

Water Utilities

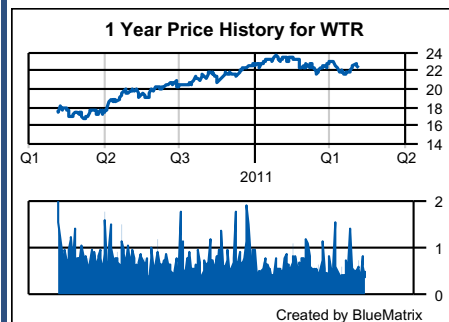
Aqua America, Inc.
(WTR) - NEUTRAL

Price: **\$22.43**
 Fair Value Estimate: \$22.00
 52-Week Range: \$23.79-\$16.52
 Market Cap (MM): \$3,095
 Shr.O/S-Diluted (mm): 138.0
 Average Daily Volume: 618,630
 Dividend: \$0.62
 Yield: 2.8%

FYE: Dec	2010A	2011E	2012E
EPS:	\$0.90A	\$1.00E	\$1.05E
Prior EPS:		\$0.95	NC
P/E Ratio:	24.9x	22.4x	21.4x

Quarterly EPS:

Quarter	2010A	2011E	2012E
Q1	\$0.16A	\$0.22A	\$0.20E
Q2	\$0.22A	\$0.23E	\$0.25E
Q3	\$0.32A	\$0.32E	\$0.35E
Q4	\$0.21A	\$0.23E	\$0.25E



Equity Research
Note

**Record Q1 Results & Positive Outlook -
 Maintain NEUTRAL on Valuation**

INVESTMENT CONCLUSION:

Among the largest and best-run companies in the water utility arena, we view Aqua America as a "best-of-breed" player in this space. Indeed, Aqua is at or near the head of the class on most key financial metrics, and the company has concentrated regulatory exposure to Pennsylvania (Aqua PA represents more than 50% of sales), which is widely regarded as among the nation's most progressive, forward-looking regulatory jurisdictions (see our 4/20/2011 Regulatory Climate Index for details). In the near-term, the company is primed to benefit from continued rate relief, with outstanding requests in seven states. Going forward, we expect Aqua America to continue delivering on its dual growth strategy of rate base investment and small-system acquisitions, with the company targeting 10% net income growth over time. WTR shares trade at a premium to the peer group, and we believe the stock's current levels accurately account for the firm's future growth outlook and cost-consciousness. We maintain our NEUTRAL rating for WTR.

KEY POINTS:

- **1Q-2011 above our estimate.** Aqua America reported adjusted first quarter earnings of \$0.19/share, ahead of both our estimate (\$0.17/share) and consensus expectations (\$0.18/share). Including a state income tax benefit of \$0.03/share, GAAP results of \$0.22/share grew 40% to set a new Q1 record.
- **Solid top-line; cost controls drive EPS.** Revenue grew 7% due primarily to new rates hitting the P&L, while O&M expenses declined from the same period last year. A system sale in Texas helped reduce O&M expenses by \$2.5 million, driving 280bps of improvement in the O&M/revenue ratio to 39.3%. Resulting Q1 operating margin was the highest we have seen since 2005 at 36.5%. Tax benefits associated with bonus depreciation on capex in Pennsylvania provided a boost to the bottom-line and will continue to benefit results approximately 1-2 cents per quarter in 2011.
- **Expect another year of strong capital investment; rates to follow.** With plans to match the record \$327 million in capital spent in 2010, Aqua will look to recover its investment with rate filings in 2011. Cases in seven states (\$26 million) are pending decision - including NC, FL, & IL. The company will file additional cases in 2011 (including its large PA rate case), providing a base for 2012 growth.
- **Acquisition growth & Marcellus opportunity.** Aqua's acquisition program drove 1% customer growth in 2010 - not insignificant considering the limited organic growth opportunities amidst the U.S. housing market. Small system acquisitions (several to be announced in Q2) should contribute to the top-line at a similar pace in 2011. Aqua's presence in the Marcellus Shale will also offer new opportunities as water-intensive "fracking" operations expand.
- **Premium valuation reflects industry leader status.** While we believe WTR shares deserve a premium valuation based upon the company's strong track record and profitability, we see limited multiple expansion from current levels. However, WTR remains a compelling source of risk-adjusted total return for long-term oriented holders, and we would look for advantageous entry points. We maintain our NEUTRAL rating and raise our fair value estimate to \$22 (\$21 previously).

Research Analyst Certifications and Important Disclosures are on pages 3 - 4 of this report

Aqua America, Inc.		Janney Montgomery Scott LLC								
Quarterly Income Statement, 2011E										
	1Q11	Y/Y	2Q11E	Y/Y	3Q11E	Y/Y	4Q11E	Y/Y	FY2011E	Y/Y
Operating Revenues	171,324	6.7%	187,366	5.0%	218,187	5.0%	188,280	5.0%	765,157	5.4%
Operations and Maintenance	67,325	-0.4%	71,199	2.7%	80,729	10.6%	72,488	3.4%	291,741	4.2%
<i>O&M Ratio</i>	39.3%		38.0%		37.0%		38.5%		38.1%	-1.1%
Depreciation	27,293		28,000		28,700		29,300		113,293	4.8%
Amortization	1,956		3,000		3,000		2,000		9,956	
Taxes other than Income Taxes	13,765		13,800		13,500		13,240		54,305	
Operating Income	60,985	20.4%	71,367	8.0%	92,258	3.0%	71,252	8.4%	295,862	8.7%
<i>Operating Margin</i>	35.6%		38.1%		42.3%		37.8%		38.7%	
Interest Expense	19,943		20,000		20,000		20,160		80,103	5.9%
Allowance for Construction Funds	(1,977)		(1,500)		(1,000)		(1,000)		(5,477)	
Gain on Sale of other Assets	(121)		(150)		(150)		(150)		(571)	
Income before Income Taxes	43,140	20.9%	53,017	7.9%	73,408	2.2%	52,242	10.2%	221,807	8.7%
Income Taxes	12,789		20,677		28,629		20,374		82,469	
<i>Tax Rate</i>	29.6%		39.0%		39.0%		39.0%		37.2%	
Net Income	30,353	41.3%	32,340	8.3%	44,779	2.3%	31,868	10.4%	139,338	12.4%
Diluted EPS	\$0.22	39.7%	\$0.23	7.1%	\$0.32	1.3%	\$0.23	9.2%	\$1.00	11.2%
Diluted Shares Outstanding	138,384		138,600		138,850		139,400		138,809	

Aqua America, Inc.		Janney Montgomery Scott LLC								
Quarterly Income Statement, 2012E										
	1Q12E	Y/Y	2Q12E	Y/Y	3Q12E	Y/Y	4Q12E	Y/Y	FY2012E	Y/Y
Operating Revenues	180,747	5.5%	197,671	5.5%	235,642	8.0%	203,342	8.0%	817,402	6.8%
Operations and Maintenance	70,491		75,115		87,187		77,270		310,064	
<i>O&M Ratio</i>	39.0%		38.0%		37.0%		38.0%		37.9%	
Depreciation	30,000		30,500		31,500		32,300		124,300	
Amortization	2,500		3,000		3,000		3,000		11,500	
Taxes other than Income Taxes	13,000		13,000		13,500		13,240		52,740	
Operating Income	64,756	6.2%	76,056	6.6%	100,454	8.9%	77,532	8.8%	318,798	7.8%
<i>Operating Margin</i>	35.8%		38.5%		42.6%		38.1%		39.0%	
Interest Expense	20,000		20,000		20,000		20,160		80,160	
Allowance for Construction Funds	(750)		(750)		(750)		(750)		(3,000)	
Gain on Sale of other Assets	(150)		(150)		(150)		(150)		(600)	
Income before Income Taxes	45,656	5.8%	56,956	7.4%	81,354	10.8%	58,272	11.5%	242,238	9.2%
Income Taxes	18,034		22,498		32,135		22,726		95,393	
<i>Tax Rate</i>	39.5%		39.5%		39.5%		39.0%		39.4%	
Net Income	27,622	-9.0%	34,459	6.5%	49,219	9.9%	35,546	11.5%	146,846	5.4%
Diluted EPS	\$0.20	-9.9%	\$0.25	5.5%	\$0.35	8.8%	\$0.25	10.7%	\$1.05	4.4%
Diluted Shares Outstanding	139,750		140,000		140,250		140,500		140,125	

Company Description

Aqua America, Inc. provides water and wastewater utility service to suburban areas outside of Philadelphia, Chicago, and Cleveland, as well as other communities throughout 13 states, including Pennsylvania, New York, Ohio, North Carolina, Illinois, Texas, Florida, New Jersey, Indiana, Virginia, Maine, Missouri, and South Carolina.

IMPORTANT DISCLOSURES

Research Analyst Certification

I, Ryan M. Connors, the Primarily Responsible Analyst for this research report, hereby certify that all of the views expressed in this research report accurately reflect my personal views about any and all of the subject securities or issuers. No part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views I expressed in this research report.

Janney Montgomery Scott LLC ("Janney") Equity Research Disclosure Legend

Janney Montgomery Scott is a market maker in the securities of WTR, and may at any time hold a long or short position in this security.

Janney Montgomery Scott or an affiliate managed or co-managed a public offering of WTR security in the past 12 months.

Janney Montgomery Scott may seek compensation for investment banking services from the subject company (ies) WTR security in the next 3 months.

The research analyst is compensated based on, in part, Janney Montgomery Scott's profitability, which includes its investment banking revenues.

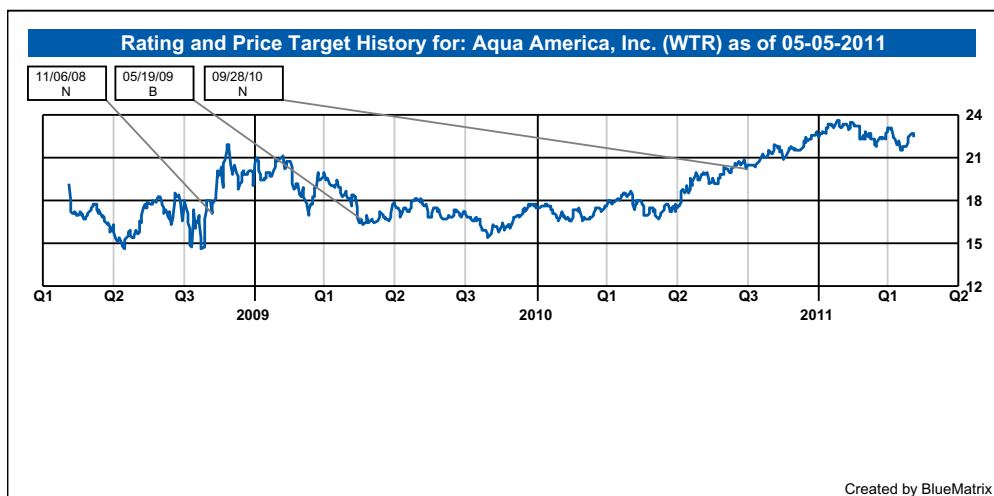
Definition of Ratings

BUY: Janney expects that the subject company will appreciate in value. Additionally, we expect that the subject company will outperform comparable companies within its sector.

NEUTRAL: Janney believes that the subject company is fairly valued and will perform in line with comparable companies within its sector. Investors may add to current positions on short-term weakness and sell on strength as the valuations or fundamentals become more or less attractive.

SELL: Janney expects that the subject company will likely decline in value and will underperform comparable companies within its sector.

Price Charts



Janney Montgomery Scott Ratings Distribution as of March 31, 2011

Rating	IB Serv./Past 12 Mos.			
	Count	Percent	Count	Percent
BUY [B]	185	53	15	8
NEUTRAL [N]	160	45	9	6
SELL [S]	8	2	0	0

***Percentages of each rating category where Janney has performed Investment Banking services over the past 12 months.**

Other Disclosures

Investment opinions are based on each stock's 6-12 month return potential. Our ratings are not based on formal price targets, however our analysts will discuss fair value and/or target price ranges in research reports. Decisions to buy or sell a stock should be based on the investor's investment objectives and risk tolerance and should not rely solely on the rating. Investors should read carefully the entire research report, which provides a more complete discussion of the analyst's views.

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