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Harmon Industries, Inc.

First Quarter Report

Three Months Ended March 31, 1995

Report to Shareholders

Our 1995 first quarter performance was mixed. Sales were up 14 percent at $29.4 million, but net earnings were down 53 percent at $706,000 compared to nearly $1.5 million for the 1994 first quarter. The principal reason for the decline in profitability relates to the costs involved in absorbing the Transportation Division of Servo Corporation of America, which was acquired late last year.

Servo, as many shareholders will recall, was the world's largest supplier of Hot Box Detector systems and other components to help railroads monitor the condition of bearings and wheels on railroad cars. Acquiring these products gave us a substantial entry into world markets and considerably expanded our product line. Since the Servo name is respected worldwide, we wanted the acquisition to proceed as seamlessly as possible, with no interruption in deliveries or service to customers.

As a consequence, we contracted with Servo to continue making product at its facilities in New York through the end of April until we could train our workers and transfer that production to our plant in Riverside, California. We paid a premium price to accomplish this, which is a major reason why our cost of sales and general and administrative expenses increased sharply during the past quarter. We deliberately overbuilt product during the first quarter so that we would have an adequate supply while we move the manufacturing equipment and inventory from New York to California, which will commence in early May. We expect to be able to produce these products in our California plant much more efficiently.

As a result, we anticipate the Servo acquisition will begin to contribute to profitability as early as this year's third quarter.

Apart from the short-term negative impact of the Servo acquisition and a deferral of some purchase orders anticipated for the first quarter, the overall operations of our first quarter were very positive.

- Our incoming order rate is 26 percent ahead of the same quarter a year ago, booking orders aggregating approximately $37 million in the first quarter. Orders for cab signal equipment, control systems and signal products were particularly strong. As a result, our backlog rose to over $51 million, the highest on record, up 16 percent from the $44.4 million backlog this time a year ago.

- Our international business is gradually accelerating. International orders (excluding Canada and Mexico) amounted to nearly $4 million in the first quarter. The largest order was for Ultra Cab and wayside equipment for the largest iron ore railroad in Australia. As our newly-acquired Servo sales force, which is already established overseas, gains familiarity with the broad Harmon product line, we anticipate it will make a material contribution to international sales.

- In addition, we acquired SERRMI Services, Inc. last February. It is a respected railroad signal design and engineering company that also provides wiring and grade crossing installations for railroads, primarily in the southeast portion of the United States. SERRMI materially expands our signal design and engineering services nationwide, and its location in Atlanta is especially important. It will enable us to better serve two Class I railroads which are major purchasers of many of the types of products that Harmon sells.

- Finally, under a grant from the Federal Railroad Administration, Harmon's Incremental Train Control System (ITCS), was selected to develop and test a high speed train control system along Amtrak's corridor between Chicago and Detroit. This grant represents the Clinton administration's continued commitment to making high-speed passenger rail a reality in this country. Harmon's system uses advanced technologies such as the Global Positioning System to monitor the location of trains and ensure their safe operation. This award demonstrates Harmon's technical excellence and its product positioning for the next generation of train control systems.

The first quarter's profit performance was not so much a disappointment as it was recognition of the reality that acquisitions are a necessary and inescapable investment to promote long-term growth. Servo was such an acquisition. The costs to absorb Servo's Transportation Division were predictable and factored into its purchase price. We believe that more than half of these "absorption" costs are already behind us.

Given that, we are looking at the total business picture, which is very favorable. Business is better than last year. Orders are much stronger. We have more products to sell, and we are in more locations. As a consequence, we are confident that 1995 will witness another record year for Harmon.

Björn E. Olsson
President & Chief Executive Officer
Blue Springs, Missouri
April 28, 1995

Consolidated Statements of Earnings (Unaudited)

(Dollars in thousands, except share data)

Three months ended March 31,	1995	1994
Net sales	$29,415	$25,902
Cost of sales	21,330	17,503
Research and development expenditures	1,022	990
Gross profit	7,063	7,409
Selling, general and administrative expenses	5,612	4,837
Amortization of cost in excess of fair value of net assets of subsidiary acquired	133	33
Miscellaneous (income) expense–net	(25)	(4)
Operating income	1,343	2,543
Interest expense	(147)	(43)
Investment income	17	14
Earnings before income taxes	1,213	2,514
Income tax expense (benefit):		
Current	535	1,063
Deferred	(28)	(45)
	507	1,018
Net earnings	$ 706	$ 1,496
Net earnings per common share	$ 0.10	$ 0.23
Weighted average shares outstanding (000s)	6,815	6,551

Corporate Data

Board of Directors

Robert E. Harmon
Chairman of the Board

Thomas F. Eagleton
Attorney-at-Law
Thompson & Mitchell
St. Louis, Missouri

Bruce M. Flohr
Chairman, President & CEO
RailTex, Inc.
San Antonio, Texas

Charles M. Foudree
Executive Vice President–
Finance, Treasurer and
Secretary

Rodney L. Gray
Chairman & CEO
Enron International, Inc.
Houston, Texas

* Lloyd T. Kaiser
President
Harmon Electronics, Inc.

Herbert M. Kohn
Attorney-at-Law
Bryan Cave
Kansas City, Missouri

Douglass Wm. List
Management Consultant
Baltimore, Maryland

Gerald E. Myers
Management Consultant
Tempe, Arizona

Björn E. Olsson
President and
Chief Executive Officer

Donald V. Rentz, President
Graham Wholesale Floral
Graham, Texas

Judith C. Whittaker
Vice President–Legal
Hallmark Cards, Inc.
Kansas City, Missouri

* Denotes Advisory Director

Condensed Consolidated Balance Sheets (Unaudited)

(Dollars in thousands)

	March 31, 1995	Dec. 31, 1994
Assets		
Current assets	$44,532	$42,730
Net property, plant and equipment	12,267	11,069
Other assets	15,166	14,596
	$71,965	$68,395
Liabilities and Stockholders' Equity		
Current liabilities	$17,100	$21,060
Long-term liabilities	11,081	4,272
Stockholders' equity	43,784	43,063
	$71,965	$68,395

Corporate Data, continued

Corporate Officers

Björn E. Olsson
President and
Chief Executive Officer

Robert E. Harmon
Chairman of the Board

Charles M. Foudree
Executive Vice President–Finance,
Treasurer and Secretary

Gary E. Ryker
Executive Vice President–
Marketing, Sales and Service

Ronald G. Breshears
Vice President–
Human Resources

Richard A. Daniels
Vice President–Transit Sales

Robert E. Heggestad
Vice President–Technology

John W. Johnson
Vice President–
Domestic Sales

William J. Scheerer
Vice President–
Business Development

Stephen L. Schmitz
Vice President–
Controller

Subsidiaries

Consolidated Asset Management Company, Inc. (CAMCO)
Riverside, California (2) †
Lee's Summit, Missouri

• J. Randall John, President

Electro Pneumatic Corporation
Riverside, California
Hicksville, New York

• Noel B. Smith, President

Harmon Electronics, Inc.
Atlanta, Georgia
Jacksonville, Florida
Louisville, Kentucky
Grain Valley, Missouri (3) †
Omaha, Nebraska
Warrensburg, Missouri (2) †

• Lloyd T. Kaiser, President

† Denotes number of plants and locations

International

Harmon Industries
Lausanne, Switzerland

Henkes-Harmon Industries, Pty. Ltd.
Mooroolbark, Victoria, Australia

Vale-Harmon Enterprises, Ltd.
Saint-Laurent, Quebec, Canada

Corporate Headquarters

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Blue Springs, Missouri 64015

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