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

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Buy: Positioning for Growth.

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22nd Century has re-focused on its core tobacco IP with the sale of GVB and the associated debt and expense reduction. The company has also taken steps to consolidate facilities to improve efficiency and lower costs. Over the coming quarters, it will be seeking to improve margins in contract manufacturing and expand VLN distribution.

Re-focusing on its core tobacco IP is key to the company's recovery. With the sale of GVB complete, 22nd Century has been able to reduce debt and operating expenses. We expect additional debt reduction with the proceeds from the insurance settlement related to the Grass Valley fire and additional expense reduction by consolidation of facilities and other efficiency measures.

As the year progresses, we expect the company to pivot to growth initiatives for its tobacco business. This includes high-grading its contract manufacturing segment, which should improve margins. We also expect an expansion of VLN distribution.

The sale and other cost reduction actions will lower the company's cash burn significantly. Through Q3 of 2023, the hemp cannabis business consumed \$20 million in cash. The reduction of cash usage is of paramount importance for the company given the state of the capital markets, even with the recent Fed-driven rally. We expect additional cost-cutting in the tobacco business and corporate overhead.

The initial actions of the company's new CEO are encouraging and unlocking the value of its IP in low-nicotine tobacco is key for the shares. Mr. Firestone purchased 100K shares as did a board member and insider buying is often a bullish predictor of stock performance.

There are catalysts in the coming months that could help the company's business and the shares. The FDA's rule proposing a menthol ban is in final review. A key concern of the FDA is offering smokers an offramp when new rules are proposed. 22nd Century's menthol VLN combustible cigarettes might be excluded from the ban, as an offramp, giving the company a unique position in the market. A \$4 to \$10 million settlement with the company's insurance carrier would also be positive. We also expect a low-nicotine mandate in the future.

Valuation: Our \$3.33 price is based on the company's ability to monetize a nicotine mandate assuming modest royalty and market share.

Risks to Target: Our price target assumes the FDA implements a nicotine mandate and the company success in negotiating royalties on its technology.

Current Price				\$0.17
Price Target				\$3.33
Estimates	F2022A	F2023E	F2024E	
Revenues (\$M's)	\$ 62.1	\$ 78.7 E	\$ 27.0	
1Q March	\$ 9.0	\$ 22.0 A	\$ 6.8	
2Q June	\$ 14.5	\$ 23.4 A	\$ 6.8	
3Q September	\$ 19.4	\$ 17.8 A	\$ 6.8	
4Q December	\$ 19.2	\$ 15.5 E	\$ 6.8	
	F2022A	F2023E	F2024E	
EBITDA (\$M's)	\$ (39.2)	\$ (51.9)E	\$ (5.8)	
1Q March	\$ (6.5)	\$ (14.6)A	\$ (1.4)	
2Q June	\$ (6.9)	\$ (16.1)A	\$ (1.4)	
3Q September	\$ (11.0)	\$ (11.7)A	\$ (1.5)	
4Q December	\$ (14.8)	\$ (9.6)E	\$ (1.5)	
EBITDA (\$Ms)	\$ (39.2)	\$ (51.9)	\$ (5.8)	
EV/Sales	0.1x	0.0x	0.1x	
Stock Data				
52-Week Range	\$0.16	-	\$18.45	
Shares Outstanding (mil.)				30.9
Market Capitalization (mil.)				\$5
Enterprise Value (mil.)				\$4
Debt to Capital				66%
Cash (mil.)				\$2.9
Cash/share				\$0.09
Average Three Months Trading Volume (K)				1,463
Insider Ownership				1.1%
Institutional Ownership				5.2%
Short interest (mil.)				3.6%
Dividend / Yield				\$0.00/0.0%



Over the course of last year, the company has suffered from the worst capital market environment for microcap stocks in our memory, a fire at the company's manufacturing facility in Oregon that hurt revenues and margins, slower than expected take-up of the company's VLN introduction, and resignation of its CEO. These combined to weaken the company's balance sheet and force the company to lower costs and sharpen its focus.

The tobacco business has a unique asset: it has the only FDA-approved combustible cigarette with a modified risk claim. We are not aware of any other combustible product even attempting to make this claim. The other advantage for this business is the FDA's long-standing attempt to reduce the harm from cigarette smoking, and its recognition that it must give smokers an off-ramp as it changes the market with menthol bans and a low-nicotine mandate.

One challenge for the tobacco business is building a brand is time-consuming and expensive. That said, the company's success to date in attracting distribution partners is impressive. Unless additional resources become available via asset sales, license agreements, or warrant exchange, a retrenchment on VLN distribution is likely. Another challenge is that the FDA moves at its own pace, often impacted by public opinion and political factors. The menthol ban is likely the most near-term catalyst, and with a final rule submitted to OMB, action is probably weeks to months away. It would be very positive for the company if its menthol VLN combustible cigarettes were exempted from the ban and given the FDA's recognition of the necessity of giving smokers an off-ramp, we believe there is a chance of an exemption. The low-nicotine mandate, we believe, is also a priority for the FDA, but its willingness and capacity to move on a menthol ban and a low-nic mandate simultaneously is unknown.

Exhibit 1. Income Statement

<i>(\$ in 000's except per-share data)</i>	2020	2021	2022	Q1 23 A	Q2 23 A	Q3 23 A	Q4 23 E	2023 E	2024 E
Revenue	\$ 28,111	\$ 30,948	\$ 62,111	\$ 21,962	\$ 23,427	\$ 17,811	\$ 15,500	\$ 78,700	\$ 27,000
Cost Of Goods Sold	26,673	28,879	60,937	23,139	25,772	19,777	15,500	84,188	25,200
Gross Profit	1,438	2,069	1,174	(1,177)	(2,345)	(1,966)	0	(5,488)	1,800
	5.1%	6.7%	1.9%	-5.4%	-10.0%	-11.0%	0.0%	-7.0%	6.7%
SG&A	14,971	25,881	44,517	14,231	14,540	11,199	9,324	49,294	12,150
R&D	4,128	3,274	6,561	1,517	1,793	1,613	1,613	6,536	1,000
Other	176	78	7,202	898	675	56,704	0	58,277	0
Depreciation & Amort.	1,346	1,248	0	0	0	0	0	0	0
Opex	20,621	30,481	58,280	16,646	17,008	69,516	10,937	114,107	13,150
Operating Income	\$ (19,183)	\$ (28,412)	\$ (57,106)	\$ (17,823)	\$ (19,353)	\$ (71,482)	\$ (10,937)	\$ (119,595)	\$ (11,350)
Interest and other, net	(490)	(4,183)	(3,129)	(359)	(1,140)	(1,238)	(1,192)	(3,929)	(4,768)
Pretax Income	(19,673)	(32,595)	(60,235)	(18,182)	(20,493)	(72,720)	(12,129)	(123,524)	(16,118)
Income Tax Expense	38	14	(434)	0	0	0	0	0	0
Net loss	\$ (19,711)	\$ (32,609)	\$ (59,801)	\$ (18,182)	\$ (20,493)	\$ (72,720)	\$ (12,129)	\$ (123,524)	\$ (16,118)
Deemed dividend Net to Common						(564)			
						\$ (73,284)			
Shares (000)	9,254	10,414	12,856	14,386	14,900	19,887	25,978	18,788	39,048
EPS	(\$2.13)	(\$3.13)	(\$4.65)	(\$1.26)	(\$1.38)	(\$3.68)	(\$0.47)	(\$6.57)	(\$0.41)
D&A	1,346	1,536	3,306	1,175	1,442	810	810	4,237	3,240
Stock Comp	1,654	3,983	5,489	1,175	1,486	576	576	3,813	2,304
Other	176	0	9,065	898	336	58,391	0	59,625	0
EBITDA	\$ (16,007)	\$ (22,893)	\$ (39,246)	\$ (14,575)	\$ (16,089)	\$ (11,705)	\$ (9,551)	\$ (51,920)	\$ (5,806)

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

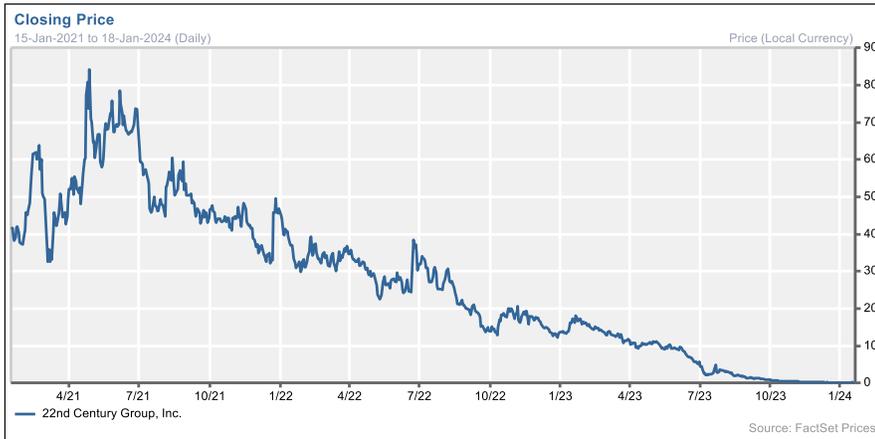
Exhibit 2. Balance Sheet and Cash Flow Statement

(\$ in 000's)	2020	2021	2022	2023 E
Cash & ST Investments	22,342	48,736	21,213	4,275
Restricted Cash				0
A/R	2,159	585	5,641	5,651
Inventory	2,034	2,881	10,008	11,273
Insurance Recovery	0	0	5,000	0
Prepaid Exp.	1,806	2,183	2,743	4,818
Total Current Assets	\$ 28,341	\$ 54,385	\$ 44,605	\$ 26,017
PP&E	2,483	5,841	13,093	10,225
Operating Lease	247	1,723	2,675	2,984
Goodwill	0	0	33,160	0
Patent, Trademark, other intangibles	8,211	7,919	16,853	6,299
Equity Investment	6,536	2,345	682	682
Restricted Cash				0
Other Assets	5,876	3,741	3,583	3,705
Total Assets	\$ 51,694	\$ 75,954	\$ 114,651	\$ 49,912
Bank Loans and N/P	539	596	908	1,441
LTD-Current	0	0	0	10,665
Operating Lease	247	308	681	1,097
A/P	1,116	2,173	4,168	5,490
Accrued Expenses & Payroll	4,830	5,014	4,627	5,793
Accrued excise taxes and fees	0	0	1,423	2,693
Deferred Income	272	119	831	704
Other	339	217	380	1,263
Total Current Liabilities	\$ 7,343	\$ 8,427	\$ 13,018	\$ 29,146
Notes and loans payable	0	0	0	156
Operating Lease	0	1,432	2,141	6,219
Long-Term Debt	0	0	3,001	0
Other	241	21	516	4,266
Shareholders' Equity	44,110	66,074	95,975	10,124
Total Liabilities And Equity	\$ 51,694	\$ 75,954	\$ 114,651	\$ 49,912
Net Income	(19,711)	(32,609)	(59,801)	(123,570)
Depreciation & Amort.	1,345	1,536	3,591	4,237
Stock Comp	1,654	3,983	5,489	3,813
Other	2,722	4,984	10,577	61,322
Working Capital	(1,631)	(733)	(11,570)	(1,318)
Operating Cash Flow	\$ (15,621)	\$ (22,839)	\$ (51,714)	\$ (55,516)
Acquisition of Patents and trademarks	(468)	(326)	(772)	(558)
CapEx	(54)	(745)	(3,657)	(4,951)
Other	16,991	(26,658)	27,007	21,736
Investing Activities	\$ 16,469	\$ (27,729)	\$ 22,578	\$ 16,227
Debt	(354)	49	(3,822)	13,736
Equity	50	50,826	32,335	34,308
Other	0	0	2,307	0
Financing Activities	\$ (304)	\$ 50,875	\$ 30,820	\$ 48,044
Change in Cash	\$ 544	\$ 307	\$ 1,684	\$ 8,755

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
Price Target Change – Buy – August 15, 2023 – Price Target changed from \$10.00 to \$7.50
Update – Buy – September 6, 2023 – Price Target \$7.50
Price Target Change – Buy – October 24, 2023 – Price Target \$3.33
Update – Buy – November 7, 2023 – Price Target \$3.33
Update – Buy – December 6, 2023 – Price Target \$3.33
Update – Buy – December 15, 2023 – Price Target \$3.33
Update – Buy – January 8, 2024 – Price Target \$3.33
Update – Buy – January 18, 2024 – Price Target \$3.33

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- 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 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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