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Vuzix Corporation (NASDAQ: VUZI)

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Buy: Q4 Shortfall. Adjusting Estimates and Price Target.

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Vuzix pre-announced Q4 revenue of \$2.1 million, below our estimate of \$3.5 million and consensus of \$3.4 million. The company also announced a plan to reduce costs by 25%. We have adjusted our estimates and price target.

Q4 revenue of \$2.1 million is below the prior quarter and year-ago quarter. Product sales increased 36% q/q to \$1.9 million and engineering sales fell 72% q/q to \$226 thousand. For the year, revenue was \$13.2 million. Since 2020 annual revenue has ranged from \$11.6 million to \$13.2 million.

The company also announced a program to reduce cash annual operating expenses by \$8 million, or 25%. This will be accomplished by focusing on the higher-volume AR glasses, streamlining its tech development and OEM efforts. Operating expenses, excluding amortization of stock compensation, have grown from \$17 million in 2020 to \$28 million in 2022, and we estimate have exceeded \$31 million in 2023.

We estimate cash at year-end 2023 of \$35 million and with our current estimates, cash is expected to end 2024 at about \$5 million.

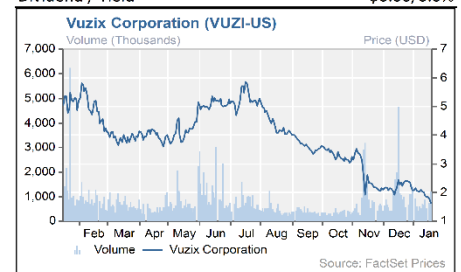
We continue to expect the company's investment in waveguide manufacturing and micro-LED development will be the primary drivers of growth in the years to come. The company has received multiple orders from aerospace and defense companies for development of waveguides and optical engines to be used in customized head-mounted displays. These are long sales cycle projects, and with the number of engagements growing, a hockey stick in revenue could occur in the next 18 months.

In the defense market, the company's development deals with a handful of major defense contractors on waveguide-based products could generate \$10 to \$15 million over a multi-year time frame. Lead times can be extended, and once deployment begins production runs can be long and very profitable. Vuzix is also working with multiple customers on supplying waveguides for the consumer market.

Price Target Methodology. Our \$3.50 price target, down from \$5, values the company's waveguide businesses at a significant discount to market transactions of \$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				\$1.63
Price Target				\$3.50
Estimates	F2022A	F2023E	F2024E	
Revenues (\$M's)	\$ 11.8	\$ 13.2 E	\$ 15.1	
1Q March	\$ 2.5	\$ 4.2 A	\$ 2.8	
2Q June	\$ 3.0	\$ 4.7 A	\$ 3.3	
3Q September	\$ 3.4	\$ 2.4 A	\$ 4.1	
4Q December	\$ 2.9	\$ 2.1 E	\$ 4.8	
	F2022A	F2023E	F2024E	
EBITDA (\$M's)	\$ (23.9)	\$ (25.6)E	\$ (21.0)	
1Q March	\$ (5.8)	\$ (6.0)A	\$ (6.5)	
2Q June	\$ (5.7)	\$ (5.5)A	\$ (6.2)	
3Q September	\$ (5.4)	\$ (6.9)A	\$ (4.8)	
4Q December	\$ (7.3)	\$ (7.2)E	\$ (3.5)	
EV/Sales	NM	5.0 x	4.3 x	
EV/EBITDA	NM	(2.5) x	(3.1) x	
Stock Data				
52-Week Range	\$1.60	-	\$6.06	
Shares Outstanding (mil.)				63.3
Market Capitalization (mil.)				\$103
Enterprise Value (mil.)				\$65
Debt to Capital				0%
Cash & Equivalents (mil.)				\$38.0
Cash/Sh.				\$0.60
Average Three Months Trading Volume (K)				383
Insider Ownership				7.6%
Institutional Ownership				42.4%
Short interest (mil.)				16.1%
Dividend / Yield				\$0.00/0.0%



Valuation

Our price target is based on market transactions in the waveguide market.

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.

Using the \$521 million average transaction value for waveguides results in a target of ~\$8 per share. However, we have discounted this sharply, to \$3.50, to reflect the risk of competition by larger and better-capitalized competitors, the time it may take to bring products to market, and the sharply higher interest rates currently compared to rates at the time of these transactions.

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)

	2020	2021	2022 A	Q1 23 A	Q2 23 A	Q3 23 A	Q4 23 E	2023 E	2024 E
Total Sales	\$ 11,581	\$ 13,165	\$ 11,836	\$ 4,191	\$ 4,691	\$ 2,180	\$ 2,092	\$ 13,154	\$ 15,069
Total COGS	10,984	11,596	10,353	3,315	3,718	2,418	2,529	11,980	14,120
Total Gross Profit	598	1,568	1,483	876	972	(238)	(437)	1,174	949
R&D	7,568	11,675	12,677	3,070	2,837	2,913	2,913	11,731	10,194
Sales & Marketing	4,040	6,119	8,078	2,540	2,510	2,832	2,832	10,714	9,912
G&A	6,915	22,503	21,039	5,132	4,260	4,467	4,467	18,326	15,799
D&A	1,129	988	1,789	964	973	959	998	3,895	3,993
Other	74	133	133	18	0	24	0	42	0
Operating Expense	19,725	41,418	43,716	11,723	10,580	11,195	11,210	44,708	39,898
Operating Income	\$ (19,127)	\$ (39,849)	\$ (42,233)	\$ (10,847)	\$ (9,608)	\$ (11,433)	\$ (11,646)	\$ (43,534)	\$ (38,949)
Interest & Other	1,175	(397)	1,469	607	563	450	450	2,068	(76)
Pretax Income	\$ (17,952)	\$ (40,246)	\$ (40,764)	\$ (10,241)	\$ (9,045)	\$ (10,983)	\$ (11,197)	\$ (41,465)	\$ (39,025)
Income Taxes	0	0	0	0	0	0	0	0	0
Net Income	\$ (17,952)	\$ (40,246)	\$ (40,764)	\$ (10,241)	\$ (9,045)	\$ (10,983)	\$ (11,197)	\$ (41,465)	\$ (39,025)
Preferred Dividends	(2,056)	0	0	0	0	0	0	0	0
Net to Common	\$ (20,008)	\$ (40,246)	\$ (40,764)	\$ (10,241)	\$ (9,045)	\$ (10,983)	\$ (11,197)	\$ (41,465)	\$ (39,025)
Diluted Shares	38,110	61,125	63,738	63,217	63,231	63,325	63,323	63,274	63,666
EPS	\$ (0.53)	\$ (0.66)	\$ (0.64)	\$ (0.16)	\$ (0.14)	\$ (0.17)	\$ (0.18)	\$ (0.66)	\$ (0.61)

Operating Income	\$ (19,127)	\$ (39,849)	\$ (42,233)	\$ (10,847)	\$ (9,608)	\$ (11,433)	\$ (11,646)	\$ (43,534)	\$ (38,949)
D&A	2,642	2,310	2,588	1,197	1,231	1,192	1,192	4,813	4,769
Stock Comp	2,806	17,303	15,776	3,668	2,833	3,297	3,297	13,094	13,188
EBITDA	\$ (13,680)	\$ (20,237)	\$ (23,870)	\$ (5,965)	\$ (5,544)	\$ (6,943)	\$ (7,157)	\$ (25,627)	\$ (20,992)
Total Sales	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Total COGS	94.8%	88.1%	87.5%	79.1%	79.3%	110.9%	120.9%	91.1%	93.7%
Total Gross Profit	5.2%	11.9%	12.5%	20.9%	20.7%	-10.9%	-20.9%	8.9%	6.3%
R&D	65.3%	88.7%	107.1%	73.2%	60.5%	133.6%	139.2%	89.2%	67.6%
Sales & Marketing	34.9%	46.5%	68.3%	60.6%	53.5%	129.9%	135.4%	81.4%	65.8%
G&A	59.7%	170.9%	177.8%	122.4%	90.8%	204.9%	213.5%	139.3%	104.8%
D&A	9.7%	7.5%	15.1%	23.0%	20.7%	44.0%	47.7%	29.6%	26.5%
Other	0.6%	1.0%	1.1%	0.4%	0.0%	1.1%	0.0%	0.3%	0.0%
Operating Expense	170.3%	314.6%	369.4%	279.7%	225.5%	513.5%	535.8%	339.9%	264.8%
Operating Income	-165.2%	-302.7%	-356.8%	-258.8%	-204.8%	-524.4%	-556.7%	-330.9%	-258.5%
Interest & Other	10.1%	-3.0%	12.4%	14.5%	12.0%	20.6%	21.5%	15.7%	-0.5%
Pretax Income	-155.0%	-305.7%	-344.4%	-244.3%	-192.8%	-503.8%	-535.2%	-315.2%	-259.0%
Income Taxes	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Net Income	-155.0%	-305.7%	-344.4%	-244.3%	-192.8%	-503.8%	-535.2%	-315.2%	-259.0%
Net to Common	-172.8%	-305.7%	-344.4%	-244.3%	-192.8%	-503.8%	-535.2%	-315.2%	-259.0%

Source: Vuzix Corporation and Dawson James Securities estimates

Exhibit 2. Balance Sheet and Cash Flow Statement

(\$ in 000's)

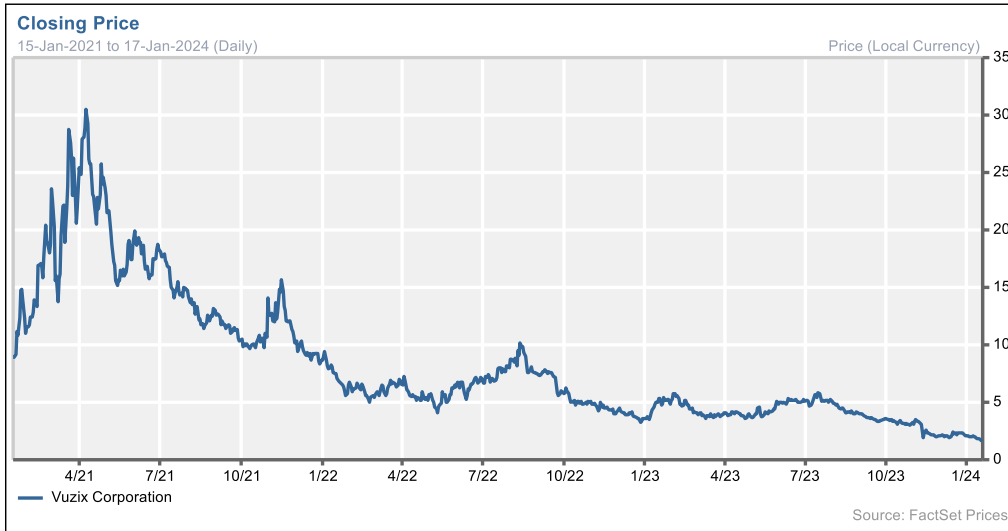
	2020	2021	2022 A	2023 E	2024 E
Cash	36,070	120,204	72,564	35,429	4,468
A/R	1,389	2,242	3,559	1,376	3,176
Revenue in excess of billings	0	0	269	437	437
Employee Retention Credit Rec.	0	0	467	0	0
Inventory	6,101	12,152	11,268	8,092	13,356
Prepaid Expenses & Other	<u>1,496</u>	<u>2,552</u>	<u>3,115</u>	<u>2,754</u>	<u>6,359</u>
Current Assets	\$ 45,055	\$ 137,150	\$ 91,241	\$ 48,088	\$ 27,796
Fixed Assets, net	2,837	5,190	3,879	6,607	4,839
Operating Lease Right of use	1,517	1,117	956	465	465
Patents & Trademarks	1,593	1,988	2,220	2,531	2,531
Licenses, net	194	1,390	30,159	46,448	46,448
Intangible Assets & Other	1,275	1,631	3,858	3,629	3,529
Total Assets	\$ 52,471	\$ 148,467	\$ 132,313	\$ 107,768	\$ 85,607
Accounts Payable	1,517	2,055	1,212	1,778	4,106
Unearned Revenue	41	28	29	98	226
Accrued Expenses	983	1,419	1,671	804	1,857
Licensing Fees Commitment	0	0	11,500	0	0
Taxes Payable	110	120	215	52	120
Operating Lease Right of use	<u>444</u>	<u>534</u>	<u>651</u>	<u>296</u>	<u>296</u>
Current Liabilities	\$ 3,095	\$ 4,156	\$ 15,277	\$ 3,029	\$ 6,605
Operating Lease Right of use	1,073	583	305	168	168
Licensing Fees Commitment	0	0	0	0	0
Equity	<u>48,303</u>	<u>143,728</u>	<u>116,730</u>	<u>104,571</u>	<u>78,834</u>
Total Liabilities & Equity	\$ 52,471	\$ 148,467	\$ 132,313	\$ 107,768	\$ 85,607

	2020	2021	2022 A	2023 E	2024 E
Net Income	\$ (17,952)	\$ (40,377)	\$ (40,764)	\$ (41,465)	\$ (39,025)
D&A	2,642	2,310	2,588	4,813	4,769
Stock Comp	2,806	17,303	15,776	13,094	13,188
Other	41	784	323	552	100
Working Capital	<u>(1,501)</u>	<u>(6,999)</u>	<u>(2,444)</u>	<u>2,977</u>	<u>(7,093)</u>
Operating Cash Flow	\$ (13,964)	\$ (26,980)	\$ (24,521)	\$ (20,029)	\$ (28,061)
CapEx	(497)	(3,809)	(1,724)	(4,359)	(3,000)
Acquisition	0	0	(18,823)	0	0
Other	<u>(989)</u>	<u>(1,043)</u>	<u>(624)</u>	<u>(12,323)</u>	<u>0</u>
Investing Activities	\$ (1,486)	\$ (4,852)	\$ (21,171)	\$ (16,682)	\$ (3,000)
Equity	39,357	127,112	(1,948)	(425)	100
Debt	1,556	0	0	0	0
Other	0	(1,144)	0	0	0
Preferred	<u>0</u>	<u>(10,000)</u>	<u>0</u>	<u>0</u>	<u>0</u>
Financing Activities	\$ 40,913	\$ 115,967	\$ (1,948)	\$ (425)	\$ 100
Change in Cash	\$ 25,463	\$ 84,134	\$ (47,640)	\$ (37,135)	\$ (30,961)

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
- Update – Buy – March 2, 2023 – Price Target \$15.00
- Update – Buy – April 11, 2023 – Price Target \$15.00
- Price Target Change – Buy – May 11, 2023 – Price Target changed from \$15.00 to \$8.00
- Update – Buy – July 11, 2023 – Price Target \$8.00
- Update – Buy – August 9, 2023 – Price Target \$8.00
- Price Target Change – Buy – November 13, 2023 – Price Target changed from \$8.00 to \$5.00
- Price Target Change – Buy – January 18, 2024 – Price Target changed from \$5.00 to \$3.50

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Current as of 14-Dec-23

	Company Coverage		Investment Banking	
Ratings Distribution	# of Companies	% of Total	# of Companies	% of Totals
Market Outperform (Buy)	21	61.76%	4	11.80%
Market Perform (Neutral)	13	38.24%	2	5.90%
Market Underperform (Sell)	0	0%	0	0.00%
Total	34	100%	6	17.70%

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