



INVESTMENT UPDATE

Microsoft (MSFT) is finally coming around to the right vision for the company, namely their "Devices and Services" strategy. This accelerates the convergence of physical devices into the world of IT. We've recently written about the strong relationship Viscount (VSYS) has cultivated with Microsoft¹. This is giving Viscount strong visibility with large enterprise customers.

This does make it fairly certain that **we have in fact reached the tipping point for the "the internet of things" or what more hardware-oriented folks describe as the "trillion sensor network."** In any case, it gives Viscount an open opportunity to add another monetization facet to their business by licensing out the building blocks of their IP-based solution to physical access control.

In the near term, the ramp of year-over-year and sequential growth trends remains intact for the company as they enter the last days of the December quarter. **Revenue from their new products (Liberty and Freedom) is leading growth and becoming a larger portion of revenues.** These results are being achieved despite government agencies (their largest market) being budget constrained by the US government sequester.

Operationally Viscount has **added senior talent in distribution channel management and regional operations** along with more technical support staff to allow them to **convert more of their opportunity pipeline to sales.** These additions increase our confidence that the company is building the internal execution capability they will need in 2014.

The reason **we are excited about the licensing opportunity** is because 1) Viscount has a strong and visible partnership with Microsoft in this area, 2) they have over 60 patents pending in and around the converged physical/logical security space and 3) probably every access control vendor will be asked to offer tight integration with IT security and access control on Microsoft Active Directory and other role-based authorization systems.

With a robust and cost-effective licensing solution Viscount can achieve excellent penetration more quickly and with less capital and risk than a direct approach. The two go hand-in-hand at this stage of market development but things are likely to move more quickly next year.

Our base case IV model for VSYS suggests a company valuation of \$0.26/share versus the current \$0.07. As business results expand in 2014 we expect to see the company move towards our IV estimate.

¹ http://s3.amazonaws.com/Published_Research/Viscount_Systems_VSYS_Update_Nov_2013.pdf

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¹ Bloomberg, Thomson/Reuters/FirstCall, S&P Capital IQ and FactSet.