22nd Century Group, Inc. (NASDAQ: XXII)

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Buy: CEO Change, Cost Cutting Capital Raise.

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22nd Century announced the resignation of CEO James Mish, a $15 million annualized cost-cutting program and an $11.7 million capital raise. We have adjusted our expense estimates, share count, and future capital raises to reflect these events. We have also adjusted our price target to reflect the greater share count.

Current Price			**$3.13**
Price Target			**$10.00**
Estimates	F2022A	F2023E	F2024E
Revenues ($M's)	$ 62.1	$ 103.0 E	$ 192.5
1Q March	$ 9.0	$ 22.0 A	$ 35.0
2Q June	$ 14.5	$ 23.0 E	$ 45.0
3Q September	$ 19.4	$ 26.5 E	$ 52.5
4Q December	$ 19.2	$ 31.5 E	$ 60.0
	F2022A	F2023E	F2024E
EBITDA ($M's)	$ (39.7)	$ (47.2)E	$ 15.7
1Q March	$ (6.5)	$ (14.9)A	$ (1.3)
2Q June	$ (7.1)	$ (13.2)E	$ 2.6
3Q September	$ (11.0)	$ (12.5)E	$ 5.4
4Q December	$ (15.0)	$ (5.7)E	$ 9.1
EBITDA ($Ms)	$ (39.7)	$ (47.2)	$ 15.7
EV/EBITDA (x)	-1.2x	-1.0x	2.9x
Stock Data			
52-Week Range	$2.19	-	$31.58
Shares Outstanding (mil.)			21.1
Market Capitalization (mil.)			$66
Enterprise Value (mil.)			$46
Debt to Capital			16%
Cash (mil.)			$41.9
Cash/share			$1.99
Average Three Months Trading Volume (K)			47
Insider Ownership			3.0%
Institutional Ownership			17.4%
Short interest (mil.)			5.3%
Dividend / Yield			$0.00/0.0%

CEO James Mish has resigned as CEO, to be replaced by John Miller, who leads the company's tobacco unit. The move could indicate greater focus on the tobacco business which we expect will be aided by a potential FDA menthol ban and low-nicotine mandate. Tobacco stocks trade at EV/Sales multiple of 3x to 5x, and as the company's tobacco sales increase, we believe the multiple can as well. Currently the shares trade at less than 1x 2023 estimated sales and about 50% of 2024 estimated sales.

The depressed multiple of sales, we believe, is a reflection of low gross margin in both the hemp and tobacco segments as well as an uncertain path to positive operational cash flow and the cash needed to get there. We expect gross margin to show noticeable improvement in the coming quarters from both the hemp and tobacco units, and the $15 million annualized cost-cutting program should result in sharply improved cash flow and positive operational cash flow by mid-year 2024.

The $11.7 million capital raise, combined with two smaller raises totaling $4.8 million, and additional insurance settlements from the Grass Valley fire, will put the company's pro forma cash balance (using the Q1 ending cash balance of $16.2 million) at about $33 to $37 million. This should cover the company's operating cash flow needs for the remainder of the year.

There is also potential cash available from the exercise of about 11 million warrants with a strike of $2.42 per share. This would raise an additional $27 million which we assume occurs in the first half of next year.

The share count is now 21 million and if the $2.42 warrants are exercised the company is near the 33.3 million authorized share limit. If necessary, the company could get approval to increase its authorized shares but we think the path or lesser resistance would be additional cost-cutting to reach cash flow break-even.

Valuation: Our $10.00 price target (down from $15) is based on a multiple of sales of about 1.5x our 2024 revenue estimate of $192 million and assumes a 32 million share count, after the warrant exercise. The multiple range is consistent with other companies in the space, but as margins and cash flow improves, we expect the multiple can increase.

Risks to Target: Our price target assumes success in VLN launches this year and this could take longer than estimated, and/or its partner could demand different terms than assumed. We assume significant margin expansion in both the tobacco and hemp segments which will be driven partly by capacity utilization. Our forecasted growth in the company's hemp segment this year could be impacted by price pressures.

We expect significant operational improvement over the coming quarters as the company's VLN business expands into 18 states serving 56% of total cigarette sales and its CBD business expands from CDMO agreements with Cookies, Old Pal. The VLN business is expanding with launches in Illinois, Colorado, New Mexico, Utah, Arizona, Florida, Texas and California. The company has agreements with Circle K in the Four Corner States and the largest C-Store operator in the nation (7-11, according to C-Store News) in California, Texas and Florida. The company estimates these eight states sell about 240 million cartons of cigarettes annually, and to achieve cash flow breakeven 22nd Century needs to sell about 1.2 million cartons annually, or a market share of 0.5%. With data showing 1% share is possible, we expect the company to achieve its goal of cash flow breakeven by the middle of next year.

By the end of Q2 22nd Century was distributing its VLN cigarettes in 10 markets addressing about 30% of the U.S. market and expects to operate in 18 markets addressing over 50% of the U.S. market by year end. The company needs to sell about 1.2 million cartons per year, or less than 0.5% of the addressable markets in those states to reach cash flow breakeven. The company is targeting the second half of next year for that event. Results in pilot markets point to a 1% market share potential in a short period of time and growing from there. As the company grows its distribution reach over the coming quarters, cash flow from VLN is expected to increase rapidly.

We expect hemp/cannabis revenue to grow meaningfully over the course of the year from Q1's $13 million to over $15 million in Q4 and doubling by the end of 2024. Margins will improve with the resumption of distillate production Q2/Q3 and isolate production in Q4/Q1 24. The company has announced two CDMO agreements with Cookies and Old Pal which it estimates could contribute over $45 million annually in sales. Also, we expect improved mix and margins as distillate and isolate capacity comes on line. Our margin forecast for the hemp/cannabis segment is below what the company expects, which could lead to upside in our EBITDA estimates as early as Q3 of this year.

The company has guided to revenue this year of $105 to $110 million. At the midpoint, this is 73% higher than revenue in 2022 and we estimate sales in 2024 of $192 million and positive EBITDA in Q2.

Exhibit 1. Income Statement

($ in 000's except per-share data)	2020	2021	2022	Q1 23 A	Q2 23 E	Q3 23 E	Q4 23 E	2023 E	2024 E
Revenue	$ 28,111	$ 30,948	$ 62,111	$ 21,962	$ 23,000	$ 26,500	$ 31,500	$ 102,962	$ 192,500
Cost Of Goods Sold	26,673	28,879	60,937	23,139	22,550	24,920	26,935	97,544	139,750
Gross Profit	1,438	2,069	1,174	(1,177)	450	1,580	4,565	5,418	52,750
	5.1%	6.7%	1.9%	-5.4%	2.0%	6.0%	14.5%	5.3%	27.4%
R&D	4,128	3,274	6,561	1,517	1,517	1,517	1,517	6,068	6,400
G&A	14,971	25,881	44,517	14,231	14,231	14,587	10,837	53,886	38,826
Other	176	78	7,202	898	0	0	0	898	0
Depreciation & Amort.	1,346	1,248	0	0	0	0	0	0	0
Opex	20,621	30,481	58,280	16,646	15,748	16,104	12,354	60,852	45,226
Operating Income	$ (19,183)	$ (28,412)	$ (57,106)	$ (17,823)	$ (15,298)	$ (14,524)	$ (7,789)	$ (55,434)	$ 7,524
Interest and other, net	(490)	(4,183)	(3,129)	(359)	(659)	(659)	(659)	(2,335)	(2,634)
Pretax Income	(19,673)	(32,595)	(60,235)	(18,182)	(15,957)	(15,182)	(8,447)	(57,768)	4,890
Income Tax Expense	38	14	(434)	0	0	0	0	0	0
Net to Common	$ (19,711)	$ (32,609)	$ (59,801)	$ (18,182)	$ (15,957)	$ (15,182)	$ (8,447)	$ (57,768)	$ 4,890
Shares (000)	9,254	10,414	12,856	14,386	15,185	18,489	21,078	17,284	30,679
EPS	($2.13)	($3.13)	($4.65)	($1.26)	($1.05)	($0.82)	($0.40)	($3.34)	$0.16
D&A	1,346	1,248	2,858	881	881	881	881	3,524	3,524
Stock Comp	1,654	3,983	5,489	1,175	1,175	1,175	1,175	4,700	4,700
Other	176	0	9,065	898	0	0	0	0	0
EBITDA	$ (16,007)	$ (23,181)	$ (39,694)	$ (14,869)	$ (13,242)	$ (12,468)	$ (5,733)	$ (47,210)	$ 15,748

Source: 22nd Century Group, Inc. and Dawson James Securities estimates

Exhibit 2. Balance Sheet and Cash Flow Statement

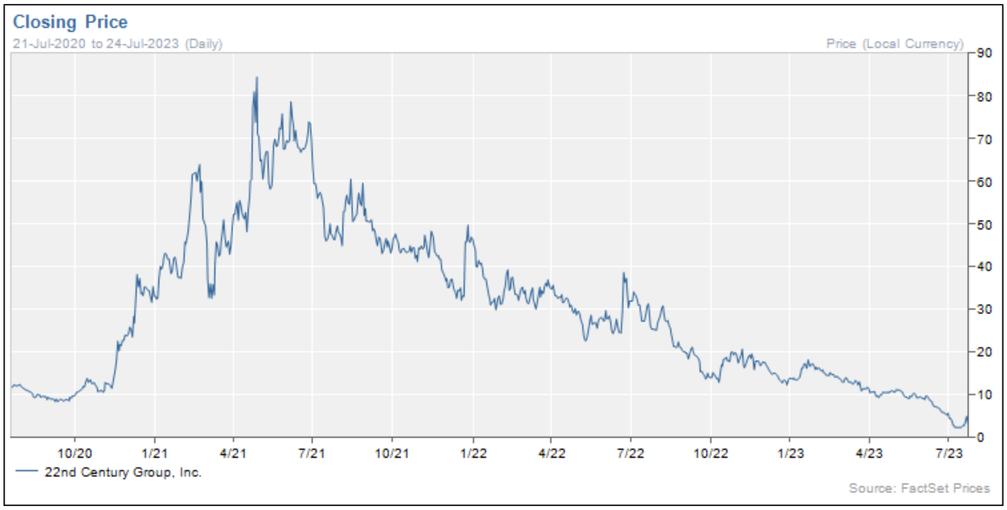
($ in 000's)	2020	2021	2022	2023 E	2024 E
Cash & ST Investments	22,342	48,736	21,213	991	25,798
A/R	2,159	585	5,641	13,097	24,946
Inventory	2,034	2,881	10,008	12,255	18,882
Insurance Recovery	0	0	5,000	0	0
Prepaid Exp.	1,806	2,183	2,743	2,252	2,252
Total Current Assets	**$ 28,341**	**$ 54,385**	**$ 44,605**	**$ 28,595**	**$ 71,878**
PP&E	2,483	5,841	13,093	15,918	18,046
Operating Lease	247	1,723	2,675	5,309	5,309
Goodwill	0	0	33,160	33,160	33,160
Patent, Trademark, other intangibles	8,211	7,919	16,853	17,521	16,369
Equity Investment	6,536	2,345	682	682	682
Restricted Cash				7,500	7,500
Other Assets	5,876	3,741	3,583	3,642	3,642
Total Assets	**$ 51,694**	**$ 75,954**	**$ 114,651**	**$ 112,327**	**$ 156,586**
Bank Loans and N/P	539	596	908	314	314
Operating Lease	247	308	681	862	862
A/P	1,116	2,173	4,168	5,357	8,254
Accrued Expenses & Payroll	4,830	5,014	4,627	8,826	13,598
Accrued excise taxes and fees	0	0	1,423	2,330	2,330
Deferred Income	272	119	831	257	257
Accrued Severance	339	217	380	923	923
Total Current Liabilities	**$ 7,343**	**$ 8,427**	**$ 13,018**	**$ 18,869**	**$ 26,538**
Long-Term Debt	0	0	3,001	16,571	16,571
Operating Lease	0	1,432	2,141	4,602	4,602
Other	241	21	516	4,736	4,736
Shareholders' Equity	44,110	66,074	95,975	67,549	104,139
Total Liabilities And Equity	**$ 51,694**	**$ 75,954**	**$ 114,651**	**$ 112,327**	**$ 156,586**

	2020	2021	2022	2023 E	2024 E
Net Income	(19,711)	(32,609)	(59,801)	(57,768)	4,890
Depreciation & Amort.	1,345	1,248	2,858	3,524	3,524
Stock Comp	1,654	3,983	5,489	4,700	4,700
Other	2,722	5,272	11,310	4,856	0
Working Capital	(1,631)	(733)	(11,570)	(2,924)	(10,807)
Operating Cash Flow	**$ (15,621)**	**$ (22,839)**	**$ (51,714)**	**$ (47,612)**	**$ 2,307**
Acquisition of Patents and trademarks	(468)	(326)	(772)	(491)	(500)
CapEx	(54)	(745)	(3,657)	(4,910)	(4,000)
Other	16,991	(26,658)	27,007	16,749	0
Investing Activities	**$ 16,469**	**$ (27,729)**	**$ 22,578**	**$ 11,348**	**$ (4,500)**
Debt	(354)	49	(3,822)	12,607	0
Equity	50	50,826	32,335	23,853	27,000
Other	0	0	2,307	0	0
Financing Activities	**$ (304)**	**$ 50,875**	**$ 30,820**	**$ 36,460**	**$ 27,000**
Change in Cash	**$ 544**	**$ 307**	**$ 1,684**	**$ 196**	**$ 24,807**

Source: 22nd Century Group, Inc. and Dawson James Securities estimates

Important Disclosures:

Price Chart:



Price target and ratings changes over the past three years:
Initiated – Buy – April 13, 2021 – Price Target $7.00
Update – Buy – April 15, 2021 – Price Target $7.00
Update – Buy – April 19, 2021 – Price Target $7.00
Update – Buy – May 7, 2021 – Price Target $7.00
Update – Buy – June 1, 2021 – Price Target $7.00
Update – Buy – June 11, 2021 – Price Target $7.00
Update – Buy – July 2, 2021 – Price Target $7.00
Update – Buy – July 23, 2021 – Price Target $7.00
Update – Buy – August 6, 2021 – Price Target $7.00
Update – Buy – August 31, 2021 – Price Target $7.00
Update – Buy – October 18, 2021 – Price Target $7.00
Update – Buy – November 5, 2021 – Price Target $7.00
Update – Buy – November 22, 2021 – Price Target $7.00
Update – Buy – December 9, 2021 – Price Target $7.00
Update – Buy – December 23, 2021 – Price Target $7.00
Price Target Change – Buy – January 6, 2022 – Price Target changed from $7.00 to $8.50
Update – Buy – January 24, 2022 – Price Target $8.50
Update – Buy – February 16, 2022 – Price Target $8.50
Update – Buy – February 24, 2022 – Price Target $8.50
Update – Buy – March 4, 2022 – Price Target $8.50
Update – Buy – May 2, 2022 – Price Target $8.50
Update – Buy – May 6, 2022 – Price Target $8.50
Update – Buy – May 16, 2022 – Price Target $8.50
Update – Buy – June 13, 2022 – Price Target $8.50
Update – Buy – June 22, 2022 – Price Target $8.50
Update – Buy – July 1, 2022 – Price Target $8.50
Update – Buy – July 26, 2022 – Price Target $8.50
Update – Buy – August 10, 2022 – Price Target $8.50
Update – Buy – September 21, 2022 – Price Target $8.50
Update – Buy – October 20, 2022 – Price Target $8.50
Update – Buy – October 27, 2022 – Price Target $8.50
Update – Buy – November 9, 2022 – Price Target $8.50
Update – Buy – November 22, 2022 – Price Target $8.50
Update – Buy – February 1, 2023 – Price Target $8.50
Update – Buy – March 6, 2023 – Price Target $8.50
Update – Buy – March 10, 2023 – Price Target $8.50
Price Target Change – Buy – May 10, 2023 – Price Target changed from $8.50 to $4.50

Price Target Change – Buy – July 3, 2023 – Price Target changed from $4.50 to $1.00
1-15 Stock split July 5, 2023
Price Target Change – Buy – July 25, 2023 – Price Target changed from $15.00 to $10.00

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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.
3) **Sell**: The analyst believes the price of the stock will decline by at least 20% over the next 12-18 months and should be sold.

The following chart reflects the range of current research report ratings for all companies, followed by the analysts of the Firm. The chart also reflects the research report ratings relating to those companies for which the Firm has performed investment banking services.

Current as of 17-Jul-23

	Company Coverage		**Investment Banking**	
Ratings Distribution	# of Companies	% of Total	# of Companies	% of Totals
Market Outperform (Buy)	25	69%	2	5.50%
Market Perform (Neutral)	11	31%	2	5.50%
Market Underperform (Sell)	0	0%	0	0.00%
Total	36	100%	4	11.00%

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