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Reports 4Q10 Results; Maintain Buy Rating, \$26 Target Price

**Buy
Target Price: \$26**

Investment Summary – Aqua America posted 4Q10 results that slightly exceeded our expectations on the top line and matched our \$0.21 forecast on the bottom line. The company continues to execute on its growth strategy, based on timely rate relief, acquisitions and expense controls. We’ve made no changes to our 2011 forecast; have introduced 2012 estimates, and we maintain our Buy rating and \$26 target price on the shares of Aqua America. We recommend investors continue to buy shares, albeit opportunistically, given the close proximity to our target price. Risks to the achievement of our target price include integration of acquisitions, weather, environmental regulations, regulation of rates, energy costs, and interest rates.

Discussion

- **4Q10 results matched our expectations.** Revenues of \$179.3MM were just above our \$176.3MM forecast, and a touch below consensus (\$184MM). EPS of \$0.21 matched our estimate and consensus. Looking through the 4Q10 income statement, all line items fell within what we would consider to be normal parameters.
- **Another year, another dividend increase.** The December 2010 dividend was increased 6.9%, to \$0.155 per share. The board of directors recently declared a quarterly cash dividend of \$0.155 per share payable to all shareholders of record on February 17, 2010. This payment is the 20th dividend increase in the last 19 years. The shares currently yield 2.7%.
- **No change to 2011 estimates; introducing 2012 forecasts.** Based on 4Q10 results, we’ve made no changes to our 2011 forecasts. We are taking this opportunity to introduce a 2012 EPS estimate of \$1.07.
- **Guidance** – The company indicated it is comfortable with consensus estimates (\$0.18 for 1Q11) and 2012 EPS of \$0.97. Our forward estimates are within a penny of both figures.

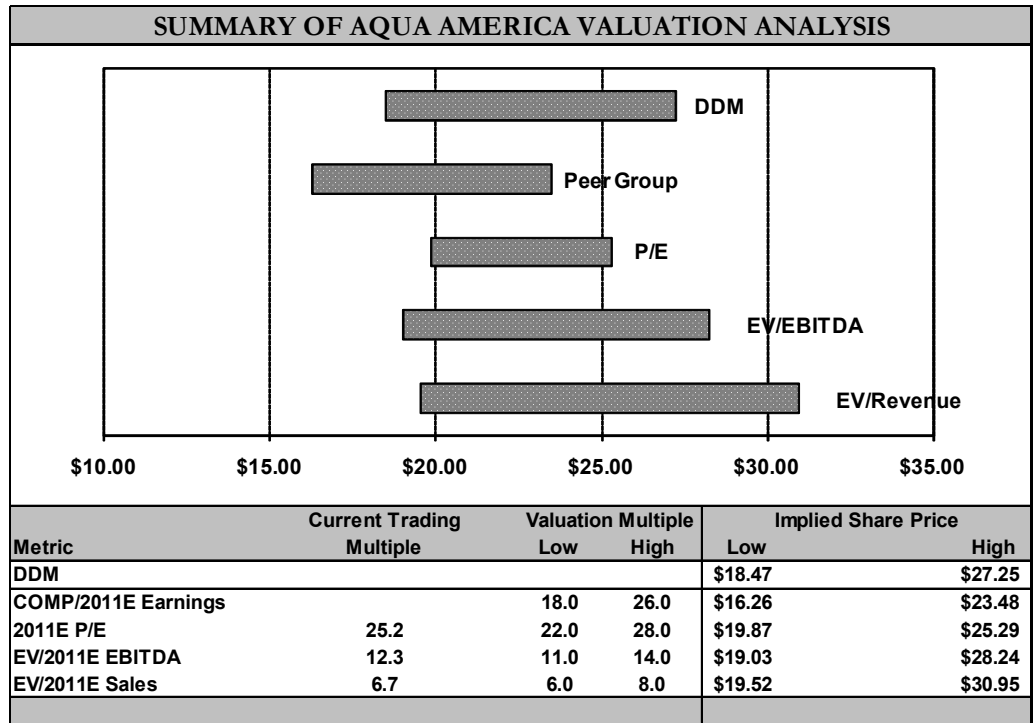
Valuation – We believe Aqua America remains poised for strong future growth. Its ability to access low-cost capital, as well as its strong internal cash generation and proven track record to acquire new systems and invest prudently in its asset base should drive top- and bottom-line growth on a go-forward basis. That said, with the shares now trading at 23x our 2011 EPS estimate of \$0.98, we continue to recommend accumulation, albeit opportunistically given the close proximity to our share price. We reiterate our Buy rating and maintain our target price of \$26, based on the shares attaining a P/E multiple of 27x our 2011 EPS estimate of \$0.98.

Price	\$22.40		
52-Week High/Low	\$23.79 - 16.52		
Shares Outstanding (mm)	137.54		
Market Cap. (mm)	\$3,080.90		
Average Daily Volume (mm)	0.61		

EPS	FY10A	FY11E	FY12E
Mar	\$0.16	\$0.19	\$0.21
Jun	\$0.22	\$0.24	\$0.26
Sep	\$0.32	\$0.31	\$0.34
Dec	\$0.21E	\$0.24	\$0.25
FY	\$0.90E	\$0.98	\$1.07
<i>Prior</i>	-	\$0.97	-
Consensus	\$0.90E	\$0.97	\$1.05

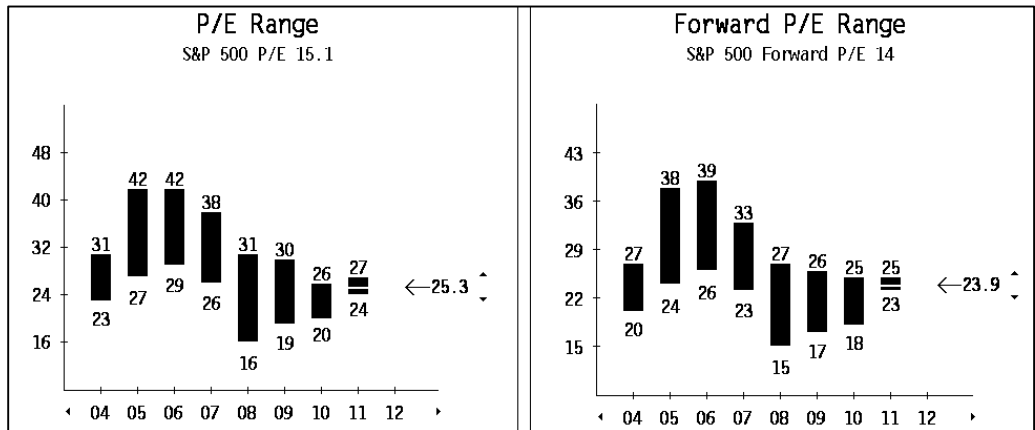
P/E	24.8Ex	22.9x	21.0x
FY Rev. (mm)	\$726.07E	\$784.16	\$831.40

Source: BigCharts.com



Source: Brean Murray, Carret & Co. estimates

Aqua America Trailing and Forward P/E Ratios, 2004 - 2010



Source: Baseline

Water Industry Comparables

Peer Group Analysis		02/24/11		Mkt. Cap	EPS	EPS	EPS	P/E	P/E	P/E	Est LT EPS
Company Name	Ticker	Price	Rating	(MM)	CY09	CY10E	CY11E	CY09	CY10E	CY11E	Growth
AMERICAN WATER WORKS	AWK	\$27.40	BUY	\$4,792	\$1.24	\$1.53	\$1.67	22.1x	17.9x	16.4x	10.0%
AQUA AMERICA	WTR	\$22.75	BUY	\$3,129	\$0.78	\$0.90	\$0.97	29.2x	25.3x	23.5x	7.0%
YORK WATER CO (THE)	YORW	\$16.97	HOLD	\$215	\$0.64	\$0.71	\$0.76	26.5x	23.9x	22.3x	6.0%
CONSOLIDATED WATER	CWCO	\$10.72	BUY	\$156	\$0.74	\$0.46	\$0.54	14.5x	23.3x	19.9x	20.0%
AMER STATES WATER	AWR	\$33.21	HOLD	\$618	\$1.62	\$2.00	\$2.14	20.5x	16.6x	15.5x	8.0%
CALIFORNIA WATER	CWT	\$36.07	BUY	\$751	\$1.95	\$1.81	\$2.19	18.5x	19.9x	16.5x	7.0%
SJW	SJW	\$23.93	HOLD	\$444	\$0.81	\$0.93	\$1.06	29.5x	25.7x	22.6x	14.0%
Group Average								23.0x	21.8x	19.5x	10.3%

Source: Baseline

Peer Group Analysis		02/24/11		Mkt. Cap	Current	Target	Target	Price	Price	Target	Upside	Yield
Company Name	Ticker	Price	Rating	(MM)	Multiple	Multiple	Multiple	Range	Range	Price	Potential	
					CY10	(Low)	(High)	(Low)	(High)			
AMERICAN WATER WORKS	AWK	\$27.40	BUY	\$4,792	17.9x	15.0x	20.0x	\$25.05	\$33.40	\$35.00	28%	3.2%
AQUA AMERICA	WTR	\$22.75	BUY	\$3,129	25.3x	18.0x	26.0x	\$17.46	\$25.22	\$26.00	14%	2.7%
YORK WATER CO (THE)	YORW	\$16.97	HOLD	\$215	23.9x	19.0x	26.0x	\$14.44	\$19.76	NA	NA	3.1%
CONSOLIDATED WATER	CWCO	\$10.72	BUY	\$156	23.3x	15.0x	23.0x	\$8.10	\$12.42	\$13.00	21%	2.8%
AMER STATES WATER	AWR	\$33.21	HOLD	\$618	16.6x	14.0x	18.0x	\$29.96	\$38.52	NA	NA	3.1%
CALIFORNIA WATER	CWT	\$36.07	BUY	\$751	19.9x	14.0x	18.0x	\$30.66	\$39.42	\$44.00	22%	3.4%
SJW	SJW	\$23.93	HOLD	\$444	25.7x	16.0x	20.0x	\$16.96	\$21.20	NA	NA	2.9%
						16.0x	21.3x					

Sources: Baseline, Brean Murray, Carret & Co.

Aqua America										
Quarterly Income Statement, 2010										
(\$000, except per share data)										
Fiscal year ends December 31										
	1Q10	% Rev or Margin	2Q10	% Rev or Margin	3Q10	% Rev or Margin	4Q10	% Rev or Margin	2010	% Rev or Margin
Sales	160,517		178,444		207,797		179,314		726,072	
Operating & maintenance	67,601	42.1%	69,310	38.8%	72,968	35.1%	70,083	39.1%	279,962	38.6%
Depreciation	26,200	16.3%	26,802	15.0%	27,431	13.2%	27,628	15.4%	108,061	14.9%
Amortization	3,172	2.0%	3,314	1.9%	3,629	1.7%	2,891	1.6%	13,006	1.8%
Non-income taxes	12,860	8.0%	12,943	7.3%	14,182	6.8%	12,982	7.2%	52,967	7.3%
Operating income	50,684	31.6%	66,075	37.0%	89,587	43.1%	65,730	36.7%	272,076	37.5%
Interest expense, net	18,430	11.5%	18,504	10.4%	19,150	9.2%	19,568	10.9%	75,652	10.4%
AFC	(1,541)	-1.0%	(1,461)	-0.8%	(1,077)	-0.5%	(983)	-0.5%	(5,062)	-0.7%
Gain on sale of other assets	(1,929)	-1.2%	(110)	-0.1%	(291)	-0.1%	(253)	-0.1%	(2,583)	-0.4%
Income before taxes	35,724	22.3%	49,142	27.5%	71,805	34.6%	47,398	26.4%	204,069	28.1%
Income taxes	14,213	39.8%	19,287	39.2%	28,054	39.1%	18,540	39.1%	80,094	39.2%
Net income	21,511	13.4%	29,855	16.7%	43,751	21.1%	28,858	16.1%	123,975	17.1%
Earnings per share	\$0.16		\$0.22		\$0.32		\$0.21		\$0.90	
Shares outstanding (000)	136,800		137,012		137,394		137,904		137,278	

Aqua America										
Quarterly Income Statement, 2011E										
(\$000, except per share data)										
Fiscal year ends December 31										
	1Q11E	% Rev or Margin	2Q11E	% Rev or Margin	3Q11E	% Rev or Margin	4Q11E	% Rev or Margin	2011E	% Rev or Margin
Sales	173,358		192,720		224,421		193,659		784,158	
Operating & maintenance	68,997	39.8%	76,124	39.5%	87,524	39.0%	75,914	39.2%	308,559	39.3%
Depreciation	27,217	15.7%	27,366	14.2%	29,624	13.2%	27,500	14.2%	111,707	14.2%
Amortization	2,947	1.7%	3,084	1.6%	3,366	1.5%	3,292	1.7%	12,689	1.6%
Non-income taxes	13,002	7.5%	13,298	6.9%	14,363	6.4%	13,362	6.9%	54,025	6.9%
Operating income	61,196	35.3%	72,848	37.8%	89,544	39.9%	73,590	38.0%	297,178	37.9%
Interest expense, net	19,243	11.1%	19,465	10.1%	21,096	9.4%	19,753	10.2%	79,556	10.1%
AFC	(1,000)	-0.6%	(1,000)	-0.5%	(1,000)	-0.4%	(1,000)	-0.5%	(4,000)	-0.5%
Gain on sale of other assets	(400)	-0.2%	(400)	-0.2%	(400)	-0.2%	(400)	-0.2%	(1,600)	-0.2%
Income before taxes	43,353	25.0%	54,783	28.4%	69,848	31.1%	55,237	28.5%	223,222	28.5%
Income taxes	17,341	40.0%	21,475	39.2%	27,381	39.2%	21,819	39.5%	88,015	39.4%
Net income	26,012	15.0%	33,308	17.3%	42,468	18.9%	33,419	17.3%	135,206	17.2%
Earnings per share	\$0.19		\$0.24		\$0.31		\$0.24		\$0.98	
Shares outstanding (000)	138,004		138,104		138,204		138,304		138,175	

Aqua America										
Quarterly Income Statement, 2012E										
(\$000, except per share data)										
Fiscal year ends December 31										
	1Q12E	% Rev or Margin	2Q12E	% Rev or Margin	3Q12E	% Rev or Margin	4Q12E	% Rev or Margin	2012E	% Rev or Margin
Sales	187,227		208,137		242,374		193,659		831,398	
Operating & maintenance	77,886	41.6%	85,336	41.0%	95,738	39.5%	76,689	39.6%	327,133	39.3%
Depreciation	26,212	14.0%	27,266	13.1%	29,085	12.0%	25,950	13.4%	108,513	13.1%
Amortization	1,872	1.0%	2,081	1.0%	1,939	0.8%	1,743	0.9%	7,636	0.9%
Non-income taxes	12,544	6.7%	13,113	6.3%	14,542	6.0%	11,813	6.1%	52,013	6.3%
Operating income	68,712	36.7%	80,341	38.6%	101,070	41.7%	77,464	40.0%	327,587	39.4%
Interest expense, net	21,157	11.3%	21,646	10.4%	23,026	9.5%	20,722	10.7%	86,550	10.4%
AFC	(1,000)	-0.5%	(800)	-0.4%	(800)	-0.3%	(800)	-0.4%	(3,400)	-0.4%
Gain on sale of other assets	(300)	-0.2%	(300)	-0.1%	(300)	-0.1%	(300)	-0.2%	(1,200)	-0.1%
Income before taxes	48,856	26.1%	59,795	28.7%	79,145	32.7%	57,842	29.9%	245,637	29.5%
Income taxes	19,542	40.0%	23,918	40.0%	31,658	40.0%	23,137	40.0%	98,255	40.0%
Net income	29,313	15.7%	35,877	17.2%	47,487	19.6%	34,705	17.9%	147,382	17.7%
Earnings per share	\$0.21		\$0.26		\$0.34		\$0.25		\$1.07	
Shares outstanding (000)	138,004		138,104		138,204		138,304		138,154	

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

Important Disclosures

Ratings and Target Price History



Priced intraday on 2/24/11.

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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	139	61.5%	17	12.23%
HOLD	63	27.88%	2	3.17%
SELL	7	3.1%	0	0%
NOT RATED	17	7.52%	0	0%
TOTAL	226			

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, based on the shares attaining a level of 27x our 2011 EPS estimate. Risks to the achievement of our target price include weather, acquisitions, interest rates, environmental / public health responsibilities and regulatory climate.

Analyst Certification

We, Michael Gaugler and Christopher Noon, hereby certify that the views expressed in this research report accurately reflect our personal views about any and all of the subject securities or issuers referred to in this document. The analyst and associate analyst further certify that they have not received and will not be receiving direct or indirect compensation in exchange for expressing the recommendation contained in this publication.

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