300,000	300,000	1,200,000	-	1,800,000	-	-	-	-	-	-	-	-	-	-
EBITDA	**(1,040,845)**	**(1,356,552)**	**(1,636,728)**	**(1,446,572)**	**(5,480,697)**	**(2,428,602)**	**(1,308,186)**	**(1,120,416)**	**(68,199)**	**(4,614,088)**	**3,221,685**	**1,634,258**	**1,587,428**	**2,634,793**	**7,484,620**
Capital expenditures	-	262,751	1,287,936	500,000	2,050,687	500,000	500,000	500,000	500,000	2,000,000	500,000	500,000	500,000	500,000	2,000,000
Free cash flow	**(1,040,845)**	**(1,619,303)**	**(2,924,664)**	**(1,946,572)**	**(7,531,384)**	**(2,928,602)**	**(1,808,186)**	**(1,620,416)**	**(568,199)**	**(6,614,088)**	**2,721,685**	**1,134,258**	**1,087,428**	**2,134,793**	**5,484,620**

Source: Company reports and Litchfield Hills Research

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