

# Security & Defense pipeline report

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## SUMMARY

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According to VBR over \$4.5 billion has been invested in US and European private security and defense companies in 2007 YTD. Private equity acquisitions and P-2-P transactions have accounted for over \$3billion of investment with the remaining \$1.5 billion invested in early-stage companies.

The US currently dominates the security and defense sector with 109 companies securing financing in 2007 compared to 70 in Europe. The US is particularly dominant in IT Security and defense technologies while the playing field is more level in bio-defense, enabling (dual-use) technologies and surveillance. The increased investment in Europe in these sub-sectors reflects unprecedented appetite among European investors for private security companies. For the first time European and American investor appetite for the security sector seems to be almost equally bullish!

Figure 1. Investment by round in Europe and the US: 2007 YTD

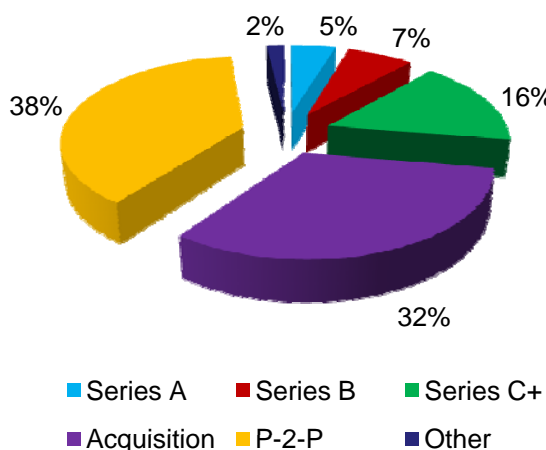
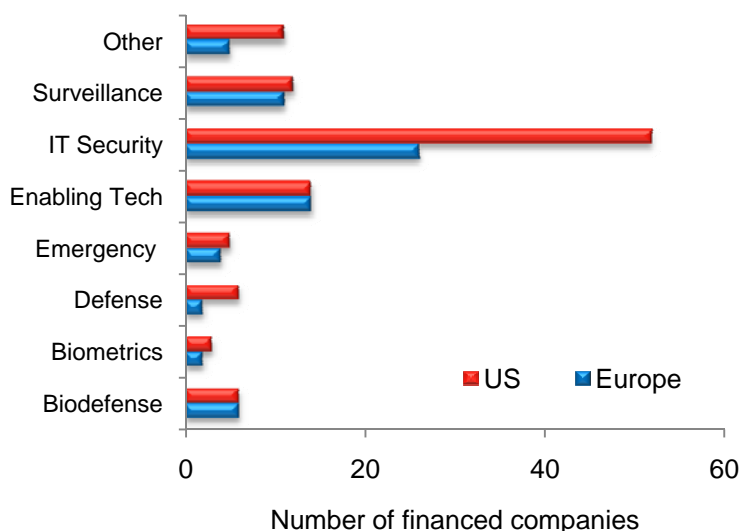


Figure 2. Number of companies financed by sub-sector in Europe and the US: 2007 YTD



Source: Venture Business Research

### VBR sub-sector coverage:

- Bio-defense and bio-surveillance
- Biometrics and identity authentication
- Detection and sensor technologies
- Emergency response and management
- IT Security
- Radio Frequency Identification
- Surveillance and perimeter security
- Training and simulation systems
- Transport security

Venture Business Research Ltd. is an independent research company based in London, UK. The information provided in this report is derived from VBR's Security & Defense Deal Monitor. Customers can purchase this deal monitor at <http://www.vbresearch.com> or by phone at +44 207 251 8000

**Pipeline© EXCLUSIVE – HI-G-TEK LAUNCHES \$15 MILLION SERIES B FUNDRAISING**

Hi-G-Tek Inc., headquartered in Rockville, MD, is a developer of an innovative active-RFID platform for the real-time monitoring and control of critical physical assets. The company was founded in Israel in 1999 to develop low-power, advanced micro-electronic products for bio-medical and military applications. Recently the company has concentrated on developing active-RFID applications for government and commercial transportation logistics.

The company's patented "sensing" technology not only detects where an asset is but also its status or condition at anytime providing an unparalleled level of real-time security irrespective of whether an asset is stationary or in transit, indoors or outdoors. This system offers mission-critical features for key markets including homeland security, transportation, fuel distribution and military.

In September 2006, Hi-G-Tek completed a \$10 million Series A funding led by L Capital Partners with participation from Battelle Ventures, L.P., and its affiliate, Innovation Valley Partners. The investment enabled Hi-G-Tek to establish its corporate headquarters in Rockville, MD and to expand into the US market. Hi-G-Tek's CEO has now informed Venture Business Research that the company is looking to raise an additional \$15 million to fund its continued expansion and for new product development. The company is actively seeking outside investors and is being advised by Silicon Valley Bank on the transaction.

For more information on Hi-G-Tek contact Larry Blue, CEO at: [larry@higtek.com](mailto:larry@higtek.com).

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**Pipeline© EXCLUSIVE – ALERT LOGIC SEEKS LEAD INVESTOR FOR SERIES C FUNDING**

Alert Logic, based in Houston, TX provides on-demand internal network security solutions. The company's service is targeted at small and medium sized businesses and can be rapidly deployed to provide network protection from intrusions and Internet worms, continuous vulnerability discovery and regulatory compliance reporting.

In July 2006 Alert Logic closed a \$5 million Series B funding led by Austin, TX-based Hunt Ventures with participation from existing investors DFJ Mercury, Access Venture Partners and OCA Ventures. The investment was used to fund the company's expansion and product development. The company's CEO has recently informed Venture Business Research that the company is now looking to raise an additional \$7 million to fund the launch of its latest 'log management for compliance' product in Q3 2007. Existing investors are reinvesting in the business. However, external investors are actively being sought to lead the Series C round.

For more information on Alert Logic contact Michael Turner, CEO at: [mturner@alertlogic.net](mailto:mturner@alertlogic.net).

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**Pipeline© EXCLUSIVE – DELTADOT TARGETS STRATEGIC PARTNERS**

Founded in 2000 as a spin out from Imperial College London, deltaDOT Ltd. is a biotechnology company that is developing and commercialising innovative technologies for the separation and analysis of bio-molecules. The company's core technology, Label Free Intrinsic Imaging (LFII™), coupled with proprietary software algorithms, forms the technical basis of deltaDOT's products. These products are able to separate and monitor proteins, peptides, nucleic acids, small molecules and pathogens without labeling, in real time and in a highly cost-effective manner.

In July, deltaDOT announced that it was a member of an US/UK based consortium that had received a \$7.9 million grant from the US Defense Advanced Research Projects Agency (DARPA) to develop a

technology and processes to accelerate the production of vaccines and response to a wide variety of biological threats. The DARPA program known as the Accelerated Manufacture of Pharmaceuticals intends to shorten the timeframe for manufacturing lifesaving vaccines and monoclonal antibodies. In the research program deltaDOT's technology platforms will provide the analytical capabilities required to track product quality throughout the development process from R&D to product testing.

According to the company's CEO, deltaDOT is now looking to expand its presence further into the homeland security and military markets. To achieve this the company is attempting to simplify and miniaturize its technology enabling it to be deployed as an analysis tool at the source of a pathogen outbreak or bioterrorist attack. In order to enter the security market successfully deltaDOT is actively seeking a co-development partner with industry expertise. The company informed Venture Business Research that it is also open to approaches by strategic investors willing to purchase a portion of the company and run the security operation as an independent spin out company.

For more information on deltaDOT contact Anthony Baxter, CEO at: [a.baxter@deltadot.com](mailto:a.baxter@deltadot.com).

#### **Pipeline© EXCLUSIVE – ADVISORS SOUGHT FOR VUMII'S AIM IPO**

Vumii Inc., based in Alpharetta, GA, is a provider of sophisticated surveillance technologies used in the physical security industry. The company's current products include the Discoverii day/night vision camera system and breakthrough situational awareness and image navigation software that dramatically improves the orientation and usability for PTZ cameras.

To date, the company has raised approximately \$8.5 million in angel investment. In 2006, Vumii reached the final of the Global Security Challenge, an annual business plan competition to find and select the most promising security technology startups in the world. According to the company's CEO, Vumii is now seeking to raise additional financing to fund market expansion and strategic acquisitions. Vumii is targeting a \$15 million fundraising through an IPO on AIM in early 2008. Venture Business Research has been informed that the company is currently contacting advisors in connection with the floatation.

For more information on Vumii Inc contact Randall Foster, CEO at: [randallfoster@vumii.com](mailto:randallfoster@vumii.com).

#### **UNDER ATTACK: GLOBAL BUSINESS AND THE THREAT OF POLITICAL VIOLENCE**

Global terrorism is one of the greatest threats for the business world. Around 20 per cent of today's terrorist attacks are aimed at the business community. A recent Lloyd's report surveyed 154 board-level executives on the issue of political violence with the following results.

Over a third of companies avoid investing in overseas markets for fear of political violence, while 20 per cent have forgone promising business opportunities for the same reason.

The recent Lloyd's report, *Under Attack? Global business and the threat of political violence*, surveyed 154 board-level executives on the issue. It concluded that business leaders believe they are operating in an increasingly dangerous world, and having to focus on the risks they face from terrorism and political violence. It also leaves little doubt that terrorism and political violence have a significant impact on businesses' strategy and operations – from employee vetting to whether or not to invest in a given location.

The financial impact of terrorism or political violence is high, with one estimate suggesting that the costs of political risk to the global economy could be \$1 trillion. But the costs due to lost opportunities could be even higher. Many businesses are avoiding investing in politically sensitive areas or locating offices in large cities to avoid 'hot spots'. In fact, over a third of companies avoid investing in overseas markets for fear of

political violence, while 20% have forgone promising business opportunities for the same reason. So with boards making decisions to invest or operate in certain areas based partly on the risks involved, the importance of having the correct information has never been greater.

So are businesses getting the right information about these risks? According to the Lloyd's report, probably not. There appears to be a significant gap between growing risk awareness and tangible action actually taken by many companies, driven by a lack of understanding of the dynamics they encounter as they globalize. Alarmingly, only one in three business leaders believe their companies have a good understanding of the political violence risks they face, while two thirds report that they rely on international media as a source of information on political violence risk.

Source: Contingency Today - [www.contingencytoday.com](http://www.contingencytoday.com)

## **NY-BASED PRIVATE EQUITY FUNDS DRIVE DEFENSE SECTOR FORWARD**

A series of major private equity acquisitions in the security and defence space in 2007 have contributed significantly to total investment in Europe and the US year-to-date exceeding \$4.5 billion. Private equity has continued to invest in the sector in August with two New York-based private equity funds announcing the completion of major acquisitions in the sector. In the larger of the two deals Veritas Capital completed the previously announced \$1.1 billion acquisition of Aeroflex Inc. (formerly Nasdaq Symbol: ARXX) by affiliates of, or funds managed by The Veritas Capital Fund III, L.P., Golden Gate Private Equity, Inc. and Goldman, Sachs & Co. The acquisition was approved by Aeroflex's shareholders, who will receive \$14.50 per share, at a meeting on July 26.

Aeroflex, a components supplier to the aerospace and defence markets based in Plainview, NY, had initially agreed in March to a takeover by General Atlantic and Francisco Partners, who had offered \$13.50 per share. A shareholder vote on the General Atlantic / Francisco Partners merger was cancelled and the acquisition by Veritas was approved by Aeroflex's shareholders at a meeting on July 26.

Founded in 1992, Veritas invests primarily in defence and aerospace related companies and has established a Defense & Aerospace Advisory Council consisting primarily of former high-ranking government and military officials to advise on investments in these sectors. Veritas is currently investing from its third fund, Veritas Capital Fund III. The acquisition of Aeroflex will be the sixth investment from the fund to enter the VBR Security & Defense Deal Database. Other investments include the acquisition of Trawick & Associates, an IT services company for the US Government in November 2006 and Athena Innovative Solutions Inc., a provider of technical expertise and solutions to government and industry clients in the field of homeland security, in September 2005.

Monomoy Capital Partners, L.P., the New York private equity firm, announced in mid-August that it had acquired Transeo, LLC, a provider of integrated vehicle solutions to the armored vehicle industry. Terms of the transaction were not disclosed.

Transeo designs, engineers and manufactures armored trucks and similar specialty vehicles for the cash-in-transit and emergency vehicle response industry. The company is a leading provider of customized armored vehicles to some of the US's largest operators of armored truck fleets, including Garda USA and Triple D Security.

Monomoy Capital Partners, L.P. is a \$280 million private equity fund that targets businesses with \$20 to \$200 million in annual revenues that require turnaround capital to improve liquidity, drive operational improvement or lead a financial restructuring. The fund typically invests \$5 to \$30 million in each acquisition and acquires businesses through bankruptcy, out-of-court restructurings, corporate divestitures and other complex transactions. Transeo is Monomoy's tenth transaction in the past 20 months but the first to be included in the VBR Security & Defense Deal Database.

## AUGUST BONANZA FOR US DEFENSE AND AEROSPACE SECTOR

August has been a highly successful month for private business in the defense and aerospace sectors with a total of four companies in the US announcing funding. In yet another example of the growing interest shown by private equity funds in the security and defense sector, Sensis Corporation, a provider of defense, air traffic control systems based in East Syracuse, NY, announced that it had secured a minority investment from private equity firms Needham Capital Partners and Dolphin Direct Equity Partners.

Sensis is Needham's third portfolio company to be included in the VBR Security & Defense Deal Database and the second investment made by the firm in the past two months. In July, Needham took part in the \$16m Series D financing of Bay Microsystems, a provider of mission-critical secure broadband networks based in San Jose, CA. Needham has also backed ChipX Inc., most recently in March 2004 when it participated in the company's \$12m Series I round.

Other deals in the defense space this month included T&K Machine Inc., a Paris TX-based manufacturer of airframe components for the commercial and military aerospace markets. The company announced the closing of a \$5 million development funding from investors Advantage Capital Partners and Stonehenge Capital Company. The funding will be used to support the company's continued growth.

Advantage Capital's investment in T&K included \$2 million in capital raised in partnership with U.S. Bank Community Development Corporation through the federal New Markets Tax Credit program. In addition, Advantage and Stonehenge each invested \$1.5 million raised in connection with Texas' Certified Capital Companies program. Both programs stimulate economic growth in areas that historically have been underserved by traditional sources of investment capital.

In early August SureFire, LLC, a Southern California-based manufacturer of compact, high-end illumination tools and tactical equipment announced that it received investments from a syndicate comprising Broadsword Partners, Brooklyn NY Holdings and Goldman, Sachs & Co. SureFire intends to use the undisclosed amount of capital to accelerate the company's growth.

Finally, the defense and aerospace sector also provided a major M&A deal this August with the announcement by Allen-Vanguard Corp. that it had agreed to acquire bomb protection specialist Med-Eng Systems Inc. in a deal valued at C\$600 million (\$568.2 million).

## ISRAELI SURVEILLANCE COMPANIES SECURE US FUNDING

The surveillance and perimeter security sector continues to be one of the hottest verticals in the industry this year with over thirty companies developing surveillance technologies having already secured venture funding in 2007. This trend has continued in August with two Israeli surveillance companies announcing investments from US-based VCs.

In the larger of the two deals Hadas Detection & Decoding Ltd announced that 21 Ventures had acquired 29% of the company for NIS 18 million (\$4.2 million). The deal will be completed in two stages, with the fund initially owning 16% of Hadas. The second stage will be completed by the end of the year.

Founded in 2002, Hadas specializes in perimeter security solutions for gas and oil pipelines, as well as underground and surface infrastructures, through an advanced electronic signal processing system that detects irregular activity in the vicinity of the protected facility in real time, and relays a precise warning on the nature and location of the activity to a control center.

The investment by 21 Ventures provides an indicative valuation of Hadas at NIS 65 million (\$15.2 million).

The company's shareholder structure pre-transaction is as follows: employees - 30%; Sitobi Group - 26%; Milstein Group - 10%; Gad Schwartz - 15%; Amir Eyal - 5%; Shaul Bar - 5%; Avi Yochanan - 4%, and others - 5%)

21Ventures, founded in January 2004, is a venture capital fund specializing in the investment and development of seed and early stage technology companies. In August 2006 the firm announced that it was switching its focus to Israeli-based start-ups primarily in the physical security, clean energy and mobile software markets. 21 Ventures currently has four portfolio companies included in the VBR Security & Defense Deal Database including Israeli companies Agent Video Intelligence and Hadas Detection & Decoding and US companies BioNanomatrix and IQinVision. The firm says it plans to invest a further \$20 million in Israeli businesses over the next eighteen months.

The second Israeli surveillance business to announce funding this month was Lod-based, Rontal Applications Ltd., a provider of incident management and business continuity systems. Rontal raised \$3.5 million of Series B funding from US-based Pegasus Capital Corp. The company's \$1.5 million Series A fundraising was sourced from private investors during 2005 and 2006. In 2004 the company also received \$750,000 of seed financing from Ozonelink and NG Funds.

## **NETWORK DEFENSE AND INTERNET SECURITY DOMINATE IT SECURITY SECTOR**

The IT Security sector has received over \$1.4 Billion of investment in 2007 year-to-date. Two sub-sectors have dominated - network defense businesses have received around 22% of total investment in the sector, with email and internet security securing a further 7%. In August this trend has continued with companies in both sub-sectors closing investment rounds.

Network Security businesses were the major winners in August with companies in Europe, the US and Israel all raising investment. In Europe, Panda Software announced that HarbourVest Partners LLC and Atlantic Bridge Ventures had acquired almost 25 % of Panda Software for an undisclosed amount. Founded in 1990 Panda Software is a leading antivirus software company with headquarters in Bilbao, Spain. In April this year the company announced the sale of 75% of its shares to Spanish investors Gala Capital and Investindustrial at a valuation of €133m. The remaining 25% were retained by existing shareholders who formed part of the company's ongoing management team. These shares have now been sold to the new investors.

Panda Software is the third investment by HarbourVest in the security and defense sector this year. In April HarbourVest led the \$22 million Series E financing of Sepaton Inc., a Marlborough, MA-based data protection and recovery business. In the same month HarbourVest's European arm, based in London, took part in the Series A financing of World-Check, a provider of structured intelligence on heightened risk individuals and entities, based in London.

A second major deal in the Network Defense sub-sector to close in August was a \$7.5 million Series C financing for PacketMotion, a San Jose, CA-based provider of enterprise security and compliance solutions. Investors included Intel Capital, ONSET Ventures, and Mohr Davidow Ventures. This brings the company's total funding to \$34.5 million over three rounds of investment.

In the email and internet security sub-sector the largest investment this month was closed by The 41st Parameter, a developer of online fraud detection and prevention solutions for eCommerce and financial services. At the start of August the company announced that it had closed a \$10m Series C round. The fundraising, which was led by JAFCO Ventures based in Palo Alto, CA with participation from Kleiner Perkins Caufield & Byers and Norwest Venture Partners, will be used to fund distribution, enterprise solution development, sales and marketing.

## GOOGLE WADES IN WITH \$625 MILLION POSTINI ACQUISITION

Google has announced a plan to acquire on-demand web security firm Postini for \$625 million payable in cash. The deal, which is subject to regulatory approval, is expected to close by end of the Q3 2007, after which Postini will become a wholly-owned subsidiary of Google.

Postini's services include email filtering, archiving, encryption, and policy enforcement and protect customers' email, instant messaging and other web-based communications from security threats and productivity drains such as spam and viruses. Google said it plans to use Postini's technology to improve security and boost the appeal of its Google Apps package of hosted office applications to larger businesses.

This deal is at least the seventh acquisition by Google of a venture-backed company this year and the second in the IT Security space. In May 2007, Google announced the acquisition of GreenBorder Technologies, a maker of anti-virus and anti-spyware technology. Both deals form part of a larger strategy Google to expand its security-related business aggressively.

### Companies and Investors mentioned in this report and **attached deal datasheet**:

Companies	Investors	
Aeroflex Inc	21 Ventures LLC	Matignon Investissement & Gestion
AirInSpace	Advantage Capital Partners	Mohr Davidow Ventures
Cordus GmbH	ATA Ventures	Monomoy Capital Partners
Hadas Detection & Decoding, Ltd	Atlantic Bridge Ventures	Needham Capital Partners
Insightix Ltd	bm-t beteiligungsmanagement	Norwest Venture Partners
Mycroft Talisen Inc	thüringen gmbh	Onset Venture Partners
PacketMotion Inc	Broadsword Partners	Pegasus Capital Corp
Panda Software	Brooklyn NY Holdings	RWI Ventures
Red Condor Inc	Dolphin Direct Equity Partners	SoftBank Capital
Rental Applications Ltd	DEWB	Square 1 Bank
Sensis Corp	Goldman Sachs & Co	Stonehenge Capital Company
SureFire LLC	HarbourVest Partners LLC	Veritas Capital
T&K Machine Inc.	Intel Capital Corp	
The 41st Parameter Inc	JAFCO Ventures	
Transeo LLC	Kleiner Perkins Caufield & Byers	
Zenteris GmbH		

### ***NEXT pipeline report – 3 SEPTEMBER 2007***

***All press releases and information should be directed to Malcolm Robertson, [malcolm.robertson@vbresearch.com](mailto:malcolm.robertson@vbresearch.com) or***

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