



**Quadnetics**

## **Interim Report 2005**



# THE Chairman's Statement

## DAVID COGLAN CHAIRMAN

### Highlights

- Successful acquisition of Protec plc, creating leading independent CCTV security services provider in the UK
- Consolidation of enlarged Quadnetics Group into two focused, scale security businesses
- Investment in launch of new US subsidiary for local support of Synectics security systems technology
- Strengthened senior management team and Group infrastructure to support growth
- First half underlying consolidated sales ahead 13% versus last year. Total sales ahead 40% (including one month's contribution from Protec).

### Overview

The current financial year has seen some crucial developments for Quadnetics. The acquisition of Protec plc, completed in early November, will result in a doubling of the Group's sales revenues as well as, more importantly, allowing us to consolidate and integrate our activities into two focused security systems businesses, each with scale and significant market presence.

The Group's businesses now comprise **Synectics** (Security Products & Software) and **Quadrant Security** (Security Services).

This integrated structure enables the Group to take maximum advantage of the benefits of, for example, consolidated purchasing power, cross-selling of Group products and shared administrative overheads.

It also provides increased leverage to our senior operating managers in exploiting growth opportunities from a broader base of activity. Implementation of the new structure should be substantially

complete by the end of May this year.

The first half of this financial year was also the first period of operation for Synectics' US subsidiary, Synectic Systems Inc. Following important contract wins last year for our digital CCTV systems in the casino market in North America, it became clear that this opportunity could not be properly addressed from the UK, and that further growth required a credible local presence for sales management and customer support. To short-circuit the recruitment process, we acquired in late May last year a small team of industry and technical specialists with the assets of Alphapoint LLC. Our Group Technical and Business Development Director has also been seconded full-time to Synectic Systems Inc. for 12 months to ensure proper integration of the UK and US activities from both a product development and operations point of view. Further casino contracts have since been won in the US and Canada, and the pipeline of upcoming

bids looks very promising. Accelerated expansion of Synectics' activities in these areas remains a key objective for the Group.

## Results

In the half year to 30 November 2005, Quadnetics produced a profit before tax, exceptional costs and goodwill amortisation of £923,000 (2004: £1.2 million) on consolidated turnover of £17.8 million (2004: £12.7 million). These results include one month's contribution of £52,000 from the Protec companies. Underlying earnings per share were 7.2p (2004: 7.7p).

Exceptional costs of £555,000 were incurred relating to Protec, principally the cost of redundancies and provision for the closure of one operating site following acquisition.

Net cash on hand at 30 November was £7.9 million (31 May 2005: £3.6 million). However, this is before payment of acquisition costs and related one-off costs within Protec anticipated to be up to £2 million in total.

## Dividend

An interim dividend of 1.5p per share (2004: 1.0p) will be paid on 31 March 2006 to shareholders on the register as at 3 March 2006.

## Operational Review

**Quadrant Security**, our security services business, designs, installs and maintains electronic security systems, and provides security monitoring and facilities management services, to

clients in the local government, retail, transport, police, prisons, petrochemical, large corporate, military and specialist high security sectors. It operates primarily in the UK, Middle East and the Republic of Ireland. With a full contribution from the Protec acquired businesses, Quadrant Security has current run-rate annual sales of over £50 million and is significantly profitable. We believe it is now the UK's largest independent CCTV security company.

During the half year, the Quadnetics continuing businesses within Quadrant Security increased like-for-like turnover by 14% to £9.2 million (2004: £8.1 million). Operating profit (before central cost allocations) declined to £869,000 (2004: £1.0 million), due primarily to three factors: increased costs from moving our on-vehicle CCTV operation to larger, more professional premises; moving a large customer from spot orders to a committed long term contract at a slightly lower gross margin; and continued margin pressure and contract delays in the local government town centre market. The first two factors result from deliberate decisions that have increased the quality of the relevant business, and we are confident will pay future dividends. The local government market is showing some signs of improving, as public perception of the importance of public space CCTV has led to discussions of renewed financial support from central government for such systems.

The acquired Protec security services activities (Protec SDA and Protec SSS) have generally been experiencing a continuation of positive momentum over recent months and performed above budget in the short period following acquisition. The integration of these businesses into Quadnetics is proceeding ahead of expectations.

During the first half, David Orme, formerly Chief Operating Officer of Bell Group plc, was recruited to Quadnetics as Group Operations Director, in particular to lead the integration and development of Quadrant Security. He has already had a major positive impact on the business. The appointment allows Russ Singleton, our Group Chief Executive, to spend proportionately more time on critical issues relating to the expansion of Synectics.

**Synectics** is the Group's security surveillance products and software business. Over recent years, Synectics CCTV recording and control systems have evolved to become what we believe is the industry standard for public space CCTV systems in the UK and some overseas markets, particularly South Africa. This strength led on to success in other market sectors, including police, financial services, casinos and, with the help of a small acquisition, marine and offshore oil and gas. Protec Falcon's special projects military surveillance business is currently being integrated into Synectics to capitalise on expansion

# THE Chairman's Statement

DAVID COGLAN CHAIRMAN

## Highlights

- First half profit before tax, exceptional costs and goodwill amortisation in line with expectations at £0.9 million (2004: £1.2 million), with strong second half anticipated
- Net cash of £7.9 million at 30 November 2005
- Interim dividend 1.5p per share (2004: 1.0p)
- Overall, the Board continues to anticipate a satisfactory financial result for the year as a whole, and substantial further progress next year

opportunities in a further attractive market sector that is a natural fit for Synectics' skills.

The Quadnetics continuing businesses within Synectics grew turnover for the half year by 25% to £5.9 million (2004: £4.7 million), and gross profit by 29% to £2.3 million (2004: £1.8 million). Operating profits, however, were virtually flat at £379,000 (2004: £392,000), due to the costs of operating the new US subsidiary and of additional R&D expenditure for product developments required for the US market. The US subsidiary is already profitable in its own right, although its contribution was small in the first half.

Significant successes during the period included contracts for explosion rated surveillance systems for a series of oil platforms in the Caspian Sea, and the adoption of Synectics' Synergy software by the Group's first Indian casino customer in the United States.

## Strategic Objectives

Quadnetics' strategy has two principal objectives:

- To maximise the growth opportunities of Synectics' digital CCTV control systems and recording technology/solutions; and
- To become one of the UK's leading electronic security services companies through creating and building on market leadership positions in key vertical customer sectors (and thereby increasing penetration of Synectics products into those sectors).

The acquisition of Protec will enable us substantially to accomplish the second objective. In addition, the creation of the integrated Quadrant Security structure should facilitate solid future profit growth through continuous operational improvements in a single business of market-leading scale. Obviously, there will be challenges to overcome, requiring commitment, skill and clear direction, but the

path is reasonably well defined. We believe we now have the management and resource requirements in place to achieve the new goals the Board will be setting for this activity.

Synectics involves a potentially substantial growth opportunity on a global scale and, of course, corresponding risks inherent in any relatively new technology-based business. The essence of Synectics' success to date has been to deliver innovative surveillance systems that provide, in an integrated Synectics control environment, all the benefits of the latest digital CCTV image storage and retrieval technology, while enabling customers an upgrade path that protects their investment in expensive installed CCTV cameras and communications infrastructure.

In the US in particular, the market for large-scale digital CCTV systems is new, rapidly evolving and potentially very large. The market now has the attention of a number of the world's largest electronics and information technology companies, as well as dozens of smaller competitors. The Board believes that, in order to succeed, Synectics must focus rigorously on its specific areas of experience and technical competitive advantage in two sectors: casinos and public space surveillance. Synectics has the advantages of a leading position in its UK home market, technical solutions (especially systems control software) we believe to be as good as anything available,

and successful reference sites in some of the largest implementations to date of digital CCTV in casinos in North America. This is an excellent base to build from.

### **Outlook**

The second half of the current financial year should produce significantly increased profits compared with those in the first half. This will flow from inclusion of a full period of contribution from the acquired Protec activities, traditional second half improvements in the local government sector and, most notably, increased sales of Synectics products outside the US that are already either contracted or confidently expected. Although the bid pipeline in the US is encouraging, the timing of contracts is difficult to predict and we expect most of the benefit of the increased activity there to fall in our next financial year.

Overall, the Board continues to anticipate a satisfactory financial result for the year as a whole, and substantial further progress next year.

**David Coghlan**  
**Chairman**

20 February 2006

# Consolidated Profit & Loss Account

FOR THE HALF YEAR ENDED 30 NOVEMBER 2005

	NOTES	BEFORE GOODWILL AMORTI- SATION AND EXCEPTIONAL ITEMS £'000	EXCEPTIONAL ITEMS £'000	GOODWILL AMORTI- SATION £'000	UNAUDITED HALF YEAR TO 30 NOV 2005 TOTAL £'000	RESTATE UNAUDITED HALF YEAR TO 30 NOV 2004 TOTAL £'000	RESTATE AUDITED YEAR TO 31 MAY 2005 TOTAL £'000
<b>Turnover</b>	1						
Continuing operations		14,455	–	–	14,455	12,743	26,761
Acquisitions		3,335	–	–	3,335	–	–
		<b>17,790</b>	–	–	<b>17,790</b>	12,743	26,761
Cost of sales		(12,623)	–	–	(12,623)	(8,700)	(18,107)
		<b>5,167</b>	–	–	<b>5,167</b>	4,043	8,654
<b>Gross profit</b>							
Net operating expenses		(4,296)	(555)	(283)	(5,134)	(3,143)	(6,528)
<b>Operating profit</b>							
Continuing operations		819	–	(247)	572	900	2,126
Acquisitions		52	(555)	(36)	(539)	–	–
		<b>871</b>	<b>(555)</b>	<b>(283)</b>	<b>33</b>	900	2,126
Net interest receivable		52	–	–	52	82	139
<b>Profit on ordinary activities before taxation</b>		<b>923</b>	<b>(555)</b>	<b>(283)</b>	<b>85</b>	982	2,265
Tax charge on ordinary activities	2				(37)	(286)	(48)
<b>Profit on ordinary activities after taxation</b>					<b>48</b>	696	2,217
Basic earnings per ordinary share	4				<b>0.4p</b>	6.0p	19.2p
Diluted earnings per ordinary share	4				<b>0.4p</b>	6.0p	19.1p
Underlying earnings per ordinary share	4				<b>7.2p</b>	7.7p	20.0p

In the half year ended 30 November 2004 and the full year ended 31 May 2005 net operating expenses included amortisation of goodwill amounting to £198,000 and £396,000 respectively.

There were no exceptional operating expenses in either period.

# Consolidated Balance Sheet

30 NOVEMBER 2005

	NOTES	UNAUDITED 30 NOV 2005 £'000	RESTATED UNAUDITED 30 NOV 2004 £'000	RESTATED AUDITED 31 MAY 2005 £'000
<b>Fixed assets</b>				
Intangible assets	5	17,788	7,523	9,183
Tangible assets		2,264	933	1,280
		<b>20,052</b>	<b>8,456</b>	<b>10,463</b>
<b>Current assets</b>				
Stocks		3,463	2,407	3,040
Debtors		17,511	8,220	9,896
Cash at bank and in hand		7,899	3,997	3,562
		<b>28,873</b>	<b>14,624</b>	<b>16,498</b>
<b>Creditors: amounts falling due within one year</b>		<b>(20,301)</b>	<b>(6,107)</b>	<b>(7,527)</b>
<b>Net current assets</b>		<b>8,572</b>	<b>8,517</b>	<b>8,971</b>
<b>Total assets less current liabilities</b>		<b>28,624</b>	<b>16,973</b>	<b>19,434</b>
<b>Creditors: amounts falling due after more than one year</b>		<b>–</b>	<b>(4)</b>	<b>(3)</b>
<b>Provisions for liabilities and charges</b>		<b>(1,414)</b>	<b>(84)</b>	<b>(1,102)</b>
<b>Net assets</b>		<b>27,210</b>	<b>16,885</b>	<b>18,329</b>
<b>Capital and reserves</b>				
Called up share capital	6	3,244	2,311	2,341
Share premium account	6	14,346	12,267	12,622
Merger reserve	6	8,436	–	–
Other reserves	6	(1,164)	715	715
Profit and loss account	6	2,348	1,592	2,651
<b>Equity shareholders' funds</b>		<b>27,210</b>	<b>16,885</b>	<b>18,329</b>

# Consolidated Cash Flow Statement

FOR THE HALF YEAR ENDED 30 NOVEMBER 2005

	NOTES	UNAUDITED HALF YEAR TO 30 NOV 2005 £'000	RESTATED UNAUDITED HALF YEAR TO 30 NOV 2004 £'000	RESTATED AUDITED YEAR TO 31 MAY 2005 £'000
<b>Net cash inflow from operating activities</b>		<b>462</b>	<b>234</b>	<b>1,939</b>
Returns on investments and servicing of finance		82	58	107
Taxation	7	176	(437)	(1,398)
Net capital expenditure and financial investment		(156)	(92)	(497)
Acquisitions and disposals	8	3,782	(446)	(867)
Equity dividends paid		–	–	(462)
<b>Cash inflow/(outflow) before use of liquid resources and financing</b>		<b>4,346</b>	<b>(683)</b>	<b>(1,178)</b>
Management of liquid resources – amounts (placed on)/withdrawn from bank deposit		(1,396)	2,500	2,500
Financing		(9)	(31)	29
<b>Increase in cash</b>		<b>2,941</b>	<b>1,786</b>	<b>1,351</b>

## RECONCILIATION OF NET CASH FLOW TO MOVEMENTS IN NET FUNDS

For the half year ended 30 November 2005

	UNAUDITED HALF YEAR TO 30 NOV 2005 £'000	RESTATED UNAUDITED HALF YEAR TO 30 NOV 2004 £'000	RESTATED AUDITED YEAR TO 31 MAY 2005 £'000
<b>Increase in cash in the year</b>	<b>2,941</b>	<b>1,786</b>	<b>1,351</b>
Increase/(decrease) in bank deposits	1,396	(2,500)	(2,500)
Decrease in debt and lease financing	359	55	63
<b>Change in net funds resulting from cash flows</b>	<b>4,696</b>	<b>(659)</b>	<b>(1,086)</b>
Acquisitions	(53)	–	–
<b>Movement in net funds in the year</b>	<b>4,643</b>	<b>(659)</b>	<b>(1,086)</b>
Opening net funds	3,200	4,286	4,286
<b>Closing net funds</b>	<b>7,843</b>	<b>3,627</b>	<b>3,200</b>

# Notes

## FOR THE HALF YEAR ENDED 30 NOVEMBER 2005

1. All turnover derives from the Group's continuing activities comprising Quadnetics Group plc, Quadrant Video Systems plc, Synectic Systems Limited, Synectic Systems, Inc., Look CCTV (trading as a division of Quadnetics Group plc) and Coex Limited, together with that of the businesses of Protec plc, trading as SDA Protec, SSS Protec and Falcon Protec, which were acquired in November 2005 (see note 8). The turnover and results of the Protec businesses are shown under Acquisitions within these statements.
2. The tax charge for the period is based on the estimated rate of corporation tax that is likely to be effective for the full year to 31 May 2006.
3. Dividend distributions have been accounted for in accordance with FRS 21 which has resulted in a restatement of the results for the half year ended 30 November 2004 and the full year ended 31 May 2005, as explained more fully in note 9.

An interim dividend of 1.5p per share, totalling approximately £225,000, will be paid on 31 March 2006 to shareholders on the register at 3 March 2006.

4. Basic, diluted and underlying earnings per share have been calculated on the following earnings and numbers of shares:

	EARNINGS			EARNINGS PER SHARE		
	HALF YEAR TO 30 NOV 2005 £'000	HALF YEAR TO 30 NOV 2004 £'000	YEAR TO 31 MAY 2005 £'000	HALF YEAR TO 30 NOV 2005 p	HALF YEAR TO 30 NOV 2004 p	YEAR TO 31 MAY 2005 p
Basic	48	696	2,217	0.4	6.0	19.2
Exceptional item	555	–	(302)	4.5	–	(2.6)
Goodwill amortisation	283	198	396	2.3	1.7	3.4
Underlying	<b>886</b>	<b>894</b>	<b>2,311</b>	<b>7.2</b>	<b>7.7</b>	<b>20.0</b>
Diluted	<b>48</b>	<b>696</b>	<b>2,217</b>	<b>0.4</b>	<b>6.0</b>	<b>19.1</b>
				'000	'000	'000
Weighted average number of ordinary shares – basic calculation				<b>12,318</b>	11,527	11,546
Dilutive potential ordinary shares arising from share options				<b>7</b>	38	44
Weighted average number of ordinary shares – diluted calculation				<b>12,325</b>	11,565	11,590

# Notes

## FOR THE HALF YEAR ENDED 30 NOVEMBER 2005

5. Intangible assets include £8.8m of goodwill arising on the acquisition of Protec plc.

6. Movements on shareholders' funds in the period are as follows:

	SHARE CAPITAL £'000	SHARE PREMIUM £'000	MERGER RESERVE £'000	OTHER RESERVES £'000	PROFIT AND LOSS ACCOUNT £'000	TOTAL £'000
b/f at 1 June 2005	2,341	12,622	–	715	2,300	17,978
Restatement of dividends	–	–	–	–	351	351
Restated	2,341	12,622	–	715	2,651	18,329
Profit after tax	–	–	–	–	48	48
Final dividend for 2005	–	–	–	–	(351)	(351)
Issue of shares to						
Employee Share Scheme	156	1,724	–	(1,880)	–	–
Acquisition of Protec plc	747	–	8,436	–	–	9,183
Currency translation adjustment	–	–	–	1	–	1
	3,244	14,346	8,436	(1,164)	2,348	27,210

Movements on share capital and share premium shown as arising from the acquisition of Protec plc include £185,000 and £1,981,000 respectively in respect of shares which will be issued after 30 November 2005.

During the half year ended 30 November 2005 780,000 ordinary shares of the Company were allotted at a value of £2.41 each to the Quadnetics Group Employee Share Scheme with the substantial majority of the funding for subscription for these shares provided as an interest-free loan by the Company. In accordance with UITF 38 the value of the shares has been deducted from shareholders' funds and the number of shares has been excluded from the earnings per share calculations.

7. Net cash inflows from taxation include a corporation tax repayment of £249,000.

8. On 9 November the Recommended All Share Offer made by Brewin Dolphin Securities Ltd on behalf of Quadnetics for Protec plc (“Protec”) was declared wholly unconditional, and therefore the results of Protec and its subsidiaries have been included in the results with effect from that date. On 8 February 2006 notice was given to those Protec shareholders who had not accepted the Offer informing them that Quadnetics will compulsorily acquire their Protec shares by applying sections 428 to 430F of the Companies Act 1985. Therefore the Company expects to acquire the entire issued share capital of Protec plc before its year end at 31 May 2006, and no minority interest (which would amount to approximately £0.1 million) has been reflected in these financial statements.

Net cash inflows from acquisitions comprise bank balances acquired in Protec of £4.132 million less a payment of £350,000 in settlement of loan notes issued as consideration for Look Closed Circuit TV Limited in February 2004.

9. The interim accounts and the comparative figures are prepared on the basis of the accounting policies set out in the financial statements of the Group for the year ended 31 May 2005, except in respect of dividends which have been dealt with in accordance with FRS 21 whereby dividends are not recognised in the profit and loss account until, in the case of final dividends, they have been approved at a general meeting of the Company, or, in the case of interim dividends they have been paid.
10. The half year results have not been audited by the Group’s auditors and do not constitute statutory accounts. The comparative figures for the year ended 31 May 2005 have been abridged from the statutory accounts for the year ended on that date, subject only to the restatement for dividends explained in note 9. The Auditors’ opinion on those accounts was unqualified and did not contain any statements under section 237(2) or (3) of the Companies Act 1985. The statutory accounts for the year ended 31 May 2005 have been filed with the Registrar of Companies.
11. Copies of this statement will be sent to shareholders and will be available on the Group’s website ([www.quadnetics.com](http://www.quadnetics.com)) and from Quadnetics Group plc, Haydon House, 5 Alcester Road, Studley, Warwickshire, B80 7AN.

For more information about Quadnetics Group please contact us at:  
**Haydon House, 5 Alcester Road, Studley, Warwickshire, B80 7AN, England**  
**Tel: 01527 850080 Fax: 01527 850081 e-mail: [info@quadnetics.com](mailto:info@quadnetics.com)**  
or visit our website: [www.quadnetics.com](http://www.quadnetics.com)  
Registered Number: 1740011

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