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Vuzix Corporation (NASDAQ: VUZI)

January 11, 2023

Buy: Multiple OEM Orders Close out 2022.

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Vuzix closed out 2022 with multiple OEM orders from defense and commercial customers. We expect this to be a source of significant growth over time. We reiterate our Buy recommendation and \$15 price target.

Vuzix closed 2022 delivering on multiple defense and commercial OEM orders, some of which continue into 2023. We also believe some of these will turn to volume production. Defense and aerospace contracts have long development times and long production cycles as well, and in our view are an attractive growth avenue for the company. Vuzix has received orders for waveguides and displays from a multinational electronics contract manufacturer for development of AR-based glasses.

Commercial opportunities could be catalyzed by Apple's long-awaited entry into the market with an [AR/VR headset](#). Vuzix offers an ultralite smartglass system for the OEM market that utilizes the company's proprietary waveguide solution and custom microdisplay engine. A consumer smartglass solution is being pursued by many of the major tech companies including Meta, Apple and Alphabet. We expect a robust market will emerge over the coming years and Vuzix is positioning itself to serve that space.

In the defense market, the company has development deals with a handful of major defense contractors on waveguide-based products. Lead times can be extended, but once deployment begins production runs can be long and very profitable. We estimate typical production contracts could generate \$10 to \$15 million over a multi-year time frame. Vuzix is also working with multiple customers on supplying waveguides for the consumer market. There is upside to our sales projections from these waveguide projects.

The company has unique expertise in waveguide design and manufacturing and is expanding its waveguide capacity both in response to customer indications of interest and to make itself the number-one choice of waveguides in the OEM market for industrial and consumer use. This investment is modest, a few million dollars, and will expand capacity, lower costs and enable a more robust feature set than the current product. We believe Vuzix can be one of the leading suppliers of waveguides and that this investment will enhance that capability.

Price Target Methodology. Our \$15 price target values the company's smart glasses and waveguide businesses at a significant discount to recent market transactions in the smart glasses space of \$775M to \$2B and \$500M to \$542M in the waveguide market (see page 2).

Risk Analysis Risks to achieving our price target include continuing negative impacts of the COVID-19 pandemic on the overall economy, changes to business practices in the medium and long-term due to the COVID-19 pandemic, potential competition from Apple and Facebook, increased competition from Google and RealWear, ability to deliver new products on time and manufacturing costs as sales ramp.

Current Price				\$4.41
Price Target				\$15.00
Estimates	F2021A	F2022E	F2023E	
Revenues (\$M's)	\$ 13.2	\$ 12.4 E	\$ 20.5	
1Q March	\$ 3.9	\$ 2.5 A	\$ 4.6	
2Q June	\$ 2.9	\$ 3.0 A	\$ 5.1	
3Q September	\$ 3.0	\$ 3.4 A	\$ 5.1	
4Q December	\$ 3.3	\$ 3.5 E	\$ 5.6	
	F2021A	F2022E	F2023E	
EBITDA (\$M's)	\$ (20.4)	\$ (22.0)E	\$ (21.1)	
1Q March	\$ (3.9)	\$ (5.6)A	\$ (5.5)	
2Q June	\$ (4.6)	\$ (5.5)A	\$ (5.3)	
3Q September	\$ (5.7)	\$ (5.4)A	\$ (5.3)	
4Q December	\$ (6.2)	\$ (5.5)E	\$ (5.1)	
EV/Sales	NM	15.3 x	9.3 x	
EV/EBITDA	NM	(8.7) x	(9.1) x	
Stock Data				
52-Week Range	\$3.27 -			\$10.49
Shares Outstanding (mil.)	63.7			
Market Capitalization (mil.)	\$281			
Enterprise Value (mil.)	\$191			
Debt to Capital	0%			
Cash & Equivalents (mil.)	\$90.4			
Cash/Sh.	\$1.42			
Average Three Months Trading Volume (K)	531			
Insider Ownership	6.8%			
Institutional Ownership	41.4%			
Short interest (mil.)	23.0%			
Dividend / Yield	\$0.00/0.0%			


Please find Important Disclosures beginning on Page 5.

Valuation

Our price target is based on recent market transactions in the smart glasses and waveguide markets. These are two distinct markets, and Vuzix has important and meaningful positions in both of them.

In the smart glasses market, Pico Interactive was acquired by ByteDance (parent of TikTok) in August of 2021 for a [reported](#) \$775 million. In October of 2021, Magic Leap raised \$500 million at a [reported](#) \$2 billion valuation. The average of these two transactions is \$1.4 billion. Financial data for each is not available, but we believe revenue for Magic Leap is minimal.

In the waveguide market, DigiLens raised \$50 million in November 2021 at a [\\$500 million valuation](#) and in May of 2021 Snap purchased Wave Optics for cash and stock [totaling \\$541.8 million](#). The average of these transactions is \$521 million. Revenue is not available for either of these companies but we believe they are minimal. Snap has [stated](#) revenue from Wave Optics was not material relative to its results.

Meta investing billions and billions shows it will take time and dollars to make the market.

Combining the average transaction value of \$1.4 billion for smart glasses with the \$521 million average transaction value for waveguides results in a combined target of \$1.9 billion, or \$30 per share after adjusting for the company's \$129 million cash balance. However, we have discounted this sharply, to \$10, to reflect the risk of competition by larger and better-capitalized competitors, the time it may take to bring products to market, the risks COVID has for the growth of the economy and potential Federal Reserve actions to combat inflation.

Risk Analysis

Risks to achieving our price target include continuing negative impacts of the COVID-19 pandemic on the overall economy, changes to business practices in the medium and long-term due to the COVID-19 pandemic, potential competition from Apple and Facebook, increased competition from Google and RealWear, ability to deliver new products on time and manufacturing costs as sales ramp.

Exhibit 1. Income Statement

(\$ in 000's except per share data)

	2019	2020	2021	Q1 22 A	Q2 22 A	Q3 22 A	Q4 22 E	2022 E	2023 E
Total Sales	\$ 5,997	\$ 11,581	\$ 13,165	\$ 2,503	\$ 3,008	\$ 3,427	\$ 3,500	\$ 12,438	\$ 20,500
Total COGS	11,079	9,654	10,714	1,864	2,582	2,559	2,512	9,294	14,246
Total Gross Profit	(4,408)	1,928	2,451	639	426	868	988	2,922	6,254
R&D	8,901	7,568	11,675	3,103	2,996	3,441	3,441	12,981	14,795
Sales & Marketing	4,216	4,040	6,119	2,023	1,851	1,981	1,981	7,836	8,701
G&A	6,600	6,915	22,503	5,454	5,040	4,854	5,250	20,598	20,481
D&A	2,442	2,458	1,870	423	540	510	449	1,922	1,794
Other	0	74	264	50	0	48	0	98	0
Operating Expense	22,158	21,055	42,431	11,053	10,427	10,834	11,120	43,434	45,771
Operating Income	\$ (26,566)	\$ (19,127)	\$ (39,980)	\$ (10,414)	\$ (10,001)	\$ (9,965)	\$ (10,132)	\$ (40,512)	\$ (39,517)
Interest & Other	90	1,175	(397)	(92)	(21)	488	488	864	(76)
Pretax Income	\$ (26,476)	\$ (17,952)	\$ (40,377)	\$ (10,506)	\$ (10,022)	\$ (9,477)	\$ (9,643)	\$ (39,648)	\$ (39,593)
Income Taxes	0	0	0	0	0	0	0	0	0
Net Income	\$ (26,476)	\$ (17,952)	\$ (40,377)	\$ (10,506)	\$ (10,022)	\$ (9,477)	\$ (9,643)	\$ (39,648)	\$ (39,593)
Preferred Dividends	(1,932)	(2,056)	0	0	0	0	0	0	0
Net to Common	\$ (28,408)	\$ (20,008)	\$ (40,377)	\$ (10,506)	\$ (10,022)	\$ (9,477)	\$ (9,643)	\$ (39,648)	\$ (39,593)
Diluted Shares	30,348	38,110	61,125	63,695	63,740	63,776	63,740	63,738	65,111
EPS	\$ (0.94)	\$ (0.53)	\$ (0.66)	\$ (0.16)	\$ (0.16)	\$ (0.15)	\$ (0.15)	\$ (0.62)	\$ (0.61)
Operating Income	\$ (26,566)	\$ (19,127)	\$ (39,980)	\$ (10,414)	\$ (10,001)	\$ (9,965)	\$ (10,132)	\$ (40,512)	\$ (39,517)
D&A	2,542	2,642	2,310	483	611	732	732	2,558	2,927
Stock Comp	1,498	2,806	17,303	4,320	3,881	3,881	3,881	15,963	15,524
EBITDA	\$ (22,526)	\$ (13,680)	\$ (20,368)	\$ (5,611)	\$ (5,509)	\$ (5,353)	\$ (5,519)	\$ (21,991)	\$ (21,065)

Source: Vuzix Corporation and Dawson James Securities estimates

Exhibit 2. Balance Sheet and Cash Flow Statement

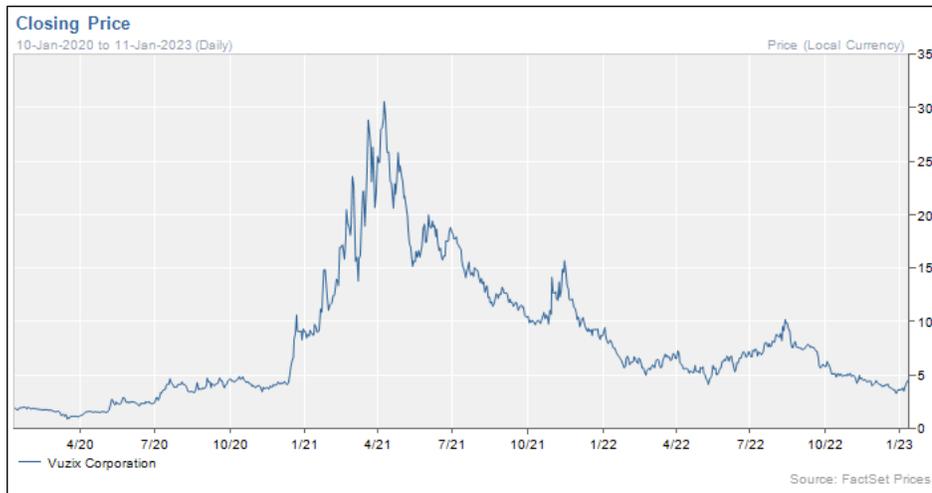
(\$ in 000's)

	2019	2020	2021	2022 E	2023 E
Cash	10,606	36,070	120,204	76,481	37,220
A/R	1,372	1,389	2,242	2,301	3,699
Note Receivable	250	0	0	0	0
Revenue in excess of billings	0	0	0	393	393
Inventory	5,708	6,101	12,152	10,046	12,357
Prepaid Expenses & Other	1,138	1,496	2,552	2,958	4,753
Current Assets	\$ 19,074	\$ 45,055	\$ 137,150	\$ 92,179	\$ 58,422
Tooling & Equipment	4,328	2,837	5,190	10,292	10,365
Operating Lease Right of use	2,096	1,517	1,117	708	708
Patents & Trademarks	1,295	1,593	1,988	2,141	2,141
Licenses, net	314	194	1,390	24,657	58,907
Intangible Assets & Other	1,340	1,275	1,631	3,692	3,592
Total Assets	\$ 28,446	\$ 52,471	\$ 148,467	\$ 133,669	\$ 134,135
Accounts Payable	1,063	1,517	2,055	2,243	3,606
Unearned Revenue	142	41	28	25	40
Accrued Expenses	886	983	1,419	1,199	1,928
Licensing Fees Commitment	0	0	0	4,250	6,250
Operating Lease Right of use	525	444	534	526	526
Current Liabilities	\$ 2,635	\$ 3,095	\$ 4,156	\$ 8,291	\$ 12,426
Operating Lease Right of use	1,571	1,073	583	182	182
Licensing Fees Commitment	0	0	0	4,750	0
Equity	24,240	48,303	143,728	120,446	121,527
Total Liabilities & Equity	\$ 28,446	\$ 52,471	\$ 148,467	\$ 133,669	\$ 134,135
	2019	2020	2021	2022 E	2023 E
Net Income	\$ (26,476)	\$ (17,952)	\$ (40,377)	\$ (39,648)	\$ (39,593)
D&A	2,542	2,642	2,310	2,558	2,927
Stock Comp	1,498	2,806	17,303	15,963	15,524
Other	4,673	41	784	123	(4,650)
Working Capital	(4,591)	(1,501)	(6,999)	1,141	(1,369)
Operating Cash Flow	\$ (22,355)	\$ (13,964)	\$ (26,980)	\$ (19,864)	\$ (27,161)
CapEx	(1,899)	(497)	(3,809)	(6,704)	(3,000)
Other	(1,259)	(989)	(1,043)	(15,488)	(11,500)
Investing Activities	\$ (3,158)	\$ (1,486)	\$ (4,852)	\$ (24,192)	\$ (14,500)
Equity	18,855	39,357	127,112	397	2,400
Debt	0	1,556	0	0	0
Other	0	0	(1,144)	0	0
Preferred	0	0	(10,000)	0	0
Financing Activities	\$ 18,855	\$ 40,913	\$ 115,967	\$ 397	\$ 2,400
Change in Cash	\$ (6,658)	\$ 25,463	\$ 84,134	\$ (43,658)	\$ (39,261)

Source: Vuzix Corporation and Dawson James Securities estimates

Important Disclosures:

Price Chart:



Price target and ratings changes over the past three years:

Initiated – Buy – December 21, 2021 – Price Target \$15.00
 Update – Buy – January 6, 2022 – Price Target \$15.00
 Update – Buy – March 4, 2022 – Price Target \$15.00
 Update – Buy – May 11, 2022 – Price Target \$15.00
 Update – Buy – May 19, 2022 – Price Target \$15.00
 Update – Buy – July 6, 2022 – Price Target \$15.00
 Update – Buy – July 18, 2022 – Price Target \$15.00
 Update – Buy – August 3, 2022 – Price Target \$15.00
 Update – Buy – August 10, 2022 – Price Target \$15.00
 Update – Buy – November 2, 2022 – Price Target \$15.00
 Update – Buy – November 10, 2022 – Price Target \$15.00
 Update – Buy – November 17, 2022 – Price Target \$15.00
 Update – Buy – January 11, 2023 – Price Target \$15.00

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- 1) **Buy:** the analyst believes the price of the stock will appreciate and produce a total return of at least 20% over the next 12-18 months;
- 2) **Neutral:** the analyst believes the price of the stock is fairly valued for the next 12-18 months;
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Current as of 5-Jan-23

	Company Coverage		Investment Banking	
Ratings Distribution	# of Companies	% of Total	# of Companies	% of Totals
Market Outperform (Buy)	22	71%	1	5%
Market Perform (Neutral)	8	26%	1	13%
Market Underperform (Sell)	1	3%	0	0%
Total	31	100%	2	6%

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