



May 9, 2011

AQUA AMERICA INC. (WTR)

Rating: **NEUTRAL**
Current Price: **\$22.56**
Target Price: **NA**

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| Industry: Water Utilities | | | | | | | Valuation | | Valuation | |
|---------------------------------|--------|-----------------|--------|--------|--------|--------|-----------|-------|-----------|-------|
| Fiscal Year: Dec | | 1Q11A | 2Q11E | 3Q11E | 4Q11E | FY11E | Multiple | FY12E | Multiple | |
| Market Cap (\$MM): | 3,097 | EPS: | \$0.19 | \$0.23 | \$0.35 | \$0.22 | \$0.99 | 22.8x | \$1.09 | 20.7x |
| | | Prior: | \$0.18 | \$0.25 | - | - | \$1.00 | | \$1.10 | |
| Net Debt (\$MM): | 1,535 | Consensus: | \$0.18 | \$0.24 | \$0.32 | \$0.23 | \$0.97 | 23.3x | \$1.06 | 21.3x |
| Enterprise Value (\$MM): | 4,632 | Last Year: | \$0.16 | \$0.22 | \$0.32 | \$0.21 | \$0.90 | | | |
| Shares - FD (MM): | 137.3 | | | | | | | | | |
| | | EBITDA: | \$0.67 | \$0.76 | \$0.95 | \$0.75 | \$3.13 | 10.8x | \$3.36 | 10.0x |
| Dividend: | \$0.58 | Growth: | 10% | 6% | 7% | 7% | 7% | | 7% | |
| Yield: | 2.6% | | | | | | | | | |
| Beta: | 0.69 | Revenue: | \$171 | \$194 | \$228 | \$188 | \$783 | 5.9x | \$836 | 5.5x |
| Rel. P/E (FY2011E): | 175% | Growth: | 7% | 9% | 10% | 5% | 8% | | 7% | |

WTR: 1Q11 Recap; Maintain NEUTRAL

SUMMARY

- WTR reported adjusted 1Q11 EPS of \$0.19 (vs. 1Q10 of \$0.16), ahead of both our and the consensus \$0.18 estimate. Results exclude a \$0.04/share positive state income tax benefit associated with bonus depreciation allowance.
- Revenues increased 7% y/y vs. our 11% forecast, most of which was attributed to rate increases. Demand was flat to down slightly on a consolidated basis due to wet weather. We were expecting flat demand. Consumption reportedly increased moderately in the company's southern markets, whereas it declined modestly in most northern markets. The results are mostly in line with our recent survey results which pointed to strength in TX offsetting mixed results in PA and weakness in NJ. Regarding its end markets, both industry and commercial consumption increased during the quarter, whereas residential construction was down due to weather and conservation.
- The company sees continued acquisition opportunities and expects to close on 15-20 small deals this year, not to mention the asset swap with AWK later this quarter. It also is expanding its presence in the Marcellus Shale in PA and could entertain energy-play opportunities in TX down the road.
- Cash flow remains strong and management guides that operating cash flow will exceed its ~\$325M capex budget this year. This should lead to 100bp in its equity/capital ratio this year which currently stands at ~43%.
- Management indicated that the First Call mean FY11 estimates of \$0.97/share look reasonable and cautioned that 2Q will be hurt by tough weather related comps, not to mention a wet start to the quarter. We have revised our 2Q11E EPS to \$0.23 (-\$0.02) and our FY11E EPS to \$0.99 (-\$0.01) as the 2Q revision offsets the 1Q beat. Given the company's recent ability to control costs to drive earnings beats, we think its FY11 guidance could prove modestly conservative.
- We are maintaining our NEUTRAL rating, mainly on valuation as the shares are trading at 22.8x our FY11E EPS of \$0.99 and 20.7x our FY12E EPS of \$1.09.

INVESTMENT THESIS

We continue to rate WTR shares NEUTRAL. While we are encouraged by the potential for earnings growth from improved ROEs under systems that were acquired in the southern states in 2003-04, as well as the resumption of acquisition activity, we believe the shares are fairly valued at these levels. The shares are currently trading at 22.8x our FY11E EPS of \$0.99 and 20.7x our FY12E EPS of \$1.09, which is a slight discount to the company's historical 23x average. While we believe WTR should be valued at a premium given the company's size and operational efficiency (the O&M ratio is currently industry leading), we see less upside potential given that valuations are reflecting historically in-line multiples.

DISCUSSION OF DETAILS

WTR reported adjusted 1Q11 EPS of \$0.19 (vs. 1Q10 of \$0.16), ahead of both our and the consensus \$0.18 estimate. Results exclude a \$0.04/share positive state income tax benefit associated with bonus depreciation allowance. Sales of \$171M increased 7% y/y vs. our 11% forecast.

| WTR Summary 1Q11 | | | | | | |
|-------------------------------|-------|-------|----------|----------|----------|------------|
| <i>FY Ends December 31</i> | 1Q10A | 1Q11A | y/y act. | LBR 1Q11 | y/y est. | Actual/LBR |
| Total Revenue | 160.5 | 171.3 | 7% | 177.8 | 11% | -4% |
| Operations & Maintenance | 67.6 | 67.3 | 0% | 73.4 | 9% | -8% |
| Depreciation and Amortization | 29.4 | 29.2 | -1% | 31.2 | 6% | -6% |
| General Taxes | 12.9 | 13.8 | 7% | 13.3 | 4% | 3% |
| Total Expenses | 109.8 | 110.3 | 0% | 118.0 | 7% | -6% |
| Income from Operations | 50.7 | 61.0 | 20% | 59.8 | 18% | 2% |
| Other Income & Expenses (net) | 3.5 | 2.1 | -40% | 1.9 | -46% | 11% |
| EBIT | 54.2 | 63.1 | 16% | 61.7 | 14% | 2% |
| Interest Expense | 18.4 | 19.9 | 8% | 19.8 | 7% | 1% |
| Income Before Taxes | 35.7 | 43.1 | 21% | 41.9 | 17% | 3% |
| Provision for Income Taxes | 14.2 | 17.1 | 20% | 16.8 | 18% | 2% |
| Net Income | 21.5 | 26.1 | 21% | 25.2 | 17% | 4% |
| EPS (fully diluted) | 0.16 | 0.19 | 21% | 0.18 | 16% | 4% |

Source: Company Reports, LBR Estimates

O&M Expenses: Operations and Maintenance expenses increased 3% y/y, excluding the impact of a utility system in Texas. Including the impact, O&M expenses would have declined 0.4% y/y. Excluding the impact of the asset sale, the company's O&M ratio declined 140bp y/y to 40.7%. We note that WTR already has the highest efficiency ratio among the large publicly traded water utilities and margins exceeded our 41.3% forecast. Management noted that chemical costs have remained largely stable throughout the course of the year and that bad debt expense remains at a manageable 0.6%. The company's focus on cost controls helps its cash flows and reduces its reliance on outside funding for its capital programs.

Rate Cases: WTR received \$11.5M in rate awards and infrastructure surcharges in 1Q11 in IN and OH. The company has \$26M of rate cases pending before seven state regulatory bodies, including statewide rate cases in NC, FL, and IL which are largely based on the recovery of capital spending. Additionally, the company expects to seek rate relief by filing cases in seven states later in FY11 that are expected to impact FY12 results, including a filing in PA, which accounts for ~52% of total revenues.



Revenue Growth: Revenues increased 7% y/y vs. our 11% forecast, most of which was attributed to rate increases and surcharges as the company indicated that consumption was flat to down slightly on a consolidated basis due to wet weather. Consumption reportedly increased moderately in the company's southern markets, whereas it declined modestly in most northern markets. Regarding its end markets, both industry and commercial consumption increased during the quarter, whereas residential construction was down due to weather and, naturally, conservation. We were forecasting flat consumption.

The company also discussed a number of interesting developments in rural parts of Pennsylvania adjacent to the Marcellus Shale project and other such natural gas fields throughout the state. In that hydraulic fracking requires nearly 1M gallons of water annually per well, WTR has set up a number of "water stations" in areas surrounding the drills in order to provide the necessary water to the drillers. The company noted that the price it can charge drillers is unregulated and, as such, carries higher margins (with added risk) than the water provided in the company's normal course of business. Management believes this business opportunity can add ~0.3-0.4% of annual growth to the topline and is expected to expand in FY12-13 as additional wells are commissioned in the state. The overall EPS contribution is currently minimal but there could be modest upside going forward. Furthermore, WTR noted that there is an opportunity to export a similar business model to Texas, where the company already maintains regulated operations. We are a bit surprised that WTR has not pursued this opportunity sooner given its initial success in PA.

Capex: WTR has invested \$60M in capex thus far in 1Q11 and expects to invest more than ~\$325M in capex this year, on par with FY10 levels. In addition, the company expects to construct three solar plants that are expected to produce 2,000 kilowatts of electricity as a means to reduce purchased energy costs. The company estimates that the solar plants will reduce its purchased power costs by \$300,000 annually.

No Need for External Financing: Given that WTR is generating ~98% of its cash internally, the company does not see an immediate need to issue equity to fund the company's robust capex program. Indeed, management noted that cash flow from operations will likely exceed its capex budget and, as a result, the company has abandoned planned borrowings in FY11, with the exception of a \$65M loan at sub-2% interest rates. Consequently, management expects its equity/capital ratio to improve ~100bp in FY11. The company has \$88M in available capacity under its existing line of credit and has an average weighted cost of fixed-rate long-term debt of 5.35%.

Acquisition Outlook: WTR reported that its asset swap transaction with AWK (BUY, \$32TP) will likely close in mid-2H11. As a reminder, AWK agreed to sell its regulated Texas operations to WTR and simultaneously purchase WTR's regulated Missouri operations, leading to greater operation efficiencies and economies of scale for both companies. In addition, the company reported that it will likely announce a number of smaller acquisitions in NC, TX and PA, all key markets, in the coming quarter. In sum, the company expects to close 15-20 smaller acquisitions this year, compared to the 23 completed in FY10. The company expects 1% growth through customer acquisitions this year, in line with the historical average.

ESTIMATE REVISIONS

The company indicated that the Street's consensus estimate of \$0.97 for FY11E appears reasonable despite a worse-than-expected start to 2Q11 amid torrential rains in the southeast and cold weather in its northern markets. Management noted that its guidance excludes the impact of the one-time tax benefit during the quarter and the expected \$0.01-0.02/share positive impact each quarter throughout the course of FY11.

Furthermore, WTR expects to generate EBITDA of ~\$420-425M in FY11. We are modeling EBITDA of \$435M and think that given its cost control success, we can see upside to its guidance. That said, our 2Q11E EPS comes down by \$0.02 to \$0.23 on lower demand due to the weather as we are now looking for low-to-mid-single-digit consumption declines vs. flat previously. Our FY11E EPS is \$0.99 (-\$0.01) primarily on the lower 2Q offsetting the 1Q beat. For FY12E, we are modeling EPS of \$1.09 (-\$0.01). We expect 8% and 7% revenue growth over the next two years, respectively.



VALUATION

WTR shares closed Friday at \$22.56 which is 22.8x our FY11E EPS of \$0.99 and 20.7x our FY12E EPS of \$1.09. The shares are trading at a discount to the company's historical 23x average, although within the normalized range of 20-30x forward P/E.

RISKS

Potential downside risks to our investment thesis and estimates include, but are not limited to: 1) a delay in rate case processing or lower rate increases by the regulators than our expectations, 2) a significant revenue loss from lower water demand caused by weather or economic conditions, 3) a significant increase in input costs, including electricity, fuel, chemical and purchase water prices, and 4) large acquisition(s) at excessive valuation(s) (significantly above the rate base).

Potential upside risks to our investment thesis and estimates include, but are not limited to: 1) favorable rate case approvals above our expected ROE, 2) weather conditions leading to near-term revenue increases, and 3) a pullback in input costs.

Aqua America (WTR)
Quarterly Earnings Statement
(dollars in millions, except per share data)

| | Mar-08 | Jun-08 | Sep-08 | Dec-08 | Mar-09 | Jun-09 | Sep-09 | Dec-09 | Mar-10 | Jun-10 | Sep-10 | Dec-10 | Mar-11 | Jun-11 | Sep-11 | Dec-11 | Mar-12 | Jun-12 | Sep-12 | Dec-12 |
|---|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| | 1Q08 | 2Q08 | 3Q08 | 4Q08 | 1Q09 | 2Q09 | 3Q09 | 4Q09 | 1Q10 | 2Q10 | 3Q10 | 4Q10 | 1Q11 | 2Q11E | 3Q11E | 4Q11E | 1Q12E | 2Q12E | 3Q12E | 4Q12E |
| <i>FY ends December 31</i> | | | | | | | | | | | | | | | | | | | | |
| Total Operating Revenue | 139.3 | 150.8 | 177.1 | 159.8 | 154.5 | 167.3 | 180.8 | 167.9 | 160.5 | 178.4 | 207.8 | 179.3 | 171.3 | 194.4 | 228.4 | 188.3 | 191.2 | 208.1 | 238.4 | 198.3 |
| Operation & Maintenance | 64.3 | 65.1 | 66.7 | 65.9 | 67.0 | 68.5 | 68.5 | 66.0 | 67.6 | 69.3 | 73.0 | 70.1 | 67.3 | 75.6 | 81.8 | 71.6 | 78.0 | 80.3 | 84.6 | 75.4 |
| Depreciation | 21.5 | 20.6 | 22.8 | 23.9 | 26.4 | 25.0 | 25.4 | 26.2 | 26.2 | 26.8 | 27.5 | 27.6 | 27.3 | 27.5 | 27.7 | 31.1 | 31.3 | 31.5 | 31.7 | 24.8 |
| Amortization | 1.2 | 1.0 | 1.8 | 1.5 | 2.8 | 3.1 | 3.0 | 3.1 | 3.2 | 3.3 | 3.6 | 2.9 | 2.0 | 3.4 | 3.4 | 3.4 | 3.4 | 3.4 | 3.4 | 3.4 |
| General Taxes | 12.1 | 10.8 | 11.2 | 10.6 | 11.6 | 11.9 | 12.4 | 12.2 | 12.9 | 12.9 | 14.2 | 13.0 | 13.8 | 15.6 | 16.0 | 13.2 | 14.3 | 14.6 | 14.3 | 13.9 |
| Recovery of restructuring costs | | | | | | | | | | | | | | | | | | | | |
| Total Expenses | 99.1 | 97.6 | 102.5 | 102.0 | 107.7 | 108.5 | 109.4 | 107.5 | 109.8 | 112.4 | 118.2 | 113.6 | 110.3 | 122.1 | 128.9 | 119.2 | 127.0 | 129.8 | 134.0 | 117.4 |
| Income from Operations | 40.2 | 53.1 | 74.6 | 57.9 | 46.8 | 58.9 | 71.5 | 60.4 | 50.7 | 66.1 | 89.6 | 65.7 | 61.0 | 72.4 | 99.6 | 69.1 | 64.1 | 78.3 | 104.4 | 80.9 |
| Operating Margin (%) | 28.9% | 35.2% | 42.1% | 36.2% | 30.3% | 35.2% | 39.5% | 36.0% | 31.6% | 37.0% | 43.1% | 36.7% | 35.6% | 37.2% | 43.6% | 36.7% | 33.6% | 37.6% | 43.8% | 40.8% |
| All. for Borrowed Funds Used in Const. | 1.0 | 1.1 | 1.0 | 0.6 | 0.6 | 0.6 | 0.7 | 0.9 | 1.5 | 1.5 | 1.1 | 1.0 | 2.0 | 1.4 | 1.4 | 1.4 | 1.5 | 1.4 | 1.4 | 1.5 |
| Gain (loss) on sale of other assets | | 0.6 | 0.5 | 0.5 | 0.1 | 0.1 | 0.2 | 0.1 | 1.9 | 0.1 | 0.3 | 0.3 | 0.1 | 0.2 | 0.2 | 0.2 | 0.2 | 0.2 | 0.2 | 0.2 |
| Other | | | | | | | | | | | | | | | | | | | | |
| EBIT | 41.2 | 54.8 | 76.1 | 59.0 | 47.5 | 59.5 | 72.4 | 61.4 | 54.2 | 67.6 | 90.9 | 67.0 | 63.1 | 73.9 | 101.1 | 70.7 | 65.9 | 79.9 | 106.0 | 82.5 |
| EBIT (%) | 29.6% | 36.3% | 43.0% | 36.9% | 30.8% | 35.6% | 40.0% | 36.6% | 33.7% | 37.9% | 43.8% | 37.3% | 36.8% | 38.0% | 44.3% | 37.5% | 34.5% | 38.4% | 44.5% | 41.6% |
| Interest Expense | 17.1 | 17.1 | 17.0 | 17.4 | 16.6 | 16.8 | 17.3 | 17.9 | 18.4 | 18.5 | 19.2 | 19.6 | 19.9 | 20.1 | 20.3 | 21.1 | 21.3 | 21.5 | 21.7 | 20.7 |
| Income Before Taxes | 24.0 | 37.7 | 59.1 | 41.7 | 30.9 | 42.7 | 55.1 | 43.5 | 35.7 | 49.1 | 71.8 | 47.4 | 43.1 | 53.8 | 80.8 | 49.6 | 44.5 | 58.4 | 84.3 | 61.8 |
| Provision for Income Taxes | 9.7 | 15.2 | 23.7 | 16.0 | 12.5 | 16.9 | 21.6 | 16.8 | 14.2 | 19.3 | 28.1 | 18.5 | 17.1 | 21.5 | 32.3 | 19.3 | 17.8 | 23.4 | 33.7 | 24.1 |
| Implied Tax Rate | 40.4% | 40.2% | 40.1% | 38.4% | 40.5% | 39.5% | 39.3% | 38.7% | 39.8% | 39.3% | 39.1% | 39.1% | 39.6% | 40.0% | 40.0% | 39.0% | 40.0% | 40.0% | 40.0% | 39.0% |
| Net Income before extraord. Item | 14.3 | 22.6 | 35.4 | 25.7 | 18.4 | 25.9 | 33.5 | 26.7 | 21.5 | 29.8 | 43.7 | 28.9 | 26.1 | 32.3 | 48.5 | 30.2 | 26.7 | 35.1 | 50.6 | 37.7 |
| Comprehensive Income | 14.3 | 22.7 | 35.2 | 25.7 | 18.4 | 26.1 | 33.3 | 26.8 | 21.1 | 29.8 | 43.7 | 28.9 | 26.1 | 32.3 | 48.5 | 30.2 | 26.7 | 35.1 | 50.6 | 37.7 |
| Diluted Net Income Per Share | 0.11 | 0.17 | 0.26 | 0.19 | 0.14 | 0.19 | 0.25 | 0.20 | 0.16 | 0.22 | 0.32 | 0.21 | 0.19 | 0.23 | 0.35 | 0.22 | 0.19 | 0.25 | 0.36 | 0.27 |
| Weighted Avg. Shares | 134.0 | 134.1 | 135.3 | 135.6 | 135.9 | 135.9 | 136.3 | 136.5 | 136.8 | 137.3 | 137.4 | 137.9 | 137.8 | 138.6 | 139.1 | 139.5 | 138.2 | 138.6 | 139.1 | 139.5 |
| Financial Summary (values in %) | | | | | | | | | | | | | | | | | | | | |
| Revenue Growth | 1.4% | 0.1% | 7.0% | 7.2% | 10.9% | 11.0% | 2.1% | 5.0% | 3.9% | 6.6% | 14.9% | 6.8% | 6.7% | 9.0% | 9.9% | 5.0% | 11.6% | 7.0% | 4.4% | 5.3% |
| Operations & Maintenance/Revenue | 46.2% | 43.2% | 37.7% | 41.2% | 43.4% | 41.0% | 37.9% | 39.3% | 42.1% | 38.8% | 35.1% | 39.1% | 39.3% | 38.9% | 35.8% | 38.0% | 40.8% | 38.6% | 35.5% | 38.0% |
| EBIT (% of rev.) | 29.6% | 36.3% | 43.0% | 36.9% | 30.8% | 35.6% | 40.0% | 36.6% | 33.7% | 37.9% | 43.8% | 37.3% | 36.8% | 38.0% | 44.3% | 37.5% | 34.5% | 38.4% | 44.5% | 41.6% |
| General taxes as % of revenue | 8.7% | 7.2% | 6.3% | 6.7% | 7.5% | 7.1% | 6.9% | 7.3% | 8.0% | 7.3% | 6.8% | 7.2% | 8.0% | 8.0% | 7.0% | 7.0% | 7.5% | 7.0% | 6.0% | 7.0% |
| EBITDA | 63.8 | 76.4 | 100.7 | 84.4 | 76.7 | 87.5 | 100.8 | 90.7 | 83.5 | 97.8 | 122.0 | 97.5 | 92.3 | 104.8 | 132.2 | 105.2 | 100.5 | 114.8 | 141.1 | 110.7 |
| Net Income Growth | -15.0% | -5.0% | 19.9% | 3.0% | 28.3% | 14.6% | -5.4% | 3.9% | 17.1% | 15.5% | 30.6% | 8.2% | 21.1% | 8.1% | 10.9% | 4.8% | 2.6% | 8.6% | 4.3% | 24.6% |
| EPS Growth | -15.5% | -5.3% | 18.6% | 1.8% | 26.5% | 13.0% | -6.1% | 3.2% | 16.3% | 14.4% | 29.5% | 7.1% | 20.2% | 7.1% | 9.6% | 3.6% | 2.3% | 8.6% | 4.3% | 24.6% |

Source: Aqua America and Longbow Research
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Aqua America (WTR)
Annual Earnings Statement
(dollars in millions, except per share data)

| <i>Income Statement</i> | FY04A | FY05A | FY06A | FY07A | FY08A | FY09 | FY10 | FY11E | FY12E |
|--|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Total Operating Revenue | 442.0 | 496.8 | 533.5 | 602.5 | 627.0 | 670.5 | 726.1 | 783 | 836 |
| Operation & Maintenance | 178.3 | 203.1 | 219.6 | 253.1 | 262.1 | 270.1 | 280.0 | 296.3 | 318.3 |
| Depreciation | 54.6 | 60.7 | 70.9 | 83.2 | 88.8 | 103.0 | 108.2 | 113.6 | 119.2 |
| Amortization | 4.3 | 4.7 | 4.1 | 4.8 | 5.5 | 11.9 | 13.0 | 12.2 | 13.6 |
| General Taxes | 27.6 | 31.7 | 33.3 | 45.4 | 44.7 | 48.1 | 53.0 | 58.5 | 57.1 |
| - | - | - | - | - | - | - | - | - | - |
| Total Expenses | 264.8 | 300.3 | 327.9 | 386.5 | 401.2 | 433.1 | 454.1 | 480.5 | 508.2 |
| Income from Operations | 177.2 | 196.5 | 205.6 | 216.0 | 225.8 | 237.5 | 272.0 | 302.0 | 327.8 |
| Operating Margin (%) | 40.1% | 39.6% | 38.5% | 35.9% | 36.0% | 35.4% | 37.5% | 38.6% | 39.2% |
| Allow. for Borrowed Funds Used in Const. | 2.3 | 2.4 | 3.9 | 3.0 | 3.7 | 2.9 | 5.1 | 6.1 | 5.8 |
| Gain (loss) on sale of other assets | 1.3 | 1.2 | 1.2 | 3.5 | 1.6 | 0.5 | 2.6 | 0.7 | 0.8 |
| Other | - | - | - | - | - | - | - | - | - |
| EBIT | 180.8 | 200.1 | 210.7 | 222.5 | 231.1 | 240.8 | 279.6 | 308.9 | 334.4 |
| EBIT (%) | 40.9% | 40.3% | 39.5% | 36.9% | 36.9% | 35.9% | 38.5% | 39.5% | 40.0% |
| Interest Expense | 48.7 | 52.1 | 58.4 | 66.9 | 68.6 | 68.6 | 76.3 | 81.6 | 85.3 |
| Income Before Taxes | 132.1 | 148.1 | 152.3 | 155.5 | 162.5 | 172.2 | 203.4 | 227.3 | 249.1 |
| Provision for Income Taxes | 52.1 | 56.9 | 60.2 | 60.5 | 64.6 | 67.8 | 80.1 | 90.3 | 99.0 |
| Implied Tax Rate | 39.4% | 38.4% | 39.6% | 38.9% | 39.7% | 39.4% | 39.4% | 39.7% | 39.8% |
| Net income | 80.0 | 91.2 | 92.0 | 95.0 | 97.9 | 104.4 | 123.3 | 137.0 | 151.1 |
| Comprehensive Income | 78.1 | 89.8 | 95.3 | 94.8 | 97.9 | 104.7 | 122.0 | 137.0 | 151.1 |
| Diluted Net Income Per Share | 0.64 | 0.71 | 0.70 | 0.71 | 0.73 | 0.77 | 0.90 | 0.99 | 1.09 |
| Weighted Avg. Shares | 125.7 | 129.2 | 131.8 | 133.6 | 134.7 | 136.1 | 137.3 | 138.7 | 138.8 |
| Financial Summary (values in %) | | | | | | | | | |
| Revenue Growth | 20.4% | 12.4% | 7.4% | 12.9% | 4.1% | 6.9% | 8.3% | 7.8% | 6.8% |
| Operations & Maintenance/Revenue | 40.3% | 40.9% | 41.2% | 42.0% | 41.8% | 40.3% | 38.6% | 37.9% | 38.1% |
| Dep/Net Fixed Asset | 3.0% | 2.9% | 3.1% | 3.3% | 3.2% | 3.4% | 3.4% | 3.3% | 3.3% |
| Depreciation Growth | 12.5% | 11.3% | 16.7% | 17.3% | 6.7% | 16.0% | 5.0% | 5.0% | 5.0% |
| General taxes as % of revenue | 6.2% | 6.4% | 6.2% | 7.5% | 7.1% | 7.2% | 7.3% | 7.5% | 6.8% |
| Interest Exp/ Average Net Debt | 5.6% | 5.3% | 5.8% | 5.9% | 5.2% | 5.0% | 5.0% | 4.8% | 4.9% |
| Interest Expense/Revenue | 11.0% | 10.5% | 11.0% | 11.1% | 10.9% | 10.2% | 10.5% | 10.4% | 10.2% |
| EBITDA | 239.7 | 265.6 | 285.7 | 310.5 | 325.4 | 355.7 | 400.8 | 434.6 | 467.2 |
| Net income growth | 13.0% | 13.9% | 0.9% | 3.3% | 3.1% | 6.6% | 18.1% | 11.2% | 10.2% |
| Average ROE | 11.4% | 11.7% | 10.6% | 10.0% | 9.6% | 9.6% | 10.8% | 11.4% | 11.8% |
| EPS Growth (exspecial items and FAS 123) | 7.0% | 10.9% | -1.0% | 1.9% | 2.2% | 5.5% | 17.1% | 10.0% | 10.2% |

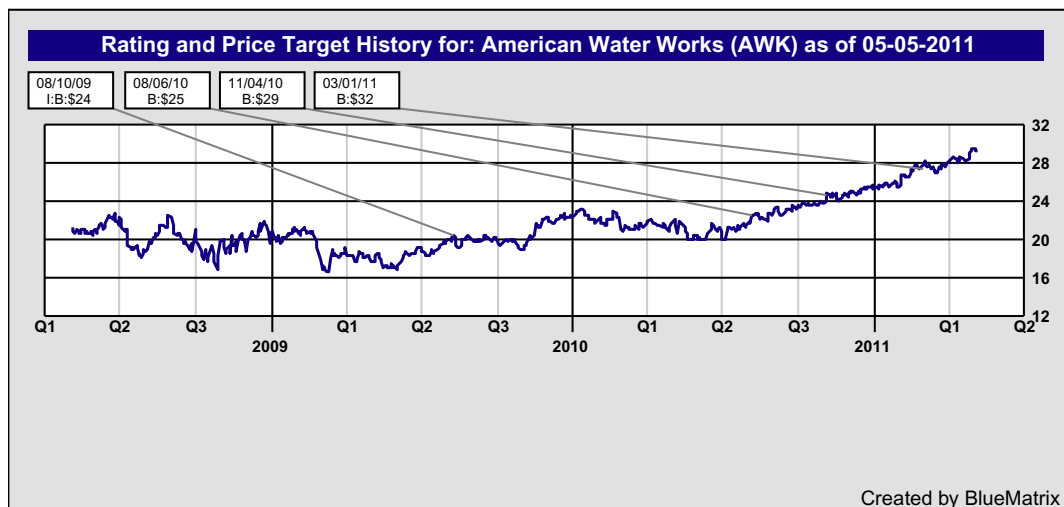
Source: Aqua America and Longbow Research
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WATER INDUSTRY PEER VALUATION
(\$ in millions, except per share data)

| Company | Ticker | FY End | Rating | Target | % Upside | Share Price | 52 Week | | Mkt Cap | Revenue Last | Last FY | Earnings per Share | | P/E | | Dividend Rate | Price/Book |
|--|--------|--------|---------|--------|----------|-------------|---------|---------|----------|--------------|---------|--------------------|---------|------------|---------|---------------|------------|
| | | | | | | | Hi | Lo | | | | Current FY | Next FY | Current FY | Next FY | | |
| U.S. WATER UTILITIES | | | | | | | | | | | | | | | | | |
| AMER STATES WATER | AWR | Dec. | Neutral | | | \$33.65 | \$39.44 | \$31.24 | \$ 631 | \$ 434 | 2.02 | 2.00 | 2.15 | 16.8x | 15.7x | 3.3% | 0.9x |
| AMERICAN WATER WORKS | AWK | Dec. | BUY | \$32 | 9% | \$29.28 | \$29.91 | \$19.41 | \$ 5,119 | \$ 2,093 | 1.53 | 1.72 | 1.88 | 17.0x | 15.6x | 3.0% | 1.1x |
| AQUA AMERICA | WTR | Dec. | Neutral | | | \$22.56 | \$23.79 | \$16.52 | \$ 3,095 | \$ 726 | 0.90 | 0.99 | 1.09 | 22.8x | 20.7x | 2.8% | 2.6x |
| CALIFORNIA WATER | CWT | Dec. | Neutral | | | \$36.49 | \$39.53 | \$33.81 | \$ 763 | \$ 460 | 1.81 | 2.04 | 2.22 | 17.9x | 16.4x | 3.4% | 1.8x |
| ARTESIAN RESOURCES | ARTNA | Dec. | NR | | | \$19.15 | \$19.99 | \$16.43 | \$ 143 | \$ 65 | 1.01 | 1.07 | 1.15 | 17.9x | 16.7x | 4.0% | 1.5x |
| CONNECTICUT WATER | CTWS | Dec. | NR | | | \$24.87 | \$28.27 | \$20.00 | \$ 217 | \$ 66 | 1.13 | 1.2 | 1.25 | 20.7x | 19.9x | 3.7% | 2.1x |
| MIDDLESEX WATER | MSEX | Dec. | NR | | | \$18.20 | \$19.31 | \$14.74 | \$ 281 | \$ 103 | 0.94 | 0.95 | 0.95 | 19.2x | 19.2x | 4.1% | 1.6x |
| PENNICHUCK | PNNW | Dec. | NR | | | \$28.40 | \$28.60 | \$20.77 | \$ 133 | \$ 36 | 0.85 | 0.8 | 1.15 | 35.5x | 24.7x | 2.6% | 1.8x |
| SIW | SIW | Dec. | NR | | | \$22.53 | \$28.00 | \$22.25 | \$ 419 | \$ 216 | 0.93 | 0.99 | 1.10 | 22.8x | 20.5x | 3.1% | 1.9x |
| YORK WATER CO (THE) | YORW | Dec. | NR | | | \$16.76 | \$18.00 | \$12.83 | \$ 214 | \$ 39 | 0.71 | 0.76 | 0.79 | 22.1x | 21.2x | 3.1% | 2.4x |
| Average | | | | | | | | | | | | | | 21.3x | 19.1x | 3.3% | 1.8x |
| EQUIPMENT/ FILTRATION/ TREATMENT SECTOR | | | | | | | | | | | | | | | | | |
| PENTAIR | PNR | Dec. | BUY | \$45 | 15% | \$39.07 | \$40.57 | \$29.41 | \$ 3,837 | \$ 3,031 | 2.00 | 2.44 | 2.82 | 16.0x | 13.9x | 2.1% | 1.7x |
| WATTS WATER TECH | WTS | Dec. | Neutral | | | \$36.22 | \$40.75 | \$27.51 | \$ 1,344 | \$ 1,275 | 1.60 | 1.68 | 2.24 | 21.6x | 16.2x | 1.2% | 1.5x |
| AMERON INT'L | AMN | Nov. | NR | | | \$67.07 | \$85.25 | \$55.42 | \$ 613 | \$ 503 | 5.10 | 1.55 | 3.62 | 43.3x | 18.5x | 1.8% | 1.1x |
| BADGER METER | BMI | Dec. | NR | | | \$36.59 | \$45.49 | \$33.98 | \$ 546 | \$ 277 | 1.88 | 1.67 | 2.01 | 21.9x | 18.2x | 1.5% | 3.9x |
| CALGON CARBON | CCC | Dec. | NR | | | \$17.32 | \$18.20 | \$11.75 | \$ 987 | \$ 482 | 0.75 | 0.82 | 0.98 | 21.1x | 17.7x | 0.0% | 2.5x |
| ENERGY RECOVERY | ERII | Dec. | NR | | | \$2.71 | \$4.88 | \$2.84 | \$ 152 | \$ 46 | -0.08 | (0.13) | 0.02 | NM | NM | 0.0% | 1.6x |
| FRANKLIN ELECTRIC | FELE | Jan. | NR | | | \$43.00 | \$48.23 | \$27.04 | \$ 988 | \$ 714 | 1.94 | 2.39 | 2.82 | 18.0x | 15.2x | 1.2% | 2.2x |
| GORMAN-RUPP | GRC | Dec. | NR | | | \$38.83 | \$40.75 | \$24.00 | \$ 646 | \$ 297 | 1.53 | 1.80 | 2.08 | 21.6x | 18.7x | 1.2% | 2.7x |
| ITRON | ITRI | Dec. | NR | | | \$52.98 | \$78.45 | \$50.76 | \$ 2,157 | \$ 2,265 | 4.00 | 4.23 | 4.25 | 12.5x | 12.5x | 0.0% | 1.6x |
| LAYNE CHRISTENSEN | LAYN | Jan. | NR | | | \$28.02 | \$38.00 | \$22.97 | \$ 548 | \$ 1,026 | 1.54 | 1.55 | 1.92 | 18.1x | 14.6x | 0.0% | - |
| MUELLER WATER PRODUC | MWA | Sept. | NR | | | \$4.23 | \$5.22 | \$2.21 | \$ 656 | \$ 1,338 | -0.19 | 0.01 | 0.15 | NM | NM | 1.7% | 1.2x |
| NORTHWEST PIPE | NWPX | Dec. | NR | | | \$22.02 | \$24.94 | \$14.62 | \$ 200 | \$ 387 | -0.16 | 0.68 | 1.34 | 32.4x | 16.4x | 0.0% | 0.9x |
| PALL | PLL | Jul. | NR | | | \$54.99 | \$59.50 | \$31.84 | \$ 6,402 | \$ 2,402 | 2.12 | 3.00 | 3 | 18.3x | 18.3x | 1.3% | 3.7x |
| SMITH (A.O.) | AOS | Dec. | NR | | | \$42.01 | \$45.80 | \$29.24 | \$ 1,910 | \$ 2,026 | 2.87 | 2.09 | 2.44 | 20.1x | 17.2x | 1.3% | 2.1x |
| Average | | | | | | | | | | | | | | 20.1x | 16.1x | 0.7% | 2.0x |
| WATER RESOURCES/ INFRASTRUCTURE | | | | | | | | | | | | | | | | | |
| INSITUFORM TECH | INSU | Dec. | NR | | | \$25.49 | \$30.00 | \$18.52 | \$ 988 | \$ 915 | 1.50 | 1.74 | 2.22 | 14.5x | 11.3x | 0.0% | 1.7x |
| LINDSAY | LNN | Aug. | NR | | | \$65.06 | \$85.87 | \$30.80 | \$ 810 | \$ 358 | 1.83 | 2.68 | - | 24.5x | 22.0x | 0.5% | 2.0x |
| TETRA TECH | TTEK | Sept. | NR | | | \$23.46 | \$27.16 | \$18.00 | \$ 1,409 | \$ 2,201 | 1.22 | 1.40 | 1.64 | 16.2x | 14.3x | 0.0% | 1.7x |
| Average | | | | | | | | | | | | | | 19.0x | 16.5x | 0.6% | 2.2x |
| Relevant Indices | | | | | | | | | | | | | | | | | |
| Dow Jones Industrials | DJ30 | | | | | Share Price | | | | | | | | | | | |
| S&P 500 | SPX | | | | | \$12,595.00 | | | | | | | | | | | |
| Nasdaq Composite | NDX | | | | | \$1,334.50 | | | | | | | | | | | |
| | | | | | | \$2,373.50 | | | | | | | | | | | |

Source: Baseline; Company reports and LBR Estimates. EPS reflects diluted EPS, excluding extraordinary items. Numbers in italics reflect consensus estimates.

** Time period for annual estimates may vary based on reporting date.



APPENDIX

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Covered Companies Mentioned In This Report:

| | | | |
|----------------------|-----|---------|---------|
| American Water Works | AWK | \$29.20 | Buy |
| Aqua America Inc. | WTR | \$22.56 | Neutral |

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