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Reports 3Q09 Results; Maintaining Buy Rating and \$26 Target Price

Buy
Target Price: \$26

Investment Summary

Aqua America reported 3Q09 results that were largely in line with expectations. On the top line, revenue of \$180.8 million (a 2.1% YoY increase) was just shy of the consensus estimate of \$189 million. The ability to post an increase in revenue in the quarter YoY was especially impressive given the extreme wet weather experienced in the company's Mid-Atlantic operations, which led to declines in customer water usage and negatively impacted bottom-line results by \$0.03 per share. That aside, EPS in the quarter of \$0.25 beat our estimate of \$0.24 by a penny and met consensus. We have slightly adjusted our estimates to account for the 3Q09 results, and maintain our Buy rating and \$26 target price, based on the shares attaining a level of 28x our 2010 EPS estimate of \$0.93.

Discussion

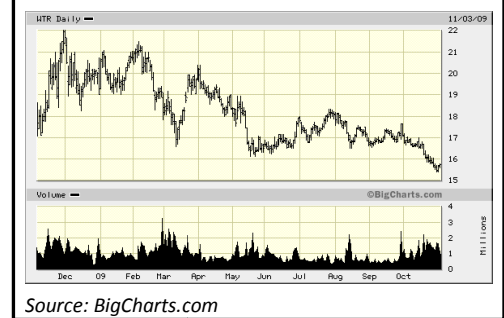
- **Poor weather (once again) negatively impacted quarterly results.** The amount of rainfall that occurred in several of Aqua America's operating areas hindered revenue growth (although it did increase 2.1% to \$180.1 million). In Pennsylvania, send-out into the system was down more than 9%, and the company noted that weather service records show that this summer was the eight-wettest summer in the past 137 years in southeastern Pennsylvania. In New Jersey, send-out was down more than 19%.

While EPS in the quarter of \$0.25 compares a bit unfavorably to the \$0.26 in the same quarter last year, it is important to note that weather accounted for a \$0.03 reduction in EPS in 3Q09, and 3Q08 saw the benefit of a system sale of \$0.02. With normal weather and adjusting for the system sale in 3Q08, third quarter results would have been favorable versus the same quarter last year.

- **Improving fundamentals.** Thus far in 2009, Aqua America has been granted rate relief to increase revenue by \$29.3 million, and has rate cases pending totaling \$12 million in New York, Indiana, Missouri, Virginia, and North Carolina. The company is expecting to seek additional rate relief of \$57 million through rate filings in 4Q09. Aqua America has also done a nice job expanding operations in 2009, completing 15 acquisitions. The company has completed more acquisitions in the first three quarters of 2009 than in all of 2008. Additionally, this October the company's largest subsidiary, Aqua Pennsylvania, Inc., announced plans to issue up to \$75 million of long-term first mortgage bonds, which were rated AA- with a 1+ recovery rating by Standard and Poor's (S&P). Aqua America intends to use the funds to help finance part of its \$1 billion multi-year capital plan to improve the distribution infrastructure for its customers in Pennsylvania. For 2009, Aqua expects to invest approximately \$300 million in infrastructure improvements.

Price	\$15.96
52-Week High/Low	\$22.00 - 15.39
Shares Outstanding (mm)	135.92
Market Cap. (mm)	\$2,169.25
Average Daily Volume (mm)	1.18

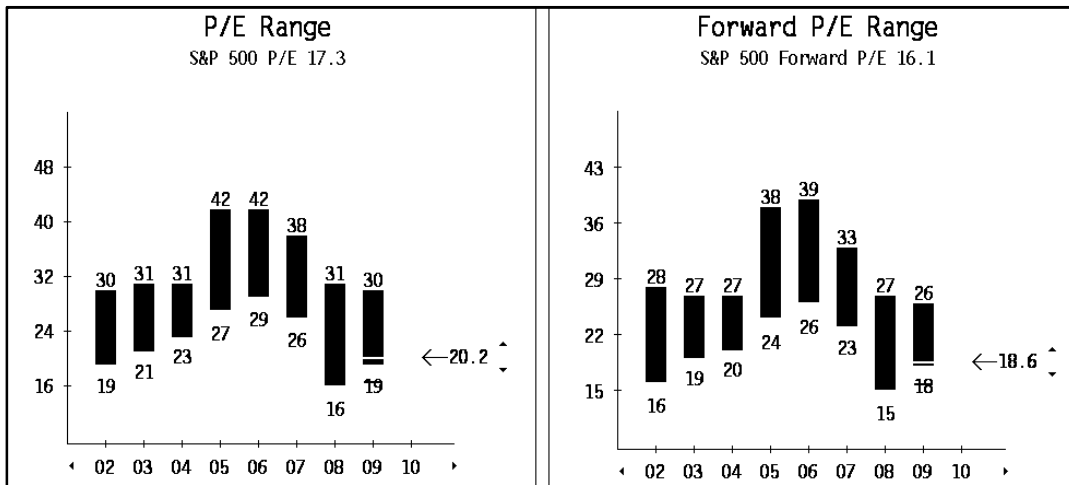
EPS	FY08A	FY09E	FY10E
Mar	\$0.11	\$0.14A	\$0.18
Jun	\$0.17	\$0.19A	\$0.22
Sep	\$0.26	\$0.25A	\$0.28
Prior	-	\$0.28	\$0.30
Dec	\$0.19	\$0.22	\$0.26
FY	\$0.73	\$0.79	\$0.93
Prior	-	\$0.83	\$0.95
Consensus	-	\$0.80	\$0.91
P/E	22.0x	20.2x	17.1x
FY Rev. (mm)	\$627.0	\$683.3	\$724.3



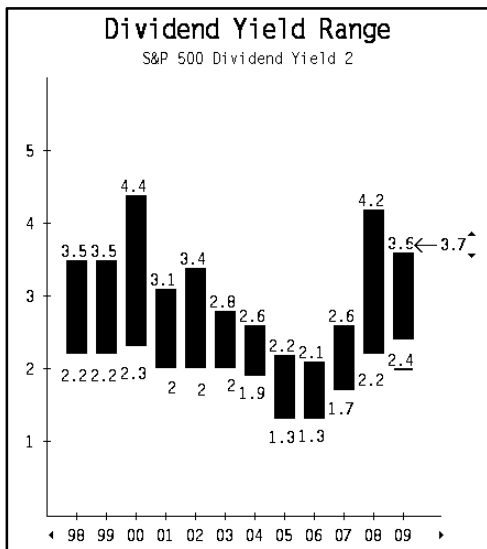
Adjusting estimates. We have adjusted our estimates slightly as follows: our new 2009 EPS estimate is now \$0.79 from \$0.83, and our new 2010 EPS estimate is now \$0.93 from \$0.95. We consider the changes insignificant from a valuation perspective.

Valuation. With the shares now trading at 17x our forward estimate, we consider them attractively priced at current levels. Despite improving fundamentals in the company’s operations, share prices have continued to edge lower. Our view is that this condition will not persist much longer, due to revenue growth via rate case activity and tuck-in acquisitions, continued focus on cost reduction, and hopefully a more normalized (better) weather pattern in 2010.

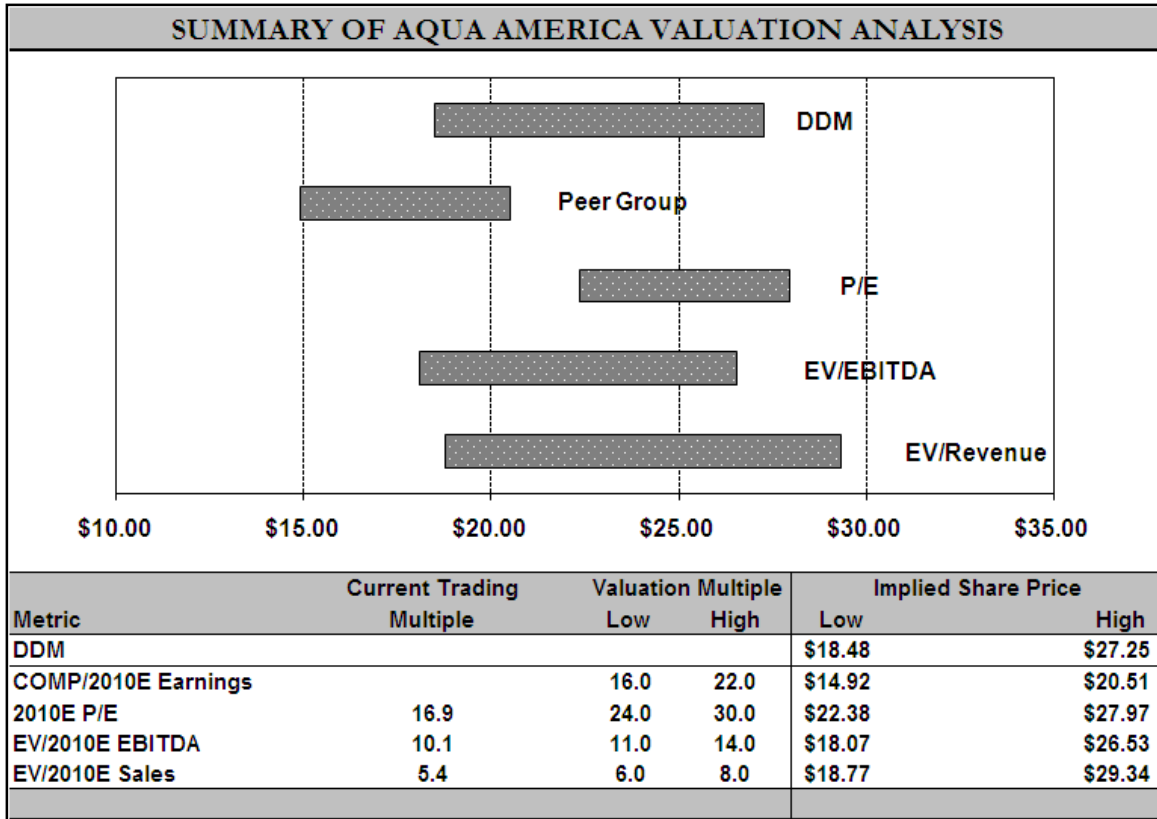
We recommend investors add to or take new positions, especially given that the shares are trading toward the bottom of historical P/E ranges and carry a dividend yield of 3.7%. We reiterate our Buy rating and maintain our target price of \$26, based on a P/E multiple of 28x our 2010 EPS estimate of \$0.93.



Source: Baseline



Source: Baseline



Soucre: Company reports, Brean Murray, Carret & Co. estimates

Aqua America		Quarterly Income Statement, 2009E								
(\$000, except per share data)										
Fiscal year ends December 31										
	1Q09	% Rev or Margin	2Q09	% Rev or Margin	3Q09	% Rev or Margin	4Q09E	% Rev or Margin	2009E	% Rev or Margin
Sales	154,487		167,333		180,826		180,619		683,265	
Operating & maintenance	66,989	43.4%	68,549	41.0%	68,488	37.9%	73,151	40.5%	277,177	40.6%
Depreciation	26,387	17.1%	24,972	14.9%	25,436	14.1%	25,829	14.3%	102,624	15.0%
Amortization	2,755	1.8%	3,064	1.8%	3,029	1.7%	3,071	1.7%	11,919	1.7%
Non-income taxes	11,590	7.5%	11,884	7.1%	12,418	6.9%	12,101	6.7%	47,993	7.0%
Operating income	46,766	30.3%	58,864	35.2%	71,455	39.5%	66,468	36.8%	243,553	35.6%
Interest expense, net	16,628	10.8%	16,809	10.0%	17,256	9.5%	17,610	9.8%	68,303	10.0%
AFC	(625)	-0.4%	(568)	-0.3%	(747)	-0.4%	(1,000)	-0.6%	(2,940)	-0.4%
Gain on sale of other assets	(133)	-0.1%	(80)	0.0%	(162)	-0.1%	(250)	-0.1%	(625)	-0.1%
Income before taxes	30,896	20.0%	42,703	25.5%	55,108	30.5%	50,107	27.7%	178,814	26.2%
Income taxes	12,525	40.5%	16,850	39.5%	21,638	39.3%	20,043	40.0%	71,056	39.7%
Net income	18,371	11.9%	25,853	15.5%	33,470	18.5%	30,064	16.6%	107,758	15.8%
Earnings per share	\$0.14		\$0.19		\$0.25		\$0.22		\$0.79	
Shares outstanding (000)	135,876		135,939		136,260		136,460		136,134	
Aqua America		Quarterly Income Statement, 2010E								
(\$000, except per share data)										
Fiscal year ends December 31										
	1Q10E	% Rev or Margin	2Q10E	% Rev or Margin	3Q10E	% Rev or Margin	4Q10E	% Rev or Margin	2010E	% Rev or Margin
Sales	163,756		177,373		191,676		191,456		724,261	
Operating & maintenance	68,123	41.6%	72,723	41.0%	75,904	39.6%	75,817	39.6%	292,566	40.4%
Depreciation	26,201	16.0%	25,187	14.2%	23,959	12.5%	25,847	13.5%	101,194	14.0%
Amortization	2,456	1.5%	2,661	1.5%	1,917	1.0%	2,106	1.1%	9,140	1.3%
Non-income taxes	10,972	6.7%	11,174	6.3%	11,501	6.0%	11,679	6.1%	45,326	6.3%
Operating income	56,005	34.2%	65,628	37.0%	78,395	40.9%	76,008	39.7%	276,036	38.1%
Interest expense, net	17,194	10.5%	17,737	10.0%	16,101	8.4%	17,997	9.4%	69,029	9.5%
AFC	(1,000)	-0.6%	(1,000)	-0.6%	(1,000)	-0.5%	(1,000)	-0.5%	(4,000)	-0.6%
Gain on sale of other assets	(500)	-0.3%	(500)	-0.3%	(500)	-0.3%	(500)	-0.3%	(2,000)	-0.3%
Income before taxes	40,310	24.6%	49,391	27.8%	63,795	33.3%	59,511	31.1%	213,007	29.4%
Income taxes	16,124	40.0%	19,756	40.0%	25,518	40.0%	23,805	40.0%	85,203	40.0%
Net income	24,186	14.8%	29,634	16.7%	38,277	20.0%	35,707	18.7%	127,804	17.6%
Earnings per share	\$0.18		\$0.22		\$0.28		\$0.26		\$0.93	
Shares outstanding (000)	136,710		136,960		137,210		137,460		137,085	

Source: Company Reports, Brean Murray, Carret & Co. estimates

Important Disclosures

Ratings and Target Price History



Priced intraday on 11/4/09.

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- Buy - Expected to appreciate by at least 10% within the next 12 months.
- Hold - Fully valued, not expected to appreciate or decline materially within the next 12 months.
- Sell - Expected to decline by at least 10% within the next 12 months.

	# of Securities	% of Total Securities	# of IB-Related Securities in Past 12 mos.	% of Total Securities
BUY	105	57.38%	10	9.52%
HOLD	65	35.52%	0	0%
SELL	11	6.01%	0	0%
NOT RATED	2	1.09%	0	0%
TOTAL	183			

Note: Stock price volatility may cause temporary non-alignment of some ratings with some target prices.

Valuation Methodology and Risks

Aqua America (WTR): Our \$26 target price is based on the shares attaining a level of 28x our 2010 EPS estimate of \$0.93. Risks to the achievement of our target price include weather, acquisitions, interest rates, environmental / public health responsibilities and regulatory climate.

Analyst Certification

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