



# QUARTERLY SECURITY REPORT

VOLUME 2, ISSUE 2

August, 2003

## Convergence of Physical and IT Security

Security convergence encompasses the integration of the physical security world with that of the IT domain. The ability to install physical security systems on a single computer network has been available for years, but the industry has been missing the capability to link those functions with IT.

New convergence technology will provide benefits to corporate security such as the ability to utilize both physical and IT resources to detect security breaches. For example, if someone logs onto a computer, but is

shown as having left the building, a red flag will be sent to the security office. Other benefits include the ability to completely monitor single or multiple properties remotely through a web-based browser, secure computers from possible virus attacks and hackers, make readily available data on facility use, and simplify management of isolated access and authentication controls within a building as well as other automation functions. The integration of all these functions will help reduce administration expense.

Security convergence will significantly

transform the security industry. Not only will security companies have to sell to a decision-maker firmly rooted in IT, but security companies will face increased competition as they vie against IT, Building Control, and other security companies.

To help the industry face its many challenges, a group of companies have recently formed the **Open Security Exchange** ([www.opensecurityexchange.com](http://www.opensecurityexchange.com)). As their website states, the purpose (continued on page 2)



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## Deal Flow - Security Industry Remains Active

Financial activity in the Security Industry was highlighted by a broad variety of transactions. Among these included a number of notable M&A and Capital Markets transactions:

**United Technologies Corp. (UTC)**, the aerospace and manufacturing conglomerate, announced the acquisition of **Chubb PLC**, a leading provider of electronic security and fire protection products and services, for \$1 billion in cash. The acquisition was part of the strategy to acquire businesses that would complement UTC's current business units that center on aerospace and building services. UTC will seek to double the size of Chubb through acquisitions in the next five or six years.

**Ingersoll-Rand Company Limited**, the diversified industrial firm, agreed to acquire the stock of **Integrated Access Systems (IAS)** and its subsidiary, Geoffrey Industries for an undisclosed amount and is expected to complete the transaction by the end of August 2003. IAS provides specialty security systems integration and Geoffrey Industries is a manufacturer of card access, alarm monitoring and integrated CCTV systems. This acquisition will continue Ingersoll-Rand's expansion of its security business after acquiring Electronic Technologies Corp. last year and will improve the company's ability to provide customers with a complete solution for managing openings, people and assets in addition to providing another

source of recurring revenues through a service-related business.

**GE Industrial Systems**, a unit of the General Electric Company, acquired **Monitoring Automation Systems**, a provider of automation software for central security station monitoring and secure business communications, for an undisclosed amount. Monitoring Automation Systems will become part of GE's Security and Life Safety business within GE Interlogix, Inc. GE made the acquisition to expand its security solutions business as well as its customer-base.

The Security Industry participated in (continued on page 3)

### Key Findings:

- Financial activity within the Security Industry remains active with a number of notable M&A and Capital Markets transactions
- The integration of physical and IT security will significantly transform the security industry
- IPTV is the future of surveillance technology

### Security Industry Coverage

*USBX Advisory Services focuses its security industry research on three broad segments, including: alarm monitoring and service businesses, alarm & related security equipment manufacturers, and integrated security systems companies. John E. Mack III, Founder, CEO and Senior Managing Director of USBX Advisory Services, was formerly one of the original founders and CEO of Protection One (NYSE: POI), the 2nd largest company in the alarm monitoring business in North America.*

# It's an IP Video Future

By: James Gompers

DVR or IPTV? It's a question many end-users are considering today or will be considering in the near future. DVR, digital video recorders, will store video surveillance streams to a hardware based storage medium that can be replayed and analyzed at any time. IPTV, Internet Protocol Television, solutions utilize IP based networks to transmit video streams to the video server. Both systems offer high-resolution digital imaging and storage, Internet and remote viewing, video motion detection, and many other standard fea-

tures. But that's where the similarities end.

## THE DVR

The DVR is one of the most innovative technologies in the surveillance industry since the camera itself. It stores video without degradation, along with highly advanced search capabilities, making video review fast and effective. The DVR has also incorporated advanced features such as video motion, multi-user remote monitoring, and pan/tilt/zoom (PTZ) control into a single platform. By eliminating the

need for multiple, adjunct peripheral components to perform similar functions, the DVR has become the system of choice for the surveillance industry. But with greater penetration of digital video recording technology, the DVRs' limitations have begun to emerge.

DVRs are built encompassing a server (computer) with physical analog video inputs, via co-axial cabling, directly from the cameras the same way standard analog systems are connected. DVRs have a limited number of control inputs and outputs for interfacing and

integrating to various systems and devices. The majority of DVR software has non-standard digitalization and compression and closed source codes to limit third party application development and high-level integration. Most digital video recorders have little or no matrix functionalities and do not offer multiple monitor outputs for security communication and surveillance control centers. When a DVR unit's video inputs are full, you need to add another unit, usually in groups of 8, 16 or 32 video input  
(continued on page 3)

# Security Equities and M&A Market Performance

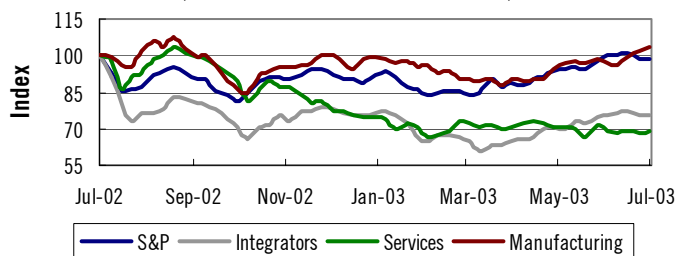
Security stocks and M&A activity rose during the second quarter of 2003. The S&P 500 ended the quarter up 15.39%, the best quarter this index has had since the fourth quarter of 1998. Integrators were able to outpace the S&P 500, while manu-

facturers matched the index. Service was the only security sector to decline. The strength in the public marketplace carried over to the M&A market as well. During the second quarter of 2003, M&A activity in the Security industry increased for the

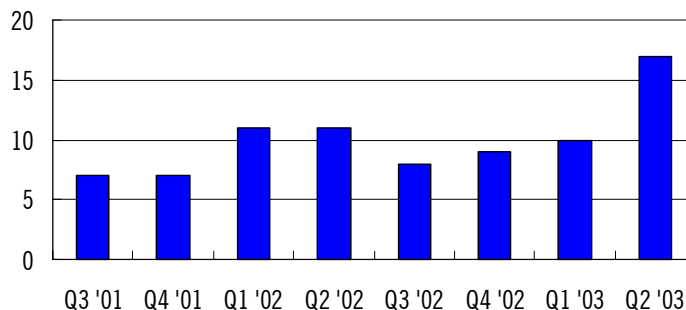
third consecutive quarter: the 17 M&A transactions reported in Q2 2003 represent a 55% increase over the 11 deals reported in Q2 2002 and a 70% increase over the first quarter deals.

The policies initiated by economic policymakers should provide stimulus to support strong economic growth during the upcoming quarters. As a result, equity and M&A markets should continue to experience growth.

USBX Advisory Services  
Security Company Index  
(Stock Performances over the Last Twelve Months)



Number of Quarterly Security Deals



# Convergence Cont.

(continued from page 1)

of this exchange is "to address today's most significant security challenge - the lack of integration between various components of the security infrastructure. The members of the Open Security Exchange are committed to developing: best practice guidelines in the area of security management; vendor-neutral technical specifications to provide interoperability between

physical and IT security technologies; and open solutions by implementing these specifications in their respective products and services."

The founding members of this new organization include **Computer Associates, Gemplus, Tyco's Software House and HID Corp.** In addition, approximately 400 people participated in a web cast about the

group, said Deb Spittler, Vice President of Marketing of HID Corp.

One company that has developed a product to integrate physical and IT security is Austin, Texas based **NetBotz Inc.** NetBotz, who recently closed a \$7 million mezzanine funding round with Austin Ventures, provides IP-based intelligent physical security solutions that secure critical assets and spaces from

physical threats. NetBotz's products give IT and systems managers a Web interface for managing a range of small, Web-enabled devices.

As the industry continues to evolve, more companies will attempt to solve the challenges facing the convergence of physical and IT security.

## IP Video Cont. *(continued from page 2)*

capacities. All of these limitations adversely affect total cost of ownership (TCO) as the security environment grows and changes.

### IPTV

Network video servers (NVS), network video storage servers (NVSS), and other IP solutions overcome the DVR's lack of flexibility. For systems exceeding 16 cameras in size (or multiples of 16) or with multiple site installation and centralized recording and monitoring, the user can reduce costs by not needing to add video servers for just a few more video inputs. Using IP networking allows some installations the advantage of leveraging existing network backbones — as opposed to directly connecting cameras to a DVR.

Most IP solutions use software licensing to overcome the hardware limitations we see with a DVR. Licensing allows the IP solution owner to choose the quality of the server and the amount of hard drive space needed. It also enables expansion of server requirements without proprietary and expensive hardware upgrades. As a software solution with standardized digitalization and compression and (usually) open software source codes, the IP video

system provides for easy integration of third party software solutions.

The advantages of IP surveillance systems over DVR technology make a strong case to be the system of choice for today's enterprise-level surveillance solutions. Beyond technology and integration advantages are the cost savings from IP.

### THE IP ADVANTAGE: ONE NETWORK

Today's network convergence technology enables the operation of all or most aspects of the business operation under one manageable network — access control, intrusion detection, IP video, fire alarm, phones, computers, temperature control and many more. Thus, by having only one infrastructure to maintain, cost of ownership can be

further reduced (see our article on convergence).

Having a single network infrastructure also gives the IT staff the ability to assist the security department in the maintenance of the surveillance infrastructure, servers, and archive storage, further increasing the cost efficiency of an enterprise class surveillance solution.

### About the Author

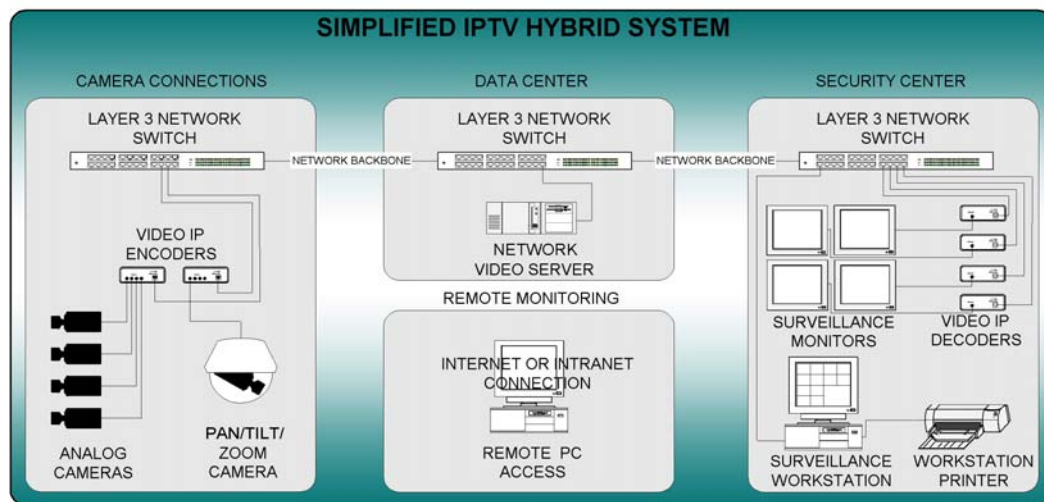
James Gompers founded Gompers Inc., which consults, designs, and manages technology projects. He also started Gompers Technologies Testing and Research Group, Inc., which tests, reviews, and develops technology products, services, and integration solutions. Jim writes a monthly column for *Access Con-*

*trol & Security Systems Integration*, entitled "Integrating the Future," and has more than 20 years of expertise in the security industry.

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### IBM LOOKS TO CAPITALIZE

As a sign the trend is gaining momentum, it is notable that IBM launched a recent initiative to take advantage of the increased demand for video surveillance by offering services to help companies make a transition from older, videotape-based surveillance systems to IP-based surveillance networks. IBM will be offering consulting, system design and integration services, as well as hardware and software installation and maintenance.



## Deal Flow - Security Industry Remains Active *(continued from page 1)*

the increase in IPO activity following the conclusion of the war with Iraq. **Integrated Alarm Services Group Inc.**, the largest wholesale alarm monitoring company in the United States, raised \$203.5 million through a public offering on July 23<sup>rd</sup>, 2003. Integrated Alarm sold 22 million shares at \$9.25 each. Integrated Alarm plans to use the proceeds of the offering to repay debt and purchase portfolios of alarm

monitoring contracts.

**Monitronics International Inc.**, a national provider of security alarm monitoring services, has been in the market for a proposed \$150 million senior secured revolving credit facility, \$175 million senior secured term loan B and a \$155 million subordinated note offering. The \$150 million senior secured revolving credit facility has been rated B1 by

Moody's Investors Service and B+ by Standard & Poor's. The \$175 million senior secured term loan B has been rated B1 by Moody's and B+ by Standard & Poor's. The \$155 million subordinated note offering has been rated single-B3 by Moody's and single-B-minus by Standard & Poor's. The ratings reflect the highly competitive nature of the alarm monitoring business, naturally high customer and dealer churn rates,

potential for increased price based competition, and the company's high leverage. The negative outlook on the deal prompted Monitronics to cut the size of the subordinated note offering from \$200 million to \$155million. The seven-year Rule 144a market offering calls for a yield of 11.75%. Proceeds will be used to repay existing debt and to fund growth.

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*USBX Advisory Services is a full-service NASD and SIPC member investment bank focused on serving the middle-market. USBX provides a full range of M&A solutions: Sell Side Advice, Buy Side Advice, Recapitalizations, Leveraged Buyouts, and Fairness Opinions. In addition, USBX provides clients with a host of Strategic Financing Placement services, including Private Equity, Mezzanine Finance and Senior Debt. We provide our clients with unmatched service and expertise through extensive industry expertise, proprietary M&A databases and strong relationships with lenders, investors, and C-level executives of the industry's largest companies.*

## Aerway Acquires ArmorGroup Integration

In April 2002, **Aerway Integration Services Inc.**, a privately owned company focused on the integrated-security industry, acquired ArmorGroup Integration Systems (AGIS), a unit of **Armor Holdings, Inc.** (NYSE: [AH](#)). USBX Advisory Services initiated this transaction and acted as financial advisor to Aerway Holdings, LLC.

With this transaction completed, Armor Holdings remains focused on completing the sale of Armor-Group Services.

### Selected USBX Clients

USBX Advisory is representing a leading access control company with web-hosted solutions that is looking for merger and acquisition and candidates.

USBX Advisory is representing a leading mobile communications software firm with software focused on the public safety sector that is seeking growth capital.

USBX Advisory is representing a large system integrator looking to be acquired or re-capitalized.

USBX Advisory is representing a digital video recorder company looking to be acquired.

### Selected Closed Security Transactions

Closed	Seller	Buyer	Target Business Description:	Synopsis
Aug-03	Integrated Access Systems	Ingersoll-Rand Co	Provides specialty security systems integration services and provides information technology services	Ingersoll-Rand Co Ltd agreed to acquire Integrated Access Systems and its subsidiary, Geoffrey Industries, for an undisclosed amount to provide a complete solution for managing openings, people, and assets
Jun-03	Protection One Europe (Westar Energy)	ABN Amro Bank NV	Provides security alarm monitoring services in France and Germany	ABN Amro Capital France acquired Protection One Europe for cash and assumed debt. The transaction is part of the plan of Westar Energy Inc to pay down debt and focus exclusively on its electric utility business
Jun-03	TecScan International Inc	Phoenix Media Group Ltd	Distributes biometric physical and logical access control solutions for security purposes	Phoenix Media Group Ltd acquired TecScan International Inc for \$40 million in stock. The transaction was structured as a reverse takeover and shareholders of TecScan would own 98.9% of Phoenix after receiving 8 million post-reverse split stock
Jun-03	Monitoring Automation Systems	General Electric Co	Develops automation software for central security station monitoring and secure business communications	GE Industrial Systems acquired Monitoring Automation Systems for an undisclosed amount in a move to expand its security solutions business as well as customer base
Jun-03 Announced	Chubb PLC	United Technologies Corp	Manufactures and sells electronic security systems, and provides security systems monitoring and physical security services	United Technologies Corp agreed to acquire Chubb PLC for about GB £621.8 million (US\$1 billion) in cash. The acquisition is part of the strategy of United Technologies Corp to acquire businesses that would complement its current business units that center on aerospace and building services
Jun-03 Announced	QSI Security Inc	Diebold Inc	Manufactures and sells closed circuit television cameras, digital video and access control systems for financial institutions	Diebold Inc agreed to acquire substantially all the assets of QSI Security Inc for an undisclosed amount. The transaction will allow Diebold to expand its product offerings and client base by folding QSI Security into its operations
May-03	Information Spectrum Inc	Anteon International Corp	Provides defense and homeland security solutions and information technology solutions	Anteon International Corp acquired Information Spectrum Inc for \$90.7 million in cash. The acquisition is consistent with Anteon International plans to expand its revenue growth and technological capabilities in the national homeland security requirements
Apr-03	International Fiber Systems	General Electric Co	Develops audio and video data transmission fiber optics	General Electric Co acquired International Fiber Systems Inc for an undisclosed amount as part of its plans to build on its security-equipment and sensor business of Interlogix
Apr-03	Dorado Products	HID	Develops magnetic strip cards and readers	Acquired the card and reader business of Dorado Products to expand its offerings with magnetic stripe products
Apr-03	ZN Vision Technologies AG	Viisage Technology Inc	Develops software and hardware for 2-D and 3-D face recognition technology	Viisage Technology Inc acquired ZN Vision Technologies AG for about \$26.6 million in stock to strengthen its market leadership position and to expand its identity verification solutions on a global scale
Apr-03	Arizona Drug Screening & Investigations	Private Group Led By Geisel-Churchill	Provides employment screening services	A private group led by Richard Geisel-Churchill and Kevin Olson acquired Arizona Drug Screening & Investigations for an undisclosed amount to expand its business into national markets
Apr-03	Armor Group Integrated Systems	Aerway Integration Services	Provides integrated security services	Aerway acquired Armor Group Integrated Systems for \$4.1 million plus a warrant for approximately 2-5% of Aerway Integration Services

Highlighted deal denotes USBX was an advisor on this transaction.

Sources: USBX Advisory Services and Mergerstat

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March 9th & 10th, 2004



Santa Monica, CA  
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- Principles of leading public and private equity or debt investment funds.
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**Steve Harter**  
Chairman and Director of  
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President, Notre Capital

I thought the Security Growth Conference was well organized with a superb level of attendance by senior level executives and investors.

**Richard Ginsburg**  
President and CEO  
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**Irv Witcosky**  
President of Diversified  
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