

Aqua America, Inc. (WTR)

3Q10 Beats, Remains on Track for Strong 2010 Results; Maintain Rating

| | | | | | | | |
|-----------------------|----------|---------------|------------|--------|-------|-------|-------|
| Price: (11/5/10) | 21.85 | Rating: | Outperform | FY Dec | 2009A | 2010E | 2011E |
| 52WK H-L: | 22 - 16 | | | Q1 | 0.14A | 0.16A | |
| Market Cap (mil): | 2,993.45 | Suitability: | Lower Risk | Q2 | 0.19A | 0.22A | |
| Shares Out (mil): | 137.0 | | | Q3 | 0.25A | 0.32A | |
| Float (mil): | 136.3 | | | Q4 | 0.20A | 0.21E | |
| Avg. Daily Vol (mil): | 0.66 | | | Total | 0.77A | 0.90E | 1.00E |
| | | Price Target: | 22 | FY P/E | 28.4 | 24.3 | 21.9 |
| Dividend | 0.58 | | | | | | |
| Yield (%) | 2.65 | | | | | | |

Please refer to Appendix - Important Disclosures and Analyst Certification.

David E. Parker
dparker@rwbaird.com
813.274.7620

Maggie Hughes
mhughes@rwbaird.com
414.765.3968

Action

WTR well positioned to report improved EPS growth and returns; maintain Outperform rating. 3Q10 EPS handily beats expectations, as water consumption (+9%) and continued O&M containment drive strong bottom line results. We expect more consistent EPS growth (8-10%) in future years, with acquisitions potentially providing upside. WTR's execution of its capital plan (2-3x depreciation) coupled with regular rate case filings and the adoption of additional recovery mechanisms could support double-digit EPS growth rates.

Summary

- **3Q10 EPS beats expectations, as hot/dry weather and continued cost control drive 30% YOY earnings growth.** WTR reported 3Q10 EPS of \$0.32 versus \$0.25 in 3Q09 and our estimate of \$0.29. 3Q10 consensus estimate was \$0.28.
 - **Upside to our EPS estimate driven by continued focus on cost control.** Revenue increased 14.9% YOY due to a 9% increase in customer usage due to warmer summer weather, while total operating expenses increased 8.1%.
- **Pending rate relief requests.** WTR has received \$48.6 million in rate relief YTD, including case completions in PA, NJ, NY, NC, MO, OH, IN, ME, and VA. \$19.1 million of rate cases are still pending.
 - An additional \$11.5 million in rate requests are expected to be filed in remainder of 2010, effective in 2011 and 2012.
- **Opportunistic acquisitions continue to grow customer base.** Management continues to be active on the acquisition front, completing 14 acquisitions YTD including two in 3Q10. WTR still plans to complete ~25 acquisitions in 2010.
- **Continued capital investment opportunities.** WTR invested \$98.5 million in 3Q10 (\$239.5 million YTD) and remains on track to invest over \$300 million for utility system improvements in 2010.
- **Baird estimates.** We are maintaining our 2010, 2011, and 2012 estimates at \$0.90, \$1.00, and \$1.05, respectively. We maintain our \$22 price target and Outperform rating. We expect solid stock price support as WTR returns to its historical performance levels, net income growth (8-10% annually) and financial and operation performance consistency.

Details

WTR reported 3Q10 EPS of \$0.32 versus \$0.25 in 3Q09 and our estimate of \$0.29. 3Q10 consensus estimate was \$0.28.

Figure 1: 3Q10 Results Variance

| Aqua America (WTR - NYSE) | | | | | | | | |
|----------------------------|-------------------|---------------|-------|---------------|----------|--------------------|-------|-------|
| Quarterly Results Variance | | | | | | | | |
| | Quarterly Results | | | | | Percent of Revenue | | |
| | 3Q10 | 3Q09 | % Chg | Baird | Variance | 3Q10 | 3Q09 | Baird |
| Revenue | \$208 | \$181 | 14.9% | \$199 | 4.2% | | | |
| Operating Expenses | 118 | 109 | 8.1% | 116 | 1.6% | 56.9% | 60.5% | 58.3% |
| Operating Income | 90 | 71 | 25.4% | 83 | 7.7% | 43.1% | 39.5% | 41.7% |
| Pretax Income | 72 | 55 | 30.3% | 64 | 12.5% | 34.6% | 30.5% | 32.0% |
| Taxes | 28 | 22 | | 25 | | 13.5% | 12.0% | 12.5% |
| Net Income | \$44 | \$33 | 30.7% | \$39 | 12.3% | 21.1% | 18.5% | 19.5% |
| EPS | \$0.32 | \$0.25 | 29.6% | \$0.29 | 9.8% | | | |
| Diluted Shares | 137 | 136 | | 138 | | | | |

3Q10 nonrecurring and other items of note: None

3Q09 nonrecurring and other items of note: None

Source: Company reports; RW Baird estimates

Outlook

With strong EPS performance YTD (+22%), we believe WTR remains on track to grow 2010 EPS by >15%, higher than its historic growth rate (7-10%) because of strong 3Q10 results. 3Q10 water consumption increased +9% YOY, and YTD consumption increased +5%. In addition, management expects 1% organic customer growth will also contribute to this YOY EPS growth.

8-10% EPS growth is expected longer term, supported by organic customer growth (2-3%), successful rate case execution, and continued infrastructure investment (2.5-3x depreciation). WTR increased its dividend rate by 7% which is expected to keep the company's dividend payout ratio between 60-70%. Management's continued focus on controlling O&M costs and reducing interest expense should add more scalability to the model going forward.

Capital expenditures are still expected to be \$300 million in 2010 (~2.5x depreciation levels), which should further support EPS growth. Over 90% of this capital will be invested in system upgrades (main, pipes, hydrants, etc.), which provide direct value to customers; <10% will be invested in mandatory environmental upgrades. Most of WTR's Midwest and Mid Atlantic states (except New Jersey) employ some type of infrastructure surcharge mechanism, which allows WTR to earn a return on its infrastructure investments in between rate cases.

Longer term, we expect a continuation of WTR's constructive regulatory environments to provide solid 7-10% annual EPS growth reflecting substantial investment opportunities to strengthen its water delivery systems. More widespread acceptance of DSIC-like mechanisms should elicit increased investment, given decreased regulatory lag. Acquisitions of water and wastewater systems, which typically have substantial capital investment needs to improve water quality and strengthen the water delivery system, should continue to provide additional upside.

Results

Revenue increased by nearly 15% YOY driven by steady rate relief, as well as increased customer consumption (+9%) reflecting more warmer and drier-than-normal weather in 3Q10 as compared to a cooler and wetter-than-normal 3Q09. Management estimated that organic growth contributed 1% for 3Q10. The remaining 14% growth can be divided evenly between increased revenue from rate cases (+7%) and increased water consumption (+7%). New Jersey, Pennsylvania, and Ohio experienced increased consumption at rates of 30%, 10%, and 12%, respectively. Other service areas, namely Texas, Illinois, and Florida, experienced YOY decreases in customer usage, highlighting the geographic diversification from which WTR benefits,

Although revenue increased 15%, O&M expense rose only about 6.5%. Though this is higher than WTR's typical O&M run rate, some non-core items contributed to the increase. 3Q10 O&M was partly driven by increased water consumption (+\$1.5 million) in addition to a non-cash charge resulting from the write-off of previously deferred expenses (~\$1.5 million). Therefore, core O&M increased \$3 million YOY, which is in line with WTR's historic O&M growth rate of 4%. O&M management is an important part of WTR's strategy, therefore, we expect core O&M to grow in the 3-4% range. WTR was able to improve its 3Q10 efficiency ratio (O&M/revenue) to 35.1% from 37.9% in 3Q09. WTR remains on track to reduce its efficiency ratio by its stated goal of 150 bps YOY; its 2009 efficiency ratio was 40.3%; we expect full-year 2010 to be in the 38.8% range.

WTR invested \$240 million in infrastructure improvements YTD, and is on track to achieve its capex target of \$300 million in 2010. Capex is primarily targeted to improve outdated infrastructure and upgrade service reliability.

Overall operating expenses increased 8.1% YOY, driven by increased O&M expenses (+6.5% YOY), increased property and other taxes (+14.2%) and increased depreciation expense (+7.8%). Net interest expense increased \$1.9 million (+11%) YOY to \$19.15 million, reflecting higher debt balances. Management expects interest expense to increase 10-15% through 2011, then dip back into single-digits in 2012.

Rate Cases

WTR has received \$48.6 million YTD in annualized revenue increases (\$4.9 million during 3Q10) in Pennsylvania, New Jersey, New York, North Carolina, Missouri, Ohio, Indiana, Maine, and Virginia. WTR settled large cases in with both PA and NJ in 2Q10. The Pennsylvania settlement was resolved sooner than expected. WTR filed for increased rates in 11/2009, and assuming the standard 11-month rate case cycle, the company expected a case conclusion in 10/2010. Therefore, the 6/15/10 effective date permitted certain rate case concessions given the rapid conclusion and implementation. WTR received \$23.6 million in rate increases (excluding the DSIC surcharge) and an ROE in the

range of 10.5-11%. All capital and pension requests were allowed, which should increase 2H10 O&M, as PA pension expenses were back-end loaded to insure rate recovery. The New Jersey settlement increased rates by \$4 million, including a 10.3% ROE (the highest ever received in the state).

\$19.1 million of rate cases remain outstanding before regulatory bodies. Most of these outstanding cases are expected to be resolved by YE 2010 or early 2011, effective in mostly 2011. An additional \$11.5 million in rate requests is expected to be filed later in 4Q10 (effective in 2011-2012). In addition, WTR will file its \$7 million PA DSIC filing in 4Q10. Rate relief is primarily sought to recover infrastructure investments and increased expenses.

In 2009, PA increased its DSIC from 5% to 7.5% of revenue, which should continue to decrease regulatory lag for water-pipe replacement projects. The acceptance of DSIC-like mechanisms in other operating states would likely spur increased pipe investment and capital expenditures. WTR continues to work with the other New Jersey investor-owned utilities to increase knowledge and potentially implementation of a DSIC-like mechanism.

Acquisitions

WTR continues to be active on the acquisition front, having made 14 acquisitions thus far in 2010, including two in 3Q10. Aqua's Pennsylvania subsidiary acquired the water system of Paupackan Lake Assc (1,200 residents) in 3Q10, and its North Carolina business acquired an additional system (900 residents). Management still expects to complete ~25 acquisitions in 2010 (vs. 18 completed in 2009), demonstrating the company's continued commitment and success in revenue growth by acquisition, usually focusing on tuck-in acquisitions. These tuck-ins can provide a steady source of customer growth and are manageable in customer size (~1,000 customers) and location (typically in proximity to an existing WTR system). WTR has acquired both water and wastewater systems in NJ, IL, TX, PA, and VA.

WTR is hoping to return to its historical customer growth level (+3-4%) over the next few years, as both organic and acquisition growth opportunities return. For 2010, management is projecting an organic customer growth rate of +1%. Organic growth opportunities are slowly returning to the market, as the economy appears to be gradually improving in WTR's service territory. Management stated that it will likely be another year until things drastically improve, though current levels are similar to those seen in 2008.

Management stated that the acquisition market is continuing to improve from the depressed levels seen over the past few years, and WTR remains an active and able purchaser in these deals. Historically, WTR completed 25-30 acquisitions annually and is hoping to return to a more normalized acquisition run rate in 2010. With continued economic weakness at the municipality level and the further deterioration of water infrastructure systems, more acquisition opportunities may develop in the next few years. Aqua's financial and industry position, longstanding history, and wide geographic presence (13 states), makes it a natural party in these acquisitions.

Investment Thesis

We rate Aqua America Outperform with a 12-month price target of \$22. Our price target is 21x our 2012 EPS estimate, we believe in line with its peers when fully valued due to its relative earnings consistency, longer-term growth opportunities and wider potential shareholder base reflecting its relative size and liquidity.

Key investment considerations include the following:

- **Strong leadership team.** We believe Aqua has a strong leadership team that has demonstrated a keen focus on developing strong regulatory relationships and engineering innovative solutions to improve water system quality while providing investors with appropriate recovery. We believe management has executed regulatory and investment plans that provide stable and consistent value creation for investors.
- **Attractive total return potential.** We expect 8-10% long-term annual EPS growth with a 60-70% dividend payout ratio, providing a current dividend yield of 2.7% to add up to attractive total returns. Upside exists if WTR is able to accelerate its acquisition program of water and wastewater systems.
- **Constructive regulatory mechanisms.** The majority of WTR's regulatory operations are located in states that maintain enhanced regulatory recovery mechanisms that enable stable earned returns, including infrastructure investment riders, statewide rates and incentive mechanisms for acquisitions of troubled water systems. We believe such mechanisms provide a constructive regulatory environment in which to make capital investments, enabling improved and more consistent earned returns, which should lead to a premium peer valuation.
- **Acquisition growth.** Aqua has successfully acquired hundreds of water and wastewater systems in the past decade to supplement its internal growth. Acquisitions also provide significant follow-on investment opportunities as WTR improves the quality of an acquired water system. We believe such acquisitions are a key value driver for the company and the stock, as it continues to be a key player in consolidating some of the 53,000 water systems outstanding in the U.S. and rehabilitating those systems to improve water quality and drive investment growth.
- **Investment shifting to pipe replacement.** Following significant investment into water treatment systems to meet advancements in water quality standards, Aqua's investment mix is shifting toward pipe replacement. While substantial capital investments will still be required to fund pipe replacement, the level of rate base growth could decline versus historical levels.
- **Water utility valuation.** We expect solid earned ROEs, 8-10% longer-term EPS growth potential and constructive regulatory investment recovery mechanisms should support a 20-22x forward P/E. The valuation is a premium to its regulated electric and gas utility peers reflecting significant industry consolidation and rate base growth opportunities with lowered regulatory risk, and generally more constructive regulatory mechanisms that enable earnings consistency.

Risks & Caveats

Our suitability rating on Aqua America is Lower Risk. Key risks include, but are not limited to, the following:

- **Regulation.** Regulated operations are subject to local, state and federal regulations. Changes in the regulatory environment can affect WTR's near-term and long-term performance.
- **Weather.** WTR's businesses are sensitive to fluctuations in the weather. Particularly wet or dry weather can impact near-term financial results.
- **Acquisition risk.** WTR may have the opportunity to purchase assets or companies in

the near future. Acquisitions carry risks related to personnel, expected-versus-actual growth and a myriad of unforeseen hurdles, all of which can negatively affect earnings.

- **Product quality.** Unique among its sister regulated utility sectors, water utilities provide a product that is ingested. Despite robust mandated service quality standards that lower risk, a quality failure could materially impact the earnings and stock of WTR.
- **Dividend legislation.** Congress has extended tax legislation that reduced the tax rate on dividends received. However, the extensions only last through 2009 and there can be no assurance that further extensions of the tax relief will occur or that a future Congress would not repeal the current legislation, which could have an adverse impact on the after-tax value of dividends and the stock.

Company Description

Aqua America is a holding company for numerous regulated water and wastewater utilities operating in the eastern half of the U.S. that serve over 2.8 million people. It is the second-largest investor-owned water utility in the U.S. Known as Philadelphia Suburban Corporation until 2004, Aqua America is headquartered in the Philadelphia suburbs where its corporate roots date back to 1886 for providing water and/or wastewater service.

Dave Parker (813) 274-7620

Aqua America
WTR - NYSE

Maggie Hughes (414) 765-3968

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Recent Price: \$21.55

| \$mil | Revenue | | | Operating Expenses | | | Operating Income | | | Other Income | | Net Int. Exp. | | Pretax Income | | | Tax Rate | Net Income | | | TTM ROE | Diluted EPS | | Div. | Diluted Shares |
|-------|---------|-------|-------|--------------------|-------|-------|------------------|-------|-------|--------------|---------|---------------|-------|---------------|-------|--------|----------|------------|-------|--------|---------|-------------|--------|------|----------------|
| | \$ | Chg. | Int. | \$ | % | Chg. | \$ | % | Chg. | \$ | Chg. | \$ | Chg. | \$ | % | Chg. | | \$ | % | Chg. | | \$ | % | | |
| 2003 | 367.2 | 14.0% | | 213.7 | 58.2% | 17.7% | 153.6 | 41.8% | 9.3% | 7.82 | -14.5% | 44.66 | 10.6% | 116.7 | 31.8% | 6.8% | 39.3% | 70.8 | 19.3% | 5.4% | 12.3% | 0.59 | 2.2% | 0.34 | 119.0 |
| 2004 | 442.0 | 20.4% | 5.4% | 267.1 | 60.4% | 25.0% | 174.9 | 39.6% | 13.9% | 5.92 | -24.3% | 48.68 | 9.0% | 132.1 | 29.9% | 13.2% | 39.4% | 80.0 | 18.1% | 13.0% | 11.4% | 0.64 | 7.0% | 0.37 | 125.7 |
| 2005 | 496.8 | 12.4% | 9.5% | 300.3 | 60.4% | 12.4% | 196.5 | 39.6% | 12.4% | 3.62 | -38.8% | 52.06 | 6.9% | 148.1 | 29.8% | 12.1% | 38.4% | 91.2 | 18.3% | 13.9% | 11.7% | 0.71 | 10.9% | 0.40 | 129.2 |
| Q1 | 117.9 | 3.5% | 2.0% | 77.3 | 65.6% | 8.6% | 40.6 | 34.4% | -5.0% | 1.19 | 40.2% | 14.17 | 10.8% | 27.6 | 23.4% | -10.3% | 40.1% | 16.6 | 14.0% | -12.2% | 11.3% | 0.13 | -13.6% | 0.11 | 130.9 |
| Q2 | 131.7 | 7.0% | 6.1% | 81.7 | 62.0% | 9.6% | 50.1 | 38.0% | 3.1% | 1.76 | 142.5% | 14.74 | 17.6% | 37.1 | 28.2% | 0.9% | 39.7% | 22.4 | 17.0% | 0.8% | 11.0% | 0.17 | -0.4% | 0.11 | 131.0 |
| Q3 | 147.0 | 7.4% | 5.8% | 87.4 | 59.5% | 12.5% | 59.5 | 40.5% | 0.7% | 0.79 | 55.7% | 14.75 | 11.1% | 45.6 | 31.0% | -1.6% | 40.0% | 27.3 | 18.6% | -2.1% | 10.6% | 0.21 | -3.9% | 0.12 | 132.7 |
| Q4 | 136.8 | 11.3% | 8.5% | 81.5 | 59.6% | 6.1% | 55.3 | 40.4% | 20.1% | 1.40 | -9.4% | 14.76 | 9.8% | 41.9 | 30.7% | 22.8% | 38.7% | 25.7 | 18.8% | 16.1% | 10.6% | 0.19 | 13.0% | 0.12 | 133.4 |
| 2006 | 533.5 | 7.4% | 6.4% | 327.9 | 61.5% | 9.2% | 205.5 | 38.5% | 4.6% | 5.14 | 41.7% | 58.43 | 12.2% | 152.3 | 28.5% | 2.8% | 39.6% | 92.0 | 17.2% | 0.9% | 10.6% | 0.70 | -1.0% | 0.44 | 131.8 |
| Q1 | 137.3 | 16.4% | 10.5% | 93.6 | 68.1% | 21.0% | 43.7 | 31.9% | 7.7% | 0.79 | -33.3% | 16.55 | 16.8% | 28.0 | 20.4% | 1.3% | 39.8% | 16.9 | 12.3% | 1.8% | 10.4% | 0.13 | 0.0% | 0.12 | 133.2 |
| Q2 | 150.6 | 14.3% | 7.9% | 95.9 | 63.6% | 17.4% | 54.8 | 36.4% | 9.3% | 1.06 | -39.6% | 16.44 | 11.5% | 39.4 | 26.2% | 6.2% | 39.8% | 23.7 | 15.8% | 6.0% | 10.3% | 0.18 | 4.0% | 0.12 | 133.5 |
| Q3 | 165.5 | 12.6% | 5.4% | 100.1 | 60.5% | 14.5% | 65.3 | 39.5% | 9.8% | 0.92 | 15.2% | 17.10 | 15.9% | 49.2 | 29.7% | 7.9% | 40.0% | 29.5 | 17.8% | 8.0% | 10.3% | 0.22 | 7.1% | 0.13 | 133.8 |
| Q4 | 149.1 | 8.9% | 7.1% | 96.9 | 65.0% | 18.9% | 52.2 | 35.0% | -5.7% | 3.68 | 162.9% | 16.83 | 14.0% | 39.0 | 26.2% | -7.0% | 36.1% | 24.9 | 16.7% | -3.2% | 10.0% | 0.19 | -3.6% | 0.13 | 134.0 |
| 2007 | 602.5 | 12.9% | 7.6% | 386.5 | 64.1% | 17.9% | 216.0 | 35.9% | 5.1% | 6.45 | 25.6% | 66.92 | 14.5% | 155.5 | 25.8% | 2.2% | 38.9% | 95.0 | 15.8% | 3.3% | 10.0% | 0.71 | 1.9% | 0.48 | 133.6 |
| Q1 | 139.3 | 1.4% | 1.0% | 99.1 | 71.1% | 5.9% | 40.2 | 28.9% | -8.1% | 0.96 | 21.0% | 17.13 | 3.5% | 24.0 | 17.3% | -14.1% | 40.4% | 14.3 | 10.3% | -15.0% | 9.6% | 0.11 | -15.5% | 0.13 | 134.0 |
| Q2 | 150.8 | 0.1% | -0.1% | 97.6 | 64.8% | 1.8% | 53.1 | 35.2% | -3.0% | 1.65 | 55.8% | 17.06 | 3.8% | 37.7 | 25.0% | -4.2% | 40.2% | 22.6 | 15.0% | -5.0% | 9.3% | 0.17 | -5.3% | 0.13 | 134.1 |
| Q3 | 177.1 | 7.0% | 4.5% | 102.5 | 57.9% | 2.4% | 74.6 | 42.1% | 14.1% | 1.51 | 64.8% | 17.01 | -0.5% | 59.1 | 33.4% | 20.2% | 40.1% | 35.4 | 20.0% | 19.9% | 9.8% | 0.26 | 18.6% | 0.13 | 135.3 |
| Q4 | 159.8 | 7.2% | 0.0% | 102.0 | 63.8% | 5.2% | 57.9 | 36.2% | 11.0% | 1.16 | -68.6% | 17.37 | 3.2% | 41.7 | 26.1% | 6.8% | 38.4% | 25.7 | 16.1% | 3.0% | 9.7% | 0.19 | 1.8% | 0.14 | 135.6 |
| 2008 | 627.0 | 4.1% | 3.1% | 401.2 | 64.0% | 3.8% | 225.8 | 36.0% | 4.5% | 5.27 | -18.2% | 68.57 | 2.5% | 162.5 | 25.9% | 4.5% | 39.7% | 97.9 | 15.6% | 3.1% | 9.6% | 0.73 | 2.2% | 0.51 | 134.7 |
| Q1 | 154.5 | 10.9% | 10.0% | 107.7 | 69.7% | 8.7% | 46.8 | 30.3% | 16.3% | 0.76 | -20.7% | 16.63 | -2.9% | 30.9 | 20.0% | 28.5% | 40.5% | 18.4 | 11.9% | 28.3% | 9.9% | 0.14 | 26.5% | 0.14 | 135.9 |
| Q2 | 167.3 | 11.0% | 9.2% | 108.5 | 64.8% | 11.1% | 58.9 | 35.2% | 10.8% | 0.65 | -60.8% | 16.81 | -1.5% | 42.7 | 25.5% | 13.2% | 39.5% | 25.9 | 15.5% | 14.6% | 10.0% | 0.19 | 12.2% | 0.14 | 136.9 |
| Q3 | 180.8 | 2.1% | -0.1% | 109.4 | 60.5% | 6.7% | 71.5 | 39.5% | -4.2% | 0.91 | -39.7% | 17.26 | 1.4% | 55.1 | 30.5% | -6.7% | 39.3% | 33.5 | 18.5% | -5.4% | 9.8% | 0.25 | -6.1% | 0.14 | 136.3 |
| Q4 | 167.9 | 5.0% | 7.1% | 107.5 | 64.0% | 5.5% | 60.4 | 36.0% | 4.3% | 1.03 | -11.1% | 17.91 | 3.2% | 43.5 | 25.9% | 4.4% | 38.7% | 26.7 | 15.9% | 3.9% | 9.7% | 0.20 | 3.2% | 0.15 | 136.5 |
| 2009 | 670.5 | 6.9% | 6.2% | 433.1 | 64.6% | 8.0% | 237.5 | 35.4% | 5.2% | 3.34 | -36.6% | 68.61 | 0.1% | 172.2 | 25.7% | 6.0% | 39.4% | 104.4 | 15.6% | 6.6% | 9.6% | 0.77 | 5.5% | 0.55 | 136.1 |
| Q1 | 160.5 | 3.9% | 3.5% | 109.8 | 68.4% | 2.0% | 50.7 | 31.6% | 8.4% | 3.47 | 357.8% | 18.43 | 10.8% | 35.7 | 22.3% | 15.6% | 39.8% | 21.5 | 13.4% | 17.1% | 9.9% | 0.16 | 16.3% | 0.15 | 136.8 |
| Q2 | 178.4 | 6.6% | 6.2% | 112.4 | 63.0% | 3.6% | 66.1 | 37.0% | 12.3% | 1.57 | 142.4% | 18.50 | 10.1% | 49.1 | 27.5% | 15.1% | 39.2% | 29.9 | 16.7% | 15.5% | 10.1% | 0.22 | 15.4% | 0.15 | 137.0 |
| Q3 | 207.8 | 14.9% | 13.4% | 118.2 | 56.9% | 8.1% | 89.6 | 43.1% | 25.4% | 1.37 | 50.5% | 19.15 | 11.0% | 71.8 | 34.6% | 30.3% | 39.1% | 43.8 | 21.1% | 30.7% | 10.9% | 0.32 | 29.6% | 0.15 | 137.4 |
| Q4E | 174.7 | 4.0% | 2.5% | 109.3 | 62.6% | 1.7% | 65.4 | 37.4% | 8.2% | (0.41) | -139.8% | 19.13 | 6.8% | 45.8 | 26.2% | 5.3% | 38.0% | 28.4 | 16.3% | 6.5% | 10.9% | 0.21 | 5.4% | 0.16 | 137.9 |
| 2010E | 721.4 | 7.6% | 6.6% | 449.7 | 62.3% | 3.8% | 271.7 | 37.7% | 14.4% | 6.00 | 79.5% | 75.22 | 9.6% | 202.5 | 28.1% | 17.6% | 39.0% | 123.5 | 17.1% | 18.4% | 10.9% | 0.90 | 17.5% | 0.59 | 137.1 |
| 2011E | 779.1 | 8.0% | 5.8% | 479.3 | 61.5% | 6.6% | 299.9 | 38.5% | 10.4% | 6.30 | 5.0% | 80.14 | 6.5% | 226.0 | 29.0% | 11.6% | 39.0% | 137.9 | 17.7% | 11.6% | 11.5% | 1.00 | 11.0% | 0.63 | 137.8 |
| 2012E | 833.7 | 7.0% | 4.8% | 509.8 | 61.2% | 6.4% | 323.9 | 38.8% | 8.0% | 6.49 | 3.0% | 89.58 | 11.8% | 240.8 | 28.9% | 6.5% | 39.0% | 146.9 | 17.6% | 6.5% | 11.4% | 1.05 | 5.3% | 0.67 | 139.4 |

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Date Printed: 11/5/2010

Fiscal Year: DEC

(in millions)

Aqua America WTR - NYSE

Dave Parker (813) 274-7620

Maggie Hughes (414) 765-3968

| Balance Sheet | 2005 | 2006 | 2007 | 2008 | 2009 | 2Q10 | Cash Flow Statement | 2005 | 2006 | 2007 | 2008 | 2009 | 2010E | 2011E | |
|---------------------------------|---------|---------|---------|---------|---------|---------|----------------------------------|-------------|-------------|-------------|-------------|-------------|--------------|---------------|---------|
| ASSETS | | | | | | | Net Income | 91.2 | 92.0 | 95.0 | 97.9 | 104.4 | 123.5 | 137.9 | |
| Cash & Equivalents | 11.9 | 44.0 | 14.5 | 14.9 | 21.9 | 13.1 | Depreciation & Amort | 65.5 | 75.0 | 88.0 | 94.3 | 114.9 | 119.0 | 128.1 | |
| Receivables | 62.7 | 72.1 | 82.9 | 84.5 | 78.7 | 85.6 | Net changes in (CA) & CL | 20.5 | (14.4) | (14.6) | (9.7) | (8.5) | (6.3) | (7.1) | |
| Inventory | 7.8 | 8.4 | 8.8 | 9.8 | 9.5 | 9.9 | Deferred taxes/Non-Cash | 22.5 | 18.1 | 25.8 | 39.0 | 47.8 | (8.6) | (8.8) | |
| Other | 7.6 | 10.2 | 9.2 | 11.8 | 11.4 | 10.5 | Cash Flow from Operations | 199.7 | 170.7 | 194.2 | 221.5 | 258.6 | 227.6 | 250.1 | |
| Total Current | 90.0 | 134.7 | 115.5 | 121.0 | 121.6 | 119.2 | Dividend Payments | (51.1) | (58.0) | (63.8) | (68.5) | (74.7) | (80.5) | (86.5) | |
| Fixed Assets | 2,280.0 | 2,506.0 | 2,792.8 | 2,997.4 | 3,227.3 | 3,341.2 | Net Capital Expenditures | (237.5) | (271.7) | (238.1) | (267.4) | (283.6) | (280.0) | (290.0) | |
| Goodwill & Intangible Asset | 20.2 | 22.6 | 36.6 | 41.0 | 43.1 | 43.2 | Free Cash Flow | (\$88.9) | (\$159.0) | (\$107.7) | (\$114.4) | (\$99.7) | (\$132.9) | (\$126.4) | |
| Other Assets | 236.6 | 214.6 | 282.0 | 325.6 | 370.6 | 363.8 | Operating Cash Flow Per Share | 1.55 | 1.30 | 1.45 | 1.64 | 1.90 | 1.66 | 1.81 | |
| Total Assets | 2,626.7 | 2,877.9 | 3,226.9 | 3,485.0 | 3,762.6 | 3,867.4 | Free Cash Flow Per Share | (0.69) | (1.21) | (0.81) | (0.85) | (0.73) | (0.97) | (0.92) | |
| LIAB. & EQUITY | | | | | | | Du Pont Formula | 2005 | 2006 | 2007 | 2008 | 2009 | 2010E | 2011E | |
| Current Debt | 163.2 | 150.3 | 80.8 | 87.9 | 87.1 | 86.7 | Net Margins (N/S) | 18.3% | 17.2% | 15.8% | 15.6% | 15.6% | 17.1% | 17.7% | |
| Payables | 55.5 | 49.4 | 45.8 | 50.0 | 57.9 | 49.7 | Assets Turnover (S/A) | 0.2 | 0.2 | 0.2 | 0.2 | 0.2 | 0.2 | 0.2 | |
| Other | 44.7 | 55.9 | 56.6 | 55.2 | 56.1 | 62.2 | Leverage (A/E) | 3.2 | 3.2 | 3.2 | 3.3 | 3.3 | 3.4 | 3.4 | |
| Total Current | 263.3 | 255.6 | 183.2 | 193.2 | 201.0 | 198.6 | Return on Equity | 11.7% | 10.6% | 10.0% | 9.6% | 9.6% | 10.9% | 11.5% | |
| L/T Debt & Lease | 878.4 | 951.7 | 1,215.1 | 1,248.1 | 1,386.6 | 1,461.6 | Valuation Parameters | 2005 | 2006 | 2007 | 2008 | 2009 | 2010E | Recent | |
| Deferred Taxes | 250.3 | 273.2 | 307.7 | 355.2 | 408.6 | 414.4 | Price (Common) - WTR | High | 29.22 | 29.79 | 26.62 | 22.00 | 21.50 | 19.95 | 21.55 |
| Other Liabilities | 422.7 | 475.8 | 544.7 | 630.1 | 657.5 | 663.3 | Low | 17.49 | 20.13 | 18.86 | 12.20 | 16.12 | 17.07 | | |
| Preferred Stock | - | - | - | - | - | - | Forward P/E Ratio | High | 37.0x | 34.9x | 32.2x | 26.4x | 25.0x | 25.0x | |
| Common Equity | 811.9 | 921.6 | 976.3 | 1,058.4 | 1,108.9 | 1,129.5 | Low | 23.8x | 25.2x | 22.8x | 14.7x | 17.1x | 17.1x | | |
| Total Liab. & Equity | 2,626.7 | 2,877.9 | 3,226.9 | 3,485.0 | 3,762.6 | 3,867.4 | Close | 33.8x | 27.6x | 25.4x | 21.4x | 18.9x | 18.9x | 21.4x | |
| Ratio Analysis: | | | | | | | Book Value | \$ | 6.30 | \$6.96 | \$7.28 | \$7.78 | \$8.14 | \$8.49 | \$8.97 |
| Current Ratio | 0.3 | 0.5 | 0.6 | 0.6 | 0.6 | 0.6 | Price/Book Ratio | High | 4.6x | 4.3x | 3.7x | 2.8x | 2.6x | 2.3x | 2.4x |
| Working Capital | (\$22) | (\$15) | (\$1) | \$1 | (\$14) | (\$6) | Low | 2.8x | 2.9x | 2.6x | 1.6x | 2.0x | 2.0x | 2.0x | |
| Working Cap/Assets | (0.8%) | (0.5%) | (0.0%) | 0.0% | (0.4%) | (0.2%) | Close | 4.3x | 3.3x | 2.9x | 2.6x | 2.5x | 2.3x | 2.3x | |
| Inventory Turns | NM | NM | NM | NM | NM | NM | EBITDA | \$260.9 | \$281.6 | \$305.6 | \$319.9 | \$343.8 | \$386.7 | \$424.4 | |
| Total Debt/Capital | 62% | 59% | 59% | 58% | 59% | 60% | Enterprise Value | High | \$4,805 | \$4,983 | \$4,838 | \$4,285 | \$4,379 | \$4,311 | \$4,607 |
| LT Debt/Equity | 108% | 103% | 124% | 118% | 125% | 129% | Low | 3,290 | 3,711 | 3,801 | 2,964 | 3,646 | 3,915 | 4,183 | |
| EBIT/Interest Expense | 3.8x | 3.6x | 3.3x | 3.4x | 3.5x | 3.5x | EV / EBITDA | High | 18.4x | 17.7x | 15.8x | 13.4x | 12.7x | 11.1x | 10.9x |
| Total Debt/EBIT | 5.2x | 5.2x | 5.8x | 5.8x | 6.1x | 6.1x | Low | 12.6x | 13.2x | 12.4x | 9.3x | 10.6x | 10.1x | 9.9x | |
| | | | | | | | Close | 17.5x | 14.4x | 13.5x | 12.8x | 12.1x | 10.9x | 10.6x | |

Please refer to "Appendix - Important Disclosures" and Analyst Certification.

Appendix - Important Disclosures and Analyst Certification



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