HARMON

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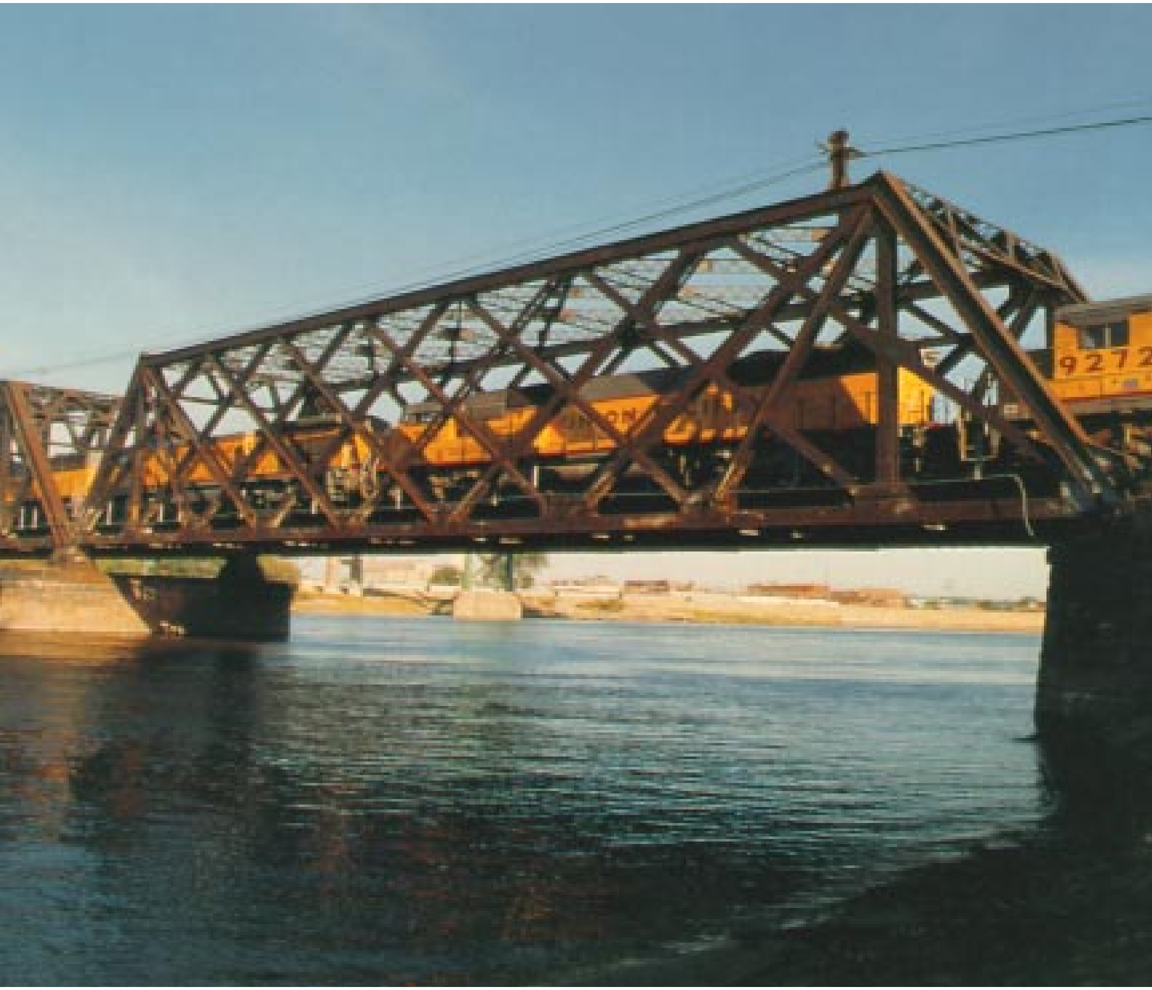

# Harmon Industries, Inc.

**Third Quarter Report**

**Nine Months Ended September 30, 1995**

## Report to Shareholders

Sales for the third quarter increased 29 percent to a record $38.0 million from $29.4 million last year. Year-to-date sales also established a new high of $100.3 million, approximately 15 percent above last year's sales of $87.5 million.

Third quarter net earnings were $2.3 million versus $2.2 million last year. Year-to-date earnings, however, trailed last year's at $5.0 million versus $6.0 million.

Earnings per share were 33 cents for both the 1995 and 1994 third quarters and 74 cents for the first nine months of 1995 compared with 91 cents for the same period a year ago.

### Profit Margins

Profit margins are lower than they were a year ago. Gross profit percentage was 25.2 percent of sales in the third quarter, down from 29.4 percent a year ago. Gross profit for nine months was 26.2 percent versus 29.0 percent the year before. The decline in gross margins to date is due to a $1.0 million increase in research and development expenditures, lower profit margins on overall revenues from our systems and contract business (but only because these contracts call for us to deliver certain non-Harmon products on which we make only a handling charge), and higher than expected costs involved in assimilating the hot box detector acquisition into our organization.

The acquired hot box detector product incurred higher than normal production costs while we manufactured it at the selling company's plant on Long Island; it absorbed one-time costs to move its production to our plant in Riverside, California; and it encountered a parts shortage that hampered normal production flow.

The parts issue is being resolved, but we are paying premium prices to do so. We are sacrificing near-term profit margins for long-term business relations. Consequently, we do not expect this acquired business to make a significant profit contribution in 1995, but we anticipate it will provide a full complement of earnings in 1996.

### High Speed Rail Contract

In September we received a $3.2 million purchase order from AMTRAK for equipment and engineering on a Federal Railroad Administration high-speed rail demonstration project with the Michigan Department of Transportation. Harmon and AMTRAK will install this test system on 45 miles of track in southwestern Michigan. Eventually this system may be used to upgrade the entire Detroit-Chicago rail corridor. The project is very significant because it uses our Incremental Train Control System (ITCS) technology, which we hope will become a standard for the railroad industry. Presently we are the only company actively marketing a system that meets the train control needs of expanded high-speed rail operations.

### New Orders Brisk

Incoming orders continued at a brisk pace. Year-to-date orders of $102 million were 27 percent ahead of last year's comparable mark of $80 million. New bookings reflected particularly increased demand for our control systems, signal products and systems, and carborne equipment.

The increase in orders reflected an excellent balance across our markets. Year-to-date orders from our freight railroad customers were up 25 percent, and our smaller but rapidly growing transit markets reflected a 50 percent increase in new orders.

Even more important, three transit authorities have approved solid state applications in the train control area. This is a major triumph for modern technology, and one that opens up new opportunities for Harmon since nearly all of our designs involve solid state technology. Plus, we were the low bidder on the third stage signal systems for the New York City subway system, which to date, has generated approximately $10 million in business for Harmon and is a further confirmation of our technological solid state leadership in speed controls.

Orders continued firm through October. October 1995 order highlights included a $2.2 million contract from the Union Pacific Railroad to provide VHLC and EC-4 systems for its suburban Chicago commuter line. In addition, we received a sizable order from the Peoples Republic of China for hot box detector systems for its main line railroad systems

### Backlog Strong and Growing

Despite record shipments in the third quarter, the strong flow of new orders kept our backlog solid at $44.5 million as of September 30, 1995, roughly 50 percent ahead of our backlog a year ago.

### ISO Certification

In October, Electro Pneumatic Corporation, our subsidiary in Riverside, California, was awarded an ISO 9001 certification for its compliance with ISO manufacturing and design standards in its train control manufacturing operations. Our Jacksonville, Florida, plant received a similar certification earlier this year.

### Outlook

We expect to report a solid fourth quarter. Sales for the full year will set a new record. After a near nine-month halt, many long-standing orders, which had been deferred because of business conditions beyond our control, are now reentering our pipeline. The business outlook remains firm.

Björn E. Olsson
President & Chief Executive Officer

Blue Springs, Missouri
November 10, 1995

## Consolidated Statements of Earnings (Unaudited)

(Dollars in thousands, except earnings per share data)

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | 1995 | 1994 | 1995 | 1994 |
| Net sales | $38,026 | $29,448 | $100,296 | $87,517 |
| Cost of sales | 26,954 | 19,997 | 70,254 | 59,382 |
| Research and development expenditures | 1,503 | 805 | 3,761 | 2,761 |
| Gross profit | 9,569 | 8,646 | 26,281 | 25,374 |
| Selling, general and administrative expenses | 5,464 | 4,973 | 17,067 | 15,188 |
| Amortization of cost in excess of fair value of net assets acquired | 144 | 11 | 410 | 78 |
| Miscellaneous (income) expense–net | (13) | 21 | (45) | (3) |
| Operating income | 3,974 | 3,641 | 8,849 | 10,111 |
| Interest expense | (197) | (85) | (534) | (208) |
| Investment income | 4 | 1 | 80 | 21 |
| Earnings before income taxes | 3,781 | 3,557 | 8,395 | 9,924 |
| Income tax expense (benefit): | | | | |
| Current | 1,524 | 1,491 | 3,473 | 4,184 |
| Deferred | (23) | (85) | (122) | (237) |
| | 1,501 | 1,406 | 3,351 | 3,947 |
| Net earnings | $ 2,280 | $ 2,151 | $ 5,044 | $ 5,977 |
| Net earnings per common share | $ 0.33 | $ 0.33 | $ 0.74 | $ 0.91 |
| Weighted average shares outstanding (000s) | 6,837 | 6,563 | 6,825 | 6,558 |

## 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)

| | Sept. 30, 1995 | Dec. 31, 1994 |
|---|---|---|
| **Assets** | | |
| Current assets | $54,401 | $42,730 |
| Net property, plant and equipment | 13,063 | 11,069 |
| Other assets | 14,766 | 14,596 |
| | $82,230 | $68,395 |
| **Liabilities and Stockholders' Equity** | | |
| Current liabilities | $22,708 | $21,060 |
| Long-term liabilities | 11,632 | 4,272 |
| Stockholders' equity | 47,890 | 43,063 |
| | $82,230 | $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
Hauppauge, New York

- Steven L. Schmitz,
  Acting 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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Harmon
INDUSTRIES

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Blue Springs, Missouri  64015

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