Q3 2021 Physical Security Industry Update

Assa does the big deal. Supply Chain Continues to Impact Business

For a couple of years now I have been writing and speaking about the restructuring in the market and saying the restructuring / consolidation with the product manufacturers has slowed as restructuring is maturing. But making the point that the channel, door & hardware system providers and security integrators is only in the 3rd inning of consolidation. Then in Q3, BOOM. Assa Abloy announced the acquisition of Spectrum Brands' HHI division including Kwikset, Baldwin, Weiser, Pfister and National Hardware for $4.3 billion. The deal alone increases Assa's total sales by 15%, advances their position in the electronic lock market, home automation, and is a big move into the retail / big box market.

Assa has followed an aggressive acquisition strategy for many years, averaging 3 deals per quarter. Meanwhile, Allegion is much more conservative with only a few smaller transactions over the past several years. Allegion's best in class financial performance is a double-edged sword. For an acquisition to be accretive to their results it needs to deliver 30% operating income which eliminates most businesses. Dormakaba is quite on the acquisition front and is still working to find synergies with the Dorma & Kaba merger, the Best acquisition followed by Mesker / Design Hardware, new ERP implementation and consolidation of several facilities.

Assa, Allegion and dormakaba have posted similar organic growth results quarter after quarter, year after year. **But not this quarter.** With all companies struggling with supply chain issues and material price inflation, Assa posted 14% organic growth, Allegion declined 3% and dormakaba declined 5.2% organically. Not sure how Assa did it, but congratulations.

Channel consolidation continued in Q3, spurred by demographics (owners wanting to retire), an abundance of money looking to go to work, attractive financial performance from physical security companies, and concern over the capital gains tax increase. I am expecting a flurry of deals to close in the 4th quarter.

With the magnitude & timing of the capital gains increase unknown, the rapid pace of M&A of activity in 2021, M&A in the channel may be significantly slower in 2022. The demographics factor doesn't change so the rate may pick back up later in the year or be slow into 2023.

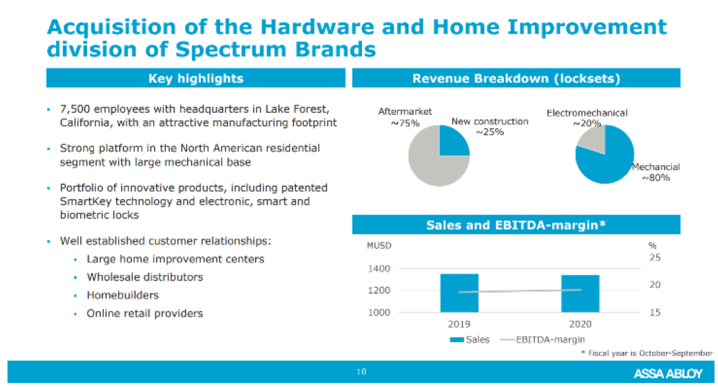
Q3 2021 Highlights from the Manufacturers

Allegion: A tough quarter. Electronic supply chain, higher material costs, & labor shortages

- Q3 total revenue was $717 million, down 1.6% organically. Adjusted EPS declined 6.6%. Adjusted Operating Margin also declined -3.3% vs PY.
- Americas' Q3 sales were $524 million, down 3.0% organically. "Strong price realization". Residential product sales were down high single digits, commercial sales down low single digits, and electronics were down high single digits.
- Americas Operating Margin was 25.5% down 19.7% from 30% PY, adjusted ebitda dropped from 32.5% to 27%. Ouch
- Allegion International – Sales were $192 million, up 1.7% vs PY, +2.5% organically, citing growth in Simons Voss & Interflex. Adjusted ebitda was flat at 16%.
- Full year outlook was lowered. Total revenue projected to drop from 7 – 7.5% to 4.0 – 4.5%. EPS forecast also lowered from $5.25 – 5.40 vs $4.95 – 5.05.
- No acquisitions were reported.
- Supply chain challenges are expected to delay $80 – $100 million of revenue in 2021.

ASSA ABLOY: Surprisingly strong sales in Americas & Entrance Systems

- Q1 total sales were 23.9 MSEK ($2.8 billion) up 8% vs PY. +7% organic, +2%, acquisitive, -1% currency. EBIT increased 7% EPS declined 5%.
- Americas Q1 Revenues were 5,400 MSEK ($635 million) up 14% organically. "Very strong sales in Access & High Security, Arch Hardware, Electromechanical, Security Doors, US Resi & Smart Home products". Operating margin was 20.6% up from 20.2%. Aggressive pricing offset increasing material costs.
- EMEA increased 7% organically. Operating margin increased 20 bps, but business divestments drove Op Margin from 15.9% to 11.3%. Strong sales in Finland, France, Africa & Middle East.
- Asia sales declined 7%. Operating margin dropped from 7.4% to 5.8%.
- Global Technology (HID & Ving) group was up 7%, operating margin was 15.8% vs 16.0% PY.
- Entrance Systems was up 10%. OM declined from 17.8% to 14.8%. "Very strong sales in residential & perimeter security.
- Completed three acquisitions in the quarter, nine YTD. Capitol Door, Omni ID & NZ Fire Doors. And announced the HHI (Kwikset+) deal.

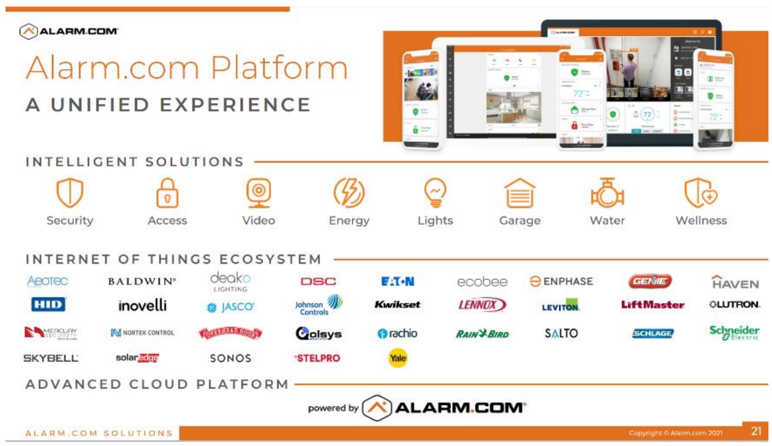


Dormakaba - <u>Full year</u> results 2020 / 2021 (June 2021) Performance better than guidance.

- Total sales 2.5 billion CHF ($2.7 billion) down 1.6% vs PY, +1.3% organic.
- EBITDA was 353 million CHF, ($384 million), 14.1% vs 12.8% PY, + 1.3%.
- America's – impacted by weak US commercial market and Mesker
- America's sales were 670 million CHF ($730 million), -5.2% organically. EBITDA dropped from 17% to 16.4%, with Mesker impacting EBITDA by -2.4%. Leading to comments "evaluating options for Mesker"
- Lodging systems were down 20% from pre COVID levels.

Alarm.com Continues to impress with financials and platform expansion

- Q3 sales were $192 million, up 21%, of which $118 million were SaaS license revenue, $74 million equipment. SaaS license renewal was 96%.
- Adjusted ebitda $38 million, 9% vs PY.
- Demonstrated 24% CAGR revenue growth since IPO in 2015.
- The company has an impressive strategy of creating a IoT linked ecosystem for much more than just security. I suggest you have a look at their Q3 earnings presentation.



M&A Highlights – Continuing at a rapid pace

RBC Capital Markets [Q3 Global M&A Report]

- The global economic recovery continued to fuel surging M&A activity in Q3, with over 27,000 deals and $3.4 trillion in combined deal value recorded in the first nine months of the year. Despite potential macroeconomic headwinds, global drivers of M&A remain intact, and both Europe and North America are on pace to easily break records in Q4.

- Dealmakers in North America remain undeterred by labor shortages and inflationary pressures, closing over 4,600 deals worth a combined $708 billion in Q3.

M&A in our Space…

Central Indiana Hardware, CIH a 100% ESOP company with 200 employees merged with St Louis based **H&G** also an ESOP company with 70 employees to create a new venture called **APTURA.** Both companies are market leaders and are service oriented businesses providing doors frames & hardware, access control, div 10 specialty products, moveable wall partitions, and store front systems.

Convergint acquired **Premier Security Group –** who focuses on the financial vertical market operating in CA, UT & AZ and two Alaska based business from the **ATS** group of companies which creates a tech support and service-based operation in Alaska.

Per Mar Security acquired **Armor Security** in the twin cities. The business serves residential & commercial customers and has a locksmith division. The business will be linked to **Floyd Lock & Safe** business, a deal that we represented last year.

CertaSite acquired **Premier Electronics** in Macomb MI. This is CertaSite's 6th fire alarm business in Michigan.

CTSI (backed by WindPoint Partners) acquired Chantilly VA based **AFA Protective Systems** in one of the larger transactions in the Qtr. AFA serves 28,000 east coast markets via 17 branches. AFA was closely held public company that reported $83 million of revenue in 2020. The deal value estimated at $120 million.

Cook & Boardman acquired south Easton MA based **Galeno**, a provider of commercial doors, frames and division 10 specialty products. C&B also acquired Everett, WA-based **JDS, Inc.** JDS is a turnkey provider of opening solutions including doors, frames, hardware, and division 10 specialty products.

Security Alarm Corp acquired Sarasota FL based **Alert Alarm Systems**. DMAG's Steve Rubin represented Alert Alarm in the transaction.

Allied Universal acquired NY based MSA Security who provides threat protection solutions including explosive detection canine teams

Best wishes for the holidays and continued strong business activities!

Dave

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