NASDAQ:DTST Q1 2026 Earnings Call Transcript

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Operator | Conference Operator:

Greetings and welcome to the Data Storage Corporation first quarter 2026 earnings conference call. At this time, all participants are in a listen-only mode. A question and answer session will follow a formal presentation. If anyone should require operator assistance, please press star zero on your telephone keypad. As a reminder, this conference is being recorded. It is now my pleasure to introduce David Walden, Investor Relations. Thank you. You may begin.

David Walden | Investor Relations:

Thank you and good morning, everyone. Welcome to Data Storage Corporation's 2026 First Quarter Business Update Conference Call. On the call with us this morning are Chuck Piluso, Chairman and Chief Executive Officer, and Chris Panagiotakos, Chief Financial Officer. The company issued a press release this morning containing its 2026 First Quarter financial results, which is also posted on the company's website. If you have any questions after the call or would like any additional information about the company, Please contact Crescendo Communications at 212-671-1020. Before we begin, please note that today's call contains forward-looking statements within the meaning of the Private Security Litigation Reform Act of 1995. Actual results may differ materially due to various risks and uncertainties described in the company's filings with the SEC. Except as required by law, the company assumes no obligation to update or revise forward-looking statements. I'd now like to turn the call over to Chuck Paluso. Please go ahead, Chuck.

Chuck Piluso | Chairman and Chief Executive Officer:

Thank you, David. Good morning, everyone. We appreciate everyone joining us today. The first quarter of 2026 marked another important milestone in the strategic transformation of Data Storage Corporation. Over the past year, we have repositioned the company following a successful sale of our cloud solution business in 2025. And today, we are operating from a position of financial strength, strategic flexibility, and operational focus. As many of you know, the sale of the Cloud First business was transformational for Data Storage Corporation. That transaction not only validated the value we created over more than two decades, but also provided us with the capital foundation necessary to reposition the company towards what we believe are significantly larger long-term market opportunities. Following the transaction, we completed a substantial tender offer that reduced our outstanding shares count by approximately 72% while still maintaining debt-free balance sheet and substantial liquidity. Importantly, the period following the sale was not a pause in activity. It was a period of evaluation, of analysis, of strategic development. We spent considerable time assessing emerging infrastructure trends, regulatory developments, competitive positioning, and areas where we believe meaningful structural market gap existed. What became increasingly clear Experimentation into mission-critical software deployment environments. Across industries such as healthcare, financial service, insurance, organizations are beginning to deploy sovereign AI in AI factory environments. On-site equipment designed to run proprietary AI models on highly sensitive data sets. These are not public AI cloud environments. These are private enterprise grade AI infrastructures that organizations increasingly rely upon for core operating workflows, security, decision making, compliance functions, and customer facing processes. As we started this market, we identified what we believe is a critical infrastructure gap As these systems are deployed, today we believe there are no widely adopted purpose-built platforms designed specifically addressing recovery, resilience, behavior validation, and regulatory compliance to these AI factory environments. After two successful decades, Operating Cloud First, we understand the client's requirements as it relates to meeting their expectations surrounding business continuity. Additional data storage systems focus primarily on restoring hardware or infrastructure uptime, but AI introduces an entirely different challenge set. Enterprises will require a business continuity service. and will increasingly need to validate those models of behaving correctly when a situation occurs. That output remains compliant, that inference consistency is maintained and that recovery procedures themselves satisfy the client and regulatory standards. We believe this creates a significantly new category of infrastructure need. To address this opportunity, we plan to establish sovereign AI Solutions, a wholly owned subsidiary focused on developing what we describe as an AI continuity control plane for regulated enterprises. Our intention is to create a platform capable of serving as a resiliency, recovery, validation, and compliance lane for sovereign AI infrastructure environments. The platform we envision is designed to detect behavioral anomalies, execute validated recovery sequences, and generated audit-ready documentation that regulated industries may interestingly require as AI becomes embedded into critical business operations. Importantly, we believe our approach is differentiated because it focuses not only on infrastructure restoration, but also on preserving operational integrity, compliance posture at the model and behavioral levels. We also believe the market timing is compelling. Earlier this month, several leading AI developers announced multi-billion dollar initiatives designed to integrate AI deeply into the enterprise-wide workflows, further validating large-scale AI deployment across mission-critical environments is accelerating rapidly. While this market remains early stage and rapidly evolving, we believe long-term opportunity could be substantial. Based on our preliminary analysis, regulatory-driven enterprise AI infrastructure spending could ultimately represent a multi-billion dollar annual market opportunity. At the same time, we are not currently aware of any other purposely built platform targeting compliance-driven AI recovery for regulated enterprises in the matter we are pursuing. Our focus throughout 2026 will be advancing the platform architecture, redefining our go to market strategy, continuing industry engagement discussions, and progressing towards potential initial customer opportunities. We expect to provide additional commercial and operational updates as these initiatives advance throughout the year. At the same time, our Nexus business continues to provide an important operational and financial foundation for DTSC. Nexus remains a stable, recurring revenue business delivering VoIP, dedicated Internet access, SD-WAN, and data transport services. During the first quarter of 2026, Nexus sales increased 10.9% year-over-year, while gross profit increased 32.1% and gross margins expanded to 53.7 compared to 45% in the prior period. We believe these results demonstrate both the continued demand for our connectivity services and operational discipline within the business. Just as importantly, Nexus provides us with a recurring revenue base and operating infrastructure that supports our broader strategic initiatives. Financially, we believe DTSP is well-positioned relative to many companies pursuing emerging technology opportunities. We ended the year with no long-term debt, substantial working capital, significant market securities, and a highly flexible balance sheet. That strength gives us the ability to remain patient, strategic, disciplined on how we allocate capital while SAIS remains our primary strategic initiative. We are also continuing to evaluate complementary opportunities. including partnerships, strategic investments, mergers and acquisitions, and other transactions that could strengthen our competitive position and enhance long-term shareholder value. Ultimately, our goal is to position DTSC at the intersection of enterprise AI infrastructure, resiliency, compliance, and mission-critical continuity areas where we believe demand will continue to expand significantly over the coming years. We appreciate the continued support and confidence of our shareholders, and we look forward to updating everyone on our progress as we move throughout 2026. I'd like to turn it over to Chris Panagiotakos for a review of the financial results. Chris?

Chris Panagiotakos | Chief Financial Officer:

Thank you, Chuck. Good morning, everyone. As previously discussed, on September 11th, 2025, we closed the sale of our Cloud First business for $40 million. As a result of the transaction, and in accordance with auditing and reporting standards, our ongoing financial reporting now reflects only our continuing operations, specifically our Nexus subsidiary. Sales from continuing operations were $347,000 for the three-month end in March 31, 2026, an increase of $34,000, or 10.9%, compared to $313,000 in the prior year. The increase was primarily attributable to continued growth in our Nexus voice and data solutions business, driven by the addition of new customers and increased spending from existing customers. Revenue growth during the period reflects continued demand for our voice and data connectivity solutions and expansion of services within our existing customer base. Gross profit for the three months ended March 31, 2026, was $186,000, an increase of $45,000 or 32.1% compared to $141,000 in the prior period. Salary in general and administrative expenses for the three months ended March 31st, 2026 increased $615,000 or 71.8% to $1.5 million from $857,000 for the three months ended March 31st, 2025. The increase was primarily driven by a $425,000 or 311% increase in non-cash stock-based compensation as a result of grants to certain employees during the three months ended March 31, 2026. Professional fees increased by $135,000 or 73.6%, attributable to higher fees paid relating to legal and consulting services during the period. Net loss attributable to common shareholders for the three months ended March 31st, 2026 was $631,000 compared to net income of $24,000 for the three months ended March 31st, 2025. We ended the quarter with cash, cash equivalents, and marketable securities of approximately $9.7 million at March 31st, 2026. We used $29.5 million of the proceeds from the sales of marketable securities to repurchase common stock from our shareholders in connection with the tender offer which closed on January 15, 2026. Thank you. And I will now turn the call back to Chuck.

Chuck Piluso | Chairman and Chief Executive Officer:

Thanks, Chris. Let's open up the call for some questions.

Operator | Conference Operator:

Thank you. And at this time, we'll conduct a Q&A session. To ask a question, press star 1 on your telephone keypad. A confirmation tone will indicate that your line is in the question queue. You may press star 2 if you would like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the star keys. One moment, please, while we pull for questions. and your first question comes from Matthew Galinko with Maxim Group. Please state your question.

Matthew Galenko | Analyst, Maxim Group:

Hey, good morning. Thanks for taking my questions. As you pursue the AI strategy, I'm curious how you'll pursue, I guess, developing technical solutions to support, you know, the go-to-market. Do you expect to bring developers in-house to the current structure or just curious how you'll approach that?

Chuck Piluso | Chairman and Chief Executive Officer:

Good morning, Matt. Thank you for the question. What we're doing right now is that just to cover it across the board essentially is that we have a recruiter working on finding us someone to run the subsidiary. We are hopefully lining up CTOs that we can interview that may want to start off as a consulting basis. and handle the overall project. We're talking to three, four other companies essentially that want to participate in everything from, you know, us subcontracting to them. to partnerships for them to do the installation. We came across this because we put out a letter of intent to a company a while ago about sovereign AI and looking into this and seeing where the holes are. So in doing that, You know, we started finding out, okay, who are the folks that are installing this sovereign AI? And then as we started looking at this very seriously, we said, well, these are companies that we can use to sub out. So from a US basis, Eastern Europe, and from Indian basis, companies are looking to develop this software that today does not exist. You know, you can do what we did at Cloud First for over 20 years, protecting someone's information and having a runbook to get the companies up and going because regulated companies using the cloud, the proprietary data, they're pretty much building it themselves. So we're really on all fronts at this point. And so we hope to start building a statement of work probably over the next 30 days. And that might involve probably three separate companies, each one having a different discipline. Right now, a number of companies, as I've gone around talking about this, and I'm kind of be somewhat quiet to a degree because, you know, you turn them into competitors. but for the most part we would say there's probably going to be three companies involved with putting this together in the two co-location centers of what our intention would to be but overall you know we have to start with someone that's going to be project management and that's why we have the recruiter going on because there'll be a lot going on but we've done it before with 10 data centers in three countries. It's very similar to that but the software to flip it over when there's Thank you very much. make it look like it was almost cloud first but on the GPU side and everything that goes along GPU and storage and the second stage of it will be building the software all along to be able to have it flip over and act behaviorally the same way. Behavioral point objective, behavioral time objective. This is very, very much similar that we did with Cloud First, but it's GPUs, and they are different. There will be multiple companies involved. I'm sorry, a short question, a very long answer, but there will be multiple companies that we're talking to today.

Matthew Galenko | Analyst, Maxim Group:

Sure, I appreciate all the color. It's helpful to kind of conceptualize what you're doing. Maybe just as a follow-up, Obviously, I think you have a better sense of timing than we do, but will we start to see expenses ramp up maybe in the second quarter or more in the third quarter around the initiative? And so will we see that starting to hit the P&L or would investments be capitalized and we won't necessarily see it on the P&L? Just curious how the participation might look or as it's looking today and if that's the right timeline to think about.

Chuck Piluso | Chairman and Chief Executive Officer:

Sure. Well, rounding our money, we have, let's say, $10 million in the bank. You know, we have some escrows going on still from the Minovas sale. We just settled one on the networking capital with them and have, you know, $700,000 that, you know, we have, you know, have come in or coming in over the last week or so. so we do have some cash the board approved at a recent board meeting for us to go out and explore this and line it completely up with all the pieces that are needed but I think that it will hit the cash but you know it won't be I don't want to use the word significant I can't imagine us spending more than 250 to 300,000 on being able to get it to the point of our statement of work part before we say go. When we say go, it's going to be capital expenses. Those capital expenses will be depreciated over five years for the most part. So the big hit on the cash, you know, I think most of it would be capital. The software development and all of that, we'll see how we can make arrangements. But that'll probably be the part that'll be just unknown at this particular point, frankly, on the software side. But there'll be capital expenditures going on. But I think we have enough money to implement this and still have a couple-a-year run if revenue wasn't generated. But we're hoping to take... hopefully taking agreements in the first quarter of 27, maybe earlier, of which I'll call reservations versus subscription, but they'll all be recurring revenue.

Matthew Galenko | Analyst, Maxim Group:

Yeah, that makes sense. And maybe, and last question, then I'll jump back in the queue, but you know, I guess referring to that you know, not a subscription, I guess that kind of speaks towards, you know, figuring out what capacity you need and, you know, relative to how many customers you have and what their demands are. But can you talk a little bit how you're thinking about, you know, how far ahead of, you know, demand that you need to build out capacity and how access to GPUs and data center space might look as you, you know, progress over the next few quarters?

Chuck Piluso | Chairman and Chief Executive Officer:

Well, I'm going to say the next one or two quarters we'll just be setting everything all up, hopefully having it all in place, you know, by the end of the year. What's interesting about it is that we wouldn't be into this, let's keep buying more and more GPUs, spending $50 billion that you're seeing, you know, that's going on. That's not the play here. The play is essentially to use just a... An example, take a mid-sized hospital. A mid-sized hospital, let's say they're going to spend a million dollars and set up their environment. They're going to run logistics for an operating room where they're pharmaceutical and they're building this critical. They might have subscribed to software. They didn't build it. You know, they install it and it keeps learning and becoming more intelligent. Well, what are they going to spend to get to the other side to have the compliance in Casablanca Oxfam? All these things that no one's talking about yet. So now are you going to double that capex or do you want to go to a service bureau? And we don't believe NVIDIA is going to build a service bureau, by the way, you know, or Corweave and people like that. They could do it. They're not really focused on it. But for the most part, they now need to have the ability to be able to recover. And so... When we talk about this recovery piece, the return on investment seems significant for them. So I would say that when we're looking at this, a mid-sized hospital is going to need to be able to be compliant, their confidential information sitting on their storage remotely, and we have runbooks. but at some point it needs to flip over and act the exact same way and recover. So, you know, I don't know if I'm answering that question completely but that's kind of the model that you're looking at. That could be insurance companies as well, financial institutions. Does that answer your question Matt? I'm not sure.

Matthew Galenko | Analyst, Maxim Group:

It helps. I guess to clarify, you know, I guess when you were hosting you know, cloud first and disaster recovery there. You had an idea of how much capacity you needed, but, you know, taking the million-dollar environment at a mid-size hospital, what would be the, you know, I assume you'll have enough capacity, you know, are you spending one to five so your environment would support five? And, you know, how do you balance the investment of, you know, customer needs to failover? in the GPU environment versus how much overcapacity you want to build.

Chuck Piluso | Chairman and Chief Executive Officer:

Well, the first thing I think we know by now after all these years providing business continuity is that a hospital is going to run this application or multiple applications to improve efficiency and all of that, and they're going to depreciate this equipment over three to five years. That hospital is not going to be in the race to add more and more GPUs and more and more GPUs. So we don't see the growth there. So we don't see them continue to build upon that at the rates that we're seeing, you know, folks spending $50 billion. So we can match their equipment on our side. So let's just say, for example, that they want to recover within 15 minutes. Well, that's going to be a higher level service, and that's not going to run a ratio. That's going to be one to one for them. And that's going to be, you know, what we would call high availability in a regular sense. Then there's another layer underneath there, like you're mentioning, Matt, where you're going to run a five to one ratio and eight to one ratio. The one things we learned during 9-11 with cloud first, you know, and then other disasters and storms that all happen is that things can happen geographically within a particular region. So if you run too high of a ratio, you can't support it. So it needs to be coming from different geographies on that. But I would assume that a 5 to 1 ratio would be successful as long as you could probably run a 10 to 1 ratio as long as the 10 are in all different parts of the United States. But I would say on standby type service where you have run books and all of that, I would say that probably 5 to 1 would be a good ratio.

Matthew Galenko | Analyst, Maxim Group:

Very helpful, thank you.

Operator | Conference Operator:

Your next question comes from Ellen Lipsack with Forth Capital. Please state your question.

Ellen Lipsack | Analyst, Forth Capital:

Yes, hi, and thank you so much for taking my question. Can you elaborate on the market opportunity you see for the silver and AI solutions and, you know, why you think now is the right time to enter the space?

Chuck Piluso | Chairman and Chief Executive Officer:

Sure, thanks, Ellen. The right time. it could be early on it but if it takes us six months when all of a sudden we believe that when everyone starts everyone looks at AI as a general population of the world now as they go into chat GPT and they ask a question or Claude and say design this and design that the fifth layer of this AI is the business process and and that's the software being developed and so these 150 executives that OpenAI is putting in place that was in a press release, you know, is going out to actually build this software. As this software gets deployed, they're going to need to be compliant the same way all the CPUs have to be compliant, you know, in industry, that they're using best practices. Today, that's not in existence. It might be all happening in one data center. So I think it's a matter of time before compliance and regulation start, you know, surrounding as more and more organizations, regulated organizations are deploying these types of software and services to make them more efficient, to learn better, reduce staff, whatever they're thinking. But that's why these 150 people are being hired because, you know, companies are interested. The talent is lacking on it. And we're there to be able to go up to sovereign AI to say, will you put this in place? How compliant are you? No one, I don't believe anyone's asking that question. And we've been talking to a lot of people. So everyone's focused on learning, training the models, installing equipment, testing it, but they're not there on compliance. and all the regulations that went on over the previous years. And that's why I believe it's a very solid business model.

Ellen Lipsack | Analyst, Forth Capital:

So, that makes sense. That kind of leads into my next question. What do you think really differentiates the, you know, sovereign AI solutions from traditional disaster recovery, cybersecurity or, you know, any enterprise infrastructure providers currently in the market?

Chuck Piluso | Chairman and Chief Executive Officer:

I think it's the same thing. Essentially, you could say it's the same thing, but none of the folks that are today in disaster recovery that we know that our research came up with are doing anything like this. Whether they're planning that, I'm not exactly sure, but there's enough room in it. Some of the ratios I've seen is that this is going to be somewhere around 5% to 10% of anyone that's putting sovereign AI in place. Some numbers I've seen and it's very tough when you start looking at market numbers is that it's, you know, sovereign AI is around a $50 billion total addressable marketplace and 10% is what some of the numbers that I've seen for this type of thing. But they're rough calculations and I wouldn't hold me to it, but I know this is a solid feeling that this is coming. And I do believe that the folks that are in this business that Cloud First competed with will eventually move into this. I think we might have a Head Start on it, and I think that that's important, but there's enough room with five or six competitors. But right now, if we get this up by the end of the year and we start talking to people in the fourth quarter, I think we'll have a little bit of a lead. Because of our background, we know about escalation risk. We know how to do that. We were doing that. We know how to have run books. and all the things that went on with that. So we do understand, you know, all of that and I think it fits in really, really well with this. But we saw the whole, you know, we saw that come up because we see what's going on with sovereign AI and AI factories. I heard some numbers from Dell of proposals outstanding. They were just some large numbers. So I'm pretty excited about it.

Ellen Lipsack | Analyst, Forth Capital:

Definitely very exciting. and I guess in terms of the development timeline and then the potential commercialization path for sovereign AI, what does that look like over the next 12 to 24 months?

Chuck Piluso | Chairman and Chief Executive Officer:

Everything's about execution. We all know that. So initially, we were going to try to do everything, you know, and then launch and then studying it some more, we felt maybe the thing to do is to do a two-stage approach. Let's get this up and going. without the behavioral side of it. So that, you know, these regulated organizations, they can be protected, but it's going to be different. It might not move over the exact same way right away behaviorally. You have the runbook and all of these things, but The first stage will be to stand it up, start taking reservations, if I want to call it reservations instead of subscription, and get it moving so they can start testing and coming over to us. And then from the very beginning, let's just say within 60 days, software starts to get developed. So by the time everything gets deployed on the hardware side, staffing is in place, you know, hopefully it's not going to take more than nine months. There's some software out there that you can work with, but a lot has to be developed. So it just doesn't exist. We dealt with this with our IBM systems with Precisely that did a roll-up of all the software companies we used for 15 plus years. And we think there'll be very, very good value in owning this software as well. But that's kind of the timeline, I think.

Ellen Lipsack | Analyst, Forth Capital:

Got it. Okay. So that's great. And are you currently evaluating any like strategic partnerships, acquisitions, or maybe even like investments that could potentially accelerate this AI infrastructure strategy?

Chuck Piluso | Chairman and Chief Executive Officer:

I originally wanted to do, and I still may, we still may, a joint venture. Folks that are already set up that are installing sovereign AI today and to do a joint venture because they have the staff already in place. and they have the knowledge of it. And it's great for them and not become an automatic partner because, you know, they're installing AI factories and sovereign AI. But we are talking to folks to be partners. One of the problems, you know, Alan, is that when you're small, a lot of times you're not going to be able to get larger organizations to go with you because, you know, that credibility is not there. They want to see a billion-dollar company. Even though the billion-dollar company can be insolvent, you know it's just for the most part they want to see the very large scope so typically working through partners and that's how we did it at Cloud First as well you know when you get that very large deal you know you're bringing a partner on it but we are looking at joint ventures we're looking at partnerships We're not really looking at investments at this time. We don't care if that's necessary, frankly. I think we can do this with money in our bank and still leave a two-year run rate because, you know, the public company is expensive. It runs probably around, you know, I'd say $1.8 to $2 million a year. But I think we have enough. I think we have enough to pull this off. But I'll know more over the next 90 days. We're trying to move pretty fast with it.

Ellen Lipsack | Analyst, Forth Capital:

Oh, no, this is super helpful. Thank you so much for taking my questions. I really appreciate it, Chuck, and if I have any other questions, I'll jump back in the queue.

Chuck Piluso | Chairman and Chief Executive Officer:

That's great. Thank you, Alan.

Operator | Conference Operator:

Thank you, and our next question comes from Matthew Galenko with Maxim Group. Please state your question.

Matthew Galenko | Analyst, Maxim Group:

Hey, appreciate you taking another one from me. Just wanted to check in on Nexus and kind of the current revenue generator for the business. I think you had decent annual growth in the first quarter here. Any opportunities to, you know, how do you see that business trending over the rest of this year? Do you have an opportunity to, you know, accelerate that in any capacity? And, you know, do you see it continuing to add to, you know, kind of cut into the burn rate, I guess, as it grows?

Chuck Piluso | Chairman and Chief Executive Officer:

You know, Matt, the gross margins are great. We have put some money into Nexus. They're not a large staff. John Canelo, who's the president of that, he owns 20% of that company. John and his staff do an excellent job. John continues to look for... business development types to accelerate it. And I know that he's trying to recruit, you know, as we speak right now, he's trying to recruit business development folks to go. It's very, very difficult, the organic growth, but they're doing a great job with it. We looked at one or two acquisitions to roll it into that company. And we're still looking at that. But I think if John gets successful with getting the right, he is successful with getting the right people on to grow that. I also believe, Matt, that, you know, because they're very limited with manpower, that getting a digital agency to start getting inbound leads going is one of the things that we've been talking about. Cloud First had a great flow of leads. Harold Schwartz did a great job with the digital agency and everything that he did on that to get significant leads coming in. And so we need that to happen and then these business development folks to work on that because no one's answering the phone, no one's letting you in the building. So John does a great job and his staff with association meetings and organizations and sponsorships, things like that. But, you know, that next step, I think, is for Chris to free up some money for him to get, you know, the website going where he can get an inflow of the way that cloud first. And I think that's the next stage. but he is trying to recruit the folks in the distance development area. He needs the help there because he's got great margins and does a good job, has a great product. The product is great.

Matthew Galenko | Analyst, Maxim Group:

Great. Thank you.

Operator | Conference Operator:

Thank you. There are no further questions at this time so I'll hand it back to Chuck Piluso for closing remarks.

Chuck Piluso | Chairman and Chief Executive Officer:

Thank you. Thank you for the questions. There were very deep questions, some of them, and, you know, Ellen, they were great. Hopefully, shortly, we'll be back to everyone, but thank you for the questions. In closing, we believe the foundation we've established over the decades of execution and value creation has positioned DTST to pursue a unique opportunity at the intersection of enterprise AI, resiliency, and regulated infrastructure. Our strategy is supported by financial strength, operational stability, and what we believe is a differentiation of long-term vision for AI continuity infrastructure. As the market continues to evolve, our focus remains on a disciplined execution, strategic flexibility, and creating substantial long-term value for our shareholders. We really do appreciate everyone's continuous support and our shareholders and look forward to sharing additional updates as we progress. Thank you.

Operator | Conference Operator:

Thank you. And with that, we conclude today's call. All parties may disconnect. Have a good day.