

## Aqua America, Inc. (WTR)

Strong 2010 EPS Driven by Best-in-Class Model; Maintain Neutral on Valuation

Price: (2/24/11)	22.31	Rating:	Neutral	FY Dec	2010A	2011E	2012E
52WK H-L:	24 - 17			Q1	0.16A		
Market Cap (mil):	3,056	Suitability:	Lower Risk	Q2	0.22A		
Shares Out (mil):	137.0			Q3	0.32A		
Float (mil):	136.4			Q4	0.21A		
Avg. Daily Vol (mil):	0.70	Price Target:	24	Total	0.90A	1.00E	1.05E
Dividend	0.58			Previous			
Yield (%)	2.60			FY P/E	24.8	22.3	21.2

Please refer to Appendix - Important Disclosures and Analyst Certification.

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### Action

**WTR's focus on operational excellence and infrastructure investment generate solid long-term EPS growth.** However, we maintain our Neutral rating, as we believe the stock is close to fair value. We would be more aggressive in the name under \$21. We consider WTR a core long-term holding, as accelerated infrastructure investment combined with effective cost control strategies are expected to drive above-average EPS growth (8-10% CAGR) coupled with a 2.5% dividend yield.

### Summary

- **Strong 2010 results due to continued cost containment efforts.** WTR reported 2010 EPS of \$0.90/share versus \$0.77/share in 2010 (19% YOY growth). On a weather-normalized basis, management stated that it is comfortable with 8% YOY EPS growth for 2011 (~\$0.97/share).
  - 4Q10 results of \$0.21 were in line with our consensus-matching estimate and increased \$0.01 YOY, despite unfavorable weather (-\$0.01/share) and new tax laws (-\$0.01/share).
- **Successful execution of acquisition strategy despite challenging economy.** In 2010, Aqua completed 23 acquisitions, 10 of which were in Texas, which the company has identified as an area of growth. We expect WTR to complete 15-20 acquisitions in 2011 with a continued focus on high-growth states.
- **Capex focused on pipe replacement.** Aqua spent \$327 million on capital investment in 2010 (primarily on system upgrade work) and intends to spend over \$300 million in 2011. The majority (90%) of this capital will go towards pipe replacement in states that employ infrastructure recovery mechanisms.
- **Decreasing regulatory lag/risk reflecting enhanced regulatory recovery mechanisms (i.e., DSIC).** These mechanisms reduce regulatory risk as recovery lag time is minimized, rate cases are filed less frequently, and requested increases are lower.
- **Maintaining estimates and Neutral rating.** Despite WTR's best-in-class business model and successful cost mitigation strategy, we believe recent stock strength has moved WTR close to full value; however, we consider WTR a core long-term holding.

## Details

WTR reported 4Q10 EPS of \$0.21, in line with our estimate and consensus and a penny improvement over 4Q09. Aqua earned \$0.90/per share in 2010, compared to \$0.77 in 2009, an impressive 19% YOY EPS growth.

**Figure 1: 4Q10 Results Variance**

Aqua America (WTR - NYSE)								
Quarterly Results Variance								
	Quarterly Results					Percent of Revenue		
	4Q10	4Q09	% Chg	Baird	Variance	4Q10	4Q09	Baird
<b>Revenue</b>	179	168	6.8%	\$175	2.6%			
Operating Expenses	114	108	5.6%	109	4.2%	63.3%	64.0%	62.4%
<b>Operating Income</b>	66	60	8.9%	69	(4.7%)	36.7%	36.0%	39.5%
Pretax Income	47	43	9.0%	49	(4.1%)	26.4%	25.9%	28.3%
Taxes	19	17		19		10.3%	10.0%	10.8%
<b>Net Income</b>	29	27	8.2%	\$31	(5.7%)	16.1%	15.9%	17.5%
<b>EPS</b>	<b>\$0.21</b>	<b>\$0.20</b>	7.2%	<b>\$0.22</b>	(5.7%)			
Diluted Shares	138	137		138				

*4Q10 nonrecurring and other items of note: None*

*4Q09 nonrecurring and other items of note: None*

Source: Company reports; RW Baird estimates

## Outlook

WTR reported strong 4Q10 and 2010 resulted aided by further cost containment efforts; WTR's 2010 efficiency ratio was 38.6%, down 170 bps YOY and the best results since acquiring the troubled AquaSource systems in 2003. Management will continue to focus on cost control going forward, likely improving its efficiency ratio 25-50 bps annually, while capex (2.5-3.0x depreciation) and customer growth also remain key long-term focus areas. WTR experienced 1% customer growth in 2010 (below the 2-3% historical rate), largely attributable to the 23 acquisitions that were completed during the year. Organic customer growth remains low, as the economy and housing market remain challenging.

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. Currently approximately 70% of WTR's operating system employs DSIC-like mechanisms (including PA, NY, IN, IL, & OH), which allow for return of an on investment outside of a full rate case. This greatly reduces regulatory risk as recovery lag time is minimized, rate cases are filed less frequently, and requested amounts are decreased; this mitigates both commission and consumer tension. We view this decreased regulatory risk favorably, as it affords WTR additional political cover. More widespread acceptance of DSIC-like mechanisms in WTR's system would elicit increased investment and further reduce regulatory risk. Efforts are underway to create a DSIC in NJ, where Aqua also has a meaningful presence.

**Capex Outlook.** Aqua spent \$327 million on capital investment in 2010 and intends to spend over \$300 again in 2011. 2010 was the first time that the majority of capital spending went to pipe replacement and system upgrade. Over 90% of 2011 capital will be invested in similar system upgrades (main, pipes, hydrants, etc.), which provide direct value to customers; while <10% will be invested in mandatory compliance upgrades.

These discretionary system upgrade investments are targeted for states with enhanced recovery mechanisms as discussed above (i.e. DSIC), which improve margin and earnings consistency. The recent increase in weather-induced main breaks only highlights the importance of having a timely and consistent main replacement plan coupled with sufficient recovery mechanisms. WTR noted that of all of the 300 main breaks that it experienced this winter, none were on pipes that have been replaced in conjunction with the DSIC program, further supporting the implementation of such mechanisms.

Management also stated that it will begin to transition a portion of its spending towards cost saving capital, investments that reduce future operating expenses (purchased water, electric, chemicals, etc.). Specifically, WTR could invest in 3-4 more solar plants in 2011, in addition to the 1 MW unit that was added in 2010, which could decrease future electricity costs. WTR is also focusing on reducing chemical costs and continues to evaluate ways to reduce employee costs, improve vehicle fuel efficiency, and increase pump performance.

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## Results

**4Q10 Highlights.** Quarterly revenue increased 6.8% driven by rate relief and modest customer growth. Operating expenses increased 6.1% and the quarterly efficiency ratio (O&M as a percentage of revenue) improved 20bp YOY. Operating income increased 8.9%, while net income grew 8.2%. Unfavorable weather (extremely cold and snowy) had a -\$0.01/share impact on 4Q10 results; a change in tax law also had a -\$0.01/share impact.

**2010 Highlights.** The utility increased revenue 8.3%, largely reflecting rate relief, but also aided by favorable weather. Simultaneously, the company kept operating costs in check and completed the year with a 38.6% efficiency ratio, a 170 basis point year-over-year improvement. This marks the first time the company's annual efficiency ratio has been below the 40% threshold since the company acquired the troubled AquaSource systems in 2005. Going forward, we expect WTR to decrease its efficiency ratio 25-50 bps annually, likely decreasing over time as diminishing returns set in.

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## Rate Cases

Aqua received rate relief of almost \$54 million during 2010 (versus \$37 million in 2009), concluding 18 cases in ten operating jurisdictions (including PA, NJ, NY, NC, MO, OH, IN, ME, VA). The \$54 million also includes nine surcharge proceedings that were completed in a handful of states. As part of its rate proceedings, WTR consolidated rates in North Carolina, Virginia, Texas, and Pennsylvania wastewater, which will reduce administrative filing costs going forward.

Currently the company has \$26.6 million of pending rate cases outstanding (18 cases), \$6.8 million of which was filed in 1/2011 (three rate cases, three surcharge cases). We expect the company to file for \$57 million in additional rate relief throughout the year, including a late-2011 request in Pennsylvania, the company's largest subsidiary. Management plans to file additional rate cases in 2011 in New Jersey, Ohio, and Texas.

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## Acquisitions

Aqua completed 23 acquisitions in 2010, in line with its 25 acquisition expectation and improved from the 18 acquisitions that were completed in 2009. In 2010, WTR acquired 10 systems in Texas, which the company has identified as an area of growth. The company's Texas presence will be further expanded by an additional 4,200 water customers and 1,100 wastewater customers once the recently announced transaction with American Water closes. We expect WTR to complete 20-25 acquisitions in 2011, in line with its historical 25-30 acquisitions/year run rate, focused on growth areas.

WTR expects to return to its historical customer growth level (+3-4%) over the next few years, as both organic and acquisition growth opportunities return. WTR achieved about 1% customer growth in 2010, driven by the aforementioned acquisitions and not organic growth. As the economy appears to be gradually improving in WTR's service territory, organic growth opportunities are slowly returning.

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## Investment Thesis

We rate Aqua America Neutral with a 12-month price target of \$24. 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.

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## 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.

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## 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.

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**Aqua America**  
**WTR - NYSE**

Date Printed: 2/24/2011

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.		\$	% 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%	14.5%	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
Q4	179.3	6.8%	5.3%	113.6	63.3%	5.6%	65.7	36.7%	8.9%	1.24	20.2%	19.57	9.2%	47.4	26.4%	9.0%	39.1%	28.9	16.1%	8.2%	11.0%	0.21	7.2%	0.16	137.9
2010	726.1	8.3%	7.6%	454.0	62.5%	4.8%	272.1	37.5%	14.6%	7.65	128.7%	75.65	10.3%	204.1	28.1%	18.5%	39.2%	124.0	17.1%	18.8%	10.9%	0.90	17.8%	0.59	137.3
2011E	782.3	7.7%	5.5%	484.8	62.0%	6.8%	297.4	38.0%	9.3%	7.95	4.0%	78.50	3.8%	226.9	29.0%	11.2%	39.2%	137.8	17.6%	11.2%	11.5%	1.00	10.7%	0.63	137.8
2012E	837.0	7.0%	4.8%	514.9	61.5%	6.2%	322.1	38.5%	8.3%	8.11	2.0%	89.58	14.1%	240.6	28.7%	6.1%	39.2%	146.2	17.5%	6.1%	11.4%	1.05	4.9%	0.67	139.4

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

## Aqua America WTR - NYSE

Date Printed: 2/24/2011

Fiscal Year: DEC

(in millions)

Balance Sheet	2005	2006	2007	2008	2009	3Q10
<b>ASSETS</b>						
Cash & Equivalents	11.9	44.0	14.5	14.9	21.9	13.1
Receivables	62.7	72.1	82.9	84.5	78.7	85.6
Inventory	7.8	8.4	8.8	9.8	9.5	9.9
Other	7.6	10.2	9.2	11.8	11.4	10.5
<b>Total Current</b>	<b>90.0</b>	<b>134.7</b>	<b>115.5</b>	<b>121.0</b>	<b>121.6</b>	<b>119.2</b>
Fixed Assets	2,280.0	2,506.0	2,792.8	2,997.4	3,227.3	3,341.2
Goodwill & Intangible Asset	20.2	22.6	36.6	41.0	43.1	43.2
Other Assets	236.6	214.6	282.0	325.6	370.6	363.8
<b>Total Assets</b>	<b>2,626.7</b>	<b>2,877.9</b>	<b>3,226.9</b>	<b>3,485.0</b>	<b>3,762.6</b>	<b>3,867.4</b>
<b>LIAB. &amp; EQUITY</b>						
Current Debt	163.2	150.3	80.8	87.9	87.1	86.7
Payables	55.5	49.4	45.8	50.0	57.9	49.7
Other	44.7	55.9	56.6	55.2	56.1	62.2
<b>Total Current</b>	<b>263.3</b>	<b>255.6</b>	<b>183.2</b>	<b>193.2</b>	<b>201.0</b>	<b>198.6</b>
L/T Debt & Lease	878.4	951.7	1,215.1	1,248.1	1,386.6	1,461.6
Deferred Taxes	250.3	273.2	307.7	355.2	408.6	414.4
Other Liabilities	422.7	475.8	544.7	630.1	657.5	663.3
Preferred Stock	-	-	-	-	-	-
Common Equity	811.9	921.6	976.3	1,058.4	1,108.9	1,129.5
<b>Total Liab. &amp; Equity</b>	<b>2,626.7</b>	<b>2,877.9</b>	<b>3,226.9</b>	<b>3,485.0</b>	<b>3,762.6</b>	<b>3,867.4</b>

**Ratio Analysis:**

Current Ratio	0.3	0.5	0.6	0.6	0.6	0.7
Working Capital	(\$22)	(\$15)	(\$1)	\$1	(\$14)	\$11
Working Cap/Assets	(0.8%)	(0.5%)	(0.0%)	0.0%	(0.4%)	0.3%
Inventory Turns	NM	NM	NM	NM	NM	NM
Total Debt/Capital	62%	59%	59%	58%	59%	59%
LT Debt/Equity	108%	103%	124%	118%	125%	127%
EBIT/Interest Expense	3.8x	3.6x	3.3x	3.4x	3.5x	3.7x
Total Debt/EBIT	5.2x	5.2x	5.8x	5.8x	6.1x	5.6x

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

Cash Flow Statement		2006	2007	2008	2009	2010	2011E	2012E
<b>Net Income</b>		92.0	95.0	97.9	104.4	124.0	137.8	146.2
Depreciation & Amort		75.0	88.0	94.3	114.9	121.1	128.0	135.1
Net changes in (CA) & CL		6.1	(29.0)	(24.3)	(18.2)	(15.3)	(13.7)	(13.6)
Deferred taxes/Non-Cash		(2.4)	40.1	53.6	57.5	(2.6)	(4.6)	(4.8)
<b>Cash Flow from Operations</b>		<b>170.7</b>	<b>194.2</b>	<b>221.5</b>	<b>258.6</b>	<b>227.1</b>	<b>247.5</b>	<b>262.9</b>
Dividend Payments		(58.0)	(63.8)	(68.5)	(74.7)	(80.8)	(86.5)	(93.0)
Net Capital Expenditures		(271.7)	(238.1)	(267.4)	(283.6)	(280.0)	(290.0)	(300.0)
<b>Free Cash Flow</b>		<b>(\$159.0)</b>	<b>(\$107.7)</b>	<b>(\$114.4)</b>	<b>(\$99.7)</b>	<b>(\$133.7)</b>	<b>(\$128.9)</b>	<b>(\$130.1)</b>
Operating Cash Flow Per Share		1.30	1.45	1.64	1.90	1.65	1.80	1.89
Free Cash Flow Per Share		(1.21)	(0.81)	(0.85)	(0.73)	(0.97)	(0.94)	(0.93)
<b>Du Pont Formula</b>		<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011E</b>	<b>2012E</b>
Net Margins (N/S)		17.2%	15.8%	15.6%	15.6%	17.1%	17.6%	17.5%
Assets Turnover (S/A)		0.2	0.2	0.2	0.2	0.2	0.2	0.2
Leverage (A/E)		3.2	3.2	3.3	3.3	3.4	3.4	3.3
<b>Return on Equity</b>		<b>10.6%</b>	<b>10.0%</b>	<b>9.6%</b>	<b>9.6%</b>	<b>10.9%</b>	<b>11.5%</b>	<b>11.4%</b>
<b>Valuation Parameters</b>		<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011E</b>	<b>Recent</b>
Price (Common) - WTR		High	29.79	26.62	22.00	21.50	19.95	21.25
		Low	20.13	18.86	12.20	16.12	17.07	18.18
<b>Forward P/E Ratio</b>		High	34.9x	32.2x	26.4x	25.0x	25.0x	25.0x
		Low	25.2x	22.8x	14.7x	17.1x	17.1x	17.1x
		Close	27.6x	25.4x	21.4x	18.9x	18.9x	18.9x
<b>Book Value</b>		\$6.96	\$7.28	\$7.78	\$8.14	\$8.49	\$8.97	\$9.57
<b>Price/Book Ratio</b>		High	4.3x	3.7x	2.8x	2.6x	2.3x	2.4x
		Low	2.9x	2.6x	1.6x	2.0x	2.0x	2.0x
		Close	3.3x	2.9x	2.6x	2.5x	2.3x	2.3x
<b>EBITDA</b>		\$281.6	\$305.6	\$319.9	\$343.8	\$387.8	\$420.4	\$452.3
<b>Enterprise Value</b>		High	\$4,983	\$4,838	\$4,285	\$4,379	\$4,316	\$4,917
		Low	3,711	3,801	2,964	3,646	3,920	4,187
<b>EV / EBITDA</b>		High	17.7x	15.8x	13.4x	12.7x	11.1x	11.0x
		Low	13.2x	12.4x	9.3x	10.6x	10.1x	10.0x
		Close	14.4x	13.5x	12.8x	12.1x	10.9x	10.6x

## Appendix - Important Disclosures and Analyst Certification



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