

22nd Century Group, Inc. (XXII - \$2.67 - Buy)

Estimate Change

COMPANY NOTE

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Stock Data	11/07/18
Price	\$2.67
52 Week Range	(\$1.92 - \$4.44)
Price Target	\$11.50
Market Cap (mil)	\$332.15
Shares out (mil)	124.40
3-Mo Avg Vol	2,079,123
Cash (mil)	\$62.12
Total Debt (mil)	\$0.68

Revenues (\$ millions)					
Yr Dec	2017A	2018E		2019E	
	Actual	Curr	Prev	Curr	Prev
Mar	2.2	6.1A	-	-	-
Jun	3.9	6.9A	-	-	-
Sep	4.5	6.3A	-	-	-
Dec	5.9	-	-	-	-
YEAR	16.6	23.3	21.0	20.0	-

EPS (\$)					
Yr Dec	2017A	2018E		2019E	
	Actual	Curr	Prev	Curr	Prev
Mar	(0.03)	0.01A	-	-	-
Jun	(0.03)	(0.05)A	-	-	-
Sep	(0.03)	0.04A	-	-	-
Dec	(0.03)	-	-	-	-
YEAR	(0.13)	(0.04)	(0.14)	(0.15)	-

One year price history XXII



XXII: Q3 Results Exceed Expectations.

Q3 revenue of \$6 million was higher than our \$4 million estimate, opex was \$1 million lower than forecast and the company booked a \$12.2 million gain on the sale of its 14.8% stake in Anandia. Cash at quarter end was \$62 million providing the company substantial runway and the resources necessary to achieve its short and long-term goals. The company hosts a conference call on Thursday at 4PM Eastern to discuss Q3 results.

During the quarter 22nd Century sold its 14.8% stake in Anandia and booked a \$12.2 million gain on the sale. The company received stock and warrants in the transaction. Sale of the stock generated \$13 million in proceeds and the warrants are on the balance sheet valued at \$6.7 million.

Before year-end we expect two major events for the company: 1) release of the FDA's NPRM on maximum nicotine levels in combustible cigarettes and 2) the company's submission of an MRTP.

We expect the FDA to release a Notice of Proposed Rulemaking (NPRM) before year-end that, like the ANPRM, proposes a rule that limits nicotine in combustible cigarettes to non-addictive levels. After the FDA releases the NPRM, there will be a comment period, after which the FDA will evaluate the comments and issue a final rule. We believe this could happen by the end of next year, but earlier is certainly possible. There is significant support for the FDA's goals from the public health community and many have called for an early and aggressive transition to cigarettes with non-addictive nicotine levels.

An MRTP from 22nd Century for its very-low nicotine, non-addictive cigarettes is also expected before year end. A decision by the FDA could take up to 12 months. The application can have two impacts for the company. First, the application could be used by the FDA as evidence there is commercially available very low nicotine tobacco for the industry to comply with a very low nic mandate. Second, the creation of a modified risk product, capturing even a 1% market share, can be worth over \$1 billion, or \$8 per share, much more than the current share price. To date the company has spent \$7 million for the application and intends to incur an additional \$4 million over the next two quarters.

We believe there is more the company can do to strengthen its position in the market including licensing agreements for its technology, producing other tobacco plant varieties, international VLN opportunities, increasing its contract manufacturing business and growing additional crops of VLN tobacco.

Regulatory changes in the US will likely be a precursor to changes in other jurisdictions. 22nd Century indicates Canada, New Zealand, Finland and the UK are investigating nicotine reduction strategies. Our price target only includes an assumption of changes in the US.

We maintain our Buy recommendation on 22nd Century and reiterate our 12-month price target of \$11.50. We believe 22nd Century's patents, covering nicotine regulation in tobacco plants, is a solution to the FDA's pending regulation of nicotine levels in combustible cigarettes. We believe XXII has the opportunity to license its technology to Big Tobacco at a fraction of the cost they are currently contemplating it will take to comply with potential FDA regulations and this could result in a royalties or licensing stream far surpassing today's market cap. While our price target is based on changes in the US market we expect other countries to follow the FDA's lead, opening up additional markets for XXII and higher expected value for the shares.

Valuation:

Our twelve-month price target of \$11.50 is based on the company garnering royalty revenue for its technology on 10% of the US market share in the next five years, discounted at a 20% annual rate.

Risks to achievement of target price:

Risks to achieving our price target include delays in the FDA process, ability to find partners for X-22, challenges in attracting contract manufacturing and selling product overseas and possibility of requiring additional capital.

Company description:

22nd Century owns or exclusively controls over 200 issued patents, 50 pending patent applications. The company's proprietary technology enables the control of nicotine levels in tobacco plants by controlling the genes responsible for nicotine production in tobacco plants.

Required Research Disclosures



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Distribution of Ratings/IB Services Chardan Capital Markets

Rating	Count	Percent	IB Serv./Past 12 Mos.	
			Count	Percent
BUY [BUY]	61	67.03	22	36.07
HOLD [NEUTRAL]	22	24.18	1	4.55
SELL [SELL]	0	0.00	0	0.00
NOT RATED [NR]	8	8.79	0	0.00

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Neutral: Returns expected to be in line with sector average over 12 months and indicates total return between negative 10% and 10% over the next 12 months.

Sell: Returns expected to be materially below sector average over 12 months and indicates total price decline of at least 10% over the next 12 months.

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