BUSINESS REVIEW

OVERVIEW

For the six months ended 30th September 2001, Johnson Electric's total sales decreased by 6% to US$372 million.

This decline resulted from a softening of demand across virtually all of the company's product application segments as the economic slowdown in North America and Europe led many of Johnson Electric's customers to reduce inventory levels and defer orders. The terrorist attacks in the United States on 11th September further compounded an already challenging market environment.

INVESTING FOR THE FUTURE

Johnson Electric has consistently sought to invest in businesses with above average growth prospects and which offer potential for enhancing the Group's competitive position in the field of precision motors. In particular, we continue to pursue opportunities that are arising from the long-term trend of US and European manufacturers to outsource the production of micromotors and motor systems. Central to this strategy is the ability of Johnson Electric to leverage its low cost supply and production platform in southern China.

In July 2001, we acquired certain manufacturing assets of the electric motor components business of Textron Automotive Company's Kautex Textron division for a purchase consideration of US$12.5 million. Based in Manchester, New Hampshire, U.S.A., the business manufactured fuel pump armatures and cruise control stators for automotive tier-one suppliers and has estimated annual sales of US$16 million. Under a related transition services agreement, Kautex Textron employees at the Manchester facility are to assist Johnson Electric for several months in the manufacture of stators and armatures while we transfer the production to our plants in Mexico and China. The transfer is expected to be complete in the second half of this year.

In August 2001, we also acquired certain manufacturing assets of the automotive electric seat motor business of ArvinMeritor's Light Vehicle Systems division for a purchase consideration of US$11.7 million. ArvinMeritor manufactured seat motors at plants in Esson, France, Queretaro, Mexico, and Gordonsville, Tennesse in the U.S.A. and has estimated annual sales of approximately US$50 million. Under a related subcontracting, supply and transition agreement, ArvinMeritor acts as a manufacturing subcontractor to Johnson Electric to ensure continuity of motor supply to the customers, while we arrange to consolidate such seat motor production at our manufacturing complex in Shajing, China. The transfer of production to China is expected to be complete by mid-2002.

For the six months ended 30th September 2001, the sales contributions from these two acquisitions amounted to US$13 million. Their full six months' sales will be included in the Group's results for the second half of the financial year. Excluding the Textron and ArvinMeritor acquisitions, total Group sales amounted to US$358 million, a decline of 9% over the corresponding period in 2000.

OPERATING PERFORMANCE

Sales Overview

Notwithstanding the broad-based impact of the global economic slowdown, Johnson Electric's sales performance varied across product segments and geographic regions.

Over the first half of the financial year, sales of the Automotive Division were relatively stable. In contrast, some major segments within the Commercial Motors Division, notably Power Tools and Business Equipment/Personal Products, reported larger declines in sales, after hitting record highs in sales in the first half of 2000.

Geographically, the Group experienced sales decreases across all regions. Sales to Europe, North America, and Hong Kong/China decreased by approximately 5%. Sales to Asia Pacific decreased nearly 16%, due mainly to a double-digit decline in sales to the business equipment customers which have their production bases in this region.

Excluding the acquisitions from Textron and ArvinMeritor, sales to North America and Europe decreased 13% and 7% respectively.

Automotive Division

Total sales of the Automotive Division increased by 0.4% to US$221 million. The Automotive Division comprises Automotive Motors Hong Kong; Gate S.p.A. ("Gate") in Europe; and Johnson Electric Automotive Motors ("JEAM") in North America.

Sales of Automotive Motors Hong Kong, representing the core automotive micromotor business based in Hong Kong, decreased 4% to US$64 million, with unit volume down slightly by 1%. Slowing demand in relatively mature products was largely offset by continuing robust growth in such new product applications as electronic throttle control and mirror adjustors.

Including the acquisitions from Textron and ArvinMeritor, sales increased 15% to US$77 million. The sales of these acquisitions have become the responsibility of Automotive Motors Hong Kong, as their production will mostly be transferred to and consolidated at our manufacturing complex in Shajing, China.

Sales of Gate in Europe continued to be stable, up 3% to US$90 million, with unit volume growth of 14%.

Sales of JEAM in North America decreased 18% to US$53 million, with unit volume down 15%. This was due partly to a decrease of 20% in the sales of starter motors used in such applications as garden equipment and outboard marine engines in the U.S.A. In addition, for most of the first half of this financial year, JEAM was engaged in a major restructuring programme aimed at enhancing its long-term competitiveness. This involved the closure of its manufacturing facility in Columbus, Mississippi, and the transfer of its production responsibilities to Johnson Electric plants in China and Mexico.

Commercial Motors Division

Sales to the power tools sector decreased 26% to US$43 million, with unit volume down 13%. This decline was mainly due to sluggish end-user demand conditions and a significant inventory correction by Johnson Electric's customers in the U.S.A. and Europe.

Sales to the home appliances sector declined 4% to US$56 million, with a decrease of 7% in unit volumes. Sales to floor-care product applications continued to grow at a rate of nearly 30%, although this increase was more than offset by lower sales in small kitchen appliances, including mixers, blenders and can openers. As the proportion of floor-care product applications increases further in the sales mix, we anticipate improved sales performance for the home appliances sector in future.

Sales to the business equipment and personal product sectors decreased 15% to US$43 million, with unit volume down 10%. With demand substantially below year 2000 levels, sales to printer products declined 17%. In personal products, the Group continued to see healthy growth in certain new product applications, including electric toothbrushes and toys, but this was more than offset by a decline in micromotor sales to hair dryer manufacturers.

Audio-visual sector sales increased 14% to US$9 million, with unit volume growth of 28%. This business sector is still in a relatively early stage of development following the commencement of a joint venture with Nidec Corporation of Japan in July 2000. Sales are not expected to be material in relation to the Group's total business until after the current financial year.

ENTERPRISE RESOURCE PLANNING ("ERP")

About a year ago, we announced our decision to work with Oracle Greater China, Oracle Corporation, in changing our system to ERP.

Based on the progress of our ERP project to date, we expect implementation of Supply Chain Management and Financial Management to be completed during this financial year as scheduled. Order Management Implementation will commence from March 2002. The project aims to improve our operational efficiencies and responsiveness in the coming years.

INVESTING IN PEOPLE

As of 30th September 2001, the Group employed a total of over 23,000 full-time employees, including contract manufacturing labour. The Group provides competitive remuneration packages and various types of benefit schemes appropriate to the local labour markets.

Organizational development constitutes the core of our human resources initiatives in the coming year. Our performance appraisal system is being modified to focus more on learning and individual development. A set of core leadership competencies has been developed against which we set our standard for behavioural and cultural change.

Johnson University ("JU") established in 1998, has now six colleges providing a wide range of vocational and technical training programmes. The JU Master of Science (M.Sc.) in engineering degree programme is in its second year and is expected to produce the first batch of graduates in the coming year. We continue to work towards broadening JU's programme offering as we believe continuous learning by our people holds the key to the Group's success.

The Group continues to increase its focus on environmental, health and safety issues as it strives to be a responsible corporate citizen in all the countries in which it operates.

PROSPECTS

Looking ahead, most macro-economic indicators suggest that the current depressed global economic environment will extend well into 2002. The Group therefore anticipates that trading conditions will remain challenging in the near term.

For the financial year 2001/02 as a whole, we expect the combination of sales contributions from recent acquisitions and our growth in new product applications to help mitigate the effects of continued weak demand conditions.

We also expect to benefit from management actions and favorable trends on our cost side. First, the closure and relocation of Johnson Electric's manufacturing facility in Columbus, Mississippi, will provide for a more cost competitive product offering in the North America market. Second, lower commodity prices for copper and steel are enabling us to minimize our raw material costs. Third, management has also instituted a number of cost reduction initiatives designed to ensure that we sustain a compelling value proposition for our customers and at the same time achieve superior levels of profitability.

In this period of unprecedented economic uncertainty, we nonetheless remain confident that the underlying factors that drive our long-term sales growth remain sound. Johnson Electric will continue to build on its unrivalled low-cost manufacturing capabilities in China and expects to make further investments in new product applications and selective new acquisitions in the months and years ahead.

We believe that Johnson Electric is better positioned than ever to exploit growth opportunities that are emerging from the fundamental restructuring of the global manufacturing supply chain now underway. Our balance sheet remains strong, and the Group is essentially debt-free, with a substantial cash reserve. Once our markets begin to recover, Johnson Electric's shareholders can be confident that the Group's competitive strengths will be a basis for continued value creation.