

H A R M O N

2



Harmon Industries, Inc.

Second Quarter Report

Six Months Ended June 30, 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 June 30,		Six months ended June 30,	
	1995	1994	1995	1994
Net sales	\$32,854	\$32,166	\$62,269	\$58,069
Cost of sales	21,971	21,882	43,279	39,386
Research and development expenditures	1,236	966	2,279	1,956
Gross profit	9,647	9,318	16,711	16,727
Selling, general and administrative expenses	5,990	5,377	11,602	10,214
Amortization of cost in excess of fair value of net assets acquired	133	33	266	67
Miscellaneous (income) expense—net	(7)	(20)	(32)	(24)
Operating income	3,531	3,928	4,875	6,470
Interest expense	(190)	(80)	(337)	(123)
Investment income	60	5	76	20
Earnings before income taxes	3,401	3,853	4,614	6,367
Income tax expense (benefit):				
Current	1,414	1,630	1,949	2,693
Deferred	(71)	(107)	(99)	(152)
	1,343	1,523	1,850	2,541
Net earnings	\$ 2,058	\$ 2,330	\$ 2,764	\$ 3,826
Net earnings per common share	\$ 0.30	\$ 0.36	\$ 0.41	\$ 0.58
Weighted average shares outstanding (000s)	6,824	6,559	6,819	6,555

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

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

* Stephen L. Schmitz
Vice President—
Controller

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

* Denotes Advisory Director

Condensed Consolidated Balance Sheets (Unaudited)

(Dollars in thousands)

	June 30, 1995	Dec. 31, 1994
Assets		
Current assets	\$ 47,412	\$ 42,730
Net property, plant and equipment	12,886	11,069
Other assets	14,876	14,596
	<u>\$ 75,174</u>	<u>\$ 68,395</u>
Liabilities and Stockholders' Equity		
Current liabilities	\$ 19,187	\$ 21,060
Long-term liabilities	10,377	4,272
Stockholders' equity	45,610	43,063
	<u>\$ 75,174</u>	<u>\$ 68,395</u>

Corporate Data, continued

Corporate Officers	Subsidiaries	International
Björn E. Olsson President and Chief Executive Officer	Consolidated Asset Management Company, Inc. (CAMCO) Riverside, California (2) † Lee's Summit, Missouri	Harmon Industries Lausanne, Switzerland
Robert E. Harmon Chairman of the Board	<ul style="list-style-type: none"> • J. Randall John, President 	Henkes-Harmon Industries, Pty. Ltd. Mooroolbark, Victoria, Australia
Charles M. Foudree Executive Vice President–Finance, Treasurer and Secretary	Electro Pneumatic Corporation Riverside, California Hicksville, New York	Vale-Harmon Enterprises, Ltd. Saint-Laurent, Quebec, Canada
Gary E. Ryker Executive Vice President– Marketing, Sales and Service	<ul style="list-style-type: none"> • Noel B. Smith, President 	
Ronald G. Breshears Vice President– Human Resources	Harmon Electronics, Inc. Atlanta, Georgia Jacksonville, Florida Louisville, Kentucky	
Richard A. Daniels Vice President–Transit Sales	Grain Valley, Missouri (3) † Omaha, Nebraska Warrensburg, Missouri (2) †	
Robert E. Heggstad Vice President–Technology	<ul style="list-style-type: none"> • Lloyd T. Kaiser, President 	
John W. Johnson Vice President– Domestic Sales	† Denotes number of plants and locations	
William J. Scheerer Vice President– Business Development		
Stephen L. Schmitz Vice President– Controller		
		Corporate Headquarters 1300 Jefferson Court Blue Springs, Missouri 64015 ☎ 816/229-3345 Telefax: 816/229-0556



1300 Jefferson Court
Blue Springs, Missouri 64015

Second Quarter Report to Shareholders