LONGBOW Research
Tactical advantage through independent research

Initiating Coverage

August 10, 2009

Analysts:
GARIK SHMOIS
T: 216-525-8414
E: gshmois@longbowresearch.com

VISHAL KHETRIWAL, CFA
T: 216-525-8469
E: vkhetriwal@longbowresearch.com

Industry: **WATER UTILITIES**

Coverage:

Ticker	Rating	Price
AWK	BUY	$20.13
AWR	NEUTRAL	$33.41
CWT	BUY	$36.97
WTR	NEUTRAL	$17.55

Initiating Coverage of Water Utilities

- We are initiating coverage of the water utilities industry and AWK (BUY-$24 PT), CWT (BUY-$45 PT), AWR (NEUTRAL) and WTR (NEUTRAL). The group is characterized by a high degree of capital spending, earnings regulation, acquisitions of smaller utility systems and attractive dividends.
- The high capital intensity of the sector requires almost continuous rate case filings, with the outcome dependent on the states in which the companies operate. On average, a rate case lasts approximately nine months and results in an allowed ROE of 9-11%, and 55-75% of the requested revenues are approved. Rate cases typically attempt to recover 18-24 months of back revenues.
- We believe that aggressive capex schedules over the next three to five years (8% above the prior three years on average) should translate to increased earnings growth once rate increases catch up to capital investments.
- The large capex needs of the industry and high fragmentation should lead to consolidation over time. In the near term, we anticipate most acquisitions will likely be of smaller private utilities selling out to publicly traded names, as municipalities choose to hold onto water assets given its predictable returns and a perception that localities are better equipped to serve the public good than the private sector.
- Valuations appear attractive and all of the stocks under our coverage are trading at a discount to historical averages. We believe multiples should expand as the group demonstrates sustained earnings growth from recent capital initiatives.

IMPORTANT DISCLOSURES ARE LOCATED IN THE APPENDIX.

Longbow Research, 6000 Lombardo Center, Suite 500, Independence, Ohio USA 44131
T: 216-986-0700 • F: 216-986-0720 • www.longbowresearch.com

TABLE OF CONTENTS

INDUSTRY INVESTMENT THESIS

We prefer AWK and CWT in the water utility space.

We are initiating coverage of the water utilities industry and AWK (BUY-$24 PT), CWT (BUY-$45 PT), AWR (NEUTRAL) and WTR (NEUTRAL). The group is characterized by a high degree of capital spending, earnings regulation, acquisitions of smaller utility systems and attractive dividends. The principal differentiator is based on geographic positioning, relative rate case catch up, and valuations compared to historical averages.

In a nutshell, we prefer AWK as we believe the shares can see multiple expansions off of current depressed levels. In our view, the discount in the shares from the RWE overhang and a lagging ROE should dissipate. While we cannot predict the timing of when RWE will sell its interest, we do see improved business fundamentals that offer a positive catalyst. We also anticipate adj. ROE improving to an average 8.9% over the next three years, which is more closely aligned to the peer group, vs. the company's 7-8% average over the past two years.

We also rate CWT a BUY as valuations are attractive relative to the company's historical performance. Additionally, the improved revenue recognition method in California under WRAM should help remove some of the volatility in earnings. AWR also benefits from this and we like the company's near-term earnings growth prospects but feel that valuations are not as compelling as they are for CWT.

We rate WTR as NEUTRAL and see the shares as fairly valued. There's a lot to like in WTR, as it has an industry-leading O&M ratio, is a principal acquirer of small systems, and should benefit from $106M in rate increases over the next two years. While we see the shares as trading at a 15% discount to their historical 23x forward P/E average, relative to our preferred AWK and CWT, WTR shares appear to offer less upside at current levels.

We also rate AWK a NEUTRAL, as we see the upside related to rate relief as largely reflected in the shares. At 17.5x our FY10E EPS of $1.91, AWR is trading at a discount to its historical 20x forward P/E average. However, should multiples expand to the historical average, the resulting fair value of $38/share does not imply the same amount of potential upside as do our preferred names in the space, AWK and CWT.

Timely Rate Increases are Key to Continued Profitability

Capex, aimed toward repair and replacement, is the main driver of organic growth.

The water utility industry is highly capital intensive and needs large investments to repair and build-out water and wastewater systems. As investments are aimed towards maintenance and repair, capex is generally less cyclical. However, impacting earnings volatility is the extent to which companies receive rate increases, granted by state PUCs, to offset high capital spending. The timing and amount of rate cases is an ongoing process that, on one hand, nearly provides a steady ROE but, on the other hand, can lead to several quarters of underperformance until rate relief is granted. While many states have instituted alternative revenue collecting mechanisms in between rate cases, the continual ebb and flow between the utilities and the PUCs determines, to a large extent, the timing and amount of earnings growth.

California and Pennsylvania are among the most progressive markets for water utilities.

The high capital intensity of the sector requires almost continuous rate case filings with the outcome dependent on the states wherein the companies operate. We note that Pennsylvania and California are among the most progressive markets. On average, a rate case lasts approximately nine months and results in an allowed ROE of 9-11%, and 55-75% of the requested revenues are approved. In states that do not use a forward test year, rate cases typically attempt to catch up for 18-24 months of back inflation.

We see the industry growing earnings 8-10% annually from FY09E to FY11E, largely as rate cases offset modest organic declines. In our view, AWK offers the most attractive near-term EPS growth prospects. The company has an aggressive capex program, which should also help sustain EPS growth in the long term. In the near term, the company is trying to recover from rate case stay-outs, which happened during RWE's ownership from FY02 to FY07.

Most Acquisitions are of Small Private Systems

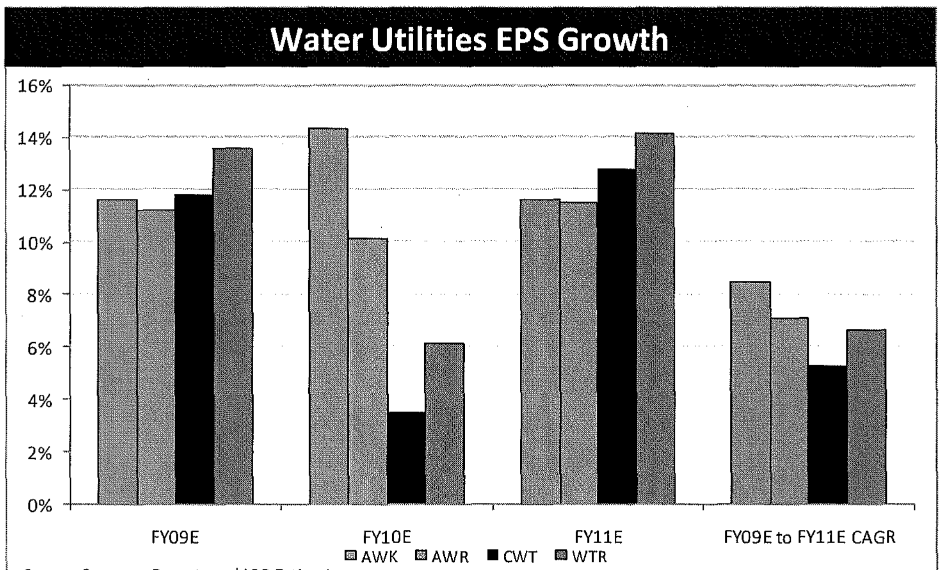
Municipal budget shortfalls during the current downturn have yet to materialize in any major acquisitions for water utilities firms.

The large capex needs of the industry and high fragmentation should lead to consolidation; however, we have principally seen small tuck-ins during the current downturn despite municipalities needing to raise cash. We anticipate most acquisitions will likely continue to be of smaller private utilities selling out to publicly traded names, as municipalities choose to hold onto water assets given its predictable returns and a perception that they are better equipped to service the public good than is the private sector. Additionally, while municipalities are struggling financially, the economic stimulus package provides low-cost financing to fund infrastructure repair programs, which is relieving pressure to sell water assets.

Large Acquisitions Can Depress Earnings in the Short to Medium Term

Large acquisitions are rare and may not be accretive to earnings. We are not modeling a meaningful acceleration in acquisitions over the next two to three years.

We caution investors that while acquisitive growth has the potential to increase somewhat, mainly on the private-to-private side, large acquisitions may not be as accretive as initially hoped, as evidenced by WTR's large purchases in FY02-FY03, which essentially contributed to flat EPS growth through FY07. Navigating the political process of new public commissions has led to publicly traded utilities being "gun-shy" about entering new states where political connections have not been established. While industry consolidation will likely continue to varying degrees, we are not modeling a meaningful acceleration over the next two to three years. However, our view of the space is that significant rate relief over this time period should lead to 8-10% earnings growth for the four companies on which we are launching coverage.

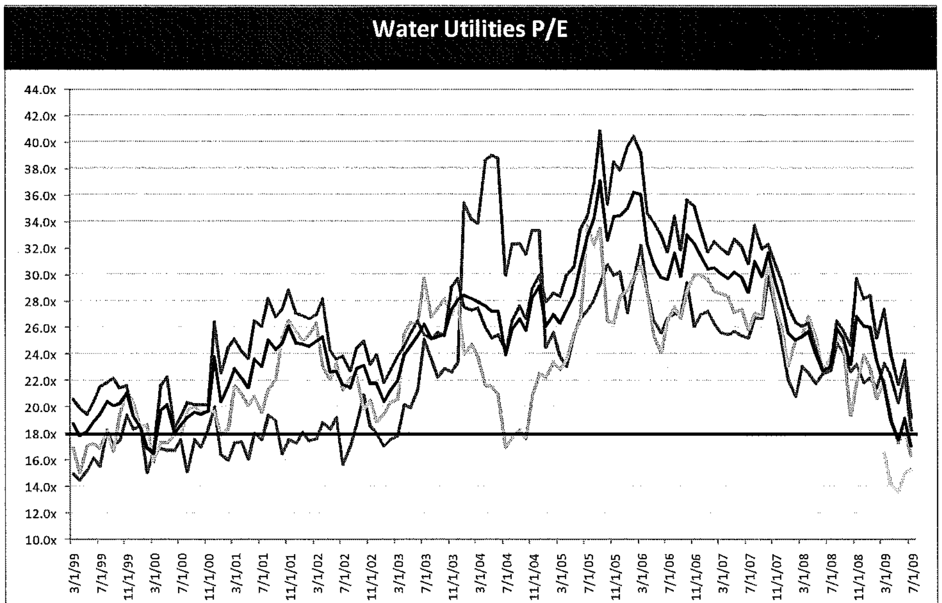


Source: Company Reports and LBR Estimates

Valuations Cheap Compared to Historical Trends

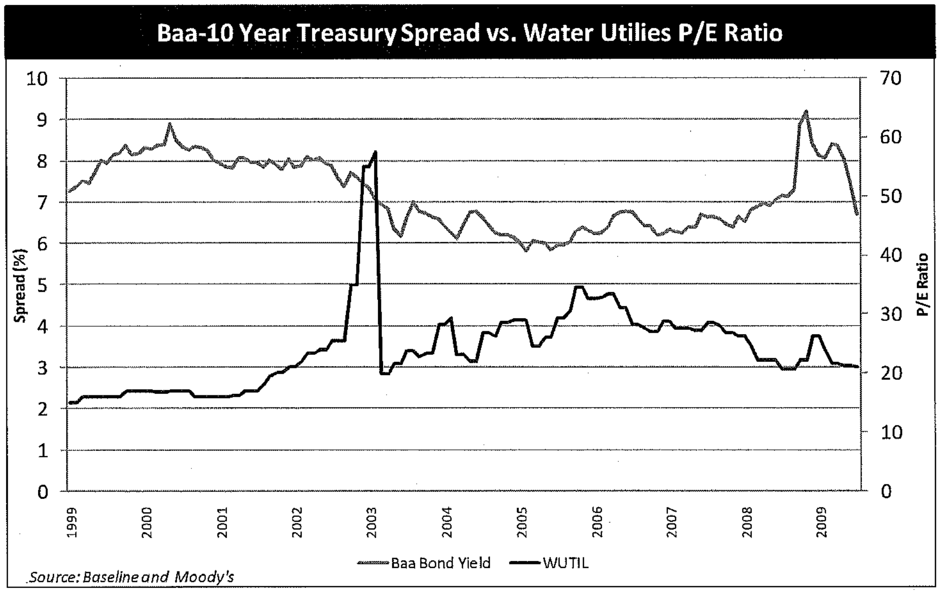
Sector is attractive, with the companies under coverage trading below historical forward P/E valuations.

We note that multiples have been under pressure in recent months, with the coverage group at valuations well off recent highs. However, rate case relief from FY09 to FY11 should help sustain earnings growth above prior levels. Consequently, we see the sector as attractive at current levels. We see the long-run valuation of 20x as reasonable, especially when compared to multiples north of 30x the group was commanding four to five years ago. Currently, P/E valuations for our coverage list average 18x and peer group average of 19x. Relative to historical performance, AWK is trading at 13.5x our FY10E EPS vs. what we believe should be an appropriate 16x multiple (a 12% discount to the coverage group, 16% discount to the peer group). CWT is trading at 16.8x our FY10E EPS, and we believe valuations should be more closely in line with the company's 20x-21x average. AWR is trading at 17.5x our FY10E, offering less upside relative to the group when compared to its 20x average. WTR is trading at 19.4x our FY10E, which is below the company's 23x average multiple. However, we agree that a premium valuation for WTR is warranted given the company's size, geographic positioning, and an industry-leading O&M ratio.



Source: Company Reports, Baseline

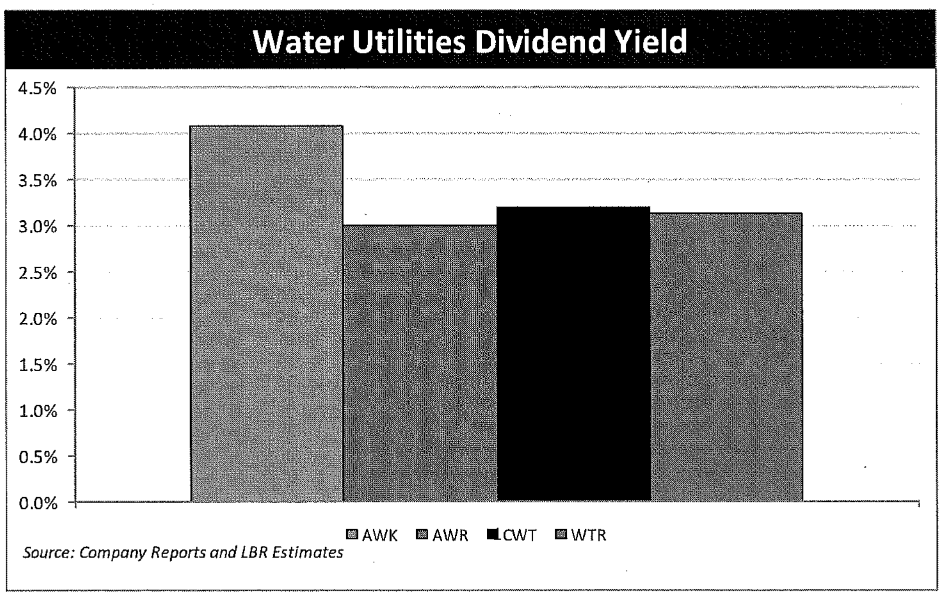
We notice a general inverse relationship between the Baa Bond and P/E ratios for water utilities, which makes sense to us as a wider credit spread negatively impacts capital spending given higher borrowing costs, and thereby lowers earnings from lower capex spending. Should the spread continue to narrow, as has been the case over the last seven months, we would expect multiples to expand in a way more closely reflecting the historical group average of 20x vs. the current 18x forward P/E for the coverage list. We note an average credit spread of 2.6% vs. the current ~3.2%. Should the credit spread revert towards its historical norm, this could be a positive implication for water utilities stocks.



Attractive Dividend Yields

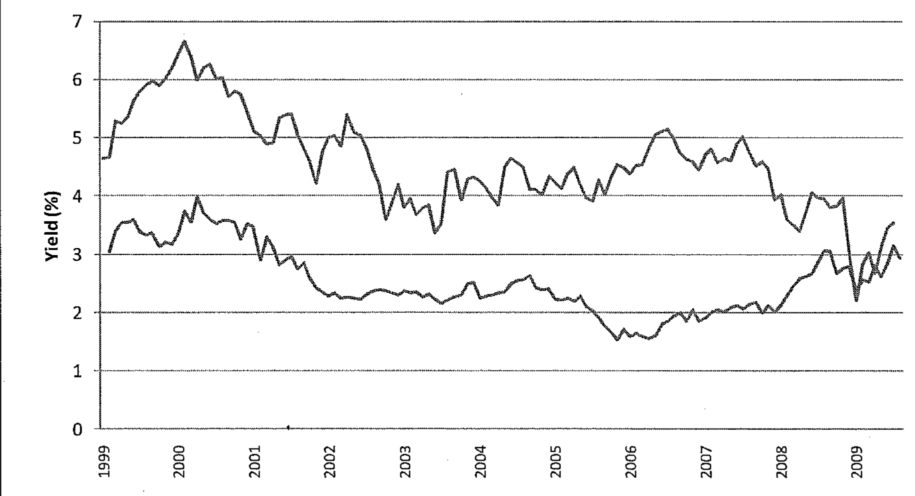
AWK offers a 4.2% dividend yield, with most companies under coverage offering dividends over 3%.

The industry offers an attractive dividend yield, with most companies under coverage offering dividends over 3% with a relatively consistent history of dividend growth. AWK offers the highest dividend yield under coverage at 4.2%. We expect dividend growth to continue, as most companies under coverage have a long history of dividend growth. The high dividend yield is also responsible for the industry's rather large retail investor base. Taking into account our cash flow projections, we find it reasonable to model continued dividend growth.



We note that water utilities' dividend yields were greater than the 10-year Treasury bond in January 2009. The spread is still near recent lows as the dividend yields 83% of the 10-year Treasury vs. a 56% historical average. A return to the historical average would imply a) water utilities cut their dividend—something most have not done in decades and an event we deem as unlikely given our 8-10% earnings growth projection over the next three years, b) the share prices of water utilities rise, or c) Treasury bond yields increase.

10 Year Treasury Yield vs. Water Utilities Dividend Yield



Source: Baseline and Moody's

AMERICAN WATER (AWK, BUY, $24/PT)—CAPEX TO DRIVE EARNINGS AND VALUATION DISCOUNT OVERDONE

We believe the RWE overhang is already priced into the stock and the discounted valuation by investors is overdone.

We are initiating coverage of American Water Works Company, Inc. (AWK) with a BUY rating and $24 target price, as we see AWK as offering an attractive risk/reward with positive catalysts relative to the peer group. We believe AWK shares are already discounting RWE's anticipated exit as the former parent company has announced plans to sell its remaining 46.6% stake in AWK by the end of the year. While the timing of this cannot be predicted, we believe AWK's discounted valuation by investors is overdone. The shares are trading at 13.5x our FY10E EPS, relative to a peer group average of 19.0x. We also believe there is also an opportunity for multiple expansion toward the peer group average of once the RWE overhang abates. However, our target price still incorporates a 16% discount to the peer group average.

We also like that AWK is investing heavily in capex, at an expected rate of $4.0-4.5B over the next five years, and is in a ROE recovery mode as the company plays catch up to the lower ROE earned from FY03-FY07. We see adjusted ROE improving to 9.3% in FY11E vs. 8.3% in FY08, putting it closer in line with the peer group average.

AWK valuations are attractive and the company is heavily investing in capex, which is the main driver of organic growth.

We are modeling 12.5% average EPS growth from FY09E to FY11E as we anticipate approximately $373M in rate relief during that time period solely from approved and pending rate cases. Additional rate cases that are expected to be filed in the remainder of FY09 and in the following years should further add to the company's earnings. Our EPS forecast is $1.31 for FY09E, $1.50 for FY10E and $1.67 for FY11E. Other notable positives for the company include an industry leading 4.3% dividend yield and the potential for further acquisitions as municipalities and smaller participants look to raise cash. The latter could offer a positive surprise, although we are not modeling for acquisitive growth. We derive a $28 fair value in our DDM, which could be conservative on expectations for a 5% long run EPS growth rate, 4% dividend growth and a 55% dividend payout ratio. AWK is also trading at 1.2x tangible BV which we believe is reasonable given the RWE overhang. Assuming this

Potential for acquisitions is prevalent, though we are not modeling for acquisitive growth.

is removed, there is a potential 40% upside to the stock value if the shares were to approach an industry and peer group average of 1.7x. Our $24 target price is based on 16.0x our FY10E EPS of $1.50. If the RWE overhang is removed, we argue that AWK should trade at least in line with the peer group P/E average of 19.0x. Our target price assumes a 16.0x forward P/E, a 16% discount to the peer group (12% to the coverage list), although we expect the discount to narrow once RWE sells its stake in the company.

CALIFORNIA WATER (CWT-BUY, $45 PT)—FAVORABLE REGULATORY ENVIRONMENT AND FAVORABLE VALUATION TO LEAD TO UPSIDE IN SHARES

Recent regulatory changes in California (WRAM and MBCA) should help reduce earnings volatility.

We are initiating coverage of California Water Service Group (CWT) with a BUY rating and $45 target price, which represents 20.5x our FY10E EPS of $2.20, in line with the company's historical average. We like CWT's position in the regulatory favorable California market. Further, with an approximate 10.2% ROE and a 51% equity/capital ratio (2Q end), we estimate for every $100M increase in net fixed assets, the company can increase its net income by $5.0M ($0.24/share). As such, CWT's $100M-120M in FY09E capex could potentially drive meaningful EPS growth in the next two-to-three years. On valuation, CWT shares are trading at 16.8x our FY10E EPS of $2.20, which we believe to be conservative when compared to the industry average of 19.0x and the company's historical average of 20.5x.

Additionally, while CWT has historically seen higher earnings volatility from variation in water consumption, recent regulatory changes in California (WRAM and MBCA implementation) should help reduce earnings volatility and provide better visibility. In summation, rate relief and improved ROE (we are modeling 10.8%) in FY09E, greater than the company's 8.9% five-year average, provide positive potential catalysts going forward.

AMERICAN STATES WATER (AWR-NEUTRAL)—FAIRLY VALUED BUT TIMING OF POSITIVE CATALYST DIFFICULT TO PREDICT

Recent regulatory changes in California (WRAM and MBCA) should help reduce earnings volatility.

We are initiating coverage of American States Water Company (AWR) with a NEUTRAL rating, as we see the upside potential related to rate relief as already largely reflected in the shares. At 17.5x our FY10E EPS of $1.91, AWR is trading at below its historical 20x forward P/E average and at a discount compared to the peer group average of 19x. While we argue that a valuation premium is justified given the company's concentration in the regulatory-favorable California market, given the company's valuation relative to our preferred names in the space – AWK and CWT – we do not see material upside potential at this time from current levels.

A principal driver of earnings growth would be the start-up of the Ft. Bragg, North Carolina construction project and successful price redeterminations at other military bases which we estimate could increase EPS by another 3%. However, due to limited visibility, we have not added these potential catalysts into our EPS forecasts. Our estimates do, however, include an average ROE of 9.8% from FY09E to FY11E vs. the company's historical 8.7% average. This is driven by increased capital spending of $75-80M in FY09, in line with FY08 levels. Since capex has grown at a CAGR of 12% from 2003-2008, AWR should see rate relief leading to 11.3% EPS growth in FY09E and potentially 10.1% in FY10E.

In the long term, we like AWR, currently the fourth largest publicly traded domestic water utility, as the WRAM/MBCA implementation in California should remove the quarterly earnings volatility caused by the changes in water consumption. We note that seasonal variation will still exist. These mechanisms have somewhat reduced the single-state operational risk that AWK faced previously. However, we believe benefits from the improved regulatory environment and earnings upside from recently approved rate cases are already mostly priced into the shares.

AQUA AMERICA (WTR, NEUTRAL)—HIGH QUALITY PROXY PLAY BUT RELATIVE UPSIDE REFLECTED IN THE SHARES

We see WTR as a proxy play on the water utility space, but it currently lacks upside potential.

We are initiating coverage of Aqua America, Inc. (WTR) with a NEUTRAL rating as we believe the shares are fairly valued on our expectations of 10.6% earnings growth over the next three years. However, we see downside risk to WTR as fairly limited as the company is trading at a 15% discount to its historical forward P/E of 23x. Additionally, at 2.2x price-to-book, it is a near full multiple point below its average 2.9x ratio (on book value of $7.91/share). Compared to the peer group, we see WTR's valuation as reasonable given the company's size and operational efficiency (O&M ratio is industry leading). We believe this justifies WTR as a proxy play on the water utilities space. However, despite the slight discount the shares are trading relative to historical averages, we see the potential upside relative to our preferred names of CWT and AWK as less attractive.

Despite three million customers in 13 states, WTR's operations are largely based in Pennsylvania.

Overall, we like WTR's position as one of the leading publicly traded water utility serving approximately three million people in 13 states. The water utilities industry is highly regulated, but also fragmented, which presents opportunities for acquisitive growth, especially as cash strapped municipalities and smaller private participants look to raise cash to weather the current economic downturn by potentially selling off water systems. More important, we expect 2009 and 2010 to be catch-up years for rate increases. $64.7M and $27.2M in rate increases were approved in 2008 and 2009 YTD, respectively, and $59.2M in increases are either pending or will be filed in the remainder of 2009. Additionally, WTR has surcharges in six of its 13 states of operations, which allows the company to start earning a return on its investment between rate increases. These factors, coupled with lower equity dilution from increased operating cash flow generation, should accelerate the pace of EPS growth in the next three years. We see WTR's estimated earnings growth of 11.3% from FY09E to FY11E outpacing the flat growth from FY05 to FY08.

RISKS

AWK

The potential downside risks to our investment thesis include, but are not limited to: 1) delays in rate case processing or lower rate increases by the regulators than our expectations, 2) 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, 4) a large acquisition at an excessive valuation (significantly above the rate base), and 5) a large goodwill impairment which could lead to a breach of debt covenants or regulatory requirements.

CWT

Potential downside risks to our investment thesis include, but are not limited to: 1) lower rate increase approvals by the California Public Utility Commission (CPUC) than our expectation, 2) near-term run-up in raw material costs, and 3) large acquisition(s) at excessive valuation(s) (significantly above the rate base).

AWR

The potential downside risks to our investment thesis include, but are not limited to: 1) lower rate increase approvals by the California Public Utility Commission (CPUC) than our expectation, 2) increases in raw material costs, and 3) an acquisition of a large water system by the local government through eminent domain.

The potential upside risks to our investment thesis include, but are not limited to: 1) favorable rate case approvals, and 2) the commencement of the large "special" construction project at Ft. Bragg, North Carolina, or any other base.

WTR

Potential downside risks to our investment thesis 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 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.

INDUSTRY OVERVIEW AND KEY THEMES

Monopoly of an Essential Commodity with High Barriers to Entry

Water utilities have been granted a monopoly; however, it does not result in extraordinary margins or earnings.

State Public Utility Commissions (PUCs) provide water utilities with a monopoly to provide water and wastewater services in their operating area. Though this does not translate to extraordinary margins and earnings, it guarantees a continued business and demand for what is truly an irreplaceable commodity. Additionally, due to the high cost of building new infrastructure and economies of scale gained through size of operation, we believe these high barriers to entry should keep competition low should the industry deregulate in the future.

Commodity Product with Similar Business Operation

Geographic positioning and the regulatory environment is an important aspect of a water utilities operation.

Regulated water utilities have, on the surface, a simple business operation. The utilities collect water from surface and groundwater sources and bulk-water suppliers, and treat it in compliance with EPA standards. Water is then distributed to residences, businesses, industries and other public consumers. In areas where the utilities operate wastewater systems, they collect wastewater from customer's premises through sewer lines and transport it to a treatment facility. The wastewater is then treated to meet required effluent standards before being released into the environment. The rates charged for the water and wastewater services are set by the regulators. The principal differentiator among publicly traded companies is based on geographic positioning and how favorable/unfavorable a local market is. Though some companies are more apt to grow via acquisitions (see WTR and AWK), this has historically been a "hit or miss" for earnings growth as new geographies bring a unique set of political hurdles to navigate.

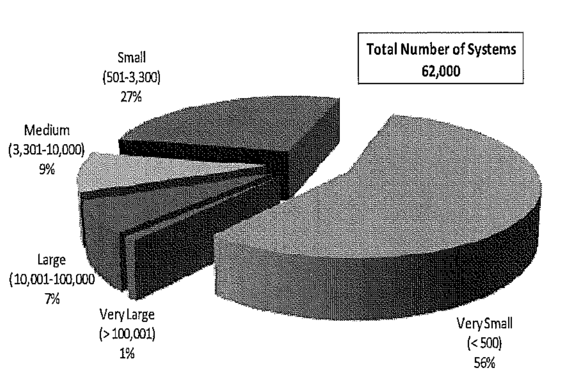
An Extremely Fragmented Industry

The industry is fragmented, offering potential for acquisitive growth.

The water and wastewater sector in the U.S. is extremely fragmented with approximately 52,000 water and 16,000 wastewater utilities. At the same time, a large number of water utilities are very small—83% of the systems serve less than 3,300 people, and only the largest 1% of the systems serve more than 10,000 people. The fragmentation and small size of most utilities have made the sector inefficient, due to lowered operating efficiency and difficulty in accessing capital markets and obtaining technological expertise.

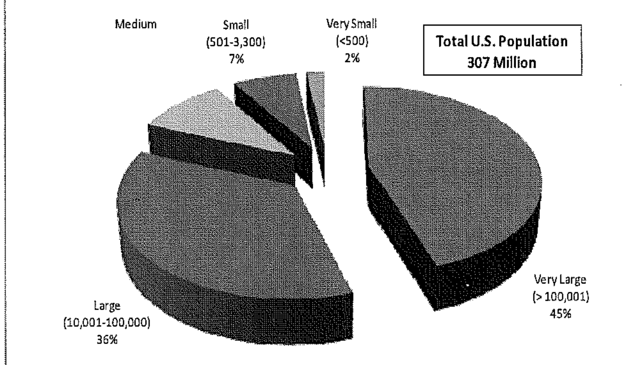
Moreover, approximately 84% of all water systems and 98% of all wastewater systems are municipally owned. However, many of the municipalities use private contractors for services ranging from complete operations and maintenance, to support functions such as billing, collections and lab testing services. Most of the remaining systems are privately owned with only 12 publicly traded water utilities; only a small fraction of the sector is served by the publicly traded companies. At the same time, the fragmentation presents an opportunity for larger utilities to grow through acquisitions.

Number of U.S. Water Systems by Size



Source: 2007 EPA Drinking Water Infrastructure Needs Survey and Assesment. Number in brackets are customers served.

U.S. Population Served by Water System Size



Source: 2007 EPA Drinking Water Infrastructure Needs Survey and Assesment. Number in brackets are customers served.

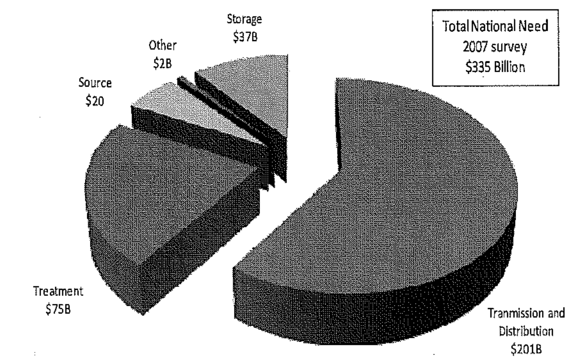
High Capex Needs Driven by Aging Infrastructure, Population Growth and More Stringent Regulations

Capex is the main driver of organic growth. The EPA estimates that $335B and $338B of investment is needed for water and wastewater infrastructure, respectively, over the next 20 years.

Due to under investment, a significant portion of water and wastewater infrastructure in the U.S. has aged beyond its intended life and requires very large investments for repair or replacement. According to the "2007 Drinking Water Infrastructure Needs Survey" by the EPA, approximately $335B is needed between 2007 and 2026 for the installation of new water infrastructure and the rehabilitation, expansion, or replacement of existing infrastructure. In addition, the EPA had estimated that approximately $388B will be needed between 2000 and 2019 for wastewater infrastructure. This compares to a total $10-12B in water supply spending annually over the past 10 years.

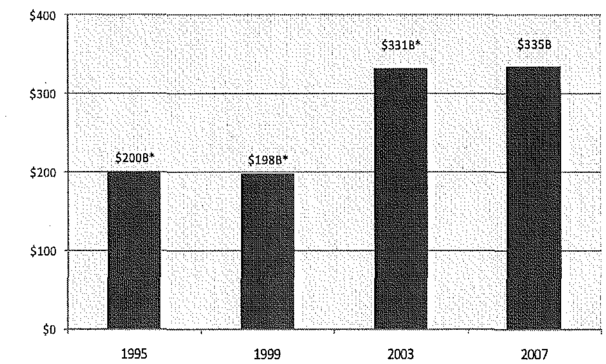
At the same time, the EPA and other regulatory bodies are implementing more stringent regulations that require additional infrastructure investment for compliance. These regulations include new mandates which are issued periodically to limit contaminants in drinking water and regulate the treatment and discharge of wastewater.

Total 20-Year Water Infrastructure Investment by Project Type -2007 EPA Survey



Source: 2007 EPA Drinking Water Infrastructure Needs Survey and Assesment.

Change in 20 -Year Water Infrastructure Investment Need in Four Successive EPA Surveys



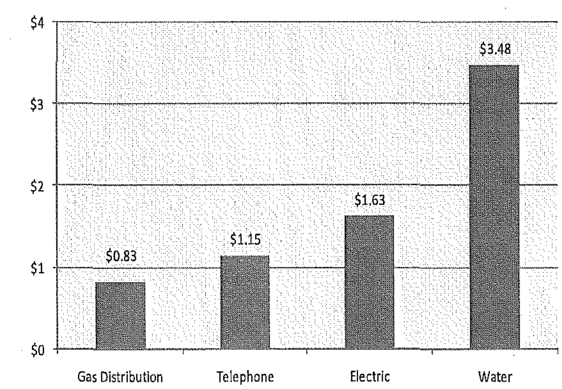
Source: 2007 EPA Drinking Water Infrastructure Needs Survey and Assesment.
* The amounts are reported in January 2007 Dollars

There is room to increase water rates to pay for infrastructure improvements.

In Spite of Large Capital Needs, Water and Wastewater Bills are Very Low

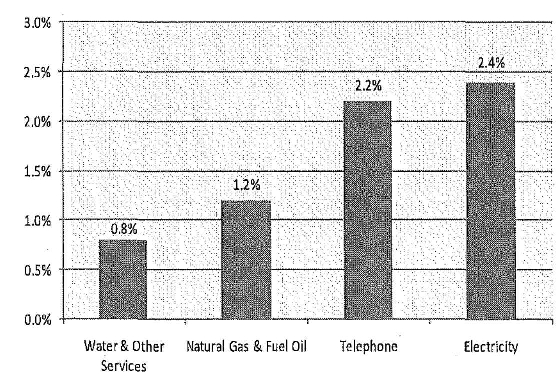
Water and wastewater services is very capital intensive businesses. According to a 2006 report by AUS, a public-utility consulting firm, $3.48 in capital investment is needed to generate every $1 in revenue for water and wastewater services vs. $0.83 for gas, $1.15 for telephone and $1.63 for electricity. At the same time, water and wastewater is the lowest utility bill paid by customers. In most parts of the U.S., it is still not much more than $1 per day, which is relatively low in comparison to other traditional utilities. This presents an opportunity for water utilities to increase rates to pay for large infrastructure spending needs as large (but gradual) percentage rate increases may not be opposed by paying customers.

Capital Invested per $1 of Revenue



Source: 2006 US Utility Reports.

% of Annual Household Budget



Source: 2004 Bureau of Labor Statistics; Assumes four person household.

Water infrastructure upgrades are ignored by politicians who would rather pave roads and build playgrounds.

Under-Charging and Inadequate Infrastructure Upgrades

Municipally owned systems often charge rates that are significantly below the economic cost of service provided, particularly if the replacement cost of infrastructure is considered. With a general perception of water being a free commodity, and community opposition to any rate increases, municipalities are unable to revise rates to keep pace with cost increases. As a result, they often have to subsidize water and wastewater services through taxes or other revenue sources. At the same time, local politicians often prefer to spend their limited budget on roads, schools and parks—which bring them recognition—instead of the underground "invisible" infrastructure needed for water and wastewater services.

A similar problem exists in small privately owned systems, which are often operationally inefficient and lack access to needed capital to make adequate infrastructure improvements.

Though publicly traded utilities have also historically under-invested in their infrastructure, they have greater operationally efficiency and have better access to capital through debt and equity markets.

Local Opposition and Regulatory Framework Preventing Consolidation

We anticipate an increase in consolidation over the course of the current economic downturn, as smaller private and cash-strapped municipalities struggle to make capital investments in their water systems and, in many cases, do not even meet the EPA mandates for water quality and wastewater treatment. So far, the pace of consolidation has been relatively slow due to local politics and the emotional attachment that communities have to their water systems. The opposition to rate increases—which will be needed to upgrade infrastructure in the event of an acquisition by a larger utility—is also a significant factor preventing consolidation.

Water and wastewater rates for privately owned systems are set by the regulators and depend on the rate base. Rate base is the total value of investment, net of depreciation, made by a utility operator in its system and is usually very close to the book value with some variations. Rates are set to allow the utility operator to recover a return on the rate base; regulators usually do not allow an acquirer to recover a return on any premium (goodwill) paid over the rate base. This prevents consolidation, as without a premium, there is little incentive for the current operator to sell the system. For smaller systems, we have seen acquisitions go for 1x the rate base, while on larger deals, 2-3x have been reported.

Pace of Consolidation MIGHT Pick Up Down the Road

Given the macro factors, we expect an increase in the pace of consolidation and public-private partnerships in the coming years.

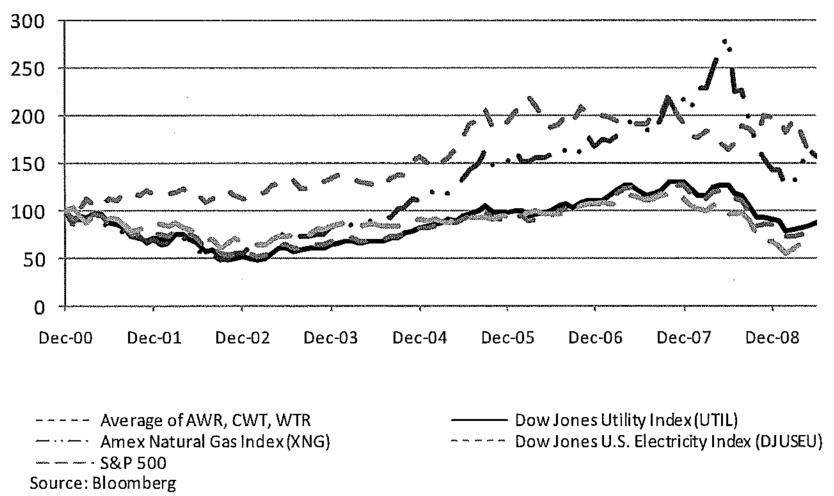
With inadequate infrastructure spending thus far, large investment will be needed at a later date to keep the water and wastewater systems running and in compliance with necessary regulations. With underfunded or constrained government budgets and limited access to capital markets, municipally owned systems are often unable to arrange for such large investments. The high level of fragmentation also makes smaller systems uneconomic and expensive to operate. The need for large investments and the desire to gain economies of scale are the main factors driving the municipalities to consider privatization or public-private partnerships for their systems. Many municipalities also consider privatization to reduce budget deficits and raise additional funds for other projects. Given the macro factors, we expect an increase in the pace of consolidation and public-private partnerships in the coming years.

Greater Share Price Returns than the Broader Market

Water utilities have offered greater returns than the broader indices over the past decade.

Overall, the water utilities names have offered greater returns than the broader indexes over the past decade. Although investors may be looking at cheaper cyclical stocks at this point in the cycle, we see broader economic trends suggesting that a return to normalized earnings may be two to three years away. As a result, we consider less-cyclical water utilities as a compelling investment opportunity, given current valuations relative to historical averages, and our conviction in 8-10% earnings growth over the next three years, which stems in large part from near-term rate relief.

Index of Comparative Returns 2000-2009



Source: Bloomberg

Water Demand

Water demand is the primary near-term revenue driver and is affected by customer growth and weather patterns.

Apart from acquisitions/divestitures and rate increases, water demand is the main short- and medium-term revenue driver for water utilities. It is important to note that any long-term change in demand due to the factors discussed below is considered by the PUCs during the rate setting process, and rates are adjusted to compensate for the change; if water demand declines, PUCs increase rates accordingly to compensate the utility. Though a fall in demand between rate cases leads to lost earnings for water utilities, and vice versa, in the long term the utilities are compensated for their investment irrespective of the water volume sold. However, an increase in customers from population growth is positive for the utilities since it serves as a platform for increasing capex, which in turn is the key revenue and earnings driver.

Water demand is affected by following factors:

Usage per-residential customer & customer growth. Due to more efficient appliances, declining family size, and general conservation (promoted by the EPA), there is a nationwide trend of a 1-2% annual decline in usage per-residential customer. However, population growth and new housing construction increases customer count. With these two opposing drivers, organic water demand either remains flat or declines in the low-single digits, on average, each year. We believe that population growth is a more significant driver of new water demand than new commercial or residential construction, which is down ~40% and 20%, respectively, this year.

Weather and precipitation. Weather and precipitation have the biggest impact on water demand, as more water is consumed by residential customers during warm and dry weather. This change of demand leads to volatility in revenue, some of which is predictable by historic weather trends, but a large part depends on the length and severity of each season. Conservation efforts in the event of a drought also lead to a decline in demand.

ECONOMIC REGULATION

Utilities are Allowed to Earn a Fixed Return on Equity (ROE) on Their Investment

Regulators must protect consumer interests, but also provide a reasonable operating environment for water utilities firms.

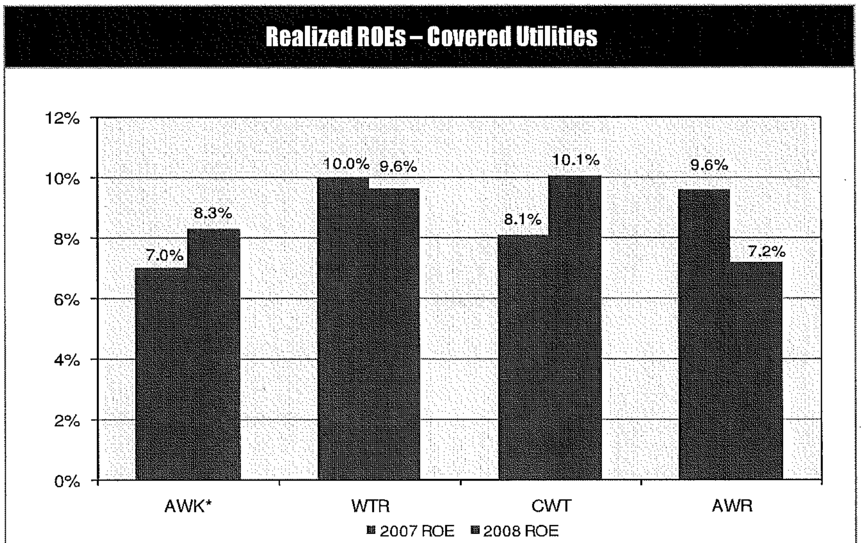
All privately owned and publicly traded water and wastewater utilities (utilities) are regulated by the state Public Utility Commissions (PUCs) in their respective states, with policies differing by state. A small number of operations are also regulated by the county or city governments. The regulators provide utilities a monopoly to operate in their area of service, and at the same time protect consumer interests by setting the rates that the utilities can charge for their service. The rates, which differ in each rate division, are established to allow the utilities to recover all their expenses, including operating cost, interest, depreciation, and taxes. The rates also allow the utilities to earn a fixed return on the equity (ROE) portion of their investment. The ROE is dependent on the current interest rate environment and can change over time, as it is calculated by adding a risk premium to the prevailing risk-free rate. Depending on the state, the allowed return is usually between 9% and 11%. However, due to the lag in rate increases, variations in consumption, and other factors, earning this allowed ROE is a constant uphill task for the utilities. The regulators also regulate capital structure (Equity/Capital, usually 45-50%), and approve infrastructure spending, accounting treatment, financing programs, merger and acquisitions and other significant financial activities.

Rate case filings are a complex and lengthy process which can take more than a year to be resolved.

With high capex, inflation in input costs, and other changes in expenses, the utilities continuously file for rate increases (called rate cases) with the regulators. Rate case filings are a complex and lengthy process which can take more than a year to be resolved. Historically, and partially to placate consumer advocates, regulators have approved only 55-75% of the requested rate increases. However, utilities have managed to work around this haircut by adjusting their initial rate case filings accordingly.

Realized ROE is Often Lower than the Allowed ROE

The water utilities sector is characterized by high capex and constant input cost inflation. At the same time, utilities have to invest capital upfront before requesting for a rate increase, and several state PUCs use historical costs (called the historical test year) to set rates, as opposed to a forward looking test year. As a result, water utilities are often unable to earn the allowed ROE. A utility's ability to earn the allowed ROE depends on regulatory policies and environment, and also on the utility's effectiveness in filing rate cases. It is easier to earn the allowed ROE in states that have a favorable regulatory environment through rate mechanisms which reduce the regulatory lag (delay in obtaining rate increases for capex, decline in water sales volume, and increase in operating expenses).



*Source: Company Information. *Excludes Goodwill & Goodwill Impairment*

Realized ROE can be lower than the allowed ROE for several reasons, including:

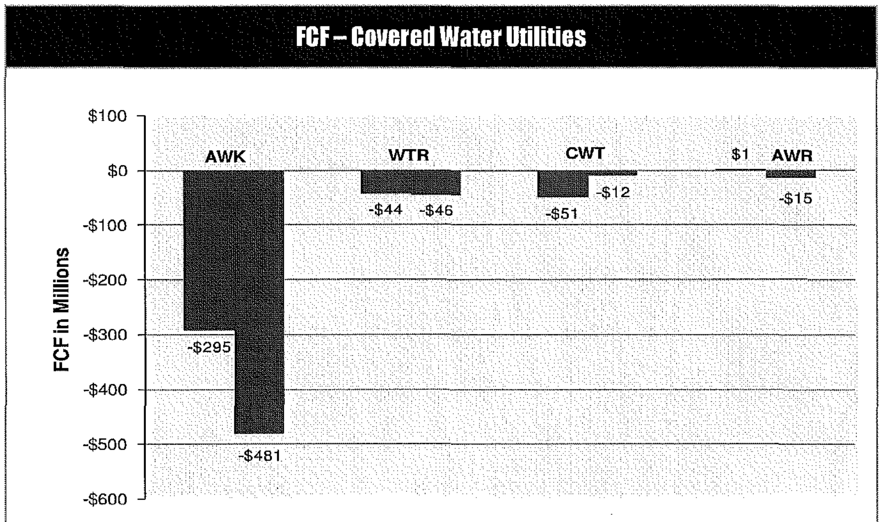
- Regulatory lag—an increase in O&M expenses, interest and taxes not yet recovered in rates or a gap between the time that a capital project is completed and the start of its cost recovery in rates.
- A fall in water consumption due to weather fluctuation, conservation efforts or other factors. Rate case filing uses an assumption of normalized consumption to determine water rates. Any fall in consumption results in a decrease in operating revenues without a corresponding decrease in O&M expenses.
- Equity investment recognized by PUCs is sometimes lower than the book value.
- Some expenses, such as charitable donations, are not reimbursed.

Large acquisitions often lead to lowered ROE as utilities struggle to win timely rate increases from the regulators. As is often the case, acquired water systems may not meet service standards and require large immediate capex to repair the infrastructure. Due to its size, the capex then works its way into rate increases over time—regulators either deny any rate increases until service standards are met or stagger rate increases over multiple years to shield customers. However, we see FY09-FY11 as a period of renewed earnings growth, as we believe announced and projected rate relief, as well as a progressively more favorable regulatory environment, helps our covered names catch up to the maximum allowed ROE. We note that over the last two to three years these companies have usually not been able to earn their allowed ROE.

Capex is the Key EPS Growth Driver

Investing in infrastructure is the main driver of organic EPS growth.

Rate increases only adjust revenue for inflation and changes in other expenses. The only way for a regulated water utility to increase EPS organically is to invest in capex and earn a return on the equity portion of the investment. Given the poor state of infrastructure, all large publicly traded water utilities have maintained a large capex program. This in turn has made them free cash flow (FCF) negative. We expect trend this to continue in the foreseeable future, as the utilities upgrade their own infrastructure and also that of systems which they acquire from time to time.



Source: Company Information

PUCs are hesitant to increase rates, thus limiting the amount of infrastructure investment made each year.

The amount of capex that a utility can make in a given year is driven by infrastructure needs, but is limited by the rate increase that the PUCs are willing to approve in the next rate cycle. Despite recognizing the need for large infrastructure investment, PUCs are apprehensive about approving large rate increases in a short span of time due to community opposition. In most states, utilities also have to absorb the cost of lag between making the investment and getting approval for rate increases to earn a return on that investment. To reduce this lag, the utilities try to time their investment around the rate case cycles and limit their investment to the corresponding rate increase that the PUCs might be willing to approve.

Regulators are Moving Towards Policies That Encourage Investment

Favorable regulatory environments encourage infrastructure investment and reduce regulatory lag in getting rate increases.

Recognizing the need for increased infrastructure spending and other difficulties faced by utilities, regulators are moving towards policies that encourage investment and reduce regulatory lag in getting rate increases. These policies differ by state, with some states being more progressive than others in adopting these policies. Some of these policies are discussed below.

Improvement in rate setting process:

- Use of a forecast test year to set rates instead of using historical cost, which is the usual practice. With a forecast test year, expenses are increased for inflation and other inputs are adjusted to calculate the rate.
- Full or partial single state tariff, which reduces administrative costs and complexity of filing separate rate case for each system within a state and also distributes the fluctuation in local costs.

Increased rates/surcharges between rate case filings:

- Recovering a return on utility plant while it is still under construction.
- Infrastructure investment surcharge, (named the Distribution Systems Improvement Charge [DSIC] in PA), which reduces the lag in recovering a return on the investment.

- Surcharge for increase in certain expenses beyond the utility's control, such as purchased water and power costs, and property taxes.

We offer a list of state-wide alternative revenue mechanisms below.

State	Covered Utilities Operating & 2008 Revenue (in $ million)	Infrastructure Investment Surcharge	Forward Looking Test Year	Updating Historical Data	Single Tariff Structure	Return on Utility Plant Before Service
AZ	AWK			☆		
CA	AWK -$129 AWR - $248 CWT - ~$387	☆	☆			☆
FL	WTR - $17					
GA	AWK					
HI	AWK CWT - ~$3		☆			
IA	AWK			☆		
IL	AWK - $188 WTR - $41	☆	☆			
IN	AWK - $156 WTR - $17	☆				
KY	AWK		☆		☆	☆
MD	AWK			☆		
ME	WTR - $10					
MI	AWK					
MO	AWK - $181 WTR	☆		☆		
MS						
NC	WTR - $35					
NJ	AWK - $518 WTR - $29			☆	☆	
NM	AWK CWT - ~$6			☆		
NY	AWK WTR - $27	☆	☆		☆	
OH	AWK WTR - $42	☆	☆			☆
PA	AWK - $448 WTR - $331	☆	☆		☆	☆
SC	WTR					
TN	AWK		☆			
TX	AWK WTR - $51			☆		☆
VA	AWK WTR - $12			☆		☆
WA	CWT - ~$13					
WV	AWK - $116			☆	☆	

Source: Company reports and Longbow Research estimates.

ECONOMIC REGULATION – CALIFORNIA

As previously mentioned, specific policies used for economic regulation vary by state. California is the most progressive in adopting policies that have reduced operation risk for utilities operating in the state, and have created an environment that is conducive to infrastructure investment.

California is the most progressive in adopting policies that have reduced operation risk for utilities operating in the state

The California Public Utilities Commission (CPUC) policies that make California progressive include:

- If the CPUC decision on a rate case is delayed beyond the effective date, utilities are allowed to implement an **interim rate increase** based on the last 12-month change in the Consumer Price Index (CPI). Once the delayed rate case is approved, utilities can **recover the revenue lost** (difference between final and interim rate increase) due to the delay over a 12-month period.
- Unlike most of other states, where utilities file rate cases at will, CPUC requires utilities to file rate cases every three years and allows rate escalations in the second and third year of the cycle.
- CPUC uses a forward test year (expense are forecasted for setting rates).
- CPUC is adopting a new procedure that will allow single rate filing for all rate divisions in the state (starting 2011 for CWT and 2013 for AWR).
- CPUC has recently allowed mechanisms—the Water Recovery Adjustment Mechanism (WRAM) and Modified Cost Balancing Account (MCBA)—that reduce earnings volatility, and eliminate the possibility of lost earnings due to lower water demand or increases in water production costs.
- Utilities can file **offset filings** between GRCs, which adjust rates for (i) construction projects approved in the GRC when the plant is placed in service and (ii) a change in production costs (purchased water, purchased power, and pump taxes).

SENSITIVITY ANALYSIS

We offer the following sensitivity analysis that compares the companies under our coverage universe and potential EPS benefit from a 10bp improvement in ROE on planned FY09 capex. We conclude that CWT has the greatest potential upside given its high equity to capital ratio. However, the company is also stretched relative to the peer group, given that it is returning an ROE close to the maximum allowable of 10.2% in California (95% of revenues).

WATER UTILITIES SURVEY

Survey Background

We recently initiated a survey of 16 public utility commissioners, staff and general managers of water utility systems, in order to gauge their sentiment regarding privatization and the need for infrastructure repair, as well as their thoughts on the likelihood of future M&A activity. The survey was completed in states where our covered water utility companies have major operations. Municipally run water systems are owned entirely by the city they operate in, and can greatly vary in size. The smallest municipally run systems might serve only hundreds of customers in small towns, whereas the largest municipally run systems might serve hundreds of thousands of customers in major metropolitan cities. Municipally run systems, no matter their size, report to their local city council, whereas private water utility companies must report to the public utility commissions of their respective states.

Summary

We have recently completed our water utilities survey for the third quarter (July-August) and offer the following takeaways:

- Contacts overwhelmingly agree that the pace of sell-off of small water systems and public/private partnerships should accelerate. Furthermore, larger municipally owned systems should continue to operate independently because of their efficiency and the financial stability they create for their city of operation. This suggests that sale of large water systems (greater than 100,000 customers) will be unlikely in the near term.
- Contacts indicate that those small systems that look to sell their assets to private firms, will have to do so at values less than their book value because of the future capex needed for infrastructure improvement. "Municipalities are not reinvesting the money they make, they are reinvesting it in the other parts of the city, like parks or filling potholes. Now that significant capital expenditures are coming up, these municipalities will not have the funds needed to make necessary improvements and will need to sell their systems to larger companies," suggested the deputy to a Pennsylvania commissioner. Furthermore, contacts indicate that the current economic downturn and lack of funding for infrastructure repair weigh heavily on a municipality's willingness to sell its system. Valuations, therefore, could be attractive.
- Contacts indicate an overwhelming need for spending for infrastructure modernization and improvement, as well as a lack of resources available to roll out such improvements. A contact in California suggested, "Smaller municipalities do not have the resources for expansion or modernization of their systems, which adversely affects their customer base. Private companies have the resources and are better able to handle infrastructure modernization." We believe the regulatory environment supporting large capital improvement projects will continue and that publicly traded companies will be incentivized to participate.
- Contacts agree larger companies are able to better provide services to their customers, as well as make necessary improvements in their infrastructure. The manager of a municipally run system in California suggests, "There has been talk in my local municipal district to sell off our assets to a larger firm, simply because they can do a better job, not because we need the money." The belief that a private company can better service its customers, coupled with massive capex needs in the coming years, indicates that small municipalities are willing to sell their assets off to a private company.

Other Notable Quotes

"Education is the big thing. Most people don't realize what goes in to our water infrastructure and the costs associated with it. Water is a commodity—going forward I think we will see it being treated more in that manner." – Commissioner's Deputy, Missouri

"The advantage to privatization is that elected officials and officials like me are subject to pressure from the voters, who are also their customers. Private firms are not under the same constraint, which means they can make rational business decisions that are in their best interest and also in the best interest of their customers." – Member under the Commission Chairman, Florida

"The private firms are run very well and are extremely efficient in the services they provide. They understand the needs of their customers and are very well suited to navigate each state's regulatory environment. I like how they operate." – Director of Utility Rates and Services, New York

"Going forward, private firms will play a far greater role in providing water utility services to the American people." – Director of Industry and Governmental Relations, New York

"Municipal budgets are tight as revenue is down—they are struggling, so they are trying to cut down and get out of certain places they don't need to be." – Superintendent, Municipal System in New York

WATER INDUSTRY PEER VALUATION

($ in millions, except per share data)

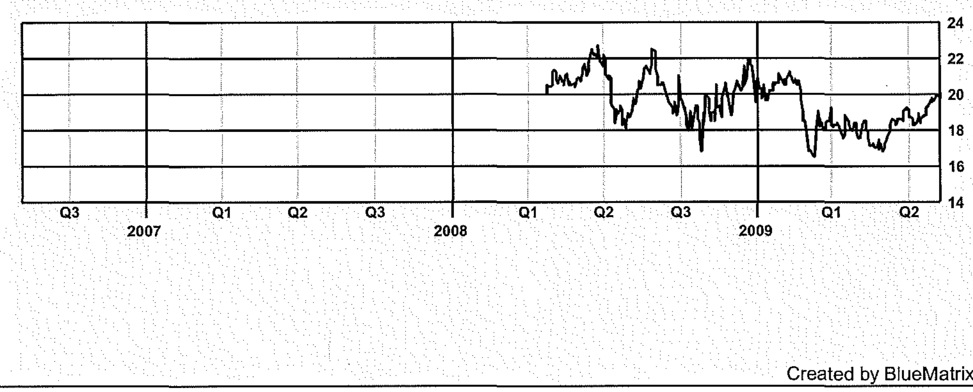
							52 Week				Earnings per Share			P/E		Dividend	Price/
Company	Ticker	FY End	Rating	Target	% Upside	Share Price	Hi	Lo	Mkt Cap	Revenue FY End	Last FY	Current FY	Next FY	Current FY	Next FY	Rate	Book
U.S. WATER UTILITIES																	
American Water Works	AWK	Dec.	BUY	$24	20%	$ 20.13	$23.12	$16.22	$ 3,514	$ 2,337	1.17	1.31	1.50	15.4x	13.5x	4.2%	0.8x
Aqua America	WTR	Dec.	Neutral			$ 17.55	$22.00	$12.20	$ 2,381	$ 627	0.73	0.82	0.91	21.4x	19.4x	3.3%	2.6x
American States Water	AWR	Dec.	Neutral			$ 33.41	$42.00	$27.00	$ 612	$ 319	1.56	1.74	1.91	19.2x	17.5x	3.0%	1.8x
California Water Service Group	CWT	Dec.	BUY	$45	22%	$ 36.97	$48.28	$27.68	$ 767	$ 410	1.90	2.12	2.20	17.4x	16.8x	3.2%	2.4x
Southwest Water Company	SWWC	Dec.	NR			$ 4.49	$13.40	$2.67	$ 112	$ 222	-0.19	*0.2*	*0.44*	22.5x	10.2x	2.2%	0.7x
Artesian Resources Corporation	ARTNA	Dec	NR			$ 16.79	$18.50	$12.81	$ 122	$ 56	0.86	*0.97*	*1.04*	17.3x	16.1x	4.3%	1.3x
Consolidated Water Co	CWCO	Dec	NR			$ 17.41	$23.91	$6.35	$ 253	$ 60	0.50	*0.69*	*0.86*	25.2x	20.2x	1.5%	1.5x
Connecticut Water Service	CTWS	Dec	NR			$ 21.30	$28.95	$17.31	$ 181	$ 61	1.12	*0.95*	*0.96*	22.4x	22.2x	4.2%	1.9x
Middlesex Water Company	MSEX	Dec	NR			$ 15.27	$18.52	$11.64	$ 205	$ 91	0.90	*0.76*	*0.79*	20.1x	19.3x	4.6%	1.7x
Pennichuck Corporation	PNNW	Dec	NR			$ 23.18	$24.80	$14.75	$ 99	$ 31	0.57	*0.63*	*0.79*	36.8x	29.3x	3.0%	1.8x
York Water Company	YORW	Dec	NR			$ 16.56	$17.95	$6.22	$ 189	$ 33	0.57	*0.65*	*0.68*	25.5x	24.4x	3.0%	2.0x
U.S. Water Utility Average														22.1x	19.0x	3.3%	1.7x
EQUIPMENT/FILTRATION/TREATMENT SECTOR																	
Calgon Carbon Corp.	CCC	Dec.	NR			$ 13.12	$23.03	$9.11	$ 718	$ 400	0.56	*0.56*	*0.81*	23.5x	16.2x	0.0%	3.3x
Danaher	DHR	Dec.	NR			$ 61.70	$85.00	$47.20	$ 19,667	$ 12,697	4.23	*3.37*	*3.59*	18.3x	17.2x	0.2%	1.8x
ITT Technologies	ITT	Dec.	NR			$ 49.40	$68.24	$31.94	$ 8,991	$ 11,695	4.04	*3.63*	*3.77*	13.6x	13.1x	1.7%	2.7x
Layne Christensen	LAYN	Jan.	NR			$ 24.17	$58.26	$10.36	$ 470	$ 1,008	2.20	*0.47*	*0.96*	51.6x	25.3x	0.0%	0.7x
Mueller Water Products	MWA	Sept	NR			$ 3.92	$12.71	$1.48	$ 453	$ 1,859	0.46	*(0.26)*	-	-	46.7x	1.8%	0.8x
Nalco	NLC	Dec.	NR			$ 17.58	$25.90	$7.80	$ 2,429	$ 4,212	1.30	*0.83*	*1.17*	21.2x	15.0x	0.8%	4.0x
Pall Corp.	PLL	Jul.	NR			$ 31.17	$42.72	$18.20	$ 3,676	$ 2,572	1.94	*1.72*	*1.95*	18.3x	16.8x	1.9%	4.3x
Pentair	PNR	Dec.	NR			$ 27.61	$41.00	$17.23	$ 2,714	$ 3,382	2.17	*1.42*	*1.7*	19.5x	16.3x	2.6%	1.2x
Watts Water Technologies	WTS	Dec.	NR			$ 28.29	$33.00	$15.85	$ 1,036	$ 1,459	1.83	*1.31*	*1.45*	21.6x	19.5x	1.6%	1.1x
Equipment/Filtration/Treatment Average (*ex BWTR and CCC)														23.5x	20.7x	1.2%	2.2x
WATER RESOURCES/ INFRASTRUCTURE																	
Insituform Technologies	INSU		NR			$ 19.28	$21.28	$9.26	$ 749	$ 537	0.77	*0.98*	*1.12*	19.6x	17.2x	0.0%	1.5x
Lindsay Manufacturing	LNN		NR			$ 40.92	$97.80	$20.89	$ 504	$ 475	3.11	*1.05*	-	32.3x	29.0x	0.8%	5.1x
Tetra Tech	TTEK		NR			$ 30.06	$30.90	$14.20	$ 1,810	$ 2,145	1.02	*1.24*	*1.42*	21.9x	22.0x	0.0%	2.8x
Water Resources/ Infrastructure Average														24.6x	22.7x	0.3%	3.1x
Relevant Indices						**Share Price**											
Dow Jones Industrials	DJ30					$ 9,370.07											
S&P 500	SPX					$ 1,010.48											
Nasdaq Composite	NDX					$ 1,619.49											

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.

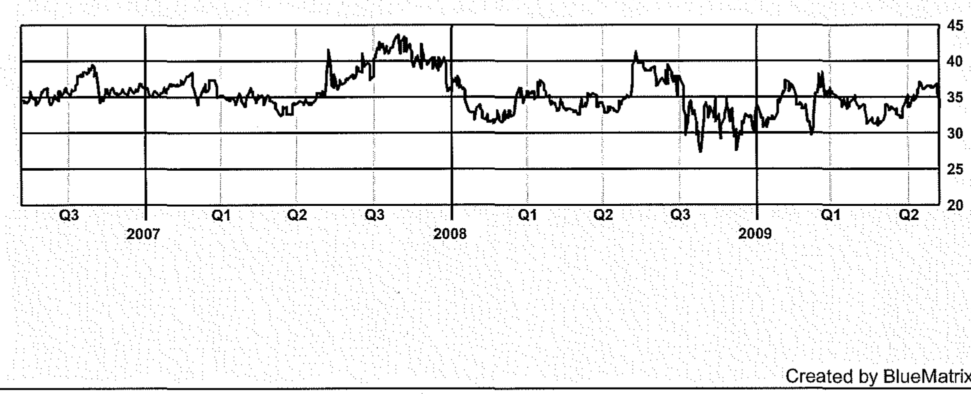
G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

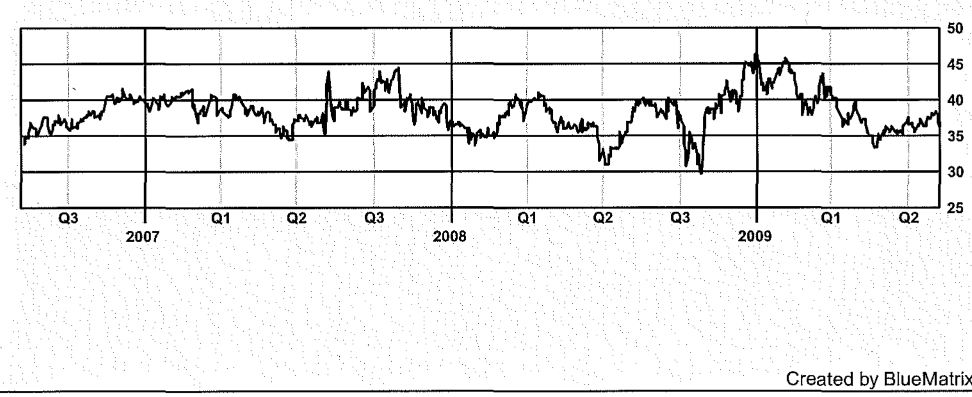
Rating and Price Target History for: American Water Works Company, Inc. (AWK) as of 08-07-2009



Rating and Price Target History for: American States Water Company (AWR) as of 08-07-2009

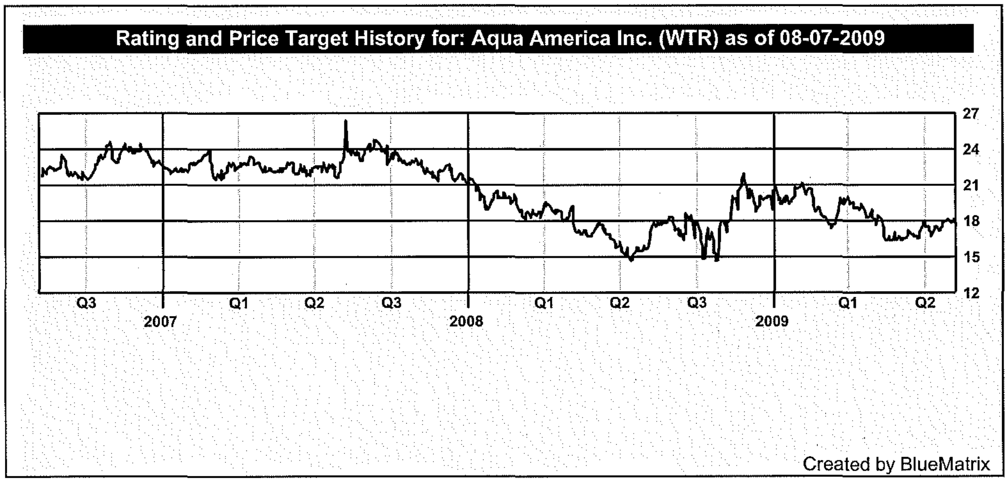


Rating and Price Target History for: California Water Service Group (CWT) as of 08-07-2009



G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469



APPENDIX

IMPORTANT DISCLOSURES

REGULATION ANALYST CERTIFICATION ("REG AC"): The Research Analyst(s) who prepared this research report hereby certifies that the views expressed in the research report accurately reflect the analyst(s) personal views about the subject companies and their securities. The Research Analyst(s) also certifies that the Analyst(s) have not been, are not, and will not be receiving direct or indirect compensation for expressing the specific recommendation(s) or view(s) in this report.

GENERAL DISCLOSURES: Longbow Securities does not make a market in any securities, nor does it hold a principal position in any security. However, any officer, director or stockholder of Longbow Securities or any member of their families may have a position in and may from time to time purchase or sell any of the securities mentioned or any related securities. Security prices in this report may either reflect the previous day's closing price or an intraday price, depending on the time of distribution. Consensus estimates are derived from either Thomson/Reuters, Bloomberg or Baseline. Designated trademarks and brands are the property of their respective owners.

SPECIFIC DISCLOSURES:

- Longbow Securities does not make a market in any securities, nor does it hold a principal position in any security.
- No officer, principal, employee, or owner of Longbow Securities owns options, rights, or warrants to purchase the subject security or any other security mentioned in this report.
- No employee of Longbow Securities serves on the Board of Directors of the subject security or any other security mentioned in this report.
- Neither the Research Analyst nor a member of the Research Analyst's household has a financial interest in the securities of the subject company or any other security mentioned in this report.
- Neither the Research Analyst nor a member of the Research Analyst's household serves on the Board of Directors of the subject company or any other security mentioned in this report.

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

- Neither Longbow Securities nor its affiliates beneficially own 1% or more of an equity security of the subject company or any other security mentioned in this report.

RATINGS DISTRIBUTIONS FOR LONGBOW RESEARCH:

Rating Category	Count	Percent
Buy	46	23.4%
Neutral	144	73.1%
Sell	7	3.6%

RATING SYSTEM:

"Buy" means that Longbow Securities expects total return to exceed 20% over a 12-month period.

"Neutral" means that Longbow Securities expects total return to be within a range of plus or minus 20% over a 12-month period.

"Sell" means that Longbow Securities expects total return to be negative by greater than 20% over a 12-month period.

Longbow Research's full research universe and related applicable disclosures can be obtained by calling (216) 986-0700 or via postal mail at: Editorial Department, Longbow Research, 6000 Lombardo Center, Suite #500, Independence, Ohio 44131.

DISCLAIMER: The information, opinions, estimates and projections contained in this report were prepared by Longbow Securities LLC, a wholly owned subsidiary of Longbow Research LLC, and constitute the current judgment of Longbow Securities as of the date of this report. Additional information may be available from Longbow Securities upon request. The information contained herein is believed to be reliable and has been obtained from sources believed to be reliable, but Longbow Securities makes no representation or warranty, either expressed or implied, as to the accuracy, completeness or reliability of such information. Longbow Securities does not undertake, and has no duty, to advise you as to any information that comes to its attention after the date of this report or any changes in its opinion, estimates or projections. Prices and availability of securities are also subject to change without notice. By accepting this report, the reader acknowledges that the report does not purport to meet the objectives or needs of specific investors, and, accordingly, constitutes only "impersonal advisory services" as that term is defined in Rule 204-3 under the Investment Advisers Act of 1940 and that any advice in this report is furnished solely through uniform publications distributed to subscribers thereto within the meaning of Section 2(a)(20)(i) of the Investment Company Act of 1940. The securities discussed in Longbow Research reports may be unsuitable for some investors depending on their specific investment objectives, financial status, risk profile, or particular needs. Investors should consider this report as only a single factor in making their investment decisions and should not rely entirely on this report in evaluating whether or not to buy or sell the securities of the subject company. Longbow Research archives and reviews outgoing and incoming email. Such may be produced at the request of regulators. Sender accepts no liability for any errors or omissions arising as a result of transmission. Use by other than intended recipients is prohibited.

DESCRIPTION: Longbow Securities LLC, a wholly owned subsidiary of Longbow Research LLC, is a primary research provider established in 2003 and headquartered at 6000 Lombardo Center, Suite 500, Independence, Ohio 44131 USA. The company provides research services to

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

LONGBOW Research
Tactical advantage through independent research

Company Update

August 12, 2009 | **AMERICAN WATER WORKS COMPANY, INC. (AWK)**

Rating:	**BUY**	
Current Price:	**$20.22**	
Target Price:	**$24.00**	

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

Industry: Water Utilities **Fiscal Year: Dec**			**1Q09A**	**2Q09A**	**3Q09E**	**4Q09E**	**FY09E**	**Valuation Multiple**	**FY10E**	**Valuation Multiple**
Market Cap ($MM):	3,302	**EPS:**	$0.19	$0.32	$0.56	$0.25	$1.31	15.4x	$1.50	13.5x
Net Debt ($MM):	4,972	Consensus:			$0.56	$0.27	$1.32	15.3x	$1.46	13.8x
Enterprise Value ($MM):	8,274	Last Year:	$0.11	$0.28	$0.55	$0.23	$1.17			
Shares - FD (MM):	163.3									
		EBITDA:	$1.15	$1.40	$1.74	$1.23	$5.53	9.2x	$5.83	8.7x
Dividend:	$0.84	Growth:	28%	10%	8%	7%	12%		12%	
Yield:	4.2%									
Beta:	0.45	**Revenue:**	$550	$613	$711	$609	$2,483	3.3x	$2,684	3.1x
Rel. P/E (FY2009E):	82%	Growth:	9%	4%	6%	7%	140%		8%	

AWK: Secondary Offering to Remove a Large Portion of the RWE Overhang

SUMMARY

- Last night, AWK announced that its former parent company, RWE, will be selling 30M shares, bringing its ownership down to ~30% of the company vs. ~46% currently (excluding a 4.5M overallotment). We view this as a positive step for AWK going forward as we believe the expectation of a large number of shares coming to the market in the near future has had a negative impact on the stock's valuation. We anticipate that AWK's discounted valuation relative to the industry average should ease as the "RWE overhang" is removed.

- As a reminder, RWE acquired AWK in 2003, but announced plans to divest the company in 2005 after facing difficulty in navigating the complex regulatory environment in the U.S. RWE finally sold 40% of its stake in AWK with an initial offering in April 2008, and 11% through a secondary offering in June 2009.

- To catch up from five years of underinvestment by RWE, AWK is now spending heavily on capex with $4-4.5B anticipated over the course of the next five years. We anticipate this to drive earnings growth over that time period.

- Assuming approximately 8.6% FY09E adjusted ROE and a 43% equity/capital ratio, we estimate an $800M capex budget for both FY09E and FY10E to increase AWK's EPS by $0.18/share annually once rates catch up to investment.

- We forecast adjusted EPS of $1.31 in FY09, $1.50 in FY10 and $1.67 in FY11 based on revenue growth assumptions of 6.2%, 8.1% and 7.4%, respectively. We are reiterating our BUY rating and $24 target price.

Investment Thesis

We continue to rate AWK shares BUY with a $24 target price, as we see AWK as offering an attractive risk/reward with positive catalysts relative to the peer group. We believe AWK shares are discounting RWE's anticipated exit as the former parent company has announced plans to sell its remaining stake in AWK. While the timing of this cannot be predicted, we believe AWK's discounted valuation by investors is overdone. Last, yesterday's news of RWE's 30M share secondary offering, while viewed as a near-term negative for the share price, should be a medium-term positive once some of the "RWE overhang" concern is removed. AWK shares are trading at 13.5x our FY10E EPS, relative to a peer group average of 18.9x. We also believe there is an opportunity for multiple expansion toward the peer group average once the RWE overhang abates. However, our target price still incorporates a 13% discount to the peer group average.

Valuation

AWK shares closed yesterday at $20.22, which is 15.4x our FY09E EPS of $1.31 and 13.5x our FY10E EPS of $1.50. The shares are trading at a discount to the peer group average of 18.9x FY10E EPS likely due in large part to the RWE overhang, which we believe the Street is already accounting for. The shares are trading at 1.2x tangible book value compared to a peer group that trades over 1.5x, on average. Our target price of $24 is based on 16.0x our FY10E EPS, a valuation that remains at a discount to the peer group. However, we see multiple expansion from current levels as justified given that AWK is currently viewed as the largest and most diversified publicly traded water utility in the U.S. and with the potential for earnings growth as the company catches up to insufficient rate increases during the past five-to-six years.

Risks

The potential downside risks to our investment thesis include, but are not limited to: 1) delays in rate case processing or lower rate increases by the regulators than our expectations, 2) 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, 4) a large acquisition at an excessive valuation (significantly above the rate base), and 5) a large goodwill impairment which could lead to a potential breach of debt covenants or regulatory requirements.

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

American Water Works— Quarterly Income Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09E	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E
Regulated Segment	419.3	508.6	571.9	487.8	449.9	527.1	603.7	502.1	497.4	554.9	646.7	547.0	524.2	605.7	700.4	592.3
% Increase			7.3%	11.2%	7.3%	3.6%	5.6%	2.9%	10.6%	5.3%	7.1%	8.9%	5.4%	9.2%	8.3%	8.3%
Non-Regulated Revenue	53.3	55.5	66.4	67.5	61.0	67.0	73.9	70.3	57.5	64.2	70.9	67.3	63.3	70.6	78.0	74.1
% Increase			0.4%	27.7%	14.4%	20.8%	9.4%	4.1%	-5.7%	-4.2%	-4.1%	-4.3%	10.0%	10.0%	10.0%	10.0%
Other	(4.0)	(5.4)	(5.1)	(1.5)	(4.1)	(4.7)	(5.4)	(3.9)	(4.7)	(6.3)	(6.5)	(5.5)	(5.2)	(6.1)	(7.0)	(5.9)
% Regulated Rev	-1.0%	-1.1%	-0.9%	-0.3%	-0.9%	-0.9%	-0.9%	-0.8%	-1.0%	-1.1%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%
Operating revenues	**468.5**	**558.7**	**633.1**	**553.8**	**506.8**	**589.4**	**672.2**	**568.6**	**550.2**	**612.7**	**711.1**	**608.8**	**582.3**	**670.3**	**771.4**	**660.4**
Operation and maintenance	282.6	299.4	328.3	336.2	311.3	330.6	342.2	319.8	314.4	330.6	359.1	344.1	329.0	361.9	382.9	359.6
Depreciation and amortization	64.6	68.1	69.7	64.9	63.9	67.3	68.4	71.6	68.8	73.2	73.2	73.2	74.8	76.3	77.9	79.5
General taxes	47.9	45.9	47.1	42.3	52.1	49.6	49.4	48.0	52.5	51.7	49.3	50.6	54.5	52.0	52.0	50.6
Loss (gain) on sale of assets	0.1	(6.2)	(0.7)	(0.5)	(0.1)	(0.8)	0.5	(0.0)	(0.2)	0.0	(0.3)	(0.3)	(0.3)	(0.3)	(0.3)	(0.3)
Impairment charges			243.3	266.0	750.0				450.0							
EBIT	**73.3**	**151.5**	**(54.6)**	**(155.1)**	**(670.4)**	**142.7**	**211.8**	**129.1**	**(335.4)**	**157.2**	**229.7**	**141.3**	**124.3**	**180.3**	**258.9**	**171.0**
Operating Margin (excluding impairment)	*16%*	*27%*	*30%*	*20%*	*16%*	*24%*	*32%*	*23%*	*21%*	*26%*	*32%*	*23%*	*21%*	*27%*	*34%*	*26%*
Interest	72.2	70.8	68.739	71.5	70.0	70.1	72.7	72.4	72.0	73.7	74.4	75.2	76.2	77.2	78.2	79.2
Other income, net	(3.0)	(1.9)	(2.9)	(4.6)	(3.7)	(3.1)	(6.7)	(8.0)	(4.8)	(2.6)	(5.5)	(5.2)	(4.6)	(4.5)	(5.0)	(4.8)
Total other income (deductions)	**69.2**	**68.9**	**65.8**	**66.8**	**66.2**	**67.0**	**66.0**	**64.5**	**67.1**	**71.1**	**68.9**	**70.0**	**71.7**	**72.7**	**73.2**	**74.4**
EBT	**4.2**	**82.6**	**(120.5)**	**(221.9)**	**(736.6)**	**75.7**	**145.8**	**64.6**	**(402.5)**	**86.1**	**160.9**	**71.3**	**52.7**	**107.6**	**185.6**	**96.7**
Provision for income taxes	1.7	32.648	39.7	12.7	(4.1)	30.2	57.5	28.2	10.6	34.1	63.8	28.2	20.8	42.5	73.3	38.2
Implied Tax Rate (excl. goodwill impairment)	42%	40%	32%	29%	-31%	40%	39%	44%	22%	39.6%	39.6%	39.6%	39.5%	39.5%	39.5%	39.5%
Income (loss) from continuing operations	**2.4**	**50.0**	**(160.2)**	**(234.6)**	**(732.5)**	**45.5**	**88.2**	**36.4**	**(413.1)**	**52.0**	**97.1**	**43.0**	**31.9**	**65.1**	**112.3**	**58.5**
Loss (income) from discontinued operations, net of tax	(0.26)	0.81	0.00	0.00												
Net Income (loss)	**2.7**	**49.2**	**(160.2)**	**(234.6)**	**(732.5)**	**45.5**	**88.2**	**36.4**	**(413.1)**	**52.0**	**97.1**	**43.0**	**31.9**	**65.1**	**112.3**	**58.5**
Diluted EPS from continuing operations	0.02	0.31	(1.00)	(1.47)	(4.58)	0.28	0.55	0.23	(2.58)	0.32	0.56	0.25	0.18	0.37	0.62	0.32
EPS excl. impairment & one-time expenses	**0.02**	**0.31**	**0.52**	**0.17**	**0.11**	**0.28**	**0.55**	**0.23**	**0.19**	**0.32**	**0.56**	**0.25**	**0.18**	**0.37**	**0.62**	**0.32**
Diluted Average Shares	160.0	160.0	160.0	160.0	160.0	159.9	160.0	159.9	159.9	164.8	174.4	174.4	175.6	177.8	180.0	182.2
Financial Summary																
Total Revenue growth			6.8%	12.4%	8.2%	5.5%	6.2%	2.7%	8.6%	4.0%	5.8%	7.1%	5.8%	9.4%	8.5%	8.5%
Non-Regulated Revenue growth			0.4%	27.7%	14.4%	20.8%	11.3%	4.1%	-5.2%	-4.5%	5.0%	5.0%	10.0%	10.0%	10.0%	10.0%
O&M/Revenue	60.3%	53.6%	51.9%	60.7%	61.4%	56.1%	50.9%	56.2%	57.1%	54.0%	50.5%	56.5%	56.5%	54.0%	49.6%	54.4%
General Taxes/ Regulated Revenue	11.4%	9.0%	8.2%	8.7%	11.6%	9.4%	8.2%	9.6%	10.6%	9.3%	7.6%	8.9%	10.4%	8.6%	7.4%	8.6%
Adj. EBITDA	137.9	219.6	258.4	175.8	143.6	210.0	280.2	200.7	183.5	230.4	302.9	214.5	199.1	256.6	336.8	250.5
EPS growth, excluding goodwill impairment charge					620.8%	-8.9%	6.0%	34.0%	73.6%	10.9%	1.0%	8.3%	-4.5%	16.0%	12.1%	30.1%

Source: Company reports, Longbow estimates

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

American Water Works— Annual Income Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	FY04A	FY05A	2006A	FY07A	FY08A	FY09E	FY10E	FY11E
Regulated Segment	1748.0	1836.1	1854.6	1987.6	2082.7	2245.9	2422.6	2594.8
% Increase		5.0%	1.0%	7.2%	4.8%	7.8%	7.9%	7.1%
Non-Regulated Revenue	290.0	310.8	248.5	242.7	272.2	259.9	285.9	314.5
% Increase		7.2%	-20.0%	-2.3%	12.2%	-4.5%	10.0%	10.0%
Other	-20.17	(10.1)	(10.0)	(16.0)	(18.0)	(23.0)	(24.2)	(25.9)
% Regulated Rev	-1.2%	-0.6%	-0.5%	-0.8%	-0.9%	-1.0%	-1.0%	-1.0%
Operating revenues	**2,017.9**	**2,136.7**	**2,093.1**	**2,214.2**	**2,336.9**	**2,482.8**	**2,684.3**	**2,883.3**
Operation and maintenance	1122.0	1201.6	1174.5	1246.5	1303.8	1348.2	1433.4	1522.4
Depreciation and amortization	225.3	261.4	259.2	267.3	271.3	288.5	308.4	322.7
General taxes	170.2	183.3	185.1	183.3	199.1	204.1	209.1	214.1
Loss (gain) on sale of assets	(8.6)	(6.5)	0.1	(7.3)	(0.4)	(0.8)	(1.2)	(1.2)
Impairment charges	78.7	385.4	221.7	509.3	750.0	450.0	0.0	0.0
EBIT	**430.4**	**111.6**	**252.5**	**15.1**	**(186.9)**	**192.8**	**734.5**	**825.3**
Operating Margin (excluding impairment)	*25%*	*23%*	*23%*	*24%*	*24%*	*25.9%*	*27.4%*	*28.6%*
Interest	315.9	345.3	366.0	283.2	285.2	295.3	310.7	324.6
Other income, net	(11.0)	(9.5)	(4.5)	(12.5)	(21.5)	(18.2)	(18.8)	(19.0)
Total other income (deductions)	**305.0**	**335.7**	**361.5**	**270.6**	**263.7**	**277.1**	**291.9**	**305.6**
EBT	**125.4**	**(224.2)**	**(108.9)**	**(255.5)**	**(450.6)**	**(84.25)**	**442.6**	**519.8**
Provision for income taxes	66.3	51.0	46.9	86.8	111.8	136.7	174.8	205.3
Implied Tax Rate (excl. goodwill impairment)	32.5%	31.6%	41.6%	34.2%	37.3%	37.4%	39.5%	39.5%
Income (loss) from continuing operations	**59.1**	**(275.1)**	**(155.9)**	**(342.3)**	**(562.4)**	**(221.0)**	**267.7**	**314.4**
Loss (income) from discontinued operations, net of tax	124.0	49.9	6.4	0.6				
Net Income (loss)	**(64.9)**	**(325.0)**	**(162.2)**	**(342.8)**	**(562.4)**	**(221.0)**	**267.7**	**314.4**
Diluted EPS from continuing operations	0.37	(1.72)	(0.97)	(2.14)	(3.52)	(1.31)	1.50	1.67
EPS excl. impairment & one-time expenses	**0.86**	**0.69**	**0.41**	**1.04**	**1.17**	**1.31**	**1.50**	**1.67**
Diluted Average Shares	160.0	160.0	160.0	160.0	160.0	168.4	178.9	188.1
Financial Summary								
Total Revenue growth		5.9%	-2.0%	5.8%	5.5%	6.2%	8.1%	7.4%
Non-Regulated Revenue growth			-20.0%	-2.3%	12.2%	-4.5%	10.0%	10.0%
O&M/Revenue	55.6%	56.2%	56.1%	56.3%	55.8%	54.3%	53.4%	52.8%
Depreciation and amortization/ Net Fixed Asset				3.1%	2.9%	2.8%	2.9%	2.9%
Depreciation Growth		16.0%	-0.8%	3.1%	1.5%	6.3%	6.9%	4.6%
General Taxes/ Regulated Revenue	9.7%	10.0%	10.0%	9.2%	9.6%	9.1%	8.6%	8.3%
Adj. EBITDA	734.3	758.4	733.4	791.8	834.4	931.3	1,042.9	1,148.0
Interest Expense/ Average Net Debt			8.9%	6.2%	5.6%	5.5%	5.6%	5.7%
Interest Expense/Revenue	15.7%	16.2%	17.5%	12.8%	12.2%	11.9%	11.6%	11.3%
Net Income Growth (excl. goodwill impairment)		338.6%	-1.6%	180.1%	12.6%	22.1%	16.9%	17.4%
EPS growth, (excl. goodwill impairment)			-40.3%	153.8%	12.3%	11.6%	14.4%	11.7%
ROE (excl. goodwill & goodwill impairment)			2.3%	7.0%	8.3%	8.6%	8.8%	9.3%

Source: Company reports, Longbow estimates

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

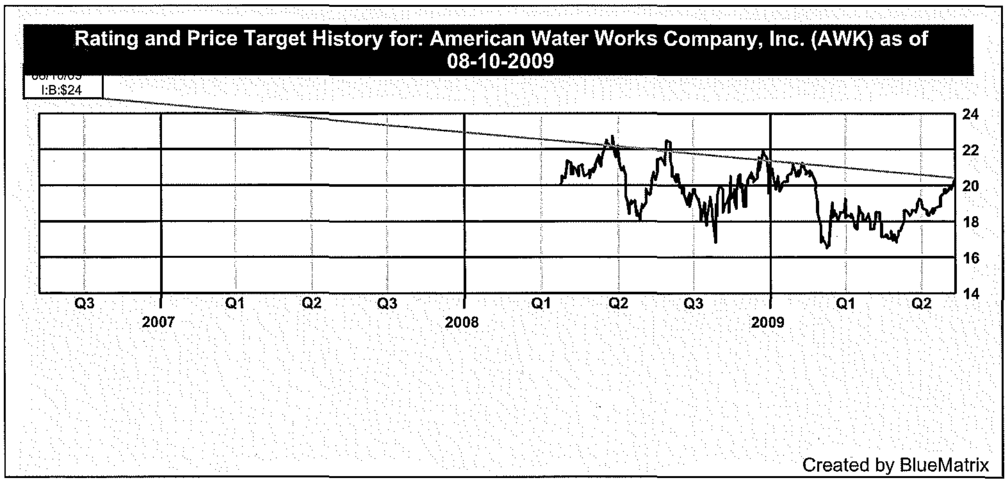
WATER INDUSTRY PEER VALUATION

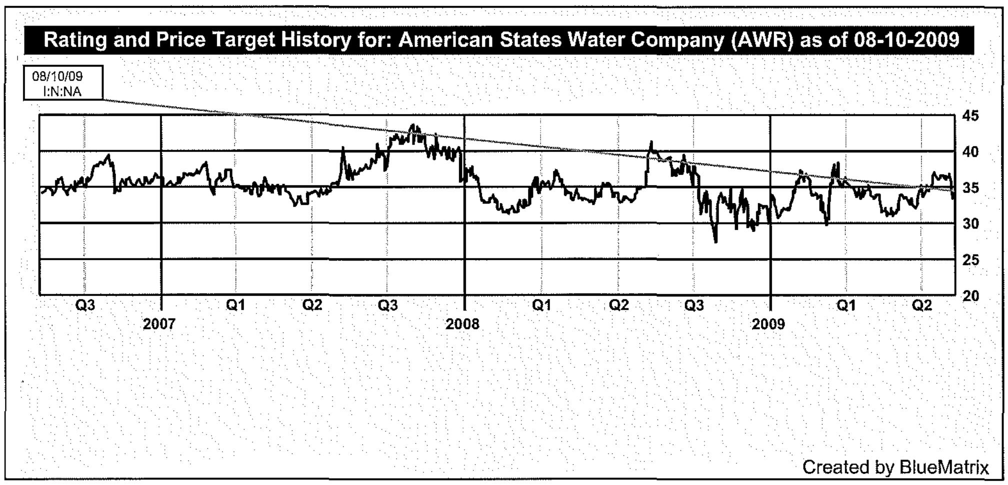
($ in millions, except per share data)

							52 Week			Revenue FY		Earnings per Share		P/E		Dividend	Price/
Company	Ticker	FY End	Rating	Target	% Upside	Share Price	Hi	Lo	Mkt Cap	End	Last FY	Current FY	Next FY	Current FY	Next FY	Rate	Book
U.S. WATER UTILITIES																	
American Water Works	AWK	Dec.	BUY	$24	20%	$ 20.22	$23.12	$16.22	$ 3,558	$ 2,337	1.17	1.31	1.50	15.4x	13.5x	4.1%	1.2x
Aqua America	WTR	Dec.	Neutral			$ 17.73	$22.00	$12.20	$ 2,405	$ 627	0.73	0.82	0.91	21.6x	19.6x	3.3%	2.6x
American States Water	AWR	Dec.	Neutral			$ 38.11	$42.00	$27.00	$ 630	$ 319	1.06	1.74	1.91	22.0x	19.9x	2.9%	1.8x
California Water Service Group	CWT	Dec.	BUY	$45	29%	$ 34.97	$48.28	$27.68	$ 785	$ 410	1.90	2.12	2.20	16.5x	15.9x	3.1%	2.4x
Southwest Water Company	SWWC	Dec.	NR			$ 4.38	$13.40	$2.67	$ 110	$ 222	-0.19	*0.2*	*0.44*	21.9x	10.0x	2.3%	0.7x
Artesian Resources Corporation	ARTNA	Dec	NR			$ 16.35	$18.50	$12.81	$ 123	$ 56	0.86	*0.97*	*1.04*	16.9x	15.7x	4.2%	1.3x
Consolidated Water Co	CWCO	Dec	NR			$ 22.49	$23.91	$6.35	$ 280	$ 60	0.50	*0.72*	*0.87*	31.2x	25.9x	1.4%	1.5x
Connecticut Water Service	CTWS	Dec	NR			$ 16.03	$28.95	$17.31	$ 184	$ 61	1.12	*0.95*	*0.96*	16.9x	16.7x	4.1%	1.9x
Middlesex Water Company	MSEX	Dec	NR			$ 19.18	$18.52	$11.64	$ 209	$ 91	0.90	*0.74*	*0.83*	25.9x	23.1x	4.6%	1.7x
Pennichuck Corporation	PNNW	Dec	NR			$ 21.22	$24.80	$14.75	$ 97	$ 31	0.57	*0.61*	*0.79*	34.8x	26.9x	3.1%	1.8x
York Water Company	YORW	Dec	NR			$ 14.76	$17.95	$6.22	$ 186	$ 33	0.57	*0.66*	*0.7*	22.4x	21.1x	3.1%	2.0x
U.S. Water Utility Average														22.3x	18.9x	3.3%	1.7x
EQUIPMENT/FILTRATION/TREATMENT SECTOR																	
Calgon Carbon Corp.	CCC	Dec.	NR			$ 13.68	$23.03	$9.11	$ 726	$ 400	0.56	*0.5*	*0.76*	26.5x	17.4x	0.0%	3.3x
Danaher	DHR	Dec.	NR			$ 60.29	$85.00	$47.20	$ 19,552	$ 12,697	4.23	*3.37*	*3.59*	18.2x	17.1x	0.2%	1.8x
ITT Technologies	ITT	Dec.	NR			$ 48.74	$68.17	$31.94	$ 9,036	$ 11,695	4.04	*3.63*	*3.77*	13.7x	13.2x	1.7%	2.7x
Layne Christensen	LAYN	Jan.	NR			$ 23.56	$58.26	$10.36	$ 474	$ 1,008	2.20	*0.47*	*0.96*	52.1x	25.5x	0.0%	0.7x
Mueller Water Products	MWA	Sept	NR			$ 3.83	$12.71	$1.48	$ 460	$ 1,859	0.46	*(0.26)*	-	-	57.7x	1.8%	0.8x
Nalco	NLC	Dec.	NR			$ 17.50	$25.90	$7.80	$ 2,416	$ 4,212	1.30	*0.81*	*1.17*	21.5x	15.0x	0.8%	4.0x
Pall Corp.	PLL	Jul.	NR			$ 30.26	$42.72	$18.20	$ 3,612	$ 2,572	1.94	*1.72*	*1.95*	18.0x	16.5x	1.9%	4.3x
Pentair	PNR	Dec.	NR			$ 27.10	$41.00	$17.23	$ 2,706	$ 3,382	2.17	*1.42*	*1.7*	19.4x	16.2x	2.6%	1.2x
Watts Water Technologies	WTS	Dec.	NR			$ 28.48	$33.00	$15.85	$ 1,041	$ 1,459	1.83	*1.31*	*1.45*	21.7x	19.6x	1.5%	1.1x
Equipment/Filtration/Treatment Average (*ex BWTR and CCC)														23.9x	22.0x	1.2%	2.2x
WATER RESOURCES/ INFRASTRUCTURE																	
Insituform Technologies	INSU		NR			$ 18.52	$21.28	$9.26	$ 728	$ 537	0.77	*0.98*	*1.12*	19.1x	16.7x	0.0%	1.5x
Lindsay Manufacturing	LNN		NR			$ 39.66	$97.80	$20.89	$ 496	$ 475	3.11	*1.05*	-	31.8x	28.6x	0.8%	5.1x
Tetra Tech	TTEK		NR			$ 29.63	$30.90	$14.20	$ 1,801	$ 2,145	1.02	*1.24*	*1.42*	21.8x	21.9x	0.0%	2.8x
Water Resources/ Infrastructure Average														24.2x	22.4x	0.3%	3.1x
Relevant Indices																	
Dow Jones Industrials	DJ30					$ 9,241.45											
S&P 500	SPX					$ 994.35											
Nasdaq Composite	NDX					$ 1,969.73											

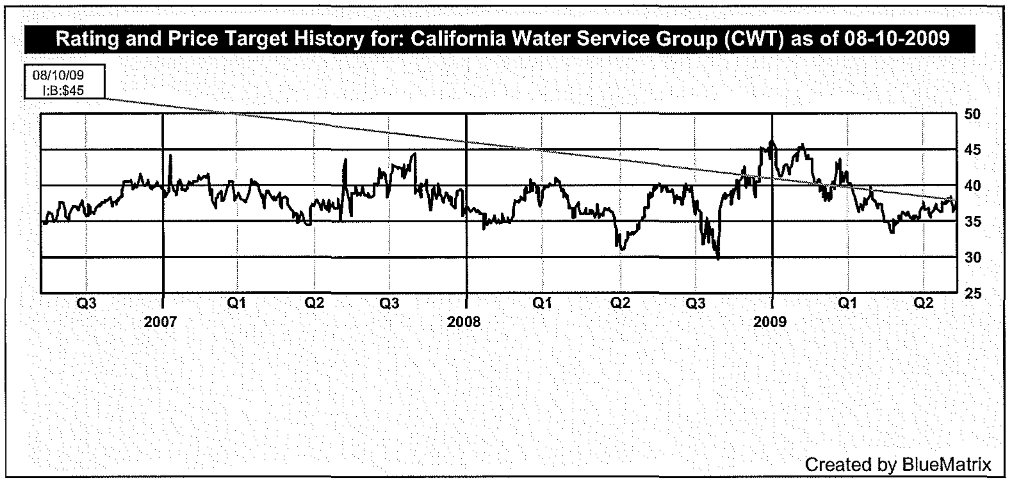
Source: Baseline; Company reports and LBR Estimates. EPS reflects diluted EPS, excluding extraordinary items. Numbers in italics reflect consensus estimates.
** Time period for annual estimates may vary based on reporting date.

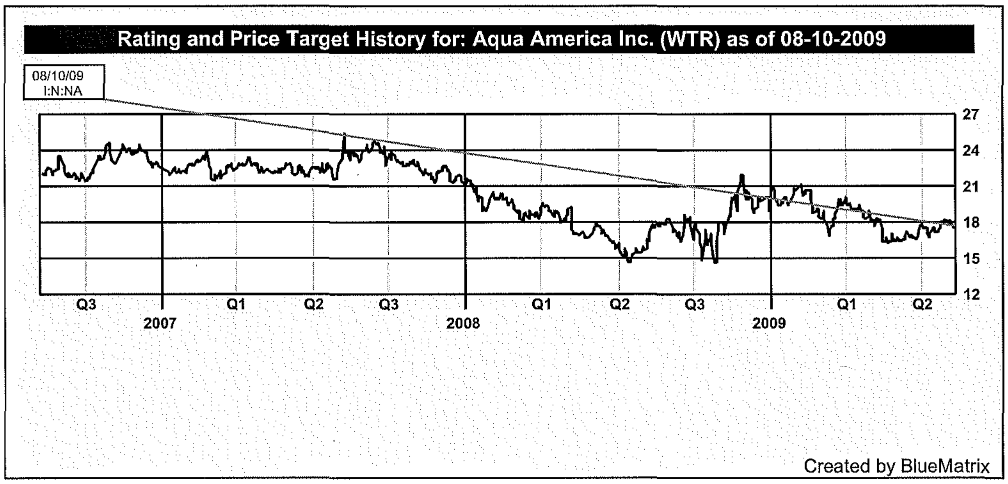
Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com





Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com





APPENDIX

IMPORTANT DISCLOSURES

REGULATION ANALYST CERTIFICATION ("REG AC"): The Research Analyst(s) who prepared this research report hereby certifies that the views expressed in the research report accurately reflect the analyst(s) personal views about the subject companies and their securities. The Research Analyst(s) also certifies that the Analyst(s) have not been, are not, and will not be receiving direct or indirect compensation for expressing the specific recommendation(s) or view(s) in this report.

Covered Companies Mentioned In This Report:

American Water Works Company, Inc.	AWK	$20.22	Buy
American States Water Company	AWR	$34.38	Neutral
California Water Service Group	CWT	$37.82	Buy
Aqua America Inc.	WTR	$17.73	Neutral

GENERAL DISCLOSURES: Longbow Securities does not make a market in any securities, nor does it hold a principal position in any security. However, any officer, director or stockholder of Longbow Securities or any member of their families may have a position in and may from time to time purchase or sell any of the securities mentioned or any related securities. Security prices in this report may either reflect the previous day's closing price or an intraday price, depending on the time of distribution. Consensus estimates are derived from either Thomson/Reuters, Bloomberg or Baseline. Designated trademarks and brands are the property of their respective owners.

SPECIFIC DISCLOSURES:

- Longbow Securities does not make a market in any securities, nor does it hold a principal position in any security.
- No officer, principal, employee, or owner of Longbow Securities owns options, rights, or warrants to purchase the subject security or any other security mentioned in this report.
- No employee of Longbow Securities serves on the Board of Directors of the subject security or any other security mentioned in this report.
- Neither the Research Analyst nor a member of the Research Analyst's household has a financial interest in the securities of the subject company or any other security mentioned in this report.
- Neither the Research Analyst nor a member of the Research Analyst's household serves on the Board of Directors of the subject company or any other security mentioned in this report.
- Neither Longbow Securities nor its affiliates beneficially own 1% or more of an equity security of the subject company or any other security mentioned in this report.

RATINGS DISTRIBUTIONS FOR LONGBOW RESEARCH:

Rating Category	Count	Percent
Buy	49	24.3%
Neutral	146	72.3%
Sell	7	3.5%

RATING SYSTEM:

"Buy" means that Longbow Securities expects total return to exceed 20% over a 12-month period.

"Neutral" means that Longbow Securities expects total return to be within a range of plus or minus 20% over a 12-month period.

"Sell" means that Longbow Securities expects total return to be negative by greater than 20% over a 12-month period.

Longbow Research's full research universe and related applicable disclosures can be obtained by calling (216) 986-0700 or via postal mail at: Editorial Department, Longbow Research, 6000 Lombardo Center, Suite #500, Independence, Ohio 44131.

DISCLAIMER: The information, opinions, estimates and projections contained in this report were prepared by Longbow Securities LLC, a wholly owned subsidiary of Longbow Research LLC, and constitute the current judgment of Longbow Securities as of the date of this report. Additional information may be available from Longbow Securities upon request. The information contained herein is believed to be reliable and has been obtained from sources believed to be reliable, but Longbow Securities makes no representation or warranty, either expressed or implied, as to the accuracy, completeness or reliability of such information. Longbow Securities does not undertake, and has no duty, to advise you as to any information that comes to its attention after the date of this report or any changes in its opinion, estimates or projections. Prices and availability of securities are also subject to change without notice. By accepting this report, the reader acknowledges that the report does not purport to meet the objectives or needs of specific investors, and, accordingly, constitutes only "impersonal advisory services" as that term is defined in Rule 204-3 under the Investment Advisers Act of 1940 and that any advice in this report is furnished solely through

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

uniform publications distributed to subscribers thereto within the meaning of Section 2(a)(20)(i) of the Investment Company Act of 1940. The securities discussed in Longbow Research reports may be unsuitable for some investors depending on their specific investment objectives, financial status, risk profile, or particular needs. Investors should consider this report as only a single factor in making their investment decisions and should not rely entirely on this report in evaluating whether or not to buy or sell the securities of the subject company. Longbow Research archives and reviews outgoing and incoming email. Such may be produced at the request of regulators. Sender accepts no liability for any errors or omissions arising as a result of transmission. Use by other than intended recipients is prohibited.

DESCRIPTION: Longbow Securities LLC, a wholly owned subsidiary of Longbow Research LLC, is a primary research provider established in 2003 and headquartered at 6000 Lombardo Center, Suite 500, Independence, Ohio 44131 USA. The company provides research services to institutional investors, investment advisers, and professional money managers. MEMBER FINRA/SIPC. Additional information supporting the statements in this report is available upon request.

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

LONGBOW Research
Tactical advantage through independent research

Estimate Changes

October 2, 2009 **AMERICAN WATER WORKS COMPANY, INC. (AWK)**

Rating:	**BUY**	
Current Price:	**$19.77**	
Target Price:	**$24.00**	

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

Industry: Water Utilities Fiscal Year: Dec			**1Q09A**	**2Q09A**	**3Q09E**	**4Q09E**	**FY09E**	**Valuation Multiple**	**FY10E**	**Valuation Multiple**
Market Cap ($MM):	3,228	**EPS:**	$0.19	$0.32	$0.54	$0.25	$1.29	15.3x	$1.50	13.2x
		Prior:	-	-	$0.56	-	$1.31		-	
Net Debt ($MM):	4,972	Consensus:			$0.55	$0.27	$1.32	15.0x	$1.46	13.5x
Enterprise Value ($MM):	8,200	Last Year:	$0.11	$0.28	$0.55	$0.23	$1.17			
Shares - FD (MM):	163.3									
		EBITDA:	$1.15	$1.40	$1.70	$1.23	$5.49	9.1x	$5.83	8.6x
Dividend:	$0.84	Growth:	28%	10%	6%	7%	11%		13%	
Yield:	4.2%									
Beta:	0.46	**Revenue:**	$550	$613	$703	$609	$2,475	3.3x	$2,684	3.1x
Rel. P/E (FY2009E):	80%	Growth:	9%	4%	5%	7%	140%		8%	

AWK: Lowering 3Q09E by $0.02 on Wet Weather, but New Wins Could Lead Upside

SUMMARY

- We are reducing our FY09E by $0.02 to $0.54 to account for wet weather in the Northeast and Midwest during the quarter.
- AWK also announced yesterday that it has been awarded 50-year contracts for O&M of the water and wastewater systems at Fort Belvoir, VA and Fort Meade, MD. The total value of these contracts over the 50-year period is $288M and $650M, respectively. We expect ~$19M additional revenue for the AWK's Non-Regulated segment going forward. While we already had already modeled 10% revenue growth ($26M) for the segment in FY10E in anticipation of such contract wins, however, there could be upside to our model if additional wins are announced.
- We also note that AWK yesterday announced the acquisition of three small municipal systems in PA for $935K. While we do not anticipate these deals will move the needle regarding earnings growth, they do serve as a confirmation of a likely increase in consolidation in the water utilities space going forward.
- We continue to rate AWK a BUY with a $24 price target and see the shares as undervalued relative to the peer group. We expect multiples to expand as a) AWK demonstrates its ability to grow EPS approximately 10-12% over the next 2-3 years as it realizes rate increases following the prior 5-6 years of underinvestment, and b) RWE liquidates its remaining ~27% position in the company.

Investment Thesis

We rate American Water Works Company, Inc. (AWK) BUY with a $24 target price, as we see AWK as offering an attractive risk/reward ratio, with positive catalysts relative to the peer group. We believe AWK shares are discounting RWE's anticipated exit as the former parent company has announced plans to sell its remaining stake in AWK. While the timing of this cannot be predicted, we believe AWK's discounted valuation by investors is overdone. The shares are trading at 13.2x our FY10E EPS, relative to a peer group average of 18.3x. We also believe there is also an opportunity for multiple expansion toward the peer group average of once the RWE overhang abates. However, our target price still incorporates a 13% discount to the peer group average.

Valuation

AWK shares closed yesterday at $19.77, which is 15.3x our FY09E EPS of $1.29 and 13.2x our FY10E EPS of $1.50. The shares are trading at a discount to the peer group average of 18.3x FY10 EPS due in large part to the RWE overhang, which we believe the Street is already accounting for. The shares are trading at 1.2x tangible book value compared to a peer group that trades over 1.7x, on average. Our target price of $24 is based on 16.0x our FY10E EPS, a valuation that remains at a discount to the peer group. However, we see multiple expansion from current levels as justified given AWK being viewed as the largest and most diversified publicly traded water utility in the U.S. and with the potential from earnings growth as the company catches up to insufficient rate increases during the past five to six years.

Risks

The potential downside risks to our investment thesis include, but are not limited to: 1) delays in rate case processing or lower rate increases by the regulators than our expectations, 2) 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, 4) a large acquisition at an excessive valuation (significantly above the rate base), and 5) a large goodwill impairment which could lead to a breach of debt covenants or regulatory requirements.

Lowering 3Q09E on Wet Weather

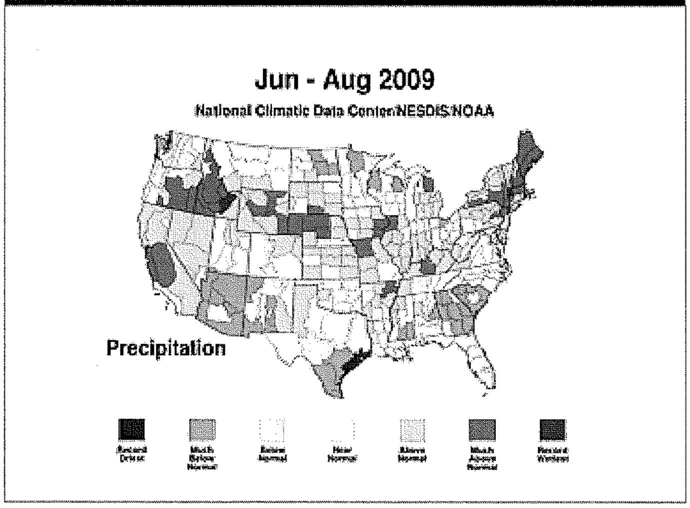
We are lowering our estimates for 3Q09 for AWK to account for wet weather in Northeast and cold weather in the Midwest during the quarter. We now forecast $0.54 (-$0.02). We note that the estimate revision does not change our opinion on the shares, as we view AWK as undervalued relative the group on expected earnings power over the next two to three years.

Water sales by utilities are dependent on the weather conditions, including temperature and precipitation. Customers consume less water in cold and wet weather, especially for landscaping, which is one of the largest uses of water for households. We note that change in water consumption does not have any impact on long-term earning potential of utilities as water rates are calculated using assumptions about average consumption over a period of time. However, short-term change in consumption causes volatility in revenue and earnings.

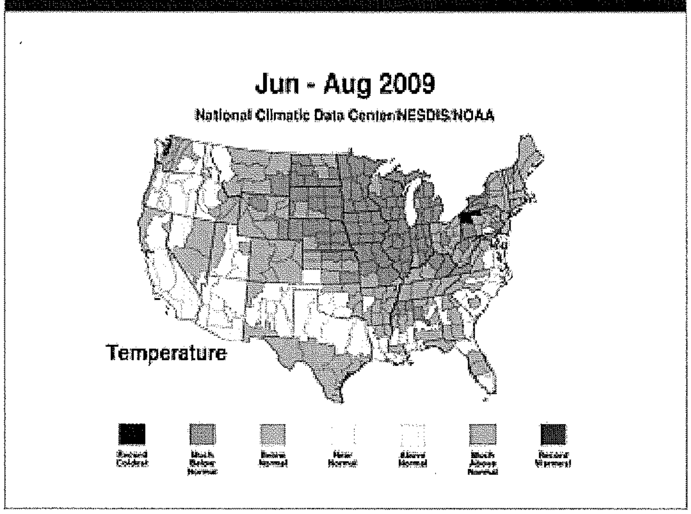
According to the "National Climatic Data Center", for the summer season (June–August), the Northeast Region had its eighth wettest period on record" and the unseasonably cool weather of July continued into the month of August throughout the Midwest. Our understanding is that September trends were similar to the prior months. Approximately 71% of AWK's service territory is in the Northeast and Midwest, including NJ 25%, PA 21%, MI 9%, IL 9%, and IN 7% (% of FY08 revenue). For another data point, Aqua America (WTR) announced during its analyst day last week that it was negatively impacted by wet weather in 3Q09 and expected a $0.03 negative EPS impact. We expect a similar impact on AWK and are lowering our revenue estimate by $8M and EPS by $0.02 to account for the lower expected water sales.

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

Avg. Precipitation Summer 2009



Avg. Temperature Summer 2009



Military Contract Wins

AWK has been awarded 50-year contracts for O&M of the water and wastewater systems at Fort Belvoir, VA and Fort Meade, MD. The total value of these contracts over the 50-year period is $288M and $650M, respectively. We note that AWK is already managing water and wastewater systems at eight other military bases around the country. Though the revenue from these wins can vary annually, we

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

expect $19M additional revenue for the AWK's Non-Regulated segment going forward. While we already had already modeled 10% revenue growth ($26M) for the segment in FY10E in anticipation of such contract wins, however, given the size of this contract, AWK appears on its way to meeting our forecast, and there could be upside to our model if additional wins are announced.

The U.S, government has been privatizing utility operations at military bases under its ""Defense Utilities Privatization Program", which was passed in 1997. The progress of this program has been slow to date and a large number of bases are expected to be privatized in the coming years. We believe AWK has a tremendous opportunity to significantly expand this business as utility systems at more bases are privatized in the coming years.

Though AWK does discuss the profitability of its military base operations, its main competitor for the business, American States Water (AWR), has been struggling to make a profit from similar operations. We expect the profitability for these contracts to be below the 8-11% operating margin for AWK's Non-Regulated business. However, the contracts are subject to price redetermination and we expect the profitability to improve in the coming years. As a caution, we note that AWR has been struggling to attain price redeterminations for its contracts. For further details on military base operations, please refer to our report "Water Utilities: A Closer Look at the Non-Regulated Side" published on 09/23/2009.

AWK Announces 3 Minor Acquisitions

AWK also announced yesterday the acquisition of three small systems from municipal authorities in north central and western Pennsylvania. The systems, which serve only 600 people, were acquired for $935K. Though these tuck-ins generally are a routine business for AWK, they are somewhat different in being municipal systems. Given municipal systems comprise ~85% of the total, and with localities facing budget crunches, we expect M&A in this sector to accelerate over the next two to three years. These small purchases by AWK serve to confirm our thesis.

One of the three acquisitions, from Wallaceton Municipal Authority, is a good example of the value that a large utility like AWK can provide to smaller communities. Wallaceton's water system was under a consent order from Department of Environmental Protection (DEP), which required the municipality to obtain a new supply source or build additional treatment facilities. This would have entailed an unfeasible expenditure for the small community. Instead, DEP, the local Representative and the Pennsylvania Infrastructure Investment Authority (PENNVEST), worked with Wallaceton Municipal Authority to facilitate the sale of the water system to AWK. AWK interconnected the Wallaceton community with its adjacent water system, providing water service at a potentially lower cost. DEP even helped to pay for extending public water service to some homeowners. Apart from increasing its customer base, the acquisition is giving AWK the opportunity to make infrastructure investment in the acquired system, which will need upgrades over the coming years. While the multiple paid was not provided, we suspect valuations were likely book value or below for this particular system.

The acquisition reinforces our thesis that the state of water/wastewater infrastructure in the U.S. will accelerate the pace of consolidation in the coming years. Acquisitions not only allow increase growth but also present additional opportunities for AWK to increase its capex program. Being a regulated utility, infrastructure investment in the only means for the company to grow its earnings faster than revenue growth.

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

American Water Works— Quarterly Income Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09E	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E
Regulated Segment	419.3	508.6	571.9	487.8	449.9	527.1	603.7	502.1	497.4	554.9	638.7	547.0	524.2	605.7	700.4	592.3
% Increase			7.3%	11.2%	7.3%	3.6%	5.6%	2.9%	10.6%	5.3%	5.8%	8.9%	5.4%	9.2%	9.7%	8.3%
Non-Regulated Revenue	53.3	55.5	66.4	67.5	61.0	67.0	73.9	70.3	57.5	64.2	70.9	67.3	63.3	70.6	78.0	74.1
% Increase			0.4%	27.7%	14.4%	20.8%	9.4%	4.1%	-5.7%	-4.2%	-4.1%	-4.3%	10.0%	10.0%	10.0%	10.0%
Other	(4.0)	(5.4)	(5.1)	(1.5)	(4.1)	(4.7)	(5.4)	(3.9)	(4.7)	(6.3)	(6.4)	(5.5)	(5.2)	(6.1)	(7.0)	(5.9)
% Regulated Rev	-1.0%	-1.1%	-0.9%	-0.3%	-0.9%	-0.9%	-0.9%	-0.8%	-1.0%	-1.1%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%
Operating revenues	**468.5**	**558.7**	**633.1**	**553.8**	**506.8**	**589.4**	**672.2**	**568.6**	**550.2**	**612.7**	**703.1**	**608.8**	**582.3**	**670.3**	**771.4**	**660.4**
Operation and maintenance	282.6	299.4	328.3	336.2	311.3	330.6	342.2	319.8	314.4	330.6	357.3	344.1	329.0	361.9	382.9	359.6
Depreciation and amortization	64.6	68.1	69.7	64.9	63.9	67.3	68.4	71.6	68.8	73.2	73.2	73.2	74.8	76.4	77.9	79.5
General taxes	47.9	45.9	47.1	42.3	52.1	49.6	49.4	48.0	52.5	51.7	49.3	50.6	54.5	52.0	52.0	50.6
Loss (gain) on sale of assets	0.1	(6.2)	(0.7)	(0.5)	(0.1)	(0.8)	0.5	(0.0)	(0.2)	0.0	(0.3)	(0.3)	(0.3)	(0.3)	(0.3)	(0.3)
Impairment charges			243.3	266.0	750.0				450.0							
EBIT	**73.3**	**151.5**	**(54.6)**	**(155.1)**	**(670.4)**	**142.7**	**211.8**	**129.1**	**(335.4)**	**157.2**	**223.6**	**141.3**	**124.3**	**180.3**	**258.8**	**171.0**
Operating Margin (excluding impairment)	*16%*	*27%*	*30%*	*20%*	*16%*	*24%*	*32%*	*23%*	*21%*	*26%*	*32%*	*23%*	*21%*	*27%*	*34%*	*26%*
Interest	72.2	70.8	68.739	71.5	70.0	70.1	72.7	72.4	72.0	73.7	74.4	75.2	76.2	77.2	78.2	79.2
Other income, net	(3.0)	(1.9)	(2.9)	(4.6)	(3.7)	(3.1)	(6.7)	(8.0)	(4.8)	(2.6)	(5.5)	(5.2)	(4.6)	(4.5)	(5.0)	(4.8)
Total other income (deductions)	**69.2**	**68.9**	**65.8**	**66.8**	**66.2**	**67.0**	**66.0**	**64.5**	**67.1**	**71.1**	**68.9**	**70.0**	**71.7**	**72.7**	**73.2**	**74.4**
EBT	**4.2**	**82.6**	**(120.5)**	**(221.9)**	**(736.6)**	**75.7**	**145.8**	**64.6**	**(402.5)**	**86.1**	**154.8**	**71.3**	**52.6**	**107.5**	**185.6**	**96.6**
Provision for income taxes	1.7	32.648	39.7	12.7	(4.1)	30.2	57.5	28.2	10.6	34.1	61.3	28.2	20.8	42.5	73.3	38.2
Implied Tax Rate (excl. goodwill impairment)	42%	40%	32%	29%	-31%	40%	39%	44%	22%	39.6%	39.6%	39.6%	39.5%	39.5%	39.5%	39.5%
Income (loss) from continuing operations	**2.4**	**50.0**	**(160.2)**	**(234.6)**	**(732.5)**	**45.5**	**88.2**	**36.4**	**(413.1)**	**52.0**	**93.4**	**43.0**	**31.9**	**65.1**	**112.3**	**58.4**
Loss (income) from discontinued operations, net of tax	(0.26)	0.81	0.00	0.00												
Net Income (loss)	**2.7**	**49.2**	**(160.2)**	**(234.6)**	**(732.5)**	**45.5**	**88.2**	**36.4**	**(413.1)**	**52.0**	**93.4**	**43.0**	**31.9**	**65.1**	**112.3**	**58.4**
Diluted EPS from continuing operations	0.02	0.31	(1.00)	(1.47)	(4.58)	0.28	0.55	0.23	(2.58)	0.32	0.54	0.25	0.18	0.37	0.62	0.32
EPS excl. impairment & one-time expenses	**0.02**	**0.31**	**0.52**	**0.17**	**0.11**	**0.28**	**0.55**	**0.23**	**0.19**	**0.32**	**0.54**	**0.25**	**0.18**	**0.37**	**0.62**	**0.32**
Diluted Average Shares	160.0	160.0	160.0	160.0	160.0	159.9	160.0	159.9	159.9	164.8	174.4	174.4	175.6	177.8	180.0	182.2
Financial Summary																
Total Revenue growth			6.8%	12.4%	8.2%	5.5%	6.2%	2.7%	8.6%	4.0%	4.6%	7.1%	5.8%	9.4%	9.7%	8.5%
Non-Regulated Revenue growth			0.4%	27.7%	14.4%	20.8%	11.3%	4.1%	-5.2%	-4.5%	5.0%	5.0%	10.0%	10.0%	10.0%	10.0%
O&M/Revenue	60.3%	53.6%	51.9%	60.7%	61.4%	56.1%	50.9%	56.2%	57.1%	54.0%	50.8%	56.5%	56.5%	54.0%	49.6%	54.4%
General Taxes/ Regulated Revenue	11.4%	9.0%	8.2%	8.7%	11.6%	9.4%	8.2%	9.6%	10.6%	9.3%	7.7%	8.9%	10.4%	8.6%	7.4%	8.6%
Adj. EBITDA	137.9	219.6	258.4	175.8	143.6	210.0	280.2	200.7	183.5	230.4	296.8	214.5	199.1	256.6	336.8	250.5
EPS growth, excluding goodwill impairment charge					620.8%	-8.9%	6.0%	34.0%	73.6%	10.9%	-2.8%	8.3%	-4.5%	16.0%	16.5%	30.0%

Source: Company reports, Longbow estimates

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

American Water Works— Annual Income Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	FY04A	FY05A	2006A	FY07A	FY08A	FY09E	FY10E	FY11E
Regulated Segment	1748.0	1836.1	1854.6	1987.6	2082.7	2237.9	2422.6	2594.8
% Increase		5.0%	1.0%	7.2%	4.8%	7.4%	8.3%	7.1%
Non-Regulated Revenue	290.0	310.8	248.5	242.7	272.2	259.9	285.9	314.5
% Increase		7.2%	-20.0%	-2.3%	12.2%	-4.5%	10.0%	10.0%
Other	-20.17	(10.1)	(10.0)	(16.0)	(18.0)	(22.9)	(24.2)	(25.9)
% Regulated Rev	-1.2%	-0.6%	-0.5%	-0.8%	-0.9%	-1.0%	-1.0%	-1.0%
Operating revenues	**2,017.9**	**2,136.7**	**2,093.1**	**2,214.2**	**2,336.9**	**2,474.9**	**2,684.3**	**2,883.4**
Operation and maintenance	1122.0	1201.6	1174.5	1246.5	1303.8	1346.3	1433.4	1522.4
Depreciation and amortization	225.3	261.4	259.2	267.3	271.3	288.5	308.6	322.7
General taxes	170.2	183.3	185.1	183.3	199.1	204.1	209.1	214.1
Loss (gain) on sale of assets	(8.6)	(6.5)	0.1	(7.3)	(0.4)	(0.8)	(1.2)	(1.2)
Impairment charges	78.7	385.4	221.7	509.3	750.0	450.0	0.0	0.0
EBIT	**430.4**	**111.6**	**252.5**	**15.1**	**(186.9)**	**186.7**	**734.3**	**825.3**
Operating Margin (excluding impairment)	*25%*	*23%*	*23%*	*24%*	*24%*	*25.7%*	*27.4%*	*28.6%*
Interest	315.9	345.3	366.0	283.2	285.2	295.29	310.74	324.55
Other income, net	(11.0)	(9.5)	(4.5)	(12.5)	(21.5)	(18.2)	(18.8)	(19.0)
Total other income (deductions)	**305.0**	**335.7**	**361.5**	**270.6**	**263.7**	**277.1**	**291.9**	**305.6**
EBT	**125.4**	**(224.2)**	**(108.9)**	**(255.5)**	**(450.6)**	**(90.35)**	**442.4**	**519.8**
Provision for income taxes	66.3	51.0	46.9	86.8	111.8	134.3	174.7	205.3
Implied Tax Rate (excl. goodwill impairment)	32.5%	31.6%	41.6%	34.2%	37.3%	37.3%	39.5%	39.5%
Income (loss) from continuing operations	**59.1**	**(275.1)**	**(155.9)**	**(342.3)**	**(562.4)**	**(224.6)**	**267.7**	**314.5**
Loss (income) from discontinued operations, net of tax	124.0	49.9	6.4	0.6				
Net Income (loss)	**(64.9)**	**(325.0)**	**(162.2)**	**(342.8)**	**(562.4)**	**(224.6)**	**267.7**	**314.5**
Diluted EPS from continuing operations	0.37	(1.72)	(0.97)	(2.14)	(3.52)	(1.33)	1.50	1.67
EPS excl. impairment & one-time expenses	**0.86**	**0.69**	**0.41**	**1.04**	**1.17**	**1.29**	**1.50**	**1.67**
Diluted Average Shares	160.0	160.0	160.0	160.0	160.0	168.4	178.9	188.1
Financial Summary								
Total Revenue growth		5.9%	-2.0%	5.8%	5.5%	5.9%	8.5%	7.4%
Non-Regulated Revenue growth			-20.0%	-2.3%	12.2%	-4.5%	10.0%	10.0%
O&M/Revenue	55.6%	56.2%	56.1%	56.3%	55.8%	54.4%	53.4%	52.8%
Depreciation and amortization/ Net Fixed Asset				3.1%	2.9%	2.8%	2.8%	2.8%
Depreciation Growth		16.0%	-0.8%	3.1%	1.5%	6.3%	7.0%	4.6%
General Taxes/ Regulated Revenue	9.7%	10.0%	10.0%	9.2%	9.6%	9.1%	8.6%	8.3%
Adj. EBITDA	734.3	758.4	733.4	791.8	834.4	925.2	1,042.9	1,148.0
Interest Expense/ Average Net Debt			8.9%	6.2%	5.6%	5.47%	5.68%	5.91%
Interest Expense/Revenue	15.7%	16.2%	17.5%	12.8%	12.2%	11.9%	11.6%	11.3%
Net Income Growth (excl. goodwill impairment)		338.6%	-1.6%	180.1%	12.6%	20.1%	18.8%	17.5%
EPS growth, (excl. goodwill impairment)			-40.3%	153.8%	12.3%	9.8%	16.2%	11.7%
ROE (excl. goodwill & goodwill impairment)			2.3%	7.0%	8.3%	8.7%	9.2%	9.7%

Source: Company reports, Longbow estimates

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

WATER INDUSTRY PEER VALUATION

($ in millions, except per share data)

							52 Week					Earnings per Share		P/E		Dividend	Price/
Company	Ticker	FY End	Rating	Target	% Upside	Share Price	Hi	Lo	Mkt Cap	Revenue FY End	Last FY	Current FY	Next FY	Current FY	Next FY	Rate	Book
U.S. WATER UTILITIES																	
American Water Works	AWK	Dec.	BUY	$24	20%	$ 19.77	$22.35	$16.22	$ 3,481	$ 2,337	1.17	1.29	1.50	15.3x	13.2x	4.2%	1.2x
Aqua America	WTR	Dec.	Neutral			$ 17.11	$22.00	$12.20	$ 2,398	$ 627	0.73	0.79	0.91	21.7x	18.9x	3.3%	2.6x
American States Water	AWR	Dec.	Neutral			$ 35.56	$39.50	$27.00	$ 669	$ 319	1.06	1.74	1.91	20.5x	18.6x	2.8%	1.8x
California Water Service Group	CWT	Dec.	BUY	$45	16%	$ 38.66	$48.28	$27.68	$ 808	$ 410	1.90	2.12	2.20	18.2x	17.6x	3.0%	2.4x
Southwest Water Company	SWWC	Dec.	NR			$ 4.68	$12.56	$2.67	$ 122	$ 222	-0.19	*0.1*	*0.39*	46.8x	12.0x	2.0%	0.7x
Artesian Resources Corporation	ARTNA	Dec	NR			$ 16.68	$18.14	$12.81	$ 125	$ 56	0.86	*1.07*	*1.11*	15.6x	15.0x	4.2%	1.3x
Consolidated Water Co	CWCO	Dec	NR			$ 15.44	$21.29	$6.35	$ 237	$ 60	0.50	*0.78*	*0.82*	19.8x	18.8x	1.8%	1.5x
Connecticut Water Service	CTWS	Dec	NR			$ 21.83	$28.71	$17.31	$ 191	$ 61	1.12	*1.08*	*1.06*	20.2x	20.6x	4.1%	1.9x
Middlesex Water Company	MSEX	Dec	NR			$ 14.90	$17.93	$11.64	$ 203	$ 91	0.90	*0.69*	*0.79*	21.6x	18.9x	4.7%	1.7x
Pennichuck Corporation	PNNW	Dec	NR			$ 21.43	$24.80	$14.75	$ 93	$ 31	0.57	*0.59*	*0.76*	36.3x	28.2x	3.2%	1.8x
York Water Company	YORW	Dec	NR			$ 13.70	$17.95	$9.74	$ 158	$ 33	0.57	*0.67*	*0.7*	20.4x	19.6x	3.6%	2.0x
U.S. Water Utility Average														23.3x	18.3x	3.4%	1.7x
EQUIPMENT/FILTRATION/TREATMENT SECTOR																	
Calgon Carbon Corp.	CCC	Dec.	NR			$ 14.55	$21.64	$9.11	$ 812	$ 400	0.56	*0.5*	*0.77*	29.6x	19.4x	0.0%	3.3x
Danaher	DHR	Dec.	NR			$ 65.29	$70.23	$47.20	$ 21,525	$ 12,697	4.23	*3.37*	*3.72*	20.0x	18.1x	0.2%	1.8x
ITT Technologies	ITT	Dec.	NR			$ 50.21	$56.15	$31.94	$ 9,512	$ 11,695	4.04	*3.65*	*3.81*	14.3x	13.7x	1.6%	2.7x
Layne Christensen	LAYN	Jan.	NR			$ 30.18	$35.48	$10.36	$ 624	$ 1,008	2.20	*0.62*	*0.95*	52.0x	33.6x	0.0%	0.7x
Mueller Water Products	MWA	Sept	NR			$ 5.19	$9.07	$1.48	$ 639	$ 1,859	0.46	*(0.38)*	-	-	96.1x	1.3%	0.8x
Nalco	NLC	Dec.	NR			$ 19.49	$20.99	$7.80	$ 2,831	$ 4,212	1.30	*0.8*	*1.17*	25.7x	17.5x	0.7%	4.0x
Pall Corp.	PLL	Jul.	NR			$ 31.32	$34.54	$18.20	$ 3,807	$ 2,329	1.94	*1.85*	*2.08*	18.2x	16.6x	1.8%	3.2x
Pentair	PNR	Dec.	NR			$ 28.61	$35.00	$17.23	$ 2,902	$ 3,382	2.17	*1.42*	*1.73*	20.8x	17.1x	2.4%	1.2x
Watts Water Technologies	WTS	Dec.	NR			$ 29.35	$32.88	$15.85	$ 1,108	$ 1,459	1.83	*1.31*	*1.45*	23.1x	20.8x	1.5%	1.1x
Equipment/Filtration/Treatment Average (*ex BWTR and CCC)														25.5x	28.1x	1.1%	2.1x
WATER RESOURCES/ INFRASTRUCTURE																	
Insituform Technologies	INSU		NR			$ 18.43	$21.28	$9.26	$ 743	$ 537	0.77	*0.96*	*1.14*	19.9x	16.8x	0.0%	1.5x
Lindsay Manufacturing	LNN		NR			$ 36.84	$76.00	$20.89	$ 485	$ 475	3.11	*1.06*	-	30.9x	27.5x	0.8%	5.1x
Tetra Tech	TTEK		NR			$ 26.04	$32.00	$14.20	$ 1,607	$ 2,145	1.02	*1.24*	*1.42*	18.6x	19.4x	0.0%	2.8x
Water Resources/ Infrastructure Average														23.1x	21.2x	0.3%	3.1x

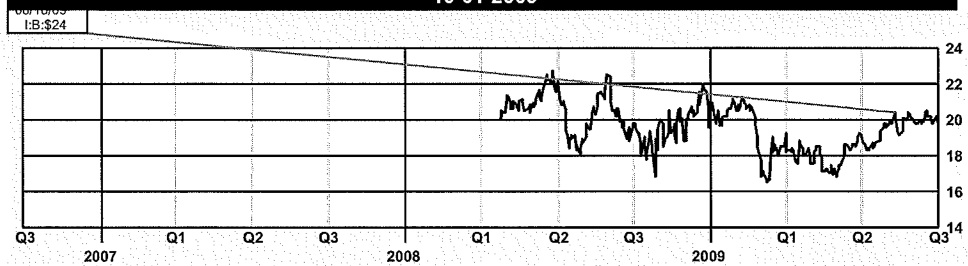
Relevant Indices		Share Price
Dow Jones Industrials	DJ30	$ 9,712.28
S&P 500	SPX	$ 1,057.08
Nasdaq Composite	NDX	$ 1,718.99

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.

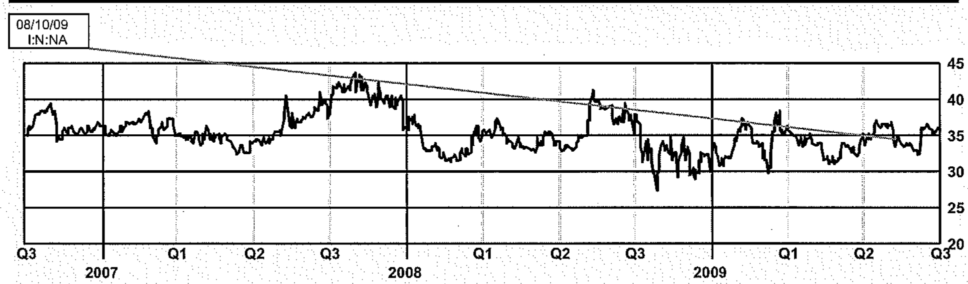
Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

Rating and Price Target History for: American Water Works Company, Inc. (AWK) as of 10-01-2009



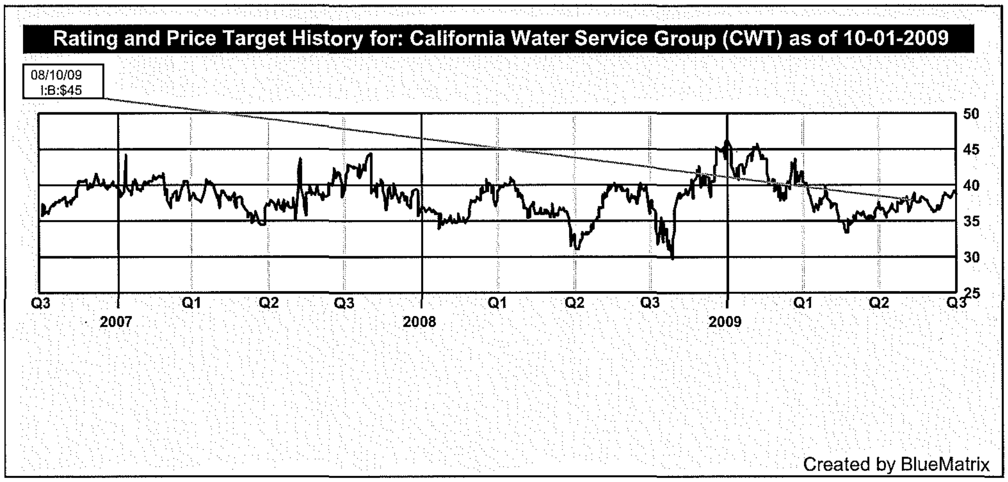
Created by BlueMatrix

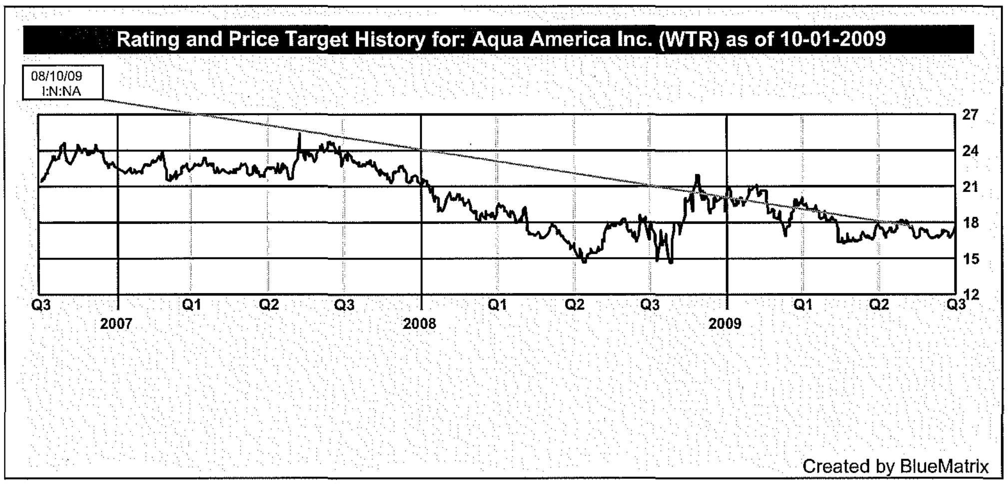
Rating and Price Target History for: American States Water Company (AWR) as of 10-01-2009



Created by BlueMatrix

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com





APPENDIX

IMPORTANT DISCLOSURES

REGULATION ANALYST CERTIFICATION ("REG AC"): The Research Analyst(s) who prepared this research report hereby certifies that the views expressed in the research report accurately reflect the analyst(s) personal views about the subject companies and their securities. The Research Analyst(s) also certifies that the Analyst(s) have not been, are not, and will not be receiving direct or indirect compensation for expressing the specific recommendation(s) or view(s) in this report.

Covered Companies Mentioned In This Report:

American Water Works Company, Inc.	AWK	$19.77	Buy
American States Water Company	AWR	$36.18	Neutral
California Water Service Group	CWT	$38.94	Buy
Aqua America Inc.	WTR	$17.64	Neutral

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

GENERAL DISCLOSURES: Longbow Securities does not make a market in any securities, nor does it hold a principal position in any security. However, any officer, director or stockholder of Longbow Securities or any member of their families may have a position in and may from time to time purchase or sell any of the securities mentioned or any related securities. Security prices in this report may either reflect the previous day's closing price or an intraday price, depending on the time of distribution. Consensus estimates are derived from either Thomson/Reuters, Bloomberg or Baseline. Designated trademarks and brands are the property of their respective owners.

SPECIFIC DISCLOSURES:

- Longbow Securities does not make a market in the securities of any company mentioned in this Report, and is not a market-maker in any securities generally. Nor does the firm does hold a principal position in any security.
- As of the date of this Report, no officer, director or stockholder of Longbow Securities, or any member of their immediate families, holds securities of any company mentioned in the Report. In the event such persons purchase, hold or sell securities of a company mentioned in the Report for their own account, any subsequent Report shall disclose the fact of any such ownership or transactions.
- No employee of Longbow Securities serves on the Board of Directors of the subject security or any other security mentioned in this report.
- Neither the Research Analyst nor a member of the Research Analyst's household has a financial interest in the securities of the subject company or any other security mentioned in this report.
- Neither the Research Analyst nor a member of the Research Analyst's household serves on the Board of Directors of the subject company or any other security mentioned in this report.
- Neither Longbow Securities nor its affiliates beneficially own 1% or more of an equity security of the subject company or any other security mentioned in this report.

RATINGS DISTRIBUTIONS FOR LONGBOW RESEARCH:

Rating Category	Count	Percent
Buy	58	28.4%
Neutral	138	67.6%
Sell	8	3.9%

RATING SYSTEM:

"Buy" means that Longbow Securities expects total return to exceed 20% over a 12-month period.

"Neutral" means that Longbow Securities expects total return to be within a range of plus or minus 20% over a 12-month period.

"Sell" means that Longbow Securities expects total return to be negative by greater than 20% over a 12-month period.

Longbow Research's full research universe and related applicable disclosures can be obtained by calling (216) 986-0700 or via postal mail at: Editorial Department, Longbow Research, 6000 Lombardo Center, Suite #500, Independence, Ohio 44131.

DISCLAIMER: The information, opinions, estimates and projections contained in this report were prepared by Longbow Securities LLC, a wholly owned subsidiary of Longbow Research LLC, and constitute the current judgment of Longbow Securities as of the date of this report. Additional information may be available from Longbow Securities upon request. The information contained herein is believed to be reliable and has been obtained from sources believed to be reliable, but Longbow Securities makes no representation or warranty, either expressed or implied, as to the accuracy, completeness or reliability of such information. Longbow Securities does not undertake, and has no duty, to advise you as to any information that comes to its attention after the date of this report or any changes in its opinion, estimates or projections. Prices and availability of securities are

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

also subject to change without notice. By accepting this report, the reader acknowledges that the report does not purport to meet the objectives or needs of specific investors, and, accordingly, constitutes only "impersonal advisory services" as that term is defined in Rule 204-3 under the Investment Advisers Act of 1940 and that any advice in this report is furnished solely through uniform publications distributed to subscribers thereto within the meaning of Section 2(a)(20)(i) of the Investment Company Act of 1940. The securities discussed in Longbow Research reports may be unsuitable for some investors depending on their specific investment objectives, financial status, risk profile, or particular needs. Investors should consider this report as only a single factor in making their investment decisions and should not rely entirely on this report in evaluating whether or not to buy or sell the securities of the subject company. Longbow Research archives and reviews outgoing and incoming email. Such may be produced at the request of regulators. Sender accepts no liability for any errors or omissions arising as a result of transmission. Use by other than intended recipients is prohibited.

DESCRIPTION: Longbow Securities LLC, a wholly owned subsidiary of Longbow Research LLC, is a primary research provider established in 2003 and headquartered at 6000 Lombardo Center, Suite 500, Independence, Ohio 44131 USA. The company provides research services to institutional investors, investment advisers, and professional money managers. MEMBER FINRA/SIPC. Additional information supporting the statements in this report is available upon request.

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

LONGBOW Research
Tactical advantage through independent research

Industry Update

October 12, 2009

Analysts:
GARIK SHMOIS
T: 216-525-8414
E: gshmois@longbowresearch.com

VISHAL KHETRIWAL, CFA
T: 216-525-8469
E: vkhetriwal@longbowresearch.com

Industry: **WATER UTILITIES**

Coverage:

Ticker	Rating	Price
AWK	BUY	$19.79
AWR	NEUTRAL	$36.80
CWT	BUY	$39.55
WTR	NEUTRAL	$16.61

Water Utilities: Capex Implications for Earnings Growth

- In the following report, we analyze the portion of increase in PP&E that our covered water utilities will finance through equity. The analyses further supports our thesis that increased capex over the next three years will support earnings growth of 8-10% vs. flattish earnings growth over the past three years.
- We see the water utilities under coverage recognizing approximately 5% earnings growth annually from capex investment alone. We believe the remainder of the 8-10% earnings growth should come from improved ROEs.
- Though capital investment need, as outlined by the EPA, is broadly distributed among states along their share of the total U.S. population, we notice states with progressive regulatory environment have a slightly lower need relative to their population. For AWK, at least 18% of their revenues come from states with a higher need for capital investment relative to its population while for WTR, 31% does.
- AWK and WTR are growing their operation in southern states, which have higher population growth rates. This offers further upside through higher organic growth. WTR should also see additional benefit over the next two to three years as the lower ROE (2-5%) earned in southern states catches up to the allowed maximum (9-11%).
- The share of investment needed (19%) in smaller systems is disproportionate to the population served by them (9%). This could be a positive for larger publicly traded utilities that look to acquire small systems, either privately held or municipally owned, that are in need of infrastructure investment. Larger systems are well maintained by comparison.

IMPORTANT DISCLOSURES ARE LOCATED IN THE APPENDIX.

Table of Contents

INTRODUCTION

In the following report, we examine the investment need for water infrastructure in the U.S. and take a closer look at the need by state, project type, and system size. Note that we have not analyzed wastewater infrastructure need in this report because these services are a very small portion of business for our covered water utilities. We also dig deeper into the capex by our covered water utilities and analyze the funding sources for their capex programs and its impact their earnings growth.

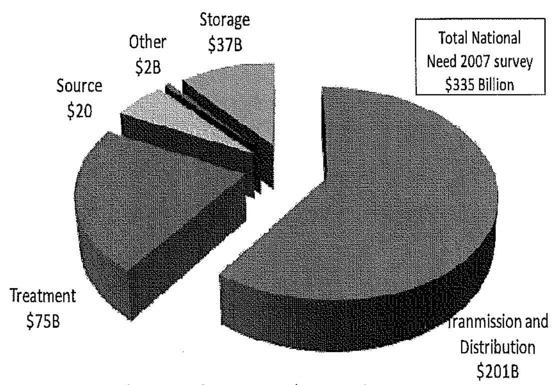
The U.S. Environmental Protection Agency (EPA) is under a government mandate to conduct a water infrastructure needs survey every four years. The results of this survey are used to allot money from the Drinking Water State Revolving Fund (DWSRF), which is a federal program that provides low-interest loans to water systems for infrastructure investment. The EPA survey only takes into consideration types of projects that are eligible for DWSRF funding, including installation of new infrastructure and rehabilitation, expansion, or replacement of existing infrastructure. Projects such as raw water dams and reservoirs, projects related to population growth, and water system O&M costs are not included in the survey. According to the 2007 survey, $335B needs to be invested by the water utilities between 2007 and 2026 to maintain the quality of service provided to existing customers.

It is interesting that the investment need associated with compliance with Safe Drinking Water Act (SDWA), which regulates the quality of water provided by the utilities, is relatively small at 16% of the projected $335B total. We view this is a positive as compliance driven spending, that is non-discretionary, causes increased regulatory lag (delay in obtaining rate increases) for publicly-traded utilities as they are often unable to time the spending around rate cases.

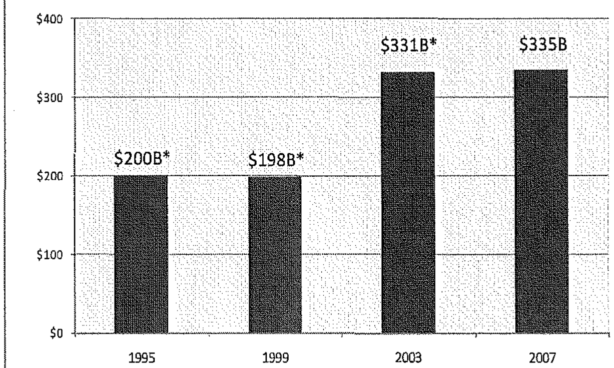
INFRASTRUCTURE NEEDS BY PROJECT TYPE

As seen in the pie chart below, 60% of the spending is needed for transmission and distribution, and another 22% is needed for treatment. This could benefit companies such as a) Watts Water (WTS, NR) and Pentair (PNR, NR), that manufacture water repair and related equipment, b) Insituform (INSU, NR), that contracts for rehabbing underground water pipes, and c) Tetra Tech (TTEK, NR), that provides engineering and consulting for water infrastructure projects.

Total 20-Year Water Infrastructure Investment by Project Type	Change in 20 –Year Water Infrastructure Investment Need in Four Successive EPA Surveys



Source: 2007 EPA Drinking Water Infrastructure Needs Survey and Assesment.



Source: 2007 EPA Drinking Water Infrastructure Needs Survey and Assesment.
* The amounts are reported in January 2007 Dollars

INFRASTRUCTURE NEEDS BY STATE

The investment need is broadly distributed among states along their share of the total U.S. population. We offer a table below outlining the infrastructure needs of important states to our covered companies.

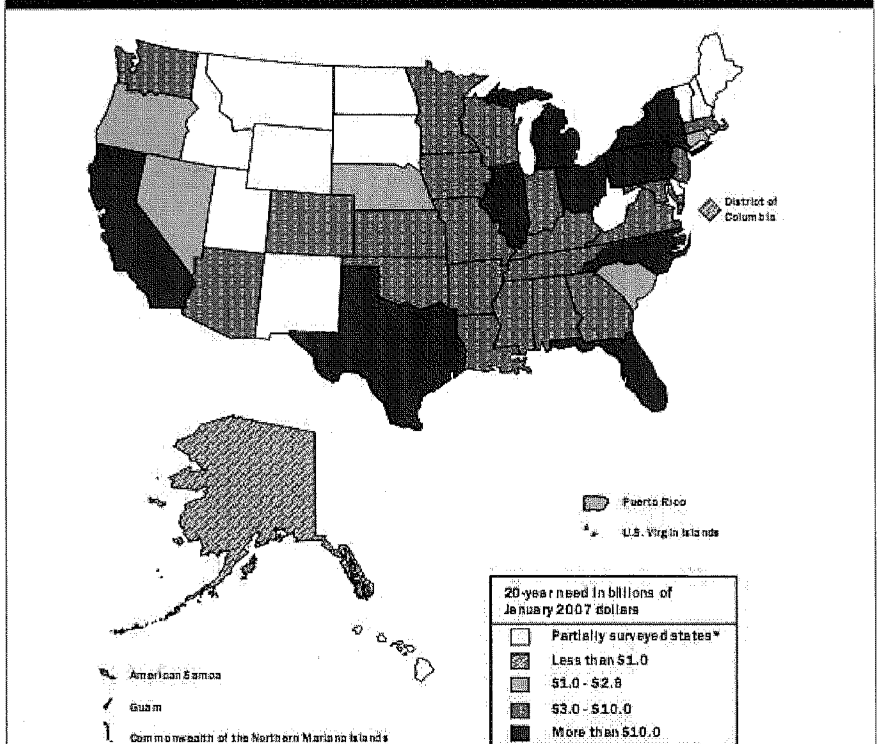
Key takeaways include:

- It is worth noting that NJ and PA, states with large presence for AWK and WTR, have a slightly lower need relative to their population even though they have older infrastructure compared to southern states. We believe this may be a result of more progressive regulatory environment in these states that encourages investment. Another reason could be the large presence of AWK and WTR in the states. These companies are better at keeping their infrastructure upgraded relative to municipal utilities.
- WTR's exposure to NY and TX should be a long-term positive for the company. NY has one of the highest infrastructure need relative to its population (1.3x), signaling a poor state of its infrastructure and giving WTR the opportunity of make investment going forward. TX on the other hand has one of the largest investment needs in the country, giving WTR a good platform for further acquisitions.
- 27% of the $335B is needed in seven states where AWK's has its largest presence. The corresponding number for WTR is 34%.
- AWK and WTR are growing their operation in southern states, which have higher population growth rates. This offers further upside through higher organic growth. WTR should also see additional benefit over the next two to three years as the lower ROE (2-5%) earned in southern states catches up to the allowed maximum (9-10%).

Infrastructure Need by State								
	% of Revenue from the state						% of Total U.S.	
State	AWK	WTR	CWT	AWR	Infra. Need	% of total Need	Population in the State	Need vs. Population
NJ	25.5%	4.7%			$8B	2.5%	2.8%	0.87
PA	20.9%	52.8%			$11.4B	3.5%	4.1%	0.86
MO	9.1%				$7.1B	2.2%	1.9%	1.14
IL	9.0%	6.6%			$15B	4.6%	4.2%	1.10
IN	7.4%				$5.9B	1.8%	2.1%	0.88
CA	6.3%		94.4%	77.7%	$39B	12.0%	12.0%	1.00
WV	5.3%				$1B	0.3%	0.6%	0.52
TX		8.2%			$26.1B	8.0%	7.8%	1.03
OH		6.7%			$12.6B	3.9%	3.8%	1.03
NC		5.6%			$10.1B	3.1%	3.1%	1.01
NY		4.3%			$27.1B	8.3%	6.3%	1.32
Total	**83.5%**	**88.9%**	**94.4%**	**77.7%**		50.3%	48.6%	

Source: Company Reports, EPA, U.S. Census

Infrastructure Need by State



Source: EPA

INFRASTRUCTURE NEEDS BY SYSTEM SIZE

As seen in tables below, the investment needed in smaller systems (19%) is disproportionate to the population served by them (9%). This is a positive for larger publicly traded utilities that seek to acquire small systems in need of infrastructure investment. We believe that the continued underinvestment in smaller systems should increase the pace of consolidation in the sector as cash-strapped municipalities consider privatization instead of increasing their financial burden to make necessary upgrades to their water systems. We note that both WTR and AWK make on average at least 10 small acquisitions every year.

Investment Need by System Size

	Investment Needed		Systems		Population Served	
System Size	$B	% of Total	# of Systems	% of Water Systems	Population	% of Total Population
Large (>100,00 persons)	$116B	36%	584	1%	129M	45%
Medium (3,301 - 100,000 persons)	$124B	45%	8,749	17%	131M	46%
Small (<3,300 persons)	$59B	19%	41,748	82%	24M	9%

Source: EPA

AWK Small Acquisitions

Year	# of Systems	Transaction Value ($ mil)
1996	13	$36.9
1997	9	2.9
1998	22	47.2
1999	21	12..4
2000	12	52.1
2001	10	56.3
2002	9	31.9
2003	10	4.6
2004	8	1.9
2005	7	5.0
2006	11	12.5
2007	8	18.0
2008	10	12.5
TOTAL	150	$281.8

Source: Company Reports

WTR Small Acquisitions

Year	2006	2007	2008	YTD 2009
# of Systems	27	26	9	9
Customers Added	17,549	24,000	10,000	4,200
Purchase Value (mil)	$12	$25	$17	$2

Source: Company Reports

CAPEX PROGRAMS FOR OUR COVERED WATER UTILITIES

Investing in capex is the only means for a regulated water utility to grow its earning. Regulators allow the utilities to earn a fixed rate of return on the equity portion of the capex. We view the portion of the capex equal to the depreciation as replacement capex. This replacement capex allows the utility to simply continue earning at its prior level. On the other hand, increase in PP&E (capex-depreciation) allows the utility to theoretically increase its earnings. Below we analyze the funding source for the increase in PP&E for our covered utilities, especially the portion that is funded though an increase in equity. Other sources of funds include debt and other assets/liabilities such as deferred taxes. We note that water utilities are reimbursed for the interest they pay for debt and usually do not earn a return on funds generated through change in other assets/liabilities.

American Water Works (AWK)

AWK - Source of Funds for Capex

	FY07	FY08	1H09	FY09E	FY10E	FY11E
Capex	**768.4**	**1,033.6**	**413.1**	**800.0**	**800.0**	**800.0**
Depreciation	265.8	311.4	162.2	274.5	308.4	322.7
Change in PP&E	502.6	722.2	250.9	525.5	491.6	477.3
Change in Tangible Equity (excl. Goodwill & Intangibles)	(519.5)	316.3	251.8	315.9	307.1	365.8
Change in Net Debt	903.5	294.3	93.6	82.4	180.0	110.0
Change in Other Assets & Lia.	118.6	111.6	(94.5)	127.2	4.5	1.6
% of PP&E Financed by Equity	**-103.4%**	**43.8%**	**100.4%**	**60.1%**	**62.5%**	**76.6%**
Avg. Equity/(Net Debt+Equity) (excl. Goodwill & Intangibles)	34.6%	30.7%	32.5%	33.3%	34.1%	36.1%

Source: Baseline

AWK increased its PP&E by $722M in FY08, a 44% increase over FY07. However, we believe that due to the adverse capital market conditions (including AWK's depressed share price), the company has scaled back its capex program in FY09. Even before the RWE acquisition in 2002, AWK had a lower equity/capital ratio compared to its peers (36-37% during FY97-00 for AWK vs. 44-47% for WTR, 57-60% for CWT, and 49% for AWR during FY07-09). To return to the 36-37% level from the current 32.5%, AWK has been funding a higher portion of its increase in PP&E through equity. As seen in the table above, the portion of increase in PP&E financed through equity varies based on the timing of new debt and equity issuance. While we believe investors are concerned that AWK will need to issue equity to reach a more typical 45-50% equity to cap requirement, prior historical levels indicate the potential degree of dilution as unfounded.

We are modeling $800M capex annually during FY09-11E, which we believe should increase its PP&E by ~$475-525M each year. This is broadly in line with the company's guidance. Assuming 65% equity funding for increase in PP&E, we estimate that AWK should be able to increase EPS by $0.07-0.10 annually (5-7%) just through its capex program. We note that for this calculation we have taken into consideration equity dilution ($0.09-0.10/share annually) caused by new equity issue and have used our expectation of AWK's ROE (8.7-9.7%) over the next three years. We believe that a relatively equal portion of earnings growth for the company will come from ROE improvement ($0.07-0.08/share annually).

California Water (CWT)

CWT - Source of Funds for Capex	FY06	FY07	FY08	Average ('06-'08)	FY09E	FY10E	FY11E
Capex	**114.4**	**101.3**	**107.8**	**107.9**	**110.0**	**110.0**	**110.0**
Dep. & Amor.	30.7	34.2	39.5	34.8	38.4	42.5	45.0
Change in PP&E	83.8	67.1	68.3	73.1	71.6	67.5	65.0
Change in Equity	84.4	7.4	13.7	35.2	21.9	37.2	35.0
Change in Net Debt	(32.4)	51.9	31.2	16.9	63.1	8.0	22.0
Change in Other Assets & Lia.	31.8	7.8	23.4	21.0	(13.3)	22.3	8.0
% of PP&E Financed by Equity	**100.7%**	**11.0%**	**20.1%**	**44.0%**	**30.5%**	**55.2%**	**53.8%**
Avg. Equity/(Net Debt+Equity)	57.4%	59.9%	56.9%	58.1%	54.9%	53.9%	54.0%

Source: Baseline

As seen in the table above, the portion of increase in PP&E financed through equity varies based on the timing of new debt and equity issuance (101% in FY06 vs. 11% in FY07). We expect annual capex of ~$110 during FY09-11E, which should increase its PP&E by ~$65-70M each year. Assuming an average 45% equity funding, we estimate CWT can increase EPS by $0.08 annually (or 3.7% CAGR) over FY10E-11E just through its capex program. We note that for this calculation we have taken into consideration equity dilution ($0.10-0.11/share) caused by new equity issue and have used our expectation of CWT's ROE (10.7-11.7%) over the next three years. We see additional growth of ~$0.03/share in FY10E coming from a 10bp ROE improvement and ~$0.19/share in FY11E from a 90bp improvement. Generally, we expect ROE improvement in FY11 due to new rates that will be implemented in Jan, 2011 for all 24 districts and headquarters.

American States Water (AWR)

AWR - Source of Funds for Capex	FY06	FY07	FY08	Average ('06-'08)	FY09E	FY10E	FY11E
Capex	**66.6**	**49.9**	**77.0**	**64.5**	**75.0**	**75.0**	**75.0**
Dep. & Amor.	26.3	28.9	31.6	28.9	43.6	39.5	37.9
Change in PP&E	40.3	21.0	45.5	35.6	43.6	39.5	37.1
Change in Equity	19.6	18.4	8.4	15.5	37.3	20.8	23.3
Change in Net Debt	14.2	6.1	31.3	17.2	(15.8)	20.0	17.0
Change in Other Assets & Lia.	6.5	(3.5)	5.8	2.9	22.1	(1.3)	(3.1)
% of PP&E Financed by Equity	**48.6%**	**87.6%**	**18.5%**	**51.6%**	**85.5%**	**52.7%**	**62.6%**
Avg. Equity/(Net Debt+Equity)	48.6%	49.4%	49.0%	49.0%	51.0%	53.8%	54.0%

Source: Baseline

We expect annual capex of ~$75 during FY09-11E, which should increase its PP&E by ~$35-45M each year. Assuming an average 65% equity funding, we believe AWR can increase its EPS by $0.05 in FY10E (3%) and $0.11 in FY11E (6%) just through its capex program. We note that for this calculation we have taken into consideration equity dilution ($0.05/share in FY10E & $0.11/share in FY11E) caused by new equity issue and have used our expectation of AWR's ROE (9.4-10.2%) over the next three years. We think additional growth should come from ROE improvement – 20bp in FY10E leading to a $0.05/share increase and 40bp in FY11E leading to ~$0.12/share increase.

Aqua America (WTR)

WTR - Source of Funds for Capex	FY06	FY07	FY08	Average ('06-'08)	FY09E	FY10E	FY11E
Capex	**271.7**	**238.1**	**267.4**	**259.1**	**315.0**	**315.0**	**290.0**
Dep. & Amor.	75.0	88.0	94.3	85.8	110.9	117.9	124.8
Change in PP&E	196.7	150.1	173.1	173.3	204.1	197.1	165.2
Change in Equity	109.7	54.7	82.1	82.2	54.7	73.4	66.5
Change in Net Debt	(90.8)	342.6	39.5	97.1	67.9	105.0	70.0
Deferred Income Tax	10.8	22.0	45.8	26.2	40.0	10.0	10.0
Change in Other Assets & Lia.	167.0	(269.2)	5.7	(32.2)	41.6	8.6	18.7
% of PP&E Financed by Equity	**55.8%**	**36.4%**	**47.5%**	**46.6%**	**26.8%**	**37.3%**	**40.2%**
Avg. Equity/(Net Debt+Equity)	46.8%	46.4%	43.9%	45.7%	45.0%	45.9%	45.9%

Source: Baseline

Apart from increase in PP&E, the large debt increase in FY07 of $342M was used to fund acquisitions and "additions to funds restricted for construction activity". We expect annual capex of ~$290-315 during FY09-11E, which should increase PP&E by ~$165-200M each year. Assuming an average 35% equity funding, WTR should be able to increase EPS by $0.03-0.05 annually (5% average) over the next three years just through its capex program. We note that for this calculation we have taken into consideration modest equity dilution ($0.01/share annually) caused by new equity issue and have used our expectation of WTR's ROE (9.9-11.4%) over the next three years. Additional growth should come from ROE improvement ($0.05-0.08/share annually).

INVESTMENT THESIS

AWK

We rate American Water Works Company, Inc. (AWK) with a BUY with a $24 target price, as we see AWK as offering an attractive risk/reward with positive catalysts relative to the peer group. We believe AWK shares are discounting RWE's anticipated exit as the former parent company has announced plans to sell its remaining stake in AWK. While the timing of this cannot be predicted, we believe AWK's discounted valuation by investors is overdone. The shares are trading at 13.2x our FY10E EPS, relative to a peer group average of 18.9x. We also believe there is also an opportunity for multiple expansion toward the peer group average of once the RWE overhang abates. However, our target price still incorporates a 15% discount to the peer group average.

CWT

We rate California Water Service Group (CWT) as a BUY with a $45 target price, which represents 20.5x our FY10E EPS of $2.20, in line with the company's historical average. We like CWT's position in the regulatory favorable California market. Furthermore, CWT's $100-120M in FY09E capex could potentially drive meaningful EPS growth in the next two to three years. On valuation, CWT shares are trading at 18x our FY10E EPS of $2.20, which we believe to be conservative when compared to the industry average of 18.9x and the company's historical average of 20.5x. Additionally, while CWT has historically seen higher earnings volatility from variation in water consumption, recent regulatory changes in California (WRAM and MBCA implementation) should help reduce earnings volatility and provide better visibility. In summation, rate relief and improved ROE (we are modeling 10.8%) in FY10E, greater than the company's 8.9% five-year average, provide positive potential catalysts going forward.

WTR

We rate Aqua America, Inc. (WTR) as a NEUTRAL. Frankly, we see downside risk to WTR as fairly limited as the company is trading at an 8% discount to its historical forward P/E of 23x. Additionally, at 2.6x price-to-book, it is trading below its average 2.9x ratio (on book value of $7.91/share). Compared to the peer group, we see WTR's valuation as reasonable given the company's size and operational efficiency (O&M ratio is industry leading). We believe this justifies WTR as a proxy play on the water utilities space. However, despite the slight discount the shares are trading relative to historical averages, we see the potential upside relative to our preferred names of CWT and AWK as lower.

Overall, we like WTR's position as one of the leading publicly traded water utility serving approximately three million people in 13 states. The water utilities industry is highly regulated, but also fragmented, which presents opportunities for acquisitive growth, especially as cash strapped municipalities and smaller private participants look to raise cash to weather the current economic downturn by potentially selling off water systems. More important, we expect 2009 and 2010 to be catch-up years for rate increases. $64.7M and $27.4M in rate increases were approved in 2008 and 2009 YTD, respectively, and $58.9M in increases are either pending or will be filed in the remainder of 2009. Additionally, WTR has surcharges in six of its 13 states of operations, which allows the company to start earning a return on its investment between rate increases. These factors, coupled with lower equity dilution from increased operating cash flow generation, should accelerate the pace of EPS growth in the next three years. We see WTR's estimated earnings growth of 11.3% from FY09E to FY11E outpacing the flat growth from FY05 to FY08.

AWR

We rate American States Water Company (AWR) as a NEUTRAL, as we see the upside potential related to rate relief as already largely reflected in the shares. At 19.3x our FY10E EPS of $1.91, AWR shares are trading broadly in line to its historical 20x forward P/E average as well as to the peer group average of 18.9x. While we argue that a valuation premium is justified given the company's concentration in the regulatory-favorable California market, given the company's valuation relative to our preferred names in the space – AWK and CWT – we do not see as much upside potential at this time from current levels.

A principal driver of earnings growth would be the start-up of the Ft. Bragg, North Carolina construction project and successful price redeterminations at other military bases, which we estimate could increase EPS by another 3%. However, due to limited visibility, we have not added these potential catalysts into our EPS forecasts. Our estimates do, however, include an average ROE of 9.8% from FY09E to FY11E vs. the company's historical 8.7% average. This is driven by increased capital spending of $75-80M in FY09, in line with FY08 levels. Since capex has grown at a CAGR of 12% from 2003-2008, AWR should see rate relief leading to 14% EPS growth in FY09E and potentially 7.5% in FY10E. In the long term, we like AWR, currently the fourth largest publicly traded domestic water utility, as the WRAM/MBCA implementation in California should remove the quarterly earnings volatility caused by the changes in water consumption. We note that seasonal variation will still exist. These mechanisms have somewhat reduced the single-state operational risk that AWK faced previously. However, we believe benefits from the improved regulatory environment and earnings upside from recently approved rate cases are already mostly priced into the shares

VALUATION

AWK

AWK shares closed yesterday at $19.79, which is 15.4x our FY09E EPS of $1.29 and 13.2x our FY10E EPS of $1.50. The shares are trading at a discount to the peer group average of 18.9x FY10E EPS due in large part to the RWE overhang, which we believe the Street is already accounting for. The shares are trading at 1.2x tangible book value compared to a peer group that trades over 1.7x, on average. Our target price of $24 is based on 16.0x our FY10E EPS, a valuation that remains at a discount to the peer group. However, we see multiple expansion from current levels as justified given AWK being viewed as the largest and most diversified publicly traded water utility in the U.S. and with the potential from earnings growth as the company catches up to insufficient rate increases during the past five-to-six years.

CWT

CWT shares closed yesterday at $39.55, which is 18.6x our FY09E EPS of $2.12 and 18x our FY10E EPS of $2.20. The shares are trading at a discount to the company's historical normalized 20.5x average and normalized range of 17-27x forward P/E. Compared to CWT's water utility peers, the company trades at a discount, although this has narrowed as more predictable earnings streams from the implementation of WRAM and MCBA has removed some the unpredictability in earnings associated with the company's extensive geographic presence in California.

AWR

At 19.3x our FY10E EPS of $1.91, AWR shares are trading broadly in line to its historical 20x forward P/E average as well as to the peer group average of 18.9x. While we argue that a valuation premium is justified for AWR given the company's concentration in the regulatory-favorable California market, should multiples expand, a fair value of $38/share does not imply the same amount of potential upside as do our preferred names in the space – AWK and CWT. AWR shares closed Wednesday at $36.80, which is 20.7x our FY09E EPS of $1.78 and 19.3x our FY10E EPS of $1.91. The shares are trading at a discount to the company's historical 20x average and a normalized range of 18-28x forward P/E.

WTR

Despite the slight discount the shares are trading relative to historical averages, we see the potential upside relative to our preferred names of CWT and AWK as less attractive. WTR shares closed yesterday at $16.61, which is 21.1x our FY09E EPS of $0.79 and 18.4x our FY10E EPS of $0.91. The shares are trading at a discount to the company's historical 23x average and normalized range of 20-30x forward P/E.

RISKS

AWK

The potential downside risks to our investment thesis include, but are not limited to: 1) delays in rate case processing or lower rate increases by the regulators than our expectations, 2) 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, 4) a large acquisition at an excessive valuation (significantly above the rate base), and 5) a large goodwill impairment which could lead to a breach of debt covenants or regulatory requirements.

CWT

Potential downside risks to our investment thesis include, but are not limited to: 1) lower rate increase approvals by the California Public Utility Commission (CPUC) than our expectation, 2) near-term run up in raw material costs, and 3) large acquisition(s) at excessive valuation(s) (significantly above the rate base).

AWR

The potential downside risks to our investment thesis include, but are not limited to: 1) lower rate increase approvals by the California Public Utility Commission (CPUC) than our expectation, 2) increases in raw material costs, and 3) an acquisition of a large water system by the local government through eminent domain.

The potential upside risks to our investment thesis include, but are not limited to: 1) favorable rate case approvals, and 2) the commencement of the large "special" construction project at Ft. Bragg, North Carolina, or any other base.

WTR

Potential downside risks to our investment thesis 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 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.

American Water Works— Quarterly Income Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09E	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E
Regulated Segment	419.3	508.6	571.9	487.8	449.9	527.1	603.7	502.1	497.4	554.9	638.7	547.0	524.2	605.7	700.4	592.3
% Increase			7.3%	11.2%	7.3%	3.6%	5.6%	2.9%	10.6%	5.3%	5.8%	8.9%	5.4%	9.2%	9.7%	8.3%
Non-Regulated Revenue	53.3	55.5	66.4	67.5	61.0	67.0	73.9	70.3	57.5	64.2	70.9	67.3	63.3	70.6	78.0	74.1
% Increase			0.4%	27.7%	14.4%	20.8%	9.4%	4.1%	-5.7%	-4.2%	-4.1%	-4.3%	10.0%	10.0%	10.0%	10.0%
Other	(4.0)	(5.4)	(5.1)	(1.5)	(4.1)	(4.7)	(5.4)	(3.9)	(4.7)	(6.3)	(6.4)	(5.5)	(5.2)	(6.1)	(7.0)	(5.9)
% Regulated Rev	-1.0%	-1.1%	-0.9%	-0.3%	-0.9%	-0.9%	-0.9%	-0.8%	-1.0%	-1.1%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%
Operating revenues	**468.5**	**558.7**	**633.1**	**553.8**	**506.8**	**589.4**	**672.2**	**568.6**	**550.2**	**612.7**	**703.1**	**608.8**	**582.3**	**670.3**	**771.4**	**660.4**
Operation and maintenance	282.6	299.4	328.3	336.2	311.3	330.6	342.2	319.8	314.4	330.6	357.3	344.1	329.0	361.9	382.9	359.6
Depreciation and amortization	64.6	68.1	69.7	64.9	63.9	67.3	68.4	71.6	68.8	73.2	73.2	73.2	74.8	76.4	77.9	79.5
General taxes	47.9	45.9	47.1	42.3	52.1	49.6	49.4	48.0	52.5	51.7	49.3	50.6	54.5	52.0	52.0	50.6
Loss (gain) on sale of assets	0.1	(6.2)	(0.7)	(0.5)	(0.1)	(0.8)	0.5	(0.0)	(0.2)	0.0	(0.3)	(0.3)	(0.3)	(0.3)	(0.3)	(0.3)
Impairment charges			243.3	266.0	750.0				450.0							
EBIT	**73.3**	**151.5**	**(54.6)**	**(155.1)**	**(670.4)**	**142.7**	**211.8**	**129.1**	**(335.4)**	**157.2**	**223.6**	**141.3**	**124.3**	**180.3**	**258.8**	**171.0**
Operating Margin (excluding impairment)	*16%*	*27%*	*30%*	*20%*	*16%*	*24%*	*32%*	*23%*	*21%*	*26%*	*32%*	*23%*	*21%*	*27%*	*34%*	*26%*
Interest	72.2	70.8	68.739	71.5	70.0	70.1	72.7	72.4	72.0	73.7	74.4	75.2	76.2	77.2	78.2	79.2
Other income, net	(3.0)	(1.9)	(2.9)	(4.6)	(3.7)	(3.1)	(6.7)	(8.0)	(4.8)	(2.6)	(5.5)	(5.2)	(4.6)	(4.5)	(5.0)	(4.8)
Total other income (deductions)	**69.2**	**68.9**	**65.8**	**66.8**	**66.2**	**67.0**	**66.0**	**64.5**	**67.1**	**71.1**	**68.9**	**70.0**	**71.7**	**72.7**	**73.2**	**74.4**
EBT	**4.2**	**82.6**	**(120.5)**	**(221.9)**	**(736.6)**	**75.7**	**145.8**	**64.6**	**(402.5)**	**86.1**	**154.8**	**71.3**	**52.6**	**107.5**	**185.6**	**96.6**
Provision for income taxes	1.7	32.648	39.7	12.7	(4.1)	30.2	57.5	28.2	10.6	34.1	61.3	28.2	20.8	42.5	73.3	38.2
Implied Tax Rate (excl. goodwill impairment)	42%	40%	32%	29%	-31%	40%	39%	44%	22%	39.6%	39.6%	39.6%	39.5%	39.5%	39.5%	39.5%
Income (loss) from continuing operations	**2.4**	**50.0**	**(160.2)**	**(234.6)**	**(732.5)**	**45.5**	**88.2**	**36.4**	**(413.1)**	**52.0**	**93.4**	**43.0**	**31.9**	**65.1**	**112.3**	**58.4**
Loss (income) from discontinued operations, net of tax	(0.26)	0.81	0.00	0.00												
Net income (loss)	**2.7**	**49.2**	**(160.2)**	**(234.6)**	**(732.5)**	**45.5**	**88.2**	**36.4**	**(413.1)**	**52.0**	**93.4**	**43.0**	**31.9**	**65.1**	**112.3**	**58.4**
Diluted EPS from continuing operations	0.02	0.31	(1.00)	(1.47)	(4.58)	0.28	0.55	0.23	(2.58)	0.32	0.54	0.25	0.18	0.37	0.62	0.32
EPS excl. impairment & one-time expenses	**0.02**	**0.31**	**0.52**	**0.17**	**0.11**	**0.28**	**0.55**	**0.23**	**0.19**	**0.32**	**0.54**	**0.25**	**0.18**	**0.37**	**0.62**	**0.32**
Diluted Average Shares	160.0	160.0	160.0	160.0	160.0	159.9	160.0	159.9	159.9	164.8	174.4	174.4	175.6	177.8	180.0	182.2
Financial Summary																
Total Revenue growth			6.8%	12.4%	8.2%	5.5%	6.2%	2.7%	8.6%	4.0%	4.6%	7.1%	5.8%	9.4%	9.7%	8.5%
Non-Regulated Revenue growth			0.4%	27.7%	14.4%	20.8%	11.3%	4.1%	-5.2%	-4.5%	5.0%	5.0%	10.0%	10.0%	10.0%	10.0%
O&M/Revenue	60.3%	53.6%	51.9%	60.7%	61.4%	56.1%	50.9%	56.2%	57.1%	54.0%	50.8%	56.5%	56.5%	54.0%	49.6%	54.4%
General Taxes/ Regulated Revenue	11.4%	9.0%	8.2%	8.7%	11.6%	9.4%	8.2%	9.6%	10.6%	9.3%	7.7%	8.9%	10.4%	8.6%	7.4%	8.6%
Adj. EBITDA	137.9	219.6	258.4	175.8	143.6	210.0	280.2	200.7	183.5	230.4	296.8	214.5	199.1	256.6	336.8	250.5
EPS growth, excluding goodwill impairment charge					620.8%	-8.9%	6.0%	34.0%	73.6%	10.9%	-2.8%	8.3%	-4.5%	16.0%	16.5%	30.0%

Source: Company reports, Longbow estimates

American Water Works— Annual Income Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	FY04A	FY05A	2006A	FY07A	FY08A	FY09E	FY10E	FY11E
Regulated Segment	1748.0	1836.1	1854.6	1987.6	2082.7	2237.9	2422.6	2594.8
% Increase		5.0%	1.0%	7.2%	4.8%	7.4%	8.3%	7.1%
Non-Regulated Revenue	290.0	310.8	248.5	242.7	272.2	259.9	285.9	314.5
% Increase		7.2%	-20.0%	-2.3%	12.2%	-4.5%	10.0%	10.0%
Other	-20.17	(10.1)	(10.0)	(16.0)	(18.0)	(22.9)	(24.2)	(25.9)
% Regulated Rev	-1.2%	-0.6%	-0.5%	-0.8%	-0.9%	-1.0%	-1.0%	-1.0%
Operating revenues	**2,017.9**	**2,136.7**	**2,093.1**	**2,214.2**	**2,336.9**	**2,474.9**	**2,684.3**	**2,883.4**
Production costs	248.5	262.6	264.4	278.1	288.6	299.5	316.7	337.4
Employee-related costs	407.7	408.8	446.2	463.4	505.6	529.6	574.4	614.2
Operating supplies and services	289.3	338.1	268.2	293.5	283.2	297.0	316.7	337.4
Maintenance materials and services	90.6	97.9	96.5	128.0	136.3	131.2	128.8	129.8
Customer billing and accounting	42.5	44.4	55.6	38.3	44.0	42.1	45.6	49.0
Other	43.4	49.8	43.6	45.3	46.1	47.0	51.0	54.8
Operation and maintenance	1122.0	1201.6	1174.5	1246.5	1303.8	1346.3	1433.4	1522.4
Depreciation and amortization	225.3	261.4	259.2	267.3	271.3	288.5	308.6	322.7
General taxes	170.2	183.3	185.1	183.3	199.1	204.1	209.1	214.1
Loss (gain) on sale of assets	(8.6)	(6.5)	0.1	(7.3)	(0.4)	(0.8)	(1.2)	(1.2)
Impairment charges	78.7	385.4	221.7	509.3	750.0	450.0	0.0	0.0
EBIT	**430.4**	**111.6**	**252.5**	**15.1**	**(186.9)**	**186.7**	**734.3**	**825.3**
Operating Margin (excluding impairment)	*25%*	*23%*	*23%*	*24%*	*24%*	*25.7%*	*27.4%*	*28.6%*
Interest	315.9	345.3	366.0	283.2	285.2	295.29	310.74	324.55
Other income, net	(11.0)	(9.5)	(4.5)	(12.5)	(21.5)	(18.2)	(18.8)	(19.0)
Total other income (deductions)	**305.0**	**335.7**	**361.5**	**270.6**	**263.7**	**277.1**	**291.9**	**305.6**
EBT	**125.4**	**(224.2)**	**(108.9)**	**(255.5)**	**(450.6)**	**(90.35)**	**442.4**	**519.8**
Provision for income taxes	66.3	51.0	46.9	86.8	111.8	134.3	174.7	205.3
Implied Tax Rate (excl. goodwill impairment)	32.5%	31.6%	41.6%	34.2%	37.3%	37.3%	39.5%	39.5%
Income (loss) from continuing operations	**59.1**	**(275.1)**	**(155.9)**	**(342.3)**	**(562.4)**	**(224.6)**	**267.7**	**314.5**
Loss (income) from discontinued operations, net of tax	124.0	49.9	6.4	0.6				
Net Income (loss)	**(64.9)**	**(325.0)**	**(162.2)**	**(342.8)**	**(562.4)**	**(224.6)**	**267.7**	**314.5**
Diluted EPS from continuing operations	0.37	(1.72)	(0.97)	(2.14)	(3.52)	(1.33)	1.50	1.67
EPS excl. impairment & one-time expenses	**0.86**	**0.69**	**0.41**	**1.04**	**1.17**	**1.29**	**1.50**	**1.67**
Diluted Average Shares	160.0	160.0	160.0	160.0	160.0	168.4	178.9	188.1
Financial Summary								
Total Revenue growth		5.9%	-2.0%	5.8%	5.5%	5.9%	8.5%	7.4%
Non-Regulated Revenue growth			-20.0%	-2.3%	12.2%	-4.5%	10.0%	10.0%
O&M/Revenue	55.6%	56.2%	56.1%	56.3%	55.8%	54.4%	53.4%	52.8%
Depreciation and amortization/Net Fixed Asset				3.1%	2.9%	2.8%	2.8%	2.8%
Depreciation Growth		16.0%	-0.8%	3.1%	1.5%	6.3%	7.0%	4.6%
General Taxes/Regulated Revenue	9.7%	10.0%	10.0%	9.2%	9.6%	9.1%	8.6%	8.3%
Adj. EBITDA	734.3	758.4	733.4	791.8	834.4	925.2	1,042.9	1,148.0
Interest Expense/Average Net Debt			8.9%	6.2%	5.6%	5.47%	5.68%	5.91%
Interest Expense/Revenue	15.7%	16.2%	17.5%	12.8%	12.2%	11.9%	11.6%	11.3%
Net Income Growth (excl. goodwill impairment)		338.6%	-1.6%	180.1%	12.6%	20.1%	18.8%	17.5%
EPS growth, (excl. goodwill impairment)			-40.3%	153.8%	12.3%	9.8%	16.2%	11.7%
ROE (excl. goodwill & goodwill impairment)			2.3%	7.0%	8.3%	8.7%	9.2%	9.7%

Source: Company reports, Longbow estimates

American States Water — Quarterly Earnings Statement

Garik Shmois/ Vishal Khetriwal, CFA
Longbow Research
216-525-8414

(dollars in millions, except per share data)

FY ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09E	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E
Water	50.3	60.8	65.4	61.3	52.1	65.4	69.4	61.1	56.8	74.2	71.8	64.1	65.4	82.7	80.3	72.0
Electric	8.9	6.3	6.3	7.2	8.8	6.2	6.7	6.7	8.6	5.9	7.1	7.9	10.0	7.3	8.2	8.1
Contracted Services	13.1	12.2	4.1	5.6	8.1	8.7	9.2	16.4	14.2	13.5	14.1	12.0	12.0	12.0	12.0	12.0
Total Revenue	**72.3**	**79.2**	**75.8**	**74.0**	**68.9**	**80.3**	**85.3**	**84.2**	**79.6**	**93.6**	**93.1**	**84.0**	**87.4**	**102.0**	**100.4**	**92.1**
Expenses																
Supply Costs	16.8	19.0	22.6	19.8	16.1	20.5	24.2	20.0	19.9	23.5	25.0	21.0	22.9	25.6	27.9	23.3
Gen. & Admin. expenses	13.0	13.7	11.8	14.2	14.8	14.9	16.3	16.6	16.9	15.5	17.0	16.4	18.4	18.9	19.1	18.4
Other O&M	9.6	10.9	10.9	11.8	11.8	11.8	11.4	11.4	11.2	11.1	12.2	11.3	12.2	14.8	13.2	12.3
ASUS Construction Expenses	9.1	8.3	1.9	2.9	3.9	4.4	5.1	10.4	8.4	7.8	6.5	6.0	6.0	6.0	6.0	6.0
Gain on sale of water rights/property	(0.4)	(0.2)	0.0	0.0					(0.0)							
Unrealized loss(gain) on purch pwr contracts	(2.7)	0.2	0.9	(0.5)	(2.8)	(1.7)	3.7	(0.8)								
Total Operation & Maintenance	**45.4**	**51.9**	**48.1**	**48.1**	**43.8**	**50.1**	**60.8**	**57.7**	**56.4**	**57.9**	**60.7**	**54.7**	**59.5**	**65.3**	**66.2**	**60.0**
Depreciation & Amortization	7.1	7.1	7.4	7.3	7.8	7.8	7.9	8.1	8.4	8.4	8.5	8.6	8.7	8.8	9.0	9.1
General Taxes	2.9	2.8	2.8	2.7	2.9	2.8	3.5	3.1	3.4	2.7	2.7	4.5	3.4	3.5	3.6	3.5
Total Expenses	**55.4**	**61.8**	**58.3**	**58.1**	**54.5**	**60.7**	**72.1**	**68.9**	**68.19**	**69.0**	**71.9**	**67.8**	**71.6**	**77.6**	**78.7**	**72.7**
Income from Operations	**16.9**	**17.5**	**17.5**	**15.9**	**14.5**	**19.6**	**13.1**	**15.3**	**11.4**	**24.5**	**21.2**	**16.2**	**15.8**	**24.4**	**21.7**	**19.4**
Operating Margin	23.3%	22.0%	23.1%	21.5%	21.0%	24.4%	15.4%	18.2%	14.3%	26.2%	22.8%	19.3%	18.1%	24.0%	21.6%	21.1%
Other Inc. (loss)	0.1	(0.1)	0.1	0.1	0.1	0.0	(0.0)	(7.7)	(0.0)	0.1						
EBIT	**16.9**	**17.4**	**17.6**	**16.0**	**14.6**	**19.6**	**13.1**	**7.6**	**11.4**	**24.6**	**21.2**	**16.2**	**15.8**	**24.4**	**21.7**	**19.4**
EBIT (%)	23.4%	21.9%	23.2%	21.6%	21.1%	24.4%	15.4%	9.0%	14.3%	26.3%	22.8%	19.3%	18.1%	24.0%	21.6%	21.1%
Interest Expense	4.9	5.0	4.8	4.5	5.0	4.5	5.1	4.8	5.1	5.4	5.0	4.7	4.8	4.9	5.0	6.5
Income Before Taxes	**12.0**	**12.4**	**12.9**	**11.4**	**9.6**	**15.1**	**8.0**	**2.8**	**6.3**	**19.2**	**16.2**	**11.5**	**11.0**	**19.6**	**16.7**	**13.0**
Provision for Income Taxes	5.0	5.2	5.2	5.3	4.3	5.8	3.4	(0.1)	1.4	7.7	6.6	4.7	4.5	8.0	6.8	5.3
Implied Tax Rate	41.8%	42.0%	40.7%	46.6%	44.5%	38.4%	42.9%	-3.2%	21.7%	40.2%	40.8%	40.8%	40.8%	40.8%	40.8%	40.8%
Net Income	7.0	7.2	7.6	6.1	5.3	9.278	4.6	2.9	4.9	11.5	9.6	6.8	6.5	11.6	9.9	7.7
EPS (fully diluted)	0.40	0.42	0.44	0.35	0.30	0.53	0.26	0.16	0.28	0.64	0.52	0.37	0.35	0.62	0.53	0.41
EPS (fully diluted, ex one-time items)	**0.31**	**0.43**	**0.47**	**0.35**	**0.30**	**0.47**	**0.39**	**0.40**	**0.28**	**0.61**	**0.52**	**0.37**	**0.35**	**0.62**	**0.53**	**0.41**
Weighted Avg. Shares	17.1	17.1	17.2	17.3	17.4	17.3	17.3	17.4	17.4	18.0	18.6	18.6	18.6	18.7	18.7	18.7
Financial Summary (values in %)																
Water revenue growth	4.5%	14.5%	0.7%	15.6%	3.5%	7.5%	6.0%	-0.3%	9.0%	13.4%	3.5%	4.9%	15.1%	11.5%	11.8%	12.3%
Electric revenue growth	6.3%	-11.0%	-2.4%	-3.9%	-0.7%	-0.8%	7.2%	-6.9%	-1.9%	-5.2%	5.9%	18.0%	16.4%	24.1%	14.2%	2.8%
Contracted Services growth	217%	512%	75.9%	-52.3%	-38.4%	-28.2%	123%	195%	76%	54.6%	54.0%	-26.9%	-15.4%	-11.2%	-14.9%	0.0%
Total Revenue growth	19.2%	27.5%	2.8%	2.6%	-4.6%	1.3%	12.4%	13.8%	15.5%	16.5%	9.1%	-0.3%	9.8%	9.1%	7.9%	9.7%
Operations & Maintenance/Revenue	62.8%	65.4%	63.4%	65.0%	63.5%	62.4%	71.3%	68.5%	70.9%	61.9%	65.2%	65.1%	68.1%	64.0%	65.9%	65.2%
Supply Costs/Revenue (excl. Military Base)	28.4%	28.4%	31.4%	28.9%	26.5%	28.7%	31.8%	29.5%	30.4%	29.4%	31.6%	29.2%	30.3%	28.4%	31.5%	29.1%
Gen. & Admin./Revenue	18.0%	17.2%	15.5%	19.2%	21.5%	18.6%	19.1%	19.8%	21.2%	16.6%	18.5%	19.5%	21.1%	18.5%	19.0%	20.0%
Other O&M/Revenue	13.2%	13.8%	14.4%	15.9%	17.1%	14.7%	13.4%	13.6%	14.1%	11.8%	13.3%	13.5%	14.0%	14.5%	13.2%	13.4%
General Taxes/Revenue	4.1%	3.6%	3.7%	3.6%	4.2%	3.5%	4.1%	3.7%	4.3%	2.9%	2.9%	5.3%	3.9%	3.4%	3.6%	3.8%
EPS Growth	14.7%	16.7%	38.3%	17.6%	-25.0%	26.2%	-40.6%	-53.4%	-5.7%	20.6%	96%	122%	23.9%	-2.9%	2.8%	12.4%

Source: Company reports, Longbow estimates

American States Water — Annual Earnings Statement

Garik Shmois/ Vishal Khetriwal, CFA
Longbow Research
216-525-8414

(dollars in millions, except per share data)

FY ends December 31	2004A	2005A	2006A	2007	2008	2009E	2010E	2011E
Water	200.6	205.5	219.2	237.9	247.9	266.9	300.3	328.3
Electric	25.6	27.2	29.3	28.6	28.4	29.5	33.6	34.5
Other	1.8	3.5	20.1	34.9	42.4	53.8	48.0	48.0
Total Revenue	**228.0**	**236.2**	**268.6**	**301.4**	**318.7**	**350.2**	**381.9**	**410.8**
Expenses								
Supply Costs	81.1	71.9	76.2	78.2	80.9	89.4	99.7	107.9
Gen. & Admin. expenses	41.8	44.3	47.1	52.6	62.7	65.8	74.8	80.1
Other O&M	31.6	32.0	36.4	43.2	46.4	45.8	52.6	56.1
ASUS Construction Expenses			9.0	22.1	23.9	28.8	24.0	24.0
Gain on sale of water rights/property	(5.7)	0.0	(0.3)	(0.6)	0.0	(0.0)	0.0	0.0
Unrealized loss on purch power contracts	0.1	(5.4)	7.1	(2.1)	(1.6)			
Total Operation & Maintenance	**148.9**	**142.8**	**175.6**	**193.4**	**212.3**	**229.8**	**251.0**	**268.1**
Depreciation & Amortization	20.8	21.9	26.3	28.9	31.6	33.8	35.5	37.1
General Taxes	8.8	9.3	10.2	11.3	12.3	13.3	14.0	15.0
Total Expenses	**178.5**	**174.0**	**212.0**	**233.6**	**256.2**	**276.9**	**300.6**	**320.3**
Income from Operations	**49.5**	**62.3**	**56.6**	**67.7**	**62.5**	**73.3**	**81.4**	**90.5**
Operating Margin	21.7%	26.4%	21.1%	22.5%	19.6%	20.9%	21.3%	22%
Other Inc. (loss)	0.3	(0.0)	0.5	0.30	(7.6)	0.1	0.0	0.0
EBIT	**49.8**	**62.2**	**57.1**	**68.0**	**54.9**	**73.3**	**81.4**	**90.5**
EBIT (%)	0.2	0.3	0.2	0.2	0.2	0.2	0.2	0.2
Interest Expense	17.9	13.6	18.3	19.21	19.5	20.2	21.1	23.0
Income Before Taxes	**31.9**	**48.6**	**38.8**	**48.8**	**35.4**	**53.2**	**60.3**	**67.6**
Provision for Income Taxes	13.4	21.9	15.7	20.8	13.4	20.4	24.6	27.5
Implied Tax Rate	41.9%	45.0%	40.5%	42.6%	37.8%	38.3%	40.8%	40.8%
Net Income	18.5	26.7	23.1	28.0	22.0	32.8	35.7	40.0
EPS (fully diluted)	1.19	1.59	1.33	1.61	1.26	1.81	1.91	2.13
EPS (fully diluted, ex.one-time items)	**1.06**	**1.16**	**1.44**	**1.56**	**1.56**	**1.78**	**1.91**	**2.13**
Weighted Avg. Shares	15.6	16.8	17.1	17.2	17.4	18.2	18.7	18.8
Financial Summary (values in %)								
Water revenue growth	7.2%	2.4%	6.7%	8.5%	4.2%	7.6%	12.5%	9.3%
Electric revenue growth	4.5%	6.4%	7.5%	-2.4%	-0.5%	3.9%	13.8%	2.6%
Other	75.1%	96.1%	477.9%	73.5%	21.3%	27.0%	-10.8%	0.0%
Total Revenue growth	7.2%	3.6%	13.7%	12.2%	5.8%	9.9%	9.1%	7.6%
Operations & Maintenance/Revenue	65.3%	60.4%	65.4%	64.2%	66.6%	65.6%	65.7%	65.3%
Supply Costs/Revenue (excl. Military Base)	35.8%	30.9%	30.7%	29.4%	29.3%	30.2%	29.8%	29.7%
Gen. & Admin./Revenue	18.3%	18.7%	17.5%	17.5%	19.7%	18.8%	19.6%	19.5%
Other O&M/Revenue	13.8%	13.5%	13.5%	14.3%	14.6%	13.1%	13.8%	13.7%
General Taxes/Revenue	3.9%	4.0%	4.1%	4.2%	4.5%	4.5%	4.2%	4.1%
(Dep + Amort)/Net Fixed Assets	3.3%	3.3%	3.7%	3.9%	4.1%	4.4%	4.1%	4.1%
(Dep + Amort)/Revenue	9.1%	9.3%	9.8%	9.6%	9.9%	9.7%	9.3%	9.0%
Interest Expense/Avg. Net Debt	6.4%	4.8%	6.1%	6.3%	6.0%	7.0%	6.5%	6.6%
Interest Expense/Revenue	7.8%	5.8%	6.8%	6.4%	6.1%	5.8%	5.5%	5.6%
Average ROE	8.0%	10.4%	8.4%	9.6%	7.2%	9.6%	9.6%	10.2%
EPS growth, excluding one-time items	52.0%	9.4%	24.1%	8.3%	0.0%	14.0%	7.5%	11.5%

Source: Company reports, Longbow estimates

California Water Service Group — Quarterly Earnings Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY Ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09E	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E
Total Revenue	71.6	95.8	113.9	85.9	72.9	105.6	131.7	100.1	86.6	116.7	136.7	107.5	93.3	121.5	142.6	112.3
Operations & Maintenance	54.0	67.8	75.8	60.2	55.0	71.9	78.2	71.1	64.8	79.7	81.5	76.8	69.6	82.6	83.9	78.2
Depreciation and Amortization	8.4	8.4	8.4	8.4	9.2	9.3	9.3	9.6	10.2	10.3	10.3	10.4	10.5	10.6	10.7	10.7
General Taxes	3.4	3.4	3.7	3.1	3.7	3.5	3.9	3.7	4.1	3.9	4.0	3.9	4.4	4.0	4.2	4.0
Total Expenses	65.8	79.6	87.9	71.8	67.9	84.7	91.4	84.3	79.1	93.9	95.7	91.0	84.5	97.3	98.7	92.9
Income from Operations	5.8	16.2	26.0	14.1	5.0	20.9	40.3	15.8	7.5	22.7	40.9	16.5	8.8	24.3	43.9	19.4
Operating Margin	8.1%	16.9%	22.8%	16.5%	6.9%	19.8%	30.6%	15.8%	8.7%	19.5%	29.9%	15.3%	9.4%	20.0%	30.8%	17.3%
Other Income & Expenses (net)	1.3	1.5	1.3	0.4	(0.1)	0.6	(0.7)	(0.6)	0.2	1.4	0.7	0.7	0.7	0.7	0.7	0.7
Gain (loss) on sale of non-util property	0.0	(0.1)	0.0	2.6	0.0	0.0	0.0	0.0	0.6	0.1	0.0	0.0	0.0	0.0	0.0	0.0
EBIT	7.1	17.6	27.2	17.1	4.9	21.5	39.6	15.2	8.4	24.2	41.6	17.1	9.4	24.9	44.6	20.1
EBIT (%)	9.9%	18.3%	23.9%	20.0%	6.7%	20.4%	30.0%	15.2%	9.6%	20.7%	30.4%	15.9%	10.1%	20.5%	31.2%	17.9%
Interest Expense	4.4	4.5	4.5	3.7	4.6	4.7	4.2	3.7	4.4	5.3	5.3	5.0	5.5	5.3	5.3	4.9
Income Before Taxes	2.6	13.1	22.8	13.4	0.3	16.8	35.4	11.4	4.0	18.9	36.3	12.1	3.9	19.6	39.3	15.2
Provision for Income Taxes	1.1	5.4	8.9	5.4	0.1	6.7	13.2	4.1	1.6	6.8	14.0	4.7	1.5	7.5	15.1	5.9
Implied Tax Rate	40.3%	40.9%	39.3%	40.0%	40.3%	39.7%	37.3%	36.0%	39.3%	36.0%	38.7%	38.7%	38.5%	38.5%	38.5%	38.5%
Net Income	1.6	7.7	13.8	8.0	0.2	10.1	22.2	7.3	2.4	12.1	22.2	7.4	2.4	12.1	24.1	9.4
Preferred Dividends	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Net Income	1.6	7.7	13.8	8.0	0.2	10.1	22.2	7.3	2.4	12.1	22.2	7.4	2.4	12.1	24.1	9.4
EPS (fully diluted)	0.07	0.37	0.67	0.39	0.01	0.48	1.06	0.35	0.12	0.58	1.07	0.36	0.11	0.56	1.10	0.42
Weighted Avg. Shares	20.7	20.7	20.7	20.7	20.7	20.7	20.7	20.7	20.8	20.8	20.8	20.8	21.2	21.6	22.0	22.4
Financial Summary (values in %)																
Revenue Growth	9.7%	18.1%	5.7%	6.5%	1.9%	10.2%	15.7%	16.6%	18.8%	10.5%	3.8%	7.4%	7.7%	4.2%	4.4%	4.5%
Operations & Maintenance/Revenue	75.4%	70.8%	66.6%	70.1%	75.4%	68.1%	59.4%	71.0%	74.8%	68.3%	59.6%	71.4%	74.6%	68.0%	58.8%	69.6%
Gen. taxes/Revenue	4.8%	3.6%	3.3%	3.6%	5.1%	3.3%	3.0%	3.7%	4.7%	3.4%	2.9%	3.6%	4.7%	3.3%	2.9%	3.5%
EBIT (% of rev.)	9.9%	18.3%	23.9%	20.0%	6.7%	20.4%	30.0%	15.2%	9.6%	20.7%	30.4%	15.9%	10.1%	20.5%	31.2%	17.9%
EBIT/Interest expense	1.6	3.9	6.1	4.6	1.1	4.6	9.5	4.1	1.9	4.5	7.8	3.4	1.7	4.7	8.4	4.1
EPS growth	75.0%	20.5%	-2.6%	23.6%	-87.2%	28.5%	58.8%	-9.2%	1205.6%	21.3%	0.9%	1.2%	-2.9%	-4.1%	2.6%	17.0%

Source: Company reports, Longbow estimates

California Water Service Group — Annual Earnings Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY Ends December 31	FY04	FY05	FY06	FY07	FY08	FY09E	FY10E	FY11E
Total Revenue	**315.6**	**320.7**	**334.7**	**367.1**	**410.3**	**447.4**	**469.7**	**526.5**
Watet Production Costs	119.1	115.7	124.3	138.9	146.6	159.8	166.3	186.4
Administrative & General	47.1	48.8	52.8	54.3	59.4	65.3	68.1	76.3
Other Operations	39.9	40.0	42.9	46.3	51.2	57.0	59.7	66.3
Maintainence	13.2	15.2	15.6	18.3	19.0	20.6	20.3	21.6
Operations & Maintenance	219.4	219.7	235.6	257.8	276.2	302.8	314.3	350.6
Depreciation and Amortization	26.1	28.7	30.7	33.6	37.3	41.2	42.5	45.0
General Taxes	11.5	12.6	12.9	13.7	14.8	15.9	16.6	18.6
Total Expenses	**257.0**	**261.0**	**279.1**	**305.0**	**328.3**	**359.8**	**373.4**	**414.2**
Income from Operations	**58.6**	**59.7**	**55.6**	**62.1**	**82.0**	**87.6**	**96.3**	**112.3**
Operating Margin	**18.6%**	**18.6%**	**16.6%**	**16.9%**	**20.0%**	**19.6%**	**20.5%**	**21.3%**
Other Income & Expenses (net)	2.4	3.0	3.4	4.4	(0.9)	2.9	2.6	2.6
Gain (loss) on sale of non-util property	0.0	2.3	0.3	2.5	0.0	0.7	0.0	0.0
EBIT	**61.0**	**64.9**	**59.4**	**69.0**	**81.1**	**91.2**	**98.9**	**114.9**
EBIT (%)	**19.3%**	**20.2%**	**17.7%**	**18.8%**	**19.8%**	**20.4%**	**21.1%**	**21.8%**
Interest Expense	17.8	17.7	17.0	17.1	17.2	20.0	21.0	23.5
Income Before Taxes	43.1	47.2	42.4	51.9	63.9	71.3	78.0	91.4
Provision for Income Taxes	**17.1**	**20.0**	**16.8**	**20.7**	**24.1**	**27.1**	**30.0**	**35.2**
Implied Tax Rate	**39.6%**	**42.4%**	**39.7%**	**39.9%**	**37.7%**	**38.0%**	**38.5%**	**38.5%**
Net Income	26.0	27.2	25.6	31.2	39.8	44.2	48.0	56.2
Preferred Dividends	-	-	-	-	-	-	-	-
Net Income	**26.0**	**27.2**	**25.6**	**31.2**	**39.8**	**44.2**	**48.0**	**56.2**
EPS (fully diluted)	**1.46**	**1.47**	**1.34**	**1.50**	**1.90**	**2.12**	**2.20**	**2.48**
Weighted Avg. Shares	17.7	18.4	18.9	20.7	20.7	20.8	21.8	22.7
Financial Summary (values in %)								
Revenue Growth	13.9%	1.6%	4.4%	9.7%	11.8%	9.0%	5.0%	12.1%
Operations & Maintenance/Revenue	69.5%	68.5%	70.4%	70.2%	67.3%	67.7%	66.9%	66.6%
(Dep + Amort)/Net Fixed Assets	3.4%	3.6%	3.6%	3.6%	3.7%	3.7%	3.6%	3.6%
Gen. taxes/Revenue	3.6%	3.9%	3.9%	3.7%	3.6%	3.5%	3.5%	3.5%
EBIT (% of rev.)	19.3%	20.2%	17.7%	18.8%	19.8%	20.4%	21.1%	21.8%
Interest Expense/Net Debt	6.7%	6.4%	6.0%	5.9%	5.5%	5.6%	5.9%	6.0%
EBIT/Interest expense	3.4	3.7	3.5	4.0	4.7	4.6	4.7	4.9
Net Income Growth	34.0%	4.6%	-6.0%	21.8%	27.7%	11.0%	8.6%	17.2%
EPS growth	20.4%	0.7%	-8.8%	11.9%	26.7%	11.8%	3.5%	12.8%
Average ROE	9.7%	9.3%	7.5%	8.1%	10.1%	10.7%	10.8%	11.5%

Source: Company reports, Longbow estimates

Aqua America - Quarterly Income Statement
Garik Shmois/ Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09E	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E
Total Operating Revenue	137.3	150.6	165.5	149.1	139.3	150.8	177.1	159.8	154.5	167.3	190.5	168.7	164.2	185.2	212.6	180.8
Operation & Maintenance	60.3	63.3	67.1	62.4	64.3	65.1	66.7	65.9	67.0	68.5	74.1	66.0	67.5	72.6	83.3	74.3
Depreciation	20.1	20.5	21.1	21.5	21.5	20.6	22.8	23.9	26.4	25.0	25.4	25.4	25.6	26.2	26.7	27.4
Amortization	1.2	1.2	1.2	1.2	1.2	1.0	1.8	1.5	2.8	3.1	3.0	3.0	3.0	3.0	3.0	3.0
General Taxes	11.9	10.8	10.8	11.8	12.1	10.8	11.2	10.6	11.6	11.9	12.4	11.8	12.3	13.0	12.8	12.7
Recovery of restructuring costs																
Total Expenses	93.6	95.9	100.1	96.9	99.1	97.6	102.5	102.0	107.7	108.5	114.9	106.2	108.4	114.8	125.8	117.4
Income from Operations	43.7	54.8	65.3	52.2	40.2	53.1	74.6	57.9	46.8	58.9	75.6	62.5	55.8	70.4	86.8	63.4
Operating Margin (%)	31.9%	36.4%	39.5%	35.0%	28.9%	35.2%	42.1%	36.2%	30.3%	35.2%	39.7%	37.1%	34.0%	38.0%	40.8%	35.1%
All. for Borrowed Funds Used in Const.	0.7	0.7	0.7	0.8	1.0	1.1	1.0	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.6
Gain (loss) on sale of other assets	0.1	0.3	0.3	2.8		0.6	0.5	0.5	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Other																
EBIT	44.5	55.8	66.3	55.8	41.2	54.8	76.1	59.0	47.5	59.5	76.3	63.2	56.5	71.1	87.5	64.1
EBIT (%)	32.4%	37.1%	40.0%	37.5%	29.6%	36.3%	43.0%	36.9%	30.8%	35.6%	40.0%	37.5%	34.4%	38.4%	41.2%	35.5%
Interest Expense	16.5	16.4	17.1	16.8	17.1	17.1	17.0	17.4	16.6	16.8	17.0	17.2	17.6	18.0	18.4	18.6
Income Before Taxes	28.0	39.4	49.2	39.0	24.0	37.7	59.1	41.7	30.9	42.7	59.3	46.0	38.9	53.1	69.1	45.5
Provision for Income Taxes	11.1	15.7	19.6	14.1	9.7	15.2	23.7	16.0	12.5	16.9	24.0	18.2	15.6	21.2	27.6	17.7
Implied Tax Rate	39.8%	39.8%	40.0%	36.1%	40.4%	40.2%	40.1%	38.4%	40.5%	39.5%	40.5%	39.5%	40.0%	40.0%	40.0%	39.0%
Net Income before extraord. Item	16.9	23.7	29.5	24.9	14.3	22.6	35.4	25.7	18.4	25.9	35.3	27.9	23.4	31.9	41.5	27.8
Reclassification adj. for gains reported in net income				(1.3)			(0.2)			0.0						
Unrealized gain on securities																
Unrealized holding gain on investments	0.0	0.2	0.9	-	-	0.2	0.0		0.0	0.2						
Minimum pension liability adjustment		-	-													
Comprehensive Income	16.9	23.9	30.4	23.6	14.3	22.7	35.2	25.7	18.4	26.1	35.3	27.9	23.4	31.9	41.5	27.8
Diluted Net Income Per Share	0.13	0.18	0.22	0.19	0.11	0.17	0.26	0.19	0.14	0.19	0.26	0.20	0.17	0.23	0.30	0.20
Weighted Avg. Shares	133.2	133.5	133.8	134.0	134.0	134.1	135.3	135.6	135.9	135.9	136.2	136.4	136.8	137.3	137.7	138.2
Financial Summary (values in %)																
Revenue Growth	16.4%	14.3%	12.6%	8.9%	1.4%	0.1%	7.0%	7.2%	10.9%	11.0%	7.6%	5.6%	6.3%	10.7%	11.6%	7.2%
Operations & Maintenance/Revenue	43.9%	42.0%	40.5%	41.9%	46.2%	43.2%	37.7%	41.2%	43.4%	41.0%	38.9%	39.1%	41.1%	39.2%	39.2%	41.1%
EBIT (% of rev.)	32.4%	37.1%	40.0%	37.5%	29.6%	36.3%	43.0%	36.9%	30.8%	35.6%	40.0%	37.5%	34.4%	38.4%	41.2%	35.5%
General taxes as % of revenue	8.7%	7.2%	6.6%	7.9%	8.7%	7.2%	6.3%	6.7%	7.5%	7.0%	6.2%	7.0%	7.5%	7.0%	6.0%	7.0%
EBITDA	65.9	77.5	88.5	78.6	63.8	76.4	100.7	84.4	76.7	87.5	104.7	91.6	85.1	100.3	117.2	94.5
Net Income Growth	1.8%	6.0%	8.0%	-3.2%	-15.0%	-5.0%	19.9%	3.0%	28.3%	14.6%	-0.3%	8.5%	27.1%	23.3%	17.6%	-0.4%
EPS Growth	0.0%	4.0%	7.1%	-3.6%	-15.5%	-5.3%	18.6%	1.8%	26.5%	13.0%	-1.0%	7.9%	26.3%	22.1%	16.3%	-1.7%

Source: Company reports and Longbow estimates

LONGBOW Research

October 12, 2009

Aqua America - Annual Income Statement
Garik Shmois/ Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	2004A	FY05A	FY06A	FY07A	FY08A	FY09E	FY10E	FY11E
Total Operating Revenue	**442.0**	**496.8**	**533.5**	**602.5**	**627.0**	**681.0**	**742.8**	**816.0**
Operation & Maintenance	178.3	203.1	219.6	253.1	262.1	275.6	297.7	325.9
Depreciation	54.6	60.7	70.9	83.2	88.8	102.2	105.9	112.8
Amortization	4.3	4.7	4.1	4.8	5.5	11.8	12.0	12.0
General Taxes	27.6	31.7	33.3	45.4	44.7	47.7	50.7	55.7
	-		-					
Total Expenses	**264.8**	**300.3**	**327.9**	**386.5**	**401.2**	**437.3**	**466.4**	**506.4**
Income from Operations	**177.2**	**196.5**	**205.6**	**216.0**	**225.8**	**243.7**	**276.4**	**309.6**
Operating Margin (%)	**40.1%**	**39.6%**	**38.5%**	**35.9%**	**36.0%**	**35.8%**	**37.2%**	**37.9%**
Allow. for Borrowed Funds Used in Const.	2.3	2.4	3.9	3.0	3.7	2.4	2.4	2.4
Gain (loss) on sale of other assets	1.3	1.2	1.2	3.5	1.6	0.4	0.4	0.4
Other	-	-	-	-				
EBIT	**180.8**	**200.1**	**210.7**	**222.5**	**231.1**	**246.5**	**279.2**	**312.4**
EBIT (%)	**40.9%**	**40.3%**	**39.5%**	**36.9%**	**36.9%**	**36.2%**	**37.6%**	**38.3%**
Interest Expense	48.7	52.1	58.4	66.9	68.6	67.6	72.6	81.6
Income Before Taxes	132.1	148.1	152.3	155.5	162.5	178.9	206.6	230.8
Provision for Income Taxes	**52.1**	**56.9**	**60.2**	**60.5**	64.6	71.6	82.2	91.8
Implied Tax Rate	**39.4%**	**38.4%**	**39.6%**	**38.9%**	**39.7%**	**40.0%**	**39.8%**	**39.8%**
Net income	80.0	91.2	92.0	95.0	97.9	107.3	124.4	139.0
Reclassification adj. for gains reported in net income	(0.2)	-	-	(1.3)	(0.2)			
Unrealized gain on securities	0.1	-	-	-				
Unrealized holding gain on investments	-	-	0.2	1.1	0.2	0.3	-	-
Minimum pension liability adjustment	(1.7)	(1.3)	3.1		-	-	-	-
Comprehensive Income	**78.1**	**89.8**	**95.3**	**94.8**	**97.9**	**107.6**	**124.4**	**139.0**
Diluted Net Income Per Share	**0.64**	**0.71**	**0.70**	**0.71**	**0.73**	**0.79**	**0.91**	**1.00**
Weighted Avg. Shares	125.7	129.2	131.8	133.6	134.7	136.1	137.5	138.8
Financial Summary (values in %)								
Revenue Growth	20.4%	12.4%	7.4%	12.9%	4.1%	8.6%	9.1%	9.9%
Operations & Maintenance/Revenue	40.3%	40.9%	41.2%	42.0%	41.8%	40.5%	40.1%	39.9%
Dep/Net Fixed Asset	3.0%	2.9%	3.1%	3.3%	3.2%	3.4%	3.3%	3.3%
Depreciation Growth	12.5%	11.3%	16.7%	17.3%	6.7%	15.1%	3.7%	6.5%
General taxes as % of revenue	6.2%	6.4%	6.2%	7.5%	7.1%	7.0%	6.8%	6.8%
Interest Exp/ Average Net Debt	5.6%	5.3%	5.8%	5.9%	5.2%	5.3%	5.3%	5.6%
Interest Expense/Revenue	11.0%	10.5%	11.0%	11.1%	10.9%	9.9%	9.8%	10.0%
EBITDA	239.7	265.6	285.7	310.5	325.4	360.5	397.2	437.2
Net income growth	13.0%	13.9%	0.9%	3.3%	3.1%	9.6%	15.9%	11.7%
Average ROE	11.4%	11.7%	10.6%	10.0%	9.6%	9.9%	10.8%	11.4%
EPS Growth (ex special items and FAS 123)	7.0%	10.9%	-1.0%	1.9%	2.2%	8.5%	14.8%	10.6%

Source: Company reports and Longbow estimates

LONGBOW Research

October 12, 2009

WATER INDUSTRY PEER VALUATION

($ in millions, except per share data)

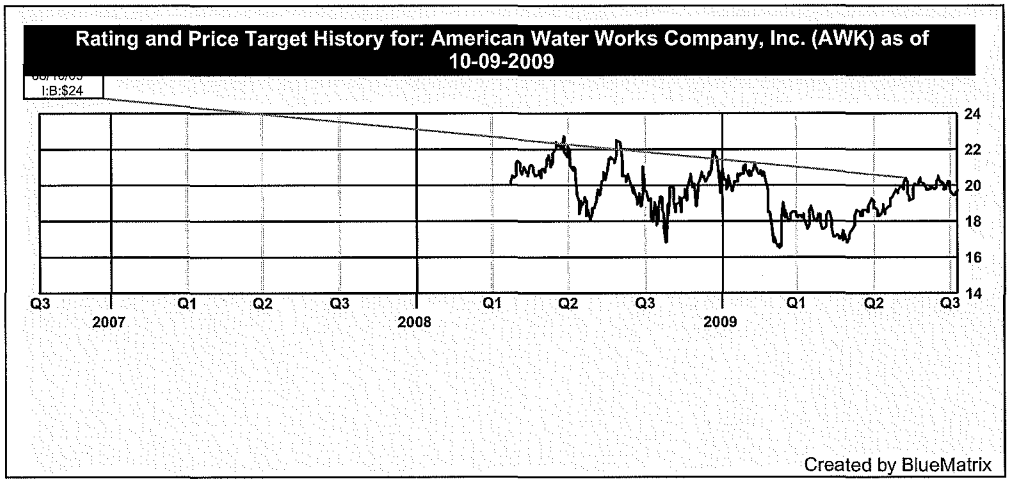
Company	Ticker	FY End	Rating	Target	% Upside	Share Price	52 Week Hi	52 Week Lo	Mkt Cap	Revenue FY End	Earnings per Share Last FY	Earnings per Share Current FY	Earnings per Share Next FY	P/E Current FY	P/E Next FY	Dividend Rate	Price/ Book
U.S. WATER UTILITIES																	
American Water Works	AWK	Dec.	BUY	$24	20%	$ 19.79	$22.35	$16.22	$ 3,435	$ 2,337	1.17	1.29	1.50	15.4x	13.2x	4.3%	0.8x
Aqua America	WTR	Dec.	Neutral			$ 16.61	$22.00	$12.20	$ 2,270	$ 627	0.73	0.79	0.91	21.1x	18.4x	3.5%	2.6x
American States Water	AWR	Dec.	Neutral			$ 36.80	$38.79	$27.00	$ 678	$ 319	1.56	1.78	1.91	20.7x	19.3x	2.7%	1.8x
California Water Service Group	CWT	Dec.	BUY	$45	14%	$ 39.55	$48.28	$27.68	$ 812	$ 410	1.90	2.12	2.20	18.6x	18.0x	3.0%	2.4x
Southwest Water Company	SWWC	Dec.	NR			$ 5.47	$11.00	$2.67	$ 134	$ 222	-0.19	*0.1*	*0.39*	54.7x	14.0x	1.9%	0.7x
Artesian Resources Corporation	ARTNA	Dec	NR			$ 17.11	$18.14	$12.81	$ 127	$ 56	0.86	*1.07*	*1.11*	16.0x	15.4x	4.2%	1.3x
Consolidated Water Co	CWCO	Dec	NR			$ 15.61	$21.29	$6.35	$ 228	$ 60	0.50	*0.78*	*0.82*	20.0x	19.0x	1.9%	1.5x
Connecticut Water Service	CTWS	Dec	NR			$ 22.62	$26.99	$17.31	$ 188	$ 61	1.12	*1.08*	*1.06*	20.9x	21.3x	4.1%	1.9x
Middlesex Water Company	MSEX	Dec	NR			$ 15.37	$17.93	$11.64	$ 208	$ 91	0.90	*0.71*	*0.81*	21.6x	19.0x	4.6%	1.7x
Pennichuck Corporation	PNNW	Dec	NR			$ 23.13	$24.80	$14.75	$ 96	$ 31	0.57	*0.59*	*0.76*	39.2x	30.4x	3.1%	1.8x
York Water Company	YORW	Dec	NR			$ 13.97	$17.95	$9.74	$ 160	$ 33	0.57	*0.67*	*0.69*	20.9x	20.2x	3.6%	2.0x
U.S. Water Utility Average														24.5x	18.9x	3.4%	1.7x
EQUIPMENT/FILTRATION/TREATMENT SECTOR																	
Calgon Carbon Corp.	CCC	Dec.	NR			$ 15.39	$21.64	$9.11	$ 838	$ 400	0.56	*0.5*	*0.77*	30.5x	20.0x	0.0%	3.3x
Danaher	DHR	Dec.	NR			$ 67.84	$69.00	$47.20	$ 21,282	$ 12,697	4.23	*3.38*	*3.74*	19.7x	17.8x	0.2%	1.8x
ITT Technologies	ITT	Dec.	NR			$ 52.05	$52.71	$31.94	$ 9,158	$ 11,695	4.04	*3.66*	*3.81*	13.7x	13.2x	1.7%	2.7x
Layne Christensen	LAYN	Jan.	NR			$ 31.55	$35.14	$10.36	$ 610	$ 1,008	2.20	*0.62*	*0.95*	50.9x	32.8x	0.0%	0.7x
Mueller Water Products	MWA	Sept	NR			$ 5.46	$8.94	$1.48	$ 598	$ 1,859	0.46	*(0.37)*	-	-	81.4x	1.4%	0.8x
Nalco	NLC	Dec.	NR			$ 21.64	$21.67	$7.80	$ 2,965	$ 4,212	1.30	*0.8*	*1.18*	26.7x	18.2x	0.7%	4.0x
Pall Corp.	PLL	Jul.	NR			$ 32.45	$34.54	$18.20	$ 3,781	$ 2,329	1.94	*1.85*	*2.08*	18.1x	16.4x	1.8%	3.2x
Pentair	PNR	Dec.	NR			$ 30.95	$33.00	$17.23	$ 3,009	$ 3,382	2.17	*1.42*	*1.73*	21.6x	17.7x	2.3%	1.2x
Watts Water Technologies	WTS	Dec.	NR			$ 30.93	$32.88	$15.85	$ 1,117	$ 1,459	1.83	*1.31*	*1.45*	23.3x	21.0x	1.4%	1.1x
Equipment/Filtration/Treatment Average (*ex BWTR and CCC)														25.6x	26.5x	1.1%	2.1x
WATER RESOURCES/ INFRASTRUCTURE																	
Insituform Technologies	INSU		NR			$ 19.25	$21.28	$9.26	$ 730	$ 537	0.77	*0.96*	*1.14*	19.5x	16.5x	0.0%	1.5x
Lindsay Manufacturing	LNN		NR			$ 38.29	$68.18	$20.89	$ 459	$ 475	3.11	*1.06*	-	29.2x	26.1x	0.9%	5.1x
Tetra Tech	TTEK		NR			$ 26.61	$32.00	$14.20	$ 1,606	$ 2,145	1.02	*1.24*	*1.42*	18.6x	19.4x	0.0%	2.8x
Water Resources/ Infrastructure Average														22.4x	20.7x	0.3%	3.1x

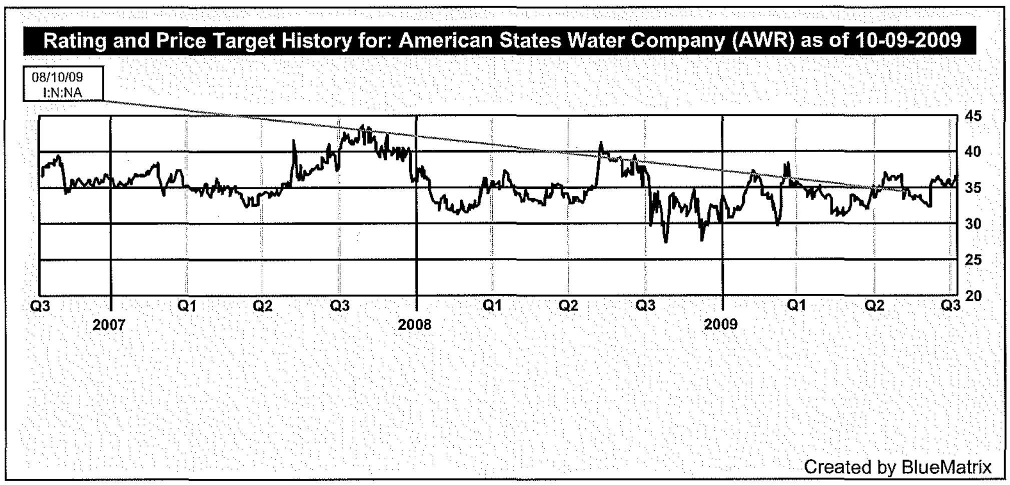
Relevant Indices		Share Price
Dow Jones Industrials	DJ30	$ 9,864.94
S&P 500	SPX	$ 1,071.49
Nasdaq Composite	NDX	$ 2,139.28

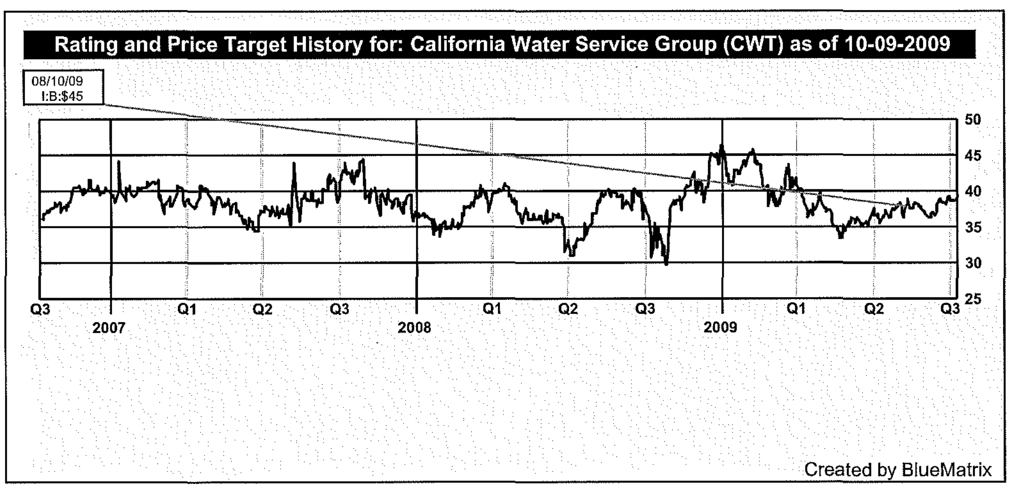
Source: Baseline; Company reports and LBR Estimates. EPS reflects diluted EPS, excluding extraordinary items. Numbers in italics reflect consensus estimates.
** Time period for annual estimates may vary based on reporting date.

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469







G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

APPENDIX

IMPORTANT DISCLOSURES

REGULATION ANALYST CERTIFICATION ("REG AC"): The Research Analyst(s) who prepared this research report hereby certifies that the views expressed in the research report accurately reflect the analyst(s) personal views about the subject companies and their securities. The Research Analyst(s) also certifies that the Analyst(s) have not been, are not, and will not be receiving direct or indirect compensation for expressing the specific recommendation(s) or view(s) in this report.

GENERAL DISCLOSURES: Longbow Securities does not make a market in any securities, nor does it hold a principal position in any security. However, any officer, director or stockholder of Longbow Securities or any member of their families may have a position in and may from time to time purchase or sell any of the securities mentioned or any related securities. Security prices in this report may either reflect the previous day's closing price or an intraday price, depending on the time of distribution. Consensus estimates are derived from either Thomson/Reuters, Bloomberg or Baseline. Designated trademarks and brands are the property of their respective owners.

SPECIFIC DISCLOSURES:

- Longbow Securities does not make a market in the securities of any company mentioned in this Report, and is not a market-maker in any securities generally. Nor does the firm does hold a principal position in any security.
- As of the date of this Report, no officer, director or stockholder of Longbow Securities, or any member of their immediate families, holds securities of any company mentioned in the Report. In the event such persons purchase, hold or sell securities of a company mentioned in the Report for their own account, any subsequent Report shall disclose the fact of any such ownership or transactions.
- No employee of Longbow Securities serves on the Board of Directors of the subject security or any other security mentioned in this report.
- Neither the Research Analyst nor a member of the Research Analyst's household has a financial interest in the securities of the subject company or any other security mentioned in

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

this report.

- Neither the Research Analyst nor a member of the Research Analyst's household serves on the Board of Directors of the subject company or any other security mentioned in this report.
- Neither Longbow Securities nor its affiliates beneficially own 1% or more of an equity security of the subject company or any other security mentioned in this report.

RATINGS DISTRIBUTIONS FOR LONGBOW RESEARCH:

Rating Category	Count	Percent
Buy	57	27.7%
Neutral	141	68.4%
Sell	8	3.9%

RATING SYSTEM:

"Buy" means that Longbow Securities expects total return to exceed 20% over a 12-month period.

"Neutral" means that Longbow Securities expects total return to be within a range of plus or minus 20% over a 12-month period.

"Sell" means that Longbow Securities expects total return to be negative by greater than 20% over a 12-month period.

Longbow Research's full research universe and related applicable disclosures can be obtained by calling (216) 986-0700 or via postal mail at: Editorial Department, Longbow Research, 6000 Lombardo Center, Suite #500, Independence, Ohio 44131.

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

LONGBOW Research
Tactical advantage through independent research

Industry Update

September 9, 2009

Analysts:
GARIK SHMOIS
T: 216-525-8414
E: gshmois@longbowresearch.com

VISHAL KHETRIWAL, CFA
T: 216-525-8469
E: vkhetriwal@longbowresearch.com

Industry: **WATER UTILITIES**

Coverage:

Ticker	Rating	Price
AWK	BUY	$19.99
AWR	NEUTRAL	$35.23
CWT	BUY	$36.75
WTR	NEUTRAL	$16.85

Water Utilities: A Closer Look at the Valuation Premium

· In the following report, we examine the reasons behind water utilities trading at a ~40% premium to electric and ~20% premium to gas utilities. We focus on capex spending, relative PEG ratio, scarcity premium and lower operational risk.

· We see water utilities growing capex 16% over the next three years vs. 4% for gas utilities and 9% for electric utilities. Consequently, we believe that higher capex growth among water utilities should allow for higher EPS growth than rest of the utility sector.

· Assuming 11% EPS growth for water utilities, the current PEG ratio at 1.56x is more attractive than the 2.29 for gas utilities and 2.37x for electric utilities.

· Water utilities have lower exposure to commodity risk, which we believe contributes to their premium valuation. Rates for purchased water usually increase at a predictable 3-5% annually. As the water utilities continuously file rate cases (rate increase request), they are typically able to recover this inflation in the next rate case. For electric and gas utilities, input costs have been more volatile and their ability to offset via timely rate increases can be potentially more difficult to achieve.

· Increasing water scarcity, especially in southern and western U.S. markets, and need for repairing and expanding water infrastructure is increasing interest in water-related investments. Growing investor interest via water-specific funds, a high retail ownership, and a generally smaller market cap contribute to what we consider a scarcity premium for water utility stocks.

IMPORTANT DISCLOSURES ARE LOCATED IN THE APPENDIX.

TABLE OF CONTENTS

INTRODUCTION

A common question we have heard from investors looking at water utilities is "why should I pay 18-19x earnings for water utilities when I can pay 12-13x for electric or gas names?" In the following report, we address this question by examining EPS growth and planned capex spending for the four water utilities under our coverage along with the six or seven largest electric and gas utilities companies. We note that, in particular, water utilities carry a lower PEG ratio, suggesting that valuations are actually relatively more attractive for this sector. We also look at other reasons for the valuation disparity, mainly a scarcity premium and lower operational risk. The former stems from both constrained supply/demand fundamentals as well as a more stable investor base for water utilities. The latter discusses more stable supply costs, as water supply costs from third parties have grown at 3-5% historically while coal and natural gas costs are more volatile and in some cases may not be fully recovered by rate increases. The end result is that while we are not arguing for a 50-60% valuation premium the water utilities garner, we do see sufficient evidence to argue that water utilities should trade at a higher multiple than electric and gas utilities.

PEG RATIO ANALYSIS

As seen below, the largest electric and gas utilities in the U.S. are currently trading at an average forward P/E of 12.2x and 14.6x, respectively, whereas our four covered water utilities are trading at average of 17.2x (exhibit 4). We believe this disparity can be partially explained through the PEG ratio. We note that the seven largest electric and gas utilities have an average PEG ratios of 2.3-2.4, which roughly corresponds to average expected five-year EPS growth rate of 7.5% for water utilities (exhibit 4). We believe that 7.5% growth is a bear-case scenario for these companies and the growth should be higher at 11%. Our EPS growth estimates are based on the capex being invested by the water utilities and expected rate increases against these investments. As seen in exhibit 1 below, the current level of capex by water utilities supports our expectation of EPS growth going forward.

Exhibit 1: EPS Impact of Capex

($ mil.)	AWK	AWR	CWT	WTR
FY09E Capex	800	75	110	315
FY09E Depriciation	289	34	41	114
Δ Net Fixed Assets	512	41	69	201
Equity/Capital FY09E	42%	53%	52%	46%
Net Fixed Assets Finance by Equity	215	22	36	92
Average ROE FY09E	8.9%	9.4%	10.7%	10.3%
Expected Return	19	2	4	10
Shares Outstanding FY09E (mil)	168	18	21	136
EPS Upside from Capital Spending	$ 0.11	$ 0.11	$ 0.18	$ 0.07
Annual Growth over FY08	10%	7%	10%	10%

Source: Longbow estimates

We expect EPS growth to further accelerate in following years due to higher ROE and lower equity dilution from higher internal cash generation. We also note that AWR's EPS below is below its peers because the calculation excludes income from electric and contracted services business, which accounts for nearly one-fourth of the company's business. Other water utilities also have unregulated businesses, which add to the ROE calculated above.

Exhibit 2: PEG Ratio Largest Electric Utilities

	Past 5 yr EPS Growth Rate	Forward P/E	Next 5 yr EPS Growth Rate	PEG Ratio
SOUTHERN CO (SO)	1.7%	13.1	5.0%	2.64
F P L GROUP INC (FPL)	11.3%	12.4	9.5%	1.30
DUKE ENERGY CP HL (DUK)	-7.2%	13.0	3.2%	4.06
DOMINION RES NEW (D)	8.6%	10.9	6.5%	1.69
Entergy Corp. (ETR)	10.6%	11.8	8.8%	1.34
American Electric Power (AEP)	7.7%	10.4	3.7%	2.85
FirstEnergy Corp. (FE)	10.2%	13.5	5.0%	2.70
Average	6.1%	12.2	5.9%	**2.37**

Source: Baseline, Yahoo Finance

Exhibit 3: PEG Ratio Largest Gas Utilities

	Past 5 yr EPS Growth Rate	Forward P/E	Next 5 yr EPS Growth Rate	PEG Ratio
TransCanada Corp. (TRP)	12.5%	15.0	5.0%	3.00
Sempra Energy (SRE)	6.0%	10.4	6.3%	1.64
EQT Corporation (EQT)	2.1%	24.3	9.0%	2.70
ONEOK Inc. (OKE)	11.9%	12.1	7.3%	1.67
National Fuel Gas Co. (NFG)	21.1%	17.3	8.5%	2.04
Energen Corp. (EGN)	27.9%	10.4	5.0%	2.08
AGL Resources Inc. (AGL)	5.5%	13	4.5%	2.89
Average	12.4%	14.6	6.5%	**2.29**

Source: Baseline, Yahoo Finance

Exhibit 4: PEG Ratio - Largest Water Utilities

	Forward P/E	Avg. 3 yr EPS Growth Rate (FY09-11), Our Model	PEG Ratio	Next 5 yr EPS Growth Rate				
				7.5%	8.0%	9.0%	10.0%	11.0%
American Water (AWK)	14.4	12.5%	1.15	1.92	1.80	1.60	1.44	1.31
Aqua America (WTR)	19.1	11.3%	1.69	2.55	2.39	2.12	1.91	1.74
California Water (CWT)	17.1	9.4%	1.82	2.28	2.14	1.90	1.71	1.55
American States (AWR)	18.1	11.0%	1.65	2.41	2.26	2.01	1.81	1.65
Average	17.2	11.1%	**1.58**	**2.29**	**2.15**	**1.91**	**1.72**	**1.56**

Source: Baseline, Yahoo Finance, LBR Estimates

As seen in exhibit 5 below, WTR, CWT and AWR's EPS has grown at an average of 11% over the past five years. We did not include AWK is this calculation as the company was private between 2002 and 2008. We expect the sector to continue this pace of EPS appreciation and anticipate 11.1% (exhibit 4) growth over the next three years (FY09-11). This gives the companies a PEG ratio of 1.56, a discount to other utility sectors.

Exhibit 5: Avg Operating EPS Growth Rate - Successive 5 yr Periods			
	2004-2008	1999-2003	1994-1998
WTR	4.4%	7.1%	12.0%
CWT	10.6%	-2.3%	2.7%
AWR	17.8%	-4.8%	0.0%
Average	11.0%	0.0%	4.9%

Source: Baseline

WTR's EPS growth has trailed over the past five years due to acquisition-related lower ROE negatively impacting results. However, we believe the company should perform at par with other utilities over the next five years, as it catches up on rate increases in southern states. We note that 17.8% EPS growth for AWR during 2004-2008 is due to signification appreciation in 2004 (47.2%) after a sharp drop-off in 2003 (-46.3%). Our expectation of 11.1% EPS growth for the water utilities is driven by increased capex and a gradually improving regulatory environment, especially in California (where CWT and AWR are located). We note that capex is the main driver of EPS growth for the regulated water utilities, which are allowed to earn a fixed return on their equity investment in water infrastructure.

As seen in exhibit 6 below, our four covered water utilities are planning to increase their capex to ~$6.5-7B over the next five years vs. ~$5.9B spend over the past five years, an average increase of 16%. This is higher than the 9% increase expected for electric utilities and the 4% increase expected for gas utilities (exhibit 7) over the next three years. We believe that higher capex growth among water utilities should allow for higher EPS growth than rest of the utility sector. Our capex expectation for the water utilities is based on companies' guidance but we believe that given the tremendous need for infrastructure investment, the spending could further accelerate over the next few years. For electric and gas utilities, we have used company guidance (when available) and Street consensus to estimate capex over the next three years.

Exhibit 6: Capex Water Utilities			
	Capex over past 5 yrs	capex over next 5 yrs	Percentage change
AWK	~$3.9B	~$4-4.5B	9%
WTR	$1.2B	~1.5B	25%
CWT	$487M	~$600M	23%
AWR	$349M	~$375M	7%
Total	**~$5.9B**	**~$6.5-7B**	16%

Source: Company Reports, LBR Estimates

Exhibit 7: Capex - Other Utilities

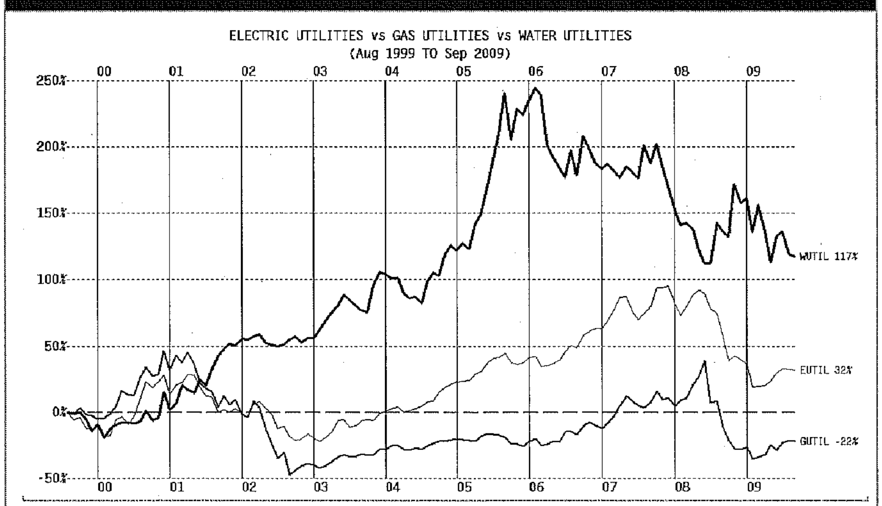
$mil	Expected Capex 2009-2011	Capex 2006-08	Percentage Change
Electric Utilities			
SO	16,600	10,500	58%
FPL	7,760	5,957	30%
DUK	14,225	10,892	31%
D	11,440	11,578	-1%
ETR	5,692	7,227	-21%
AEP	6,375	11,236	-43%
Average			**9%**
Gas Utilities			
SRE	6,975	6,464	8%
EQT	2,314	2,526	-8%
OKE	1,600	2,733	-41%
NFG	1,064	969	10%
EGN	1,183	1,136	4%
AGL	1,329	884	50%
Average			**4%**

Source: Bloomberg, Baseline

OTHER FACTORS CONTRIBUTING TO THE VALUATION PREMIUM

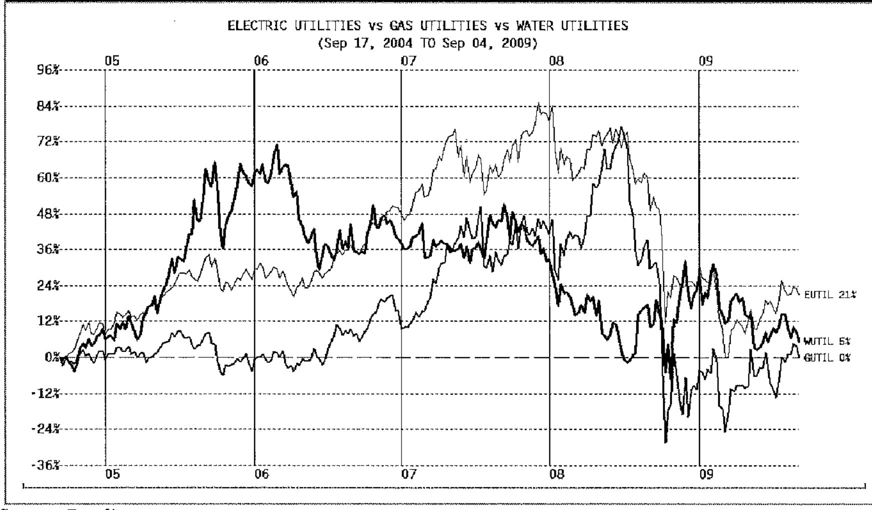
As seen in exhibit 8 and 9 below, water utilities out-performed other utility sectors over the last ten years (water up 117% vs. electric up 32% and gas down 22%) and the gas utilities over the last five years (water up 5% vs. electric up 21% and gas flat at 0%). Over the last year (exhibit 9), as the market plummeted, water utilities again out-performed other utility sectors (water down 7% vs. electric down 21% and gas down 23%). We believe that apart from higher EPS growth discussed above, higher valuation multiples and higher stock returns enjoyed by the water utilities can be attributed to (i) low operational risk, and (ii) scarcity premium.

Exhibit 8: Utility Sector Returns Last 10 yrs



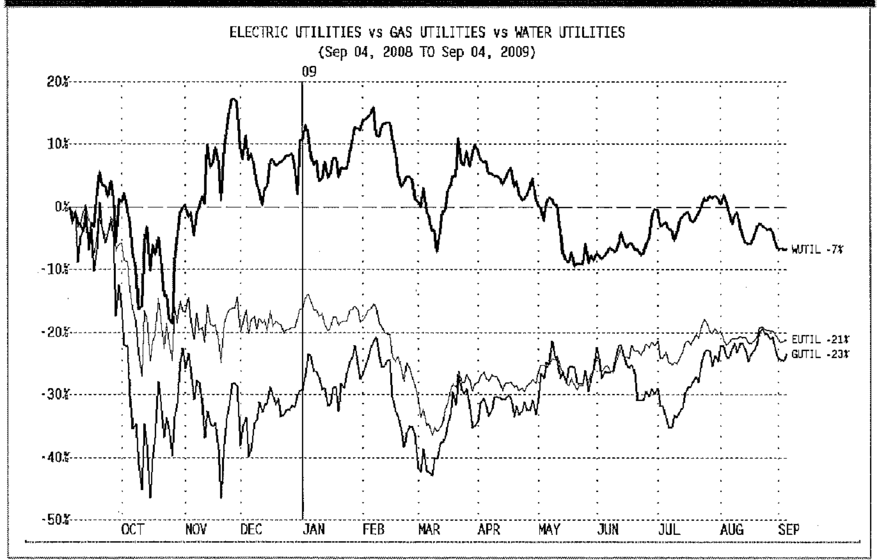
Source: Baseline

Exhibit 9: Utility Sector Returns Last 5 yrs



Source: Baseline

Exhibit 10: Utility Sector Returns Last 1 yrs

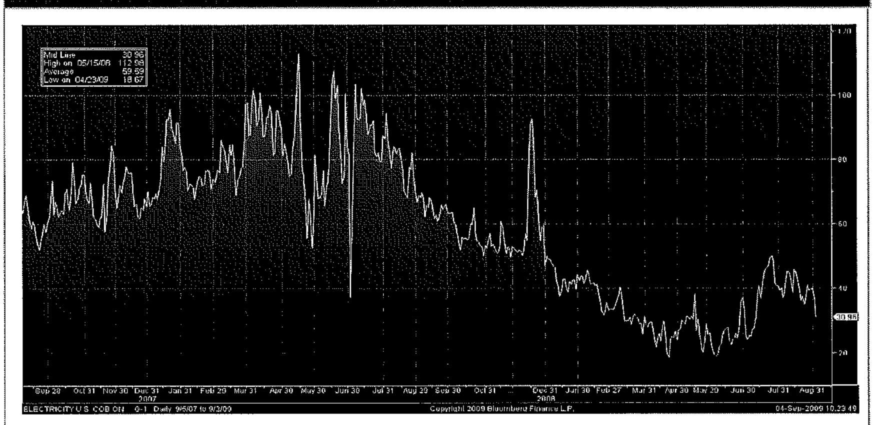


Source: Baseline

Lower operational risk: Unlike electric and gas utilities, water utilities are not as exposed to commodity risk, which we believe contributed to their premium valuation. Water utilities either own pumping rights to local water resources or mostly buy it from public entities or semi-public water co-ops. Rates for purchased water usually increase at a predictable 3-5% annually – at or slightly above inflation. As the water utilities continuously file rate cases (rate increase request), they are able to recover this inflation in the next rate case. In several states, water utilities are even allowed a surcharge for increase in purchased water rates between rate cases.

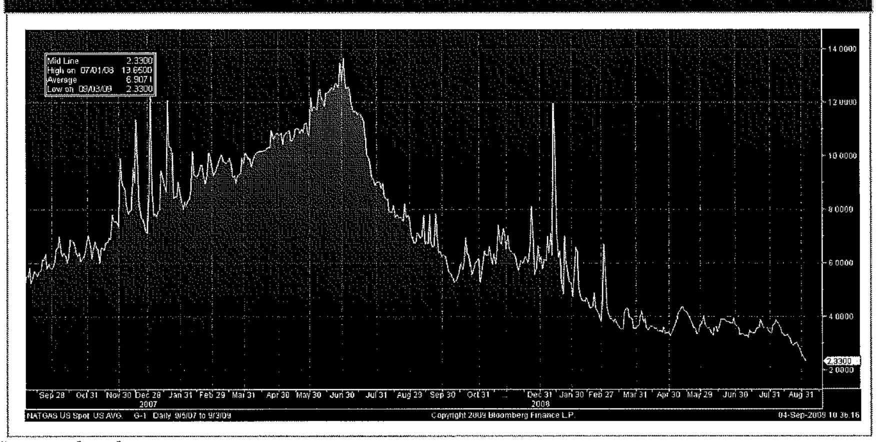
Electric utilities have varying degrees of operating risk from commodity prices depending on their business (integrated utilities/ regulated utilities/independent power producer/ etc.). Several electricity transmission and distribution companies sell electricity to customers at fixed prices set by the State Public Utility Commissions, but have to purchase electricity from the wholesale market, where prices are set by market forces. As seen in exhibit 11 below, wholesale electricity prices can by quite volatile, creating commodity risk for these companies. Electricity generators can be exposed to both wholesale electricity prices and prevailing market prices for coal, natural gas, uranium, fuel oil, and other fuels used in the generation facilities. Fuel costs (exhibit 12, 13) can also be quite volatile. Gas utilities are also similarly exposed to natural gas prices.

Exhibit 11: On- Peak Spot Wholesale Electricity Price at California-Oregon Border



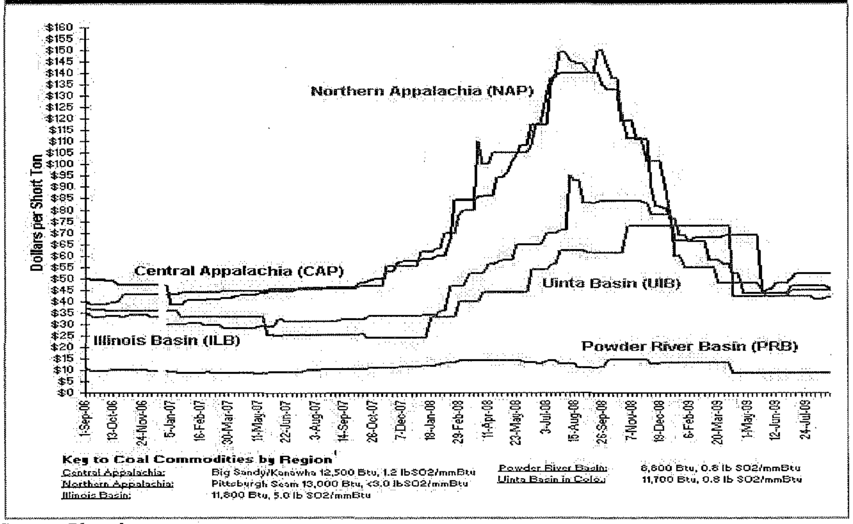
Source: Bloomberg

Exhibit 12: US Average Natural Gas Price



Source: Bloomberg

Exhibit 13: US Coal Prices



Source: Bloomberg

Scarcity Premium: Over a last decade, the water sector has been receiving increased attention as a separate investment class because of (i) increasing demand for water and the need for investment in water-related infrastructure, and (ii) increasing water scarcity – both in the U.S. and around the globe. A 2003 survey by the General Accounting Office, an investigative arm of the U.S. Congress, found that water managers in 36 states anticipated water shortages locally, regionally or statewide within the next ten years. Increasing population shift to arid regions in western and southeastern U.S., where water resources are already strained, is exacerbating the problem. Though 70-75% of earth's surface is covered by water only three-tenths of a percent of this water, present in groundwater aquifers, rivers, and freshwater lakes, is useable. Apart from population growth, per-capita water consumption is also growing rapidly in developing countries due to urbanization and industrialization. This is putting strain on water resources, requiring large investments to build and expand water-related infrastructure.

A number of ETFs and funds have been launched in the last decade that exclusively invest in water-related public companies. In 2007, Global Water Intelligence, a leading industry publication, calculated that between September 2005 and July 2007, money held by specialist water funds increased ten times from $1.2B to $13.4B. Also 15 new specialist water funds were launched just between January and July 2007. Since then we have seen a steady increase in number of water funds.

As 85% of water utilities are owned by the municipalities, there are only 11 publicly-traded water utilities in the U.S. with a total market cap of just $8.4B. This compares to $131.2B market cap for seven largest electric utilities and $50.3B for seven largest gas utilities. We believe that the increased investment in water utility stocks , which have a limited total market cap, has created a scarcity premium for them, giving them a higher multiple than the broader utility sector. The scarcity is further exacerbated by large retail ownership of water utility stocks (WTR 53%, CWT 46%, and AWR 41%).

We believe that as these factors continue to play a role, water utilities should enjoy higher valuation multiples and stock returns vs. the broader utility sector going forward.

INVESTMENT THESIS

AWK

We rate American Water Works Company, Inc. (AWK) a BUY with a $24 target price, as we see AWK as offering an attractive risk/reward with positive catalysts relative to the peer group. We believe AWK shares are already discounting RWE's anticipated exit as the former parent company has announced plans to soon sell its remaining 24% stake in AWK. While the timing of this cannot be predicted, we believe AWK's discounted valuation by investors is overdone. The shares are trading at 13.4x our FY10E EPS, relative to a peer group average of 19.0x. We also believe there is also an opportunity for multiple expansion toward the peer group average of once the RWE overhang abates. However, our target price still incorporates a 16% discount to the peer group average. We also like that AWK is investing heavily in capex, at an expected rate of $4.0-4.5B over the next five years, and is in a ROE recovery mode as the company plays catch up to the lower ROE earned from FY03-FY07. We see adjusted ROE improving to 9.7% in FY11E vs. 8.3% in FY08, putting it closer in line with the peer group average. Other notable positives for the company include an industry leading 4.2% dividend yield and the potential for further acquisitions as municipalities and smaller participants look to raise cash. The latter could offer a positive surprise, although we are not modeling for acquisitive growth.

CWT

We rate California Water Service Group (CWT) as a BUY with a $45 target price, which represents 20.5x our FY10E EPS of $2.20, in line with the company's historical average. We like CWT's position in the regulatory favorable California market. Further, with an approximate 10.2% ROE and a 51% equity/capital ratio (2Q end), we estimate for every $100M increase in net fixed assets, the company can increase its net income by $5.0M ($0.24/share). As such, CWT's $100M-120M in FY09E capex could potentially drive meaningful EPS growth in the next two-to-three years. On valuation, CWT shares are trading at 16.7x our FY10E EPS of $2.20, which we believe to be conservative when compared to the industry average of 19.0x and the company's historical average of 20.5x. Additionally, while CWT has historically seen higher earnings volatility from variation in water consumption, recent regulatory changes in California (WRAM and MBCA implementation) should help reduce earnings volatility and provide better visibility. In summation, rate relief and improved ROE (we are modeling 10.8%) in FY10E, greater than the company's 8.9% five-year average, provide positive potential catalysts going forward.

WTR

We rate Aqua America, Inc. (WTR) as a NEUTRAL as we believe the shares are fairly valued on our expectations of 11.3% earnings growth over the next three years. However, we see downside risk to WTR as fairly limited as the company is trading at a 19% discount to its historical forward P/E of 23x. Additionally, at 2.1x price-to-book, it is a near full multiple point below its average 2.9x ratio (on book value of $7.91/share). Compared to the peer group, we see WTR's valuation as reasonable given the company's size and operational efficiency (O&M ratio is industry leading). We believe this justifies WTR as a proxy play on the water utilities space. However, despite the slight discount the shares are trading relative to historical averages, we see the potential upside relative to our preferred names of CWT and AWK as less attractive.

Overall, we like WTR's position as one of the leading publicly traded water utility serving approximately three million people in 13 states. The water utilities industry is highly regulated, but also fragmented, which presents opportunities for acquisitive growth, especially as cash strapped municipalities and smaller private participants look to raise cash to weather the current economic downturn by potentially selling off water systems. More important, we expect 2009 and 2010 to be catch-up years for rate increases. $64.7M and $27.2M in rate increases were approved in 2008 and 2009 YTD, respectively, and $59.2M in increases are either pending or will be filed in the remainder of 2009. Additionally, WTR has surcharges in six of its 13 states of operations, which allows the company to start earning a return on its investment between rate increases. These factors, coupled with lower equity dilution from increased operating cash flow generation, should accelerate the pace of EPS growth in the next three years. We see WTR's estimated earnings growth of 11.3% from FY09E to FY11E outpacing the flat growth from FY05 to FY08.

AWR

We rate American States Water Company (AWR) as a NEUTRAL, as we see the upside potential related to rate relief as already largely reflected in the shares. At 18.4x our FY10E EPS of $1.91, AWR is trading at below its historical 20x forward P/E average and at a discount compared to the peer group average of 19.0x. While we argue that a valuation premium is justified given the company's concentration in the regulatory-favorable California market, given the company's valuation relative to our preferred names in the space – AWK and CWT – we do not see material upside potential at this time from current levels.

A principal driver of earnings growth would be the start-up of the Ft. Bragg, North Carolina construction project and successful price redeterminations at other military bases, which we estimate could increase EPS by another 3%. However, due to limited visibility, we have not added these potential catalysts into our EPS forecasts. Our estimates do, however, include an average ROE of 9.7% from FY09E to FY11E vs. the company's historical 8.7% average. This is driven by increased capital spending of $75-80M in FY09, in line with FY08 levels. Since capex has grown at a CAGR of 12% from 2003-2008, AWR should see rate relief leading to 11.3% EPS growth in FY09E and potentially 10.1% in FY10E. In the long term, we like AWR, currently the fourth largest publicly traded domestic water utility, as the WRAM/MBCA implementation in California should remove the quarterly earnings volatility caused by the changes in water consumption. We note that seasonal variation will still exist. These mechanisms have somewhat reduced the single-state operational risk that AWK faced previously. However, we believe benefits from the improved regulatory environment and earnings upside from recently approved rate cases are already mostly priced into the shares.

VALUATION

AWK

AWK shares closed yesterday at $19.99, which is 15.3x our FY09E EPS of $1.31 and 13.4x our FY10E EPS of $1.50. The shares are trading at a discount to the peer group average of 19.0x due in large part to the RWE overhang, which we believe the Street is already accounting for. The shares are trading at 1.2x tangible book value compared to a peer group that trades over 1.8x, on average. Our target price of $24 is based on 16.0x our FY10E EPS, a valuation that remains at a discount to the peer group. However, we see multiple expansion from current levels as justified given AWK's position as the largest and most diversified publicly-traded water utility in the U.S. and with the potential from earnings growth as the company catches up to insufficient rate increases during the past five-to-six years.

CWT

CWT shares closed yesterday at $36.75, which is 17.3x our FY09E EPS estimate of $2.12 and 16.7x our FY10E EPS estimate of $2.20. The shares are trading at a discount to the company's historical normalized 20.5x average and normalized range of 17-27x forward P/E. Compared to CWT's water utility peers, the company trades at a discount, although this has narrowed as more predictable earnings streams from the implementation of WRAM and MCBA has removed some the unpredictability in earnings associated with the company's extensive geographic presence in California.

WTR

We believe WTR is fairly valued on our expectations of 11.3% earnings growth over the next three years. Despite the slight discount the shares are trading relative to historical averages, we see the potential upside relative to our preferred names of CWT and AWK as less attractive. WTR shares closed yesterday at $16.85, which is 20.5x our FY09E EPS estimate of $0.82 and 18.6x our FY10E EPS estimate of $0.91. The shares are trading at a discount to the company's historical 23x average and normalized range of 20-30x forward P/E.

AWR

At 18.4x our FY10E EPS of $1.91, AWR shares are trading at a discount to its historical 20x forward P/E average as well as to the peer group average of 19.0x. While we argue that a valuation premium is justified for AWR given the company's concentration in the regulatory-favorable California market, should multiples expand to 20x, a fair value of $38/share does not imply the same amount of potential upside as do our preferred names in the space – AWK and CWT. AWR shares closed Friday at $35.23, which is 20.3x our FY09E EPS of $1.74 and 18.4x our FY10E EPS of $1.91. The shares are trading at a discount to the company's historical 20x average and a normalized range of 18-28x forward P/E.

RISKS

AWK

The potential downside risks to our investment thesis include, but are not limited to: 1) delays in rate case processing or lower rate increases by the regulators than our expectations, 2) 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, 4) a large acquisition at an excessive valuation (significantly above the rate base), and 5) a large goodwill impairment which could lead to a breach of debt covenants or regulatory requirements.

CWT

Potential downside risks to our investment thesis include, but are not limited to: 1) lower rate increase approvals by the California Public Utility Commission (CPUC) than our expectation, 2) near-term run up in raw material costs, and 3) large acquisition(s) at excessive valuation(s) (significantly above the rate base).

WTR

Potential downside risks to our investment thesis 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 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.

AWR

The potential downside risks to our investment thesis include, but are not limited to: 1) lower rate increase approvals by the California Public Utility Commission (CPUC) than our expectation, 2) increases in raw material costs, and 3) an acquisition of a large water system by the local government through eminent domain.

The potential upside risks to our investment thesis include, but are not limited to: 1) favorable rate case approvals, and 2) the commencement of the large "special" construction project at Ft. Bragg, North Carolina, or any other base.

American Water Works— Quarterly Income Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09E	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E
Regulated Segment	419.3	508.6	571.9	487.8	449.9	527.1	603.7	502.1	497.4	554.9	646.7	547.0	524.2	605.7	700.4	592.3
% Increase			7.3%	11.2%	7.3%	3.6%	5.6%	2.9%	10.6%	5.3%	7.1%	8.9%	5.4%	9.2%	8.3%	8.3%
Non-Regulated Revenue	53.3	55.5	66.4	67.5	61.0	67.0	73.9	70.3	57.5	64.2	70.9	67.3	63.3	70.6	78.0	74.1
% Increase			0.4%	27.7%	14.4%	20.8%	9.4%	4.1%	-5.7%	-4.2%	-4.1%	-4.3%	10.0%	10.0%	10.0%	10.0%
Other	(4.0)	(5.4)	(5.1)	(1.5)	(4.1)	(4.7)	(5.4)	(3.9)	(4.7)	(6.3)	(6.5)	(5.5)	(5.2)	(6.1)	(7.0)	(5.9)
% Regulated Rev	-1.0%	-1.1%	-0.9%	-0.3%	-0.9%	-0.9%	-0.9%	-0.8%	-1.0%	-1.1%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%
Operating revenues	**468.5**	**558.7**	**633.1**	**553.8**	**506.8**	**589.4**	**672.2**	**568.6**	**550.2**	**612.7**	**711.1**	**608.8**	**582.3**	**670.3**	**771.4**	**660.4**
Operation and maintenance	282.6	299.4	328.3	336.2	311.3	330.6	342.2	319.8	314.4	330.6	359.1	344.1	329.0	361.9	382.9	359.6
Depreciation and amortization	64.6	68.1	69.7	64.9	63.9	67.3	68.4	71.6	68.8	73.2	73.2	73.2	74.8	76.3	77.9	79.5
General taxes	47.9	45.9	47.1	42.3	52.1	49.6	49.4	48.0	52.5	51.7	49.3	50.6	54.5	52.0	52.0	50.6
Loss (gain) on sale of assets	0.1	(6.2)	(0.7)	(0.5)	(0.1)	(0.8)	0.5	(0.0)	(0.2)	0.0	(0.3)	(0.3)	(0.3)	(0.3)	(0.3)	(0.3)
Impairment charges			243.3	266.0	750.0				450.0							
EBIT	**73.3**	**151.5**	**(54.6)**	**(155.1)**	**(670.4)**	**142.7**	**211.8**	**129.1**	**(335.4)**	**157.2**	**229.7**	**141.3**	**124.3**	**180.3**	**258.9**	**171.0**
Operating Margin (excluding impairment)	*16%*	*27%*	*30%*	*20%*	*16%*	*24%*	*32%*	*23%*	*21%*	*26%*	*32%*	*23%*	*21%*	*27%*	*34%*	*26%*
Interest	72.2	70.8	68.739	71.5	70.0	70.1	72.7	72.4	72.0	73.7	74.4	75.2	76.2	77.2	78.2	79.2
Other income, net	(3.0)	(1.9)	(2.9)	(4.6)	(3.7)	(3.1)	(6.7)	(8.0)	(4.8)	(2.6)	(5.5)	(5.2)	(4.6)	(4.5)	(5.0)	(4.8)
Total other income (deductions)	**69.2**	**68.9**	**65.8**	**66.8**	**66.2**	**67.0**	**66.0**	**64.5**	**67.1**	**71.1**	**68.9**	**70.0**	**71.7**	**72.7**	**73.2**	**74.4**
EBT	**4.2**	**82.6**	**(120.5)**	**(221.9)**	**(736.6)**	**75.7**	**145.8**	**64.6**	**(402.5)**	**86.1**	**160.9**	**71.3**	**52.7**	**107.6**	**185.6**	**96.7**
Provision for income taxes	1.7	32.648	39.7	12.7	(4.1)	30.2	57.5	28.2	10.6	34.1	63.8	28.2	20.8	42.5	73.3	38.2
Implied Tax Rate (excl. goodwill impairment)	42%	40%	32%	29%	-31%	40%	39%	44%	22%	39.6%	39.6%	39.6%	39.5%	39.5%	39.5%	39.5%
Income (loss) from continuing operations	**2.4**	**50.0**	**(160.2)**	**(234.6)**	**(732.5)**	**45.5**	**88.2**	**36.4**	**(413.1)**	**52.0**	**97.1**	**43.0**	**31.9**	**65.1**	**112.3**	**58.5**
Loss (income) from discontinued operations, net of tax	(0.26)	0.81	0.00	0.00												
Net Income (loss)	**2.7**	**49.2**	**(160.2)**	**(234.6)**	**(732.5)**	**45.5**	**88.2**	**36.4**	**(413.1)**	**52.0**	**97.1**	**43.0**	**31.9**	**65.1**	**112.3**	**58.5**
Diluted EPS from continuing operations	0.02	0.31	(1.00)	(1.47)	(4.58)	0.28	0.55	0.23	(2.58)	0.32	0.56	0.25	0.18	0.37	0.62	0.32
EPS excl. impairment & one-time expenses	**0.02**	**0.31**	**0.52**	**0.17**	**0.11**	**0.28**	**0.55**	**0.23**	**0.19**	**0.32**	**0.56**	**0.25**	**0.18**	**0.37**	**0.62**	**0.32**
Diluted Average Shares	160.0	160.0	160.0	160.0	160.0	159.9	160.0	159.9	159.9	164.8	174.4	174.4	175.6	177.8	180.0	182.2
Financial Summary																
Total Revenue growth			6.8%	12.4%	8.2%	5.5%	6.2%	2.7%	8.6%	4.0%	5.8%	7.1%	5.8%	9.4%	8.5%	8.5%
Non-Regulated Revenue growth			0.4%	27.7%	14.4%	20.8%	11.3%	4.1%	-5.2%	-4.5%	5.0%	5.0%	10.0%	10.0%	10.0%	10.0%
O&M/Revenue	60.3%	53.6%	51.9%	60.7%	61.4%	56.1%	50.9%	56.2%	57.1%	54.0%	50.5%	56.5%	56.5%	54.0%	49.6%	54.4%
General Taxes/ Regulated Revenue	11.4%	9.0%	8.2%	8.7%	11.6%	9.4%	8.2%	9.6%	10.6%	9.3%	7.6%	8.9%	10.4%	8.6%	7.4%	8.6%
Adj. EBITDA	137.9	219.6	258.4	175.8	143.6	210.0	280.2	200.7	183.5	230.4	302.9	214.5	199.1	256.6	336.8	250.5
EPS growth, excluding goodwill impairment charge					620.8%	-8.9%	6.0%	34.0%	73.6%	10.9%	1.0%	8.3%	-4.5%	16.0%	12.1%	30.1%

Source: Company reports, Longbow estimates

American Water Works— Annual Income Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	FY04A	FY05A	2006A	FY07A	FY08A	FY09E	FY10E	FY11E
Regulated Segment	1748.0	1836.1	1854.6	1987.6	2082.7	2245.9	2422.6	2594.8
% Increase		5.0%	1.0%	7.2%	4.8%	7.8%	7.9%	7.1%
Non-Regulated Revenue	290.0	310.8	248.5	242.7	272.2	259.9	285.9	314.5
% Increase		7.2%	-20.0%	-2.3%	12.2%	-4.5%	10.0%	10.0%
Other	-20.17	(10.1)	(10.0)	(16.0)	(18.0)	(23.0)	(24.2)	(25.9)
% Regulated Rev	-1.2%	-0.6%	-0.5%	-0.8%	-0.9%	-1.0%	-1.0%	-1.0%
Operating revenues	**2,017.9**	**2,136.7**	**2,093.1**	**2,214.2**	**2,336.9**	**2,482.8**	**2,684.3**	**2,883.3**
Operation and maintenance	1122.0	1201.6	1174.5	1246.5	1303.8	1348.2	1433.4	1522.4
Depreciation and amortization	225.3	261.4	259.2	267.3	271.3	288.5	308.4	322.7
General taxes	170.2	183.3	185.1	183.3	199.1	204.1	209.1	214.1
Loss (gain) on sale of assets	(8.6)	(6.5)	0.1	(7.3)	(0.4)	(0.8)	(1.2)	(1.2)
Impairment charges	78.7	385.4	221.7	509.3	750.0	450.0	0.0	0.0
EBIT	**430.4**	**111.6**	**252.5**	**15.1**	**(186.9)**	**192.8**	**734.5**	**825.3**
Operating Margin (excluding impairment)	*25%*	*23%*	*23%*	*24%*	*24%*	*25.9%*	*27.4%*	*28.6%*
Interest	315.9	345.3	366.0	283.2	285.2	295.3	310.7	324.6
Other income, net	(11.0)	(9.5)	(4.5)	(12.5)	(21.5)	(18.2)	(18.8)	(19.0)
Total other Income (deductions)	**305.0**	**335.7**	**361.5**	**270.6**	**263.7**	**277.1**	**291.9**	**305.6**
EBT	**125.4**	**(224.2)**	**(108.9)**	**(255.5)**	**(450.6)**	**(84.25)**	**442.6**	**519.8**
Provision for income taxes	66.3	51.0	46.9	86.8	111.8	136.7	174.8	205.3
Implied Tax Rate (excl. goodwill impairment)	32.5%	31.6%	41.6%	34.2%	37.3%	37.4%	39.5%	39.5%
Income (loss) from continuing operations	**59.1**	**(275.1)**	**(155.9)**	**(342.3)**	**(562.4)**	**(221.0)**	**267.7**	**314.4**
Loss (income) from discontinued operations, net of tax	124.0	49.9	6.4	0.6				
Net Income (loss)	**(64.9)**	**(325.0)**	**(162.2)**	**(342.8)**	**(562.4)**	**(221.0)**	**267.7**	**314.4**
Diluted EPS from continuing operations	0.37	(1.72)	(0.97)	(2.14)	(3.52)	(1.31)	1.50	1.67
EPS excl. impairment & one-time expenses	**0.86**	**0.69**	**0.41**	**1.04**	**1.17**	**1.31**	**1.50**	**1.67**
Diluted Average Shares	160.0	160.0	160.0	160.0	160.0	168.4	178.9	188.1
Financial Summary								
Total Revenue growth		5.9%	-2.0%	5.8%	5.5%	6.2%	8.1%	7.4%
Non-Regulated Revenue growth			-20.0%	-2.3%	12.2%	-4.5%	10.0%	10.0%
O&M/Revenue	55.6%	56.2%	56.1%	56.3%	55.8%	54.3%	53.4%	52.8%
Depreciation and amortization/ Net Fixed Asset				3.1%	2.9%	2.8%	2.9%	2.9%
Depreciation Growth		16.0%	-0.8%	3.1%	1.5%	6.3%	6.9%	4.6%
General Taxes/ Regulated Revenue	9.7%	10.0%	10.0%	9.2%	9.6%	9.1%	8.6%	8.3%
Adj. EBITDA	734.3	758.4	733.4	791.8	834.4	931.3	1,042.9	1,148.0
Interest Expense/ Average Net Debt			8.9%	6.2%	5.6%	5.5%	5.6%	5.7%
Interest Expense/Revenue	15.7%	16.2%	17.5%	12.8%	12.2%	11.9%	11.6%	11.3%
Net Income Growth (excl. goodwill impairment)		338.6%	-1.6%	180.1%	12.6%	22.1%	16.9%	17.4%
EPS growth, (excl. goodwill impairment)			-40.3%	153.8%	12.3%	11.6%	14.4%	11.7%
ROE (excl. goodwill & goodwill impairment)			2.3%	7.0%	8.3%	8.6%	8.8%	9.3%

Source: Company reports, Longbow estimates

American States Water — Quarterly Earnings Statement

Garik Shmois/ Vishal Khetriwal, CFA
Longbow Research
216-525-8414

(dollars in millions, except per share data)

FY ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09E	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E
Water	50.3	60.8	65.4	61.3	52.1	65.4	69.4	61.1	56.8	74.2	71.8	64.1	65.4	82.7	80.3	72.0
Electric	8.9	6.3	6.3	7.2	8.8	6.2	6.7	6.7	8.6	5.9	7.1	7.9	10.0	7.3	8.2	8.1
Contracted Services	13.1	12.2	4.1	5.6	8.1	8.7	9.2	16.4	14.2	13.5	13.0	12.0	12.0	12.0	12.0	12.0
Total Revenue	**72.3**	**79.2**	**75.8**	**74.0**	**68.9**	**80.3**	**85.3**	**84.2**	**79.6**	**93.6**	**92.0**	**84.0**	**87.4**	**102.0**	**100.4**	**92.1**
Expenses																
Supply Costs	16.8	19.0	22.6	19.8	16.1	20.5	24.2	20.0	19.9	23.5	25.0	21.0	22.9	25.6	27.9	23.3
Gen. & Admin. expenses	13.0	13.7	11.8	14.2	14.8	14.9	16.3	16.6	16.9	15.5	17.0	16.4	18.4	18.9	19.1	18.4
Other O&M	9.6	10.9	10.9	11.8	11.8	11.8	11.4	11.4	11.2	11.1	12.2	11.3	12.2	14.8	13.2	12.3
ASUS Construction Expenses	9.1	8.3	1.9	2.9	3.9	4.4	5.1	10.4	8.4	7.8	6.5	6.0	6.0	6.0	6.0	6.0
Gain on sale of water rights/property	(0.4)	(0.2)	0.0	0.0					(0.0)							
Unrealized loss(gain) on purch pwr contracts	(2.7)	0.2	0.9	(0.5)	(2.8)	(1.7)	3.7	(0.8)								
Total Operation & Maintenance	**45.4**	**51.9**	**48.1**	**48.1**	**43.8**	**50.1**	**60.8**	**57.7**	**56.4**	**57.9**	**60.7**	**54.7**	**59.5**	**65.3**	**66.2**	**60.0**
Depreciation & Amortization	7.1	7.1	7.4	7.3	7.8	7.8	7.9	8.1	8.4	8.4	8.5	8.6	8.7	8.8	9.0	9.1
General Taxes	2.9	2.8	2.8	2.7	2.9	2.8	3.5	3.1	3.4	2.7	2.7	4.5	3.4	3.5	3.6	3.5
Total Expenses	**55.4**	**61.8**	**58.3**	**58.1**	**54.5**	**60.7**	**72.1**	**68.9**	**68.19**	**69.0**	**71.9**	**67.8**	**71.6**	**77.6**	**78.7**	**72.7**
Income from Operations	**16.9**	**17.5**	**17.5**	**15.9**	**14.5**	**19.6**	**13.1**	**15.3**	**11.4**	**24.5**	**20.1**	**16.2**	**15.8**	**24.4**	**21.7**	**19.4**
Operating Margin	23.3%	22.0%	23.1%	21.5%	21.0%	24.4%	15.4%	18.2%	14.3%	26.2%	21.8%	19.3%	18.1%	24.0%	21.6%	21.1%
Other Inc. (loss)	0.1	(0.1)	0.1	0.1	0.1	0.0	(0.0)	(7.7)	(0.0)	0.1						
EBIT	**16.9**	**17.4**	**17.6**	**16.0**	**14.6**	**19.6**	**13.1**	**7.6**	**11.4**	**24.6**	**20.1**	**16.2**	**15.8**	**24.4**	**21.7**	**19.4**
EBIT (%)	23.4%	21.9%	23.2%	21.6%	21.1%	24.4%	15.4%	9.0%	14.3%	26.3%	21.8%	19.3%	18.1%	24.0%	21.6%	21.1%
Interest Expense	4.9	5.0	4.8	4.5	5.0	4.5	5.1	4.8	5.1	5.4	5.0	4.7	4.8	4.9	5.0	6.5
Income Before Taxes	**12.0**	**12.4**	**12.9**	**11.4**	**9.6**	**15.1**	**8.0**	**2.8**	**6.3**	**19.2**	**15.1**	**11.5**	**11.0**	**19.6**	**16.7**	**13.0**
Provision for Income Taxes	5.0	5.2	5.2	5.3	4.3	5.8	3.4	(0.1)	1.4	7.7	6.1	4.7	4.5	8.0	6.8	5.3
Implied Tax Rate	41.8%	42.0%	40.7%	46.6%	44.5%	38.4%	42.9%	-3.2%	21.7%	40.2%	40.8%	40.8%	40.8%	40.8%	40.8%	40.8%
Net Income	7.0	7.2	7.6	6.1	5.3	9.278	4.6	2.9	4.9	11.5	8.9	6.8	6.5	11.6	9.9	7.7
EPS (fully diluted)	0.40	0.42	0.44	0.35	0.30	0.53	0.26	0.16	0.28	0.64	0.48	0.37	0.35	0.62	0.53	0.41
EPS (fully diluted, ex one-time items)	**0.31**	**0.43**	**0.47**	**0.35**	**0.30**	**0.47**	**0.39**	**0.40**	**0.28**	**0.61**	**0.48**	**0.37**	**0.35**	**0.62**	**0.53**	**0.41**
Weighted Avg. Shares	17.1	17.1	17.2	17.3	17.4	17.3	17.3	17.4	17.4	18.0	18.6	18.6	18.6	18.7	18.7	18.7
Financial Summary (values in %)																
Water revenue growth	4.5%	14.5%	0.7%	15.6%	3.5%	7.5%	6.0%	-0.3%	9.0%	13.4%	3.5%	4.9%	15.1%	11.5%	11.8%	12.3%
Electric revenue growth	6.3%	-11.0%	-2.4%	-3.9%	-0.7%	-0.8%	7.2%	-6.9%	-1.9%	-5.2%	5.9%	18.0%	16.4%	24.1%	14.2%	2.8%
Contracted Services growth	217%	512%	75.9%	-52.3%	-38.4%	-28.2%	123%	195%	76%	54.6%	42.0%	-26.9%	-15.4%	-11.2%	-7.7%	0.0%
Total Revenue growth	19.2%	27.5%	2.8%	2.6%	-4.6%	1.3%	12.4%	13.8%	15.5%	16.5%	7.9%	-0.3%	9.8%	9.1%	9.2%	9.7%
Operations & Maintenance/Revenue	62.8%	65.4%	63.4%	65.0%	63.5%	62.4%	71.3%	68.5%	70.9%	61.9%	66.0%	65.1%	68.1%	64.0%	65.9%	65.2%
Supply Costs/Revenue (excl. Military Base)	28.4%	28.4%	31.4%	28.9%	26.5%	28.7%	31.8%	29.5%	30.4%	29.4%	31.6%	29.2%	30.3%	28.4%	31.5%	29.1%
Gen. & Admin./Revenue	18.0%	17.2%	15.5%	19.2%	21.5%	18.6%	19.1%	19.8%	21.2%	16.6%	18.5%	19.5%	21.1%	18.5%	19.0%	20.0%
Other O&M/Revenue	13.2%	13.8%	14.4%	15.9%	17.1%	14.7%	13.4%	13.6%	14.1%	11.8%	13.3%	13.5%	14.0%	14.5%	13.2%	13.4%
General Taxes/Revenue	4.1%	3.6%	3.7%	3.6%	4.2%	3.5%	4.1%	3.7%	4.3%	2.9%	2.9%	5.3%	3.9%	3.4%	3.6%	3.8%
EPS Growth	14.7%	16.7%	38.3%	17.6%	-25.0%	26.2%	-40.6%	-53.4%	-5.7%	20.6%	83%	122%	23.9%	-2.9%	10.3%	12.4%

Source: Company reports, Longbow estimates

American States Water — Annual Earnings Statement
Garik Shmois/ Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	2004A	2005A	2006A	2007	2008	2009E	2010E	2011E
Water	200.6	205.5	219.2	237.9	247.9	266.9	300.3	328.3
Electric	25.6	27.2	29.3	28.6	28.4	29.5	33.6	34.5
Other	1.8	3.5	20.1	34.9	42.4	52.7	48.0	48.0
Total Revenue	**228.0**	**236.2**	**268.6**	**301.4**	**318.7**	**349.1**	**381.9**	**410.8**
Expenses								
Supply Costs	81.1	71.9	76.2	78.2	80.9	89.4	99.7	107.9
Gen. & Admin. expenses	41.8	44.3	47.1	52.6	62.7	65.8	74.8	80.1
Other O&M	31.6	32.0	36.4	43.2	46.4	45.8	52.6	56.1
ASUS Construction Expenses			9.0	22.1	23.9	28.8	24.0	24.0
Gain on sale of water rights/property	(5.7)	0.0	(0.3)	(0.6)	0.0	0.0	0.0	0.0
Unrealized loss on purch power contracts	0.1	(5.4)	7.1	(2.1)	(1.6)			
Total Operation & Maintenance	**148.9**	**142.8**	**175.6**	**193.4**	**212.3**	**229.8**	**251.0**	**268.1**
Depreciation & Amortization	20.8	21.9	26.3	28.9	31.6	33.8	35.5	37.1
General Taxes	8.8	9.3	10.2	11.3	12.3	13.3	14.0	15.0
Total Expenses	**178.5**	**174.0**	**212.0**	**233.6**	**256.2**	**276.9**	**300.6**	**320.3**
Income from Operations	**49.5**	**62.3**	**56.6**	**67.7**	**62.5**	**72.2**	**81.4**	**90.5**
Operating Margin	21.7%	26.4%	21.1%	22.5%	19.6%	20.7%	21.3%	22%
Other Inc. (loss)	0.3	(0.0)	0.5	0.30	(7.6)	0.1	0.0	0.0
EBIT	**49.8**	**62.2**	**57.1**	**68.0**	**54.9**	**72.2**	**81.4**	**90.5**
EBIT (%)	0.2	0.3	0.2	0.2	0.2	0.2	0.2	0.2
Interest Expense	17.9	13.6	18.3	19.21	19.5	20.2	21.1	23.0
Income Before Taxes	**31.9**	**48.6**	**38.8**	**48.8**	**35.4**	**52.1**	**60.3**	**67.6**
Provision for Income Taxes	13.4	21.9	15.7	20.8	13.4	19.9	24.6	27.5
Implied Tax Rate	41.9%	45.0%	40.5%	42.6%	37.8%	38.3%	40.8%	40.8%
Net Income	18.5	26.7	23.1	28.0	22.0	32.1	35.7	40.0
EPS (fully diluted)	1.19	1.59	1.33	1.61	1.26	1.77	1.91	2.13
EPS (fully diluted, ex.one-time items)	**1.06**	**1.16**	**1.44**	**1.56**	**1.56**	**1.74**	**1.91**	**2.13**
Weighted Avg. Shares	15.6	16.8	17.1	17.2	17.4	18.2	18.7	18.8
Financial Summary (values in %)								
Water revenue growth	7.2%	2.4%	6.7%	8.5%	4.2%	7.6%	12.5%	9.3%
Electric revenue growth	4.5%	6.4%	7.5%	-2.4%	-0.5%	3.9%	13.8%	2.6%
Other	75.1%	96.1%	477.9%	73.5%	21.3%	24.4%	-8.9%	0.0%
Total Revenue growth	7.2%	3.6%	13.7%	12.2%	5.8%	9.5%	9.4%	7.6%
Operations & Maintenance/Revenue	65.3%	60.4%	65.4%	64.2%	66.6%	65.8%	65.7%	65.3%
Supply Costs/Revenue (excl. Military Base)	35.8%	30.9%	30.7%	29.4%	29.3%	30.2%	29.8%	29.7%
Gen. & Admin./Revenue	18.3%	18.7%	17.5%	17.5%	19.7%	18.8%	19.6%	19.5%
Other O&M/Revenue	13.8%	13.5%	13.5%	14.3%	14.6%	13.1%	13.8%	13.7%
General Taxes/Revenue	3.9%	4.0%	4.1%	4.2%	4.5%	4.5%	4.2%	4.1%
(Dep + Amort)/Net Fixed Assets	3.3%	3.3%	3.7%	3.9%	4.1%	4.1%	4.1%	4.1%
(Dep + Amort)/Revenue	9.1%	9.3%	9.8%	9.6%	9.9%	9.7%	9.3%	9.0%
Interest Expense/Avg. Net Debt	6.4%	4.8%	6.1%	6.3%	6.0%	5.9%	6.0%	6.2%
Interest Expense/Revenue	7.8%	5.8%	6.8%	6.4%	6.1%	5.8%	5.5%	5.6%
Average ROE	8.0%	10.4%	8.4%	9.6%	7.2%	9.6%	9.7%	10.2%
EPS growth, excluding one-time items	52.0%	9.4%	24.1%	8.3%	0.0%	11.3%	10.1%	11.5%

Source: Company reports, Longbow estimates

California Water Service Group — Quarterly Earnings Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414

(dollars in millions, except per share data)

FY Ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09E	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E
Total Revenue	71.6	95.8	113.9	85.9	72.9	105.6	131.7	100.1	86.6	116.7	136.7	107.5	93.3	121.5	142.6	112.3
Watet Production Costs	25.8	37.3	45.1	30.8	25.4	40.3	46.5	34.4	28.9	41.7						
Administrative & General	12.6	14.3	14.7	12.7	13.4	13.8	15.0	17.2	18.9	19.4						
Other Operations	11.1	11.0	11.8	12.5	12.1	12.8	12.9	13.4	12.5	14.3						
Maintainence	4.5	5.2	4.2	4.4	4.1	4.9	3.8	6.1	4.6	4.3						
Operations & Maintenance	54.0	67.8	75.8	60.2	55.0	71.9	78.2	71.1	64.8	79.7	81.5	76.8	69.6	82.6	83.9	78.2
Depreciation and Amortization	8.4	8.4	8.4	8.4	9.2	9.3	9.3	9.6	10.2	10.3	10.3	10.4	10.5	10.6	10.7	10.7
General Taxes	3.4	3.4	3.7	3.1	3.7	3.5	3.9	3.7	4.1	3.9	4.0	3.9	4.4	4.0	4.2	4.0
Total Expenses	65.8	79.6	87.9	71.8	67.9	84.7	91.4	84.3	79.1	93.9	95.7	91.0	84.5	97.3	98.7	92.9
Income from Operations	5.8	16.2	26.0	14.1	5.0	20.9	40.3	15.8	7.5	22.7	40.9	16.5	8.8	24.3	43.9	19.4
Operating Margin	8.1%	16.9%	22.8%	16.5%	6.9%	19.8%	30.6%	15.8%	8.7%	19.5%	29.9%	15.3%	9.4%	20.0%	30.8%	17.3%
Other Income & Expenses (net)	1.3	1.5	1.3	0.4	(0.1)	0.6	(0.7)	(0.6)	0.2	1.4	0.7	0.7	0.7	0.7	0.7	0.7
Gain (loss) on sale of non-util property	0.0	(0.1)	0.0	2.6	0.0	0.0	0.0	0.0	0.6	0.1	0.0	0.0	0.0	0.0	0.0	0.0
EBIT	7.1	17.6	27.2	17.1	4.9	21.5	39.6	15.2	8.4	24.2	41.6	17.1	9.4	24.9	44.6	20.1
EBIT (%)	9.9%	18.3%	23.9%	20.0%	6.7%	20.4%	30.0%	15.2%	9.6%	20.7%	30.4%	15.9%	10.1%	20.5%	31.2%	17.9%
Interest Expense	4.4	4.5	4.5	3.7	4.6	4.7	4.2	3.7	4.4	5.3	5.3	5.0	5.5	5.3	5.3	4.9
Income Before Taxes	2.6	13.1	22.8	13.4	0.3	16.8	35.4	11.4	4.0	18.9	36.3	12.1	3.9	19.6	39.3	15.2
Provision for Income Taxes	1.1	5.4	8.9	5.4	0.1	6.7	13.2	4.1	1.6	6.8	14.0	4.7	1.5	7.5	15.1	5.9
Implied Tax Rate	40.3%	40.9%	39.3%	40.0%	40.3%	39.7%	37.3%	36.0%	39.3%	36.0%	38.7%	38.7%	38.5%	38.5%	38.5%	38.5%
Net Income	1.6	7.7	13.8	8.0	0.2	10.1	22.2	7.3	2.4	12.1	22.2	7.4	2.4	12.1	24.1	9.4
Preferred Dividends	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Net Income	1.6	7.7	13.8	8.0	0.2	10.1	22.2	7.3	2.4	12.1	22.2	7.4	2.4	12.1	24.1	9.4
EPS (fully diluted)	0.07	0.37	0.67	0.39	0.01	0.48	1.06	0.35	0.12	0.58	1.07	0.36	0.11	0.56	1.10	0.42
Weighted Avg. Shares	20.7	20.7	20.7	20.7	20.7	20.7	20.7	20.7	20.8	20.8	20.8	20.8	21.2	21.6	22.0	22.4
Financial Summary (values in %)																
Revenue Growth	9.7%	18.1%	5.7%	6.5%	1.9%	10.2%	15.7%	16.6%	18.8%	10.5%	3.8%	7.4%	7.7%	4.2%	4.4%	4.5%
Operations & Maintenance/Revenue	75.4%	70.8%	66.6%	70.1%	75.4%	68.1%	59.4%	71.0%	74.8%	68.3%	59.6%	71.4%	74.6%	68.0%	58.8%	69.6%
Gen. taxes/Revenue	4.8%	3.6%	3.3%	3.6%	5.1%	3.3%	3.0%	3.7%	4.7%	3.4%	2.9%	3.6%	4.7%	3.3%	2.9%	3.5%
EBIT (% of rev.)	9.9%	18.3%	23.9%	20.0%	6.7%	20.4%	30.0%	15.2%	9.6%	20.7%	30.4%	15.9%	10.1%	20.5%	31.2%	17.9%
EBIT/Interest expense	1.6	3.9	6.1	4.6	1.1	4.6	9.5	4.1	1.9	4.5	7.8	3.4	1.7	4.7	8.4	4.1
EPS growth	75.0%	20.5%	-2.6%	23.6%	-87.2%	28.5%	58.8%	-9.2%	1205.6%	21.3%	0.9%	1.2%	-2.9%	-4.1%	2.6%	17.0%

Source: Company reports, Longbow estimates

California Water Service Group — Annual Earnings Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY Ends December 31	FY04	FY05	FY06	FY07	FY08	FY09E	FY10E	FY11E
Total Revenue	**315.6**	**320.7**	**334.7**	**367.1**	**410.3**	**447.4**	**469.7**	**526.5**
Watet Production Costs	119.1	115.7	124.3	138.9	146.6	159.8	166.3	186.4
Administrative & General	47.1	48.8	52.8	54.3	59.4	65.3	68.1	76.3
Other Operations	39.9	40.0	42.9	46.3	51.2	57.0	59.7	66.3
Maintainence	13.2	15.2	15.6	18.3	19.0	20.6	20.3	21.6
Operations & Maintenance	219.4	219.7	235.6	257.8	276.2	302.8	314.3	350.6
Depreciation and Amortization	26.1	28.7	30.7	33.6	37.3	41.2	42.5	45.0
General Taxes	11.5	12.6	12.9	13.7	14.8	15.9	16.6	18.6
Total Expenses	**257.0**	**261.0**	**279.1**	**305.0**	**328.3**	**359.8**	**373.4**	**414.2**
Income from Operations	**58.6**	**59.7**	**55.6**	**62.1**	**82.0**	**87.6**	**96.3**	**112.3**
Operating Margin	**18.6%**	**18.6%**	**16.6%**	**16.9%**	**20.0%**	**19.6%**	**20.5%**	**21.3%**
Other Income & Expenses (net)	2.4	3.0	3.4	4.4	(0.9)	2.9	2.6	2.6
Gain (loss) on sale of non-util property	0.0	2.3	0.3	2.5	0.0	0.7	0.0	0.0
EBIT	**61.0**	**64.9**	**59.4**	**69.0**	**81.1**	**91.2**	**98.9**	**114.9**
EBIT (%)	**19.3%**	**20.2%**	**17.7%**	**18.8%**	**19.8%**	**20.4%**	**21.1%**	**21.8%**
Interest Expense	17.8	17.7	17.0	17.1	17.2	20.0	21.0	23.5
Income Before Taxes	43.1	47.2	42.4	51.9	63.9	71.3	78.0	91.4
Provision for Income Taxes	**17.1**	**20.0**	**16.8**	**20.7**	**24.1**	**27.1**	**30.0**	**35.2**
Implied Tax Rate	**39.6%**	**42.4%**	**39.7%**	**39.9%**	**37.7%**	**38.0%**	**38.5%**	**38.5%**
Net Income	26.0	27.2	25.6	31.2	39.8	44.2	48.0	56.2
Preferred Dividends	-	-	-	-	-	-	-	-
Net Income	**26.0**	**27.2**	**25.6**	**31.2**	**39.8**	**44.2**	**48.0**	**56.2**
EPS (fully diluted)	**1.46**	**1.47**	**1.34**	**1.50**	**1.90**	**2.12**	**2.20**	**2.48**
Weighted Avg. Shares	17.7	18.4	18.9	20.7	20.7	20.8	21.8	22.7
Financial Summary (values in %)								
Revenue Growth	13.9%	1.6%	4.4%	9.7%	11.8%	9.0%	5.0%	12.1%
Operations & Maintenance/Revenue	69.5%	68.5%	70.4%	70.2%	67.3%	67.7%	66.9%	66.6%
(Dep + Amort)/Net Fixed Assets	3.4%	3.6%	3.6%	3.6%	3.7%	3.7%	3.6%	3.6%
Gen. taxes/Revenue	3.6%	3.9%	3.9%	3.7%	3.6%	3.5%	3.5%	3.5%
EBIT (% of rev.)	19.3%	20.2%	17.7%	18.8%	19.8%	20.4%	21.1%	21.8%
Interest Expense/Net Debt	6.7%	6.4%	6.0%	5.9%	5.5%	5.6%	5.9%	6.0%
EBIT/Interest expense	3.4	3.7	3.5	4.0	4.7	4.6	4.7	4.9
Net Income Growth	34.0%	4.6%	-6.0%	21.8%	27.7%	11.0%	8.6%	17.2%
EPS growth	20.4%	0.7%	-8.8%	11.9%	26.7%	11.8%	3.5%	12.8%
Average ROE	9.7%	9.3%	7.5%	8.1%	10.1%	10.7%	10.8%	11.5%

Source: Company reports, Longbow estimates

LONGBOW Research

September 9, 2009

Aqua America - Annual Income Statement
Garik Shmois/ Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09E	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E
Total Operating Revenue	137.3	150.6	165.5	149.1	139.3	150.8	177.1	159.8	154.5	167.3	200.5	168.7	164.2	185.2	212.6	180.8
Operation & Maintenance	60.3	63.3	67.1	62.4	64.3	65.1	66.7	65.9	67.0	68.5	76.8	66.0	67.5	72.6	83.3	74.3
Depreciation	20.1	20.5	21.1	21.5	21.5	20.6	22.8	23.9	26.4	25.0	25.4	25.4	25.6	26.2	26.7	27.4
Amortization	1.2	1.2	1.2	1.2	1.2	1.0	1.8	1.5	2.8	3.1	3.0	3.0	3.0	3.0	3.0	3.0
General Taxes	11.9	10.8	10.8	11.8	12.1	10.8	11.2	10.6	11.6	11.9	12.4	11.8	12.3	13.0	12.8	12.7
Recovery of restructuring costs																
Total Expenses	93.6	95.9	100.1	96.9	99.1	97.6	102.5	102.0	107.7	108.5	117.6	106.2	108.4	114.8	125.8	117.4
Income from Operations	43.7	54.8	65.3	52.2	40.2	53.1	74.6	57.9	46.8	58.9	82.9	62.5	55.8	70.4	86.8	63.4
Operating Margin (%)	31.9%	36.4%	39.5%	35.0%	28.9%	35.2%	42.1%	36.2%	30.3%	35.2%	41.3%	37.1%	34.0%	38.0%	40.8%	35.1%
All. for Borrowed Funds Used in Const.	0.7	0.7	0.7	0.8	1.0	1.1	1.0	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.6
Gain (loss) on sale of other assets	0.1	0.3	0.3	2.8		0.6	0.5	0.5	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Other																
EBIT	44.5	55.8	66.3	55.8	41.2	54.8	76.1	59.0	47.5	59.5	83.6	63.2	56.5	71.1	87.5	64.1
EBIT (%)	32.4%	37.1%	40.0%	37.5%	29.6%	36.3%	43.0%	36.9%	30.8%	35.6%	41.7%	37.5%	34.4%	38.4%	41.2%	35.5%
Interest Expense	16.5	16.4	17.1	16.8	17.1	17.1	17.0	17.4	16.6	16.8	17.0	17.2	17.6	18.0	18.4	18.6
Income Before Taxes	28.0	39.4	49.2	39.0	24.0	37.7	59.1	41.7	30.9	42.7	66.6	46.0	38.9	53.1	69.1	45.5
Provision for Income Taxes	11.1	15.7	19.6	14.1	9.7	15.2	23.7	16.0	12.5	16.9	27.0	18.2	15.6	21.2	27.6	17.7
Implied Tax Rate	39.8%	39.8%	40.0%	36.1%	40.4%	40.2%	40.1%	38.4%	40.5%	39.5%	40.5%	39.5%	40.0%	40.0%	40.0%	39.0%
Net Income before extraord. Item	16.9	23.7	29.5	24.9	14.3	22.6	35.4	25.7	18.4	25.9	39.6	27.9	23.4	31.9	41.5	27.8
Reclassification adj. for gains reported in net income				(1.3)			(0.2)			0.0						
Unrealized gain on securities																
Unrealized holding gain on investments	0.0	0.2	0.9	-	-	0.2	0.0		0.0	0.2						
Minimum pension liability adjustment		-	-													
Comprehensive Income	16.9	23.9	30.4	23.6	14.3	22.7	35.2	25.7	18.4	26.1	39.6	27.9	23.4	31.9	41.5	27.8
Diluted Net Income Per Share	0.13	0.18	0.22	0.19	0.11	0.17	0.26	0.19	0.14	0.19	0.29	0.20	0.17	0.23	0.30	0.20
Weighted Avg. Shares	133.2	133.5	133.8	134.0	134.0	134.1	135.3	135.6	135.9	135.9	136.2	136.4	136.8	137.3	137.7	138.2
Financial Summary (values in %)																
Revenue Growth	16.4%	14.3%	12.6%	8.9%	1.4%	0.1%	7.0%	7.2%	10.9%	11.0%	13.2%	5.6%	6.3%	10.7%	6.0%	7.2%
Operations & Maintenance/Revenue	43.9%	42.0%	40.5%	41.9%	46.2%	43.2%	37.7%	41.2%	43.4%	41.0%	38.3%	39.1%	41.1%	39.2%	39.2%	41.1%
EBIT (% of rev.)	32.4%	37.1%	40.0%	37.5%	29.6%	36.3%	43.0%	36.9%	30.8%	35.6%	41.7%	37.5%	34.4%	38.4%	41.2%	35.5%
General taxes as % of revenue	8.7%	7.2%	6.6%	7.9%	8.7%	7.2%	6.3%	6.7%	7.5%	7.0%	6.2%	7.0%	7.5%	7.0%	6.0%	7.0%
EBITDA	65.9	77.5	88.5	78.6	63.8	76.4	100.7	84.4	76.7	87.5	112.0	91.6	85.1	100.3	117.2	94.5
Net Income Growth	1.8%	6.0%	8.0%	-3.2%	-15.0%	-5.0%	19.9%	3.0%	28.3%	14.6%	12.0%	8.5%	27.1%	23.3%	4.6%	-0.4%
EPS Growth	0.0%	4.0%	7.1%	-3.6%	-15.5%	-5.3%	18.6%	1.8%	26.5%	13.0%	11.2%	7.9%	26.3%	22.1%	3.5%	-1.7%

Source: Company reports and Longbow estimates

Aqua America - Annual Income Statement
Garik Shmois/ Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	2004A	FY05A	FY06A	FY07A	FY08A	FY09E	FY10E	FY11E
Total Operating Revenue	442.0	496.8	533.5	602.5	627.0	691.0	742.8	816.0
Operation & Maintenance	178.3	203.1	219.6	253.1	262.1	278.3	297.7	325.9
Depreciation	54.6	60.7	70.9	83.2	88.8	102.2	105.9	112.8
Amortization	4.3	4.7	4.1	4.8	5.5	11.8	12.0	12.0
General Taxes	27.6	31.7	33.3	45.4	44.7	47.7	50.7	55.7
Total Expenses	264.8	300.3	327.9	386.5	401.2	440.0	466.4	506.4
Income from Operations	177.2	196.5	205.6	216.0	225.8	251.0	276.4	309.6
Operating Margin (%)	40.1%	39.6%	38.5%	35.9%	36.0%	36.3%	37.2%	37.9%
Allow. for Borrowed Funds Used in Const.	2.3	2.4	3.9	3.0	3.7	2.4	2.4	2.4
Gain (loss) on sale of other assets	1.3	1.2	1.2	3.5	1.6	0.4	0.4	0.4
Other	-	-	-	-				
EBIT	180.8	200.1	210.7	222.5	231.1	253.9	279.2	312.4
EBIT (%)	40.9%	40.3%	39.5%	36.9%	36.9%	36.7%	37.6%	38.3%
Interest Expense	48.7	52.1	58.4	66.9	68.6	67.6	72.6	81.6
Income Before Taxes	132.1	148.1	152.3	155.5	162.5	186.2	206.6	230.8
Provision for Income Taxes	52.1	56.9	60.2	60.5	64.6	74.5	82.2	91.8
Implied Tax Rate	39.4%	38.4%	39.6%	38.9%	39.7%	40.0%	39.8%	39.8%
Net income	80.0	91.2	92.0	95.0	97.9	111.7	124.4	139.0
Reclassification adj. for gains reported in net income	(0.2)	-	-	(1.3)	(0.2)			
Unrealized gain on securities	0.1	-	-	-				
Unrealized holding gain on investments	-	-	0.2	1.1	0.2	0.3	-	-
Minimum pension liability adjustment	(1.7)	(1.3)	3.1		-	-	-	-
Comprehensive Income	78.1	89.8	95.3	94.8	97.9	112.0	124.4	139.0
Diluted Net Income Per Share	0.64	0.71	0.70	0.71	0.73	0.82	0.91	1.00
Weighted Avg. Shares	125.7	129.2	131.8	133.6	134.7	136.1	137.5	138.8
Financial Summary (values in %)								
Revenue Growth	20.4%	12.4%	7.4%	12.9%	4.1%	10.2%	7.5%	9.9%
Operations & Maintenance/Revenue	40.3%	40.9%	41.2%	42.0%	41.8%	40.3%	40.1%	39.9%
Dep/Net Fixed Asset	3.0%	2.9%	3.1%	3.3%	3.2%	3.4%	3.3%	3.3%
Depreciation Growth	12.5%	11.3%	16.7%	17.3%	6.7%	15.1%	3.7%	6.5%
General taxes as % of revenue	6.2%	6.4%	6.2%	7.5%	7.1%	6.9%	6.8%	6.8%
Interest Exp/ Average Net Debt	5.6%	5.3%	5.8%	5.9%	5.2%	4.8%	5.2%	5.4%
Interest Expense/Revenue	11.0%	10.5%	11.0%	11.1%	10.9%	9.8%	9.8%	10.0%
EBITDA	239.7	265.6	285.7	310.5	325.4	367.8	397.2	437.2
Net income growth	13.0%	13.9%	0.9%	3.3%	3.1%	14.1%	11.4%	11.7%
Average ROE	11.4%	11.7%	10.6%	10.0%	9.6%	10.1%	10.2%	10.4%
EPS Growth (ex special items and FAS 123)	7.0%	10.9%	-1.0%	1.9%	2.2%	12.9%	10.3%	10.6%

Source: Company reports and Longbow estimates

WATER INDUSTRY PEER VALUATION

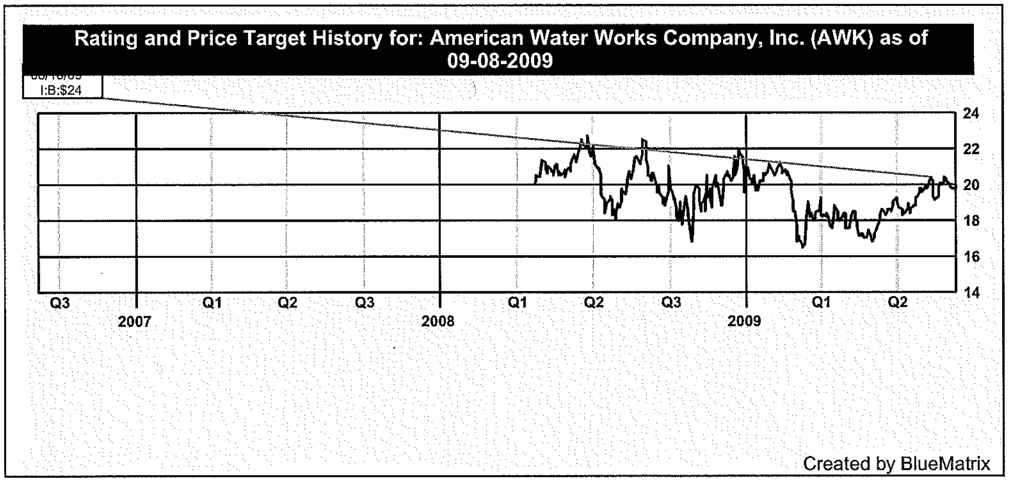
($ in millions, except per share data)

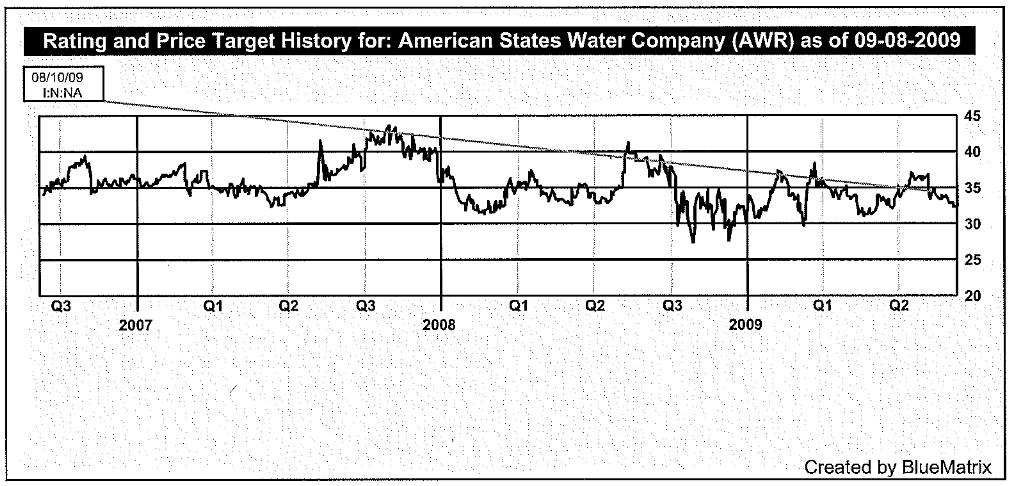
							52 Week				Earnings per Share			P/E		Dividend	Price/
Company	Ticker	FY End	Rating	Target	% Upside	Share Price	Hi	Lo	Mkt Cap	Revenue FY End	Last FY	Current FY	Next FY	Current FY	Next FY	Rate	Book
U.S. WATER UTILITIES																	
American Water Works	AWK	Dec.	BUY	$24	20%	$ 19.99	$22.35	$16.22	$ 3,458	$ 2,337	1.17	1.31	1.50	15.3x	13.4x	4.2%	0.8x
Aqua America	WTR	Dec.	Neutral			$ 16.85	$22.00	$12.20	$ 2,273	$ 627	0.73	0.82	0.91	20.5x	18.6x	3.5%	2.6x
American States Water	AWR	Dec.	Neutral			$ 35.23	$41.20	$27.00	$ 595	$ 319	1.06	1.74	1.91	20.3x	18.4x	3.1%	1.8x
California Water Service Group	CWT	Dec.	BUY	$45	22%	$ 36.75	$48.28	$27.68	$ 752	$ 410	1.90	2.12	2.20	17.3x	16.7x	3.3%	2.4x
Southwest Water Company	SWWC	Dec.	NR			$ 4.99	$13.40	$2.67	$ 120	$ 222	-0.19	*0.21*	*0.44*	23.8x	11.3x	2.1%	0.7x
Artesian Resources Corporation	ARTNA	Dec	NR			$ 17.60	$18.14	$12.81	$ 126	$ 56	0.86	*1.07*	*1.11*	16.4x	15.9x	4.1%	1.3x
Consolidated Water Co	CWCO	Dec	NR			$ 18.41	$23.91	$6.35	$ 268	$ 60	0.50	*0.78*	*0.86*	23.6x	21.4x	1.6%	1.5x
Connecticut Water Service	CTWS	Dec	NR			$ 21.74	$28.95	$17.31	$ 185	$ 61	1.12	*1.08*	*1.06*	20.1x	20.5x	4.2%	1.9x
Middlesex Water Company	MSEX	Dec	NR			$ 15.31	$17.93	$11.64	$ 204	$ 91	0.90	*0.69*	*0.79*	22.2x	19.4x	4.7%	1.7x
Pennichuck Corporation	PNNW	Dec	NR			$ 23.42	$24.80	$14.75	$ 101	$ 31	0.57	*0.59*	*0.76*	39.7x	30.8x	3.0%	1.8x
York Water Company	YORW	Dec	NR			$ 16.03	$17.95	$6.22	$ 179	$ 33	0.57	*0.67*	*0.7*	23.9x	22.9x	3.2%	2.0x
U.S. Water Utility Average														22.1x	19.0x	3.4%	1.7x
EQUIPMENT/FILTRATION/TREATMENT SECTOR																	
Calgon Carbon Corp.	CCC	Dec.	NR			$ 15.12	$21.99	$9.11	$ 772	$ 400	0.56	*0.5*	*0.76*	28.1x	18.5x	0.0%	3.3x
Danaher	DHR	Dec.	NR			$ 65.87	$80.01	$47.20	$ 20,961	$ 12,697	4.23	*3.37*	*3.64*	19.5x	18.1x	0.2%	1.8x
ITT Technologies	ITT	Dec.	NR			$ 51.17	$62.84	$31.94	$ 9,302	$ 11,695	4.04	*3.65*	*3.81*	14.0x	13.4x	1.7%	2.7x
Layne Christensen	LAYN	Jan.	NR			$ 28.55	$48.50	$10.36	$ 555	$ 1,008	2.20	*0.59*	*0.94*	48.7x	30.5x	0.0%	0.7x
Mueller Water Products	MWA	Sept	NR			$ 4.52	$12.71	$1.48	$ 526	$ 1,859	0.46	*(0.39)*	-	-	214.8x	1.6%	0.8x
Nalco	NLC	Dec.	NR			$ 17.49	$25.90	$7.80	$ 2,365	$ 4,212	1.30	*0.8*	*1.17*	21.5x	14.7x	0.8%	4.0x
Pall Corp.	PLL	Jul.	NR			$ 30.71	$39.70	$18.20	$ 3,566	$ 2,572	1.94	*1.73*	*1.99*	17.7x	16.2x	1.9%	4.3x
Pentair	PNR	Dec.	NR			$ 29.05	$41.00	$17.23	$ 2,877	$ 3,382	2.17	*1.42*	*1.7*	20.6x	17.2x	2.4%	1.2x
Watts Water Technologies	WTS	Dec.	NR			$ 29.66	$33.00	$15.85	$ 1,068	$ 1,459	1.83	*1.31*	*1.45*	22.2x	20.1x	1.5%	1.1x
Equipment/Filtration/Treatment Average (*ex BWTR and CCC)														24.0x	40.4x	1.1%	2.2x
WATER RESOURCES/ INFRASTRUCTURE																	
Insituform Technologies	INSU		NR			$ 18.42	$21.28	$9.26	$ 699	$ 537	0.77	*0.98*	*1.12*	18.3x	16.0x	0.0%	1.5x
Lindsay Manufacturing	LNN		NR			$ 41.62	$97.80	$20.89	$ 503	$ 475	3.11	*1.07*	-	32.1x	28.3x	0.8%	5.1x
Tetra Tech	TTEK		NR			$ 29.24	$32.00	$14.20	$ 1,756	$ 2,145	1.02	*1.24*	*1.42*	21.0x	21.3x	0.0%	2.8x
Water Resources/ Infrastructure Average														23.8x	21.9x	0.3%	3.1x
Relevant Indices						**Share Price**											
Dow Jones Industrials	DJ30					$ 9,497.34											
S&P 500	SPX					$ 1,025.39											
Nasdaq Composite	NDX					$ 2,037.77											

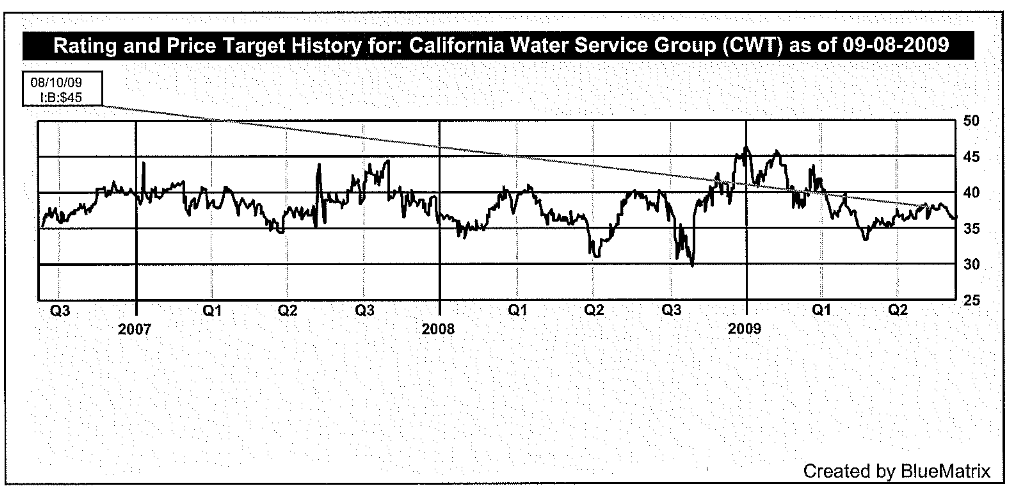
Source: Baseline; Company reports and LBR Estimates. EPS reflects diluted EPS, excluding extraordinary items. Numbers in italics reflect consensus estimates.
** Time period for annual estimates may vary based on reporting date.

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

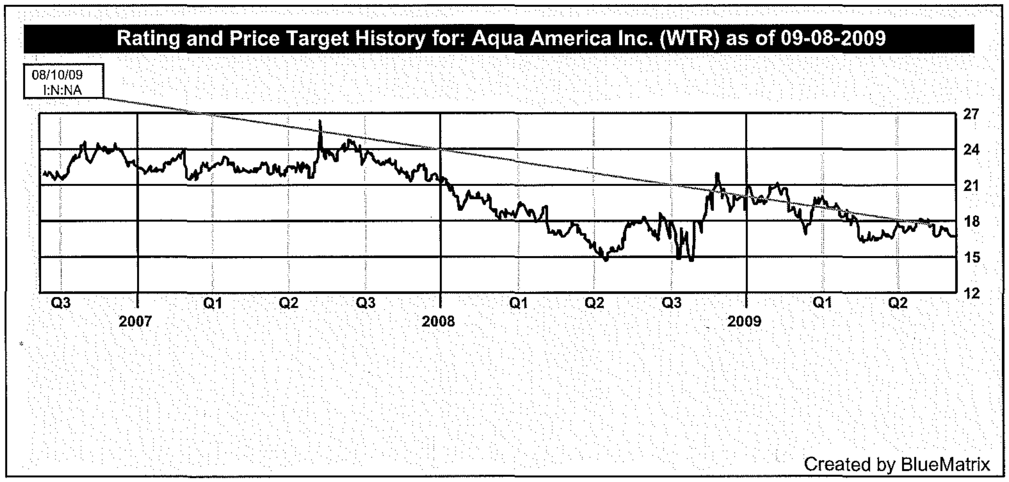






G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469



APPENDIX

IMPORTANT DISCLOSURES

REGULATION ANALYST CERTIFICATION ("REG AC"): The Research Analyst(s) who prepared this research report hereby certifies that the views expressed in the research report accurately reflect the analyst(s) personal views about the subject companies and their securities. The Research Analyst(s) also certifies that the Analyst(s) have not been, are not, and will not be receiving direct or indirect compensation for expressing the specific recommendation(s) or view(s) in this report.

GENERAL DISCLOSURES: Longbow Securities does not make a market in any securities, nor does it hold a principal position in any security. However, any officer, director or stockholder of Longbow Securities or any member of their families may have a position in and may from time to time purchase or sell any of the securities mentioned or any related securities. Security prices in this report may either reflect the previous day's closing price or an intraday price, depending on the time of distribution. Consensus estimates are derived from either Thomson/Reuters, Bloomberg or Baseline. Designated trademarks and brands are the property of their respective owners.

SPECIFIC DISCLOSURES:

- Longbow Securities does not make a market in the securities of any company mentioned in this Report, and is not a market-maker in any securities generally. Nor does the firm does hold a principal position in any security.
- As of the date of this Report, no officer, director or stockholder of Longbow Securities, or any member of their immediate families, holds securities of any company mentioned in the Report. In the event such persons purchase, hold or sell securities of a company mentioned in the Report for their own account, any subsequent Report shall disclose the fact of any such ownership or transactions.
- No employee of Longbow Securities serves on the Board of Directors of the subject security or any other security mentioned in this report.
- Neither the Research Analyst nor a member of the Research Analyst's household has a financial interest in the securities of the subject company or any other security mentioned in

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

this report.

- Neither the Research Analyst nor a member of the Research Analyst's household serves on the Board of Directors of the subject company or any other security mentioned in this report.
- Neither Longbow Securities nor its affiliates beneficially own 1% or more of an equity security of the subject company or any other security mentioned in this report.

RATINGS DISTRIBUTIONS FOR LONGBOW RESEARCH:

Rating Category	Count	Percent
Buy	51	25.1%
Neutral	145	71.4%
Sell	7	3.4%

RATING SYSTEM:

"Buy" means that Longbow Securities expects total return to exceed 20% over a 12-month period.

"Neutral" means that Longbow Securities expects total return to be within a range of plus or minus 20% over a 12-month period.

"Sell" means that Longbow Securities expects total return to be negative by greater than 20% over a 12-month period.

Longbow Research's full research universe and related applicable disclosures can be obtained by calling (216) 986-0700 or via postal mail at: Editorial Department, Longbow Research, 6000 Lombardo Center, Suite #500, Independence, Ohio 44131.

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

LONGBOW Research
Tactical advantage through independent research

Estimate Changes

November 10, 2009 **AMERICAN WATER WORKS COMPANY, INC. (AWK)**

Rating: BUY
Current Price: $20.50
Target Price: $24.00

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

Industry: Water Utilities / Fiscal Year: Dec			1Q09A	2Q09A	3Q09A	4Q09E	FY09E	Valuation Multiple	FY10E	Valuation Multiple
Market Cap ($MM):	3,581	**EPS:**	$0.19	$0.32	$0.52	$0.25	$1.28	16.0x	$1.52	13.5x
		Prior:	-	-	$0.54	-	$1.29		$1.50	
Net Debt ($MM):	5,345	Consensus:				$0.27	$1.08	19.0x	$1.44	14.2x
Enterprise Value ($MM):	8,926	Last Year:	$0.11	$0.28	$0.55	$0.23	$1.17			
Shares - FD (MM):	174.7									
		EBITDA:	$1.15	$1.40	$1.66	$1.67	$5.38	9.5x	$5.87	8.7x
Dividend:	$0.84	Growth:	28%	10%	3%	5%	9%		17%	
Yield:	4.1%									
Beta:	0.46	**Revenue:**	$550	$613	$680	$591	$2,434	3.7x	$2,676	3.3x
Rel. P/E (FY2009E):	82%	Growth:	9%	4%	1%	4%	140%		10%	

AWK: Weather Drives Lower Consumption and 3Q Miss But Outlook Remains Positive

SUMMARY

- AWK reported 3Q09 EPS of $0.52 vs. our and the consensus estimate of $0.54. Unfavorable weather in the quarter and declining consumption from both conservation efforts and the weaker economy reduced the volume of water sold by 7.4%, revenues by $44.2M and EPS by $0.14 y/y. Excluding both the weather and consumption declines, Regulated revenues would have increased 9.9% y/y.

- Despite a 30% ($6.4M) increase in pension and post-retirement expenses and a 25% ($3.7M) increase in chemical expenses, the O&M ratio declined 80bp y/y. That being said, most of the improvement came from the Non-Regulated side, where, despite an 11.7% revenue decline, gross margins increased from 9.2% to 26.4%.

- YTD in 2009, the company has received $72.4M of rate increases and currently has $306.7M of rate cases pending for approval in various states. We expect rate increases and surcharges to increase revenues by 9.8% and 7.1% in FY09E and FY10E, respectively.

- We are maintaining our 4Q09E EPS of $0.25 as lower water consumption in October driven by the weather should be offset by an improved margin profile. Our FY10E EPS is now $1.52 (vs. $1.50 previously) on account of the timing of rate cases that were approved recently.

- We are maintaining our BUY rating and $24 target price on AWK shares, based on 15.8x our FY10E EPS.

Longbow Research
6000 Lombardo Center, Suite 500, Independence, Ohio USA 44131
T: 216-986-0700 • F: 216-986-0720 • www.longbowresearch.com

DISCUSSION OF DETAILS

AWK reported 3Q09 EPS of $0.52 vs. our and the consensus estimate of $0.54. EPS decreased 4.8% y/y but net income was up 4.0%. Operating revenues grew 1.2% y/y from rate increases. Unfavorable weather in the quarter and declining consumption from both conservation efforts and the weaker economy reduced the volume of water sold by 7.4%, revenues by $44.2M and EPS by $0.14 y/y. Revenues for the Regulated segment increased 2.9% y/y, with rate increases and surcharges increasing revenue by $58.2M, or 9.6%. The completion of the design and build phase of the large DBO contract contributed to the 11.7% decline on Non-Regulated segment revenue. While we were disappointed with the earnings miss, both the weather and the economic impact of lower water consumption played a bigger role than we had anticipated. That being said, AWK was able to keep O&M margins down 80bp y/y despite a marked increase in chemical and pension costs. Going forward, we expect revenue increases longer-term to offer margin expansion opportunities.

AWK Summary 3Q09

FY Ends December 31	3Q08A	3Q09A	y/y act.	LBR 3Q09	y/y est.	Actual/LBR
Total Revenue	**672.2**	**680.0**	**1.2%**	**703.1**	**4.6%**	**-3.3%**
Operations & Maintenance	342.2	340.9	-0.4%	357.3	4.4%	-4.6%
Depreciation and Amortization	68.4	74.9	9.4%	73.2	7.0%	2.3%
General Taxes	49.4	50.6	2.5%	49.3	-0.1%	2.6%
Loss (gain) on sale of assets	0.5	-0.8		-0.3		
Total Expenses	**460.5**	**465.6**	**1.1%**	**479.5**	**4.1%**	**-2.9%**
Income from Operations	**211.7**	**214.4**	**1.3%**	**223.6**	**5.6%**	**-4.1%**
Other income, net	(6.7)	(1.5)	-77.3%	(5.5)	-17.4%	-72.5%
EBIT	**218.4**	**215.9**	**-1.1%**	**229.2**	**4.9%**	**-5.8%**
Interest Expense	72.7	74.1	2.0%	74.4	2.3%	-0.4%
Income Before Taxes	145.7	141.8	-2.7%	154.8	6.2%	-8.4%
Provision for Income Taxes	57.5	50.2	-12.8%	61.3	6.6%	-18.2%
Net Income	**88.1**	**91.6**	**4.0%**	**93.4**	**6.0%**	**-1.9%**
EPS (fully diluted)	**0.55**	**0.52**	**-4.8%**	**0.54**	**-2.8%**	**-2.1%**

Source: Company Reports, LBR Estimates

- YTD in 2009, the company has received $72.4M of rate increases and currently has $306.7M of rate cases pending for approval in various states. We expect rate increases and surcharges to increase revenues by 9.8% and 7.1% in FY09E and FY10E, respectively.
- AWK is on-track to reach its $800M FY09 capex target with $592.9M spent in 1-3Q09. The capex program was scaled back in 2009 due to adverse capital market conditions and management indicated at least a similar level of spending in FY10.
- Cash provided by operating activities increased by $78.6M, or 20% y/y, during 1-3Q09. The company is using its increased cash generation, along with new debt ($403.6M YTD) and equity issuance ($242.3M YTD) to finance its capex program.
- There was no new update on the timing of RWE's exit on the conference call, but three secondary offerings over the last year have brought RWE's ownership down to 23.5%. Given the pace of RWE's ownership reduction over the past 12 months, we expect a complete exit by sometime in 2010, which could reduce what we view as an artificial cap on AWK's stock price and act as a possible upside catalyst.

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

OUTLOOK

Rate Increases, As Expected. Lower Consumption Drag Should Reverse In 2010.
Although Regulated segment revenues increased only 2.9% y/y during the quarter because of lower water sales, we are pleased with the impact of the rate increases and surcharges on revenue. Excluding the ($44.2M) impact of lower water sales, revenue would have increased by 9.9% y/y. Approximately half of the lower water sales were from residential customers, which we believe was mostly due to wet and colder weather. Assuming normal weather conditions in 2010, we expect this portion of the water sales loss to reverse next year. On the other hand, the remaining half of the lower water sales from commercial and industrial customers was mostly a result of the economy, which might not reverse as quickly.

Based on the approved and pending rate cases, we expect $50.0M, or a 10% y/y revenue increase in 4Q09E from rate increases. However, given the unfavorable weather in October, we expect a net revenue increase of just 3.9% during the quarter. For FY10E, we expect $156.6M, or a 7.1% y/y revenue increase from rate increases. However, we also expect a $47.6M benefit from an assumed increase in water consumption, which should increase revenues by a net 10.0% y/y.

AWK Continues to Perform On the Cost Side
We were pleased with AWK's performance on the cost side. Despite 7.4% ($44.2M) lower water sales, a 30% ($6.4M) increase in pension and post-retirement expenses and a 25% ($3.7M) increase in chemical expenses, the O&M ratio declined 80bp y/y. However, most of the improvement came from the Non-Regulated side, where, despite an 11.6% revenue decline, gross margins increased from 9.2% to 26.4%. The $8M decline in operating expenses corresponds to the $8.6M decline in revenues. A majority of the decrease was due to the completion of the design and build phase of a large DBO contract in California. Although we do not expect the 26.4% gross margin to continue, we believe we could possibly see increased profitability in the Non-Regulated segment going forward.

Regulated segment gross margin decreased 100bp to 32.8% in this tough quarter, which we believe is an overall positive and continues the trend of an improving O&M ratio. We expect a further 190bp improvement in the O&M ratio in FY10E. Pension and post-retirement expenses continue to remain a drag on the ratio, with AWK still waiting for a final decision to recover or defer as a regulatory asset $7.5M of increased expenses until the next rate case. The y/y increase is mainly from the 2008 stock market decline and should not continue next year in 2010E.

Acquisition/ New O&M Contracts
AWK completed five "tuck in" acquisitions in October 2009 in PA and IN that serve a total of 4,700 people. The company is awaiting a decision from the New Jersey Supreme Court on the Trenton, NJ acquisition and might be closer to completing the purchase after two and half years of delays. However, the company is still lagging its peer, Aqua America (WTR - NEUTRAL), in making "tuck in" acquisitions. WTR has completed 15 acquisitions YTD. After a slew of unprofitable O&M contracts earlier this decade, AWK also seems much more guarded in aggressively pursuing new contracts, in our view. However, we believe the improving performance in the existing Regulated business should make up for the slow pace of new acquisitions. At the same time, AWK is winning additional military base contracts, which, although we believe are not very profitable, should contribute to top line growth and improve operating leverage. The company won two additional contracts in Ft. Belvoir, VA and Ft. Meade in MD during the quarter.

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

INVESTMENT THESIS

We continue to rate AWK shares BUY with a $24 target price as we see AWK as offering an attractive risk/reward with positive catalysts relative to the peer group. We believe AWK shares are discounting RWE's anticipated exit as the former parent company has announced plans to sell its remaining stake in AWK. While the timing of this cannot be predicted, we believe AWK's discounted valuation by investors is overdone. The shares are trading at 13.5x our FY10E EPS, relative to a peer group average of 18.8x. We also believe there is an opportunity for multiple expansion toward the peer group average once the RWE overhang abates. However, our target price still incorporates a 16% discount to the peer group average.

VALUATION

AWK shares closed yesterday at $20.50, which is 16.0x our FY09E EPS of $1.28 and 13.5x our FY10E EPS of $1.52. The shares are trading at a discount to the peer group average of 18.8x FY10E EPS we believe due in large part to the RWE overhang, which we estimate the Street is already accounting for. The shares are trading at 1.3x tangible book value ($15.69/share) compared to a peer group that trades over 1.7x, on average. Our target price of $24 is based on 15.8x our FY10E EPS, a valuation that remains at a discount to the peer group. However, we see multiple expansion from current levels as justified given AWK being viewed as the largest and most diversified publicly traded water utility in the U.S. and with earnings growth potential as the company catches up to insufficient rate increases during the past five-to-six years.

RISKS

Potential downside risks to our investment thesis, rating, target price and estimates include, but are not limited to: 1) delays in rate case processing or lower rate increases by the regulators than our expectations, 2) 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, 4) a large acquisition at an excessive valuation (significantly above the rate base), and 5) a large goodwill impairment which could lead to a potential breach of debt covenants or regulatory requirements.

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

LONGBOW Research

AWK November 10, 2009

INCREMENTAL REVENUE FROM RATE CASES & SURCHARGES (i) ALREADY APPROVED & (ii) CURRENTLY PENDING																		
State	Date Filed	Amount Filed	Actual Amount Granted	% Granted	Effective Dates	Days for Processing												
Approved Rate Cases (in $ million)							1Q09E	2Q09E	3Q09E	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E	1Q11E	2Q11E	3Q11E	4Q11E
CA (Sacram., etc)	1/1/07	16.4	13.0	79%	6/1/08	517		2.2										
AZ (Sun City Water)	4/30/07	2.2	1.9	86%	6/1/08	398		0.3										
AZ (Anthem)	6/16/06	7.0	4.3	61%	6/4/08	719		0.7										
VA	1/30/08	4.3	3.4	79%	7/8/08	160		0.9										
IL	8/31/07	32.8	21.6	66%	8/8/08	343		5.4	1.8									
TN	3/14/08	7.6	1.7	22%	10/1/08	201		0.4	0.4									
OH	10/1/07	5.5	5.3	96%	11/13/08	409		1.3	1.3	0.7								
PA (WW)	4/28/08	2.7	1.9	70%	11/14/08	200		0.5	0.5	0.2								
MO	3/31/08	49.8	34.5	69%	11/28/08	242		8.6	8.6	5.8								
NJ	1/14/08	125.0	72.1	58%	12/8/08	329		18.0	18.0	12.0								
WV	5/30/08	14.8	5.2	35%	3/26/09	300		1.3	1.3	1.3	1.3							
CA (ROE)	5/1/08	2.8	0.1	4%	5/6/09	370		0.0	0.0	0.0	0.0	0.0						
CA (Monterey Water)	1/31/08	37.1	12.1	33%	5/11/09	466		1.5	3.0	3.0	3.0	1.5						
CA (General Office)	1/31/08	6.4	2.2	34%	5/11/09	466		0.3	0.6	0.6	0.6	0.3						
NM	6/30/08	2.2	1.4	62%	5/12/09	316		0.2	0.3	0.3	0.3	0.2						
AWWM (NJ)	8/1/08	3	1.6	53%	5/21/09			0.1	0.2	0.2	0.2	0.2	0.1	0.1	0.1	0.1	0.0	0.0
KY	10/31/08	18.5	10.3	56%	6/1/09	213		0.9	2.6	2.6	2.6	1.7						
MI	6/22/09	0.2	0.2	100%	7/1/09				0.1	0.1	0.1	0.1						
CA (Monterey WW)	1/31/08	1.8	1.7	94%	7/9/09	525			0.4	0.4	0.4	0.4						
MD	5/2/09	0.8	0.8	100%	9/23/09	144				0.2	0.2	0.2	0.2					
IA	4/30/09	9.4	6.1	64%	10/9/09	162			1.7	1.5	1.5	1.5	0.0					
PA	4/30/09	58.1	30.8	53%	11/7/09	191				5.1	7.7	7.7	7.7	2.6				
VA (non-jurisdictional customers)			0.3					0.1										
TOTAL/AVERAGE				63%		337		**42.6**	**40.8**	**33.9**	**17.8**	**13.7**						
Approved Surcharge (in $ million)							1Q09E	2Q09E	3Q09E	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E	1Q11E	2Q11E	3Q11E	4Q11E
PA			5.7		9/1/08			1.4	1.4									
AZ			0.6		9/1/08			0.2	0.2									
PA			6		1/1/09			1.5	1.5	1.5								
NY			0.4		1/1/09			0.1	0.1	0.1								
AZ			0.2		1/1/09			0.1	0.1	0.1								
PA			2.4		4/1/09			0.6	0.6	0.6	0.6							
IN			3.8		4/1/09			1.0	1.0	1.0	1.0							
IL			0.7					0.2	0.2	0.2	0.2							
OH			0.6					0.2	0.2	0.2	0.2							
7/1/09 - 9/17/09			11.5						1.9	2.9	2.9	2.9	1.0					
TOTAL								**5.1**	**7.0**	**6.4**	**4.8**	**2.9**	**1.0**					
Approved Interim Rates (in $ million)							1Q09E	2Q09E	3Q09E	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E	1Q11E	2Q11E	3Q11E	4Q11E
TX	2/21/08	0.9	0.4	44%	6/1/08			0.1										
HI	11/1/07	1.3	0.7	54%	9/1/08			0.2	0.2									
TOTAL								**0.2**	**0.2**									
State	Date Filed	Amount Filed ($ million)	Expected Amount Granted ($ million)		Expected Effective Dates													
Pending Rate Cases & Expected Surcharges (in $ million)							1Q09E	2Q09E	3Q09E	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E	1Q11E	2Q11E	3Q11E	4Q11E
AZ (multiple)	5/1/08	20.0	13.2		11/1/09					2.2	3.3	3.3	3.3	1.1				
CA (Sac, LA, Lark)	1/23/09	26.1	17.2		6/1/10								4.3	4.3	4.3	4.3		
		6.6	4.4		1/1/11										1.1	1.1	1.1	1.1
IN	5/1/09	46.9	31.0		5/1/10							5.2	7.7	7.7	7.7	2.6		
OH	5/7/09	8.8	5.8		5/7/10							1.0	1.5	1.5	1.5	0.5		
IL	5/29/09	58.6	38.7		5/29/10							3.2	9.7	9.7	9.7	6.4		
AZ (multiple)	7/2/09	20.6	13.6		7/2/10								3.4	3.4	3.4	3.4		
NM	8/21/09	0.7	0.5		8/21/10								0.0	0.1	0.1	0.1	0.1	
MO	10/30/09	48.7	32.1		10/30/10									5.4	8.0	8.0	8.0	2.7
Surcharges									7.5	7.5	7.5	7.5	10.5	12.0	12.0	12.0	12.0	12.0
TOTAL								0.0	7.5	9.7	10.8	20.2	40.4	45.1	47.8	38.5	21.2	15.8
TOTAL INCREMENTAL REVENUE Quarterly							**47.1**	**47.9**	**55.5**	**50.0**	**33.4**	**36.7**	**41.4**	**45.1**	**47.8**	**38.5**	**21.2**	**15.8**
TOTAL INCREMENTAL REVENUE Annual							2009E **200.6**				2010E **156.6**				2011E **123.2**			

Source: Company reports; Longbow Research

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

American Water Works— Quarterly Income Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E
Regulated Segment	419.3	508.6	571.9	487.8	449.9	527.1	603.7	502.1	497.4	554.9	621.0	528.7	533.4	603.6	710.2	586.3
% increase			7.3%	11.2%	7.3%	3.6%	5.6%	2.9%	10.6%	5.3%	2.9%	5.3%	7.2%	8.8%	14.4%	10.9%
Non-Regulated Revenue	53.3	55.5	66.4	67.5	61.0	67.0	73.9	70.3	57.5	64.2	65.2	67.3	60.4	67.4	68.5	70.7
% increase			0.4%	27.7%	14.4%	20.8%	9.4%	4.1%	-5.7%	-4.2%	-11.7%	-4.3%	5.0%	5.0%	5.0%	5.0%
Other	(4.0)	(5.4)	(5.1)	(1.5)	(4.1)	(4.7)	(5.4)	(3.9)	(4.7)	(6.3)	(6.3)	(5.3)	(5.3)	(6.0)	(7.1)	(5.9)
% Regulated Rev	-1.0%	-1.1%	-0.9%	-0.3%	-0.9%	-0.9%	-0.9%	-0.8%	-1.0%	-1.1%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%
Operating revenues	**468.5**	**558.7**	**633.1**	**553.8**	**506.8**	**589.4**	**672.2**	**568.6**	**550.2**	**612.7**	**680.0**	**590.7**	**588.4**	**665.0**	**771.6**	**651.2**
Production costs	61.1	69.8	83.5	63.6	64.2	72.6	84.1	67.7	69.0	77.2	86.7					
Employee-related costs	109.8	119.2	112.8	121.5	126.8	131.4	127.4	119.9	132.6	133.2	139.6					
Operating supplies and services	63.8	63.9	83.9	81.8	69.5	66.7	72.2	74.8	56.8	58.6	60.2					
Maintenance materials and services	30.1	26.3	27.6	43.9	34.9	37.2	32.0	32.1	32.2	31.8	31.7					
Customer billing and accounting	8.3	9.1	8.6	12.2	7.4	11.9	13.4	11.2	10.8	13.2	12.7					
Other	9.5	11.0	11.8	13.1	8.3	10.7	13.1	14.0	12.9	16.7	9.9					
Operation and maintenance	282.6	299.4	328.3	336.2	311.3	330.6	342.2	319.8	314.4	330.6	340.9	330.8	327.4	348.8	375.2	354.9
Depreciation and amortization	64.6	68.1	69.7	64.9	63.9	67.3	68.4	71.6	68.8	73.2	74.9	73.2	75.3	77.3	79.4	81.5
General taxes	47.9	45.9	47.1	42.3	52.1	49.6	49.4	48.0	52.5	51.7	50.6	49.3	54.5	52.0	52.0	50.6
Loss (gain) on sale of assets	0.1	(6.2)	(0.7)	(0.5)	(0.1)	(0.8)	0.5	(0.0)	(0.2)	0.0	(0.8)	(0.3)	(0.3)	(0.3)	(0.3)	(0.3)
Impairment charges			243.3	266.0	750.0				450.0							
EBIT	**73.3**	**151.5**	**(54.6)**	**(155.1)**	**(670.4)**	**142.7**	**211.8**	**129.1**	**(335.4)**	**157.2**	**214.4**	**137.7**	**131.5**	**187.1**	**265.2**	**164.5**
Operating Margin (excluding impairment)	*15.6%*	*27.1%*	*29.8%*	*20.0%*	*15.7%*	*24.2%*	*31.5%*	*22.7%*	*20.8%*	*25.7%*	*31.5%*	*23.3%*	*22.4%*	*28.1%*	*34.4%*	*25.3%*
Interest	72.2	70.8	68.739	71.5	70.0	70.1	72.7	72.4	72.0	73.7	74.1	73.6	74.7	75.8	76.9	78.0
Other income, net	(3.0)	(1.9)	(2.9)	(4.6)	(3.7)	(3.1)	(6.7)	(8.0)	(4.8)	(2.6)	(1.5)	(4.2)	(3.3)	(2.9)	(3.0)	(3.4)
Total other income (deductions)	**69.2**	**68.9**	**65.8**	**66.8**	**66.2**	**67.0**	**66.0**	**64.5**	**67.1**	**71.1**	**72.6**	**69.4**	**71.4**	**72.9**	**73.9**	**74.6**
EBT	**4.2**	**82.6**	**(120.5)**	**(221.9)**	**(736.6)**	**75.7**	**145.8**	**64.6**	**(402.5)**	**86.1**	**141.8**	**68.3**	**60.1**	**114.3**	**191.4**	**89.9**
Provision for income taxes	1.7	32.648	39.7	12.7	(4.1)	30.2	57.5	28.2	10.6	34.1	50.2	24.2	23.8	45.1	75.6	35.5
Implied Tax Rate (excl. goodwill impairment)	42%	40%	32%	29%	-31%	40%	39%	44%	22%	39.6%	35.4%	35.4%	39.5%	39.5%	39.5%	39.5%
Income (loss) from continuing operations	**2.4**	**50.0**	**(160.2)**	**(234.6)**	**(732.5)**	**45.5**	**88.2**	**36.4**	**(413.1)**	**52.0**	**91.6**	**44.2**	**36.4**	**69.1**	**115.8**	**54.4**
Loss (income) from discontinued operations, net of tax	(0.26)	0.81	0.00	0.00												
Net Income (loss)	**2.7**	**49.2**	**(160.2)**	**(234.6)**	**(732.5)**	**45.5**	**88.2**	**36.4**	**(413.1)**	**52.0**	**91.6**	**44.2**	**36.4**	**69.1**	**115.8**	**54.4**
Diluted EPS from continuing operations	0.02	0.31	(1.00)	(1.47)	(4.58)	0.28	0.55	0.23	(2.58)	0.32	0.52	0.25	0.21	0.39	0.63	0.29
EPS excl. impairment & one-time expenses	**0.02**	**0.31**	**0.52**	**0.17**	**0.11**	**0.28**	**0.55**	**0.23**	**0.19**	**0.32**	**0.52**	**0.25**	**0.21**	**0.39**	**0.63**	**0.29**
Diluted Average Shares	160.0	160.0	160.0	160.0	160.0	159.9	160.0	159.9	159.9	164.8	174.7	174.7	176.3	179.4	182.5	185.6
Financial Summary																
Total Revenue growth			6.8%	12.4%	8.2%	5.5%	6.2%	2.7%	8.6%	4.0%	1.2%	3.9%	7.0%	8.5%	13.5%	10.2%
Non-Regulated Revenue growth			0.4%	27.7%	14.4%	20.8%	11.3%	4.1%	-5.2%	-4.5%	-10.3%	5.0%	5.0%	5.0%	5.0%	5.0%
O&M/Revenue	60.3%	53.6%	51.9%	60.7%	61.4%	56.1%	50.9%	56.2%	57.1%	54.0%	50.1%	56.0%	55.6%	52.5%	48.6%	54.5%
General Taxes/ Regulated Revenue	11.4%	9.0%	8.2%	8.7%	11.6%	9.4%	8.2%	9.6%	10.6%	9.3%	8.2%	8.9%	10.2%	8.6%	7.3%	8.6%
Adj. EBITDA	137.9	219.6	258.4	175.8	143.6	210.0	280.2	200.7	183.5	230.4	289.3	210.9	206.8	264.5	344.6	246.0
EPS growth, excluding goodwill impairment charge					620.8%	-8.9%	6.0%	34.0%	73.6%	10.9%	-4.8%	11.0%	8.6%	22.1%	20.9%	15.9%

Source: Company reports, Longbow estimates

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

American Water Works— Annual Income Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	FY04A	FY05A	2006A	FY07A	FY08A	FY09E	FY10E	FY11E
Regulated Segment	1748.0	1836.1	1854.6	1987.6	2082.7	2202.0	2433.5	2606.5
% Increase		5.0%	1.0%	7.2%	4.8%	5.7%	10.5%	7.1%
Non-Regulated Revenue	290.0	310.8	248.5	242.7	272.2	254.3	267.0	280.4
% Increase		7.2%	-20.0%	-2.3%	12.2%	-6.6%	5.0%	5.0%
Other	-20.17	(10.1)	(10.0)	(16.0)	(18.0)	(22.6)	(24.3)	(26.1)
% Regulated Rev	-1.2%	-0.6%	-0.5%	-0.8%	-0.9%	-1.0%	-1.0%	-1.0%
Operating revenues	**2,017.9**	**2,136.7**	**2,093.1**	**2,214.2**	**2,336.9**	**2,433.6**	**2,676.1**	**2,860.8**
Production costs	248.5	262.6	264.4	278.1	288.6	294.5	309.1	327.6
Employee-related costs	407.7	408.8	446.2	463.4	505.6	520.8	562.0	597.9
Operating supplies and services	289.3	338.1	268.2	293.5	283.2	292.0	313.1	331.8
Maintenance materials and services	90.6	97.9	96.5	128.0	136.3	129.0	128.5	134.5
Customer billing and accounting	42.5	44.4	55.6	38.3	44.0	41.4	42.8	42.9
Other	43.4	49.8	43.6	45.3	46.1	46.2	50.8	51.5
Operation and maintenance	1122.0	1201.6	1174.5	1246.5	1303.8	1323.9	1406.3	1486.2
Depreciation and amortization	225.3	261.4	259.2	267.3	271.3	290.1	313.5	324.9
General taxes	170.2	183.3	185.1	183.3	199.1	204.1	209.1	214.1
Loss (gain) on sale of assets	(8.6)	(6.5)	0.1	(7.3)	(0.4)	(1.3)	(1.2)	(1.2)
Impairment charges	78.7	385.4	221.7	509.3	750.0	450.0	0.0	0.0
EBIT	**430.4**	**111.6**	**252.5**	**15.1**	**(186.9)**	**166.7**	**748.4**	**836.7**
Operating Margin (excluding impairment)	*25.2%*	*23.3%*	*22.7%*	*23.7%*	*24.1%*	*25.3%*	*28.0%*	*29.2%*
Interest	315.9	345.3	366.0	283.2	285.2	293.4	305.3	324.0
Other income, net	(11.0)	(9.5)	(4.5)	(12.5)	(21.5)	(13.2)	(12.6)	(12.6)
Total other income (deductions)	**305.0**	**335.7**	**361.5**	**270.6**	**263.7**	**280.2**	**292.7**	**311.4**
EBT	**125.4**	**(224.2)**	**(108.9)**	**(255.5)**	**(450.6)**	**(113.45)**	**455.7**	**525.3**
Provision for income taxes	66.3	51.0	46.9	86.8	111.8	119.0	180.0	207.5
Implied Tax Rate (excl. goodwill impairment)	32.5%	31.6%	41.6%	34.2%	37.3%	35.4%	39.5%	39.5%
Income (loss) from continuing operations	**59.1**	**(275.1)**	**(155.9)**	**(342.3)**	**(562.4)**	**(232.5)**	**275.7**	**317.8**
Loss (income) from discontinued operations, net of tax	124.0	49.9	6.4	0.6				
Net Income (loss)	**(64.9)**	**(325.0)**	**(162.2)**	**(342.8)**	**(562.4)**	**(232.5)**	**275.7**	**317.8**
Diluted EPS from continuing operations	0.37	(1.72)	(0.97)	(2.14)	(3.52)	(1.38)	1.52	1.64
EPS excl. impairment & one-time expenses	**0.86**	**0.69**	**0.41**	**1.04**	**1.17**	**1.28**	**1.52**	**1.64**
Diluted Average Shares	160.0	160.0	160.0	160.0	160.0	168.5	180.9	193.5
Financial Summary								
Total Revenue growth		5.9%	-2.0%	5.8%	5.5%	4.1%	10.0%	6.9%
Non-Regulated Revenue growth			-20.0%	-2.3%	12.2%	-6.6%	5.0%	5.0%
O&M/Revenue	55.6%	56.2%	56.1%	56.3%	55.8%	54.4%	52.6%	52.0%
Depreciation and amortization/ Net Fixed Asset				3.1%	2.9%	2.9%	2.8%	2.7%
Depreciation Growth		16.0%	-0.8%	3.1%	1.5%	7.0%	8.0%	3.7%
General Taxes/ Regulated Revenue	9.7%	10.0%	10.0%	9.2%	9.6%	9.3%	8.6%	8.2%
Adj. EBITDA	734.3	758.4	733.4	791.8	834.4	906.9	1,061.9	1,161.7
Interest Expense/ Average Net Debt			8.9%	6.2%	5.6%	5.5%	5.6%	5.9%
Interest Expense/Revenue	15.7%	16.2%	17.5%	12.8%	12.2%	12.1%	11.4%	11.3%
Net Income Growth (excl. goodwill impairment)		338.6%	-1.6%	180.1%	12.6%	16.0%	26.8%	15.3%
EPS growth, (excl. goodwill impairment)			-40.3%	153.8%	12.3%	9.4%	18.8%	7.8%
ROE (excl. goodwill & goodwill impairment)			2.3%	7.0%	8.3%	8.4%	9.3%	9.4%

Source: Company reports, Longbow estimates

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

WATER INDUSTRY PEER VALUATION

($ in millions, except per share data)

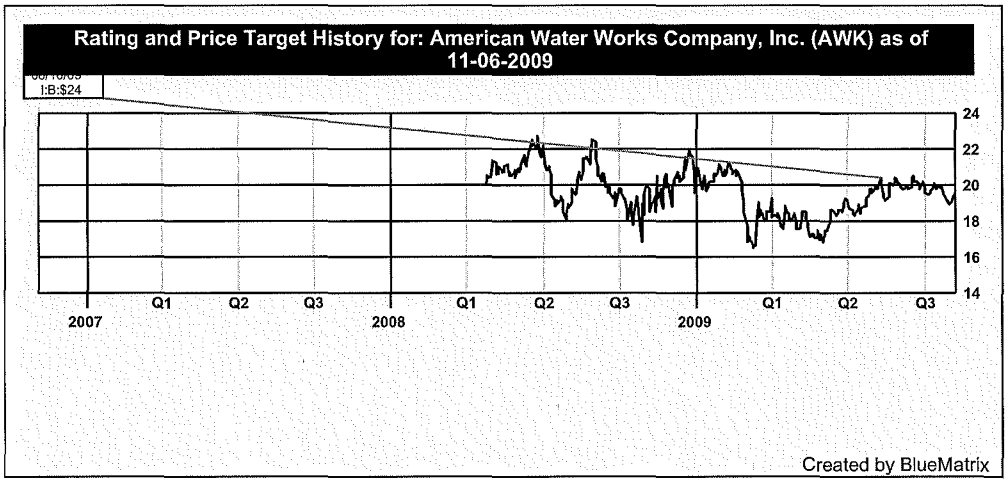
							52 Week			Revenue FY	Earnings per Share			P/E		Dividend	Price/
Company	Ticker	FY End	Rating	Target	% Upside	Share Price	Hi	Lo	Mkt Cap	End	Last FY	Current FY	Next FY	Current FY	Next FY	Rate	Book
U.S. WATER UTILITIES																	
American Water Works	**AWK**	**Dec.**	**BUY**	**$24**	**20%**	**$ 20.50**	**$22.35**	**$16.22**	**$ 3,517**	**$ 2,337**	**1.17**	**1.28**	**1.52**	**16.0x**	**13.5x**	**4.3%**	**1.3x**
Aqua America	**WTR**	**Dec.**	**Neutral**			**$ 16.17**	**$22.00**	**$15.39**	**$ 2,196**	**$ 627**	**0.73**	**0.78**	**0.93**	**20.8x**	**17.4x**	**3.6%**	**2.6x**
American States Water	**AWR**	**Dec.**	**Neutral**			**$ 34.41**	**$38.79**	**$27.56**	**$ 642**	**$ 319**	**1.56**	**1.85**	**1.97**	**18.6x**	**17.4x**	**3.0%**	**1.8x**
California Water Service Group	**CWT**	**Dec.**	**BUY**	**$45**	**24%**	**$ 36.27**	**$48.28**	**$33.49**	**$ 753**	**$ 410**	**1.90**	**2.00**	**2.20**	**18.1x**	**16.5x**	**3.2%**	**2.4x**
Southwest Water Company	SWWC	Dec.	NR			$ 6.11	$8.31	$2.67	$ 151	$ 222	-0.19	*0.17*	*0.39*	35.9x	15.7x	3.3%	0.7x
Artesian Resources Corporation	ARTNA	Dec	NR			$ 17.20	$18.14	$12.81	$ 122	$ 56	0.86	*1.03*	*1.11*	16.7x	15.5x	4.6%	1.3x
Consolidated Water Co	CWCO	Dec	NR			$ 14.52	$21.29	$6.35	$ 209	$ 60	0.50	*0.79*	*0.82*	18.4x	17.7x	2.1%	1.5x
Connecticut Water Service	CTWS	Dec	NR			$ 22.87	$25.94	$17.31	$ 200	$ 61	1.12	*1.06*	*1.06*	21.6x	21.6x	3.9%	1.9x
Middlesex Water Company	MSEX	Dec	NR			$ 16.39	$17.93	$11.64	$ 216	$ 91	0.90	*0.7*	*0.8*	23.4x	20.5x	4.5%	1.7x
Pennichuck Corporation	PNNW	Dec	NR			$ 23.33	$24.80	$14.75	$ 98	$ 31	0.57	*0.54*	*0.76*	43.2x	30.7x	3.1%	1.8x
York Water Company	YORW	Dec	NR			$ 14.08	$17.95	$9.74	$ 161	$ 33	0.57	*0.66*	*0.69*	21.3x	20.4x	3.6%	2.0x
U.S. Water Utility Average														23.1x	18.8x	3.6%	1.7x
EQUIPMENT/FILTRATION/TREATMENT SECTOR																	
Calgon Carbon Corp.	CCC	Dec.	NR			$ 13.85	$19.31	$10.00	$ 793	$ 400	0.56	*0.5*	*0.77*	27.7x	18.0x	0.0%	3.3x
Danaher	DHR	Dec.	NR			$ 72.55	$72.78	$47.20	$ 23,008	$ 12,697	4.23	*3.45*	*3.88*	21.0x	18.7x	0.2%	1.8x
ITT Technologies	ITT	Dec.	NR			$ 53.01	$56.95	$31.94	$ 9,472	$ 11,695	4.04	*3.75*	*3.94*	14.1x	13.5x	1.6%	2.7x
Layne Christensen	LAYN	Jan.	NR			$ 28.30	$35.14	$10.36	$ 544	$ 1,008	2.20	*0.63*	*0.92*	44.9x	30.8x	0.0%	0.7x
Mueller Water Products	MWA	Sept	NR			$ 4.98	$8.55	$1.48	$ 566	$ 1,428	0.46	*(0.34)*	*0.16*	-14.6x	31.1x	1.4%	1.9x
Nalco	NLC	Dec.	NR			$ 23.07	$23.13	$7.80	$ 3,161	$ 4,212	1.30	*0.84*	*1.24*	27.5x	18.6x	0.6%	4.0x
Pall Corp.	PLL	Jul.	NR			$ 34.05	$34.54	$18.20	$ 3,919	$ 2,329	1.94	*1.85*	*2.08*	18.4x	16.4x	1.7%	3.2x
Pentair	**PNR**	**Dec.**	**BUY**	**$37**	**18%**	**$ 30.57**	**$34.27**	**$17.23**	**$ 3,018**	**$ 3,382**	**2.20**	**1.42**	**1.80**	**21.5x**	**16.9x**	**2.3%**	**1.2x**
Watts Water Technologies	**WTS**	**Dec.**	**Neutral**			**$ 31.47**	**$32.88**	**$15.85**	**$ 1,108**	**$ 1,459**	**1.83**	**1.54**	**1.52**	**20.5x**	**20.7x**	**1.5%**	**1.1x**
Equipment/Filtration/Treatment Average (*ex BWTR and CCC)														20.1x	20.5x	1.0%	2.2x
WATER RESOURCES/ INFRASTRUCTURE																	
Insituform Technologies	INSU		NR			$ 21.01	$23.00	$11.02	$ 836	$ 537	0.77	*1.05*	*1.29*	20.5x	16.7x	0.0%	1.5x
Lindsay Manufacturing	LNN		NR			$ 34.97	$51.46	$20.89	$ 417	$ 336	3.11	*0.85*	*1.22*	30.5x	27.3x	0.9%	2.5x
Tetra Tech	TTEK		NR			$ 26.77	$32.00	$14.20	$ 1,578	$ 2,145	1.02	*1.24*	*1.42*	18.3x	19.1x	0.0%	2.8x
Water Resources/ Infrastructure Average														23.1x	21.0x	0.3%	2.3x

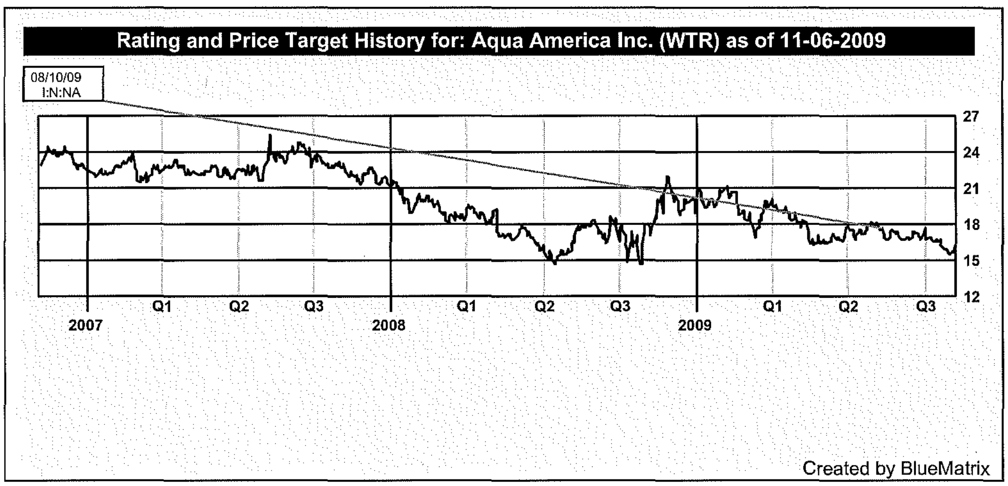
Relevant Indices		**Share Price**
Dow Jones Industrials	DJ30	$ 10,226.94
S&P 500	SPX	$ 1,093.07
Nasdaq Composite	NDX	$ 2,154.06

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.

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com





APPENDIX

IMPORTANT DISCLOSURES

REGULATION ANALYST CERTIFICATION ("REG AC"): The Research Analyst(s) who prepared this research report hereby certifies that the views expressed in the research report accurately reflect the analyst(s) personal views about the subject companies and their securities. The Research Analyst(s) also certifies that the Analyst(s) have not been, are not, and will not be receiving direct or indirect compensation for expressing the specific recommendation(s) or view(s) in this report.

Covered Companies Mentioned In This Report:

American Water Works Company, Inc.	AWK	$20.50	Buy
Aqua America Inc.	WTR	$16.16	Neutral

GENERAL DISCLOSURES: Longbow Securities does not make a market in any securities, nor does it hold a principal

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

position in any security. However, any officer, director or stockholder of Longbow Securities or any member of their families may have a position in and may from time to time purchase or sell any of the securities mentioned or any related securities. Security prices in this report may either reflect the previous day's closing price or an intraday price, depending on the time of distribution. Consensus estimates are derived from either Thomson/Reuters, Bloomberg or Baseline. Designated trademarks and brands are the property of their respective owners.

SPECIFIC DISCLOSURES:

- Longbow Securities does not make a market in the securities of any company mentioned in this Report, and is not a market-maker in any securities generally. Nor does the firm does hold a principal position in any security.
- As of the date of this Report, no officer, director or stockholder of Longbow Securities, or any member of their immediate families, holds securities of any company mentioned in the Report. In the event such persons purchase, hold or sell securities of a company mentioned in the Report for their own account, any subsequent Report shall disclose the fact of any such ownership or transactions.
- No employee of Longbow Securities serves on the Board of Directors of the subject security or any other security mentioned in this report.
- Neither the Research Analyst nor a member of the Research Analyst's household has a financial interest in the securities of the subject company or any other security mentioned in this report.
- Neither the Research Analyst nor a member of the Research Analyst's household serves on the Board of Directors of the subject company or any other security mentioned in this report.
- Neither Longbow Securities nor its affiliates beneficially own 1% or more of an equity security of the subject company or any other security mentioned in this report.

RATINGS DISTRIBUTIONS FOR LONGBOW RESEARCH:

Rating Category	Count	Percent
Buy	62	29.7%
Neutral	143	68.4%
Sell	4	1.9%

RATING SYSTEM:

"Buy" means that Longbow Securities expects total return to exceed 20% over a 12-month period.

"Neutral" means that Longbow Securities expects total return to be within a range of plus or minus 20% over a 12-month period.

"Sell" means that Longbow Securities expects total return to be negative by greater than 20% over a 12-month period.

Longbow Research's full research universe and related applicable disclosures can be obtained by calling (216) 986-0700 or via postal mail at: Editorial Department, Longbow Research, 6000 Lombardo Center, Suite #500, Independence, Ohio 44131.

DISCLAIMER: The information, opinions, estimates and projections contained in this report were prepared by Longbow Securities LLC, a wholly owned subsidiary of Longbow Research LLC, and constitute the current judgment of Longbow Securities as of the date of this report. Additional information may be available from Longbow Securities upon request. The information contained herein is believed to be reliable and has been obtained from sources believed to be reliable, but Longbow Securities makes no representation or warranty, either expressed or implied, as to the accuracy, completeness or reliability of such information. Longbow Securities does not undertake, and has no duty, to advise you as to any information that comes to its attention after the date of this report or any changes in its opinion, estimates or projections. Prices and availability of securities are also subject to change without notice. By accepting this report, the reader acknowledges that the report does not purport to meet

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

LONGBOW Research
Tactical advantage through independent research

Company Update

November 17, 2009 **AMERICAN WATER WORKS COMPANY, INC. (AWK)**

Rating:	**BUY**	
Current Price:	**$20.42**	
Target Price:	**$24.00**	

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

Industry: Water Utilities **Fiscal Year: Dec**			**1Q09A**	**2Q09A**	**3Q09A**	**4Q09E**	**FY09E**	**Valuation Multiple**	**FY10E**	**Valuation Multiple**
Market Cap ($MM):	3,567	**EPS:**	$0.19	$0.32	$0.52	$0.25	$1.28	16.0x	$1.52	13.4x
Net Debt ($MM):	5,345	Consensus:				$0.25	$1.29	15.8x	$1.44	14.2x
Enterprise Value ($MM):	8,912	Last Year:	$0.11	$0.28	$0.55	$0.23	$1.17			
Shares - FD (MM):	174.7									
		EBITDA:	$1.15	$1.40	$1.66	$1.67	$5.38	9.5x	$5.87	8.7x
Dividend:	$0.84	Growth:	28%	10%	3%	5%	9%		17%	
Yield:	4.1%									
Beta:	0.46	**Revenue:**	$550	$613	$680	$591	$2,434	3.7x	$2,676	3.3x
Rel. P/E (FY2009E):	83%	Growth:	9%	4%	1%	4%	140%		10%	

AWK: RWE Announces Complete Exit

SUMMARY

- Last night, AWK announced that its former parent company, RWE, will sell 37.4M AWK shares, and offer another 3.7M shares to the underwriters for purchase under a 30-day option. As was the case with other offerings recently, we expect underwriters to use the option, resulting in the complete exit of RWE from AWK (vs. a current 23.5% ownership).

- We view this as a very positive announcement for AWK, as we believe the expectation of a large number of shares coming to the market in the near future was placing an artificial cap on AWK's share price. We anticipate that AWK's discounted valuation (13.4x our 2010E EPS) relative to the industry average (19.0x) should ease gradually after the "RWE overhang" is removed.

- As a reminder, RWE acquired AWK in 2003, but announced plans to divest the company in 2005 after facing difficulty in navigating the complex regulatory environment in the U.S. RWE finally sold 40% of its stake in AWK with an initial offering in April 2008, with two more rounds of secondary offerings (prior to yesterday's announcement) in June and August 2009.

- To catch up from five years of underinvestment by RWE, AWK is now spending heavily on capex with $4.0-4.5B anticipated over the course of the next five years. We anticipate this to drive earnings growth over that time period.

- We continue to estimate adjusted EPS of $1.28 in FY09, $1.52 in FY10 and $1.64 in FY11 based on revenue growth assumptions of 4.1%, 10.0% and 6.9%, respectively. We are reiterating our BUY rating and $24 target price.

INVESTMENT THESIS

We rate American Water Works Company, Inc. (AWK) a BUY with a $24 target price, as we see AWK as offering an attractive risk/reward with positive catalysts relative to the peer group. We believe AWK shares were trading at a discount partially due to the "RWE overhang." As this overhang will now be removed, AWK's discounted valuation relative to the industry average should gradually ease. However, our target price still incorporates a 17% discount to the peer group average. The shares are trading at 13.4x our FY10E EPS, relative to a peer group average of 19.0x. As the largest and most geographically diversified water utility in the U.S., AWK should benefit by investing to replace and expand the aging water infrastructure in the country. As such, the company is planning to spend $4.0-4.5B over the next five years, which should drive earnings growth over that time period.

VALUATION

AWK shares closed yesterday at $20.42, which is 16.0x our FY09E EPS of $1.28 and 13.4x our FY10E EPS of $1.52. The shares are trading at a discount to the peer group average of 19.0x FY10E EPS due in large part to the RWE overhang, which we believe the Street was already accounting for. The shares are trading at 1.3x tangible book value ($15.69/share) compared to a peer group that trades over 1.7x, on average. Our target price of $24 is based on 15.8x our FY10E EPS, a valuation that remains at a discount to the peer group. However, we see multiple expansion from current levels as justified given AWK being viewed as the largest and most diversified publicly traded water utility in the U.S., with potential from earnings growth as the company catches up after insufficient rate increases in the past five to six years.

RISKS

The potential risks to our investment thesis include, but are not limited to: 1) delays in rate case processing or lower rate increases by the regulators than our expectations, 2) 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, 4) a large acquisition at an excessive valuation (significantly above the rate base), and 5) a large goodwill impairment that could lead to a breach of debt covenants or regulatory requirements.

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

INCREMENTAL REVENUE FROM RATE CASES & SURCHARGES (i) ALREADY APPROVED & (ii) CURRENTLY PENDING

State	Date Filed	Amount Filed	Actual Amount Granted	% Granted	Effective Dates	Days for Processing	1Q09E	2Q09E	3Q09E	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E	1Q11E	2Q11E	3Q11E	4Q11E
Approved Rate Cases (in $ million)							**1Q09E**	**2Q09E**	**3Q09E**	**4Q09E**	**1Q10E**	**2Q10E**	**3Q10E**	**4Q10E**	**1Q11E**	**2Q11E**	**3Q11E**	**4Q11E**
CA (Sacram., etc)	1/1/07	16.4	13.0	79%	6/1/08	517		2.2										
AZ (Sun City Water)	4/30/07	2.2	1.9	86%	6/1/08	398		0.3										
AZ (Anthem)	6/16/06	7.0	4.3	61%	6/4/08	719		0.7										
VA	1/30/08	4.3	3.4	79%	7/8/08	160		0.9										
IL	8/31/07	32.8	21.6	66%	8/8/08	343		5.4	1.8									
TN	3/14/08	7.6	1.7	22%	10/1/08	201		0.4	0.4									
OH	10/1/07	5.5	5.3	96%	11/13/08	409		1.3	1.3	0.7								
PA (WW)	4/28/08	2.7	1.9	70%	11/14/08	200		0.5	0.5	0.2								
MO	3/31/08	49.8	34.5	69%	11/28/08	242		8.6	8.6	5.8								
NJ	1/14/08	125.0	72.1	58%	12/8/08	329		18.0	18.0	12.0								
WV	5/30/08	14.8	5.2	35%	3/26/09	300		1.3	1.3	1.3	1.3							
CA (ROE)	5/1/08	2.8	0.1	4%	5/6/09	370		0.0	0.0	0.0	0.0	0.0						
CA (Monterey Water)	1/31/08	37.1	12.1	33%	5/11/09	466		1.5	3.0	3.0	3.0	1.5						
CA (General Office)	1/31/08	6.4	2.2	34%	5/11/09	466		0.3	0.6	0.6	0.6	0.3						
NM	6/30/08	2.2	1.4	62%	5/12/09	316		0.2	0.3	0.3	0.3	0.2						
AWWM (NJ)	8/1/08	3	1.6	53%	5/21/09			0.1	0.2	0.2	0.2	0.2	0.1	0.1	0.1	0.1	0.0	0.0
KY	10/31/08	18.5	10.3	56%	6/1/09	213		0.9	2.6	2.6	2.6	1.7						
MI	6/22/09	0.2	0.2	100%	7/1/09				0.1	0.1	0.1	0.1						
CA (Monterey WW)	1/31/08	1.8	1.7	94%	7/9/09	525			0.4	0.4	0.4	0.4						
MD	5/2/09	0.8	0.8	100%	9/23/09	144				0.2	0.2	0.2	0.2					
IA	4/30/09	9.4	6.1	64%	10/9/09	162			1.7	1.5	1.5	1.5	0.0					
PA	4/30/09	58.1	30.8	53%	11/7/09	191				5.1	7.7	7.7	7.7	2.6				
VA (non-jurisdictional customers)			0.3					0.1										
TOTAL/AVERAGE				63%		337		**42.6**	**40.8**	**33.9**	**17.8**	**13.7**						
Approved Surcharge (in $ million)							**1Q09E**	**2Q09E**	**3Q09E**	**4Q09E**	**1Q10E**	**2Q10E**	**3Q10E**	**4Q10E**	**1Q11E**	**2Q11E**	**3Q11E**	**4Q11E**
PA			5.7		9/1/08			1.4	1.4									
AZ			0.6		9/1/08			0.2	0.2									
PA			6		1/1/09			1.5	1.5	1.5								
NY			0.4		1/1/09			0.1	0.1	0.1								
AZ			0.2		1/1/09			0.1	0.1	0.1								
PA			2.4		4/1/09			0.6	0.6	0.6	0.6							
IN			3.8		4/1/09			1.0	1.0	1.0	1.0							
IL			0.7					0.2	0.2	0.2	0.2							
OH			0.6					0.2	0.2	0.2	0.2							
7/1/09 - 9/17/09			11.5						1.9	2.9	2.9	2.9	1.0					
TOTAL								**5.1**	**7.0**	**6.4**	**4.8**	**2.9**	**1.0**					
Approved Interim Rates (in $ million)							**1Q09E**	**2Q09E**	**3Q09E**	**4Q09E**	**1Q10E**	**2Q10E**	**3Q10E**	**4Q10E**	**1Q11E**	**2Q11E**	**3Q11E**	**4Q11E**
TX	2/21/08	0.9	0.4	44%	6/1/08			0.1										
HI	11/1/07	1.3	0.7	54%	9/1/08			0.2	0.2									
TOTAL								**0.2**	**0.2**									
State	**Date Filed**	**Amount Filed ($ million)**	**Expected Amount Granted ($ million)**		**Expected Effective Dates**													
Pending Rate Cases & Expected Surcharges (in $ million)							**1Q09E**	**2Q09E**	**3Q09E**	**4Q09E**	**1Q10E**	**2Q10E**	**3Q10E**	**4Q10E**	**1Q11E**	**2Q11E**	**3Q11E**	**4Q11E**
AZ (multiple)	5/1/08	20.0	13.2		11/1/09					2.2	3.3	3.3	3.3	1.1				
CA (Sac, LA, Lark)	1/23/09	26.1	17.2		6/1/10								4.3	4.3	4.3	4.3		
		6.6	4.4		1/1/11										1.1	1.1	1.1	1.1
IN	5/1/09	46.9	31.0		5/1/10							5.2	7.7	7.7	7.7	2.6		
OH	5/7/09	8.8	5.8		5/7/10							1.0	1.5	1.5	1.5	0.5		
IL	5/29/09	58.6	38.7		5/29/10							3.2	9.7	9.7	9.7	6.4		
AZ (multiple)	7/2/09	20.6	13.6		7/2/10								3.4	3.4	3.4	3.4		
NM	8/21/09	0.7	0.5		8/21/10								0.0	0.1	0.1	0.1	0.1	
MO	10/30/09	48.7	32.1		10/30/10									5.4	8.0	8.0	8.0	2.7
Surcharges									7.5	7.5	7.5	7.5	10.5	12.0	12.0	12.0	12.0	12.0
TOTAL								0.0	7.5	9.7	10.8	20.2	40.4	45.1	47.8	38.5	21.2	15.8
TOTAL INCREMENTAL REVENUE Quarterly							**47.1**	**47.9**	**55.5**	**50.0**	**33.4**	**36.7**	**41.4**	**45.1**	**47.8**	**38.5**	**21.2**	**15.8**
							2009E				2010E				2011E			
TOTAL INCREMENTAL REVENUE Annual							**200.6**				**156.6**				**123.2**			

Source: Company reports and Longbow Research estimates.

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

American Water Works— Quarterly Income Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E
Regulated Segment	419.3	508.6	571.9	487.8	449.9	527.1	603.7	502.1	497.4	554.9	621.0	528.7	533.4	603.6	710.2	586.3
% Increase			7.3%	11.2%	7.3%	3.6%	5.6%	2.9%	10.6%	5.3%	2.9%	5.3%	7.2%	8.8%	14.4%	10.9%
Non-Regulated Revenue	53.3	55.5	66.4	67.5	61.0	67.0	73.9	70.3	57.5	64.2	65.2	67.3	60.4	67.4	68.5	70.7
% Increase			0.4%	27.7%	14.4%	20.8%	9.4%	4.1%	-5.7%	-4.2%	-11.7%	-4.3%	5.0%	5.0%	5.0%	5.0%
Other	(4.0)	(5.4)	(5.1)	(1.5)	(4.1)	(4.7)	(5.4)	(3.9)	(4.7)	(6.3)	(6.3)	(5.3)	(5.3)	(6.0)	(7.1)	(5.9)
% Regulated Rev	-1.0%	-1.1%	-0.9%	-0.3%	-0.9%	-0.9%	-0.9%	-0.8%	-1.0%	-1.1%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%
Operating revenues	**468.5**	**558.7**	**633.1**	**553.8**	**506.8**	**589.4**	**672.2**	**568.6**	**550.2**	**612.7**	**680.0**	**590.7**	**588.4**	**665.0**	**771.6**	**651.2**
Production costs	61.1	69.8	83.5	63.6	64.2	72.6	84.1	67.7	69.0	77.2	86.7					
Employee-related costs	109.8	119.2	112.8	121.5	126.8	131.4	127.4	119.9	132.6	133.2	139.6					
Operating supplies and services	63.8	63.9	83.9	81.8	69.5	66.7	72.2	74.8	56.8	58.6	60.2					
Maintenance materials and services	30.1	26.3	27.6	43.9	34.9	37.2	32.0	32.1	32.2	31.8	31.7					
Customer billing and accounting	8.3	9.1	8.6	12.2	7.4	11.9	13.4	11.2	10.8	13.2	12.7					
Other	9.5	11.0	11.8	13.1	8.3	10.7	13.1	14.0	12.9	16.7	9.9					
Operation and maintenance	282.6	299.4	328.3	336.2	311.3	330.6	342.2	319.8	314.4	330.6	340.9	330.8	327.4	348.8	375.2	354.9
Depreciation and amortization	64.6	68.1	69.7	64.9	63.9	67.3	68.4	71.6	68.8	73.2	74.9	73.2	75.3	77.3	79.4	81.5
General taxes	47.9	45.9	47.1	42.3	52.1	49.6	49.4	48.0	52.5	51.7	50.6	49.3	54.5	52.0	52.0	50.6
Loss (gain) on sale of assets	0.1	(6.2)	(0.7)	(0.5)	(0.1)	(0.8)	0.5	(0.0)	(0.2)	0.0	(0.8)	(0.3)	(0.3)	(0.3)	(0.3)	(0.3)
Impairment charges			243.3	266.0	750.0				450.0							
EBIT	**73.3**	**151.5**	**(54.6)**	**(155.1)**	**(670.4)**	**142.7**	**211.8**	**129.1**	**(335.4)**	**157.2**	**214.4**	**137.7**	**131.5**	**187.1**	**265.2**	**164.5**
Operating Margin (excluding impairment)	*15.6%*	*27.1%*	*29.8%*	*20.0%*	*15.7%*	*24.2%*	*31.5%*	*22.7%*	*20.8%*	*25.7%*	*31.5%*	*23.3%*	*22.4%*	*28.1%*	*34.4%*	*25.3%*
Interest	72.2	70.8	68.739	71.5	70.0	70.1	72.7	72.4	72.0	73.7	74.1	73.6	74.7	75.8	76.9	78.0
Other income, net	(3.0)	(1.9)	(2.9)	(4.6)	(3.7)	(3.1)	(6.7)	(8.0)	(4.8)	(2.6)	(1.5)	(4.2)	(3.3)	(2.9)	(3.0)	(3.4)
Total other Income (deductions)	**69.2**	**68.9**	**65.8**	**66.8**	**66.2**	**67.0**	**66.0**	**64.5**	**67.1**	**71.1**	**72.6**	**69.4**	**71.4**	**72.9**	**73.9**	**74.6**
EBT	**4.2**	**82.6**	**(120.5)**	**(221.9)**	**(736.6)**	**75.7**	**145.8**	**64.6**	**(402.5)**	**86.1**	**141.8**	**68.3**	**60.1**	**114.3**	**191.4**	**89.9**
Provision for income taxes	1.7	32.648	39.7	12.7	(4.1)	30.2	57.5	28.2	10.6	34.1	50.2	24.2	23.8	45.1	75.6	35.5
Implied Tax Rate (excl. goodwill impairment)	42%	40%	32%	29%	-31%	40%	39%	44%	22%	39.6%	35.4%	35.4%	39.5%	39.5%	39.5%	39.5%
Income (loss) from continuing operations	**2.4**	**50.0**	**(160.2)**	**(234.6)**	**(732.5)**	**45.5**	**88.2**	**36.4**	**(413.1)**	**52.0**	**91.6**	**44.2**	**36.4**	**69.1**	**115.8**	**54.4**
Loss (income) from discontinued operations, net of tax	(0.26)	0.81	0.00	0.00												
Net Income (loss)	**2.7**	**49.2**	**(160.2)**	**(234.6)**	**(732.5)**	**45.5**	**88.2**	**36.4**	**(413.1)**	**52.0**	**91.6**	**44.2**	**36.4**	**69.1**	**115.8**	**54.4**
Diluted EPS from continuing operations	0.02	0.31	(1.00)	(1.47)	(4.58)	0.28	0.55	0.23	(2.58)	0.32	0.52	0.25	0.21	0.39	0.63	0.29
EPS excl. impairment & one-time expenses	**0.02**	**0.31**	**0.52**	**0.17**	**0.11**	**0.28**	**0.55**	**0.23**	**0.19**	**0.32**	**0.52**	**0.25**	**0.21**	**0.39**	**0.63**	**0.29**
Diluted Average Shares	160.0	160.0	160.0	160.0	160.0	159.9	160.0	159.9	159.9	164.8	174.7	174.7	176.3	179.4	182.5	185.6
Financial Summary																
Total Revenue growth			6.8%	12.4%	8.2%	5.5%	6.2%	2.7%	8.6%	4.0%	1.2%	3.9%	7.0%	8.5%	13.5%	10.2%
Non-Regulated Revenue growth			0.4%	27.7%	14.4%	20.8%	11.3%	4.1%	-5.2%	-4.5%	-10.3%	5.0%	5.0%	5.0%	5.0%	5.0%
O&M/Revenue	60.3%	53.6%	51.9%	60.7%	61.4%	56.1%	50.9%	56.2%	57.1%	54.0%	50.1%	56.0%	55.6%	52.5%	48.6%	54.5%
General Taxes/ Regulated Revenue	11.4%	9.0%	8.2%	8.7%	11.6%	9.4%	8.2%	9.6%	10.6%	9.3%	8.2%	8.9%	10.2%	8.6%	7.3%	8.6%
Adj. EBITDA	137.9	219.6	258.4	175.8	143.6	210.0	280.2	200.7	183.5	230.4	289.3	210.9	206.8	264.5	344.6	246.0
EPS growth, excluding goodwill impairment charge					620.8%	-8.9%	6.0%	34.0%	73.6%	10.9%	-4.8%	11.0%	8.6%	22.1%	20.9%	15.9%

Source: Company reports, Longbow estimates

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

American Water Works— Annual Income Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	FY04A	FY05A	2006A	FY07A	FY08A	FY09E	FY10E	FY11E
Regulated Segment	1748.0	1836.1	1854.6	1987.6	2082.7	2202.0	2433.5	2606.5
% Increase		5.0%	1.0%	7.2%	4.8%	5.7%	10.5%	7.1%
Non-Regulated Revenue	290.0	310.8	248.5	242.7	272.2	254.3	267.0	280.4
% Increase		7.2%	-20.0%	-2.3%	12.2%	-6.6%	5.0%	5.0%
Other	-20.17	(10.1)	(10.0)	(16.0)	(18.0)	(22.6)	(24.3)	(26.1)
% Regulated Rev	-1.2%	-0.6%	-0.5%	-0.8%	-0.9%	-1.0%	-1.0%	-1.0%
Operating revenues	**2,017.9**	**2,136.7**	**2,093.1**	**2,214.2**	**2,336.9**	**2,433.6**	**2,676.1**	**2,860.8**
Production costs	248.5	262.6	264.4	278.1	288.6	294.5	309.1	327.6
Employee-related costs	407.7	408.8	446.2	463.4	505.6	520.8	562.0	597.9
Operating supplies and services	289.3	338.1	268.2	293.5	283.2	292.0	313.1	331.8
Maintenance materials and services	90.6	97.9	96.5	128.0	136.3	129.0	128.5	134.5
Customer billing and accounting	42.5	44.4	55.6	38.3	44.0	41.4	42.8	42.9
Other	43.4	49.8	43.6	45.3	46.1	46.2	50.8	51.5
Operation and maintenance	1122.0	1201.6	1174.5	1246.5	1303.8	1323.9	1406.3	1486.2
Depreciation and amortization	225.3	261.4	259.2	267.3	271.3	290.1	313.5	324.9
General taxes	170.2	183.3	185.1	183.3	199.1	204.1	209.1	214.1
Loss (gain) on sale of assets	(8.6)	(6.5)	0.1	(7.3)	(0.4)	(1.3)	(1.2)	(1.2)
Impairment charges	78.7	385.4	221.7	509.3	750.0	450.0	0.0	0.0
EBIT	**430.4**	**111.6**	**252.5**	**15.1**	**(186.9)**	**166.7**	**748.4**	**836.7**
Operating Margin (excluding impairment)	*25.2%*	*23.3%*	*22.7%*	*23.7%*	*24.1%*	*25.3%*	*28.0%*	*29.2%*
Interest	315.9	345.3	366.0	283.2	285.2	293.4	305.3	324.0
Other income, net	(11.0)	(9.5)	(4.5)	(12.5)	(21.5)	(13.2)	(12.6)	(12.6)
Total other income (deductions)	**305.0**	**335.7**	**361.5**	**270.6**	**263.7**	**280.2**	**292.7**	**311.4**
EBT	**125.4**	**(224.2)**	**(108.9)**	**(255.5)**	**(450.6)**	**(113.45)**	**455.7**	**525.3**
Provision for income taxes	66.3	51.0	46.9	86.8	111.8	119.0	180.0	207.5
Implied Tax Rate (excl. goodwill impairment)	32.5%	31.6%	41.6%	34.2%	37.3%	35.4%	39.5%	39.5%
Income (loss) from continuing operations	**59.1**	**(275.1)**	**(155.9)**	**(342.3)**	**(562.4)**	**(232.5)**	**275.7**	**317.8**
Loss (income) from discontinued operations, net of tax	124.0	49.9	6.4	0.6				
Net Income (loss)	**(64.9)**	**(325.0)**	**(162.2)**	**(342.8)**	**(562.4)**	**(232.5)**	**275.7**	**317.8**
Diluted EPS from continuing operations	0.37	(1.72)	(0.97)	(2.14)	(3.52)	(1.38)	1.52	1.64
EPS excl. impairment & one-time expenses	**0.86**	**0.69**	**0.41**	**1.04**	**1.17**	**1.28**	**1.52**	**1.64**
Diluted Average Shares	160.0	160.0	160.0	160.0	160.0	168.5	180.9	193.5
Financial Summary								
Total Revenue growth		5.9%	-2.0%	5.8%	5.5%	4.1%	10.0%	6.9%
Non-Regulated Revenue growth			-20.0%	-2.3%	12.2%	-6.6%	5.0%	5.0%
O&M/Revenue	55.6%	56.2%	56.1%	56.3%	55.8%	54.4%	52.6%	52.0%
Depreciation and amortization/ Net Fixed Asset				3.1%	2.9%	2.9%	2.8%	2.7%
Depreciation Growth		16.0%	-0.8%	3.1%	1.5%	7.0%	8.0%	3.7%
General Taxes/ Regulated Revenue	9.7%	10.0%	10.0%	9.2%	9.6%	9.3%	8.6%	8.2%
Adj. EBITDA	734.3	758.4	733.4	791.8	834.4	906.9	1,061.9	1,161.7
Interest Expense/ Average Net Debt			8.9%	6.2%	5.6%	5.5%	5.6%	5.9%
Interest Expense/Revenue	15.7%	16.2%	17.5%	12.8%	12.2%	12.1%	11.4%	11.3%
Net Income Growth (excl. goodwill impairment)		338.6%	-1.6%	180.1%	12.6%	16.0%	26.8%	15.3%
EPS growth, (excl. goodwill impairment)			-40.3%	153.8%	12.3%	9.4%	18.8%	7.8%
ROE (excl. goodwill & goodwill impairment)			2.3%	7.0%	8.3%	8.4%	9.3%	9.4%

Source: Company reports, Longbow estimates

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

WATER INDUSTRY PEER VALUATION

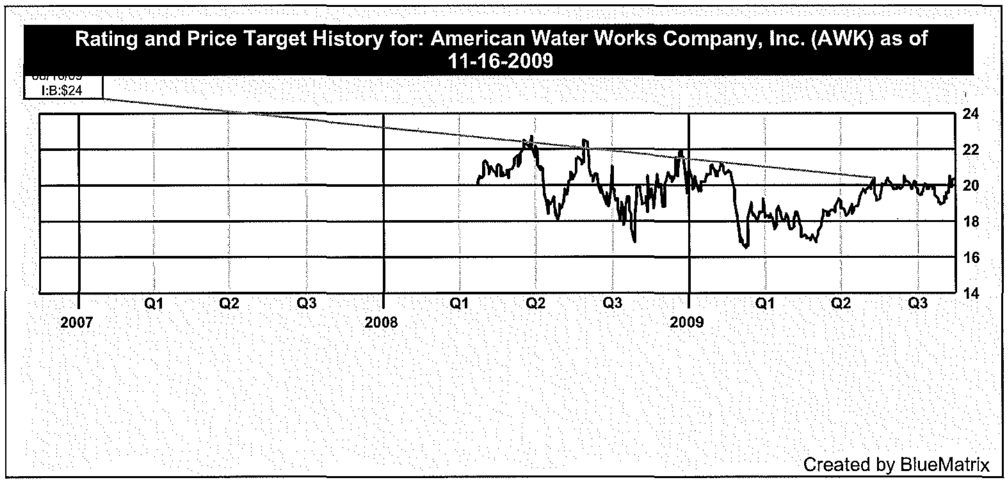
($ in millions, except per share data)

							52 Week			Revenue FY	Earnings per Share			P/E		Dividend	Price/
Company	Ticker	FY End	Rating	Target	% Upside	Share Price	Hi	Lo	Mkt Cap	End	Last FY	Current FY	Next FY	Current FY	Next FY	Rate	Book
U.S. WATER UTILITIES																	
American Water Works	**AWK**	**Dec.**	**BUY**	**$24**	**20%**	**$ 20.42**	**$22.35**	**$16.22**	**$ 3,543**	**$ 2,337**	**1.17**	**1.28**	**1.52**	**15.9x**	**13.4x**	**4.1%**	**1.3x**
Aqua America	**WTR**	**Dec.**	**Neutral**			**$ 16.10**	**$22.00**	**$15.39**	**$ 2,153**	**$ 627**	**0.73**	**0.78**	**0.93**	**20.7x**	**17.3x**	**3.7%**	**2.6x**
American States Water	**AWR**	**Dec.**	**Neutral**			**$ 33.17**	**$38.79**	**$27.56**	**$ 598**	**$ 319**	**1.56**	**1.85**	**1.97**	**18.0x**	**16.8x**	**3.2%**	**1.8x**
California Water Service Group	**CWT**	**Dec.**	**BUY**	**$45**	**24%**	**$ 36.22**	**$48.28**	**$33.49**	**$ 732**	**$ 410**	**1.90**	**2.00**	**2.20**	**18.1x**	**16.5x**	**3.3%**	**2.4x**
Southwest Water Company	SWWC	Dec.	NR			$ 6.18	$6.32	$2.67	$ 154	$ 222	-0.19	*0.16*	*0.36*	38.6x	17.2x	3.2%	0.7x
Artesian Resources Corporation	ARTNA	Dec	NR			$ 17.12	$18.14	$12.81	$ 120	$ 56	0.86	*0.95*	*1.08*	18.0x	15.9x	4.6%	1.3x
Consolidated Water Co	CWCO	Dec	NR			$ 13.29	$21.29	$6.35	$ 200	$ 60	0.50	*0.67*	*0.79*	19.8x	16.8x	2.2%	1.5x
Connecticut Water Service	CTWS	Dec	NR			$ 22.93	$25.94	$17.31	$ 190	$ 61	1.12	*1.13*	*1.08*	20.3x	21.2x	4.1%	1.9x
Middlesex Water Company	MSEX	Dec	NR			$ 16.41	$17.93	$11.64	$ 212	$ 91	0.90	*0.7*	*0.8*	23.4x	20.5x	4.6%	1.7x
Pennichuck Corporation	PNNW	Dec	NR			$ 23.59	$24.80	$14.75	$ 99	$ 31	0.57	*0.56*	*0.74*	42.1x	31.9x	3.0%	1.8x
York Water Company	YORW	Dec	NR			14.34	$17.95	$9.74	$ 173	$ 33	0.57	*0.65*	*0.68*	22.1x	21.1x	3.6%	2.0x
U.S. Water Utility Average														23.4x	19.0x	3.6%	1.7x
EQUIPMENT/FILTRATION/TREATMENT SECTOR																	
Calgon Carbon Corp.	CCC	Dec.	NR			$ 13.89	$19.31	$10.00	$ 743	$ 400	0.56	*0.52*	*0.79*	26.7x	17.6x	0.0%	3.3x
Danaher	DHR	Dec.	NR			$ 73.08	$73.37	$47.20	$ 23,210	$ 12,697	4.23	*3.45*	*3.88*	21.2x	18.8x	0.2%	1.8x
ITT Technologies	ITT	Dec.	NR			$ 53.74	$56.95	$31.94	$ 9,576	$ 11,695	4.04	*3.73*	*3.94*	14.4x	13.6x	1.6%	2.7x
Layne Christensen	LAYN	Jan.	NR			$ 29.10	$35.14	$10.36	$ 535	$ 1,008	2.20	*0.63*	*0.92*	46.2x	31.6x	0.0%	0.7x
Mueller Water Products	MWA	Sept	NR			$ 4.70	$8.55	$1.48	$ 529	$ 1,428	0.46	*(0.35)*	*0.16*	-13.4x	29.4x	1.5%	1.9x
Nalco	NLC	Dec.	NR			$ 24.34	$23.74	$7.80	$ 3,288	$ 4,212	1.30	*0.86*	*1.26*	28.3x	19.3x	0.6%	4.0x
Pall Corp.	PLL	Jul.	NR			$ 34.87	$34.54	$18.20	$ 4,062	$ 2,329	1.94	*1.85*	*2.08*	18.8x	16.8x	1.7%	3.2x
Pentair	**PNR**	**Dec.**	**BUY**	**$37**	**17%**	**$ 32.03**	**$34.27**	**$17.23**	**$ 3,069**	**$ 3,382**	**2.20**	**1.42**	**1.80**	**22.5x**	**17.8x**	**2.3%**	**1.2x**
Watts Water Technologies	**WTS**	**Dec.**	**Neutral**			**$31.57**	**$32.88**	**$15.85**	**$ 1,113**	**$ 1,459**	**1.83**	**1.54**	**1.52**	**20.5x**	**20.7x**	**1.4%**	**1.1x**
Equipment/Filtration/Treatment Average (*ex BWTR and CCC)														20.6x	20.6x	1.0%	2.2x
WATER RESOURCES/ INFRASTRUCTURE																	
Insituform Technologies	INSU		NR			$ 21.85	$23.00	$11.02	$ 840	$ 537	0.77	*1.02*	*1.29*	21.3x	16.8x	0.0%	1.5x
Lindsay Manufacturing	LNN		NR			$ 36.32	$47.69	$20.89	$ 427	$ 336	3.11	*0.84*	*1.26*	31.3x	27.5x	0.9%	2.5x
Tetra Tech	TTEK		NR			26.80	$32.00	$14.20	$ 1,547	$ 2,287	1.02	*1.24*	*1.39*	20.9x	19.1x	0.0%	2.8x
Water Resources/ Infrastructure Average														24.5x	21.1x	0.3%	2.3x

Relevant Indices		Share Price
Dow Jones Industrials	DJ30	$ 10,226.94
S&P 500	SPX	$ 1,093.07
Nasdaq Composite	NDX	$ 2,154.06

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.

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com



APPENDIX

IMPORTANT DISCLOSURES

REGULATION ANALYST CERTIFICATION ("REG AC"): The Research Analyst(s) who prepared this research report hereby certifies that the views expressed in the research report accurately reflect the analyst(s) personal views about the subject companies and their securities. The Research Analyst(s) also certifies that the Analyst(s) have not been, are not, and will not be receiving direct or indirect compensation for expressing the specific recommendation(s) or view(s) in this report.

Covered Companies Mentioned In This Report:

American Water Works Company, Inc.	AWK	$20.42	Buy
American States Water Company	AWR	$32.33	Neutral
California Water Service Group	CWT	$35.28	Buy
Pentair, Inc.	PNR	$31.22	Buy
Aqua America Inc.	WTR	$15.84	Neutral
Watts Water Technologies, Inc.	WTS	$30.40	Neutral

GENERAL DISCLOSURES: Longbow Securities does not make a market in any securities, nor does it hold a principal position in any security. Security prices in this report may either reflect the previous day's closing price or an intraday price, depending on the time of distribution. Consensus estimates are derived from either Thomson/Reuters, Bloomberg or Baseline. Designated trademarks and brands are the property of their respective owners.

SPECIFIC DISCLOSURES:

- Longbow Securities does not make a market in the securities of any company mentioned in this report, and is not a market maker in any securities. Nor does the firm hold a principal position in any security.

- As of the date of this report, no officer, director or stockholder of Longbow Securities, or any member of their immediate families, holds securities of any company mentioned in the report. In the event such persons purchase, hold or sell securities of a company mentioned in the report for their own account, any subsequent report shall disclose the fact of any such ownership or transactions.

- As of the date of this report, no employee of Longbow Securities serves on the Board of Directors of the subject security or any other security mentioned in this report.

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

- As of the date of this report, neither the Research Analyst nor a member of the Research Analyst's household has a financial interest in the securities of the subject company or any other security mentioned in this report.
- As of the date of this report, neither the Research Analyst nor a member of the Research Analyst's household serves on the Board of Directors of the subject company or any other security mentioned in this report.
- As of the date of this report, neither Longbow Securities nor its affiliates beneficially own 1% or more of an equity security of the subject company or any other security mentioned in this report.

RATINGS DISTRIBUTIONS FOR LONGBOW RESEARCH:

Rating Category	Count	Percent
Buy	63	30.0%
Neutral	143	68.1%
Sell	4	1.9%

RATING SYSTEM:

"Buy" means that Longbow Securities expects total return to exceed 20% over a 12-month period.

"Neutral" means that Longbow Securities expects total return to be within a range of plus or minus 20% over a 12-month period.

"Sell" means that Longbow Securities expects total return to be negative by greater than 20% over a 12-month period.

Longbow Research's full research universe and related applicable disclosures can be obtained by calling (216) 986-0700 or via postal mail at: Editorial Department, Longbow Research, 6000 Lombardo Center, Suite #500, Independence, Ohio 44131.

DESCRIPTION: Longbow Securities LLC, a wholly owned subsidiary of Longbow Research LLC, is a primary research provider established in 2003 and headquartered at 6000 Lombardo Center, Suite 500, Independence, Ohio 44131 USA. The company provides research services to institutional investors, investment advisers, and professional money managers. MEMBER FINRA/SIPC. Additional information supporting the statements in this report is available upon request.

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

LONGBOW Research
Tactical advantage through independent research

Company Update

December 9, 2009 **AMERICAN WATER WORKS COMPANY, INC. (AWK)**

Rating:	**BUY**	
Current Price:	**$21.60**	
Target Price:	**$24.00**	

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

Industry: Water Utilities **Fiscal Year: Dec**			**1Q09A**	**2Q09A**	**3Q09A**	**4Q09E**	**FY09E**	**Valuation Multiple**	**FY10E**	**Valuation Multiple**
Market Cap ($MM):	3,774	**EPS:**	$0.19	$0.32	$0.52	$0.25	$1.28	16.9x	$1.52	14.2x
Net Debt ($MM):	5,345	Consensus:				$0.24	$1.28	16.9x	$1.43	15.1x
Enterprise Value ($MM):	9,119	Last Year:	$0.11	$0.28	$0.55	$0.23	$1.17			
Shares - FD (MM):	174.7									
		EBITDA:	$1.15	$1.40	$1.66	$1.67	$5.38	9.7x	$5.87	8.9x
Dividend:	$0.84	Growth:	28%	10%	3%	5%	9%		17%	
Yield:	3.9%									
Beta:	0.46	**Revenue:**	$550	$613	$680	$591	$2,434	3.7x	$2,676	3.4x
Rel. P/E (FY2009E):	83%	Growth:	9%	4%	1%	4%	140%		10%	

AWK: Highlights from Investor Day

SUMMARY

- We attended AWK's investor day held in New York on December 7th. We believe the company should be able to narrow its 400bp gap between earned ROEs and allowed ROEs, through strategic timing of capex projects around rate cases, and implementing investment surcharges where applicable. However, given regulatory lag, completely narrowing the gap will be difficult.

- Management indicated it would like to increase the company's equity ratio from the current 42.7% to 45-50% over the next four to five years, as indicated by state PUC's. However, the implied equity raise going forward is a likely contributor to the discounted valuation for AWK vs. its peers.

- The company estimates that it lost $0.14 in EPS just in 3Q09 from wet weather and declining consumption due to the recession. However, the unfavorable conditions in 2009 should make for easier y/y comps in 2010.

- AWK has won all four major military base contacts that have been awarded in the last two years. With a larger number of bases (>50) expected to be privatized over the next decade, we believe that military base operations offer a growth opportunity for the company.

- Regarding M&A, the rate of deals for AWK hinted that it does not expect another Trenton-sized (mid-level) or larger acquisition by the mid-2010. The company has completed five tuck-in acquisitions. We believe that there is potential for AWK to further increase the pace of its acquisition activity going forward with smaller tuck-ins more likely.

- We continue rate AWK as a BUY with a $24 price target. We see multiple expansion from earnings growth percentages in the low teens over the next three years, as the company overcomes the insufficient rate increases of the past five to six years, and catches up.

IMPORTANT DISCLOSURES ARE LOCATED IN THE APPENDIX.

INVESTMENT THESIS

We rate American Water Works Company, Inc. (AWK) a BUY with a $24 target price, as we see AWK as offering an attractive risk/reward with positive catalysts relative to the peer group. We believe AWK shares were trading at a discount partially due to the "RWE overhang." As this overhang is now removed, AWK's discounted valuation relative to the industry average should ease. However, our target price still incorporates an 18% discount to the peer group average. The shares are trading at 14.2x our FY10E EPS, relative to a peer group average of 19.5x. As the largest and most geographically diversified water utility in the U.S., AWK should benefit by investing to replace and expand the aging water infrastructure in the country. As such, the company is planning to spend $4.0-4.5 billion over the next five years, which should drive earnings growth over that time period.

DISCUSSION OF DETAILS

We attended AWK's investor conference on December 7th in New York City. During the presentation, among other areas, the company highlighted its (i) environmental stewardship programs, (ii) improvement in customer service, and (iii) increased focus on business development. We were pleased to see the company's increased focus of transparency and investor education including (i) its estimate of its market size and market share – $100 billion and 2.2%, (ii) ROE gap (difference between authorized and earned ROE) caused by regulatory lag of 50-100bp, and (iii) savings from cost cutting efforts – $42M in 2008. We believe that management is taking the right steps to reduce its consolidated ROE gap of ~400bp, but were underwhelmed with the company's performance on business development, which includes both acquisition growth and new non-regulated contracts. At the same time, additional details on the military base operation business increased our confidence in its long-term profitable growth opportunity. Here are some key takeaways from the presentation:

Narrowing the ROE Gap

AWK is still catching up to rate increases after years of rate stay-outs during RWE ownership. Apart from the rate stay-outs, some factors have increased the rate increase needed by the company, Firstly, after the current CEO, Don Correll, was brought on three years ago, he had to further increase operating expenses to improve customer service and management oversight. Secondly, over the last two to three years the company has also significantly increased its capex. These two factors have increased the delay in bringing the earned ROE closer to the authorized ROE. Management believes that over the next one to two rate cycles (each lasting one and half to two years), the company should be able to narrow the ROE gap. We note that the company has received authorized ROEs in the range of 10.0% to 10.8% during the last year. However, the LTM earned ROE has been only 6.5% (excluding interest expense related to goodwill).

The company is taking several steps to close the regulatory lag, including making most of the discretionary capex in eight states which have infrastructure surcharge mechanisms. These mechanisms allow the company to start earning a return on its investment at an earlier date. In other states, which do not have such mechanisms, the company tries to time the capex investment around the rate case process to reduce the regulatory lag. However, for the first time, the company accepted that, even in a perfect world, after all the rate increases have caught up to years of rate stay-outs, regulatory lag will still cause earned ROEs to be perpetually below allowed ROEs by approximately 50-100bps.

Capital Structure

AWK wants to increase its equity ratio from the current 42.7% to 45-50% over the next four to five years. Though this level of equity is required even now by state Public Utility Commissions, the company works around the requirement by using parent company's debt as equity at the subsidiary level. Though increasing the equity ratio will have negative effect on the consolidated ROE (interest paid on debt at parent level is less than the return allowed on equity at subsidiary level), we believe the company is taking this step to improve its credit rating and reduce the

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

balance sheet risk perceived by the investors. The weaker capital structure might be one of the reasons investors have historically paid a discounted valuation for AWK vs. its peers.

Effect of Weather and Economy in 2009

With unfavorable weather and the weak economy, AWK described 2009 as having been the perfect storm. The company estimates that it lost $0.14 in EPS just in 3Q09 from these factors. Additionally, the weak economy had a double impact on the regulated business. Firstly, it lowers consumption by industrial and commercial customers, and secondly foreclosures and decreased housing starts lower organic residential customer growth. California, Arizona and Illinois have been particularly hit by the latter. Decline in new construction activity, both residential and commercial, also reduces opportunities for developer-related non-regulated business growth. However, the unfavorable conditions in 2009 should make for easier y/y comps in 2010. The impact of weather can completely reverse next year, and the fall in consumption due to economic conditions is taken into consideration by the regulators for rate setting during the next rate cycle.

Military Base Operations

Unlike American States Water (AWR, NEUTRAL), AWK does not disclose the financial results of its military base operations. However, during the event we received additional insights into the business. It seems that AWK has been more successful in this business than AWR. The company has already won four price determinations, and only has a few minor equitable adjustment requests pending. Also, AWK has won all four major contacts that have been awarded in the last two years. In our view, the company's experience with contract operations business is the main factor in its success in this business. With a larger number of bases (>50) expected to be privatized over the next decade, we believe that military base operations is a strong growth opportunity for the company.

Acquisitions and Business Development

AWK is taking a much more analytical and customer-focused approach to business development for its non-regulated business. The company currently is in discussion with over 75 municipalities for deals ranging from outright purchase to various forms/levels of public-private partnerships.

The company spent time highlighting the lease & operate/concession model for public-private partnership (PPP). Though this model is common in Europe and South America for water systems, and has been used in the U.S. for roads, bridges, airports and ports, it is rarely used in the U.S. for water systems. The model requires lessee to pay an upfront amount, fixed annual amount, or percentage of revenue to the leaser for the right to operate the water system. Though this model can increase the investment required for PPP, the company mentioned the possibility of partnership with investment firms to finance such deals. The contracts that the company has received in Elizabeth, NJ and Edison, NJ are one of the few concession transactions in the U.S. for the water sector. Though success of this model in expanding the company's PPP business is hard to predict, we were pleased to see the company using innovative ways to grow its business. We also note that AWR's targets for PPP's and acquisitions in general have a great deal of overlap with AWK's current geographic footprint. This suggests that riskier deals in new geographies are lower on the priority list.

Regarding M&A, the rate of deals for AWK has lagged its principal peer in this regard, Aqua America (WTR, NEUTRAL), and the company hinted that it does not expect another Trenton-sized (mid-level) or larger acquisition by the middle of 2010. The company has completed five tuck-in acquisitions this year vs. 15 for WTR. We believe that there is potential for AWK to further increase the pace of its acquisition activity, with smaller tuck-ins more likely.

Improved Customer Service Looks Good to Regulators

The company highlighted the improvements it has made in customer service which indirectly impacts its ability to receive higher authorized ROEs from the regulators. The company has lowered the average wait time for its service calls to less than 30 seconds. Also, the percentage of customers in surveys who were "satisfied" or "very satisfied"

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

after service requests increased to 87%. As a part of the recent rate settlement in Pennsylvania, the company increased assistance to low-income customers from 150K to 250K. AWK has also started a web-based, self-service tool that allows customers to discontinue service, make payments, check account balances, and update their accounts online. Even without external marketing, about 50,000 customers have already signed up for this tool. We believe that these service improvements can be helpful in narrowing the ROE gap, as regulators take the number of customer complains into consideration while granting rate increases.

Other Highlights:

- The company gave an estimate of its market size. AWK estimates the U.S. water services to be a $90-100 billion market, giving it a 2.2% market share. The market includes public portion (municipal wages, overhead, etc.) – 66%, water chemical and equipment – 14%, engineering construction and other – 13.5%, and revenue for regulated private utilities – 6.5%.
- AWK's regulated business is well positioned geographically, considering the nation's water infrastructure need. It operates in most of the states (CA, TX, MI, IL, OH, PA and NY) that need more than $10 billion of investment over the next 20 years. Most of its other states need investment between $3 billion and $10 billion.
- AWK is active in promoting favorable regulations at the federal level, including removing the cap on private activity bonds (tax-free bonds by private sector for infrastructure investment) and increasing the size of the state revolving funds. Both of these have the potential to reduce financing costs for the company.
- The pace of regulatory reform at the state level has been slow. For example, though it has been a while since AWK filed a request for an infrastructure surcharge mechanism in New Jersey, there is still no definite date for a next step in the approval process.
- Implementation of an infrastructure surcharge mechanism has a notable effect on the company's ability to make infrastructure investment. For example in Pennsylvania, since DSIC has been implemented, miles of main replaced annually has increased from 25 to 81, reducing the years to replace main in distribution system from 225 to 117.
- AWK quantified its savings from cost cutting efforts. In 2008, with a $520 million spend, the company saved $42 million (8%). The savings included lower purchase price for valves, hydrants, and meters (50%), pipes (25%), and chemicals (15%) vs. the distributor price. The company attributed these savings to economies of scale through consolidated purchasing.
- AWK has a target to voluntarily reduce its carbon footprint by 16% in 2017, mainly by reducing power use by switching to more efficient pumps. This should also lower operating expenses through lower electric bills.

VALUATION

AWK shares closed yesterday at $21.60, which is 16.9x our FY09E EPS of $1.28 and 14.2x our FY10E EPS of $1.52. The shares are trading at a discount to the peer group average of 19.5x FY10E EPS. The shares are trading at 1.4x tangible book value ($15.69/share), compared to a peer group that trades over 1.8x, on average. Our target price of $24 is based on 16x our FY10E EPS, a valuation that remains at a discount to the peer group. However, we see multiple expansion from current levels as justified given AWK being viewed as the largest and most diversified publicly traded water utility in the U.S., and with the potential from earnings growth as the company catches up after insufficient rate increases for the past five to six years.

RISKS

Potential downside risks to our investment thesis include, but are not limited to: 1) delays in rate case processing or lower rate increases by the regulators than our expectations, 2) 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, 4) a large acquisition at an excessive valuation (significantly above the rate base), and 5) a large goodwill impairment, which could lead to a breach of debt covenants or regulatory requirements.

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

American Water Works— Quarterly Income Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E
Regulated Segment	419.3	508.6	571.9	487.8	449.9	527.1	603.7	502.1	497.4	554.9	621.0	528.7	533.4	603.6	710.2	586.3
% Increase			7.3%	11.2%	7.3%	3.6%	5.6%	2.9%	10.6%	5.3%	2.9%	5.3%	7.2%	8.8%	14.4%	10.9%
Non-Regulated Revenue	53.3	55.5	66.4	67.5	61.0	67.0	73.9	70.3	57.5	64.2	65.2	67.3	60.4	67.4	68.5	70.7
% Increase			0.4%	27.7%	14.4%	20.8%	9.4%	4.1%	-5.7%	-4.2%	-11.7%	-4.3%	5.0%	5.0%	5.0%	5.0%
Other	(4.0)	(5.4)	(5.1)	(1.5)	(4.1)	(4.7)	(5.4)	(3.9)	(4.7)	(6.3)	(6.3)	(5.3)	(5.3)	(6.0)	(7.1)	(5.9)
% Regulated Rev	-1.0%	-1.1%	-0.9%	-0.3%	-0.9%	-0.9%	-0.9%	-0.8%	-1.0%	-1.1%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%
Operating revenues	**468.5**	**558.7**	**633.1**	**553.8**	**506.8**	**589.4**	**672.2**	**568.6**	**550.2**	**612.7**	**680.0**	**590.7**	**588.4**	**665.0**	**771.6**	**651.2**
Production costs	61.1	69.8	83.5	63.6	64.2	72.6	84.1	67.7	69.0	77.2	86.7					
Employee-related costs	109.8	119.2	112.8	121.5	126.8	131.4	127.4	119.9	132.6	133.2	139.6					
Operating supplies and services	63.8	63.9	83.9	81.8	69.5	66.7	72.2	74.8	56.8	58.6	60.2					
Maintenance materials and services	30.1	26.3	27.6	43.9	34.9	37.2	32.0	32.1	32.2	31.8	31.7					
Customer billing and accounting	8.3	9.1	8.6	12.2	7.4	11.9	13.4	11.2	10.8	13.2	12.7					
Other	9.5	11.0	11.8	13.1	8.3	10.7	13.1	14.0	12.9	16.7	9.9					
Operation and maintenance	282.6	299.4	328.3	336.2	311.3	330.6	342.2	319.8	314.4	330.6	340.9	330.8	327.4	348.8	375.2	354.9
Depreciation and amortization	64.6	68.1	69.7	64.9	63.9	67.3	68.4	71.6	68.8	73.2	74.9	73.2	75.3	77.3	79.4	81.5
General taxes	47.9	45.9	47.1	42.3	52.1	49.6	49.4	48.0	52.5	51.7	50.6	49.3	54.5	52.0	52.0	50.6
Loss (gain) on sale of assets	0.1	(6.2)	(0.7)	(0.5)	(0.1)	(0.8)	0.5	(0.0)	(0.2)	0.0	(0.8)	(0.3)	(0.3)	(0.3)	(0.3)	(0.3)
Impairment charges			243.3	266.0	750.0				450.0							
EBIT	**73.3**	**151.5**	**(54.6)**	**(155.1)**	**(670.4)**	**142.7**	**211.8**	**129.1**	**(335.4)**	**157.2**	**214.4**	**137.7**	**131.5**	**187.1**	**265.2**	**164.5**
Operating Margin (excluding impairment)	*15.6%*	*27.1%*	*29.8%*	*20.0%*	*15.7%*	*24.2%*	*31.5%*	*22.7%*	*20.8%*	*25.7%*	*31.5%*	*23.3%*	*22.4%*	*28.1%*	*34.4%*	*25.3%*
Interest	72.2	70.8	68.739	71.5	70.0	70.1	72.7	72.4	72.0	73.7	74.1	73.6	74.7	75.8	76.9	78.0
Other income, net	(3.0)	(1.9)	(2.9)	(4.6)	(3.7)	(3.1)	(6.7)	(8.0)	(4.8)	(2.6)	(1.5)	(4.2)	(3.3)	(2.9)	(3.0)	(3.4)
Total other income (deductions)	**69.2**	**68.9**	**65.8**	**66.8**	**66.2**	**67.0**	**66.0**	**64.5**	**67.1**	**71.1**	**72.6**	**69.4**	**71.4**	**72.9**	**73.9**	**74.6**
EBT	**4.2**	**82.6**	**(120.5)**	**(221.9)**	**(736.6)**	**75.7**	**145.8**	**64.6**	**(402.5)**	**86.1**	**141.8**	**68.3**	**60.1**	**114.3**	**191.4**	**89.9**
Provision for income taxes	1.7	32.648	39.7	12.7	(4.1)	30.2	57.5	28.2	10.6	34.1	50.2	24.2	23.8	45.1	75.6	35.5
Implied Tax Rate (excl. goodwill impairment)	42%	40%	32%	29%	-31%	40%	39%	44%	22%	39.6%	35.4%	35.4%	39.5%	39.5%	39.5%	39.5%
Income (loss) from continuing operations	**2.4**	**50.0**	**(160.2)**	**(234.6)**	**(732.5)**	**45.5**	**88.2**	**36.4**	**(413.1)**	**52.0**	**91.6**	**44.2**	**36.4**	**69.1**	**115.8**	**54.4**
Loss (income) from discontinued operations, net of tax	(0.26)	0.81	0.00	0.00												
Net Income (loss)	**2.7**	**49.2**	**(160.2)**	**(234.6)**	**(732.5)**	**45.5**	**88.2**	**36.4**	**(413.1)**	**52.0**	**91.6**	**44.2**	**36.4**	**69.1**	**115.8**	**54.4**
Diluted EPS from continuing operations	0.02	0.31	(1.00)	(1.47)	(4.58)	0.28	0.55	0.23	(2.58)	0.32	0.52	0.25	0.21	0.39	0.63	0.29
EPS excl. impairment & one-time expenses	**0.02**	**0.31**	**0.52**	**0.17**	**0.11**	**0.28**	**0.55**	**0.23**	**0.19**	**0.32**	**0.52**	**0.25**	**0.21**	**0.39**	**0.63**	**0.29**
Diluted Average Shares	160.0	160.0	160.0	160.0	160.0	159.9	160.0	159.9	159.9	164.8	174.7	174.7	176.3	179.4	182.5	185.6
Financial Summary																
Total Revenue growth			6.8%	12.4%	8.2%	5.5%	6.2%	2.7%	8.6%	4.0%	1.2%	3.9%	7.0%	8.5%	13.5%	10.2%
Non-Regulated Revenue growth			0.4%	27.7%	14.4%	20.8%	11.3%	4.1%	-5.2%	-4.5%	-10.3%	5.0%	5.0%	5.0%	5.0%	5.0%
O&M/Revenue	60.3%	53.6%	51.9%	60.7%	61.4%	56.1%	50.9%	56.2%	57.1%	54.0%	50.1%	56.0%	55.6%	52.5%	48.6%	54.5%
General Taxes/ Regulated Revenue	11.4%	9.0%	8.2%	8.7%	11.6%	9.4%	8.2%	9.6%	10.6%	9.3%	8.2%	8.9%	10.2%	8.6%	7.3%	8.6%
Adj. EBITDA	137.9	219.6	258.4	175.8	143.6	210.0	280.2	200.7	183.5	230.4	289.3	210.9	206.8	264.5	344.6	246.0
EPS growth, excluding goodwill impairment charge					620.8%	-8.9%	6.0%	34.0%	73.6%	10.9%	-4.8%	11.0%	8.6%	22.1%	20.9%	15.9%

Source: Company reports, Longbow estimates

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

American Water Works— Annual Income Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	FY04A	FY05A	2006A	FY07A	FY08A	FY09E	FY10E	FY11E
Regulated Segment	1748.0	1836.1	1854.6	1987.6	2082.7	2202.0	2433.5	2606.5
% Increase		5.0%	1.0%	7.2%	4.8%	5.7%	10.5%	7.1%
Non-Regulated Revenue	290.0	310.8	248.5	242.7	272.2	254.3	267.0	280.4
% Increase		7.2%	-20.0%	-2.3%	12.2%	-6.6%	5.0%	5.0%
Other	-20.17	(10.1)	(10.0)	(16.0)	(18.0)	(22.6)	(24.3)	(26.1)
% Regulated Rev	-1.2%	-0.6%	-0.5%	-0.8%	-0.9%	-1.0%	-1.0%	-1.0%
Operating revenues	**2,017.9**	**2,136.7**	**2,093.1**	**2,214.2**	**2,336.9**	**2,433.6**	**2,676.1**	**2,860.8**
Production costs	248.5	262.6	264.4	278.1	288.6	294.5	309.1	327.6
Employee-related costs	407.7	408.8	446.2	463.4	505.6	520.8	562.0	597.9
Operating supplies and services	289.3	338.1	268.2	293.5	283.2	292.0	313.1	331.8
Maintenance materials and services	90.6	97.9	96.5	128.0	136.3	129.0	128.5	134.5
Customer billing and accounting	42.5	44.4	55.6	38.3	44.0	41.4	42.8	42.9
Other	43.4	49.8	43.6	45.3	46.1	46.2	50.8	51.5
Operation and maintenance	1122.0	1201.6	1174.5	1246.5	1303.8	1323.9	1406.3	1486.2
Depreciation and amortization	225.3	261.4	259.2	267.3	271.3	290.1	313.5	324.9
General taxes	170.2	183.3	185.1	183.3	199.1	204.1	209.1	214.1
Loss (gain) on sale of assets	(8.6)	(6.5)	0.1	(7.3)	(0.4)	(1.3)	(1.2)	(1.2)
Impairment charges	78.7	385.4	221.7	509.3	750.0	450.0	0.0	0.0
EBIT	**430.4**	**111.6**	**252.5**	**15.1**	**(186.9)**	**166.7**	**748.4**	**836.7**
Operating Margin (excluding impairment)	*25.2%*	*23.3%*	*22.7%*	*23.7%*	*24.1%*	*25.3%*	*28.0%*	*29.2%*
Interest	315.9	345.3	366.0	283.2	285.2	293.4	305.3	324.0
Other income, net	(11.0)	(9.5)	(4.5)	(12.5)	(21.5)	(13.2)	(12.6)	(12.6)
Total other income (deductions)	**305.0**	**335.7**	**361.5**	**270.6**	**263.7**	**280.2**	**292.7**	**311.4**
EBT	**125.4**	**(224.2)**	**(108.9)**	**(255.5)**	**(450.6)**	**(113.45)**	**455.7**	**525.3**
Provision for income taxes	66.3	51.0	46.9	86.8	111.8	119.0	180.0	207.5
Implied Tax Rate (excl. goodwill impairment)	32.5%	31.6%	41.6%	34.2%	37.3%	35.4%	39.5%	39.5%
Income (loss) from continuing operations	**59.1**	**(275.1)**	**(155.9)**	**(342.3)**	**(562.4)**	**(232.5)**	**275.7**	**317.8**
Loss (income) from discontinued operations, net of tax	124.0	49.9	6.4	0.6				
Net Income (loss)	**(64.9)**	**(325.0)**	**(162.2)**	**(342.8)**	**(562.4)**	**(232.5)**	**275.7**	**317.8**
Diluted EPS from continuing operations	0.37	(1.72)	(0.97)	(2.14)	(3.52)	(1.38)	1.52	1.64
EPS excl. impairment & one-time expenses	**0.86**	**0.69**	**0.41**	**1.04**	**1.17**	**1.28**	**1.52**	**1.64**
Diluted Average Shares	160.0	160.0	160.0	160.0	160.0	168.5	180.9	193.5
Financial Summary								
Total Revenue growth		5.9%	-2.0%	5.8%	5.5%	4.1%	10.0%	6.9%
Non-Regulated Revenue growth			-20.0%	-2.3%	12.2%	-6.6%	5.0%	5.0%
O&M/Revenue	55.6%	56.2%	56.1%	56.3%	55.8%	54.4%	52.6%	52.0%
Depreciation and amortization/ Net Fixed Asset				3.1%	2.9%	2.9%	2.8%	2.7%
Depreciation Growth		16.0%	-0.8%	3.1%	1.5%	7.0%	8.0%	3.7%
General Taxes/ Regulated Revenue	9.7%	10.0%	10.0%	9.2%	9.6%	9.3%	8.6%	8.2%
Adj. EBITDA	734.3	758.4	733.4	791.8	834.4	906.9	1,061.9	1,161.7
Interest Expense/ Average Net Debt			8.9%	6.2%	5.6%	5.5%	5.6%	5.9%
Interest Expense/Revenue	15.7%	16.2%	17.5%	12.8%	12.2%	12.1%	11.4%	11.3%
Net Income Growth (excl. goodwill impairment)		338.6%	-1.6%	180.1%	12.6%	16.0%	26.8%	15.3%
EPS growth, (excl. goodwill impairment)			-40.3%	153.8%	12.3%	9.4%	18.8%	7.8%
ROE (excl. goodwill & goodwill impairment)			2.3%	7.0%	8.3%	8.4%	9.3%	9.4%

Source: Company reports, Longbow estimates

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

WATER INDUSTRY PEER VALUATION

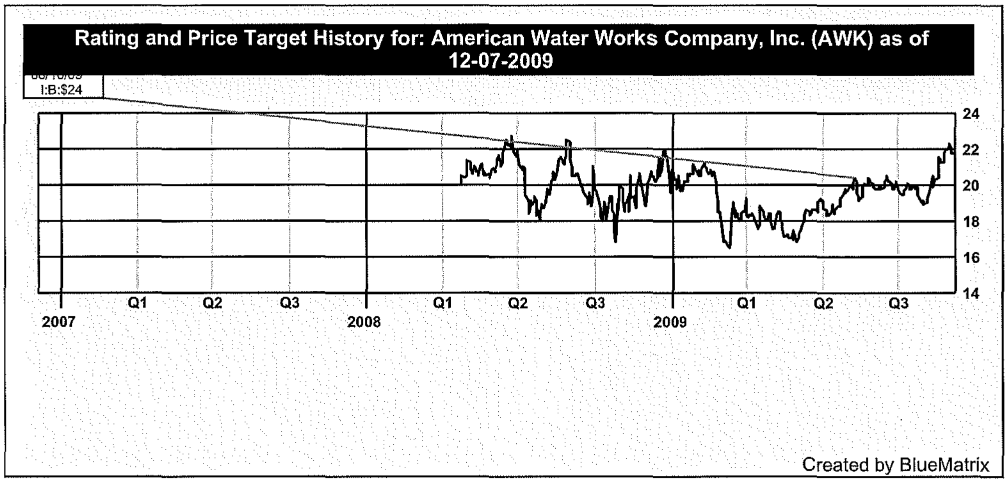
($ in millions, except per share data)

							52 Week			Revenue FY	Earnings per Share			P/E		Dividend	Price/
Company	Ticker	FY End	Rating	Target	% Upside	Share Price	Hi	Lo	Mkt Cap	End	Last FY	Current FY	Next FY	Current FY	Next FY	Rate	Book
U.S. WATER UTILITIES																	
American Water Works	**AWK**	**Dec.**	**BUY**	**$24**	**20%**	**$ 21.60**	**$22.50**	**$16.22**	**$ 3,799**	**$ 2,337**	**1.17**	**1.28**	**1.52**	**16.8x**	**14.2x**	**3.9%**	**1.3x**
Aqua America	**WTR**	**Dec.**	**Neutral**			**$ 16.98**	**$21.50**	**$15.39**	**$ 2,300**	**$ 627**	**0.73**	**0.78**	**0.93**	**21.9x**	**18.3x**	**3.4%**	**2.6x**
American States Water	**AWR**	**Dec.**	**Neutral**			**$ 34.89**	**$38.79**	**$27.56**	**$ 665**	**$ 319**	**1.56**	**1.85**	**1.97**	**18.9x**	**17.7x**	**2.9%**	**1.8x**
California Water Service Group	**CWT**	**Dec.**	**BUY**	**$45**	**19%**	**$ 37.73**	**$48.28**	**$33.49**	**$ 788**	**$ 410**	**1.90**	**2.00**	**2.20**	**18.8x**	**17.2x**	**3.1%**	**2.4x**
Southwest Water Company	SWWC	Dec.	NR			$ 6.15	$6.32	$2.67	$ 153	$ 222	-0.19	*0.05*	*0.36*	123.0x	17.1x	3.3%	0.7x
Artesian Resources Corporation	ARTNA	Dec	NR			$ 17.76	$18.14	$12.81	$ 133	$ 56	0.86	*0.95*	*1.08*	18.7x	16.4x	4.2%	1.3x
Consolidated Water Co	CWCO	Dec	NR			$ 13.15	$21.29	$6.35	$ 191	$ 60	0.50	*0.64*	*0.79*	20.5x	16.6x	2.3%	1.5x
Connecticut Water Service	CTWS	Dec	NR			$ 23.86	$24.98	$17.31	$ 204	$ 61	1.12	*1.19*	*1.1*	20.1x	21.7x	3.8%	1.9x
Middlesex Water Company	MSEX	Dec	NR			$ 16.99	$17.93	$11.64	$ 229	$ 91	0.90	*0.7*	*0.8*	24.3x	21.2x	4.2%	1.7x
Pennichuck Corporation	PNNW	Dec	NR			$ 23.76	$24.80	$14.75	$ 101	$ 31	0.57	*0.54*	*0.74*	44.0x	32.1x	2.9%	1.8x
York Water Company	YORW	Dec	NR			$ 15.02	$17.95	$9.74	$ 188	$ 33	0.57	*0.65*	*0.68*	23.1x	22.1x	3.4%	2.0x
U.S. Water Utility Average														31.8x	19.5x	3.4%	1.7x
EQUIPMENT/FILTRATION/TREATMENT SECTOR																	
Calgon Carbon Corp.	CCC	Dec.	NR			$ 14.25	$19.31	$10.93	$ 780	$ 400	0.56	*0.53*	*0.78*	26.9x	18.3x	0.0%	3.3x
Danaher	DHR	Dec.	NR			$ 72.42	$73.81	$47.73	$ 23,155	$ 12,697	4.23	*3.46*	*3.9*	20.9x	18.6x	0.2%	1.8x
ITT Technologies	ITT	Dec.	NR			$ 52.58	$56.95	$31.94	$ 9,591	$ 11,695	4.04	*3.73*	*3.94*	14.1x	13.3x	1.6%	2.7x
Layne Christensen	LAYN	Jan.	NR			$ 27.17	$35.14	$12.55	$ 529	$ 1,008	2.20	*0.67*	*0.92*	40.6x	29.5x	0.0%	0.7x
Mueller Water Products	MWA	Sept	NR			$ 5.18	$8.55	$1.48	$ 797	$ 1,428	0.46	*(0.36)*	*0.15*	-14.4x	34.5x	1.4%	1.9x
Nalco	NLC	Dec.	NR			$ 24.50	$25.61	$9.38	$ 3,386	$ 4,212	1.30	*0.87*	*1.26*	28.2x	19.4x	0.6%	4.0x
Pall Corp.	PLL	Jul.	NR			$ 32.07	$35.23	$18.20	$ 3,782	$ 2,329	1.94	*1.81*	*2.07*	17.7x	15.5x	1.8%	3.2x
Pentair	**PNR**	**Dec.**	**BUY**	**$37**	**18%**	**$ 31.11**	**$34.27**	**$17.23**	**$ 3,115**	**$ 3,382**	**2.20**	**1.42**	**1.80**	**21.9x**	**17.2x**	**2.3%**	**1.2x**
Watts Water Technologies	**WTS**	**Dec.**	**Neutral**			**$31.45**	**$32.88**	**$15.85**	**$ 1,167**	**$ 1,459**	**1.83**	**1.54**	**1.52**	**20.4x**	**20.7x**	**1.4%**	**1.1x**
Equipment/Filtration/Treatment Average (*ex BWTR and CCC)														19.6x	20.8x	1.0%	2.2x
WATER RESOURCES/ INFRASTRUCTURE																	
Insituform Technologies	INSU		NR			$ 20.99	$23.00	$11.42	$ 815	$ 537	0.77	*1.02*	*1.29*	20.7x	16.3x	0.0%	1.5x
Lindsay Manufacturing	LNN		NR			$ 36.84	$47.02	$20.89	$ 454	$ 336	3.11	*0.83*	*1.23*	33.2x	30.6x	0.9%	2.5x
Tetra Tech	TTEK		NR			$ 26.75	$32.00	$18.49	$ 1,620	$ 2,287	1.02	*1.24*	*1.38*	21.9x	20.2x	0.0%	2.5x
Water Resources/ Infrastructure Average														25.3x	22.4x	0.3%	2.2x

Relevant Indices		Share Price
Dow Jones Industrials	DJ30	$ 10,226.94
S&P 500	SPX	$ 1,093.07
Nasdaq Composite	NDX	$ 2,154.06

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.

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com



APPENDIX

IMPORTANT DISCLOSURES

REGULATION ANALYST CERTIFICATION ("REG AC"): The Research Analyst(s) who prepared this research report hereby certifies that the views expressed in the research report accurately reflect the analyst(s) personal views about the subject companies and their securities. The Research Analyst(s) also certifies that the Analyst(s) have not been, are not, and will not be receiving direct or indirect compensation for expressing the specific recommendation(s) or view(s) in this report.

Covered Companies Mentioned In This Report:

American Water Works Company, Inc.	AWK	$21.60	Buy
American States Water Company	AWR	$35.96	Neutral
California Water Service Group	CWT	$37.97	Buy
Pentair, Inc.	PNR	$31.68	Buy
Aqua America Inc.	WTR	$16.92	Neutral
Watts Water Technologies, Inc.	WTS	$31.87	Neutral

GENERAL DISCLOSURES: Longbow Securities does not make a market in any securities, nor does it hold a principal position in any security. Security prices in this report may either reflect the previous day's closing price or an intraday price, depending on the time of distribution. Consensus estimates are derived from either Thomson/Reuters, Bloomberg or Baseline. Designated trademarks and brands are the property of their respective owners.

SPECIFIC DISCLOSURES:

- Longbow Securities does not make a market in the securities of any company mentioned in this report, and is not a market maker in any securities. Nor does the firm hold a principal position in any security.
- As of the date of this report, no officer, director or stockholder of Longbow Securities, or any member of their immediate families, holds securities of any company mentioned in the report. In the event such persons purchase, hold or sell securities of a company mentioned in the report for their own account, any subsequent report shall disclose the fact of any such ownership or transactions.
- As of the date of this report, no employee of Longbow Securities serves on the Board of Directors of the subject security or any other security mentioned in this report.

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

- As of the date of this report, neither the Research Analyst nor a member of the Research Analyst's household has a financial interest in the securities of the subject company or any other security mentioned in this report.
- As of the date of this report, neither the Research Analyst nor a member of the Research Analyst's household serves on the Board of Directors of the subject company or any other security mentioned in this report.
- As of the date of this report, neither Longbow Securities nor its affiliates beneficially own 1% or more of an equity security of the subject company or any other security mentioned in this report.

RATINGS DISTRIBUTIONS FOR LONGBOW RESEARCH:

Rating Category	Count	Percent
Buy	67	31.0%
Neutral	145	67.1%
Sell	4	1.9%

RATING SYSTEM:

"Buy" means that Longbow Securities expects total return to exceed 20% over a 12-month period.

"Neutral" means that Longbow Securities expects total return to be within a range of plus or minus 20% over a 12-month period.

"Sell" means that Longbow Securities expects total return to be negative by greater than 20% over a 12-month period.

Longbow Research's full research universe and related applicable disclosures can be obtained by calling (216) 986-0700 or via postal mail at: Editorial Department, Longbow Research, 6000 Lombardo Center, Suite #500, Independence, Ohio 44131.

DISCLAIMER: The information, opinions, estimates and projections contained in this report were prepared by Longbow Securities LLC, a wholly owned subsidiary of Longbow Research LLC, and constitute the current judgment of Longbow Securities as of the date of this report. Additional information may be available from Longbow Securities upon request. The information contained herein is believed to be reliable and has been obtained from sources believed to be reliable, but Longbow Securities makes no representation or warranty, either expressed or implied, as to the accuracy, completeness or reliability of such information. Longbow Securities does not undertake, and has no duty, to advise you as to any information that comes to its attention after the date of this report or any changes in its opinion, estimates or projections. Prices and availability of securities are also subject to change without notice. By accepting this report, the reader acknowledges that the report does not purport to meet the objectives or needs of specific investors, and, accordingly, constitutes only "impersonal advisory services" as that term is defined in Rule 204-3 under the Investment Advisers Act of 1940 and that any advice in this report is furnished solely through uniform publications distributed to subscribers thereto within the meaning of Section 2(a)(20)(i) of the Investment Company Act of 1940. The securities discussed in Longbow Research reports may be unsuitable for some investors depending on their specific investment objectives, financial status, risk profile, or particular needs. Investors should consider this report as only a single factor in making their investment decisions and should not rely entirely on this report in evaluating whether or not to buy or sell the securities of the subject company. Longbow Research archives and reviews outgoing and incoming email. Such may be produced at the request of regulators. Sender accepts no liability for any errors or omissions arising as a result of transmission. Use by other than intended recipients is prohibited.

DESCRIPTION: Longbow Securities LLC, a wholly owned subsidiary of Longbow Research LLC, is a primary research provider established in 2003 and headquartered at 6000 Lombardo Center, Suite 500, Independence, Ohio 44131 USA. The company provides research services to institutional investors, investment advisers, and professional money managers. MEMBER FINRA/SIPC. Additional information supporting the statements in this report is available upon request.

Garik Shmois
T: 216-525-8414
E: gshmois@longbowresearch.com

Estimate Changes

LONGBOW Research
Tactical advantage through independent research

January 7, 2010

Analysts:
GARIK SHMOIS
T: 216-525-8414
E: gshmois@longbowresearch.com

VISHAL KHETRIWAL, CFA
T: 216-525-8469
E: vkhetriwal@longbowresearch.com

Industry: **WATER UTILITIES**

Coverage:

Ticker	Rating	Price
AWK	BUY	$23.00
AWR	NEUTRAL	$35.19
CWT	BUY	$35.62
WTR	NEUTRAL	$17.56

Water Utilities: Update on Rate Cases and Impact on Revenues

- In this report we examine the pending rate cases of our four covered water utilities and the impact on FY10E and FY11E revenues.
- We expect the pending and approved rate case to drive an average of 8-11% revenue growth for our covered water utilities for the next two years.
- We are lowering our AWK EPS forecasts for FY10 and FY11 by $0.02 each to $1.50 and $1.62 due to timing issues of announced rate case filings and infrastructure surcharges relative to our prior expectations. We maintain our BUY rating and $24 price target on the shares. We made no modeling changes to the other names under coverage.
- CWT had several small rate increases approved in FY09 but is waiting for $120M in its 2009 GRC to be ruled on in late 2010.
- For WTR, we expect revenue growth of 10% annually in FY10E and FY11E. We note that WTR has grown its top line at a CAGR of 7.2% over the last five years. We remain NEUTRAL mainly on valuation concerns.
- AWR's $51.5M General Rate Case for Regions II and III should be ruled on soon but, given the initial CPUC decision, there could be downside risk to expectations.

IMPORTANT DISCLOSURES ARE LOCATED IN THE APPENDIX.

SUMMARY

Rate increases for inflation and additional capex are the primary revenue drivers for regulated water utilities. In this report, we examine the pending rate cases of our four covered utilities and the impact on FY10E and FY11E revenues. We closely track each individual rate case filed by each utility to model its impact on revenue going forward. **In summary, we expect the pending and approved rate case to drive an average of 8-11% revenue growth for our covered water utilities for the next two years. After reviewing principal rate case proceedings during 4Q09, we are lowering our AWK EPS estimates for FY10 and FY11 by $0.02 each to $1.50 and $1.62,** respectively, as we have reduced our regulated segment revenue forecast by $43M for FY10 and $46M for FY11. After reviewing rate case proceedings for other companies under coverage, we made no additional changes to our models.

Historically, regulators take approximately a year to process rate cases (request for rate increase) and approve only 60-70% of the requested amount. In most states, the utilities are allowed to file rate cases when required, but without "pancaking," i.e., not file a case when another is pending. In California, which has one of the most progressive regulatory environments in the country, and where two of our covered utilities primarily operate, utilities are required to file rate cases every three years and receive a decision in a scheduled 18 months. However, to the benefit of the utilities, if a final decision is delayed beyond the scheduled date, utilities are allowed to charge an interim rate, and also recover or return the difference between the interim and final rates when a final decision is issued.

RATE CASE UPDATES

American Water Works (AWK, BUY, pt $24)
AWK received approximately $86M of rate increases in 2009 and $26.4M of annualized infrastructure surcharges as of November 30, 2009. The company also has approximately $218M of rate cases pending, which are expected to mostly be approved in 2Q10-3Q10. Partially offsetting this, AWK estimates it lost $52.3M and $70.2M in revenues, respectively, in FY08 and through the first three quarters of FY09 from lower consumption due to unfavorable weather and the economic downturn. We have modeled a further pullback of $18.5M in 4Q09. However, we expect AWK to recover some of this decline ($44.4M) in FY10 through normalized weather patterns and an improved demand from new home construction.

As detailed in the tables blow, we expect $142.1M of revenue increase in FY10 from rate increases and surcharges, both from rate cases already approved and currently pending. Though our table details only $117.2M of announced rate cases and surcharges for FY11, we expect revenue increase of $170.0M to account for rate cases that will be filed throughout 2010. That being said, **we reduced our regulated segment revenue estimate by $43M for FY10 and $46M for FY11** due to timing issues of announced rate case filings and infrastructure surcharges relative to our prior expectations. **We now expect overall AWK's revenue to increase 9.7% and 6.9% in FY10 and FY11,** respectively, a 30bp reduction from our prior estimate, as offsetting this is a $1.6M increase in FY10E from customer growth and acquisitions, mostly from acquisitions already completely in 2009. Though we expect additional "tuck-in" acquisitions in 2010 and 2011, we have not assumed additional revenue from these acquisitions, and we expect Non-Regulated revenue to increase by $50M, or 19.7%, in FY10 on account of the Environmental Management Corporation (EMC) acquisition which had annualized revenue of the same amount. For FY11 we expect a much lower 5% organic growth for the Non-Regulated segment. The overall impact of our revenue changes is a $0.02 EPS reduction to $1.50 in FY10E and $1.62 in FY11E.

INCREMENTAL REVENUE FROM RATE CASES & SURCHARGES (i) ALREADY APPROVED & (ii) CURRENTLY PENDING

State	Date Filed	Amount Filed	Actual Amount Granted	% Granted	Effective Dates	Days for Processing									
Approved Rate Cases (in $ million)							4Q09E	1Q10E	2Q10E	3Q10E	4Q10E	1Q11E	2Q11E	3Q11E	4Q11E
OH	10/1/07	5.5	5.3	96%	11/13/08	409	0.7								
PA (WW)	4/28/08	2.7	1.9	70%	11/14/08	200	0.2								
MO	3/31/08	49.8	34.5	69%	11/28/08	242	5.8								
NJ	1/14/08	125.0	72.1	58%	12/8/08	329	12.0								
WV	5/30/08	14.8	5.2	35%	3/26/09	300	1.3	1.3							
CA (ROE)	5/1/08	2.8	0.1	4%	5/6/09	370	0.0	0.0	0.0						
CA (Monterey Water)	1/31/08	37.1	12.1	33%	5/11/09	466	3.0	3.0	1.5						
CA (General Office)	1/31/08	6.4	2.2	34%	5/11/09	466	0.6	0.6	0.3						
NM	6/30/08	2.2	1.4	62%	5/12/09	316	0.3	0.3	0.2						
AWWM (NJ)	8/1/08	3	1.6	53%	5/21/09		0.2	0.2	0.2	0.1	0.1	0.1	0.1	0.0	0.0
KY	10/31/08	18.5	10.3	56%	6/1/09	213	2.6	2.6	1.7						
MI	6/22/09	0.2	0.2	100%	7/1/09		0.1	0.1	0.1						
CA (Monterey WW)	1/31/08	1.8	1.7	94%	7/9/09	525	0.4	0.4	0.4						
MD	5/2/09	0.8	0.8	100%	9/23/09	144	0.2	0.2	0.2	0.2					
IA	4/30/09	9.4	6.1	64%	10/9/09	162	1.5	1.5	1.5	0.0					
PA	4/30/09	58.1	30.8	53%	11/7/09	191	5.1	7.7	7.7	7.7	2.6				
AZ (multiple)	5/1/08	20.0	13.2		11/1/09	549	2.2	3.3	3.3	3.3	1.1				
TX	2/21/08	0.9	0.5	53%	11/17/09	635									
VA (non-jurisdictional customers)			0.3												
TOTAL/AVERAGE				63%		356	**36.1**	**21.1**	**17.0**						
Approved Surcharge (in $ million)							4Q09E	1Q10E	2Q10E	3Q10E	4Q10E	1Q11E	2Q11E	3Q11E	4Q11E
4Q08			6.3		9/1/08		0.8								
1Q09			6.6				1.7	0.8							
2Q09			7.5		1/1/09		1.9	1.9	0.9						
3Q09			6.9		1/1/09		1.7	1.7	1.7	0.9					
Oct 1 - Nov 30 09			5.4		4/1/09		0.7	1.4	1.4	1.4	0.7				
TOTAL							**6.7**	**5.8**	**4.0**	**2.2**					
State	Date Filed	Amount Filed ($ million)	Expected Amount Granted ($ million)		Expected Effective Dates										
Pending Rate Cases & Expected Surcharges (in $ million)							4Q09E	1Q10E	2Q10E	3Q10E	4Q10E	1Q11E	2Q11E	3Q11E	4Q11E
CA (Sac, LA, Lark)	1/23/09	26.1	17.2		6/1/10					4.3	4.3	4.3	4.3		
		6.6	4.4		1/1/11							1.1	1.1	1.1	1.1
IN	5/1/09	46.9	31.0		5/1/10				5.2	7.7	7.7	7.7	2.6		
OH	5/7/09	8.8	5.8		5/7/10				1.0	1.5	1.5	1.5	0.5		
IL	5/29/09	58.6	38.7		5/29/10				3.2	9.7	9.7	9.7	6.4		
AZ (multiple)	7/2/09	20.6	13.6		7/2/10					3.4	3.4	3.4	3.4		
NM	8/21/09	0.7	0.5		8/21/10					0.0	0.1	0.1	0.1	0.1	
MO	10/30/09	48.7	32.1		10/30/10						5.4	8.0	8.0	8.0	2.7
Surcharges							0.8	1.7	3.5	8.3	10.5	10.5	10.5	10.5	10.5
TOTAL							0.8	1.7	12.8	34.9	42.5	46.3	37.0	19.7	14.3
TOTAL(Quarterly)							**43.6**	**28.6**	**33.8**	**37.1**	**42.5**	**46.3**	**37.0**	**19.7**	**14.3**
TOTAL (Annual)									**142.1**				**117.2**		

Source: Company Information and LBR estimates

FY ends December 31($ mil)	2006A	FY07A	FY08A	FY09E	FY10E	FY11E
Rate Increase & Surcharge	26.1	77.4	137.3	196.8	142.1	170.0
% increase		4%	7%	9.5%	6.5%	7.1%
Customer Growth & Acquisitions			3.3	3.2	1.6	
Lower Consumption			(52.3)	(88.7)	44.4	
Non-Regulated	(62.3)	(5.8)	29.5	(16.8)	50.0	15.2
Other	(7.5)	49.5	4.9	2.3	(1.3)	(1.7)
Total	(43.7)	121.1	122.7	96.8	236.8	183.5

Source: Company Information and LBR estimates

California Water Service (CWT, BUY, pt $45)

As detailed in the table below, CWT had several small rate increases approved in 2009 though an escalation increase, interim rates, offset letters, and an increase in the State of Washington and City of Hawthorne. The company is also scheduled to receive an escalation increase for 16 districts and interim rates for eight districts in July 2010. In the table below we have assumed that these increases will be same as July 2009. And finally, the company filed its 2009 GRC for $120.2M ($70.6M for 2011, $24.8M for 2012, and $24.8M for 2013) on July 2, 2009. According the new Rate Case Plan, the California Public Utility Commission (CPUC) has 18 months to review this rate case, but new rates are effective form January 1 of each year. As per historical trends, we have assumed 66% approval for the $70.6M request for 2011.

Rate Increases

			FY10E				FY11E			
Proceeding	Amount ($mil)	Implemented	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q
APPROVED										
Offset Letters	11.7	Jan/Feb 09	1.0							
Hawthorne	0.8	Feb, 09	0.1							
Hawthorne	1.0	Jul, 09	0.3	0.3						
Hawthorne	1.2	Jan, 10	0.3	0.3	0.3	0.3				
2009 Escalation inc. (16 Dis.)	9.0	Jul, 09	2.3	2.3						
2009 Interim Rates (8 Disc)	2.4	Jul, 09	0.6	0.6						
Cost of Capital	(1.8)	Jun, 09	(0.5)	(0.5)						
WA Rate Case	1.2	Jul, 09	0.3	0.3	0.1					
Offset Letters	0.7	Jul, 09	0.2	0.2						
TO BE FILED/APROVED										
2010 Escalation inc. (16 Dis.)	9.0	Jul, 09			2.3	2.3				
2010 Interim Rates (8 Disc)	2.4	Jul, 10			0.6	0.6				
GRC 09	46.7	Jul, 11					11.7	11.7	11.7	11.7
TOTAL (Quaterly)			4.5	3.4	3.3	3.2	11.7	11.7	11.7	11.7
TOTAL (Annual)						14.3				46.7

Source: Company Information and LBR Estimates

Though the table above details $14.3M and $46.7M in rate increases for FY10 and FY11, respectively, for our model we have assumed rate increase of $20.3M and $50.7M, respectively. The difference accounts for additional offset letters or other small rate increases that CWT receives on a regular basis. We have also modeled $2M annually for usage by new customers driven by a modest improvement in new home demand. **In total, we expect CWT to increase revenue by 5% and 12% in FY10 and FY11, respectively.** Our incremental annual revenue assumptions are provided below.

FY Ends December 31	FY04	FY05	FY06	FY07	FY08	FY09E	FY10E	FY11E
Revenue Growth								
Rate Increase	29.8	12.2	10.1	15.0	42.1	49.2	20.3	54.7
% change	10.8%	3.9%	3.1%	4.5%	11.5%	12.0%	4.5%	11.6%
Net Revenue Increase due to WRAM and MCBA					2.0	-3.8		
Usage by New Customers	5.4	3.8	3.1	2.7	4.0	10.1	2.0	2.0
Change is Presentation of Commission Fees					-2.7	0.0		
Decrease in Usage by Existing Customers & Others	3.3	-10.9	0.8	14.7	-2.2	-16.5		
Net Operating Revenue Increase	**38.5**	**5.1**	**14.0**	**32.4**	**43.2**	**39.1**	**22.3**	**56.7**

Source: Company Information and LBR Estimates

Aqua America (WTR, NEUTRAL)

WTR operates in 14 states and, unlike AWK, very few of its states have consolidated state-wide rate case filings. In fact, the company's water and wastewater operations are made up of approximately 200 rate divisions, each of which requires a separate rate filing. This makes it comparatively difficult to track WTR's each individual rate filing.

What we do know is that the company has received $29.3M of rate increases in through the first three quarters of FY09, had $12M of rate cases pending in NY, IN, MO, VA and NC at the end of 3Q09, and was planning to file for another $57M of rate case in 4Q09. Following the typical pattern, we expect 65-70% of the filing amount to be granted within 9-12 months of the filing date subsequently impacting late 2010/2011 earnings. As detailed in the tables below, we expect $44.8M and $68M of incremental revenues in FY10 and FY11, respectively from rate increases, $5.2 annually from acquisitions, and $16.8M in FY10 from increased consumption increase to offset the approximately $17M of consumption-related revenue decline in FY09. **These increases should allow revenue growth to increase approximately 10% annually in both years. We note that WTR has grown its top line at a CAGR of 7.2% over the last five years.** However, we believe that increased capex and rate catch-up in southern states, where WTR is expected to go in for a second round of increases in 2010-11, should allow the company to exceed this growth over the next several years.

Rate Increase	Amount ($ mil)	1Q09	2Q09	3Q09	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E
		Incremental Revenue							
Approved									
2008	64.7			15.3					
FL & NC	13.2	1.7	3.3	3.3	3.3	1.7			
Other Received in 1Q09	9.4	1.2	2.3	2.3	2.3	1.2			
Received in 2Q09	4.6		0.6	1.2	1.2	1.2	0.6		
Received in 3Q09	2.1			0.3	0.5	0.5	0.5	0.3	
Pending									
NY	4.7					0.3	0.8	0.8	0.8
VA	3.2						0.5	0.5	0.5
Other Pending	4.1					0.3	0.7	0.7	0.7
To be filed									
PA	35.0						5.8	5.8	5.8
NJ	5.0						0.8	0.8	0.8
Other 2009 filing	17.0							2.8	2.8
Surcharges				0.3	0.8	1.3	1.8	2.0	2.0
TOTAL (Quaterly)		**14.0**	**19.5**	**17.1**	**8.1**	**6.3**	**11.4**	**13.6**	**13.4**
TOTAL (Annual)			$58.7M				$44.8M		

Source: Company Information and LBR estimates

FY ends December 31 ($mil)	FY04A	FY05A	FY06A	FY07A	FY08A	FY09E	FY10E	FY11E
Revenue Δ	74.8	54.7	36.7	69.0	24.5	44.9	66.8	73.2
Acquisitions-Regulated	54.9	13.7	8.7	33.3	5.9	5.2	5.2	5.2
Rate Increase	15.8	26.8	32.0	25.7	28.9	58.7	44.8	68.0
% of Previous Year Revenue		6.1%	6.4%	4.8%	4.8%	9.4%	6.7%	9.2%
Δ Non-Regulated Segment	2.1	1.3	3.9	5.6	(0.9)	(0.3)		
Other (Mostly change in consumption)	2.0	13.0	(7.8)	4.4	(9.3)	(18.7)	16.8	-

Source: Company Information and LBR estimates

American States Water (AWR, NEUTRAL)

The California Public Utilities Commission (CPUC) is still processing the AWR's $51.5M General Rate Case (GRC) for Regions II and III and the general office (GO) and is expected to issue a final decision soon. CPUC did issue an unfavorable proposed decision for this case in November 2009, and the company is working hard to get many of the issues turned around.

On October 15, 2009, the CPUC issued a final decision approving $6.4M of rate increases over a four-year period for the Bear Valley Electric Service (BVES) division. This rate case, which was filed in June 2008, was the first full rate increase for BVES since 1996. Rates will increase $4.8M in 2009, $1.2M in 2010, $209K in 2011, and $168K in 2012, and will be effective on November 1st of each year. Following the usual pattern, the 10.5% ROE allowed for the rate increase was higher than the 10.2% allowed for the water service. These rates can also be updated in 2010 for corporate headquarters' costs based on the CPUC's decision on the water GRC by the end of 2009. The Electric segment has been underperforming the Water segment, but we expect improved profitability going forward as a result of these rate increases.

On October 8, 2009, the Arizona Corporation Commission (ACC) approved a $1.7M rate increase for the company's water service in the state, which was a 23% increase over the current rate at the time and was effective from October 15, 2009.

We expect the Water segment revenue to increase 11.9% in FY10 from the $33.3M in rate increases detailed in the table below. For FY11, we have assumed lower revenue growth of 9% since we do not yet know the size of the rate case for Region I, which will be effective from January 1, 2011. For the Electric segment, we expect revenue increase of $4.2M, or 14.7%, in FY10 from rate increases detailed below. We are assuming modest 2.4% growth in FY11, more in line with historical growth without rate increases.

RATE INCREASES IMPACTING 2009 & 2010 (in $mil.)									
Rate Increase/ Surcharge	Effective Date/ Expected	Region	Filing Amount	Approved/ Expected	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E
Water - Approved									
Step Rate	1/1/09	I		0.3	0.1				
Step Rate	1/1/09	II		5.1	1.3				
Interim	1/1/09	III		4.0	1.0				
10.2% ROE				0.7	0.2	0.2	0.2	0.1	
Chaparral, AZ			2.9	1.7	0.4	0.4	0.4	0.4	
Water - Pending									
GRC	1/1/10	I, III & GO	42.2	31.7		7.9	7.9	7.9	7.9
Total Water					**2.9**	**8.5**	**8.5**	**8.4**	**7.9**
Electric									
	1/7/09		6.8	4.8	0.8	1.2	1.2	1.2	0.4
	1/1/2010 (3 yrs)		3.7	1.2					0.2
Total Electric					**0.8**	**1.2**	**1.2**	**1.2**	**0.6**

Source: Company Information and LBR Estimates

INVESTMENT THESIS

AWK

We rate American Water Works Company, Inc. (AWK) with a BUY with a $24 target price, as we see AWK as offering an attractive risk/reward with positive catalysts relative to the peer group. We believe AWK shares were trading at a discount partially due to the "RWE overhang." As this overhang is now removed, AWK's discounted valuation relative to the industry average should ease. However, our target price still incorporates a 16% discount to the peer group average. The shares are trading at 15.3x our FY10E EPS, relative to a peer group average of 19.0x. As the largest and most geographically diversified water utility in the U.S., AWK should benefit by investing to replace and expand the aging water infrastructure in the country. As such, the company is planning to spend $4.0-4.5B over the next five years, which should drive earnings growth over that time period.

CWT

We rate California Water Service Group (CWT) as a BUY with a $45 target price, which represents 20.5x our FY10E EPS of $2.20, in line with the company's historical average. We like CWT's position in the regulatory favorable California market. Furthermore, CWT's $120M in FY09E and $125M in FY10E capex could potentially drive meaningful EPS growth in the next two to three years. On valuation, CWT shares are trading at 16.2x our FY10E EPS of $2.20, which we believe to be conservative when compared to the industry average of 19.0x and the company's historical average of 20.5x. Additionally, while CWT has historically seen higher earnings volatility from variation in water consumption, regulatory changes in California (WRAM and MBCA implementation) have reduced earnings volatility and provide better visibility. In summation, rate relief and improved ROE (we are modeling 10.9%) in FY10E, greater than the company's 8.9% five-year average, provide positive potential catalysts going forward.

WTR

We rate Aqua America, Inc. (WTR) as a NEUTRAL as, while the shares are trading at an 18% discount to its historical forward P/E of 23x, we see the potential upside relative to our preferred names of CWT and AWK as lower when looking at 2010-2011 earnings power. Overall, we like WTR's position as one of the leading publicly traded water utilities, serving approximately three million people in 13 states. The water utilities industry is highly regulated, but also fragmented, which presents opportunities for acquisitive growth, especially as cash strapped municipalities and smaller private participants look to raise cash to weather the current economic downturn by potentially selling off water systems. More important, we expect 2009 and 2010 to be catch-up years for rate increases: $64.7M and $29.3M in rate increases were approved in 2008 and 1-3Q09, respectively, and $69M in increases are either pending or will be filed soon. Additionally, WTR has surcharges in six of its 14 states of operations, which allows the company to start earning a return on its investment between rate increases. These factors, coupled with lower equity dilution from increased operating cash flow generation, should accelerate the pace of EPS growth over the next three years. We see WTR's estimated earnings growth of 12.1% from FY09E to FY11E outpacing the flat growth from FY05 to FY08.

AWR

We rate American States Water Company (AWR) a NEUTRAL. At 17.8x our FY10E EPS of $1.97, AWR shares are trading at a discount both to its last 10-year average forward P/E of 20.6x as well as to the current peer group average of 19.0x. However, given AWR's valuation relative to our preferred names in the space – AWK and CWT – and the company's earning potential over the next two to three years, we do not see much upside potential at this time from current levels. Our EPS estimates include an average ROE of 10% from FY09E to FY11E vs. the company's last five-year average of 8.7%. This is driven by increased capex, which the company expects to be $85-90M in FY10 vs. $75M in FY09. Since capex has grown at a CAGR of 12% from 2003-2008, AWR should see rate relief leading to 7% EPS growth in FY10E and potentially 10% in FY11E. In the long term, we like AWR, currently the fourth largest publicly traded domestic water utility, as the WRAM/MBCA implementation in California has removed the quarterly earnings volatility caused by the changes in water consumption. We note that seasonal variation will still exist. These mechanisms have somewhat reduced the single-state operational risk that AWK faced previously. However, we believe benefits from the improved regulatory environment and earnings upside from recently approved rate cases are already mostly priced into the shares.

VALUATION

AWK

AWK shares closed yesterday at $23.00, which is 17.9x our FY09E EPS of $1.28 and 15.3x our FY10E EPS of $1.50. The shares are trading at a discount to the peer group average of 19.0x FY10 EPS. The shares are trading at 1.5x tangible book value ($15.67/share) compared to a peer group that trades over 1.8x, on average. Our target price of $24 is based on 16x our FY10E EPS, a valuation that remains at a discount to the peer group. However, we see multiple expansion from current levels as justified given AWK being viewed as the largest and most diversified publicly traded water utility in the U.S. and with the potential from earnings growth as the company catches up to insufficient rate increases during the past five-to-six years.

CWT

CWT shares closed yesterday at $35.62, which is 17.8x our FY09E EPS of $2.00 and 16.2x our FY10E EPS of $2.20. The shares are trading at a discount to the company's historical normalized 20.5x average and normalized range of 17-27x forward P/E. Compared to CWT's water utility peers, the company trades at a discount, although this has narrowed as more predictable earnings streams from the implementation of WRAM and MCBA has removed some the unpredictability in earnings associated with the company's extensive geographic presence in California.

WTR

WTR shares closed yesterday at $17.56 which is 22.6x our FY09E EPS of $0.78 and 18.9x our FY10E EPS of $0.93. The shares are trading at a discount to the company's historical 23x average and normalized range of 20-30x forward P/E.

AWR

At 17.8x our FY10E EPS of $1.97, AWR shares are trading at a discount to its last ten-year average forward P/E of 20.6x average as well as to the current peer group average of 19.0x. Should multiples expand, a fair value of $38/share does not imply the same amount of potential upside as do our preferred names in the space – AWK and CWT. AWR shares closed Wednesday at $35.19, which is 19.1x our FY09E EPS of $1.85 and 17.8x our FY10E EPS of $1.97. The shares are trading at a discount to the company's historical 20.6x average and a normalized range of 18-28x forward P/E.

RISKS

AWK

The potential downside risks to our investment thesis include, but are not limited to: 1) delays in rate case processing or lower rate increases by the regulators than our expectations, 2) 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, 4) a large acquisition at an excessive valuation (significantly above the rate base), and 5) a large goodwill impairment which could lead to a breach of debt covenants or regulatory requirements.

CWT

Potential downside risks to our investment thesis include, but are not limited to: 1) lower rate increase approvals by the California Public Utility Commission (CPUC) than our expectation, 2) near-term run up in raw material costs, and 3) large acquisition(s) at excessive valuation(s) (significantly above the rate base).

WTR

Potential downside risks to our investment thesis 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 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.

AWR

The potential downside risks to our investment thesis include, but are not limited to: 1) lower rate increase approvals by the California Public Utility Commission (CPUC) than our expectation, 2) increases in raw material costs, and 3) an acquisition of a large water system by the local government through eminent domain.

The potential upside risks to our investment thesis include, but are not limited to: 1) favorable rate case approvals, and 2) the commencement of the large "special" construction project at Ft. Bragg, North Carolina, or any other base.

American Water Works— Quarterly Income Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E
Regulated Segment	419.3	508.6	571.9	487.8	449.9	527.1	603.7	502.1	497.4	554.9	621.0	528.8	528.6	600.7	680.2	580.6
% Increase			7.3%	11.2%	7.3%	3.6%	5.6%	2.9%	10.6%	5.3%	2.9%	5.3%	6.3%	8.3%	9.5%	9.8%
Non-Regulated Revenue	53.3	55.5	66.4	67.5	61.0	67.0	73.9	70.3	57.5	64.2	65.2	67.3	70.0	76.7	77.7	79.8
% Increase			0.4%	27.7%	14.4%	20.8%	9.4%	4.1%	-5.7%	-4.2%	-11.7%	-4.3%	21.7%	19.5%	19.2%	18.6%
Other	(4.0)	(5.4)	(5.1)	(1.5)	(4.1)	(4.7)	(5.4)	(3.9)	(4.7)	(6.3)	(6.3)	(5.3)	(5.3)	(6.0)	(6.8)	(5.8)
% Regulated Rev	-1.0%	-1.1%	-0.9%	-0.3%	-0.9%	-0.9%	-0.9%	-0.8%	-1.0%	-1.1%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%
Operating revenues	**468.5**	**558.7**	**633.1**	**553.8**	**506.8**	**589.4**	**672.2**	**568.6**	**550.2**	**612.7**	**680.0**	**590.8**	**593.3**	**671.4**	**751.1**	**654.6**
Operation and maintenance	282.6	299.4	328.3	336.2	311.3	330.6	342.2	319.8	314.4	330.6	340.9	330.9	330.2	353.2	365.3	358.7
Depreciation and amortization	64.6	68.1	69.7	64.9	63.9	67.3	68.4	71.6	68.8	73.2	74.9	73.2	75.3	77.3	79.4	81.5
General taxes	47.9	45.9	47.1	42.3	52.1	49.6	49.4	48.0	52.5	51.7	50.6	49.3	54.5	52.0	52.0	50.6
Loss (gain) on sale of assets	0.1	(6.2)	(0.7)	(0.5)	(0.1)	(0.8)	0.5	(0.0)	(0.2)	0.0	(0.8)	(0.3)	(0.3)	(0.3)	(0.3)	(0.3)
Impairment charges			243.3	266.0	750.0				450.0							
EBIT	**73.3**	**151.5**	**(54.6)**	**(155.1)**	**(670.4)**	**142.7**	**211.8**	**129.1**	**(335.4)**	**157.2**	**214.4**	**137.7**	**133.7**	**189.2**	**254.8**	**164.1**
Operating Margin (excluding impairment)	*15.6%*	*27.1%*	*29.8%*	*20.0%*	*15.7%*	*24.2%*	*31.5%*	*22.7%*	*20.8%*	*25.7%*	*31.5%*	*23.3%*	*22.5%*	*28.2%*	*33.9%*	*25.1%*
Interest	72.2	70.8	68.739	71.5	70.0	70.1	72.7	72.4	72.0	73.7	74.1	73.6	74.7	75.8	76.9	78.0
Other income, net	(3.0)	(1.9)	(2.9)	(4.6)	(3.7)	(3.1)	(6.7)	(8.0)	(4.8)	(2.6)	(1.5)	(4.2)	(3.3)	(2.9)	(3.0)	(3.4)
Total other income (deductions)	**69.2**	**68.9**	**65.8**	**66.8**	**66.2**	**67.0**	**66.0**	**64.5**	**67.1**	**71.1**	**72.6**	**69.4**	**71.4**	**72.9**	**73.9**	**74.6**
EBT	**4.2**	**82.6**	**(120.5)**	**(221.9)**	**(736.6)**	**75.7**	**145.8**	**64.6**	**(402.5)**	**86.1**	**141.8**	**68.4**	**62.3**	**116.4**	**180.9**	**89.5**
Provision for income taxes	1.7	32.648	39.7	12.7	(4.1)	30.2	57.5	28.2	10.6	34.1	50.2	24.2	24.6	46.0	71.4	35.3
Implied Tax Rate (excl. goodwill impairment)	42%	40%	32%	29%	-31%	40%	39%	44%	22%	39.6%	35.4%	35.4%	39.5%	39.5%	39.5%	39.5%
Income (loss) from continuing operations	**2.4**	**50.0**	**(160.2)**	**(234.6)**	**(732.5)**	**45.5**	**88.2**	**36.4**	**(413.1)**	**52.0**	**91.6**	**44.2**	**37.7**	**70.4**	**109.4**	**54.1**
Loss (income) from discontinued operations, net of tax	(0.26)	0.81	0.00	0.00												
Net Income (loss)	**2.7**	**49.2**	**(160.2)**	**(234.6)**	**(732.5)**	**45.5**	**88.2**	**36.4**	**(413.1)**	**52.0**	**91.6**	**44.2**	**37.7**	**70.4**	**109.4**	**54.1**
Diluted EPS from continuing operations	0.02	0.31	(1.00)	(1.47)	(4.58)	0.28	0.55	0.23	(2.58)	0.32	0.52	0.25	0.21	0.39	0.60	0.29
EPS excl. impairment & one-time expenses	**0.02**	**0.31**	**0.52**	**0.17**	**0.11**	**0.28**	**0.55**	**0.23**	**0.19**	**0.32**	**0.52**	**0.25**	**0.21**	**0.39**	**0.60**	**0.29**
Diluted Average Shares	160.0	160.0	160.0	160.0	160.0	159.9	160.0	159.9	159.9	164.8	174.7	174.7	176.3	179.4	182.5	185.6
Financial Summary																
Total Revenue growth			6.8%	12.4%	8.2%	5.5%	6.2%	2.7%	8.6%	4.0%	1.2%	3.9%	7.8%	9.6%	10.5%	10.8%
Non-Regulated Revenue growth			0.4%	27.7%	14.4%	20.8%	11.3%	4.1%	-5.2%	-4.5%	-10.3%	5.0%	21.7%	19.5%	19.2%	18.6%
O&M/Revenue	60.3%	53.6%	51.9%	60.7%	61.4%	56.1%	50.9%	56.2%	57.1%	54.0%	50.1%	56.0%	55.6%	52.6%	48.6%	54.8%
General Taxes/ Regulated Revenue	11.4%	9.0%	8.2%	8.7%	11.6%	9.4%	8.2%	9.6%	10.6%	9.3%	8.2%	8.9%	10.3%	8.7%	7.6%	8.7%
Adj. EBITDA	137.9	219.6	258.4	175.8	143.6	210.0	280.2	200.7	183.5	230.4	289.3	210.9	209.0	266.5	334.2	245.5
EPS growth, excluding goodwill impairment charge					620.8%	-8.9%	6.0%	34.0%	73.6%	10.9%	-4.8%	11.1%	12.6%	24.4%	14.3%	15.3%

Source: Company reports, Longbow estimates

American Water Works— Annual Income Statement

Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414

(dollars in millions, except per share data)

FY ends December 31	FY04A	FY05A	2006A	FY07A	FY08A	FY09E	FY10E	FY11E
Regulated Segment	1748.0	1836.1	1854.6	1987.6	2082.7	2202.1	2390.1	2560.1
% Increase		5.0%	1.0%	7.2%	4.8%	5.7%	8.5%	7.1%
Non-Regulated Revenue	290.0	310.8	248.5	242.7	272.2	254.3	304.3	319.5
% Increase		7.2%	-20.0%	-2.3%	12.2%	-6.6%	19.7%	5.0%
Other	-20.17	(10.1)	(10.0)	(16.0)	(18.0)	(22.6)	(23.9)	(25.6)
% Regulated Rev	-1.2%	-0.6%	-0.5%	-0.8%	-0.9%	-1.0%	-1.0%	-1.0%
Operating revenues	**2,017.9**	**2,136.7**	**2,093.1**	**2,214.2**	**2,336.9**	**2,433.7**	**2,670.5**	**2,854.0**
Production costs	248.5	262.6	264.4	278.1	288.6	294.5	312.4	331.1
Employee-related costs	407.7	408.8	446.2	463.4	505.6	520.8	560.8	596.5
Operating supplies and services	289.3	338.1	268.2	293.5	283.2	292.0	312.4	331.1
Maintenance materials and services	90.6	97.9	96.5	128.0	136.3	129.0	128.2	134.1
Customer billing and accounting	42.5	44.4	55.6	38.3	44.0	41.4	42.7	42.8
Other	43.4	49.8	43.6	45.3	46.1	46.2	50.7	51.4
Operation and maintenance	1122.0	1201.6	1174.5	1246.5	1303.8	1323.9	1407.4	1486.9
Depreciation and amortization	225.3	261.4	259.2	267.3	271.3	290.1	313.5	324.9
General taxes	170.2	183.3	185.1	183.3	199.1	204.1	209.1	214.1
Loss (gain) on sale of assets	(8.6)	(6.5)	0.1	(7.3)	(0.4)	(1.3)	(1.2)	(1.2)
Impairment charges	78.7	385.4	221.7	509.3	750.0	450.0	0.0	0.0
EBIT	**430.4**	**111.6**	**252.5**	**15.1**	**(186.9)**	**166.8**	**741.7**	**829.2**
Operating Margin (excluding impairment)	*25.2%*	*23.3%*	*22.7%*	*23.7%*	*24.1%*	*25.3%*	*27.8%*	*29.1%*
Interest	315.9	345.3	366.0	283.2	285.2	293.4	305.3	324.0
Other income, net	(11.0)	(9.5)	(4.5)	(12.5)	(21.5)	(13.2)	(12.6)	(12.6)
Total other income (deductions)	**305.0**	**335.7**	**361.5**	**270.6**	**263.7**	**280.2**	**292.7**	**311.4**
EBT	**125.4**	**(224.2)**	**(108.9)**	**(255.5)**	**(450.6)**	**(113.40)**	**449.0**	**517.8**
Provision for income taxes	66.3	51.0	46.9	86.8	111.8	119.1	177.4	204.5
Implied Tax Rate (excl. goodwill impairment)	32.5%	31.6%	41.6%	34.2%	37.3%	35.4%	39.5%	39.5%
Income (loss) from continuing operations	**59.1**	**(275.1)**	**(155.9)**	**(342.3)**	**(562.4)**	**(232.5)**	**271.6**	**313.3**
Loss (income) from discontinued operations, net of tax	124.0	49.9	6.4	0.6				
Net Income (loss)	**(64.9)**	**(325.0)**	**(162.2)**	**(342.8)**	**(562.4)**	**(232.5)**	**271.6**	**313.3**
Diluted EPS from continuing operations	0.37	(1.72)	(0.97)	(2.14)	(3.52)	(1.38)	1.50	1.62
EPS excl. impairment & one-time expenses	**0.86**	**0.69**	**0.41**	**1.04**	**1.17**	**1.28**	**1.50**	**1.62**
Diluted Average Shares	160.0	160.0	160.0	160.0	160.0	168.5	180.9	193.5
Financial Summary								
Total Revenue growth		5.9%	-2.0%	5.8%	5.5%	4.1%	9.7%	6.9%
Non-Regulated Revenue growth			-20.0%	-2.3%	12.2%	-6.6%	19.7%	5.0%
O&M/Revenue	55.6%	56.2%	56.1%	56.3%	55.8%	54.4%	52.7%	52.1%
Depreciation and amortization/ Net Fixed Asset				3.1%	2.9%	2.9%	2.8%	2.7%
Depreciation Growth		16.0%	-0.8%	3.1%	1.5%	7.0%	8.0%	3.7%
General Taxes/ Regulated Revenue	9.7%	10.0%	10.0%	9.2%	9.6%	9.3%	8.8%	8.4%
Adj. EBITDA	734.3	758.4	733.4	791.8	834.4	906.9	1,055.2	1,154.1
Interest Expense/ Average Net Debt			8.9%	6.2%	5.6%	5.5%	5.6%	5.9%
Interest Expense/Revenue	15.7%	16.2%	17.5%	12.8%	12.2%	12.1%	11.4%	11.4%
Net Income Growth (excl. goodwill impairment)		338.6%	-1.6%	180.1%	12.6%	16.0%	24.9%	15.3%
EPS growth, (excl. goodwill impairment)			-40.3%	153.8%	12.3%	9.4%	17.0%	7.8%
ROE (excl. goodwill & goodwill impairment)			2.3%	7.0%	8.3%	8.4%	9.2%	9.2%

Source: Company reports, Longbow estimates

American States Water — Quarterly Earnings Statement

Garik Shmois/ Vishal Khetriwal, CFA
Longbow Research
216-525-8414

(dollars in millions, except per share data)

FY ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E
Water	50.3	60.8	65.4	61.3	52.1	65.4	69.4	61.1	70.0	65.3	82.7	86.7	78.0
Electric	8.9	6.3	6.3	7.2	8.8	6.2	6.7	6.7	7.5	9.8	7.1	7.8	8.1
Contracted Services	13.1	12.2	4.1	5.6	8.1	8.7	9.2	16.4	14.0	12.0	12.0	12.0	12.0
Total Revenue	**72.3**	**79.2**	**75.8**	**74.0**	**68.9**	**80.3**	**85.3**	**84.2**	**91.5**	**87.1**	**101.8**	**106.5**	**98.0**
Expenses													
Supply Costs	16.8	19.0	22.6	19.8	16.1	20.5	24.2	20.0	22.9	22.7	26.2	31.3	25.2
Gen. & Admin. expenses	13.0	13.7	11.8	14.2	14.8	14.9	16.3	16.6	17.2	17.6	18.0	18.4	18.8
Other O&M	9.6	10.9	10.9	11.8	11.8	11.8	11.4	11.4	11.6	12.1	11.8	12.1	12.3
ASUS Construction Expenses	9.1	8.3	1.9	2.9	3.9	4.4	5.1	10.4	9.1	7.8	7.8	7.8	7.8
Gain on sale of water rights/property	(0.4)	(0.2)	0.0	0.0									
Unrealized loss(gain) on purch pwr contracts	(2.7)	0.2	0.9	(0.5)	(2.8)	(1.7)	3.7	(0.8)					
Total Operation & Maintenance	**45.4**	**51.9**	**48.1**	**48.1**	**43.8**	**50.1**	**60.8**	**57.7**	**60.8**	**60.2**	**63.8**	**69.6**	**64.1**
Depreciation & Amortization	7.1	7.1	7.4	7.3	7.8	7.8	7.9	8.1	8.7	8.7	8.8	9.0	9.1
General Taxes	2.9	2.8	2.8	2.7	2.9	2.8	3.5	3.1	3.6	3.7	3.0	3.9	3.9
Total Expenses	**55.4**	**61.8**	**58.3**	**58.1**	**54.5**	**60.7**	**72.1**	**68.9**	**73.1**	**72.5**	**75.6**	**82.4**	**77.0**
Income from Operations	**16.9**	**17.5**	**17.5**	**15.9**	**14.5**	**19.6**	**13.1**	**15.3**	**18.4**	**14.6**	**26.2**	**24.0**	**21.0**
Operating Margin	23.3%	22.0%	23.1%	21.5%	21.0%	24.4%	15.4%	18.2%	20.1%	16.8%	-25.7%	22.6%	21.4%
Other Inc. (loss)	0.1	(0.1)	0.1	0.1	0.1	0.0	(0.0)	(7.7)					
EBIT	**16.9**	**17.4**	**17.6**	**16.0**	**14.6**	**19.6**	**13.1**	**7.6**	**18.4**	**14.6**	**26.2**	**24.0**	**21.0**
EBIT (%)	23.4%	21.9%	23.2%	21.6%	21.1%	24.4%	15.4%	9.0%	20.1%	16.8%	25.7%	22.6%	21.4%
Interest Expense	4.9	5.0	4.8	4.5	5.0	4.5	5.1	4.8	5.7	5.8	5.8	5.9	5.9
Income Before Taxes	**12.0**	**12.4**	**12.9**	**11.4**	**9.6**	**15.1**	**8.0**	**2.8**	**12.7**	**8.9**	**20.3**	**18.1**	**15.1**
Provision for Income Taxes	5.0	5.2	5.2	5.3	4.3	5.8	3.4	(0.1)	5.2	3.6	8.3	7.4	6.2
Implied Tax Rate	41.8%	42.0%	40.7%	46.6%	44.5%	38.4%	42.9%	-3.2%	40.8%	40.8%	40.8%	40.8%	40.8%
Net Income	7.0	7.2	7.6	6.1	5.3	9.278	4.6	2.9	7.5	5.2	12.1	10.7	9.0
EPS (fully diluted)	0.40	0.42	0.44	0.35	0.30	0.53	0.26	0.16	0.40	0.28	0.64	0.57	0.48
EPS (fully diluted, ex one-time items)	**0.31**	**0.43**	**0.47**	**0.35**	**0.30**	**0.47**	**0.39**	**0.40**	**0.40**	**0.28**	**0.64**	**0.57**	**0.48**
Weighted Avg. Shares	17.1	17.1	17.2	17.3	17.4	17.3	17.3	17.4	18.7	18.7	18.7	18.7	18.8
Financial Summary (values in %)													
Water revenue growth	4.5%	14.5%	0.7%	15.6%	3.5%	7.5%	6.0%	-0.3%	14.6%	15.0%	11.5%	10.7%	11.3%
Electric revenue growth	6.3%	-11.0%	-2.4%	-3.9%	-0.7%	-0.8%	7.2%	-6.9%	12.0%	13.9%	20.4%	18.3%	8.0%
Contracted Services growth	217%	512%	75.9%	-52.3%	-38.4%	-28.2%	123%	195%	-14.7%	-15.4%	-11.2%	-27.9%	-14.3%
Total Revenue growth	19.2%	27.5%	2.8%	2.6%	-4.6%	1.3%	12.4%	13.8%	8.7%	9.4%	8.8%	4.9%	7.1%
Operations & Maintenance/Revenue	62.8%	65.4%	63.4%	65.0%	63.5%	62.4%	71.3%	68.5%	66.4%	69.1%	62.7%	65.4%	65.3%
Supply Costs/Revenue (excl. Military Base)	28.4%	28.4%	31.4%	28.9%	26.5%	28.7%	31.8%	29.5%	29.5%	30.2%	29.2%	33.2%	29.3%
Gen. & Admin./Revenue	18.0%	17.2%	15.5%	19.2%	21.5%	18.6%	19.1%	19.8%	18.8% #	20.2%	17.7%	17.3%	19.2%
Other O&M/Revenue	13.2%	13.8%	14.4%	15.9%	17.1%	14.7%	13.4%	13.6%	12.7%	13.9%	11.6%	11.3%	12.5%
General Taxes/Revenue	4.1%	3.6%	3.7%	3.6%	4.2%	3.5%	4.1%	3.7%	4.0%	4.2%	2.9%	3.6%	3.9%
EPS Growth	14.7%	16.7%	38.3%	17.6%	-25.0%	26.2%	-40.6%	-53.4%	146%	-0.8%	0.7%	10.0%	18.2%

Source: Company reports, Longbow estimates

LONGBOW Research

January 7, 2010

American States Water — Annual Earnings Statement

Garik Shmois/ Vishal Khetriwal, CFA
Longbow Research
216-525-8414

(dollars in millions, except per share data)

FY ends December 31	2004A	2005A	2006A	2007	2008	2009E	2010E	2011E
Water	200.6	205.5	219.2	237.9	247.9	279.3	312.6	340.6
Electric	25.6	27.2	29.3	28.6	28.4	28.6	32.8	33.6
Contracted Services	1.8	3.5	20.1	34.9	42.4	58.3	48.0	48.0
Total Revenue	**228.0**	**236.2**	**268.6**	**301.4**	**318.7**	**366.2**	**393.4**	**422.2**
Expenses								
Supply Costs	81.1	71.9	76.2	78.2	80.9	94.6	105.5	113.5
Gen. & Admin. expenses	41.8	44.3	47.1	52.6	62.7	66.6	72.8	79.2
Other O&M	31.6	32.0	36.4	43.2	46.4	45.6	48.3	51.0
ASUS Construction Expenses			9.0	22.1	23.9	34.6	31.2	31.2
Gain on sale of water rights/property	(5.7)	0.0	(0.3)	(0.6)	0.0	0.7	0.0	0.0
Unrealized loss on purch power contracts	0.1	(5.4)	7.1	(2.1)	(1.6)			
Total Operation & Maintenance	**148.9**	**142.8**	**175.6**	**193.4**	**212.3**	**242.2**	**257.7**	**274.9**
Depreciation & Amortization	20.8	21.9	26.3	28.9	31.6	33.8	35.5	37.1
General Taxes	8.8	9.3	10.2	11.3	12.3	13.3	14.3	15.3
Total Expenses	**178.5**	**174.0**	**212.0**	**233.6**	**256.2**	**289.4**	**307.6**	**327.3**
Income from Operations	**49.5**	**62.3**	**56.6**	**67.7**	**62.5**	**76.8**	**85.8**	**94.8**
Operating Margin	21.7%	26.4%	21.1%	22.5%	19.6%	21.0%	21.8%	22%
Other Inc. (loss)	0.3	(0.0)	0.5	0.30	(7.6)	0.1	0.0	0.0
EBIT	**49.8**	**62.2**	**57.1**	**68.0**	**54.9**	**76.9**	**85.8**	**94.8**
EBIT (%)	0.2	0.3	0.2	0.2	0.2	0.2	0.2	0.2
Interest Expense	17.9	13.6	18.3	19.21	19.5	21.8	23.4	25.6
Income Before Taxes	**31.9**	**48.6**	**38.8**	**48.8**	**35.4**	**55.1**	**62.4**	**69.3**
Provision for Income Taxes	13.4	21.9	15.7	20.8	13.4	21.4	25.4	28.2
Implied Tax Rate	41.9%	45.0%	40.5%	42.6%	37.8%	38.9%	40.8%	40.8%
Net Income	18.5	26.7	23.1	28.0	22.0	33.7	37.0	41.0
EPS (fully diluted)	1.19	1.59	1.33	1.61	1.26	1.85	1.97	2.18
EPS (fully diluted, ex.one-time items)	**1.06**	**1.16**	**1.44**	**1.56**	**1.56**	**1.85**	**1.97**	**2.18**
Weighted Avg. Shares	15.6	16.8	17.1	17.2	17.4	18.2	18.7	18.8
Financial Summary (values in %)								
Water revenue growth	7.2%	2.4%	6.7%	8.5%	4.2%	12.6%	11.9%	9.0%
Electric revenue growth	4.5%	6.4%	7.5%	-2.4%	-0.5%	0.5%	14.7%	2.4%
Other	75.1%	96.1%	477.9%	73.5%	21.3%	37.7%	-17.7%	0.0%
Total Revenue growth	7.2%	3.6%	13.7%	12.2%	5.8%	14.9%	7.4%	7.3%
Operations & Maintenance/Revenue	65.3%	60.4%	65.4%	64.2%	66.6%	66.2%	65.5%	65.1%
Supply Costs/Revenue (excl. Military Base)	35.8%	30.9%	30.7%	29.4%	29.3%	30.7%	30.5%	30.3%
Gen. & Admin./Revenue	18.3%	18.7%	17.5%	17.5%	19.7%	18.2%	18.5%	18.8%
Other O&M/Revenue	13.8%	13.5%	13.5%	14.3%	14.6%	12.5%	12.3%	12.1%
General Taxes/Revenue	3.9%	4.0%	4.1%	4.2%	4.5%	4.3%	4.1%	4.1%
(Dep + Amort)/Net Fixed Assets	3.3%	3.3%	3.7%	3.9%	4.1%	4.4%	4.1%	4.1%
(Dep + Amort)/Revenue	9.1%	9.3%	9.8%	9.6%	9.9%	9.2%	9.0%	8.8%
Interest Expense/Avg. Net Debt	6.4%	4.8%	6.1%	6.3%	6.0%	7.6%	7.2%	7.4%
Interest Expense/Revenue	7.8%	5.8%	6.8%	6.4%	6.1%	6.0%	5.9%	6.1%
Average ROE	8.0%	10.4%	8.4%	9.6%	7.2%	9.8%	9.9%	10.3%
EPS growth, excluding one-time items	52.0%	9.4%	24.1%	8.3%	0.0%	18.5%	6.8%	10.4%

Source: Company reports, Longbow estimates

California Water Service Group — Quarterly Earnings Statement

Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414

(dollars in millions, except per share data)

FY Ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E
Total Revenue	71.6	95.8	113.9	85.9	72.9	105.6	131.7	100.1	86.6	116.7	139.2	107.5	93.3	121.5	145.1	112.3
Watet Production Costs	25.8	37.3	45.1	30.8	25.4	40.3	46.5	34.4	28.9	41.7	48.9	37.6	30.5	42.7	50.1	38.6
Administrative & General	12.6	14.3	14.7	12.7	13.4	13.8	15.0	17.2	18.9	19.4	19.1	19.4	19.5	19.6	19.8	19.9
Other Operations	11.1	11.0	11.8	12.5	12.1	12.8	12.9	13.4	12.5	14.3	14.6	15.0	13.2	14.7	15.0	15.5
Maintainence	4.5	5.2	4.2	4.4	4.1	4.9	3.8	6.1	4.6	4.3	4.4	4.4	4.4	4.4	4.4	4.4
Operations & Maintenance	54.0	67.8	75.8	60.2	55.0	71.9	78.2	71.1	64.8	79.7	87.0	76.5	67.7	81.4	89.3	78.4
Depreciation and Amortization	8.4	8.4	8.4	8.4	9.2	9.3	9.3	9.6	10.2	10.3	10.3	10.4	10.5	10.6	10.7	10.7
General Taxes	3.4	3.4	3.7	3.1	3.7	3.5	3.9	3.7	4.1	3.9	4.4	3.9	4.4	4.0	4.2	4.0
Total Expenses	65.8	79.6	87.9	71.8	67.9	84.7	91.4	84.3	79.1	93.9	101.7	90.8	82.6	96.1	104.2	93.1
Income from Operations	5.8	16.2	26.0	14.1	5.0	20.9	40.3	15.8	7.5	22.7	37.5	16.7	10.7	25.5	40.9	19.2
Operating Margin	8.1%	16.9%	22.8%	16.5%	6.9%	19.8%	30.6%	15.8%	8.7%	19.5%	27.0%	15.6%	11.5%	20.9%	28.2%	17.1%
Other Income & Expenses (net)	1.3	1.5	1.3	0.4	(0.1)	0.6	(0.7)	(0.6)	0.2	1.4	1.7	0.7	0.7	0.7	0.7	0.7
Gain (loss) on sale of non-util property	0.0	(0.1)	0.0	2.6	0.0	0.0	0.0	0.0	0.6	0.1	(0.7)	0.0	0.0	0.0	0.0	0.0
EBIT	7.1	17.6	27.2	17.1	4.9	21.5	39.6	15.2	8.4	24.2	38.5	17.4	11.3	26.1	41.6	19.9
EBIT (%)	9.9%	18.3%	23.9%	20.0%	6.7%	20.4%	30.0%	15.2%	9.6%	20.7%	27.7%	16.2%	12.2%	21.5%	28.7%	17.7%
Interest Expense	4.4	4.5	4.5	3.7	4.6	4.7	4.2	3.7	4.4	5.3	5.5	5.0	5.5	5.3	5.3	4.9
Income Before Taxes	2.6	13.1	22.8	13.4	0.3	16.8	35.4	11.4	4.0	18.9	33.0	12.4	5.8	20.8	36.3	15.0
Provision for Income Taxes	1.1	5.4	8.9	5.4	0.1	6.7	13.2	4.1	1.6	6.8	13.5	4.8	2.3	8.0	14.0	5.8
Implied Tax Rate	40.3%	40.9%	39.3%	40.0%	40.3%	39.7%	37.3%	36.0%	39.3%	36.0%	40.9%	38.7%	38.5%	38.5%	38.5%	38.5%
Net Income	1.6	7.7	13.8	8.0	0.2	10.1	22.2	7.3	2.4	12.1	19.5	7.6	3.6	12.8	22.3	9.2
Preferred Dividends	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Net Income	1.6	7.7	13.8	8.0	0.2	10.1	22.2	7.3	2.4	12.1	19.5	7.6	3.6	12.8	22.3	9.2
EPS (fully diluted)	0.07	0.37	0.67	0.39	0.01	0.48	1.06	0.35	0.12	0.58	0.94	0.36	0.17	0.59	1.01	0.41
Weighted Avg. Shares	20.7	20.7	20.7	20.7	20.7	20.7	20.7	20.7	20.8	20.8	20.7	20.8	21.2	21.6	22.0	22.4
Financial Summary (values in %)																
Revenue Growth	9.7%	18.1%	5.7%	6.5%	1.9%	10.2%	15.7%	16.6%	18.8%	10.5%	5.7%	7.4%	7.7%	4.2%	4.3%	4.5%
Operations & Maintenance/Revenue	75.4%	70.8%	66.6%	70.1%	75.4%	68.1%	59.4%	71.0%	74.8%	68.3%	62.5%	71.1%	72.6%	67.0%	61.5%	69.8%
Gen. taxes/Revenue	4.8%	3.6%	3.3%	3.6%	5.1%	3.3%	3.0%	3.7%	4.7%	3.4%	3.1%	3.6%	4.7%	3.3%	2.9%	3.5%
EBIT (% of rev.)	9.9%	18.3%	23.9%	20.0%	6.7%	20.4%	30.0%	15.2%	9.6%	20.7%	27.7%	16.2%	12.2%	21.5%	28.7%	17.7%
EBIT/Interest expense	1.6	3.9	6.1	4.6	1.1	4.6	9.5	4.1	1.9	4.5	7.0	3.5	2.1	4.9	7.8	4.1
EPS growth	75.0%	20.5%	-2.6%	23.6%	-87.2%	28.5%	58.8%	-9.2%	1205.6%	21.3%	-11.4%	3.4%	45.5%	1.8%	8.0%	12.8%

Source: Company reports, Longbow estimates

LONGBOW Research

January 7, 2010

California Water Service Group — Annual Earnings Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY Ends December 31	FY04	FY05	FY06	FY07	FY08	FY09E	FY10E	FY11E
Total Revenue	**315.6**	**320.7**	**334.7**	**367.1**	**410.3**	**449.9**	**472.2**	**529.0**
Watet Production Costs	119.1	115.7	124.3	138.9	146.6	157.1	162.0	181.4
Administrative & General	47.1	48.8	52.8	54.3	59.4	76.7	78.8	87.5
Other Operations	39.9	40.0	42.9	46.3	51.2	56.5	58.4	65.5
Maintainence	13.2	15.2	15.6	18.3	19.0	17.8	17.6	18.6
Operations & Maintenance	219.4	219.7	235.6	257.8	276.2	308.0	316.8	353.0
Depreciation and Amortization	26.1	28.7	30.7	33.6	37.3	41.2	42.5	45.0
General Taxes	11.5	12.6	12.9	13.7	14.8	16.2	16.6	18.7
Total Expenses	**257.0**	**261.0**	**279.1**	**305.0**	**328.3**	**365.4**	**375.9**	**416.7**
Income from Operations	**58.6**	**59.7**	**55.6**	**62.1**	**82.0**	**84.5**	**96.3**	**112.3**
Operating Margin	**18.6%**	**18.6%**	**16.6%**	**16.9%**	**20.0%**	**18.8%**	**20.4%**	**21.2%**
Other Income & Expenses (net)	2.4	3.0	3.4	4.4	(0.9)	4.0	2.6	2.6
Gain (loss) on sale of non-util property	0.0	2.3	0.3	2.5	0.0	(0.0)	0.0	0.0
EBIT	**61.0**	**64.9**	**59.4**	**69.0**	**81.1**	**88.5**	**98.9**	**114.9**
EBIT (%)	**19.3%**	**20.2%**	**17.7%**	**18.8%**	**19.8%**	**19.7%**	**20.9%**	**21.7%**
Interest Expense	17.8	17.7	17.0	17.1	17.2	20.2	21.0	23.5
Income Before Taxes	43.1	47.2	42.4	51.9	63.9	68.3	77.9	91.4
Provision for Income Taxes	**17.1**	**20.0**	**16.8**	**20.7**	**24.1**	**26.7**	**30.0**	**35.2**
Implied Tax Rate	**39.6%**	**42.4%**	**39.7%**	**39.9%**	**37.7%**	**39.1%**	**38.5%**	**38.5%**
Net Income	26.0	27.2	25.6	31.2	39.8	41.6	47.9	56.2
Preferred Dividends	-	-	-	-	-	-	-	-
Net Income	**26.0**	**27.2**	**25.6**	**31.2**	**39.8**	**41.6**	**47.9**	**56.2**
EPS (fully diluted)	**1.46**	**1.47**	**1.34**	**1.50**	**1.90**	**2.00**	**2.20**	**2.48**
Weighted Avg. Shares	17.7	18.4	18.9	20.7	20.7	20.8	21.8	22.7
Financial Summary (values in %)								
Revenue Growth	13.9%	1.6%	4.4%	9.7%	11.8%	9.7%	5.0%	12.0%
Operations & Maintenance/Revenue	69.5%	68.5%	70.4%	70.2%	67.3%	68.5%	67.1%	66.7%
(Dep + Amort)/Net Fixed Assets	3.4%	3.6%	3.6%	3.6%	3.7%	3.7%	3.6%	3.6%
Gen. taxes/Revenue	3.6%	3.9%	3.9%	3.7%	3.6%	3.6%	3.5%	3.5%
EBIT (% of rev.)	19.3%	20.2%	17.7%	18.8%	19.8%	19.7%	20.9%	21.7%
Interest Expense/Net Debt	6.7%	6.4%	6.0%	5.9%	5.5%	5.5%	5.2%	5.6%
EBIT/Interest expense	3.4	3.7	3.5	4.0	4.7	4.4	4.7	4.9
Net Income Growth	34.0%	4.6%	-6.0%	21.8%	27.7%	4.5%	15.2%	17.3%
EPS growth	20.4%	0.7%	-8.8%	11.9%	26.7%	5.4%	9.8%	12.9%
Average ROE	9.7%	9.3%	7.5%	8.1%	10.1%	10.1%	10.9%	11.8%

Source: Company reports, Longbow estimates

LONGBOW Research

January 7, 2010

Aqua America - Annual Income Statement
Garik Shmois/ Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E
Total Operating Revenue	**137.3**	**150.6**	**165.5**	**149.1**	**139.3**	**150.8**	**177.1**	**159.8**	**154.5**	**167.3**	**180.8**	**169.2**	**162.1**	**180.1**	**212.6**	**183.9**
Operation & Maintenance	60.3	63.3	67.1	62.4	64.3	65.1	66.7	65.9	67.0	68.5	68.5	66.2	66.6	69.9	80.4	71.9
Depreciation	20.1	20.5	21.1	21.5	21.5	20.6	22.8	23.9	26.4	25.0	25.4	25.4	25.6	26.2	26.7	27.4
Amortization	1.2	1.2	1.2	1.2	1.2	1.0	1.8	1.5	2.8	3.1	3.0	3.0	3.0	3.0	3.0	3.0
General Taxes	11.9	10.8	10.8	11.8	12.1	10.8	11.2	10.6	11.6	11.9	12.4	11.8	12.2	12.6	12.8	12.9
Recovery of restructuring costs																
Total Expenses	**93.6**	**95.9**	**100.1**	**96.9**	**99.1**	**97.6**	**102.5**	**102.0**	**107.7**	**108.5**	**109.4**	**106.4**	**107.4**	**111.7**	**122.8**	**115.2**
Income from Operations	**43.7**	**54.8**	**65.3**	**52.2**	**40.2**	**53.1**	**74.6**	**57.9**	**46.8**	**58.9**	**71.5**	**62.8**	**54.7**	**68.4**	**89.8**	**68.7**
Operating Margin (%)	**31.9%**	**36.4%**	**39.5%**	**35.0%**	**28.9%**	**35.2%**	**42.1%**	**36.2%**	**30.3%**	**35.2%**	**39.5%**	**37.1%**	**33.8%**	**38.0%**	**42.2%**	**37.4%**
All. for Borrowed Funds Used in Const.	0.7	0.7	0.7	0.8	1.0	1.1	1.0	0.6	0.6	0.6	0.7	0.6	0.6	0.6	0.7	0.6
Gain (loss) on sale of other assets	0.1	0.3	0.3	2.8		0.6	0.5	0.5	0.1	0.1	0.2	0.1	0.1	0.1	0.1	0.1
Other																
EBIT	**44.5**	**55.8**	**66.3**	**55.8**	**41.2**	**54.8**	**76.1**	**59.0**	**47.5**	**59.5**	**72.4**	**63.5**	**55.5**	**69.1**	**90.5**	**69.5**
EBIT (%)	**32.4%**	**37.1%**	**40.0%**	**37.5%**	**29.6%**	**36.3%**	**43.0%**	**36.9%**	**30.8%**	**35.6%**	**40.0%**	**37.5%**	**34.2%**	**38.4%**	**42.6%**	**37.8%**
Interest Expense	16.5	16.4	17.1	16.8	17.1	17.1	17.0	17.4	16.6	16.8	17.3	17.2	17.6	18.0	18.4	18.6
Income Before Taxes	28.0	39.4	49.2	39.0	24.0	37.7	59.1	41.7	30.9	42.7	55.1	46.3	37.9	51.1	72.1	50.9
Provision for Income Taxes	**11.1**	**15.7**	**19.6**	**14.1**	**9.7**	**15.2**	**23.7**	**16.0**	**12.5**	**16.9**	**21.6**	**18.3**	**15.2**	**20.5**	**28.9**	**19.8**
Implied Tax Rate	**39.8%**	**39.8%**	**40.0%**	**36.1%**	**40.4%**	**40.2%**	**40.1%**	**38.4%**	**40.5%**	**39.5%**	**39.3%**	**39.5%**	**40.0%**	**40.0%**	**40.0%**	**39.0%**
Net Income before extraord. Item	**16.9**	**23.7**	**29.5**	**24.9**	**14.3**	**22.6**	**35.4**	**25.7**	**18.4**	**25.9**	**33.5**	**28.0**	**22.7**	**30.7**	**43.3**	**31.0**
Reclassification adj. for gains reported in net income				(1.3)			(0.2)			0.0						
Unrealized gain on securities																
Unrealized holding gain on investments	0.0	0.2	0.9	-	-	0.2	0.0		0.0	0.2	(0.1)					
Minimum pension liability adjustment		-	-													
Comprehensive Income	16.9	23.9	30.4	23.6	14.3	22.7	35.2	25.7	18.4	26.1	33.3	28.0	22.7	30.7	43.3	31.0
Diluted Net Income Per Share	**0.13**	**0.18**	**0.22**	**0.19**	**0.11**	**0.17**	**0.26**	**0.19**	**0.14**	**0.19**	**0.25**	**0.21**	**0.17**	**0.22**	**0.31**	**0.22**
Weighted Avg. Shares	133.2	133.5	133.8	134.0	134.0	134.1	135.3	135.6	135.9	135.9	136.3	136.4	136.8	137.3	137.7	138.2
Financial Summary (values in %)																
Revenue Growth	16.4%	14.3%	12.6%	8.9%	1.4%	0.1%	7.0%	7.2%	10.9%	11.0%	2.1%	5.9%	4.9%	7.6%	17.6%	8.7%
Operations & Maintenance/Revenue	43.9%	42.0%	40.5%	41.9%	46.2%	43.2%	37.7%	41.2%	43.4%	41.0%	37.9%	39.1%	41.1%	38.8%	37.8%	39.1%
EBIT (% of rev.)	32.4%	37.1%	40.0%	37.5%	29.6%	36.3%	43.0%	36.9%	30.8%	35.6%	40.0%	37.5%	34.2%	38.4%	42.6%	37.8%
General taxes as % of revenue	8.7%	7.2%	6.6%	7.9%	8.7%	7.2%	6.3%	6.7%	7.5%	7.0%	107.0%	7.0%	7.5%	7.0%	6.0%	7.0%
EBITDA	65.9	77.5	88.5	78.6	63.8	76.4	100.7	84.4	76.7	87.5	100.8	91.9	84.1	98.3	120.2	99.9
Net Income Growth	1.8%	6.0%	8.0%	-3.2%	-15.0%	-5.0%	19.9%	3.0%	28.3%	14.6%	-5.4%	9.2%	23.8%	18.7%	29.3%	10.8%
EPS Growth	0.0%	4.0%	7.1%	-3.6%	-15.5%	-5.3%	18.6%	1.8%	26.5%	13.0%	-6.1%	8.5%	22.9%	17.6%	28.0%	9.3%

Source: Company reports and Longbow estimates

Aqua America - Annual Income Statement Garik Shmois/ Vishal Khetriwal, CFA Longbow Research 216-525-8414 *(dollars in millions, except per share data)*								
FY ends December 31	**FY04A**	**FY05A**	**FY06A**	**FY07A**	**FY08A**	**FY09E**	**FY10E**	**FY11E**
Total Operating Revenue	**442.0**	**496.8**	**533.5**	**602.5**	**627.0**	**671.9**	**738.7**	**811.9**
Operation & Maintenance	178.3	203.1	219.6	253.1	262.1	270.2	288.8	317.5
Depreciation	54.6	60.7	70.9	83.2	88.8	102.2	105.9	112.8
Amortization	4.3	4.7	4.1	4.8	5.5	11.8	12.0	12.0
General Taxes	27.6	31.7	33.3	45.4	44.7	47.7	50.4	55.4
	-		-					
Total Expenses	**264.8**	**300.3**	**327.9**	**386.5**	**401.2**	**432.0**	**457.1**	**497.7**
Income from Operations	**177.2**	**196.5**	**205.6**	**216.0**	**225.8**	**239.9**	**281.6**	**314.2**
Operating Margin (%)	**40.1%**	**39.6%**	**38.5%**	**35.9%**	**36.0%**	**35.7%**	**38.1%**	**38.7%**
Allow. for Borrowed Funds Used in Const.	2.3	2.4	3.9	3.0	3.7	2.5	2.6	2.6
Gain (loss) on sale of other assets	1.3	1.2	1.2	3.5	1.6	0.5	0.5	0.5
Other	-	-	-	-				
EBIT	**180.8**	**200.1**	**210.7**	**222.5**	**231.1**	**242.9**	**284.7**	**317.2**
EBIT (%)	**40.9%**	**40.3%**	**39.5%**	**36.9%**	**36.9%**	**36.2%**	**38.5%**	**39.1%**
Interest Expense	48.7	52.1	58.4	66.9	68.6	67.9	72.6	81.6
Income Before Taxes	132.1	148.1	152.3	155.5	162.5	175.0	212.1	235.6
Provision for Income Taxes	**52.1**	**56.9**	**60.2**	**60.5**	64.6	69.3	84.3	93.7
Implied Tax Rate	**39.4%**	**38.4%**	**39.6%**	**38.9%**	**39.7%**	**39.6%**	**39.8%**	**39.8%**
Net income	80.0	91.2	92.0	95.0	97.9	105.7	127.7	141.9
Reclassification adj. for gains reported in net income	(0.2)	-	-	(1.3)	(0.2)			
Unrealized gain on securities	0.1	-	-	-				
Unrealized holding gain on investments	-	-	0.2	1.1	0.2	0.1	-	-
Minimum pension liability adjustment	(1.7)	(1.3)	3.1		-	-	-	-
Comprehensive Income	**78.1**	**89.8**	**95.3**	**94.8**	**97.9**	**105.8**	**127.7**	**141.9**
Diluted Net Income Per Share	**0.64**	**0.71**	**0.70**	**0.71**	**0.73**	**0.78**	**0.93**	**1.02**
Weighted Avg. Shares	125.7	129.2	131.8	133.6	134.7	136.1	137.5	138.8
Financial Summary (values in %)								
Revenue Growth	20.4%	12.4%	7.4%	12.9%	4.1%	7.2%	9.9%	9.9%
Operations & Maintenance/Revenue	40.3%	40.9%	41.2%	42.0%	41.8%	40.2%	39.1%	39.1%
Dep/Net Fixed Asset	3.0%	2.9%	3.1%	3.3%	3.2%	3.4%	3.3%	3.3%
Depreciation Growth	12.5%	11.3%	16.7%	17.3%	6.7%	15.1%	3.6%	6.5%
General taxes as % of revenue	6.2%	6.4%	6.2%	7.5%	7.1%	7.1%	6.8%	6.8%
Interest Exp/ Average Net Debt	5.6%	5.3%	5.8%	5.9%	5.2%	5.2%	5.3%	5.6%
Interest Expense/Revenue	11.0%	10.5%	11.0%	11.1%	10.9%	10.1%	9.8%	10.1%
EBITDA	239.7	265.6	285.7	310.5	325.4	356.9	402.6	442.0
Net income growth	13.0%	13.9%	0.9%	3.3%	3.1%	8.0%	20.8%	11.1%
Average ROE	11.4%	11.7%	10.6%	10.0%	9.6%	9.8%	11.3%	11.8%
EPS Growth (ex special items and FAS 123)	7.0%	10.9%	-1.0%	1.9%	2.2%	6.8%	19.6%	10.0%
Source: Company reports and Longbow estimates								

WATER INDUSTRY PEER VALUATION

($ in millions, except per share data)

Company	Ticker	FY End	Rating	Target	% Upside	Share Price	52 Week Hi	52 Week Lo	Mkt Cap	Revenue Last FY	Earnings per Share Last FY	Earnings per Share Current FY	Earnings per Share Next FY	P/E Current FY	P/E Next FY	Dividend Rate	Price/ Book
U.S. WATER UTILITIES																	
American Water Works	**AWK**	**Dec.**	**BUY**	**$24**	**4%**	**$ 23.00**	**$23.03**	**$16.22**	**$ 3,995**	**$ 2,337**	**1.17**	**1.28**	**1.50**	**17.9x**	**15.3x**	**3.7%**	**1.3x**
Aqua America	**WTR**	**Dec.**	**Neutral**			**$ 17.56**	**$21.50**	**$15.39**	**$ 2,389**	**$ 627**	**0.73**	**0.78**	**0.93**	**22.6x**	**18.9x**	**3.3%**	**2.6x**
American States Water	**AWR**	**Dec.**	**Neutral**			**$ 35.19**	**$38.79**	**$29.76**	**$ 655**	**$ 319**	**1.56**	**1.85**	**1.97**	**19.1x**	**17.8x**	**2.9%**	**1.8x**
California Water Service Group	**CWT**	**Dec.**	**BUY**	**$45**	**26%**	**$ 35.62**	**$46.19**	**$33.49**	**$ 745**	**$ 410**	**1.90**	**2.00**	**2.20**	**17.8x**	**16.2x**	**3.3%**	**2.4x**
Southwest Water Company	SWWC	Dec.	NR			$ 5.97	$6.32	$3.20	$ 148	$ 222	-0.19	*0.05*	*0.36*	119.4x	16.6x	3.4%	0.7x
Artesian Resources Corporation	ARTNA	Dec	NR			$ 17.68	$18.73	$12.81	$ 136	$ 56	0.86	*0.95*	*1.08*	18.6x	16.4x	4.1%	1.3x
Consolidated Water Co	CWCO	Dec	NR			$ 14.11	$21.29	$6.35	$ 203	$ 60	0.50	*0.64*	*0.79*	22.0x	17.9x	2.1%	1.5x
Connecticut Water Service	CTWS	Dec	NR			$ 23.55	$26.44	$17.31	$ 207	$ 61	1.12	*1.23*	*1.15*	19.1x	20.5x	3.8%	1.9x
Middlesex Water Company	MSEX	Dec	NR			$ 16.98	$18.00	$11.64	$ 233	$ 91	0.90	*0.7*	*0.8*	24.3x	21.2x	4.2%	1.7x
Pennichuck Corporation	PNNW	Dec	NR			$ 20.88	$24.80	$16.56	$ 97	$ 31	0.57	*0.58*	*0.75*	36.0x	27.8x	3.3%	1.8x
York Water Company	YORW	Dec	NR			$ 14.26	$17.95	$9.74	$ 184	$ 33	0.57	*0.65*	*0.69*	21.9x	20.7x	3.5%	2.0x
U.S. Water Utility Average														30.8x	19.0x	3.4%	1.7x
EQUIPMENT/FILTRATION/TREATMENT SECTOR																	
Calgon Carbon Corp.	CCC	Dec.	NR			$ 14.72	$19.31	$10.93	$ 812	$ 400	0.56	*0.53*	*0.78*	27.8x	18.9x	0.0%	3.3x
Danaher	DHR	Dec.	NR			$ 75.20	$76.56	$47.73	$ 24,112	$ 12,697	4.23	*3.48*	*4.02*	21.6x	18.7x	0.2%	1.8x
ITT Technologies	ITT	Dec.	NR			$ 48.54	$56.95	$31.94	$ 8,925	$ 11,695	4.04	*3.74*	*4.01*	13.0x	12.1x	1.7%	2.7x
Layne Christensen	LAYN	Jan.	NR			$ 27.13	$35.14	$14.13	$ 532	$ 1,008	2.20	*0.84*	*0.95*	32.3x	28.6x	0.0%	0.7x
Mueller Water Products	MWA	Sept	NR			$ 5.40	$8.30	$1.48	$ 831	$ 1,428	0.46	*(0.36)*	*0.15*	-15.0x	36.0x	1.3%	1.9x
Nalco	NLC	Dec.	NR			$ 26.41	$26.22	$9.38	$ 3,658	$ 4,212	1.30	*0.87*	*1.27*	30.4x	20.8x	0.5%	4.0x
Pall Corp.	PLL	Jul.	NR			$ 36.82	$37.25	$18.20	$ 4,300	$ 2,329	1.94	*1.87*	*2.25*	19.7x	16.4x	1.6%	3.2x
Pentair	**PNR**	**Dec.**	**BUY**	**$37**	**19%**	**$ 32.85**	**$34.27**	**$17.23**	**$ 3,221**	**$ 3,382**	**2.20**	**1.42**	**1.80**	**23.1x**	**18.3x**	**2.2%**	**1.2x**
Watts Water Technologies	**WTS**	**Dec.**	**Neutral**			**$ 31.00**	**$32.96**	**$15.85**	**$ 1,146**	**$ 1,459**	**1.83**	**1.54**	**1.55**	**20.2x**	**20.0x**	**1.4%**	**1.1x**
Equipment/Filtration/Treatment Average (*ex BWTR and CCC)														19.2x	21.1x	1.0%	2.2x
WATER RESOURCES/ INFRASTRUCTURE																	
Insituform Technologies	INSU		NR			$ 22.77	$24.22	$11.42	$ 888	$ 537	0.77	*1.03*	*1.29*	22.3x	17.8x	0.0%	1.5x
Lindsay Manufacturing	LNN		NR			$ 43.83	$47.02	$20.89	$ 533	$ 336	3.11	*1.13*	*1.28*	38.7x	30.1x	0.7%	2.5x
Tetra Tech	TTEK		NR			$ 27.17	$32.00	$19.83	$ 1,682	$ 2,287	1.02	*1.24*	*1.38*	22.5x	20.7x	0.0%	2.5x
Water Resources/ Infrastructure Average														27.8x	22.9x	0.2%	2.2x

Relevant Indices		Share Price
Dow Jones Industrials	DJ30	$ 10,574
S&P 500	SPX	$ 1,137
Nasdaq Composite	NDX	$ 2,301

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.

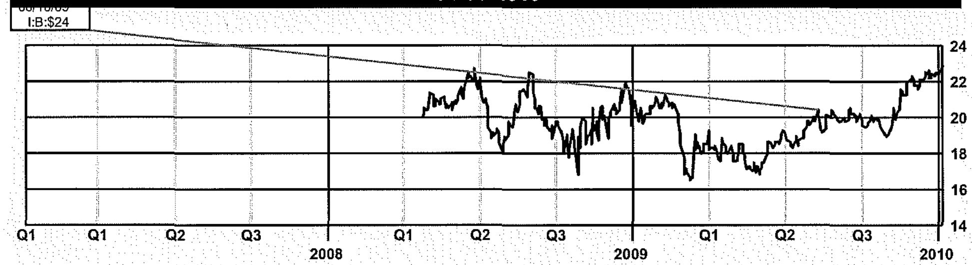
LONGBOW Research

January 7, 2010

G. Shmois
216-525-8414

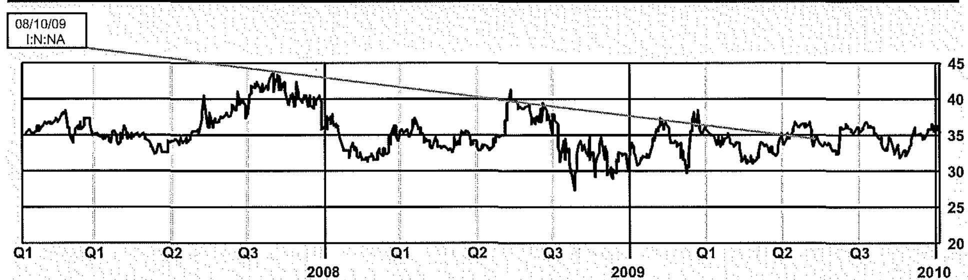
V. Khetriwal, CFA
216-525-8469

Rating and Price Target History for: American Water Works Company, Inc. (AWK) as of 01-06-2010



Created by BlueMatrix

Rating and Price Target History for: American States Water Company (AWR) as of 01-06-2010



Created by BlueMatrix

Rating and Price Target History for: California Water Service Group (CWT) as of 01-06-2010

Created by BlueMatrix

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

APPENDIX

IMPORTANT DISCLOSURES

REGULATION ANALYST CERTIFICATION ("REG AC"): The Research Analyst(s) who prepared this research report hereby certifies that the views expressed in the research report accurately reflect the analyst(s) personal views about the subject companies and their securities. The Research Analyst(s) also certifies that the Analyst(s) have not been, are not, and will not be receiving direct or indirect compensation for expressing the specific recommendation(s) or view(s) in this report.

GENERAL DISCLOSURES: Longbow Securities does not make a market in any securities, nor does it hold a principal position in any security. Security prices in this report may either reflect the previous day's closing price or an intraday price, depending on the time of distribution. Consensus estimates are derived from either Thomson/Reuters, Bloomberg or Baseline. Designated trademarks and brands are the property of their respective owners.

SPECIFIC DISCLOSURES:

- Longbow Securities does not make a market in the securities of any company mentioned in this report, and is not a market maker in any securities. Nor does the firm hold a principal position in any security.

- As of the date of this report, no officer, director or stockholder of Longbow Securities, or any member of their immediate families, holds securities of any company mentioned in the report. In the event such persons purchase, hold or sell securities of a company mentioned in the report for their own account, any subsequent report shall disclose the fact of any such ownership or transactions.

- As of the date of this report, no employee of Longbow Securities serves on the Board of Directors of the subject security or any other security mentioned in this report.

- As of the date of this report, neither the Research Analyst nor a member of the Research Analyst's household has a financial interest in the securities of the subject company or any other security mentioned in this report.

- As of the date of this report, neither the Research Analyst nor a member of the Research

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

Analyst's household serves on the Board of Directors of the subject company or any other security mentioned in this report.

- As of the date of this report, neither Longbow Securities nor its affiliates beneficially own 1% or more of an equity security of the subject company or any other security mentioned in this report.

RATINGS DISTRIBUTIONS FOR LONGBOW RESEARCH:

Rating Category	Count	Percent
Buy	71	33.5%
Neutral	138	65.1%
Sell	3	1.4%

RATING SYSTEM:

"Buy" means that Longbow Securities expects total return to exceed 20% over a 12-month period.

"Neutral" means that Longbow Securities expects total return to be within a range of plus or minus 20% over a 12-month period.

"Sell" means that Longbow Securities expects total return to be negative by greater than 20% over a 12-month period.

Longbow Research's full research universe and related applicable disclosures can be obtained by calling (216) 986-0700 or via postal mail at: Editorial Department, Longbow Research, 6000 Lombardo Center, Suite #500, Independence, Ohio 44131.

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

DESCRIPTION: Longbow Securities LLC, a wholly owned subsidiary of Longbow Research LLC, is a primary research provider established in 2003 and headquartered at 6000 Lombardo Center, Suite 500, Independence, Ohio 44131 USA. The company provides research services to institutional investors, investment advisers, and professional money managers. MEMBER FINRA/SIPC. Additional information supporting the statements in this report is available upon request.

LONGBOW Research
Tactical advantage through independent research

Industry Update

February 8, 2010

Analysts:
GARIK SHMOIS
T: 216-525-8414
E: gshmois@longbowresearch.com

VISHAL KHETRIWAL, CFA
T: 216-525-8469
E: vkhetriwal@longbowresearch.com

Industry: **WATER INFRASTRUCTURE**

Coverage:

Ticker	Rating	Price
AWK	BUY	$21.68
AWR	NEUTRAL	$32.74
CWT	BUY	$36.03
PNR	BUY	$30.32
WTR	NEUTRAL	$16.92
WTS	NEUTRAL	$28.48

The Water Rundown

Research of the Week

- Highlights from PNR 4Q09 Earnings

End Market & Industry Updates

- Cadiz study shows enough desert water to supply 400,000 people
- Obama seeks $3.3 billion for SRFs
- Obama to cancel $52M from Army Corps' 2011 budget
- Cold snap wreaked havoc on Tampa's water pipes

Water Utilities Updates

- AWK subsidiary buys Pennsylvania system
- WTR declares dividend
- CWT schedules 4Q09 Earnings Announcement
- AWR announces dividend

Water Equipment/Treatment Updates

- WTS 4Q09 Earnings Call date announced
- MWA reports 1Q10 results
- MWA to close U.S. Pipe manufacturing plant

Water Resources/ Infrastructure Updates

- INSU Awarded $6.7M Contract for Sewer Rehabilitation

Graphs

- Comparative Index of Utilities Returns
- CPI: Water and Sewage

IMPORTANT DISCLOSURES ARE LOCATED IN THE APPENDIX.

Longbow Research, 6000 Lombardo Center, Suite 500, Independence, Ohio USA 44131
T: 216-986-0700 • F: 216-986-0720 • www.longbowresearch.com

Highlights from PNR 4Q09 Earnings

Discussion of Details

Pentair (PNR, BUY, $37, 12-month target price) reported 4Q09 adjusted EPS of $0.47/share vs. our estimate and consensus of $0.43. Revenues decreased 9% but operating margins of 11% were up 140 bp. The beat came from better than expected revenues from the water business in large part to stabilization in residential and improved municipal sales.

The Water Group saw revenues down 7% y/y vs. our -14.5% forecast. Margins of 11.6% were below our 12.3% forecast. Despite lower sales, the water group saw a 7% increase in EBIT y/y. Flow sales were down 3% as global municipal demand offset declines in commercial, industrial and residential. Filtration sales were down 9% y/y and pool sales were down 13%.

Technical Products sales declined 12% and were down 15% excluding fx benefits. We were looking for a -15% forecast. Electrical sales were down 16% due to the pullback in industrial demand while electronic sales declined 7%. Adjusted EBIT of $35M was up 30% y/y. Margins of 15.3% were up 220bp y/y due improved productivity and material savings. Margins were in line with our 15% forecast.

Guidance Revision

PNR raised its 1Q10 EPS guidance to $0.32 to $0.35 vs. at least $0.30 previously on 6-8% water revenue growth and mid-single-digit growth in technical products. Consolidated margins are expected to be ~9.5% vs. 6.3% in 1Q09 and 11% in 4Q09 (the major delta sequentially is seasonality in the pool business) . For FY10, PNR sees EPS of $1.75 to $1.90 vs. at least $1.70 previously on mid- to high-single-digit revenue growth. While the guidance adjustment puts PNR's earnings expectations around where consensus estimates currently are, we believe it could prove conservative as 2H10 assumes flattish to only slightly up y/y growth. There could be upside, especially as PNR sees over $60M in revenues from its large municipal pump order in New Orleans, as well as sales momentum from stable to improving residential end markets. Additionally, PNR is confident it can secure pricing to offset material cost inflation. In turn, 100-200bp y/y margin expansion should be sustainable.

Outlook for 1Q10 and FY10

- While steel costs have been trending up over the past several months, PNR COGS tend to lag commodity inflation by approximately 1-2 quarters. Given this visibility, we expect PNR to secure price increases to offset, and management is confident given initial market responses that 100-200bp in pricing could be obtained should commodity costs continue to rise.
- PNR expects $50M in carryover productivity benefit in 2010 ($30M in material and $20M in labor) from actions already completed in 2009.
- The company is resuming several employee benefits such as pension expense, higher medical costs, 401k contributions, merit increases, sales incentives, and bonus accruals that will impact earnings negatively by $30M in FY10 ($0.05/share in 1Q).
- 1Q09 will likely be the last quarter for planned restructuring actions and plant closures. Shift of attention to LEAN initiatives in the consolidated plants should provide additional efficiencies (not quantified by the company).
- Current order activity for the residential market point to recovery in the U.S. residential market. We expect 8% revenue growth for the Water segment in 1Q10 driven by this recovery. Infrastructure, defense, and security markets also improved y/y in 4Q09 and should contribute to growth.
- Technical Products is benefiting the most from stimulus spending. We expect 6% revenue growth in 1Q10 with 410bp y/y margin improvement to 14.2% (though down 110pb from 4Q09 due to seasonality). Stabilization in the European enclosures market, consolidation of electric and electronic manufacturing footprint, and continued impressive margins in electrical business should drive this performance.
- With reduced debt, management intends to resume acquisitions, with focus on ~$50M-sized bolt-on purchases for technical expertise and international expansion.

END MARKET & INDUSTRY UPDATES

Cadiz study shows enough desert water to supply 400,000 people – Cadiz Inc., the owner of thousands of acres of California desert, said a study shows there's more water under its land than the company previously estimated, giving it enough to supply 400,000 people. A study conducted by engineering company CH2M Hill shows the aquifer under the Mojave Desert land ranges in size from 17 million to 34 million acre-feet, potentially larger than the Lake Mead reservoir near Las Vegas, according to Cadiz. The company wants to supply water to Southern California to become profitable for the first time since 1990. A water shortage in the western U.S. has spurred suppliers to consider desalination of ocean water and other alternatives for meeting the state's demands. With the amount of water now believed available to Cadiz in the aquifer system, the company would be able to ship 50,000 acre-feet south each year, enough for 400,000 Californians, Chief Financial Officer Tim Shaheen said. Before the CH2M Hill study, peer-reviewed by geologists from the University of Texas and the University of Southern California, Cadiz officials expected they might have enough groundwater to pump as little as 20,000 acre-feet a year. CH2M Hill, based in Englewood, Colorado, does engineering and construction work for energy companies and government agencies. The closely held company has $6.4 billion in revenue and 25,000 employees. Shaheen and Slater declined to say how much revenue they expect the water to generate. Some believe Cadiz probably will be able to sell the water for at least $1,000 an acre-foot, or a total of $50 million a year.
Source: Newsweek

LBR Note: Water rights is a contentious issue in Western U.S. Increasing water shortages could provide upside for companies owning large water rights in the region, including American States Water (AWR, Neutral), which owns one of the largest adjusted water rights in California.

Obama seeks $3.3 billion for SRFs – President Obama's 2011 budget request seeks $3.3 billion for USEPA's Clean Water and Drinking Water State Revolving Funds (SRFs) and $1.3 billion – a 14 percent increase from 2010 and the highest level ever – to help states and tribes protect their air, water, and land. As submitted to Congress, the budget request would also provide $274 million – a $45 million increase – for state water pollution control grants. Overall, the Obama Administration seeks a record $10 billion for USEPA even as it imposes a three-year freeze on non-security discretionary funding.
Source: Associated Press

LBR Note: As SRFs are the primary source of low-interest funding for cities and municipalities to invest in water infrastructure, and EPA is the primary enforcer of federal water and wastewater related regulation, the budget for these has a significant impact on water sector in the country.

Obama to cancel $52M from Army Corps' 2011 budget – President Obama's budget for fiscal 2011 (FY11) includes $4.939 billion in gross discretionary funding for the civil works program of the U.S. Army Corps of Engineers (USACE), offset in part by a proposal to cancel $52 million of prior year funding, according to an agency press release. The budget funds the planning, design, construction, and the operation and maintenance of projects, and focuses on the Corps' three main civil works mission areas: commercial navigation, flood and coastal storm damage reduction, and aquatic ecosystem restoration. The Army Civil Works program additionally contributes to the protection of the nation's waters and wetlands, the restoration of sites contaminated as a result of the nation's early atomic weapons development program, and emergency preparedness and training to respond to natural disasters. The new federal funding in the civil works budget consists of $4.051 billion from the general fund, $764.4 million from the Harbor Maintenance Trust Fund, $82.3 million from the Inland Waterways Trust Fund, and $41 million from Special Recreation User Fees.
Source : AWWA

LBR Note: USACE is responsible for maintenance and expansion of public water infrastructure, such as dams, levees, and waterways in the U.S. The agency's budget has a direct impact on business prospects of companies providing water infrastructure-related equipment and services.

Cold snap wreaked havoc on Tampa's water pipes – The recent cold snap that resulted in more than a week of below-freezing temperatures took a toll on Tampa's aging infrastructure, and its finances. For the past two weeks, city workers and private contractors have been busy repairing more than 1,600 breaks in water distribution pipes throughout the city. The breaks weren't confined to any one area of the city and ranged from water mains to residential hookups. Costs to the city for the repairs are estimated at upwards of $400,000. Substantial drop in water temperature, which at the height of the cold snap dipped as low as 50 degrees, caused the epoxy seal on the seam to contract and leak. Warmer weather in the past few days has caused the seam to expand and the dam has stopped leaking. But the city plans to repair the seam, at an estimated cost of $15,000. The cost of the repairs has just about drained the water department's maintenance fund, straining the finances of a city department that has suffered a sizeable drop in operating funds in the past several years from a loss of customer accounts and other factors. In 2006, the city battled similar citywide pipe breaks during November and December. As temperatures went up and down, pipes burst in nearly every corner of the city.
Source: Tampa Tribune

LBR Note: The massive breaks in water pipes in Tampa highlights the poor state of water distribution system in large parts of the country, which brings much needed public attention to the exacerbating problem.

WATER UTILITIES UPDATES

American Water Works (AWK, BUY, 12-mo. TP$24) – AWK announced that it has acquired the water system assets of Nittany Water Company in north-central Pennsylvania. The purchase price of the newly acquired system, which serves nearly 1,500 people in Centre and Clinton counties, is approximately $520,000. The transaction provides Pennsylvania American Water with its first operation in Clinton County, expanding the company's footprint to 36 counties across the state. With this acquisition, Pennsylvania American Water takes over a troubled water system with a history of water outages, frequent main breaks, and service reliability issues due to aging infrastructure. According to Pennsylvania American Water President Kathy L. Pape, the acquisition provides a long-term solution for customers of the water system, which has been under a Department of Environmental Protection (DEP) consent order since July 2008 over service reliability issues.

Aqua America (WTR, NEUTRAL) – The Board of Directors of Aqua WTR declared a quarterly cash dividend payment of $0.145 per share payable on March 1, 2010, to all shareholders of record on February 16, 2010. The March dividend payment of $0.145 per share is 7.4 percent higher than the dividend the company paid in March 2009 of $0.135 per share. Aqua has paid a consecutive quarterly dividend for more than 60 years.

California Water (CWT, BUY, 12-mo. TP$45) – CWT announced that its fourth quarter and year-end earnings results will be released after the market-close on Wednesday, February 24, 2010, and its teleconference will be held at 11:00 a.m. EST on Thursday, February 25, 2010. The 2009 fourth quarter and year-end conference call may be accessed by dialing 1-866-837-9789 and keying in ID# 1427079.

American States Water (AWR, NEUTRAL) – On February 1, 2010, the Board of Directors of AWR approved a quarterly dividend of $0.26 per share on the Common Shares of the Company. This action marks the 295th consecutive dividend payment by the Company. Dividends on the Common Shares will be payable on March 1, 2010 to shareholders of record at the close of business on February 12, 2010.

WATER EQUIPMENT/TREATMENT UPDATES

Watts Water (WTS, NEUTRAL) – WTS will hold a live webcast of its conference call to discuss fourth quarter results for 2009 on Tuesday, February 16, 2010, at 5:00 p.m. Eastern Time. Watts Water Technologies will announce its financial results for this period in a press release to be issued after market close on Tuesday, February 16, 2010.

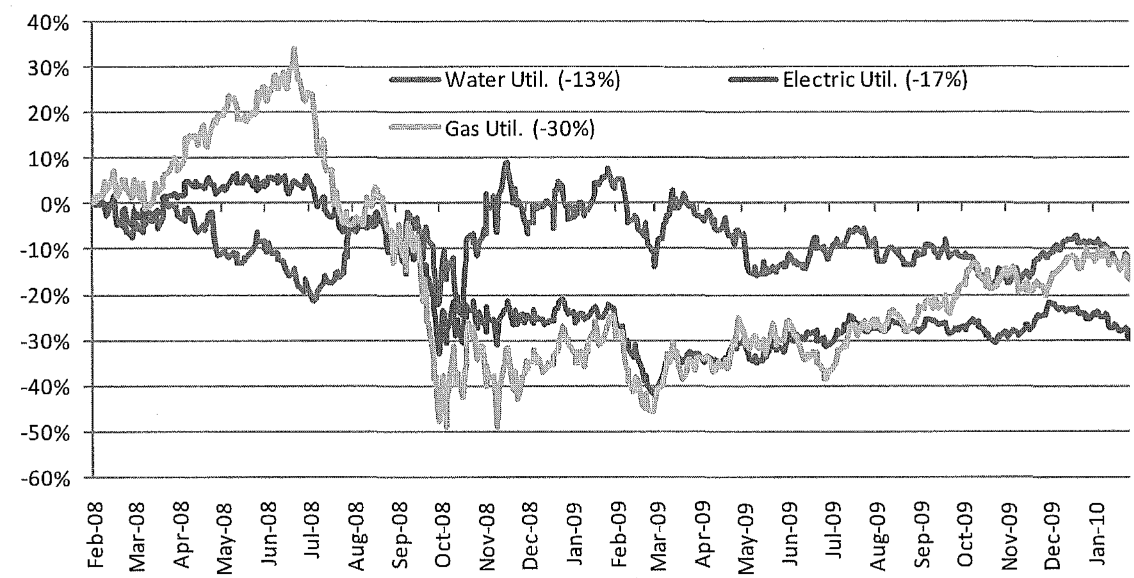
Mueller Water Products (MWA, NR) – MWA reported net sales of $313.1 million and a net loss of $10.7 million in the quarter ended December 31, 2009. Summarized consolidated 2010 first quarter results compared to 2009 first quarter results are as follows: Net sales in the 2010 first quarter were $313.1 million, down 14.8 percent compared to $367.7 million in the 2009 first quarter. Net loss per share was $0.07 in the 2010 first quarter compared to a net loss per share of $3.47 in the 2009 first quarter. Adjusted net loss per share was $0.00 in the 2009 first quarter. Cash provided by operating activities in the 2010 first quarter was $60.1 million compared to cash used in operating activities of $17.9 million in the 2009 first quarter. Free cash flow was $51.4 million in the 2010 first quarter compared to negative $27.9 million in the 2009 first quarter.

MWA announced that U.S. Pipe and Foundry Company LLC (U.S. Pipe) will close its ductile iron pipe manufacturing plant in North Birmingham, Alabama by March 31, 2010, eliminating approximately 260 positions. Production from the North Birmingham plant will be managed using existing capacity at U.S. Pipe's Bessemer, Alabama and Union City, California facilities. Over the past three years, U.S. Pipe has focused on streamlining and upgrading its operations to improve safety and quality, and reduce costs. Most significantly, the company invested in a new automated ductile iron pipe manufacturing process that increases quality and output while substantially reducing costs. A facility for this new manufacturing technology was built adjacent to its Bessemer, Alabama facility

WATER RESOURCES/INFRASTRUCTURE UPDATES

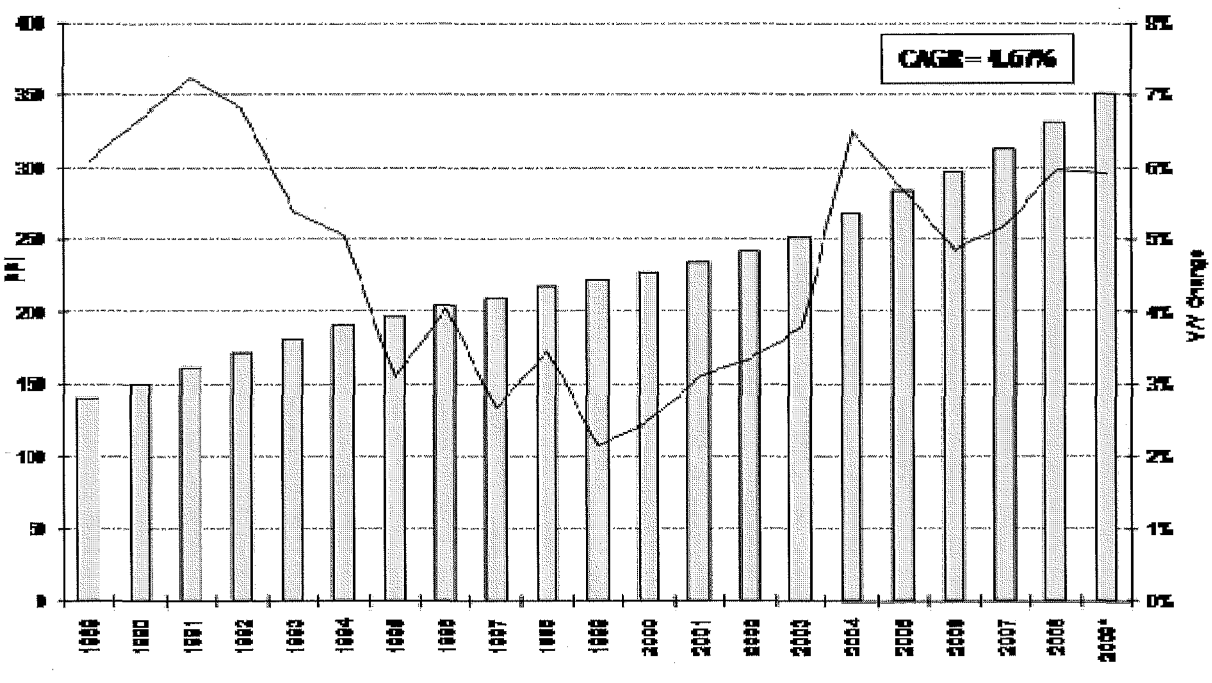
Insituform (INSU, NR) – INSU announced that it was awarded $6.7 million in sewer pipe rehabilitation work for Pell City, Alabama, which has used a grant from the American Recovery and Reinvestment Act of 2009 to award the largest CIPP project in Pell City's history to INSU. Under this contract, INSU will rehabilitate approximately 115,000 feet of sewer pipelines in residential and rural areas. This contract also marks the first time INSU has worked with Pell City, Alabama. Insituform® cured-in-place pipe (CIPP) will be used to eliminate inflow and infiltration on the 25-year old small- to medium-diameter sanitary sewers. Work on this project is expected to begin in February 2010 and take approximately one year to complete.

Comparative Returns of Different Utilities – Last 2 yrs



Source: Baseline

CPI: Water and Sewerage



Source: Bureau of Labor Statistics

WATER INDUSTRY PEER VALUATION

($ in millions, except per share data)

Company	Ticker	FY End	Rating	Target	% Upside	Share Price	52 Week Hi	52 Week Lo	Mkt Cap	Revenue Last FY	Earnings per Share Last FY	Earnings per Share Current FY	Earnings per Share Next FY	P/E Current FY	P/E Next FY	Dividend Rate	Price/ Book
U.S. WATER UTILITIES																	
American Water Works	**AWK**	**Dec.**	**BUY**	**$24**	**11%**	**$ 21.68**	**$23.77**	**$16.22**	**$ 3,785**	**$ 2,337**	**1.17**	**1.28**	**1.50**	**16.9x**	**14.4x**	**3.9%**	**1.3x**
Aqua America	**WTR**	**Dec.**	**Neutral**			**$ 16.92**	**$21.29**	**$15.39**	**$ 2,306**	**$ 627**	**0.73**	**0.78**	**0.93**	**21.8x**	**18.2x**	**3.4%**	**2.6x**
American States Water	**AWR**	**Dec.**	**Neutral**			**$ 32.74**	**$38.79**	**$29.76**	**$ 606**	**$ 319**	**1.56**	**1.85**	**1.97**	**17.7x**	**16.6x**	**3.2%**	**1.8x**
California Water Service Group	**CWT**	**Dec.**	**BUY**	**$45**	**25%**	**$ 36.03**	**$46.19**	**$33.49**	**$ 747**	**$ 410**	**1.90**	**2.00**	**2.20**	**18.0x**	**16.4x**	**3.3%**	**2.4x**
Southwest Water Company	SWWC	Dec.	NR			$ 5.92	$6.48	$3.67	$ 147	$ 222	0.05	*0.36*	-	16.4x	#VALUE!	3.4%	0.7x
Artesian Resources Corporation	ARTNA	Dec	NR			$ 17.51	$18.85	$12.81	$ 131	$ 56	0.94	*1.08*	-	16.2x	#VALUE!	4.3%	1.3x
Consolidated Water Co	CWCO	Dec	NR			$ 13.29	$21.29	$6.35	$ 193	$ 60	0.65	*0.83*	*0.8*	16.0x	16.6x	2.3%	1.5x
Connecticut Water Service	CTWS	Dec	NR			$ 21.80	$26.44	$17.31	$ 186	$ 61	1.23	*1.15*	*1.44*	19.0x	15.1x	4.2%	1.9x
Middlesex Water Company	MSEX	Dec	NR			$ 16.78	$18.00	$11.64	$ 227	$ 91	0.69	*0.8*	*0.89*	21.0x	18.9x	4.3%	1.7x
Pennichuck Corporation	PNNW	Dec	NR			$ 19.77	$24.80	$17.00	$ 91	$ 31	0.58	*0.75*	*0.79*	26.4x	25.0x	3.6%	1.8x
York Water Company	YORW	Dec	NR			$ 13.23	$17.95	$9.74	$ 166	$ 33	0.63	*0.69*	*0.82*	19.2x	16.1x	3.9%	2.0x
U.S. Water Utility Average														19.0x	#VALUE!	3.6%	1.7x
EQUIPMENT/FILTRATION/TREATMENT SECTOR																	
Calgon Carbon Corp.	CCC	Dec.	NR			$ 12.90	$19.31	$10.93	$ 722	$ 400	0.53	*0.78*	*0.9*	16.5x	14.3x	0.0%	3.3x
Danaher	DHR	Dec.	NR			$ 71.01	$78.02	$47.73	$ 22,811	$ 11,185	3.53	*4.06*	*4.62*	17.5x	15.4x	0.2%	2.1x
ITT Technologies	ITT	Dec.	NR			$ 48.51	$56.95	$31.94	$ 8,863	$ 10,905	3.78	*4.05*	*4.47*	12.0x	10.9x	1.8%	2.3x
Layne Christensen	LAYN	Jan.	NR			$ 25.56	$35.14	$14.13	$ 497	$ 1,008	0.85	*0.95*	*1.45*	26.9x	17.6x	0.0%	0.7x
Mueller Water Products	MWA	Sept	NR			$ 5.03	$5.93	$1.48	$ 774	$ 1,428	-0.29	*0.05*	*0.15*	100.6x	33.5x	1.4%	1.9x
Nalco	NLC	Dec.	NR			$ 21.93	$26.63	$9.62	$ 3,031	$ 3,747	0.95	*1.35*	*1.65*	16.2x	13.3x	0.6%	4.0x
Pall Corp.	PLL	Jul.	NR			$ 33.92	$37.85	$18.20	$ 3,965	$ 2,329	1.77	*2.25*	*2.25*	15.1x	15.1x	1.9%	3.2x
Pentair	**PNR**	**Dec.**	**BUY**	**$37**	**30%**	**$ 30.32**	**$34.27**	**$17.23**	**$ 2,982**	**$ 2,692**	**1.47**	**1.85**	**2.28**	**16.4x**	**13.3x**	**2.5%**	**1.5x**
Watts Water Technologies	**WTS**	**Dec.**	**Neutral**			**$ 28.48**	**$32.96**	**$15.85**	**$ 1,045**	**$ 1,459**	**1.83**	**1.54**	**1.55**	**18.5x**	**18.4x**	**1.5%**	**1.1x**
Equipment/Filtration/Treatment Average (*ex BWTR and CCC)														26.6x	16.9x	1.1%	2.2x
WATER RESOURCES/ INFRASTRUCTURE																	
Insituform Technologies	INSU		NR			$ 20.71	$24.22	$11.42	$ 805	$ 537	1.03	*1.31*	*1.47*	15.9x	14.1x	0.0%	1.5x
Lindsay Manufacturing	LNN		NR			$ 36.61	$47.45	$20.89	$ 454	$ 336	1.11	*1.28*	*1.75*	24.3x	22.7x	0.9%	2.5x
Tetra Tech	TTEK		NR			$ 20.79	$32.00	$19.51	$ 1,274	$ 2,287	1.22	*1.20*	*1.35*	17.6x	15.2x	0.0%	2.5x
Water Resources/ Infrastructure Average														19.3x	17.3x	0.3%	2.2x
Relevant Indices						**Share Price**											
Dow Jones Industrials	DJ30					$ 10,012											
S&P 500	SPX					$ 1,066											
Nasdaq Composite	NDX					$ 1,746											

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.

Garik Shmois
216-525-8414
gshmois@longbowresearch.com

Vishal Khetriwal, CFA
216-525-8469
vkhetriwal@longbowresearch.com

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

APPENDIX

IMPORTANT DISCLOSURES

REGULATION ANALYST CERTIFICATION ("REG AC"): The Research Analyst(s) who prepared this research report hereby certifies that the views expressed in the research report accurately reflect the analyst(s) personal views about the subject companies and their securities. The Research Analyst(s) also certifies that the Analyst(s) have not been, are not, and will not be receiving direct or indirect compensation for expressing the specific recommendation(s) or view(s) in this report.

GENERAL DISCLOSURES: Longbow Securities does not make a market in any securities, nor does it hold a principal position in any security. Security prices in this report may either reflect the previous day's closing price or an intraday price, depending on the time of distribution. Consensus estimates are derived from either Thomson/Reuters, Bloomberg or Baseline. Designated trademarks and brands are the property of their respective owners.

SPECIFIC DISCLOSURES:

- Longbow Securities does not make a market in the securities of any company mentioned in this report, and is not a market maker in any securities. Nor does the firm hold a principal position in any security.
- As of the date of this report, no officer, director or stockholder of Longbow Securities, or any member of their immediate families, holds securities of any company mentioned in the report. In the event such persons purchase, hold or sell securities of a company mentioned in the report for their own account, any subsequent report shall disclose the fact of any such ownership or transactions.
- As of the date of this report, no employee of Longbow Securities serves on the Board of Directors of the subject security or any other security mentioned in this report.
- As of the date of this report, neither the Research Analyst nor a member of the Research Analyst's household has a financial interest in the securities of the subject company or any other security mentioned in this report.
- As of the date of this report, neither the Research Analyst nor a member of the Research Analyst's household serves on the Board of Directors of the subject company or any other security mentioned in this report.
- As of the date of this report, neither Longbow Securities nor its affiliates beneficially own 1% or more of an equity security of the subject company or any other security mentioned in this report.

RATINGS DISTRIBUTIONS FOR LONGBOW RESEARCH:

Rating Category	Count	Percent
Buy	84	37.7%
Neutral	137	61.4%
Sell	2	0.9%

RATING SYSTEM:

"Buy" means that Longbow Securities expects total return to exceed 20% over a 12-month period.

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

"Neutral" means that Longbow Securities expects total return to be within a range of plus or minus 20% over a 12-month period.

"Sell" means that Longbow Securities expects total return to be negative by greater than 20% over a 12-month period.

Longbow Research's full research universe and related applicable disclosures can be obtained by calling (216) 986-0700 or via postal mail at: Editorial Department, Longbow Research, 6000 Lombardo Center, Suite #500, Independence, Ohio 44131.

DISCLAIMER: The information, opinions, estimates and projections contained in this report were prepared by Longbow Securities LLC, a wholly owned subsidiary of Longbow Research LLC, and constitute the current judgment of Longbow Securities as of the date of this report. Additional information may be available from Longbow Securities upon request. The information contained herein is believed to be reliable and has been obtained from sources believed to be reliable, but Longbow Securities makes no representation or warranty, either expressed or implied, as to the accuracy, completeness or reliability of such information. Longbow Securities does not undertake, and has no duty, to advise you as to any information that comes to its attention after the date of this report or any changes in its opinion, estimates or projections. Prices and availability of securities are also subject to change without notice. By accepting this report, the reader acknowledges that the report does not purport to meet the objectives or needs of specific investors, and, accordingly, constitutes only "impersonal advisory services" as that term is defined in Rule 204-3 under the Investment Advisers Act of 1940 and that any advice in this report is furnished solely through uniform publications distributed to subscribers thereto within the meaning of Section 2(a)(20)(i) of the Investment Company Act of 1940. The securities discussed in Longbow Research reports may be unsuitable for some investors depending on their specific investment objectives, financial status, risk profile, or particular needs. Investors should consider this report as only a single factor in making their investment decisions and should not rely entirely on this report in evaluating whether or not to buy or sell the securities of the subject company. Longbow Research archives and reviews outgoing and incoming email. Such may be produced at the request of regulators. Sender accepts no liability for any errors or omissions arising as a result of transmission. Use by other than intended recipients is prohibited.

DESCRIPTION: Longbow Securities LLC, a wholly owned subsidiary of Longbow Research LLC, is a primary research provider established in 2003 and headquartered at 6000 Lombardo Center, Suite 500, Independence, Ohio 44131 USA. The company provides research services to institutional investors, investment advisers, and professional money managers. MEMBER FINRA/SIPC. Additional information supporting the statements in this report is available upon request.

Water Utilities

Industry Update

LONGBOW Research
Tactical advantage through independent research

February 16, 2010

Analysts:
GARIK SHMOIS
T: 216-525-8414
E: gshmois@longbowresearch.com

VISHAL KHETRIWAL, CFA
T: 216-525-8469
E: vkhetriwal@longbowresearch.com

Industry: **WATER UTILITIES**

Coverage:

Ticker	Rating	Price
AWK	BUY	$22.16
AWR	NEUTRAL	$32.05
CWT	BUY	$35.92
WTR	NEUTRAL	$16.59

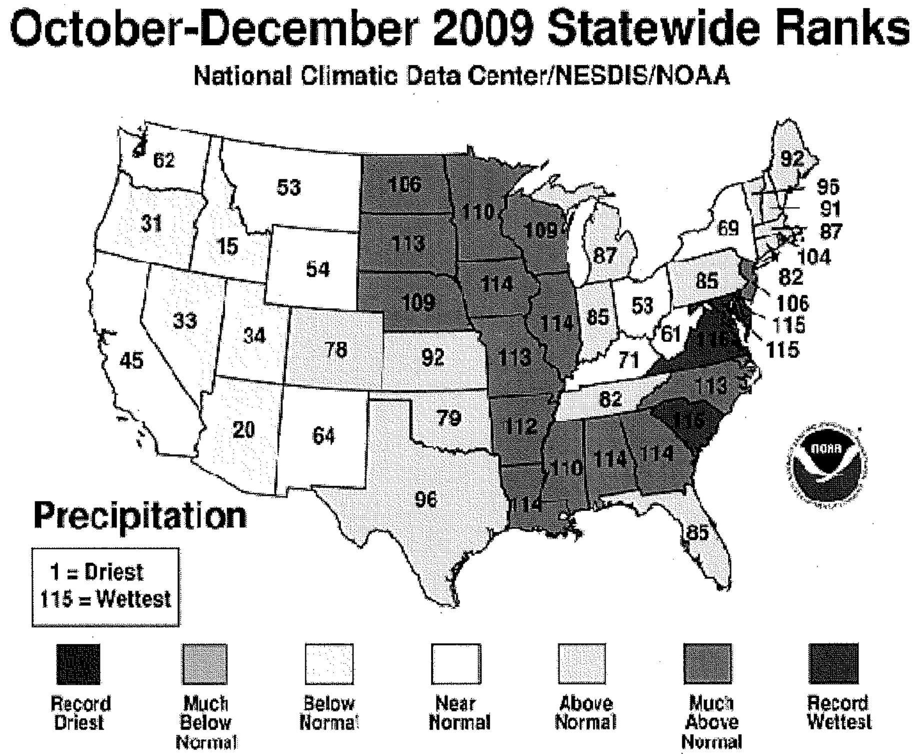
Water Utilities: 4Q09 Earnings Preview

- In the following report, we offer our 4Q09 earnings expectations for the water utilities under our research coverage. As was the case with recent quarters, on the upcoming conference calls, we are most interested in rate case proceedings, capex forecasts and M&A expectations.
- While wet weather typically has less impact on 4Q results than 2Q and 3Q, given the adverse weather conditions seen this year, we do expect at least a modest negative for AWK and WTR as almost the entire Northeast, Midwest and South had "above normal" or "much above normal" precipitation in 4Q09.
- Weaker construction activity and industrial demand should continue to remain a drag on the group's organic growth prospects. The good news is that residential construction appears to be stabilizing. Accordingly, we expect the mid-single-digit organic sales declines the water utilities reported in 1Q09-3Q09 to continue in 4Q, but we are modeling an improvement in FY10 to reflect a decline in the low-single-digits.
- WTR made two tuck-in acquisitions during the quarter, falling short of its target of ten announced on its 3Q09 conference call. AWK acquired EMC, a large water system contract operator, but we believe it has also fallen behind in making tuck-in acquisitions.
- In 4Q09, we anticipate AWK and WTR to offer y/y earnings growth of 11% and 9%, respectively, driven primarily by rate increases. We also expect to receive an update from AWK on the Trenton, NJ acquisition, and the request to recover or defer pension expenses.
- For CWT and AWR, we anticipate 3% and 0% EPS growth, respectively. We expect AWR's earnings growth to be limited until it receives price determinations for its base operations or receives a favorable ruling on its $51.5M General Rate Case.
- We continue to rate AWK and CWT as BUY-rated stocks and see valuations and FY10-FY11E EPS growth prospects as relatively more attractive than the coverage group. We remain NEUTRAL-rated on WTR and AWR shares.

IMPORTANT DISCLOSURES ARE LOCATED IN THE APPENDIX.

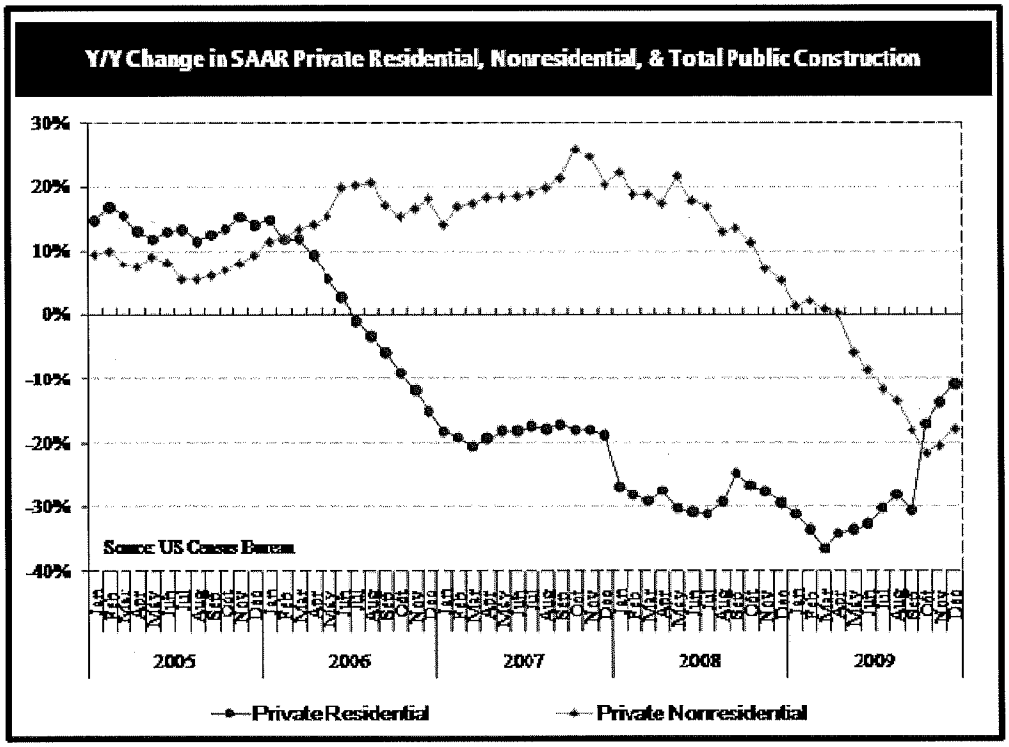
INTRODUCTION

In addition to updates on rate case proceedings, capex forecasts and M&A activity (discussed in greater detail below), we believe lower levels of construction activity and industrial demand had a generally adverse impact on the quarter. While wet weather normally has a more adverse impact in the second and third quarters of the year, given that almost the entire Northeast, Midwest and South had "above normal" or "much above normal" precipitation in 4Q09, we would think that the weather had at least some negative impact on the quarter. Given their geographic positioning, this would imply that the weather was a bigger negative to AWK and WTR, both of which have a large Northeast (greater than 50% of revenues derived here) and significant Midwest and South presence.



Source: National Climactic Data Center

We expect weaker construction activity, and in turn a lack of potential new customers, to continue to remain a drag on the group's organic growth prospects in the near-term. The good news is that residential construction appears to be stabilizing, albeit on a low base. Commercial construction, however, remains weak, and we anticipate another 25% drop in commercial construction in FY10. All in, the mid-single-digit organic sales declines the water utilities reported in 1Q09-3Q09 are likely to improve in FY10 to low-single-digit declines, mainly on residential stability.



Opinion. Our views on AWK, AWR, CWT and WTR remain unchanged. We continue to rate AWK and CWT as BUY-rated stocks. For AWK, we see upside potential both through multiple expansion and earnings growth opportunities over the next two years as the company should see rate relief catch up to nearly five years of under-investment and rate filing stay-outs. We also like CWT's earnings growth potential over the next one-to-two years, as well as the stock's relative undervaluation at 16.3x FY10E P/E vs. the company's historical normalized 20.5x average and normalized range of 17-27x forward P/E. While we believe WTR and AWR offer better 4Q09 y/y EPS growth prospects, at valuations of 17.9x and 16.2x FY10E EPS, respectively, we believe that near-term upside is already reflected in the shares.

COMPANY SPECIFIC THOUGHTS

American Water Works (AWK)

AWK is scheduled to report 4Q09 earnings results on March 1. For 4Q09, we expect EPS of $0.25 vs. consensus of $0.24, and revenue of $590.8M vs. consensus of $600.6M. For FY09, we expect EPS of $1.28, in-line with consensus, and revenue of $2,433.7M vs. consensus of $2,452M.

4Q09 EPS Projections and Comparisons									
		First Call Mean		LBR Estimate	Variance				
Ticker	Rating	4Q09E	Range	4Q09E	4Q08A	y/y Δ	3Q09A	y/y Δ
AWK	Buy	$0.24	$0.21-0.27	$0.25	$0.23	9%	$0.52	-52%

Source: Company Inforation, Baseline, LBR Estimates

During the company's conference call, we will also look for an update on:

Rate Cases: We will look for details on the company's expectations on new rate case filings in 1Q10 and throughout FY10. Although the rate cases and surcharges filed in FY09 increased to $313.3M from $310.9M in FY08, the annualized revenues that were approved dropped to $103.3M from $206.3M during FY08 due to timing issues. We expect this trend to reverse in FY10 as we estimate $162.9M in annualized rate increases and surcharges in FY10, including from $218.3M of cases currently pending. We expect a majority of these pending cases to be approved in 2Q10-3Q10, yielding $143.2M in an estimated annualized revenue increase during these two quarters. We note that the approved amount is usually 60-70% of the filed amount.

Acquisitions: Since 3Q09, AWK has acquired five water systems in Pennsylvania, one water system in Indiana, and the Environmental Management Corporation, a Missouri-based company that operates water systems under contract. The pace of acquisitions improved in late FY09, and we expect similar M&A momentum going forward as municipalities continue to look to raise cash during the current economic environment.

Trenton, NJ Acquisition: For the last two years, AWK has been trying to acquire a 40,000-customer water system from the city of Trenton, NJ, for approximately $80M. Although the regulators have approved the sale, the acquisition has been held up by litigation filed by a Trenton citizens' group seeking to block the transaction. Although we have been tracking the litigation, we will look for an update from management.

Capex: AWK is on track to reach its $800M FY09 capex target with $592.9M spent in 1Q09-3Q09. The capex program was scaled back in FY09 due to adverse capital market conditions and management has indicated at least a similar level of spending expected in FY10. On the call, we will look for an update on spending levels for FY10.

Pension Expenses: AWK experienced a sharp increase in pension and post-retirement benefit costs in FY09 due to the performance of the stock market in 2008 and its impact on the pension plans' assets and returns. As of 3Q09, AWK received authorization from regulators to recover or defer $7.1M of this annual increase and requested permission to recover or defer an additional $7.5M as a regulatory asset until the next rate case is concluded. As this has a material impact on AWK's margins, we will look for an update on these requests. At the same time, we believe that the stock market improvement in 2009 will somewhat mitigate the cost increase in FY10.

California Water (CWT)

CWT is scheduled to release 4Q09 and FY09 earnings results after market close on February 24, and will host a conference call on February 25 at 11AM ET to discuss the results (Dial in: 1-866-837-9789; ID# 1427079). For the quarter, we expect EPS of $0.36 vs. consensus of $0.35, and revenue of $107.3M vs. consensus of $104.5M. For the year, we expect EPS of $2.00 vs. consensus of $1.99, and revenue of $449.8M vs. consensus of $449.0M. We note that CWT's earnings are not impacted by water conservation efforts and weather-related consumption variation because of Water Revenue Adjustment Mechanism (WRAM), which decouples revenue from water sales.

4Q09 EPS Projections and Comparisons

		First Call Mean		LBR Estimate	Variance			
Ticker	Rating	4Q09E	Range	4Q09E	4Q08A	y/y Δ	3Q09A	y/y Δ
CWT	Buy	$0.35	$0.29-0.42	$0.36	$0.35	3%	$0.94	-62%

Source: Company Inforation, Baseline, LBR Estimates

Regulatory Affairs: On the company's conference call, we will look for an update on the $120.2M 2009 General Rate Case (GRC) filed in July 2009 for rates effective 2011-2013. According to the new rate plan, the California Public Utility Commission (CPUC) has 18 months to rule on this rate request. The 2009 GRC also includes: (a) a request for a pension and healthcare cost balancing account, which, if granted, will remove the earnings volatility related to these expenses, and (b) a request to add certain elements of the $16M conservation investment in 2011 to the rate base, so that the company can earn on those investments.

Acquisitions: Although CWT has traditionally limited acquisition opportunities in California, the company has been modestly expanding in other states, including Washington, Hawaii and New Mexico. On the call, we will look for management's expectations on acquisition opportunities going forward, although we anticipate future comments to be centered mainly around tuck-ins within its current geographic markets.

Capex Program: CWT is on target to hit the high end of its $100-120M FY09 capex guidance with $83M of investments made in 1Q09-3Q09. Additionally, management expects to exceed this target in FY10. We are now forecasting $120M in FY09 and $125M in FY10. On the call, we will look for an update on capex expectations going forward.

Aqua America (WTR)

WTR is scheduled to release 4Q09 and FY09 earnings results before the market open on February 25, and will host a conference call on the same day at 10AM ET to discuss the results (Dial in: 1-888-378-4436; ID# 3371054). For 4Q09, we expect EPS of $0.21, in-line with consensus, and revenue of $169.2M vs. consensus of $178.0M. For FY09, we expect EPS of $0.78 vs. consensus of $0.79, and revenue of $671.9M vs. consensus of $678.0M.

4Q09 EPS Projections and Comparisons

		First Call Mean		LBR Estimate	Variance			
Ticker	Rating	4Q09E	Range	4Q09E	4Q08A	y/y Δ	3Q09A	y/y Δ
WTR	Hold	$0.21	$0.18-0.22	$0.21	$0.19	11%	$0.25	-16%

Source: Company Inforation, Baseline, LBR Estimates

During the company's conference call, we will look for an update on:

Rate Cases: Unlike AWK, WTR does not release information about rate filing and approvals in between quarterly result announcements. We will therefore look for an update on: (a) $12M in rate cases that were pending as of 11/03/10, including $4.7M in New York and $3.2M in Virginia, and (b) rate cases filed since, including $43.2M in Pennsylvania and ~$5M in New Jersey.

Acquisitions: WTR is currently viewed as the industry leader in making tuck-in acquisitions with 17 purchases in 2009. On its 3Q09 conference call on 11/04/09, the company mentioned that it could make ten additional acquisitions before the end of the year, but has announced only two since that date. We will look for an update on these acquisitions and any additions to the pipeline. We expect the pace of acquisitions to accelerate going forward as small municipal and private systems are struggling in the current tough economic environment and with increasingly stringent water quality regulations.

Capex: On the last call, the company announced that capex will stay in the $300-310M range in FY10, broadly in-line with the FY09 level. We will look for any update to this outlook.

Rate Relief in Southern States: WTR's earnings were flat between FY05-FY08 mainly due to delays in obtaining rate increases in its southern operation (NC, SC, VA, FL and TX) that were acquired through the purchase of AquaSource in 2003 and Heater and Florida Water in 2004. Since these acquisitions, WTR has invested $223M in these states. Although the company has obtained at least one round of rate increases for all of these operations, the ROE earned in these states (0-7%) is still significantly below the maximum allowed (10-11%). This is mainly because regulators stagger rate increase to two or more rate cycles to limit the one-time rate increases experienced by the consumers. On the call, we will look for an update on WTR's plans to go in for a second round of rate increases in the southern states.

American States Water (AWR)

AWR has not yet announced the date for its earnings release and conference call yet. For 4Q09, we expect EPS of $0.40, in-line with consensus, and revenue of $91.5M vs. consensus of $88.4M. For FY09, we expect EPS of $1.85 vs. consensus of $1.84, and revenue of $366.2M vs. consensus of $360.0M.

Similar to CWT, AWR's revenues are not impacted by water conservation efforts and weather-related consumption variation because of WRAM.

4Q09 EPS Projections and Comparisons

		First Call Mean		LBR Estimate	Variance			
Ticker	Rating	4Q09E	Range	4Q09E	4Q08A	y/y Δ	3Q09A	y/y Δ
AWR	Hold	$0.40	$0.37-0.42	$0.40	$0.40	0%	$0.52	-23%

Source: Company Inforation, Baseline, LBR Estimates

During the company's conference call, we will look for an update on:

Rate Case: The California Public Utilities Commission (CPUC) is still processing AWR's $51.5M General Rate Case (GRC) for Regions II and III and the general office (GO). The CPUC did issue an unfavorable proposed decision for this case in November 2009, and AWR was working hard to get many of the issues turned. In our last communication, the company stated that it believed the CPUC was is in the process of revising the proposed decision and expected to have a decision by the end of January. Also, the CPUC did not approve an interim rate against the increase because of the negative inflation factor in 2009.

Fort Bragg Project: AWR management has previously pointed to a large construction project at Fort Bragg, NC, which is in the pipeline and is expected (by management) to be larger than the $20M Fort Bliss project performed in 2007. The Fort Bragg project, which could start in 1H10, could offer upside to our EPS estimate, as it is currently not included in our forecast. We will look for an update on possible start date for this project.

Military Base Business: We will look for an update on: (a) management's expectation of additional construction contract wins going forward, (b) the status of bids for new O&M contracts, and (c) the status of requests for equitable adjustment and price redeterminations at existing bases.

INVESTMENT THESES

AWK

We continue to rate AWK shares BUY with a $24 target price, as we see AWK as offering an attractive risk/reward with positive catalysts relative to the peer group. We believe AWK shares were trading at a discount partially due to the "RWE overhang." As we believe this overhang has now been removed, AWK's discounted valuation relative to the industry average should ease. However, our target price still incorporates a 14% discount to the peer group average. The shares are trading at 14.8x our FY10E EPS, relative to the peer group average of 18.5x. Viewed as the largest and most geographically diversified water utility in the U.S., AWK should benefit by investing to replace and expand the aging water infrastructure in the country. As such, the company is planning to spend $4-4.5B over the next five years, which should drive earnings growth over that time period. As the company benefits from rate catch-ups and increased capex after years of rate stay-outs and underinvestment under RWE ownership, we believe low-teens percent EPS growth should lead to multiple expansion over the next one-to-two years.

CWT

We continue to rate CWT shares BUY with a $45 target price, which represents 20.5x our FY10E EPS of $2.20, in-line with the company's historical average. We like CWT's position in the regulatory favorable California market. Furthermore, CWT's $120M+ in FY10E capex could potentially drive meaningful EPS growth in the next two-to-three years. On valuation, CWT shares are trading at 16.3x our FY10E EPS of $2.20, which we believe to be conservative when compared to the industry average of 18.5x and the company's historical average of 20.5x. Additionally, while CWT has historically seen higher earnings volatility from variation in water consumption, regulatory changes in California (WRAM and MBCA implementation) have helped to reduce earnings volatility and provide better visibility. In summation, rate relief and improved ROE (we are modeling 10.9%) in FY10E, greater than the company's 8.9% five-year average, provide positive potential catalysts going forward.

WTR

We continue to rate WTR shares NEUTRAL with a positive catalyst coming from improved ROEs from under earning systems that were acquired in the southern states in 2003-04. Overall, we see downside risk potential to WTR as fairly limited as the company is trading at a 22% discount to its historical forward P/E of 23x. Additionally, at 2.6x price-to-book, it is trading below its historical average of 2.9x (on book value of $7.91/share). 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 have difficulty justifying the magnitude of WTR's valuation premium when compared to other names under coverage.

AWR

We continue to rate AWR shares NEUTRAL as we see the upside potential related to rate relief as already largely reflected in the shares. At 16.2x our FY10E EPS of $1.97, AWR shares are trading below its historical 20x forward P/E average as well the peer group average of 18.5x. However, given the company's valuation relative to our preferred names in the space – AWK and CWT – we do not see as much upside potential at this time from current levels.

A principal potential driver of earnings growth would be the start-up of the Ft. Bragg, NC construction project and successful price redeterminations at other military bases, which we estimate could increase EPS by another 3%. However, due to limited visibility, we have not added these potential catalysts into our EPS forecasts. Our estimates do, however, include an average ROE of 10% from FY09E to FY11E vs. the company's historical 8.7% average. This is driven by an expectation of increased capital spending of $80M+ in FY10, in-line with FY09 levels. Since capex has grown at a CAGR of 12% from FY03-08, AWR should see rate relief leading to 6.8% EPS growth in FY10E and potentially 10.4% in FY11E. In the long-term, we like AWR, currently viewed as the fourth largest publicly traded domestic water utility, as we believe the WRAM/MBCA implementation in California has removed the quarterly earnings volatility caused by the changes in water consumption. We note that seasonal variation will still exist. We believe these mechanisms have somewhat reduced the single-state operational risk that AWK faced previously. However, we believe the benefits from the improved regulatory environment and earnings upside from the recently approved rate cases are already mostly priced into the shares.

VALUATION

AWK

AWK shares closed Friday at $22.16, which is 14.8x our FY10E EPS of $1.50 and 13.7x our FY11E EPS of $1.62. The shares are trading at a discount to the peer group average of 18.5x FY10E, and at 1.4x tangible book value compared to a peer group that trades over 1.7x, on average. Our target price of $24 is based on 16.0x our FY10E EPS, a valuation that remains at a discount to the peer group. However, we see multiple expansion from current levels as justified given AWK being currently viewed as the largest and most diversified publicly traded water utility in the U.S. and with the potential from earnings growth as the company catches up to insufficient rate increases during the past five-to-six years.

CWT

CWT shares closed Friday at $35.92, which is 16.3x our FY10E EPS of $2.20 and 14.5x our FY11E EPS of $2.48. The shares are trading at a discount to the company's historical normalized 20.5x average and normalized range of 17-27x forward P/E. Compared to CWT's water utility peers, the company usually trades at a discount, although this is narrowing as more predictable earnings streams from the implementation of WRAM and MCBA have removed some the unpredictability in earnings associated with the company's extensive geographic presence in California.

WTR

WTR shares closed Friday at $16.59, which is 17.9x our FY10E EPS of $0.93 and 16.2x our FY11E EPS of $1.02. The shares are trading at a discount to the company's historical 23x average and normalized range of 20-30x forward P/E.

AWR

At 16.2x our FY10E EPS of $1.97, AWR shares are trading below its historical 20x forward P/E average as well as the peer group average of 18.5x. AWR shares closed Friday at $32.05, which is 14.7x our FY11E EPS of $2.18.

RISKS

AWK

The potential downside risks to our investment thesis, rating, target price and estimates include, but are not limited to: 1) delays in rate case processing or lower rate increases by the regulators than our expectations; 2) 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; 4) a large acquisition at an excessive valuation (significantly above the rate base); and 5) a large goodwill impairment which could lead to a possible breach of debt covenants or regulatory requirements.

CWT

The potential downside risks to our investment thesis, rating, target price and estimates include, but are not limited to: 1) lower rate increase approvals by the California Public Utility Commission (CPUC) than our expectation; 2) a near-term run-up in raw material costs; and 3) large acquisition(s) at excessive valuation(s) (significantly above the rate base).

WTR

The 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).

The 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.

AWR

The potential downside risks to our investment thesis and estimates include, but are not limited to: 1) lower rate increase approvals by the California Public Utility Commission (CPUC) than our expectation; 2) increases in raw material costs; and 3) an acquisition of a large water system by the local government through eminent domain.

The potential upside risks to our investment thesis and estimates include, but are not limited to: 1) favorable rate case approvals; and 2) the commencement of the large "special" construction project at Fort Bragg, North Carolina, or any other base.

American Water Works — Quarterly Income Statement
Garik Shmois\Vishal Khetpal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

Fiscal Ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E	1Q11E	2Q11E	3Q11E	4Q11E
Regulated segment	419.3	509.6	471.6	462.8	449.5	527.2	609.7	502.1	497.1	549.9	621.0	518.8	529.6	600.7	665.2	528.6	566.2	642.5	727.8	621.2
% Increase			3.3%	11.2%	7.3%	3.6%	3.6%	2.5%	10.6%	5.3%	2.9%	5.3%	6.3%	9.3%	9.5%	5.5%	7.5%	7.0%	7.0%	7.0%
Non-Reg. Net Revenue	53.3	55.5	66.4	57.5	61.0	67.0	75.5	70.3	57.5	64.2	65.2	57.3	70.0	76.7	77.7	79.8	73.5	80.5	81.6	83.3
% Increase			0.4%	27.7%	14.4%	20.0%	0.4%	4.1%	-5.7%	-4.1%	-11.7%	-4.1%	21.7%	19.3%	19.2%	10.5%	5.0%	5.0%	5.0%	5.0%
Other	(4.8)	(5.4)	(5.2)	(3.5)	(4.3)	(5.4)	(5.1)	(3.9)	(4.7)	(5.8)	(6.6)	(5.8)	(6.2)	(6.0)	(6.8)	(5.8)	(6.7)	(6.4)	(7.3)	(6.2)
% Regulated Rev	-1.0%	-1.1%	-0.8%	-0.8%	-0.9%	-0.8%	-0.8%	-0.8%	-1.0%	-1.1%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%
Operating revenues	468.5	558.7	533.1	518.8	506.8	583.4	572.3	563.6	550.2	617.7	680.0	570.8	595.3	671.4	751.1	654.6	635.1	716.9	802.2	698.6
Production costs	51.1	60.0	80.5	53.0	64.2	72.0	84.1	67.7	60.5	77.2	86.7									
Employee related costs	109.8	116.2	112.6	121.6	126.6	121.4	127.7	139.9	132.5	133.2	129.5									
Operating supplies and services	53.8	63.9	83.8	51.8	65.5	65.7	72.1	74.8	56.5	55.6	60.1									
Maintenance materials and services	30.1	26.3	27.6	43.3	34.5	37.2	32.0	37.1	32.3	31.8	31.7									
Customer billing and accounting	8.3	5.1	8.6	12.2	7.4	11.0	10.4	11.2	10.0	10.2	12.7									
Other	9.5	13.0	11.5	12.1	8.2	10.7	12.1	19.0	12.5	12.7	9.5									
Operation and maintenance	262.6	298.4	328.3	336.1	311.2	320.6	342.1	335.2	314.4	330.6	340.8	330.9	330.2	353.2	365.3	358.7	350.1	372.2	385.3	378.7
Depreciation and amortization	54.6	68.1	69.7	54.4	69.4	67.3	68.4	71.6	68.5	73.2	74.9	73.2	75.3	77.3	79.4	81.5	81.4	81.7	81.7	81.1
General taxes	47.9	45.5	47.3	42.3	52.1	41.0	49.4	41.0	52.0	51.7	50.0	49.3	54.0	52.0	52.0	50.0	51.8	50.2	51.0	51.0
Loss (gain) on sale of assets	0.1	(6.2)	(0.7)	(0.5)	(0.3)	(0.2)	0.2	(1.0)	(0.2)	0.0	(0.6)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)
Impairment charges			243.2	256.0	750.0				450.0											
EBIT	73.3	151.5	(54.9)	(155.1)	(670.4)	151.7	111.8	119.3	(335.4)	157.2	211.4	137.7	133.7	188.2	254.8	164.1	149.3	205.5	182.7	187.4
Operating Margin (Excluding impairments)	15.6%	27.1%	29.5%	30.0%	15.7%	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Interest	71.1	70.2	68.7	71.1	70.0	70.1	71.7	72.7	72.0	73.7	74.1	73.5	74.7	75.2	75.9	76.0	79.2	80.4	81.5	82.2
Other income, net	(3.0)	(1.8)	(2.8)	(4.5)	(3.7)	(3.2)	(3.7)	(8.2)	(4.8)	(2.5)	(1.5)	(4.1)	(3.3)	(2.8)	(3.0)	(2.4)	(3.1)	(3.1)	(3.1)	(3.2)
Total other income (deductions)	68.2	68.5	65.0	66.5	66.2	67.0	65.0	64.5	67.1	71.1	72.6	69.4	71.4	72.0	73.0	74.6	76.0	77.3	78.4	79.6
EBT	4.1	82.6	(120.5)	(221.9)	(736.6)	75.7	145.8	54.6	(402.5)	86.1	141.8	68.4	62.3	116.4	180.9	89.5	73.1	131.6	104.3	107.8
Provision for income taxes	1.7	33.6	39.7	12.7	(7.1)	30.2	57.5	28.2	10.6	34.1	50.2	24.2	24.6	46.0	71.4	35.3	28.6	52.4	40.7	42.6
Implied Tax Rate (excl. goodwill impairment)	42%	40%	33%	29%	-1.0%	40%	39%	44%	23%	33.6%	35.4%	35.4%	39.5%	39.5%	39.5%	39.5%	39.5%	39.5%	39.5%	39.5%
Income (loss) from continuing operations	2.4	49.0	(160.2)	(234.5)	(729.5)	45.5	88.2	36.4	(413.1)	52.0	91.6	44.2	37.7	70.4	109.4	54.1	44.2	79.2	123.5	65.2
Less: income from discontinued operations, net of tax	(0.23)	0.81	0.03	0.03																
Net income (loss)	2.7	49.2	(160.2)	(234.5)	(729.5)	45.5	88.2	36.4	(413.1)	52.0	91.6	44.2	37.7	70.4	109.4	54.1	44.2	80.2	123.5	65.2
Diluted EPS from continuing operations	0.02	0.31	(1.00)	(1.47)	(4.56)	0.28	0.55	0.23	(2.58)	0.30	0.52	0.25	0.21	0.39	0.60	0.29	0.25	0.42	0.65	0.33
EPS excl. impairment & one-time expenses	0.02	0.31	0.52	0.17	0.11	0.28	0.55	0.23	0.19	0.30	0.52	0.25	0.21	0.39	0.60	0.29	0.23	0.42	0.63	0.33
Diluted Average shares	160.0	160.0	160.0	160.0	160.0	159.9	160.0	159.5	159.9	169.2	174.7	174.7	176.2	179.1	182.5	185.6	188.5	191.9	195.1	198.2
Financial Summary																				
Total Revenue growth			0.8%	12.4%	8.2%	5.5%	0.0%	2.7%	8.5%	4.0%	1.2%	0.9%	7.0%	9.6%	10.5%	10.0%	7.2%	6.0%	5.8%	6.0%
Non Regulated Revenue growth			0.4%	27.7%	14.5%	20.0%	11.5%	1.5%	[illegible]	[illegible]	10.2%	[illegible]	21.7%	19.5%	19.2%	10.6%	5.0%	5.0%	5.0%	5.0%
O&M/Revenue	60.3%	53.3%	61.5%	60.7%	61.4%	55.1%	59.8%	59.5%	57.1%	54.0%	50.1%	58.0%	55.5%	52.6%	48.6%	54.8%	55.0%	52.0%	48.0%	54.2%
General Taxes/Regulated Revenue	11.4%	8.9%	8.3%	8.7%	11.6%	8.4%	8.2%	8.6%	10.5%	8.3%	8.1%	8.9%	10.3%	8.7%	7.8%	8.7%	8.8%	8.5%	7.3%	8.4%
Adj. EBITDA	137.9	219.6	258.4	175.5	149.6	219.0	280.2	202.7	183.5	230.4	286.3	210.9	209.0	265.5	334.2	245.5	230.5	287.2	263.3	268.5
EPS growth, excluding goodwill impairment charge					620.8%	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	31.1%	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Source: Company reports, Longbow estimates

American Water Works— Annual Income Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	FY04A	FY05A	2006A	FY07A	FY08A	FY09E	FY10E	FY11E
Regulated Segment	1748.0	1836.1	1854.6	1987.6	2082.7	2202.1	2390.1	2560.1
% Increase		5.0%	1.0%	7.2%	4.8%	5.7%	8.5%	7.1%
Non-Regulated Revenue	290.0	310.8	248.5	242.7	272.2	254.3	304.3	319.5
% Increase		7.2%	-20.0%	-2.3%	12.2%	-6.6%	19.7%	5.0%
Other	-20.17	(10.1)	(10.0)	(16.0)	(18.0)	(22.6)	(23.9)	(25.6)
% Regulated Rev	-1.2%	-0.6%	-0.5%	-0.8%	-0.9%	-1.0%	-1.0%	-1.0%
Operating revenues	**2,017.9**	**2,136.7**	**2,093.1**	**2,214.2**	**2,336.9**	**2,433.7**	**2,670.5**	**2,854.0**
Production costs	248.5	262.6	264.4	278.1	288.6	294.5	312.4	331.1
Employee-related costs	407.7	408.8	446.2	463.4	505.6	520.8	560.8	596.5
Operating supplies and services	289.3	338.1	268.2	293.5	283.2	292.0	312.4	331.1
Maintenance materials and services	90.6	97.9	96.5	128.0	136.3	129.0	128.2	134.1
Customer billing and accounting	42.5	44.4	55.6	38.3	44.0	41.4	42.7	42.8
Other	43.4	49.8	43.6	45.3	46.1	46.2	50.7	51.4
Operation and maintenance	1122.0	1201.6	1174.5	1246.5	1303.8	1323.9	1407.4	1486.9
Depreciation and amortization	225.3	261.4	259.2	267.3	271.3	290.1	313.5	324.9
General taxes	170.2	183.3	185.1	183.3	199.1	204.1	209.1	214.1
Loss (gain) on sale of assets	(8.6)	(6.5)	0.1	(7.3)	(0.4)	(1.3)	(1.2)	(1.2)
Impairment charges	78.7	385.4	221.7	509.3	750.0	450.0	0.0	0.0
EBIT	**430.4**	**111.6**	**252.5**	**15.1**	**(186.9)**	**166.8**	**741.7**	**829.2**
Operating Margin (excluding impairment)	*25.2%*	*23.3%*	*22.7%*	*23.7%*	*24.1%*	*25.3%*	*27.8%*	*29.1%*
Interest	315.9	345.3	366.0	283.2	285.2	293.4	305.3	324.0
Other income, net	(11.0)	(9.5)	(4.5)	(12.5)	(21.5)	(13.2)	(12.6)	(12.6)
Total other income (deductions)	**305.0**	**335.7**	**361.5**	**270.6**	**263.7**	**280.2**	**292.7**	**311.4**
EBT	**125.4**	**(224.2)**	**(108.9)**	**(255.5)**	**(450.6)**	**(113.40)**	**449.0**	**517.8**
Provision for income taxes	66.3	51.0	46.9	86.8	111.8	119.1	177.4	204.5
Implied Tax Rate (excl. goodwill impairment)	32.5%	31.6%	41.6%	34.2%	37.3%	35.4%	39.5%	39.5%
Income (loss) from continuing operations	**59.1**	**(275.1)**	**(155.9)**	**(342.3)**	**(562.4)**	**(232.5)**	**271.6**	**313.3**
Loss (income) from discontinued operations, net of tax	124.0	49.9	6.4	0.6				
Net Income (loss)	**(64.9)**	**(325.0)**	**(162.2)**	**(342.8)**	**(562.4)**	**(232.5)**	**271.6**	**313.3**
Diluted EPS from continuing operations	0.37	(1.72)	(0.97)	(2.14)	(3.52)	(1.38)	1.50	1.62
EPS excl. impairment & one-time expenses	**0.86**	**0.69**	**0.41**	**1.04**	**1.17**	**1.28**	**1.50**	**1.62**
Diluted Average Shares	160.0	160.0	160.0	160.0	160.0	168.5	180.9	193.5
Financial Summary								
Total Revenue growth		5.9%	-2.0%	5.8%	5.5%	4.1%	9.7%	6.9%
Non-Regulated Revenue growth			-20.0%	-2.3%	12.2%	-6.6%	19.7%	5.0%
O&M/Revenue	55.6%	56.2%	56.1%	56.3%	55.8%	54.4%	52.7%	52.1%
Depreciation and amortization/ Net Fixed Asset				3.1%	2.9%	2.9%	2.8%	2.7%
Depreciation Growth		16.0%	-0.8%	3.1%	1.5%	7.0%	8.0%	3.7%
General Taxes/ Regulated Revenue	9.7%	10.0%	10.0%	9.2%	9.6%	9.3%	8.8%	8.4%
Adj. EBITDA	734.3	758.4	733.4	791.8	834.4	906.9	1,055.2	1,154.1
Interest Expense/ Average Net Debt			8.9%	6.2%	5.6%	5.5%	5.6%	5.9%
Interest Expense/Revenue	15.7%	16.2%	17.5%	12.8%	12.2%	12.1%	11.4%	11.4%
Net Income Growth (excl. goodwill impairment)		338.6%	-1.6%	180.1%	12.6%	16.0%	24.9%	15.3%
EPS growth, (excl. goodwill impairment)			-40.3%	153.8%	12.3%	9.4%	17.0%	7.8%
ROE (excl. goodwill & goodwill impairment)			2.3%	7.0%	8.3%	8.4%	9.2%	9.2%

Source: Company reports, Longbow estimates

California Water Service Group — Quarterly Earnings Statement

Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414

(dollars in millions, except per share data)

FY Ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E	1Q11	2Q11E	3Q11E	4Q11E
Total Revenue	71.6	95.8	113.9	85.9	72.9	105.6	131.7	100.1	86.6	116.7	139.2	107.3	93.3	121.5	145.1	112.1	107.5	135.7	159.3	126.3
Watet Production Costs	25.8	37.3	45.1	30.8	25.4	40.3	46.5	34.4	28.9	41.7	48.9	37.6	30.5	42.7	50.1	38.5	35.2	47.7	55.0	43.3
Administrative & General	12.6	14.3	14.7	12.7	13.4	13.8	15.0	17.2	18.9	19.4	19.1	19.4	19.5	19.6	19.8	19.9	20.7	21.5	22.3	23.1
Other Operations	11.1	11.0	11.8	12.5	12.1	12.8	12.9	13.4	12.5	14.3	14.6	15.0	13.2	14.7	15.0	15.5	15.2	16.4	16.4	17.4
Maintainence	4.5	5.2	4.2	4.4	4.1	4.9	3.8	6.1	4.6	4.3	4.4	4.4	4.4	4.4	4.4	4.4	4.5	4.6	4.7	4.8
Operations & Maintenance	54.0	67.8	75.8	60.2	55.0	71.9	78.2	71.1	64.8	79.7	87.0	76.4	67.7	81.4	89.3	78.2	75.6	90.2	98.4	88.6
Depreciation and Amortization	8.4	8.4	8.4	8.4	9.2	9.3	9.3	9.6	10.2	10.3	10.3	10.4	10.5	10.6	10.7	10.7	10.9	11.1	11.3	11.7
General Taxes	3.4	3.4	3.7	3.1	3.7	3.5	3.9	3.7	4.1	3.9	4.4	3.9	4.4	4.0	4.2	3.9	5.1	4.5	4.7	4.4
Total Expenses	65.8	79.6	87.9	71.8	67.9	84.7	91.4	84.3	79.1	93.9	101.7	90.7	82.6	96.1	104.2	92.9	91.6	105.8	114.4	104.7
Income from Operations	5.8	16.2	26.0	14.1	5.0	20.9	40.3	15.8	7.5	22.7	37.5	16.6	10.7	25.5	40.9	19.2	15.9	29.9	44.9	21.6
Operating Margin	8.1%	16.9%	22.8%	16.5%	6.9%	19.8%	30.6%	15.8%	8.7%	19.5%	27.0%	15.5%	11.5%	20.9%	28.2%	17.2%	14.8%	22.1%	28.2%	17.1%
Other Income & Expenses (net)	1.3	1.5	1.3	0.4	(0.1)	0.6	(0.7)	(0.6)	0.2	1.4	1.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7
Gain (loss) on sale of non-util property	0.0	(0.1)	0.0	2.6	0.0	0.0	0.0	0.0	0.6	0.1	(0.7)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
EBIT	7.1	17.6	27.2	17.1	4.9	21.5	39.6	15.2	8.4	24.2	38.5	17.3	11.3	26.1	41.6	19.9	16.5	30.6	45.6	22.2
EBIT (%)	9.9%	18.3%	23.9%	20.0%	6.7%	20.4%	30.0%	15.2%	9.6%	20.7%	27.7%	16.1%	12.2%	21.5%	28.7%	17.7%	15.4%	22.5%	28.6%	17.6%
Interest Expense	4.4	4.5	4.5	3.7	4.6	4.7	4.2	3.7	4.4	5.3	5.5	5.0	5.5	5.3	5.3	4.9	6.2	5.9	5.9	5.5
Income Before Taxes	2.6	13.1	22.8	13.4	0.3	16.8	35.4	11.4	4.0	18.9	33.0	12.3	5.8	20.8	36.3	15.0	10.3	24.7	39.7	16.7
Provision for Income Taxes	1.1	5.4	8.9	5.4	0.1	6.7	13.2	4.1	1.6	6.8	13.5	4.8	2.3	8.0	14.0	5.8	4.0	9.5	15.3	6.4
Implied Tax Rate	40.3%	40.9%	39.3%	40.0%	40.3%	39.7%	37.3%	36.0%	39.3%	36.0%	40.9%	38.7%	38.5%	38.5%	38.5%	38.5%	38.5%	38.5%	38.5%	38.5%
Net Income	1.6	7.7	13.8	8.0	0.2	10.1	22.2	7.3	2.4	12.1	19.5	7.5	3.6	12.8	22.3	9.2	6.4	15.2	24.4	10.3
Preferred Dividends	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Net Income	1.6	7.7	13.8	8.0	0.2	10.1	22.2	7.3	2.4	12.1	19.5	7.5	3.6	12.8	22.3	9.2	6.4	15.2	24.4	10.3
EPS (fully diluted)	0.07	0.37	0.67	0.39	0.01	0.48	1.06	0.35	0.12	0.58	0.94	0.36	0.17	0.59	1.01	0.41	0.28	0.67	1.07	0.45
Weighted Avg. Shares	20.7	20.7	20.7	20.7	20.7	20.7	20.7	20.7	20.8	20.8	20.7	20.8	21.2	21.6	22.0	22.4	22.5	22.6	22.7	22.8
Financial Summary (values in %)																				
Revenue Growth	9.7%	18.1%	5.7%	6.5%	1.9%	10.2%	15.7%	16.6%	18.8%	10.5%	5.7%	7.2%	7.7%	4.2%	4.3%	4.5%	15.2%	11.7%	9.8%	12.6%
Operations & Maintenance/Revenue	75.4%	70.8%	66.6%	70.1%	75.4%	68.1%	59.4%	71.0%	74.8%	68.3%	62.5%	71.2%	72.6%	67.0%	61.5%	69.8%	70.3%	66.4%	61.8%	70.2%
Gen. taxes/Revenue	4.8%	3.6%	3.3%	3.6%	5.1%	3.3%	3.0%	3.7%	4.7%	3.4%	3.1%	3.6%	4.7%	3.3%	2.9%	3.5%	4.7%	3.3%	2.9%	3.5%
EBIT (% of rev.)	9.9%	18.3%	23.9%	20.0%	6.7%	20.4%	30.0%	15.2%	9.6%	20.7%	27.7%	16.1%	12.2%	21.5%	28.7%	17.7%	15.4%	22.5%	28.6%	17.6%
EBIT/Interest expense	1.6	3.9	6.1	4.6	1.1	4.6	9.5	4.1	1.9	4.5	7.0	3.5	2.1	4.9	7.8	4.1	2.7	5.2	7.7	4.1
EPS growth	75.0%	20.5%	-2.6%	23.6%	-87.2%	28.5%	58.8%	-9.2%	1205.6%	21.3%	-11.4%	2.7%	45.5%	1.8%	8.0%	13.8%	66.7%	13.4%	6.0%	9.5%

Source: Company reports, Longbow estimates

California Water Service Group — Annual Earnings Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY Ends December 31	FY04	FY05	FY06	FY07	FY08	FY09E	FY10E	FY11E
Total Revenue	**315.6**	**320.7**	**334.7**	**367.1**	**410.3**	**449.8**	**472.1**	**528.8**
Watet Production Costs	119.1	115.7	124.3	138.9	146.6	157.0	161.8	181.2
Administrative & General	47.1	48.8	52.8	54.3	59.4	76.7	78.8	87.5
Other Operations	39.9	40.0	42.9	46.3	51.2	56.5	58.4	65.5
Maintainence	13.2	15.2	15.6	18.3	19.0	17.8	17.6	18.6
Operations & Maintenance	219.4	219.7	235.6	257.8	276.2	308.0	316.6	352.8
Depreciation and Amortization	26.1	28.7	30.7	33.6	37.3	41.2	42.5	45.0
General Taxes	11.5	12.6	12.9	13.7	14.8	16.2	16.6	18.7
Total Expenses	**257.0**	**261.0**	**279.1**	**305.0**	**328.3**	**365.4**	**375.7**	**416.5**
Income from Operations	**58.6**	**59.7**	**55.6**	**62.1**	**82.0**	**84.4**	**96.3**	**112.3**
Operating Margin	**18.6%**	**18.6%**	**16.6%**	**16.9%**	**20.0%**	**18.8%**	**20.4%**	**21.2%**
Other Income & Expenses (net)	2.4	3.0	3.4	4.4	(0.9)	4.0	2.6	2.6
Gain (loss) on sale of non-util property	0.0	2.3	0.3	2.5	0.0	(0.0)	0.0	0.0
EBIT	**61.0**	**64.9**	**59.4**	**69.0**	**81.1**	**88.4**	**98.9**	**114.9**
EBIT (%)	**19.3%**	**20.2%**	**17.7%**	**18.8%**	**19.8%**	**19.7%**	**21.0%**	**21.7%**
Interest Expense	17.8	17.7	17.0	17.1	17.2	20.2	21.0	23.5
Income Before Taxes	43.1	47.2	42.4	51.9	63.9	68.2	78.0	91.4
Provision for Income Taxes	**17.1**	**20.0**	**16.8**	**20.7**	**24.1**	**26.6**	**30.0**	**35.2**
Implied Tax Rate	**39.6%**	**42.4%**	**39.7%**	**39.9%**	**37.7%**	**39.1%**	**38.5%**	**38.5%**
Net Income	26.0	27.2	25.6	31.2	39.8	41.5	48.0	56.2
Preferred Dividends	-	-	-	-	-	-	-	-
Net Income	**26.0**	**27.2**	**25.6**	**31.2**	**39.8**	**41.5**	**48.0**	**56.2**
EPS (fully diluted)	**1.46**	**1.47**	**1.34**	**1.50**	**1.90**	**2.00**	**2.20**	**2.48**
Weighted Avg. Shares	17.7	18.4	18.9	20.7	20.7	20.8	21.8	22.7
Financial Summary (values in %)								
Revenue Growth	13.9%	1.6%	4.4%	9.7%	11.8%	9.6%	5.0%	12.0%
Operations & Maintenance/Revenue	69.5%	68.5%	70.4%	70.2%	67.3%	68.5%	67.1%	66.7%
(Dep + Amort)/Net Fixed Assets	3.4%	3.6%	3.6%	3.6%	3.7%	3.7%	3.6%	3.6%
Gen. taxes/Revenue	3.6%	3.9%	3.9%	3.7%	3.6%	3.6%	3.5%	3.5%
EBIT (% of rev.)	19.3%	20.2%	17.7%	18.8%	19.8%	19.7%	21.0%	21.7%
Interest Expense/Net Debt	6.7%	6.4%	6.0%	5.9%	5.5%	5.5%	5.2%	5.6%
EBIT/Interest expense	3.4	3.7	3.5	4.0	4.7	4.4	4.7	4.9
Net Income Growth	34.0%	4.6%	-6.0%	21.8%	27.7%	4.4%	15.4%	17.3%
EPS growth	20.4%	0.7%	-8.8%	11.9%	26.7%	5.3%	10.0%	12.9%
Average ROE	9.7%	9.3%	7.5%	8.1%	10.1%	10.1%	10.9%	11.8%

Source: Company reports, Longbow estimates

Aqua America - Annual Income Statement
Garik Shmois/ Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08
Total Operating Revenue	137.3	150.6	165.5	149.1	139.3	150.8	177.1	159.8
Operation & Maintenance	60.3	63.3	67.1	62.4	64.3	65.1	66.7	65.9
Depreciation	20.1	20.5	21.1	21.5	21.5	20.6	22.8	23.9
Amortization	1.2	1.2	1.2	1.2	1.2	1.0	1.8	1.5
General Taxes	11.9	10.8	10.8	11.8	12.1	10.8	11.2	10.6
Recovery of restructuring costs								
Total Expenses	93.6	95.9	100.1	96.9	99.1	97.6	102.5	102.0
Income from Operations	43.7	54.8	65.3	52.2	40.2	53.1	74.6	57.9
Operating Margin (%)	31.9%	36.4%	39.5%	35.0%	28.9%	35.2%	42.1%	36.2%
All. for Borrowed Funds Used in Const.	0.7	0.7	0.7	0.8	1.0	1.1	1.0	0.6
Gain (loss) on sale of other assets	0.1	0.3	0.3	2.8		0.6	0.5	0.5
Other								
EBIT	44.5	55.8	66.3	55.8	41.2	54.8	76.1	59.0
EBIT (%)	32.4%	37.1%	40.0%	37.5%	29.6%	36.3%	43.0%	36.9%
Interest Expense	16.5	16.4	17.1	16.8	17.1	17.1	17.0	17.4
Income Before Taxes	28.0	39.4	49.2	39.0	24.0	37.7	59.1	41.7
Provision for Income Taxes	11.1	15.7	19.6	14.1	9.7	15.2	23.7	16.0
Implied Tax Rate	39.8%	39.8%	40.0%	36.1%	40.4%	40.2%	40.1%	38.4%
Net Income before extraord. Item	16.9	23.7	29.5	24.9	14.3	22.6	35.4	25.7
Reclassification adj. for gains reported in net income				(1.3)			(0.2)	
Unrealized gain on securities								
Unrealized holding gain on investments	0.0	0.2	0.9	-	-	0.2	0.0	
Minimum pension liability adjustment		-	-					
Comprehensive Income	16.9	23.9	30.4	23.6	14.3	22.7	35.2	25.7
Diluted Net Income Per Share	0.13	0.18	0.22	0.19	0.11	0.17	0.26	0.19
Weighted Avg. Shares	133.2	133.5	133.8	134.0	134.0	134.1	135.3	135.6
Financial Summary (values in %)								
Revenue Growth	16.4%	14.3%	12.6%	8.9%	1.4%	0.1%	7.0%	7.2%
Operations & Maintenance/Revenue	43.9%	42.0%	40.5%	41.9%	46.2%	43.2%	37.7%	41.2%
EBIT (% of rev.)	32.4%	37.1%	40.0%	37.5%	29.6%	36.3%	43.0%	36.9%
General taxes as % of revenue	8.7%	7.2%	6.6%	7.9%	8.7%	7.2%	6.3%	6.7%
EBITDA	65.9	77.5	88.5	78.6	63.8	76.4	100.7	84.4
Net Income Growth	1.8%	6.0%	8.0%	-3.2%	-15.0%	-5.0%	19.9%	3.0%
EPS Growth	0.0%	4.0%	7.1%	-3.6%	-15.5%	-5.3%	18.6%	1.8%

FY ends December 31	1Q09	2Q09	3Q09	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E	1Q11E	2Q11E	3Q11E	4Q11E
Total Operating Revenue	154.5	167.3	180.8	169.2	162.1	180.1	212.6	183.9	180.4	198.4	230.9	202.2
Operation & Maintenance	67.0	68.5	68.5	66.2	66.6	69.9	80.4	71.9	74.2	77.0	87.3	79.1
Depreciation	26.4	25.0	25.4	25.4	25.6	26.2	26.7	27.4	27.7	28.0	28.3	28.8
Amortization	2.8	3.1	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
General Taxes	11.6	11.9	12.4	11.8	12.2	12.6	12.8	12.9	13.5	13.9	13.9	14.2
Recovery of restructuring costs												
Total Expenses	107.7	108.5	109.4	106.4	107.4	111.7	122.8	115.2	118.4	121.8	132.4	125.0
Income from Operations	46.8	58.9	71.5	62.8	54.7	68.4	89.8	68.7	62.0	76.5	98.5	77.2
Operating Margin (%)	30.3%	35.2%	39.5%	37.1%	33.8%	38.0%	42.2%	37.4%	34.4%	38.6%	42.6%	38.2%
All. for Borrowed Funds Used in Const.	0.6	0.6	0.7	0.6	0.6	0.6	0.7	0.6	0.6	0.6	0.6	0.6
Gain (loss) on sale of other assets	0.1	0.1	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Other												
EBIT	47.5	59.5	72.4	63.5	55.5	69.1	90.5	69.5	62.8	77.3	99.2	77.9
EBIT (%)	30.8%	35.6%	40.0%	37.5%	34.2%	38.4%	42.6%	37.8%	34.8%	39.0%	43.0%	38.5%
Interest Expense	16.6	16.8	17.3	17.2	17.6	18.0	18.4	18.6	18.9	19.9	20.8	22.0
Income Before Taxes	30.9	42.7	55.1	46.3	37.9	51.1	72.1	50.9	43.9	57.4	78.4	55.9
Provision for Income Taxes	12.5	16.9	21.6	18.3	15.2	20.5	28.9	19.8	17.6	22.9	31.4	21.8
Implied Tax Rate	40.5%	39.5%	39.3%	39.5%	40.0%	40.0%	40.0%	39.0%	40.0%	40.0%	40.0%	39.0%
Net Income before extraord. Item	18.4	25.9	33.5	28.0	22.7	30.7	43.3	31.0	26.3	34.4	47.0	34.1
Reclassification adj. for gains reported in net income		0.0										
Unrealized gain on securities												
Unrealized holding gain on investments	0.0	0.2	(0.1)									
Minimum pension liability adjustment												
Comprehensive Income	18.4	26.1	33.3	28.0	22.7	30.7	43.3	31.0	26.3	34.4	47.0	34.1
Diluted Net Income Per Share	0.14	0.19	0.25	0.21	0.17	0.22	0.31	0.22	0.19	0.25	0.34	0.24
Weighted Avg. Shares	135.9	135.9	136.3	136.4	136.8	137.3	137.7	138.2	138.2	138.6	139.1	139.5
Financial Summary (values in %)												
Revenue Growth	10.9%	11.0%	2.1%	5.9%	4.9%	7.6%	17.6%	8.7%	11.3%	10.2%	8.6%	10.0%
Operations & Maintenance/Revenue	43.4%	41.0%	37.9%	39.1%	41.1%	38.8%	37.8%	39.1%	41.1%	38.8%	37.8%	39.1%
EBIT (% of rev.)	30.8%	35.6%	40.0%	37.5%	34.2%	38.4%	42.6%	37.8%	34.8%	39.0%	43.0%	38.5%
General taxes as % of revenue	7.5%	7.0%	107.0%	7.0%	7.5%	7.0%	6.0%	7.0%	7.5%	7.0%	6.0%	7.0%
EBITDA	76.7	87.5	100.8	91.9	84.1	98.3	120.2	99.9	93.5	108.3	130.5	109.7
Net Income Growth	28.3%	14.6%	-5.4%	9.2%	23.8%	18.7%	29.3%	10.8%	15.9%	12.2%	8.7%	10.0%
EPS Growth	26.5%	13.0%	-6.1%	8.5%	22.9%	17.6%	28.0%	9.3%	14.7%	11.1%	7.6%	8.9%

Source: Company reports and Longbow estimates

Aqua America - Annual Income Statement
Garik Shmois/ Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	FY04A	FY05A	FY06A	FY07A	FY08A	FY09E	FY10E	FY11E
Total Operating Revenue	**442.0**	**496.8**	**533.5**	**602.5**	**627.0**	**671.9**	**738.7**	**811.9**
Operation & Maintenance	178.3	203.1	219.6	253.1	262.1	270.2	288.8	317.5
Depreciation	54.6	60.7	70.9	83.2	88.8	102.2	105.9	112.8
Amortization	4.3	4.7	4.1	4.8	5.5	11.8	12.0	12.0
General Taxes	27.6	31.7	33.3	45.4	44.7	47.7	50.4	55.4
	-		-					
Total Expenses	**264.8**	**300.3**	**327.9**	**386.5**	**401.2**	**432.0**	**457.1**	**497.7**
Income from Operations	**177.2**	**196.5**	**205.6**	**216.0**	**225.8**	**239.9**	**281.6**	**314.2**
Operating Margin (%)	**40.1%**	**39.6%**	**38.5%**	**35.9%**	**36.0%**	**35.7%**	**38.1%**	**38.7%**
Allow. for Borrowed Funds Used in Const.	2.3	2.4	3.9	3.0	3.7	2.5	2.6	2.6
Gain (loss) on sale of other assets	1.3	1.2	1.2	3.5	1.6	0.5	0.5	0.5
Other	-	-	-	-				
EBIT	**180.8**	**200.1**	**210.7**	**222.5**	**231.1**	**242.9**	**284.7**	**317.2**
EBIT (%)	**40.9%**	**40.3%**	**39.5%**	**36.9%**	**36.9%**	**36.2%**	**38.5%**	**39.1%**
Interest Expense	48.7	52.1	58.4	66.9	68.6	67.9	72.6	81.6
Income Before Taxes	132.1	148.1	152.3	155.5	162.5	175.0	212.1	235.6
Provision for Income Taxes	**52.1**	**56.9**	**60.2**	**60.5**	64.6	69.3	84.3	93.7
Implied Tax Rate	**39.4%**	**38.4%**	**39.6%**	**38.9%**	**39.7%**	**39.6%**	**39.8%**	**39.8%**
Net income	80.0	91.2	92.0	95.0	97.9	105.7	127.7	141.9
Reclassification adj. for gains reported in net incom	(0.2)	-	-	(1.3)	(0.2)			
Unrealized gain on securities	0.1	-	-	-				
Unrealized holding gain on investments	-	-	0.2	1.1	0.2	0.1	-	-
Minimum pension liability adjustment	(1.7)	(1.3)	3.1		-	-	-	-
Comprehensive Income	**78.1**	**89.8**	**95.3**	**94.8**	**97.9**	**105.8**	**127.7**	**141.9**
Diluted Net Income Per Share	**0.64**	**0.71**	**0.70**	**0.71**	**0.73**	**0.78**	**0.93**	**1.02**
Weighted Avg. Shares	125.7	129.2	131.8	133.6	134.7	136.1	137.5	138.8
Financial Summary (values in %)								
Revenue Growth	20.4%	12.4%	7.4%	12.9%	4.1%	7.2%	9.9%	9.9%
Operations & Maintenance/Revenue	40.3%	40.9%	41.2%	42.0%	41.8%	40.2%	39.1%	39.1%
Dep/Net Fixed Asset	3.0%	2.9%	3.1%	3.3%	3.2%	3.4%	3.3%	3.3%
Depreciation Growth	12.5%	11.3%	16.7%	17.3%	6.7%	15.1%	3.6%	6.5%
General taxes as % of revenue	6.2%	6.4%	6.2%	7.5%	7.1%	7.1%	6.8%	6.8%
Interest Exp/ Average Net Debt	5.6%	5.3%	5.8%	5.9%	5.2%	5.2%	5.3%	5.6%
Interest Expense/Revenue	11.0%	10.5%	11.0%	11.1%	10.9%	10.1%	9.8%	10.1%
EBITDA	239.7	265.6	285.7	310.5	325.4	356.9	402.6	442.0
Net income growth	13.0%	13.9%	0.9%	3.3%	3.1%	8.0%	20.8%	11.1%
Average ROE	11.4%	11.7%	10.6%	10.0%	9.6%	9.8%	11.3%	11.8%
EPS Growth (ex special items and FAS 123)	7.0%	10.9%	-1.0%	1.9%	2.2%	6.8%	19.6%	10.0%

Source: Company reports and Longbow estimates

American States Water — Quarterly Earnings Statement

Garik Shmois/ Vishal Khetriwal, CFA
Longbow Research
216-525-8414

(dollars in millions, except per share data)

FY ends December 31	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09E	1Q10E	2Q10E	3Q10E	4Q10E	1Q11E	2Q11E	3Q11E	4Q11E
Water	52.1	65.4	69.4	61.1	56.8	74.2	78.3	70.0	65.3	82.7	86.7	78.0	72.3	89.7	93.7	85.0
Electric	8.8	6.2	6.7	6.7	8.6	5.9	6.6	7.5	9.8	7.1	7.8	8.1	10.0	7.3	8.0	8.3
Contracted Services	8.1	8.7	9.2	16.4	14.2	13.5	16.6	14.0	12.0	12.0	12.0	12.0	12.0	12.0	12.0	12.0
Total Revenue	**68.9**	**80.3**	**85.3**	**84.2**	**79.6**	**93.6**	**101.5**	**91.5**	**87.1**	**101.8**	**106.5**	**98.0**	**94.3**	**109.0**	**113.7**	**105.2**
Expenses																
Supply Costs	16.1	20.5	24.2	20.0	19.9	23.5	28.3	22.9	22.7	26.2	31.3	25.2	24.7	28.1	33.5	27.1
Gen. & Admin. expenses	14.8	14.9	16.3	16.6	16.9	15.5	17.0	17.2	17.6	18.0	18.4	18.8	19.2	19.6	20.0	20.4
Other O&M	11.8	11.8	11.4	11.4	11.2	11.1	11.7	11.6	12.1	11.8	12.1	12.3	12.9	12.4	12.7	12.9
ASUS Construction Expenses	3.9	4.4	5.1	10.4	8.4	7.8	9.3	9.1	7.8	7.8	7.8	7.8	7.8	7.8	7.8	7.8
Gain on sale of water rights/property					(0.0)		0.76									
Unrealized loss(gain) on purch pwr contracts	(2.8)	(1.7)	3.7	(0.8)												
Total Operation & Maintenance	**43.8**	**50.1**	**60.8**	**57.7**	**56.4**	**57.9**	**67.1**	**60.8**	**60.2**	**63.8**	**69.6**	**64.1**	**64.6**	**68.0**	**74.0**	**68.3**
Depreciation & Amortization	7.8	7.8	7.9	8.1	8.4	8.4	8.4	8.7	8.7	8.8	9.0	9.1	9.2	9.3	9.3	9.4
General Taxes	2.9	2.8	3.5	3.1	3.4	2.7	3.6	3.6	3.7	3.0	3.9	3.9	3.9	3.2	4.1	4.1
Total Expenses	**54.5**	**60.7**	**72.1**	**68.9**	**68.19**	**69.0**	**79.0**	**73.1**	**72.5**	**75.6**	**82.4**	**77.0**	**77.7**	**80.4**	**87.4**	**81.8**
Income from Operations	**14.5**	**19.6**	**13.1**	**15.3**	**11.4**	**24.5**	**22.5**	**18.4**	**14.6**	**26.2**	**24.0**	**21.0**	**16.6**	**28.5**	**26.3**	**23.5**
Operating Margin	21.0%	24.4%	15.4%	18.2%	14.3%	26.2%	22.1%	20.1%	16.8%	25.7%	22.6%	21.4%	17.6%	26.2%	23.1%	22.3%
Other Inc. (loss)	0.1	0.0	(0.0)	(7.7)	(0.0)	0.1	0.0									
EBIT	**14.6**	**19.6**	**13.1**	**7.6**	**11.4**	**24.6**	**22.5**	**18.4**	**14.6**	**26.2**	**24.0**	**21.0**	**16.6**	**28.5**	**26.3**	**23.5**
EBIT (%)	21.1%	24.4%	15.4%	9.0%	14.3%	26.3%	22.2%	20.1%	16.8%	25.7%	22.6%	21.4%	17.6%	26.2%	23.1%	22.3%
Interest Expense	5.0	4.5	5.1	4.8	5.1	5.4	5.7	5.7	5.8	5.8	5.9	5.9	6.3	6.4	6.5	6.4
Income Before Taxes	**9.6**	**15.1**	**8.0**	**2.8**	**6.3**	**19.2**	**16.8**	**12.7**	**8.9**	**20.3**	**18.1**	**15.1**	**10.3**	**22.2**	**19.7**	**17.0**
Provision for Income Taxes	4.3	5.8	3.4	(0.1)	1.4	7.7	7.1	5.2	3.6	8.3	7.4	6.2	4.2	9.0	8.0	6.9
Implied Tax Rate	44.5%	38.4%	42.9%	-3.2%	21.7%	40.2%	42.3%	40.8%	40.8%	40.8%	40.8%	40.8%	40.8%	40.8%	40.8%	40.8%
Net Income	5.3	9.278	4.6	2.9	4.9	11.5	9.7	7.5	5.2	12.1	10.7	9.0	6.1	13.1	11.7	10.1
EPS (fully diluted)	0.30	0.53	0.26	0.16	0.28	0.64	0.52	0.40	0.28	0.64	0.57	0.48	0.33	0.70	0.62	0.54
EPS (fully diluted, ex one-time items)	**0.30**	**0.47**	**0.39**	**0.40**	**0.28**	**0.64**	**0.52**	**0.40**	**0.28**	**0.64**	**0.57**	**0.48**	**0.33**	**0.70**	**0.62**	**0.54**
Weighted Avg. Shares	17.4	17.3	17.3	17.4	17.4	18.0	18.6	18.7	18.7	18.7	18.7	18.8	18.8	18.8	18.8	18.9
Financial Summary (values in %)																
Water revenue growth	3.5%	7.5%	6.0%	-0.3%	9.0%	13.4%	12.9%	14.6%	15.0%	11.5%	10.7%	11.3%	10.7%	8.5%	8.1%	9.0%
Electric revenue growth	-0.7%	-0.8%	7.2%	-6.9%	-1.9%	-5.2%	-2.7%	12.0%	13.9%	20.4%	18.3%	8.0%	2.0%	2.8%	2.6%	2.5%
Contracted Services growth	-38.4%	-28.2%	123%	195%	76%	54.6%	81.8%	-14.7%	-15.4%	-11.2%	-27.9%	-14.3%	0.0%	0.0%	0.0%	0.0%
Total Revenue growth	-4.6%	1.3%	12.4%	13.8%	15.5%	16.5%	19.0%	8.7%	9.4%	8.8%	4.9%	7.1%	8.3%	7.1%	6.8%	7.3%
Operations & Maintenance/Revenue	63.5%	62.4%	71.3%	68.5%	70.9%	61.9%	66.1%	66.4%	69.1%	62.7%	65.4%	65.3%	68.5%	62.4%	65.1%	64.9%
Supply Costs/Revenue (excl. Military Base)	26.5%	28.7%	31.8%	29.5%	30.4%	29.4%	33.4%	29.5%	30.2%	29.2%	33.2%	29.3%	30.0%	29.0%	33.0%	29.1%
Gen. & Admin./Revenue	21.5%	18.6%	19.1%	19.8%	21.2%	16.6%	16.8%	18.8% #	20.2%	17.7%	17.3%	19.2% #	20.4%	18.0%	17.6%	19.4%
Other O&M/Revenue	17.1%	14.7%	13.4%	13.6%	14.1%	11.8%	11.5%	12.7%	13.9%	11.6%	11.3%	12.5%	13.7%	11.4%	11.1%	12.3%
General Taxes/Revenue	4.2%	3.5%	4.1%	3.7%	4.3%	2.9%	3.5%	4.0%	4.2%	2.9%	3.6%	3.9%	4.1%	2.9%	3.6%	3.9%
EPS Growth	-3.2%	9.3%	-17.0%	15%	-5.3%	36.2%	33.4%	0%	-1.2%	0.6%	10.0%	18%	16.0%	8.4%	8.5%	12%

Source: Company reports, Longbow estimates

American States Water — Annual Earnings Statement
Garik Shmois/ Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	2004A	2005A	2006A	2007	2008	2009E	2010E	2011E
Water	200.6	205.5	219.2	237.9	247.9	279.3	312.6	340.6
Electric	25.6	27.2	29.3	28.6	28.4	28.6	32.8	33.6
Contracted Services	1.8	3.5	20.1	34.9	42.4	58.3	48.0	48.0
Total Revenue	**228.0**	**236.2**	**268.6**	**301.4**	**318.7**	**366.2**	**393.4**	**422.2**
Expenses								
Supply Costs	81.1	71.9	76.2	78.2	80.9	94.6	105.5	113.5
Gen. & Admin. expenses	41.8	44.3	47.1	52.6	62.7	66.6	72.8	79.2
Other O&M	31.6	32.0	36.4	43.2	46.4	45.6	48.3	51.0
ASUS Construction Expenses			9.0	22.1	23.9	34.6	31.2	31.2
Gain on sale of water rights/property	(5.7)	0.0	(0.3)	(0.6)	0.0	0.7	0.0	0.0
Unrealized loss on purch power contracts	0.1	(5.4)	7.1	(2.1)	(1.6)			
Total Operation & Maintenance	**148.9**	**142.8**	**175.6**	**193.4**	**212.3**	**242.2**	**257.7**	**274.9**
Depreciation & Amortization	20.8	21.9	26.3	28.9	31.6	33.8	35.5	37.1
General Taxes	8.8	9.3	10.2	11.3	12.3	13.3	14.3	15.3
Total Expenses	**178.5**	**174.0**	**212.0**	**233.6**	**256.2**	**289.4**	**307.6**	**327.3**
Income from Operations	**49.5**	**62.3**	**56.6**	**67.7**	**62.5**	**76.8**	**85.8**	**94.8**
Operating Margin	21.7%	26.4%	21.1%	22.5%	19.6%	21.0%	21.8%	22%
Other Inc. (loss)	0.3	(0.0)	0.5	0.30	(7.6)	0.1	0.0	0.0
EBIT	**49.8**	**62.2**	**57.1**	**68.0**	**54.9**	**76.9**	**85.8**	**94.8**
EBIT (%)	0.2	0.3	0.2	0.2	0.2	0.2	0.2	0.2
Interest Expense	17.9	13.6	18.3	19.21	19.5	21.8	23.4	25.6
Income Before Taxes	**31.9**	**48.6**	**38.8**	**48.8**	**35.4**	**55.1**	**62.4**	**69.3**
Provision for Income Taxes	13.4	21.9	15.7	20.8	13.4	21.4	25.4	28.2
Implied Tax Rate	41.9%	45.0%	40.5%	42.6%	37.8%	38.9%	40.8%	40.8%
Net Income	18.5	26.7	23.1	28.0	22.0	33.7	37.0	41.0
EPS (fully diluted)	1.19	1.59	1.33	1.61	1.26	1.85	1.97	2.18
EPS (fully diluted, ex.one-time items)	**1.06**	**1.16**	**1.44**	**1.56**	**1.56**	**1.85**	**1.97**	**2.18**
Weighted Avg. Shares	15.6	16.8	17.1	17.2	17.4	18.2	18.7	18.8
Financial Summary (values in %)								
Water revenue growth	7.2%	2.4%	6.7%	8.5%	4.2%	12.6%	11.9%	9.0%
Electric revenue growth	4.5%	6.4%	7.5%	-2.4%	-0.5%	0.5%	14.7%	2.4%
Other	75.1%	96.1%	477.9%	73.5%	21.3%	37.7%	-17.7%	0.0%
Total Revenue growth	7.2%	3.6%	13.7%	12.2%	5.8%	14.9%	7.4%	7.3%
Operations & Maintenance/Revenue	65.3%	60.4%	65.4%	64.2%	66.6%	66.2%	65.5%	65.1%
Supply Costs/Revenue (excl. Military Base)	35.8%	30.9%	30.7%	29.4%	29.3%	30.7%	30.5%	30.3%
Gen. & Admin./Revenue	18.3%	18.7%	17.5%	17.5%	19.7%	18.2%	18.5%	18.8%
Other O&M/Revenue	13.8%	13.5%	13.5%	14.3%	14.6%	12.5%	12.3%	12.1%
General Taxes/Revenue	3.9%	4.0%	4.1%	4.2%	4.5%	4.3%	4.1%	4.1%
(Dep + Amort)/Net Fixed Assets	3.3%	3.3%	3.7%	3.9%	4.1%	4.4%	4.1%	4.1%
(Dep + Amort)/Revenue	9.1%	9.3%	9.8%	9.6%	9.9%	9.2%	9.0%	8.8%
Interest Expense/Avg. Net Debt	6.4%	4.8%	6.1%	6.3%	6.0%	7.6%	7.2%	7.4%
Interest Expense/Revenue	7.8%	5.8%	6.8%	6.4%	6.1%	6.0%	5.9%	6.1%
Average ROE	8.0%	10.4%	8.4%	9.6%	7.2%	9.8%	9.9%	10.3%
EPS growth, excluding one-time items	52.0%	9.4%	24.1%	8.3%	0.0%	18.5%	6.8%	10.4%

Source: Company reports, Longbow estimates

WATER INDUSTRY PEER VALUATION

($ in millions, except per share data)

Company	Ticker	FY End	Rating	Target	% Upside	Share Price	52 Week Hi	52 Week Lo	Mkt Cap	Revenue Last FY	Earnings per Share Last FY	Earnings per Share Current FY	Earnings per Share Next FY	P/E Current FY	P/E Next FY	Dividend Rate	Price/ Book
U.S. WATER UTILITIES																	
American States Water	**AWR**	**Dec.**	**Neutral**			**$ 32.05**	**$38.79**	**$29.76**	**$ 590**	**$ 319**	**1.85**	**1.97**	**2.18**	**16.2x**	**14.7x**	**3.3%**	**1.8x**
American Water Works	**AWK**	**Dec.**	**BUY**	**$24**	**8%**	**$ 22.16**	**$23.77**	**$16.22**	**$ 3,810**	**$ 2,337**	**1.28**	**1.50**	**1.62**	**14.8x**	**13.7x**	**3.8%**	**1.4x**
Aqua America	**WTR**	**Dec.**	**Neutral**			**$ 16.59**	**$21.00**	**$15.39**	**$ 2,274**	**$ 627**	**0.78**	**0.93**	**1.02**	**17.9x**	**16.2x**	**3.5%**	**2.6x**
Artesian Resources Corporation	ARTNA	Dec	NR			$ 17.42	$18.85	$12.81	$ 132	$ 56	0.94	*1.08*	*n/a*	16.1x	*n/a*	4.3%	1.3x
California Water Service Group	**CWT**	**Dec.**	**BUY**	**$45**	**25%**	**$ 35.92**	**$44.65**	**$33.49**	**$ 744**	**$ 410**	**2.00**	**2.20**	**2.48**	**16.3x**	**14.5x**	**3.3%**	**2.4x**
Connecticut Water Service	CTWS	Dec	NR			$ 22.53	$26.44	$17.31	$ 191	$ 61	1.23	*1.15*	*1.44*	19.6x	15.6x	4.1%	1.9x
Consolidated Water Co	CWCO	Dec	NR			$ 12.51	$21.29	$6.35	$ 188	$ 60	0.65	*0.83*	*0.8*	15.1x	15.6x	2.3%	1.5x
Middlesex Water Company	MSEX	Dec	NR			$ 16.42	$18.00	$11.64	$ 223	$ 91	0.69	*0.8*	*0.89*	20.5x	18.4x	4.4%	1.7x
Pennichuck Corporation	PNNW	Dec	NR			$ 19.90	$24.80	$17.10	$ 92	$ 31	0.58	*0.75*	*0.79*	26.5x	25.2x	3.6%	1.8x
Southwest Water Company	SWWC	Dec.	NR			$ 7.49	$6.55	$3.67	$ 170	$ 222	0.05	*0.36*	*n/a*	20.8x	*n/a*	2.9%	0.7x
York Water Company	YORW	Dec	NR			$ 13.45	$17.95	$9.74	$ 170	$ 33	0.63	*0.69*	*0.82*	19.5x	16.4x	3.8%	2.0x
U.S. Water Utility Average														18.5x	16.7x	3.6%	1.7x
EQUIPMENT/FILTRATION/TREATMENT SECTOR																	
Calgon Carbon Corp.	CCC	Dec.	NR			$ 13.39	$19.31	$10.93	$ 728	$ 400	0.53	*0.78*	*0.9*	17.2x	14.9x	0.0%	3.3x
Danaher	DHR	Dec.	NR			$ 71.93	$78.02	$47.73	$ 23,097	$ 11,185	3.53	*4.06*	*4.62*	17.7x	15.6x	0.2%	2.1x
ITT Technologies	ITT	Dec.	NR			$ 49.27	$56.95	$31.94	$ 8,961	$ 10,905	3.78	*4.06*	*4.49*	12.1x	11.0x	1.7%	2.3x
Layne Christensen	LAYN	Jan.	NR			$ 26.17	$35.14	$14.13	$ 501	$ 1,008	0.85	*0.95*	*1.45*	27.5x	18.0x	0.0%	0.7x
Mueller Water Products	MWA	Sept	NR			$ 5.26	$5.93	$1.48	$ 799	$ 1,428	-0.29	*0.03*	*0.15*	175.3x	35.1x	1.4%	1.9x
Nalco	NLC	Dec.	NR			$ 22.17	$26.63	$9.62	$ 3,054	$ 3,747	0.95	*1.36*	*1.65*	16.3x	13.4x	0.6%	7.5x
Pall Corp.	PLL	Jul.	NR			$ 34.82	$37.85	$18.20	$ 4,015	$ 2,329	1.77	*2.25*	*2.25*	15.5x	15.5x	1.9%	3.2x
Pentair	**PNR**	**Dec.**	**BUY**	**$37**	**30%**	**$ 31.13**	**$34.27**	**$17.23**	**$ 3,019**	**$ 2,692**	**1.47**	**1.87**	**2.32**	**16.6x**	**13.4x**	**2.5%**	**1.5x**
Watts Water Technologies	**WTS**	**Dec.**	**Neutral**			**$ 28.49**	**$32.96**	**$15.85**	**$ 1,044**	**$ 1,459**	**1.54**	**1.55**	**1.83**	**18.4x**	**15.6x**	**1.5%**	**1.1x**
Equipment/Filtration/Treatment Average (*ex BWTR and CCC)														35.2x	16.9x	1.1%	2.6x
WATER RESOURCES/ INFRASTRUCTURE																	
Insituform Technologies	INSU		NR			$ 21.36	$24.22	$11.42	$ 815	$ 537	1.03	*1.31*	*1.47*	16.1x	14.3x	0.0%	1.5x
Lindsay Manufacturing	LNN		NR			$ 39.45	$47.45	$20.89	$ 488	$ 336	1.11	*1.35*	*1.82*	25.7x	23.8x	0.8%	2.5x
Tetra Tech	TTEK		NR			$ 21.16	$32.00	$19.51	$ 1,304	$ 2,287	1.22	*1.15*	*1.32*	19.8x	15.9x	0.0%	2.5x
Water Resources/Infrastructure Average														20.5x	18.0x	0.3%	2.2x

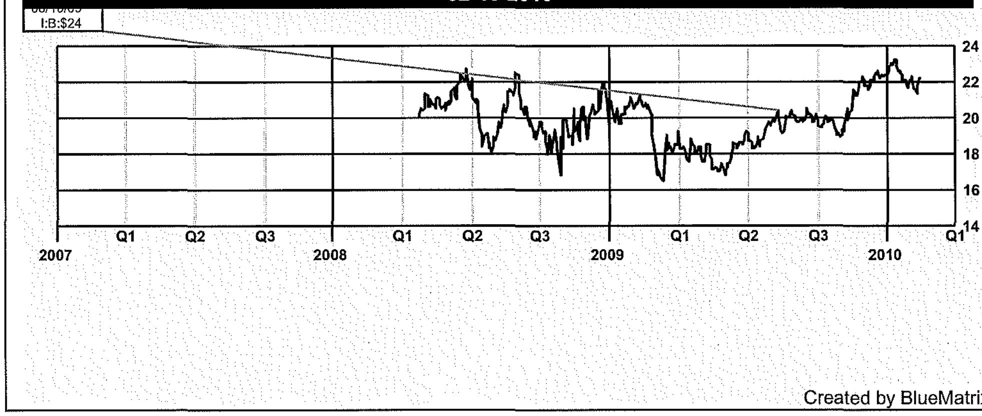
Relevant Indices		Share Price
Dow Jones Industrials	DJ30	$ 10,099
S&P 500	SPX	$ 1,076
Nasdaq Composite	NDX	$ 2,184

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.

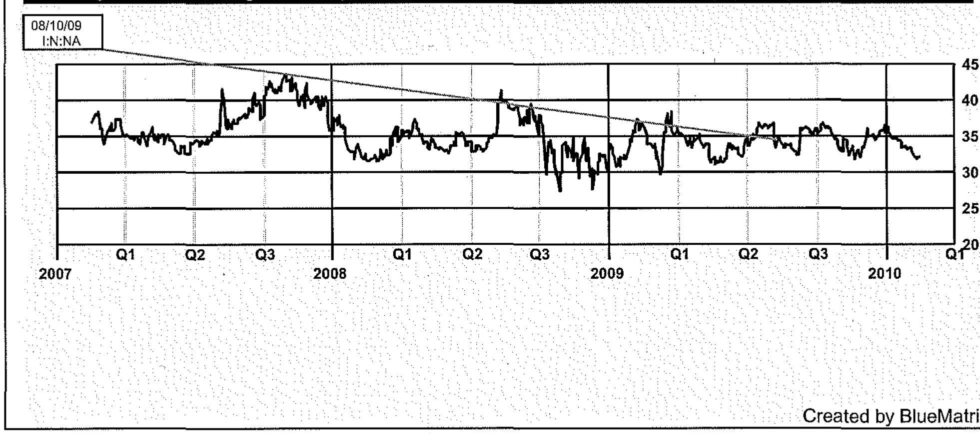
G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

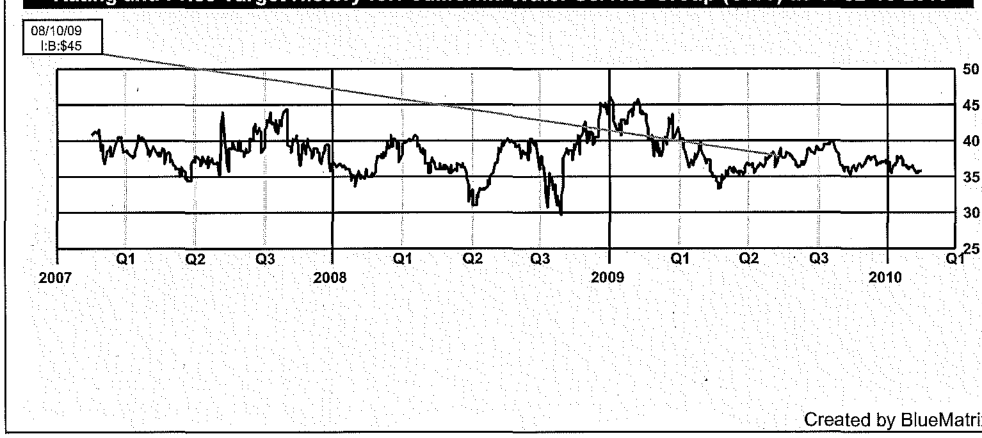
Rating and Price Target History for: American Water Works Company, Inc. (AWK) as of 02-15-2010



Rating and Price Target History for: American States Water Company (AWR) as of 02-15-2010

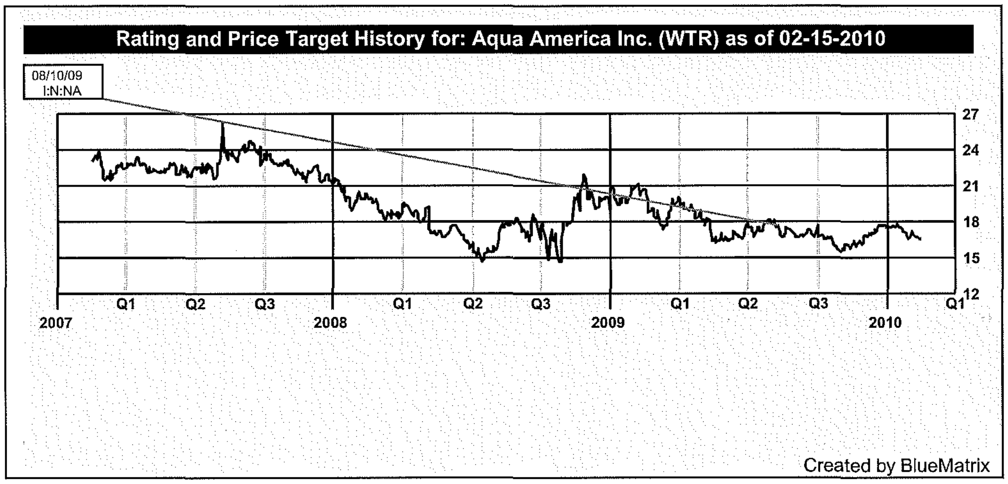


Rating and Price Target History for: California Water Service Group (CWT) as of 02-15-2010



G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469



APPENDIX

IMPORTANT DISCLOSURES

REGULATION ANALYST CERTIFICATION ("REG AC"): The Research Analyst(s) who prepared this research report hereby certifies that the views expressed in the research report accurately reflect the analyst(s) personal views about the subject companies and their securities. The Research Analyst(s) also certifies that the Analyst(s) have not been, are not, and will not be receiving direct or indirect compensation for expressing the specific recommendation(s) or view(s) in this report.

GENERAL DISCLOSURES: Longbow Securities does not make a market in any securities, nor does it hold a principal position in any security. Security prices in this report may either reflect the previous day's closing price or an intraday price, depending on the time of distribution. Consensus estimates are derived from either Thomson/Reuters, Bloomberg or Baseline. Designated trademarks and brands are the property of their respective owners.

SPECIFIC DISCLOSURES:

- Longbow Securities does not make a market in the securities of any company mentioned in this report, and is not a market maker in any securities. Nor does the firm hold a principal position in any security.

- As of the date of this report, no officer, director or stockholder of Longbow Securities, or any member of their immediate families, holds securities of any company mentioned in the report. In the event such persons purchase, hold or sell securities of a company mentioned in the report for their own account, any subsequent report shall disclose the fact of any such ownership or transactions.

- As of the date of this report, no employee of Longbow Securities serves on the Board of Directors of the subject security or any other security mentioned in this report.

- As of the date of this report, neither the Research Analyst nor a member of the Research Analyst's household has a financial interest in the securities of the subject company or any other security mentioned in this report.

- As of the date of this report, neither the Research Analyst nor a member of the Research

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

Analyst's household serves on the Board of Directors of the subject company or any other security mentioned in this report.

- As of the date of this report, neither Longbow Securities nor its affiliates beneficially own 1% or more of an equity security of the subject company or any other security mentioned in this report.

RATINGS DISTRIBUTIONS FOR LONGBOW RESEARCH:

Rating Category	Count	Percent
Buy	84	37.8%
Neutral	136	61.3%
Sell	2	0.9%

RATING SYSTEM:

"Buy" means that Longbow Securities expects total return to exceed 20% over a 12-month period.

"Neutral" means that Longbow Securities expects total return to be within a range of plus or minus 20% over a 12-month period.

"Sell" means that Longbow Securities expects total return to be negative by greater than 20% over a 12-month period.

Longbow Research's full research universe and related applicable disclosures can be obtained by calling (216) 986-0700 or via postal mail at: Editorial Department, Longbow Research, 6000 Lombardo Center, Suite #500, Independence, Ohio 44131.

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

Industry Update

LONGBOW Research
Tactical advantage through independent research

March 15, 2010

Analysts:
GARIK SHMOIS
T: 216-525-8414
E: gshmois@longbowresearch.com

VISHAL KHETRIWAL, CFA
T: 216-525-8469
E: vkhetriwal@longbowresearch.com

Industry: **WATER INFRASTRUCTURE**

Coverage:

Ticker	Rating	Price
AWK	BUY	$20.96
AWR	NEUTRAL	$32.50
CWT	BUY	$36.55
PNR	BUY	$34.16
WTR	NEUTRAL	$16.88
WTS	NEUTRAL	$31.18

The Water Rundown

IMPORTANT DISCLOSURES ARE LOCATED IN THE APPENDIX.

Summary of Water Utilites Survey

We recently completed our survey of municipal water systems and wholesale water suppliers in the states where our two largest utilities, American Water (AWK - BUY, TP $24) and Aqua America (WTR - NEUTRAL) under coverage currently have the largest presence. The states include New Jersey, Pennsylvania, Illinois, Missouri, Indiana, California and Texas. We asked our contacts for an update on YTD 2010 y/y changes in water consumption, water treatment costs and wholesale water prices.

By way of background, only inflation in water treatment costs have a direct financial impact on our covered utilities based in California – California Water (CWT - BUY, TP $43) and American States (AWR - NEUTRAL). Since the passage of the Water Recovery Adjustment Mechanism (WRAM) and Modified Cost Balancing Account (MCBA), revenues and costs have been decoupled from water consumption and wholesale water prices. Consequently, California water utilities are allowed to recover losses due to consumption declines or increases in water prices and vice-versa. However, an increase in wholesale prices encourages utilities to use more water from internal sources, with regulatory lag the principal risk to recovering the increased treatment costs. As a result, we view this survey as more impactful for AWK and WTR.

Key takeaways include:

- Water consumption, on average, was flat in the Northeast, was down 2-3% in the Midwest and Texas, and was down 10% in California. As the Northeast (PA & NJ), Midwest (OH, IL & IN), and Texas contributed at least 57%, 16% and 8%, respectively, of WTR's total revenues in 2009, we expect overall consumption to be flat to slightly down in 1Q10. We note that although WTR's total send-out was down 3-5% in 2009, we calculate that it lost less than $1.0M of revenues in 1Q09 due to lower water consumption (most of the impact was in the summer – 2Q and 3Q). We again expect variations in water consumption to have a limited impact on 1Q10 revenues. However, WTR should benefit in the middle of the year as weather-related comparisons ease.

  For AWK, the Northeast (PA & NJ), Midwest (MO, IL & IN), and California contributed at least 45%, 25% and 6%, respectively, of total revenues in 2009. The company lost $94M in revenues in 2009 from lower consumption by existing customers, although only $2M of that was in 1Q09. In our forecast for the company, we have modeled a $4.5M consumption-related decline in the current quarter. We see declining consumption trends from lower industrial demand driving what could be an admittedly worst-case scenario. We believe that in 1Q10, the loss could come between $2-5M. The company should not be impacted by the ~10% water sales drop seen in California as this should be hedged by WRAM.

- Water treatment costs increased roughly at the rate of inflation, 2-3% y/y. This was a little slower than the long-term average of above-inflation increases driven by increasing energy and chemical prices. WTR is viewed as an industry leader in efficiency ratio (O&M/revenues) and has a solid track-record of cost containment. The company's adjusted O&M expense increased only 1% in 2009, with 1% growth in the number of customers through acquisitions. The O&M expense was also impacted by 2-5% in lower water sales. The company has guided for a 50-100bp y/y increase in 2010 as a percentage of revenues. We have modeled at the higher end of this guidance range, reducing the O&M ratio from 40.3% in 2009 to 39.3% in 2010. Given the read from our survey, we are confident that WTR should be able to achieve this improvement.

  AWK's O&M expenses also increased by only 2% in 2009, aided by a 6% drop in water sales. As we are forecasting only a 1% drop in water sales in 2010, we see O&M expense increasing by 5%. We note that this is more or less in line with its historical average. However, due to operating leverage from rate increases that are already in the pipeline, we expect the O&M ratio to decline by 110bp, from 54.3% in 2009 to 53.2% in 2010.

- Wholesale water prices have mostly been flat across the country, with the exception of California, where rates are up ~10% y/y.

For further information, see the entire survey *Water Utilities: Survey Of Consumption and Cost Trends* published this morning.

END MARKET & INDUSTRY UPDATES

Mitsui, Marubeni Seek Income Streams in World's Waste Water – Mitsui & Co. and Marubeni Corp., Japan's second- and fifth-largest trading companies, plan to increase investments in water projects to benefit from global spending forecast to reach $1.2T by 2025. Mitsui, Marubeni and worldwide rivals are competing for water projects and government asset tenders to lock in stable income streams and tap a rise in spending in Asia, the Middle East and South America. China, the most populous nation, needs to build as many as 300 wastewater treatment plants a year to meet government targets, according to Global Water Intelligence. Mitsui and Tokyo-based Sumitomo have submitted bids for a $250M tender to build and operate a wastewater plant in Bahrain, according to Global Water's Web site. The bidding, involving six groups, should be decided by June. Global freshwater needs may triple by 2030 and Asia will be the region with the fastest-growing demand, according to General Electric Co., which provided water-filtration technology for the 2008 Beijing Olympics. Mitsubishi Corp. and plant engineer JGC Corp. agreed last month to take 33% stakes in Ebara Engineering Services Co. to expand into the global water market. Annual spending on water is forecast to grow to 111T yen (US$1.22T) by 2025, according to Toray Industries Inc., the world's No. 3 maker of reverse osmosis membranes used in water filtration. About 100T yen of that will be for the management of plants, Toray estimates.
Source: Bloomberg News

LBR Note: Entry of Japanese companies in to the already crowded water/ wastewater infrastructure space should bring increased competition, but could also promote innovation and help draw down costs.

A Better Vintage Of Tap Water–The economic downturn appears to have whetted consumers' appetite for tap water. The average per capita consumption of bottled water slipped an estimated 3.5% last year from 2008, according to Beverage Marketing Corp. Many consumers do not want their tap water au naturel, however. According to a Gallup poll released last year, pollution of drinking water is Americans' No. 1 environmental concern. Many express worries about the risk of diseases, including cancer, that can be associated with contaminants such as arsenic, chlorine and pharmaceuticals sometimes found in drinking water.
Source: WSJ Online

LBR Note: Decreases in bottled water usage is positive for companies manufacturing residential and commercial water treatment units. Pentair (PNR, BUY, TP $37) should benefit from this trend.

United Water Signs contract with East Providence to Upgrade and operate City's Wastewater Facilities – United Water announced it had reached agreement with the City of East Providence, RI, for a 10-year, design-build-operate (DBO) contract for the city's wastewater collection and treatment facilities, which provide service to roughly two-thirds of East Providence's 50,000 residents. The contract calls for United Water to begin operational responsibility for the system today, while also implementing $52.5M worth of infrastructure and treatment process upgrades necessary to bring the collection system and plant into compliance with new state Department of Environmental Management mandates. As a part of the agreement with the city, United Water will manage plant operations and improvements. This is expected to save the city $13M over what was budgeted to be spent under a traditional project delivery approach. Construction is slated to begin at the plant, which was built in 1954 and upgraded in the mid-1970s, before the end of the year with a completion deadline of September 2012. In addition to the renovations at the plant, United Water is scheduled to build a new pump station and a wastewater pipeline by August 2013.
Source: WaterTechOnline

LBR Note: Public-private partnerships (PPP), such as this, are becoming increasingly common in the U.S. water utilities sector. PPPs bring financial resources as well as managerial and technological expertise to city/municipal owner water system, while allowing private companies a bigger role in the sector which is ~ 85% municipally owned.

Drinking water projects meet Recovery Act deadline – Of the $6B allocated for drinking water and clean water state revolving funds (SRFs) by the American Reinvestment and Recovery Act, 100% was committed to signed contracts in time for the February 17 deadline. The Drinking Water SRF, which received an extra $2B appropriation from ARRA, has 1,348 project agreements signed with contracts executed. Construction has begun on more than 80% of those projects — 1,097 projects, valued at $1.5B. The drinking water projects exceeded the requirement that 20% of the projects be "green." The final tally showed 513 drinking water projects (valued at $539.1M) met the green requirements — 28.8%. Those projects were about 97% all-American, as the act required. Only 44 projects needed "Buy American" waivers, usually granted because the product was not available domestically or available in sufficient quantity or quality or the cost was "unreasonable."
Source: AWWA

LBR Note: AARA funding through the SRF program has done an excellent job in propping water infrastructure investment depressed by falling municipal tax receipts. Since construction on a majority of projects is still ongoing, it should continue to support spending in 2010 and 1H11.

WATER UTILITIES UPDATES

American States Water Reports 4Q Results – Last week, American States Water (AWR, Neutral) reported 4Q09 EPS of $0.18 vs. our estimate of $0.40 and consensus of $0.39. However, operating expenses included $3.8M from a legal settlement agreement, which reduced EPS by $0.12 on an after-tax basis. The rest of the miss was due to $6.3M lower water revenue and $1.8M higher maintenance expense vs. our expectations. Water revenues only increased 4% y/y in the quarter vs. a 12% increase from 1Q09-3Q09. Though water consumption fell by 8% y/y, it was offset by a $6.1M increase from Water Revenue Adjustment Mechanism (WRAM). Rate increases also added $1.4M to revenues. Electric revenues increased at a better than expected 17.5% y/y rate due to higher demand and rates increase approved in Oct, 2009. We were looking for a 12% increase. Contracted Services revenues decreased by $1.6M, broadly in line with our estimate, due to a decrease in construction activity. Construction activity decreased in Ft. Bliss, TX and military bases in VA after special projects occurred in 2008. However, construction increased at Ft. Bragg, NC. Water and electric gross profit increased by $2.3M due to rate increases over the last year. This contributed $0.07/share to earnings. An increase in the effective tax rate in 4Q09 due to changes between book and taxable income negatively impacted EPS by $0.08 vs. 4Q08 adj. EPS of $0.40. To view a full report on our thoughts, see *AWR: Reducing Estimates After 4Q09 Earnings; Maintain NEUTRAL published* March 12, 2010.
Source: Longbow Research Estimates, Company Reports

Virginia American Water files General Rate Case – Virginia American Water filed an application with the State Corporation Commission (SCC) requesting an increase in total revenues of $6.879M. If the company's application is approved in full, the proposed increase would increase the quarterly bill of a residential customer using 4,500 gallons per month in Alexandria by $4.98 ($1.66 per month) or approximately 5.4 cents per day; in Hopewell by $12.15 ($4.05 per month) or approximately 11.3 cents per day; and in Prince William by $7.41 ($2.47 per month) or approximately 8.1 cents per day.

Artesian Resources Corp (ARTNA, NR) – ARTNA announced that revenues for 2009 were $60.9M, up 8.4% from $56.2M in 2008. Net income was $7.3M, compared to $6.4M last year. Diluted net income per common share for 2009 rose 12.8% to $0.97 from $0.86 in 2008. Artesian's revenue increase in 2009 was partially due to a 17% increase in non-utility revenue, which climbed to $4.8M from $4.1M in 2008. Revenues from water sales also increased as a result of the full-year implementation of a 15% rate increase, which was made permanent in 2009 with the settlement of the Company's rate case in Delaware. Revenue also increased as a result of the addition of more than 1,000 water customers and 100 wastewater customers. However, water revenues increases were partially offset by the record rainfall of 2009, which lowered per customer demand.

Consolidated Water (CWCO, NR) – CWCO announced that it has scheduled a conference call for 11:00 a.m. EDT on Wednesday, March 17, 2010, to review the Company's operating results for the fourth quarter and full year ended December 31, 2009. The dial in is 800-860-2442 (international/local participants dial 412-858-4600).

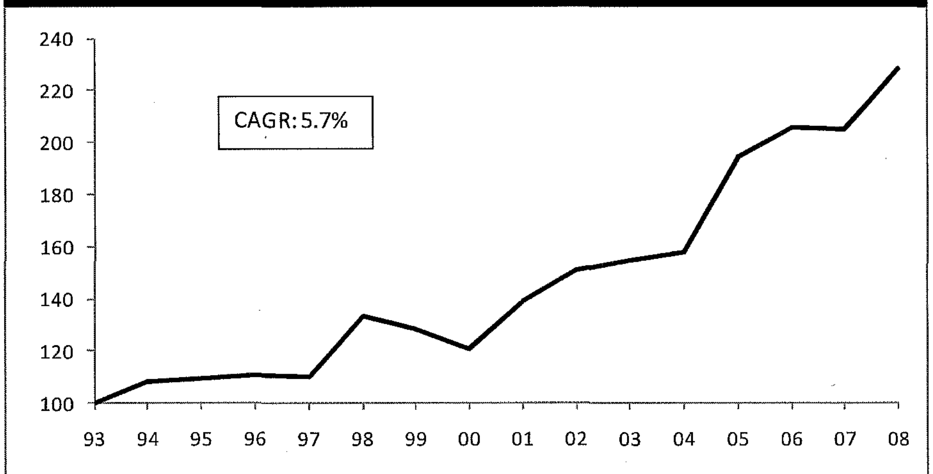
Middlesex Water Company (MSEX, NR) – MSEX announced operating revenues of $91.2M for the year ended December 31, 2009, compared to $91.0M in 2008. Net income for the year ended December 31, 2009 was $10.0M, down $2.2M from the same period in 2008. Earnings applicable to common stock for the year ended December 31, 2009, were $9.8M, or $0.73 per basic share, compared with $12.0M, or $0.90 per basic share, in 2008. On a fully diluted basis, earnings per share were $0.72 for 2009, compared to $0.89 per share in 2008.

WATER EQUIPMENT/TREATMENT UPDATES

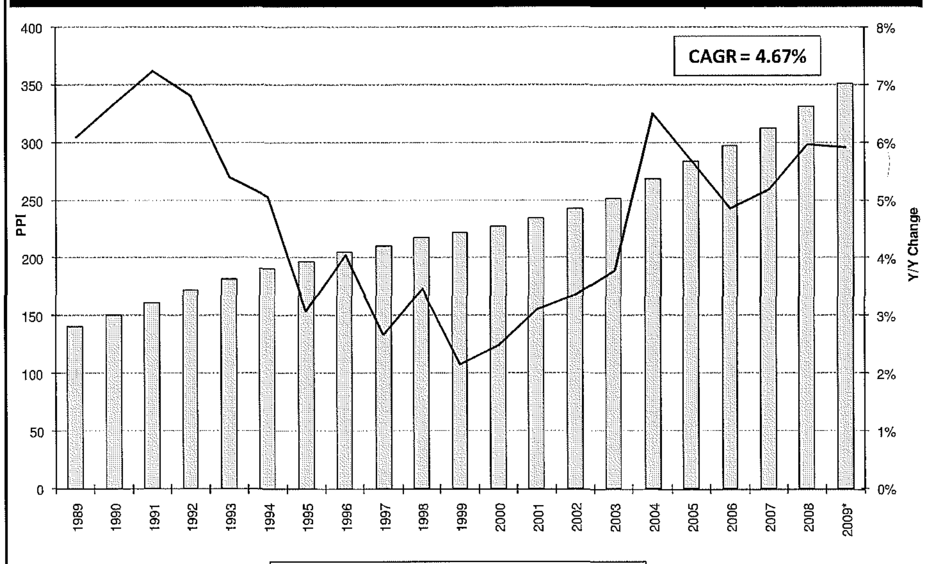
Pall Corporation (PLL, NR) – PLL reported financial results for the second quarter ended January 31, 2010. Sales for the second quarter were $560.4M, an increase of 3.2% compared to the second quarter of fiscal year 2009. Sales in local currency ("LC") decreased 2.8%. Foreign currency translation increased reported sales by $32.5M or 6% in the quarter. Net earnings were $49.6M, compared to $38.9M in the second quarter of fiscal year 2009. Both diluted and pro forma earnings per share ("EPS") were $0.42, compared to diluted EPS of $0.33 and pro forma EPS, excluding restructuring and other charges, of $0.38 last year. The estimated impact of foreign currency translation increased second quarter 2010 EPS by $0.04.

WATER INFRASTRUCURE UPDATES

Insituform Technologies (INSU, NR) – INSU announced it has been awarded two contracts with a combined value of $6.5M from the Hallsdale-Powell Utility District in Knoxville, Tennessee. These contracts mark the first time Insituform will work with the District. Hallsdale-Powell will fund the projects with a state revolving fund loan secured through the American Recovery and Reinvestment Act (ARRA), Hallsdale-Powell had planned to complete this project in a series of contracts to be awarded over the next three years. However, by accessing the additional funds available through the ARRA, the District will be able to upgrade its system more quickly, significantly reducing infiltration into its existing system. Insituform will rehabilitate approximately 25 miles of sewer pipelines with its core cured-in-place pipe (CIPP) technology. The project is expected to be completed by June 2011.



Source: Bloomberg and Longbow Research



Source: Bureau of Labor Statistics

WATER INDUSTRY PEER VALUATION

($ in millions, except per share data)

							52 Week				Earnings per Share			P/E		Dividend	Price/
Company	Ticker	FY End	Rating	Target	% Upside	Share Price	Hi	Lo	Mkt Cap	Revenue Last FY	Last FY	Current FY	Next FY	Current FY	Next FY	Rate	Book
U.S. WATER UTILITIES																	
American Water Works	**AWK**	**Dec.**	**BUY**	**$24**	**14%**	**$ 21.02**	**$23.77**	**$16.55**	**$ 3,661**	**$ 2,337**	**1.25**	**1.40**	**1.60**	**15.0x**	**13.1x**	**4.0%**	**1.3x**
Aqua America	**WTR**	**Dec.**	**Neutral**			**$ 16.84**	**$20.37**	**$15.39**	**$ 2,300**	**$ 671**	**0.77**	**0.88**	**0.95**	**19.1x**	**17.8x**	**3.4%**	**2.2x**
American States Water	**AWR**	**Dec.**	**Neutral**			**$ 33.74**	**$38.79**	**$30.82**	**$ 602**	**$ 361**	**1.63**	**1.71**	**2.08**	**19.8x**	**16.2x**	**3.2%**	**1.8x**
California Water Service Group	**CWT**	**Dec.**	**BUY**	**$43**	**17%**	**$ 36.71**	**$44.06**	**$33.49**	**$ 759**	**$ 449**	**1.95**	**2.00**	**2.40**	**18.3x**	**15.3x**	**3.3%**	**1.8x**
Artesian Resources Corporation	ARTNA	Dec	NR			$ 18.50	$18.85	$13.34	$ 135	$ 61	0.97	*1.12*	*n/a*	16.5x	*n/a*	4.1%	1.3x
Consolidated Water Co	CWCO	Dec	NR			$ 14.39	$21.29	$7.28	$ 211	$ 60	0.65	*0.8*	*0.8*	18.0x	18.0x	2.1%	1.5x
Connecticut Water Service	CTWS	Dec	NR			$ 24.06	$26.44	$18.67	$ 205	$ 61	1.23	*1.2*	*1.44*	20.1x	16.7x	3.8%	1.9x
Middlesex Water Company	MSEX	Dec	NR			$ 17.36	$18.00	$12.61	$ 238	$ 91	0.72	*0.8*	*0.89*	21.7x	19.5x	4.1%	1.7x
Pennichuck Corporation	PNNW	Dec	NR			$ 21.20	$24.80	$18.69	$ 98	$ 33	0.55	*0.74*	*0.79*	28.6x	26.8x	3.4%	1.8x
York Water Company	YORW	Dec	NR			$ 14.30	$17.95	$11.31	$ 176	$ 37	0.64	*0.7*	*0.72*	20.4x	19.9x	3.7%	2.0x
U.S. Water Utility Average														19.8x	18.1x	3.5%	1.7x
EQUIPMENT/FILTRATION/TREATMENT SECTOR																	
Calgon Carbon Corp.	CCC	Dec.	NR			$ 15.82	$19.31	$10.93	$ 916	$ 412	0.69	*0.80*	*0.96*	19.8x	16.5x	0.0%	2.5x
Danaher	DHR	Dec.	NR			$ 78.28	$78.28	$51.18	$ 25,095	$ 11,185	3.53	*4.08*	*4.63*	19.2x	16.9x	0.2%	2.1x
ITT Technologies	ITT	Dec.	NR			$ 52.97	$56.95	$35.38	$ 9,685	$ 10,905	3.78	*4.07*	*4.5*	13.0x	11.8x	1.9%	2.3x
Layne Christensen	LAYN	Jan.	NR			$ 29.71	$35.14	$15.69	$ 576	$ 1,008	0.85	*0.95*	*1.45*	31.3x	20.5x	0.0%	0.7x
Mueller Water Products	MWA	Sept	NR			$ 4.85	$5.93	$2.26	$ 721	$ 1,428	-0.29	*0.01*	*0.15*	NM	32.3x	1.5%	1.9x
Nalco	NLC	Dec.	NR			$ 23.50	$26.63	$11.36	$ 3,275	$ 3,747	0.95	*1.36*	*1.65*	17.3x	14.2x	0.6%	7.5x
Pall Corp.	PLL	Jul.	NR			$ 40.84	$41.82	$18.61	$ 4,544	$ 2,329	1.77	*2.24*	*2.24*	18.2x	18.2x	1.6%	3.2x
Pentair	**PNR**	**Dec.**	**BUY**	**$37**	**18%**	**$ 34.30**	**$34.88**	**$18.80**	**$ 3,359**	**$ 2,692**	**1.47**	**1.85**	**2.28**	**18.5x**	**15.0x**	**2.2%**	**1.6x**
Watts Water Technologies	**WTS**	**Dec.**	**Neutral**			**$ 31.24**	**$32.96**	**$16.84**	**$ 1,144**	**$ 1,234**	**1.54**	**1.60**	**1.88**	**19.6x**	**16.6x**	**1.4%**	**1.3x**
Equipment/Filtration/Treatment Average (*exBWTR and CCC)														19.6x	18.0x	1.0%	2.6x
WATER RESOURCES/ INFRASTRUCTURE																	
Insituform Technologies	INSU		NR			$ 27.30	$27.47	$13.03	$ 1,057	$ 727	1.04	*1.48*	*1.73*	18.3x	15.7x	0.0%	1.6x
Lindsay Manufacturing	LNN		NR			$ 42.80	$47.45	$22.97	$ 539	$ 336	1.11	*1.35*	*1.82*	28.3x	26.3x	0.7%	2.5x
Tetra Tech	TTEK		NR			$ 21.10	$32.00	$19.51	$ 1,279	$ 2,287	1.22	*1.14*	*1.32*	18.3x	15.6x	0.0%	2.5x
Water Resources/Infrastructure Average														21.6x	19.2x	0.2%	2.2x

Relevant Indices		Share Price
Dow Jones Industrials	DJ30	$ 10,612
S&P 500	SPX	$ 1,150
Nasdaq Composite	NDX	$ 1,923

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.

Garik Shmois
216-525-8414
gshmois@longbowresearch.com

Vishal Khetriwal, CFA
216-525-8469
vkhetriwal@longbowresearch.com

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

APPENDIX

IMPORTANT DISCLOSURES

REGULATION ANALYST CERTIFICATION ("REG AC"): The Research Analyst(s) who prepared this research report hereby certifies that the views expressed in the research report accurately reflect the analyst(s) personal views about the subject companies and their securities. The Research Analyst(s) also certifies that the Analyst(s) have not been, are not, and will not be receiving direct or indirect compensation for expressing the specific recommendation(s) or view(s) in this report.

GENERAL DISCLOSURES: Longbow Securities does not make a market in any securities, nor does it hold a principal position in any security. Security prices in this report may either reflect the previous day's closing price or an intraday price, depending on the time of distribution. Consensus estimates are derived from either Thomson/Reuters, Bloomberg or Baseline. Designated trademarks and brands are the property of their respective owners.

SPECIFIC DISCLOSURES:

- Longbow Securities does not make a market in the securities of any company mentioned in this report, and is not a market maker in any securities. Nor does the firm hold a principal position in any security.
- As of the date of this report, no officer, director or stockholder of Longbow Securities, or any member of their immediate families, holds securities of any company mentioned in the report. In the event such persons purchase, hold or sell securities of a company mentioned in the report for their own account, any subsequent report shall disclose the fact of any such ownership or transactions.
- As of the date of this report, no employee of Longbow Securities serves on the Board of Directors of the subject security or any other security mentioned in this report.
- As of the date of this report, neither the Research Analyst nor a member of the Research Analyst's household has a financial interest in the securities of the subject company or any other security mentioned in this report.
- As of the date of this report, neither the Research Analyst nor a member of the Research Analyst's household serves on the Board of Directors of the subject company or any other security mentioned in this report.
- As of the date of this report, neither Longbow Securities nor its affiliates beneficially own 1% or more of an equity security of the subject company or any other security mentioned in this report.

RATINGS DISTRIBUTIONS FOR LONGBOW RESEARCH:

Rating Category	Count	Percent
Buy	86	38.6%
Neutral	135	60.5%
Sell	2	0.9%

RATING SYSTEM:

"Buy" means that Longbow Securities expects total return to exceed 20% over a 12-month period.

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

"Neutral" means that Longbow Securities expects total return to be within a range of plus or minus 20% over a 12-month period.

"Sell" means that Longbow Securities expects total return to be negative by greater than 20% over a 12-month period.

Longbow Research's full research universe and related applicable disclosures can be obtained by calling (216) 986-0700 or via postal mail at: Editorial Department, Longbow Research, 6000 Lombardo Center, Suite #500, Independence, Ohio 44131.

DISCLAIMER: The information, opinions, estimates and projections contained in this report were prepared by Longbow Securities LLC, a wholly owned subsidiary of Longbow Research LLC, and constitute the current judgment of Longbow Securities as of the date of this report. Additional information may be available from Longbow Securities upon request. The information contained herein is believed to be reliable and has been obtained from sources believed to be reliable, but Longbow Securities makes no representation or warranty, either expressed or implied, as to the accuracy, completeness or reliability of such information. Longbow Securities does not undertake, and has no duty, to advise you as to any information that comes to its attention after the date of this report or any changes in its opinion, estimates or projections. Prices and availability of securities are also subject to change without notice. By accepting this report, the reader acknowledges that the report does not purport to meet the objectives or needs of specific investors, and, accordingly, constitutes only "impersonal advisory services" as that term is defined in Rule 204-3 under the Investment Advisers Act of 1940 and that any advice in this report is furnished solely through uniform publications distributed to subscribers thereto within the meaning of Section 2(a)(20)(i) of the Investment Company Act of 1940. The securities discussed in Longbow Research reports may be unsuitable for some investors depending on their specific investment objectives, financial status, risk profile, or particular needs. Investors should consider this report as only a single factor in making their investment decisions and should not rely entirely on this report in evaluating whether or not to buy or sell the securities of the subject company. Longbow Research archives and reviews outgoing and incoming email. Such may be produced at the request of regulators. Sender accepts no liability for any errors or omissions arising as a result of transmission. Use by other than intended recipients is prohibited.

DESCRIPTION: Longbow Securities LLC, a wholly owned subsidiary of Longbow Research LLC, is a primary research provider established in 2003 and headquartered at 6000 Lombardo Center, Suite 500, Independence, Ohio 44131 USA. The company provides research services to institutional investors, investment advisers, and professional money managers. MEMBER FINRA/SIPC. Additional information supporting the statements in this report is available upon request.

Survey

LONGBOW Research
Tactical advantage through independent research

March 15, 2010

Analysts:
GARIK SHMOIS
T: 216-525-8414
E: gshmois@longbowresearch.com

VISHAL KHETRIWAL, CFA
T: 216-525-8469
E: vkhetriwal@longbowresearch.com

Industry: **WATER UTILITIES**

Coverage:

Ticker	Rating	Price
AWK	BUY	$20.96
AWR	NEUTRAL	$32.50
CWT	BUY	$36.55
WTR	NEUTRAL	$16.88

Water Utilities: Survey Of Consumption and Cost Trends

- We recently completed a survey of municipal water systems and wholesale water suppliers in the states where our two largest utilities under research coverage, American Water (AWK) and Aqua America (WTR), have the largest presence. We focused our findings on year-to-date consumption trends, water treatment costs and wholesale water prices.
- Water consumption, on average, was flat in the Northeast, was down 2-3% in the Midwest and Texas, and was down 10% in California. Given that both AWK and WTR have ~50% of revenues coming from the Northeast, we would expect near-term water consumption declines to be in the low single-digits.
- According to our contacts, water treatment costs have increased 2-3% y/y and the findings from our survey support our assumptions of inflation-level increases in O&M costs. For FY10E, we have modeled approximately a 100bp y/y O&M ratio improvement for both WTR and AWK as revenue growth from rate increases should offset cost increases.
- Wholesale water prices have mostly been flat except in California, where rates are up ~10% y/y. While wholesale water prices are recovered under the WRAM and MBCA, an increase in wholesale prices does encourage utilities to use more water from internal sources, with regulatory lag the principal risk to recovering the increased treatment costs.
- We are maintaining our BUY ratings, target prices and estimates on AWK and CWT shares. We remain NEUTRAL-rated on WTR and AWR shares and are maintaining our estimates.

IMPORTANT DISCLOSURES ARE LOCATED IN THE APPENDIX.

SUMMARY

We recently completed our survey of municipal water systems and wholesale water suppliers in the states where our two largest utilities, American Water (AWK - BUY, TP $24) and Aqua America (WTR - NEUTRAL) under coverage currently have the largest presence. The states include New Jersey, Pennsylvania, Illinois, Missouri, Indiana, California and Texas. We asked our contacts for an update in YTD 2010 y/y changes in water consumption, water treatment costs and wholesale water prices.

By way of background, only inflation in water treatment costs have a direct financial impact on our covered utilities based in California – California Water (CWT - BUY, TP $43) and American States (AWR - NEUTRAL). Since the passage of the Water Recovery Adjustment Mechanism (WRAM) and Modified Cost Balancing Account (MCBA), their revenues and costs have been decoupled from water consumption and wholesale water prices. They are allowed to recover any loss due to consumption declines or increases in water prices and vice-versa. However, an increase in wholesale prices does encourage utilities to use more water from internal sources, with regulatory lag the principal risk to recovering the increased treatment costs. Consequently, we view this survey as more impactful for AWK and WTR.

Key takeaways include:

- Water consumption, on average, was flat in the Northeast, was down 2-3% in the Midwest and Texas, and was down 10% in California. As the Northeast (PA & NJ), Midwest (OH, IL & IN), and Texas contributed at least 57%, 16% and 8%, respectively, of WTR's total revenues in 2009, we expect overall consumption to be flat to slightly down in 1Q10. We note that although WTR's total send-out was down 3-5% in 2009, we calculate that it lost less than $1.0M of revenues in 1Q09 due to lower water consumption (most of the impact was in the summer – 2Q and 3Q). We again expect variations in water consumption to have a limited impact on 1Q10 revenues. However, WTR should benefit in the middle of the year as weather-related comparisons ease.

  For AWK, the Northeast (PA & NJ), Midwest (MO, IL & IN), and California contributed at least 45%, 25% and 6%, respectively, of total revenues in 2009. The company lost $94M in revenues in 2009 from lower consumption by existing customers, although only $2M of that was in 1Q09. In our forecast for the company, we have modeled a $4.5M consumption-related decline in the current quarter. We see declining consumption trends from lower industrial demand driving what could be an admittedly worst-case scenario. We believe that in 1Q10, the loss could come between $2-5M. The company should not be impacted by the ~10% water sales drop seen in California as this should be hedged by WRAM.

- Water treatment costs increased roughly at the rate of inflation, 2-3% y/y. This was a little slower than the long-term average of above-inflation increases driven by increasing energy and chemical prices. WTR is viewed as an industry leader in efficiency ratio (O&M/revenues) and has a track record of cost containment. The company's adjusted O&M expense increased only 1% in 2009, with 1% growth in number of customers through acquisitions. The O&M expense was also aided by 2-5% in lower water sales. The company has guided for a 50-100bp y/y increase in 2010 as a percentage of revenues. We have modeled at the higher end of this guidance range, reducing the O&M ratio from 40.3% in 2009 to 39.3% in 2010. Given the trend we see in our survey, we are confident that WTR should be able to achieve this improvement.

  AWK's O&M expenses also increased by only 1.6% in 2009, aided by a 5.8% drop in water sales. As we are forecasting only a 1% drop in water sales in 2010, we see O&M expense increasing by 4.7%. We note that this is more or less in line with its historical average. However, due to operating leverage from rate increases that are already in the pipeline, we expect the O&M ratio to decline by 110bp, from 54.3% in 2009 to 53.2% in 2010.

- Wholesale water prices have mostly been flat across the country, with the exception of California, where rates are up ~10% y/y.

WATER CONSUMPTION

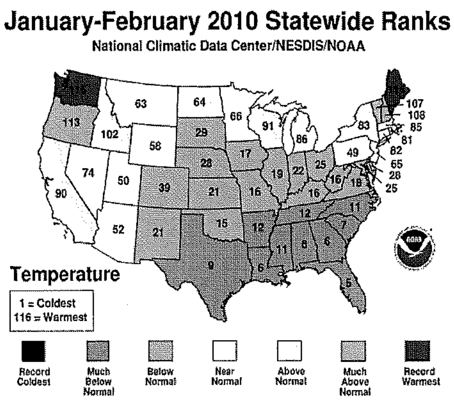
There was a notable difference in y/y consumption changes in various parts of the country depending on regional economic and weather conditions. On average, water consumption was flat in the Northeast, down 2-3% in the Midwest and Texas, and down 10% in California. Water consumption usually declines significantly during the winter vs. the rest of the year as consumers stop watering their lawns. At reduced consumption levels, the variation in water sales due to temperature and precipitation is also lower compared to the rest of the year. However, at the same time, consumption has also been declining around the country (more so in California and southern states that have significantly higher per-household consumption than the national average) due to more efficient household fixtures and more efficient commercial and industrial processes.

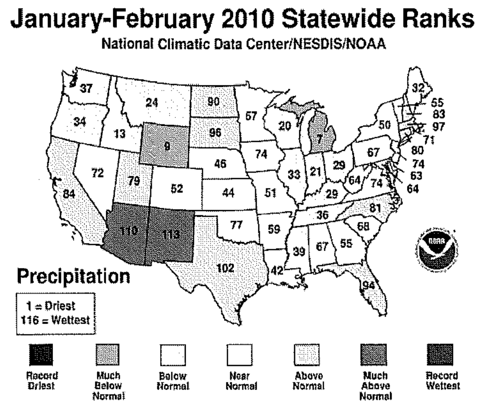
We believe that the above-normal (warmer) temperature in the Northe*ast and below-normal (colder) temperature in the Midwest could have contributed to the flat and 2-3% declines,* respectively, in those regions. In California, above-normal precipitation could have contributed to the 10% average decline, but it seems to be more a result of mandates to reduce consumption in the face of continuing water shortages in the state. Weak economic conditions were also often mentioned by our contacts as a reason for the declines in water sales around the country. Texas also received above-normal precipitation, which could have contributed to the 2-3% average decline.

Additionally, we found that water systems that have lost a large commercial or industrial consumer, or have installed water meters in the last year (vs. flat rates previously) saw significant (10-30%) declines in water sales. Some of our contacts also mentioned that water leakage from aging water pipes was also increasing their send-out every year, which is increasing costs without increasing revenues.

Notable Quotes

- "Consumption was down 20-22% in 2009. Down 35% in January (2010) versus the five-year average for the month. We implemented metered billing in January, 2008 vs. flat rate previously, which has caused this decline." – *General Manager, Water System in California*
- "We have a mandate to reduce our consumption below 10%. But in the last few months because of the wet weather, consumption has declined 15%." – *Manager, Water System in California*
- "Consumption has been declining long-term and was down 2-4% this winter. It could be tied to the economy, or more efficient fixtures…it's hard to say." – *Director, Water System in Indiana*
- "Consumption usually declines 1-2% annually but we lost an industry in our region last year, so in recent months consumption has been down 5-10% y/y." – *Manager, Water System in California*
- "Our water consumption has been going up for the last few years as our economy has been doing well: 9M-gallon increase over the last three years from 120M gallons. Increased water loss from aging pipes is also contributing to the increased send-out. Consumption has been flat y/y in last few months." – *Treatment Plant Operator, Pennsylvania*

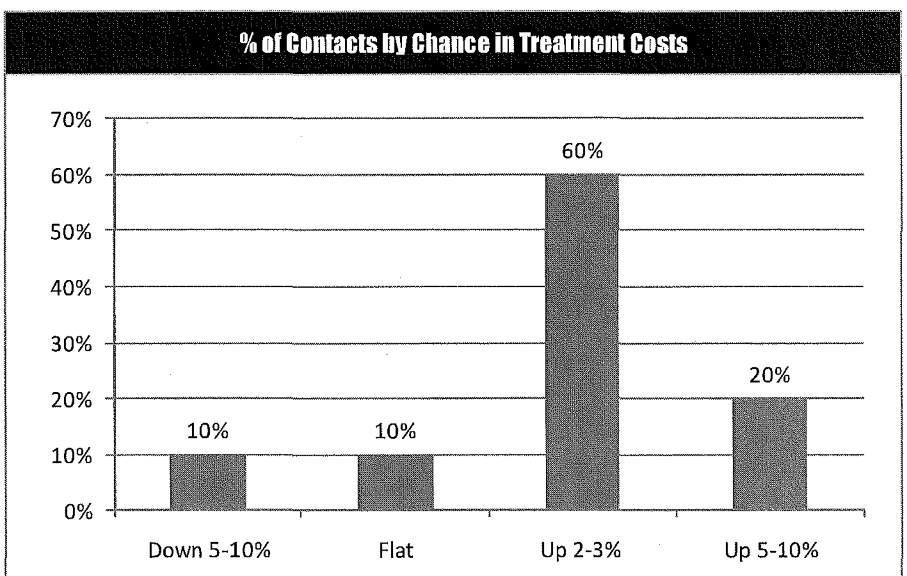




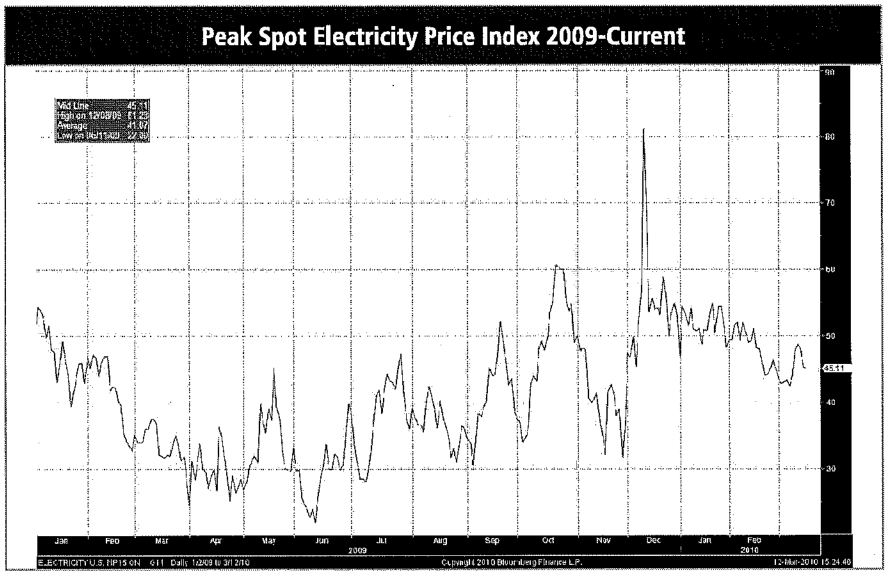
Source: National Climactic Data Center

TREATMENT COSTS

Traditionally, treatment costs increase at slightly above inflationary levels mainly due to rising electricity and chemical prices. In the current economic environment, most of our contacts reported a 2-3% y/y cost increase. There were notable exceptions, with some systems using desalination reporting a 5-10% y/y cost increase, driven again by rising electricity prices. We believe this could impact AWK given its exposure to desalination operations. As seen in the graph below, electricity prices have been moving up, with average YTD prices 10% higher vs. the same period in 2009. This could prove an additional headwind if recent trends are sustainable.



Source: LBR Survey



Source: Bloomberg

Notable Quotes Related to Treatment Costs

- "We use the reverse osmosis process for desalinating water from our lake, which is very salty. Lately, costs have been increasing above inflation at 5-7%." – *Engineer, Water System in Texas*
- "Treatment costs have been going up at the rate of inflation, 2-3%. Electricity costs are one of the main drivers. We are usually not affected by short-term fluctuation in chemical prices as we are locked in one or two-year price contracts." – *Operator, Water System in Pennsylvania*
- "We do very little treatment as 85% is purchased water. We also have a two-tier water rate: fixed component and variable component based on treatment component. Therefore, we think we are able to recover any increase in treatment costs." – *General Manager, Water System in California*

WHOLESALE WATER PRICES

Wholesale water prices around the country have been flat except for an ~10% y/y increase in California. Several water systems we spoke with have long-term price contracts with their suppliers which have not been renegotiated because of current economic conditions. Some of the wholesale water suppliers mentioned that they have offset cost inflation with process efficiencies as they do not want to increase prices in the current environment. However, in California, the Metropolitan Water District (MWD) increased prices by 11% in 2009. As a large number of utilities in the state buy water directly or indirectly from MWD, they have experienced significant price increases.

Some Quotes

- "We purchase 85% of our water from wholesale water suppliers. They have increased prices by 11% in 2009 and 19% in 2008." – *General Manager, Water System in California*
- "We have to buy 25% of water from a wholesale supplier for the next 15 months. We are developing additional internal sources to replace that portion. Purchased water price has been flat because of agreement we made in 2006." – *Director, Water System in Indiana*
- "Our rates have been flat. We've been able to offset any cost increase with improved efficiencies." – *Manager, Agency supplying wholesale water in New Jersey*

AWK INVESTMENT THESIS

We continue to rate AWK shares BUY with a $24 12-month target price, as we see AWK as offering an attractive risk/reward even after the disappointing FY10 guidance. We believe AWK shares were trading at a discount partially due to the "RWE overhang." As we believe this overhang has now been removed, AWK's discounted valuation relative to the industry average should gradually ease. However, our target price still incorporates a 13% discount to the peer group average. The shares are trading at 14.9x our FY10E EPS, relative to the peer group average of 19.5x. Viewed as the largest and most geographically diversified water utility in the U.S., AWK should benefit by investing to replace and expand the aging water infrastructure in the country. As such, the company is planning to spend $4-4.5B over the next five years, which should drive earnings growth over that time period. As the company benefits from increased CAPEX after years of underinvestment under RWE ownership, and from operating leverage through rate increases, we believe a low-teens percent EPS growth should lead to multiple expansion over the next one-to-two years.

AWK VALUATION

AWK shares closed Friday at $20.96, which is 14.9x our FY10E EPS of $1.40 and 13.1x our FY11E EPS of $1.60. The shares are trading at a discount to the peer group average of 19.5x FY10E, and at 1.3x tangible book value compared to a peer group that trades over 1.7x, on average. Our target price of $24 is based on 15x our FY11E EPS, a valuation that remains at a discount to the peer group. However, we see multiple expansion from current levels as justified given AWK being currently viewed as the largest and most diversified publicly-traded water utility in the U.S. and with the potential from earnings growth as the company benefits from rate increases and operating leverage given its high fixed costs.

AWK RISKS

The potential downside risks to our investment thesis, rating and estimates include, but are not limited to: 1) delays in rate case processing or lower rate increases by the regulators than our expectations, 2) 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, 4) a large acquisition at an excessive valuation (significantly above the rate base), and 5) a large goodwill impairment which could potentially lead to a breach of debt covenants or regulatory requirements.

AWR INVESTMENT THESIS

In the long-term, we like AWR, currently viewed as the fourth largest publicly traded domestic water utility, as we believe the WRAM/MBCA implementation in California has removed the quarterly earnings volatility caused by the changes in water consumption. We note that seasonal variation will still exist. We believe these mechanisms have somewhat reduced the single-state operational risk that AWR faced previously. However, we believe the benefits from the improved regulatory environment and earnings upside potential from the recently approved rate cases are already mostly priced into the shares. Consequently, we continue to rate the shares NEUTRAL as we see the upside potential related to rate relief as already largely reflected in the shares and valuations at a slight premium compared to our preferred names in the space – AWK and CWT.

AWR VALUATION

AWR shares closed Friday at $32.50. At 19.1x our FY10E EPS of $1.71, AWR shares are trading broadly in line to its last ten-year average forward P/E of 20.6x as well as to the current peer group average of 19.5x. At 15.6x our FY11E EPS of $2.08, the shares are trading at a discount to the peer average of 18.0x. However, should multiples expand, we believe a fair value of $38/share does not imply the same amount of potential upside as would our preferred names in the space – AWK and CWT.

AWR RISKS

The potential downside risks to our investment thesis, rating and estimates include, but are not limited to: 1) lower rate increase approvals by the CPUC than our expectation, 2) increases in raw material costs, and 3) an acquisition of a large water system by the local government through eminent domain.

The potential upside risks to our investment thesis, rating and estimates include, but are not limited to: 1) favorable rate case approvals, and 2) the commencement of the large "special" construction project at Ft. Bragg, North Carolina, or any other base.

CWT INVESTMENT THESIS

We continue to rate CWT shares BUY with a $43 12-month target price, which represents 18x our FY11E EPS of $2.40, in line with the peer group average. While we expect FY10E to offer limited EPS growth opportunities given the timing of rate cases coupled with near-term cost inflation, we believe 20% earnings growth in FY11 is achievable given the pent up revenue opportunity associated with its 2009 General Rate Case. On valuation, CWT shares are trading at 15.2x our FY11E EPS of $2.40, which we believe to be conservative when compared to the industry average of 18.0x and the company's historical average of 21x.

CWT VALUATION

CWT shares closed Friday at $36.55, which is 18.2x our FY10E EPS of $2.00 and 15.2x our FY11E EPS of $2.40. The shares are trading at a discount to the company's historical normalized 21x average and normalized range of 17-27x forward P/E. CWT trades at a discount to its peer group which is currently valued at 19.5x FY10E and 18.0x FY11E.

CWT RISKS

Potential downside risks to our investment thesis, rating and estimates include, but are not limited to: 1) lower rate increase approvals by the California Public Utility Commission (CPUC) than our expectation, 2) a near-term run-up in pension, legal, conservation and maintenance expenses, and 3) large acquisition(s) at excessive valuation(s) (significantly above the rate base).

WTR INVESTMENT THESIS

We continue to rate WTR shares NEUTRAL. We would potentially become more positive on the shares if we were to see earnings growth from improved ROEs in under-earning systems that were acquired in the southern states in 2003-04 and/or an acceleration of acquisitions. Overall, we see downside risk potential to WTR as fairly limited as the company is trading at a 17% discount to its historical forward P/E of 23x. 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 have difficulty justifying the magnitude of WTR's valuation premium when compared to other names under coverage.

WTR VALUATION

WTR shares closed Friday at $16.88 which is 19.1x our FY10E EPS of $0.88 and 17.8x our FY11E EPS of $0.95. The shares are trading at a discount to the company's historical 23x average and normalized range of 20-30x forward P/E.

WTR RISKS

Potential downside risks to our investment thesis, rating 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, rating 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.

LONGBOW Research

March 15, 2010

American Water Works— Quarterly Income Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09	1Q10E	2Q10E	3Q10E	4Q10E	1Q11E	2Q11E	3Q11E	4Q11E
Regulated Segment	449.9	527.1	603.7	502.1	497.4	554.9	621.0	532.5	520.7	583.3	650.7	567.1	558.4	625.4	697.5	608.0
% Increase	7.3%	3.6%	5.6%	2.9%	10.6%	5.3%	2.9%	6.1%	4.7%	5.1%	4.8%	6.5%	7.2%	7.2%	7.2%	7.2%
Non-Regulated Revenue	61.0	67.0	73.9	70.3	57.5	64.2	65.2	70.9	70.0	76.7	77.7	83.4	73.5	80.5	81.6	87.6
% Increase	14.4%	20.8%	9.4%	4.1%	-5.7%	-4.2%	-11.7%	0.9%	21.7%	19.5%	19.2%	17.6%	5.0%	5.0%	5.0%	5.0%
Other	(4.1)	(4.7)	(5.4)	(3.9)	(4.7)	(6.3)	(6.3)	(5.6)	(5.2)	(5.8)	(6.5)	(5.7)	(5.6)	(6.3)	(7.0)	(6.1)
% Regulated Rev	-0.9%	-0.9%	-0.9%	-0.8%	-1.0%	-1.1%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%
Operating revenues	**506.8**	**589.4**	**672.2**	**568.6**	**550.2**	**612.7**	**680.0**	**597.8**	**585.6**	**654.2**	**722.0**	**644.8**	**626.4**	**699.7**	**772.2**	**689.5**
Production costs	64.2	72.6	84.1	67.7	69.0	77.2	86.7									
Employee-related costs	126.8	131.4	127.4	119.9	132.6	133.2	139.6									
Operating supplies and services	69.5	66.7	72.2	74.8	56.8	58.6	60.2									
Maintenance materials and services	34.9	37.2	32.0	32.1	32.2	31.8	31.7									
Customer billing and accounting	7.4	11.9	13.4	11.2	10.8	13.2	12.7									
Other	8.3	10.7	13.1	14.0	12.9	16.7	9.9									
Operation and maintenance	311.3	330.6	342.2	319.8	314.4	330.6	340.9	338.5	327.6	345.1	353.3	360.7	342.9	360.7	368.6	377.4
Depreciation and amortization	63.9	67.3	68.4	71.6	68.8	73.2	74.9	77.3	75.8	76.9	77.9	79.0	78.9	79.9	80.9	81.9
General taxes	52.1	49.6	49.4	48.0	52.5	51.7	50.6	44.4	52.5	51.7	50.6	44.4	53.5	52.7	51.6	45.4
Loss (gain) on sale of assets	(0.1)	(0.8)	0.5	(0.0)	(0.2)	0.0	(0.8)	0.2	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)
Impairment charges	750.0				450.0											
EBIT	**(670.4)**	**142.7**	**211.8**	**129.1**	**(335.4)**	**157.2**	**214.4**	**137.4**	**129.9**	**180.7**	**240.4**	**160.9**	**151.3**	**206.6**	**271.3**	**184.9**
Operating Margin (excluding impairment)	*15.7%*	*24.2%*	*31.5%*	*22.7%*	*20.8%*	*25.7%*	*31.5%*	*23.0%*	*22.2%*	*27.6%*	*33.3%*	*25.0%*	*24.2%*	*29.5%*	*35.1%*	*26.8%*
Interest	70.0	70.1	72.7	72.4	72.0	73.7	74.1	76.8	77.1	77.6	78.2	78.8	80.7	81.1	81.5	81.9
Other income, net	(3.7)	(3.1)	(6.7)	(8.0)	(4.8)	(2.6)	(1.5)	(2.3)	(2.8)	(2.8)	(2.8)	(2.8)	(2.8)	(2.8)	(2.8)	(2.8)
Total other income (deductions)	**66.2**	**67.0**	**66.0**	**64.5**	**67.1**	**71.1**	**72.6**	**74.5**	**74.3**	**74.8**	**75.4**	**76.0**	**77.9**	**78.3**	**78.7**	**79.1**
EBT	**(736.6)**	**75.7**	**145.8**	**64.6**	**(402.5)**	**86.1**	**141.8**	**62.9**	**55.6**	**105.9**	**165.0**	**84.9**	**73.4**	**128.3**	**192.6**	**105.8**
Provision for income taxes	(4.1)	30.2	57.5	28.2	10.6	34.1	50.2	26.5	21.7	41.3	64.3	33.1	28.6	50.0	75.1	41.3
Implied Tax Rate (excl. goodwill impairment)	-31%	40%	39%	43.6%	22%	39.6%	35.4%	42.2%	39.0%	39.0%	39.0%	39.0%	39.0%	39.0%	39.0%	39.0%
Income (loss) from continuing operations	**(732.5)**	**45.5**	**88.2**	**36.4**	**(413.1)**	**52.0**	**91.6**	**36.4**	**33.9**	**64.6**	**100.6**	**51.8**	**44.8**	**78.3**	**117.5**	**64.5**
Loss (income) from discontinued operations, net of tax																
Net Income (loss)	**(732.5)**	**45.5**	**88.2**	**36.4**	**(413.1)**	**52.0**	**91.6**	**36.4**	**33.9**	**64.6**	**100.6**	**51.8**	**44.8**	**78.3**	**117.5**	**64.5**
Diluted EPS from continuing operations	(4.58)	0.28	0.55	0.23	(2.58)	0.32	0.52	0.21	0.19	0.37	0.56	0.28	0.24	0.41	0.61	0.33
EPS excl. impairment & one-time expenses	**0.11**	**0.28**	**0.55**	**0.23**	**0.19**	**0.32**	**0.52**	**0.21**	**0.19**	**0.37**	**0.56**	**0.28**	**0.24**	**0.41**	**0.61**	**0.33**
Diluted Average Shares	160.0	159.9	160.0	159.9	159.9	164.8	174.7	174.8	174.9	176.7	180.2	183.8	186.7	189.2	191.6	194.0
Financial Summary																
Total Revenue growth	8.2%	5.5%	6.2%	2.7%	8.6%	4.0%	1.2%	5.2%	6.4%	6.8%	6.2%	7.9%	7.0%	7.0%	7.0%	6.9%
Non-Regulated Revenue growth	14.4%	20.8%	11.3%	4.1%	-5.2%	-4.5%	-10.3%	-0.3%	21.7%	19.5%	19.2%	17.6%	5.0%	5.0%	5.0%	5.0%
O&M/Revenue	61.4%	56.1%	50.9%	56.2%	57.1%	54.0%	50.1%	56.6%	55.9%	52.8%	48.9%	55.9%	54.7%	51.6%	47.7%	54.7%
General Taxes/ Regulated Revenue	11.6%	9.4%	8.2%	9.6%	10.6%	9.3%	8.2%	8.3%	10.1%	8.9%	7.8%	7.8%	9.6%	8.4%	7.4%	7.5%
D&A/ Net Fixed Asset	0.59%	0.62%	0.62%	0.64%	0.61%	0.64%	0.64%	0.66%	0.71%	0.71%	0.71%	0.71%	0.70%	0.70%	0.70%	0.70%
Interest/Avg. Total Debt (Annualized)	5.53%	5.53%	5.75%	5.59%	5.40%	5.48%	5.53%	5.67%	5.60%	5.60%	5.60%	5.60%	5.70%	5.70%	5.70%	5.70%
Adj. EBITDA	143.6	210.0	280.2	200.7	183.5	230.4	289.3	214.7	205.7	257.6	318.3	239.9	230.2	286.5	352.2	266.8
EPS growth, excluding goodwill impairment charge	620.8%	-8.9%	6.0%	34.0%	73.6%	10.9%	-4.8%	-8.6%	2.0%	15.9%	6.5%	35.5%	23.7%	13.2%	9.8%	18.0%

Source: Company reports, Longbow estimates

LONGBOW Research

March 15, 2010

American Water Works— Annual Income Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	FY04A	FY05A	2006A	FY07A	FY08A	FY09A	FY10E	FY11E
Regulated Segment	1748.0	1836.1	1854.6	1987.6	2082.7	2207.3	2321.9	2489.3
% Increase		5.0%	1.0%	7.2%	4.8%	6.0%	5.2%	7.2%
Non-Regulated Revenue	290.0	310.8	248.5	242.7	272.2	257.7	307.9	323.3
% Increase		7.2%	-20.0%	-2.3%	12.2%	-5.3%	19.5%	5.0%
Other	-20.17	(10.1)	(10.0)	(16.0)	(18.0)	(24.3)	(23.2)	(24.9)
% Regulated Rev	-1.2%	-0.6%	-0.5%	-0.8%	-0.9%	-1.1%	-1.0%	-1.0%
Operating revenues	**2,017.9**	**2,136.7**	**2,093.1**	**2,214.2**	**2,336.9**	**2,440.7**	**2,606.6**	**2,787.7**
Production costs	248.5	262.6	264.4	278.1	288.6		307.6	317.8
Employee-related costs	407.7	408.8	446.2	463.4	505.6		552.6	585.4
Operating supplies and services	289.3	338.1	268.2	293.5	283.2		307.6	320.6
Maintenance materials and services	90.6	97.9	96.5	128.0	136.3		127.7	133.8
Customer billing and accounting	42.5	44.4	55.6	38.3	44.0		41.7	41.8
Other	43.4	49.8	43.6	45.3	46.1		49.5	50.2
Operation and maintenance	1122.0	1201.6	1174.5	1246.5	1303.8	1324.4	1386.7	1449.6
Depreciation and amortization	225.3	261.4	259.2	267.3	271.3	294.2	309.6	321.6
General taxes	170.2	183.3	185.1	183.3	199.1	199.3	199.3	203.3
Loss (gain) on sale of assets	(8.6)	(6.5)	0.1	(7.3)	(0.4)	(0.8)	(0.8)	(0.8)
Impairment charges	78.7	385.4	221.7	509.3	750.0	450.0		
EBIT	**430.4**	**111.6**	**252.5**	**15.1**	**(186.9)**	**173.6**	**711.8**	**814.1**
Operating Margin (excluding impairment)	*25.2%*	*23.3%*	*22.7%*	*23.7%*	*24.1%*	*25.6%*	*27.3%*	*29.2%*
Interest	315.9	345.3	366.0	283.2	285.2	296.5	311.7	325.2
Other income, net	(11.0)	(9.5)	(4.5)	(12.5)	(21.5)	(11.3)	(11.2)	(11.2)
Total other income (deductions)	**305.0**	**335.7**	**361.5**	**270.6**	**263.7**	**285.3**	**300.5**	**314.0**
EBT	**125.4**	**(224.2)**	**(108.9)**	**(255.5)**	**(450.6)**	**(111.7)**	**411.4**	**500.0**
Provision for income taxes	66.3	51.0	46.9	86.8	111.8	121.4	160.4	195.0
Implied Tax Rate (excl. goodwill impairment)	32.5%	31.6%	41.6%	34.2%	37.3%	35.9%	39.0%	39.0%
Income (loss) from continuing operations	**59.1**	**(275.1)**	**(155.9)**	**(342.3)**	**(562.4)**	**(233.1)**	**250.9**	**305.0**
Loss (income) from discontinued operations, net of tax	124.0	49.9	6.4	0.6				
Net Income (loss)	**(64.9)**	**(325.0)**	**(162.2)**	**(342.8)**	**(562.4)**	**(233.1)**	**250.9**	**305.0**
Diluted EPS from continuing operations	0.37	(1.72)	(0.97)	(2.14)	(3.52)	(1.39)	1.40	1.60
EPS excl. impairment & one-time expenses	**0.86**	**0.69**	**0.41**	**1.04**	**1.10**	**1.25**	**1.40**	**1.60**
Diluted Average Shares	160.0	160.0	160.0	160.0	160.0	168.2	178.9	190.4
Financial Summary								
Total Revenue growth		5.9%	-2.0%	5.8%	5.5%	4.4%	6.8%	6.9%
Non-Regulated Revenue growth			-20.0%	-2.3%	12.2%	-5.3%	19.5%	5.0%
O&M/Revenue	55.6%	56.2%	56.1%	56.3%	55.8%	54.3%	53.2%	52.0%
Depreciation and amortization/ Net Fixed Asset				3.0%	2.8%	2.8%	2.9%	2.9%
Depreciation Growth		16.0%	-0.8%	3.1%	1.5%	8.5%	5.2%	3.9%
General Taxes/ Regulated Revenue	9.7%	10.0%	10.0%	9.2%	9.6%	9.0%	8.6%	8.2%
Adj. EBITDA	734.3	758.4	733.4	791.8	834.4	917.8	1,021.4	1,135.6
Net Income Growth (excl. goodwill impairment)		338.6%	-1.6%	180.1%	12.6%	15.6%	15.7%	21.6%
EPS growth, (excl. goodwill impairment)			-40.3%	153.8%	5.3%	13.6%	12.2%	14.2%
ROE (excl. goodwill & goodwill impairment)			2.3%	7.0%	8.3%	8.4%	8.5%	9.1%

Source: Company reports, Longbow estimates

American States Water — Quarterly Earnings Statement
Garik Shmois/ Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09	1Q10E	2Q10E	3Q10E	4Q10E	1Q11E	2Q11E	3Q11E	4Q11E
Water	52.1	65.4	69.4	61.1	56.8	74.2	78.3	63.7	57.4	74.7	78.8	70.6	66.8	84.2	88.2	73.1
Electric	8.8	6.2	6.7	6.7	8.6	5.9	6.6	7.8	9.8	7.1	7.8	8.4	10.4	7.7	8.4	9.0
Contracted Services	8.1	8.7	9.2	16.4	14.2	13.5	16.6	14.8	15.6	12.5	12.5	12.5	13.0	13.0	13.0	13.0
Total Revenue	**68.9**	**80.3**	**85.3**	**84.2**	**79.6**	**93.6**	**101.5**	**86.3**	**82.8**	**94.3**	**99.0**	**91.6**	**90.2**	**104.9**	**109.6**	**95.1**
Expenses																
Supply Costs	16.1	20.5	24.2	20.0	19.9	23.5	28.3	21.5	18.8	22.9	27.4	23.3	21.6	25.5	30.4	24.1
Gen. & Admin. expenses	14.8	14.9	16.3	16.6	16.9	15.5	17.0	20.7	17.1	17.2	17.3	17.4	17.7	18.0	18.3	18.6
Other O&M	11.8	11.8	11.4	11.4	11.2	11.1	11.7	13.0	11.1	11.0	11.2	13.6	12.5	12.2	12.4	13.8
ASUS Construction Expenses	3.9	4.4	5.1	10.4	8.4	7.8	9.3	8.2	7.8	7.8	7.8	7.8	8.0	8.0	8.0	8.0
Gain on sale of water rights/property					(0.0)		0.76									
Unrealized loss(gain) on purch pwr contracts	(2.8)	(1.7)	3.7	(0.8)												
Total Operation & Maintenance	**43.8**	**50.1**	**60.8**	**57.7**	**56.4**	**57.9**	**67.1**	**63.4**	**54.8**	**58.9**	**63.8**	**62.1**	**59.9**	**63.7**	**69.1**	**64.5**
Depreciation & Amortization	7.8	7.8	7.9	8.1	8.4	8.4	8.4	8.4	8.6	8.8	9.0	9.2	9.4	9.6	9.7	9.9
General Taxes	2.9	2.8	3.5	3.1	3.4	2.7	3.6	3.4	3.4	3.5	3.5	3.6	3.6	3.7	3.8	3.8
Total Expenses	**54.5**	**60.7**	**72.1**	**68.9**	**68.19**	**69.0**	**79.0**	**75.2**	**66.9**	**71.2**	**76.3**	**74.9**	**72.9**	**77.0**	**82.7**	**78.2**
Income from Operations	**14.5**	**19.6**	**13.1**	**15.3**	**11.4**	**24.5**	**22.5**	**11.1**	**16.0**	**23.2**	**22.7**	**16.7**	**17.3**	**27.9**	**26.9**	**16.9**
Operating Margin	21.0%	24.4%	15.4%	18.2%	14.3%	26.2%	22.1%	12.9%	19.3%	24.6%	23.0%	18.2%	19.2%	26.6%	24.6%	17.8%
Other Inc. (loss)	0.1	0.0	(0.03)	(7.7)	(0.0)	0.1	0.0									
EBIT	**14.6**	**19.6**	**13.1**	**7.6**	**11.4**	**24.6**	**22.5**	**11.1**	**16.0**	**23.2**	**22.7**	**16.7**	**17.3**	**27.9**	**26.9**	**16.9**
EBIT (%)	21.1%	24.4%	15.4%	9.0%	14.3%	26.3%	22.2%	12.9%	19.3%	24.6%	23.0%	18.2%	19.2%	26.6%	24.6%	17.8%
Interest Expense	5.0	4.5	5.1	4.8	5.1	5.4	5.7	5.1	5.2	5.3	5.5	5.5	5.6	5.7	5.7	5.9
Income Before Taxes	**9.6**	**15.1**	**8.0**	**2.8**	**6.3**	**19.2**	**16.8**	**6.0**	**10.8**	**17.9**	**17.2**	**11.2**	**11.7**	**22.2**	**21.2**	**11.0**
Provision for Income Taxes	4.3	5.8	3.4	(0.1)	1.4	7.7	7.1	2.6	4.4	7.3	7.0	4.5	4.8	9.0	8.6	4.5
Implied Tax Rate	44.5%	38.4%	42.9%	-3.2%	21.7%	40.2%	42.3%	43.5%	40.8%	40.8%	40.8%	40.8%	40.8%	40.8%	40.8%	40.8%
Net Income	5.3	9.278	4.6	2.9	4.9	11.5	9.7	3.4	6.4	10.6	10.2	6.6	7.0	13.1	12.6	6.5
EPS (fully diluted)	0.30	0.53	0.26	0.16	0.28	0.64	0.52	0.18	0.34	0.57	0.55	0.35	0.37	0.70	0.67	0.35
EPS (fully diluted, ex one-time items)	**0.30**	**0.47**	**0.39**	**0.40**	**0.28**	**0.64**	**0.52**	**0.18**	**0.24**	**0.57**	**0.55**	**0.35**	**0.37**	**0.70**	**0.67**	**0.35**
Weighted Avg. Shares	17.4	17.3	17.3	17.4	17.4	18.0	18.6	18.7	18.7	18.7	18.7	18.8	18.8	18.8	18.8	18.9
Financial Summary (values in %)																
Water revenue growth	3.5%	7.5%	6.0%	-0.3%	9.0%	13.4%	12.9%	4.2%	1.0%	0.8%	0.6%	10.9%	16.4%	12.6%	12.0%	3.5%
Electric revenue growth	-0.7%	-0.8%	7.2%	-6.9%	-1.9%	-5.2%	-2.7%	17.5%	13.9%	20.4%	18.3%	7.7%	6.1%	8.5%	7.7%	7.1%
Contracted Services growth	-38.4%	-28.2%	123%	195%	76%	54.6%	81.8%	-9.9%	10.0%	-7.5%	-24.9%	-15.5%	-16.7%	4.0%	4.0%	4.0%
Total Revenue growth	-4.6%	1.3%	12.4%	13.8%	15.5%	16.5%	19.0%	2.5%	4.0%	0.8%	-2.4%	6.1%	9.0%	11.2%	10.6%	3.9%
Operations & Maintenance/Revenue	63.5%	62.4%	71.3%	68.5%	70.9%	61.9%	66.1%	73.4%	66.2%	62.4%	64.4%	67.9%	66.3%	60.8%	63.1%	67.8%
Supply Costs/Revenue (excl. Military Base)	26.5%	28.7%	31.8%	29.5%	30.4%	29.4%	33.4%	30.0%	28.0%	28.0%	31.7%	29.5%	28.0%	27.8%	31.5%	29.3%
Gen. & Admin./Revenue	21.5%	18.6%	19.1%	19.8%	21.2%	16.6%	16.8%	24.0% #	20.6%	18.2%	17.5%	19.0%	19.6%	17.2%	16.7%	19.6%
Other O&M/Revenue	17.1%	14.7%	13.4%	13.6%	14.1%	11.8%	11.5%	15.1% #	13.4%	11.6%	11.3%	14.9%	13.9%	11.6%	11.3%	14.5%
General Taxes/Revenue	4.2%	3.5%	4.1%	3.7%	4.3%	2.9%	3.5%	3.9%	4.2%	3.7%	3.6%	3.9%	4.0%	3.5%	3.4%	4.0%
EPS Growth	-25.0%	26.2%	-40.6%	-53.4%	-5.7%	20.6%	98.0%	10.8%	20.7%	-11.4%	4.8%	93.2%	8.6%	23.4%	22.3%	-1.9%

Source: Company reports, Longbow estimates

American States Water — Annual Earnings Statement
Garik Shmois/ Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	2005A	2006A	2007A	2008A	2009A	2010E	2011E
Water	205.5	219.2	237.9	247.9	272.9	281.5	312.3
Electric	27.2	29.3	28.6	28.4	28.9	33.1	35.5
Contracted Services	3.5	20.1	34.9	42.4	59.1	53.1	52.0
Total Revenue	**236.2**	**268.6**	**301.4**	**318.7**	**361.0**	**367.8**	**399.8**
Expenses							
Supply Costs	71.9	76.2	78.2	80.9	93.2	92.5	101.6
Gen. & Admin. expenses	44.3	47.1	52.6	62.7	70.1	69.0	72.6
Other O&M	32.0	36.4	43.2	46.4	47.0	46.9	50.9
ASUS Construction Expenses		9.0	22.1	23.9	33.7	31.2	32.0
Gain on sale of water rights/property	0.0	(0.3)	(0.6)	0.0	0.8	0.0	0.0
Unrealized loss on purch power contracts	(5.4)	7.1	(2.1)	(1.6)	(0.0)		
Total Operation & Maintenance	**142.8**	**175.6**	**193.4**	**212.3**	**244.9**	**239.6**	**257.2**
Depreciation & Amortization	21.9	26.3	28.9	31.6	33.6	35.6	38.6
General Taxes	9.3	10.2	11.3	12.3	13.1	14.0	14.9
Total Expenses	**174.0**	**212.0**	**233.6**	**256.2**	**291.5**	**289.2**	**310.8**
Income from Operations	**62.3**	**56.6**	**67.7**	**62.5**	**69.5**	**78.5**	**89.0**
Operating Margin	26.4%	21.1%	22.5%	19.6%	19.3%	21.4%	22.3%
Other Inc. (loss)	(0.0)	0.5	0.30	(7.6)	0.2	0.0	0.0
EBIT	**62.2**	**57.1**	**68.0**	**54.9**	**69.7**	**78.5**	**89.0**
EBIT (%)	0.3	0.2	0.2	0.2	0.2	0.2	0.2
Interest Expense	13.6	18.3	19.21	19.5	21.4	21.5	22.9
Income Before Taxes	**48.6**	**38.8**	**48.8**	**35.4**	**48.4**	**57.0**	**66.1**
Provision for Income Taxes	21.9	15.7	20.8	13.4	18.8	23.2	26.9
Implied Tax Rate	45.0%	40.5%	42.6%	37.8%	38.9%	40.8%	40.8%
Net Income	26.7	23.1	28.0	22.0	29.5	33.8	39.2
EPS (fully diluted)	1.59	1.33	1.61	1.26	1.62	1.81	2.08
EPS (fully diluted, ex.one-time items)	**1.16**	**1.44**	**1.56**	**1.56**	**1.63**	**1.71**	**2.08**
Weighted Avg. Shares	16.8	17.1	17.2	17.4	18.2	18.7	18.8
Financial Summary (values in %)							
Water revenue growth	2.4%	6.7%	8.5%	4.2%	10.1%	3.2%	10.9%
Electric revenue growth	6.4%	7.5%	-2.4%	-0.5%	1.8%	14.5%	7.2%
Other	96.1%	477.9%	73.5%	21.3%	39.6%	-10.2%	-2.1%
Total Revenue growth	3.6%	13.7%	12.2%	5.8%	13.3%	1.9%	8.7%
Operations & Maintenance/Revenue	60.4%	65.4%	64.2%	66.6%	67.8%	65.1%	64.3%
Supply Costs/Revenue (excl. Military Base)	30.9%	30.7%	29.4%	29.3%	30.9%	29.4%	29.2%
Gen. & Admin./Revenue	18.7%	17.5%	17.5%	19.7%	19.4%	18.8%	18.2%
Other O&M/Revenue	13.5%	13.5%	14.3%	14.6%	13.0%	12.8%	12.7%
General Taxes/Revenue	4.0%	4.1%	4.2%	4.5%	4.3%	4.5%	4.3%
(Dep + Amort)/Revenue	9.3%	9.8%	9.6%	9.9%	9.3%	9.7%	9.7%
Interest Expense/Revenue	5.8%	6.8%	6.4%	6.1%	5.9%	5.8%	5.7%
Average ROE	10.4%	8.4%	9.6%	7.2%	8.6%	9.2%	10.1%
EPS growth, excluding one-time items	9.4%	24.1%	8.3%	0.0%	4.3%	4.8%	22.1%

Source: Company reports, Longbow estimates

LONGBOW Research

March 15, 2010

California Water Service Group — Quarterly Earnings Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414

(dollars in millions, except per share data)

FY Ends December 31	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09
Total Revenue	71.6	95.8	113.9	85.9	72.9	105.6	131.7	100.1	86.6	116.7	139.2	106.9
Water Production Costs	25.8	37.3	45.1	30.8	25.4	40.3	46.5	34.4	28.9	41.7	48.9	40.0
Administrative & General	12.6	14.3	14.7	12.7	13.4	13.8	15.0	17.2	18.9	19.4	19.1	17.9
Other Operations	11.1	11.0	11.8	12.5	12.1	12.8	12.9	13.4	12.5	14.3	14.6	15.2
Maintainence	4.5	5.2	4.2	4.4	4.1	4.9	3.8	6.1	4.6	4.3	4.4	5.2
Operations & Maintenance	54.0	67.8	75.8	60.2	55.0	71.9	78.2	71.1	64.8	79.7	87.0	78.3
Depreciation and Amortization	8.4	8.4	8.4	8.4	9.2	9.3	9.3	9.6	10.2	10.3	10.3	9.0
General Taxes	3.4	3.4	3.7	3.1	3.7	3.5	3.9	3.7	4.1	3.9	4.4	4.5
Total Expenses	65.8	79.6	87.9	71.8	67.9	84.7	91.4	84.3	79.1	93.9	101.7	91.8
Income from Operations	5.8	16.2	26.0	14.1	5.0	20.9	40.3	15.8	7.5	22.7	37.5	15.2
Operating Margin	8.1%	16.9%	22.8%	16.5%	6.9%	19.8%	30.6%	15.8%	8.7%	19.5%	27.0%	14.2%
Other Income & Expenses (net)	1.3	1.5	1.3	0.4	(0.1)	0.6	(0.7)	(0.6)	0.2	1.4	1.7	0.9
Gain (loss) on sale of non-util property	0.0	(0.1)	0.0	2.6	0.0	0.0	0.0	0.0	0.6	0.1	(0.7)	(0.1)
EBIT	7.1	17.6	27.2	17.1	4.9	21.5	39.6	15.2	8.4	24.2	38.5	15.9
EBIT (%)	9.9%	18.3%	23.9%	20.0%	6.7%	20.4%	30.0%	15.2%	9.6%	20.7%	27.7%	14.9%
Interest Expense	4.4	4.5	4.5	3.7	4.6	4.7	4.2	3.7	4.4	5.3	5.5	6.1
Income Before Taxes	2.6	13.1	22.8	13.4	0.3	16.8	35.4	11.4	4.0	18.9	33.0	9.8
Provision for Income Taxes	1.1	5.4	8.9	5.4	0.1	6.7	13.2	4.1	1.6	6.8	13.5	3.4
Implied Tax Rate	40.3%	40.9%	39.3%	40.0%	40.3%	39.7%	37.3%	36.0%	39.3%	36.0%	40.9%	34.3%
Net Income	1.6	7.7	13.8	8.0	0.2	10.1	22.2	7.3	2.4	12.1	19.5	6.5
Preferred Dividends	-	-	-	-	-	-	-	-	-	-	-	-
Net Income	1.6	7.7	13.8	8.0	0.2	10.1	22.2	7.3	2.4	12.1	19.5	6.5
EPS (fully diluted)	0.07	0.37	0.67	0.39	0.01	0.48	1.06	0.35	0.12	0.58	0.94	0.31
Weighted Avg. Shares	20.7	20.7	20.7	20.7	20.7	20.7	20.7	20.7	20.8	20.8	20.7	20.8
Financial Summary (values in %)												
Revenue Growth	9.7%	18.1%	5.7%	6.5%	1.9%	10.2%	15.7%	16.6%	18.8%	10.5%	5.7%	6.8%
Operations & Maintenance/Revenue	75.4%	70.8%	66.6%	70.1%	75.4%	68.1%	59.4%	71.0%	74.8%	68.3%	62.5%	73.2%
Gen. taxes/Revenue	4.8%	3.6%	3.3%	3.6%	5.1%	3.3%	3.0%	3.7%	4.7%	3.4%	3.1%	4.2%
EBIT (% of rev.)	9.9%	18.3%	23.9%	20.0%	6.7%	20.4%	30.0%	15.2%	9.6%	20.7%	27.7%	14.9%
EBIT/Interest expense	1.6	3.9	6.1	4.6	1.1	4.6	9.5	4.1	1.9	4.5	7.0	2.6
EPS growth	75.0%	20.5%	-2.6%	23.6%	-87.2%	28.5%	58.8%	-9.2%	1205.6%	21.3%	-11.4%	-12.0%

FY Ends December 31	1Q10E	2Q10E	3Q10E	4Q10E	1Q11	2Q11E	3Q11E	4Q11E
Total Revenue	95.6	127.1	149.4	117.1	111.1	142.6	164.9	132.6
Water Production Costs	32.0	46.0	53.0	42.5	37.8	51.6	58.5	48.4
Administrative & General	19.0	19.7	19.7	19.2	19.8	20.0	20.0	19.5
Other Operations	14.3	17.3	16.7	16.4	17.4	19.2	18.5	18.6
Maintainence	5.5	4.5	4.5	4.5	6.5	5.5	5.5	5.5
Operations & Maintenance	70.9	87.5	94.0	82.6	81.5	96.4	102.5	92.0
Depreciation and Amortization	10.5	10.5	11.0	11.0	11.2	11.2	11.3	11.4
General Taxes	4.5	4.3	4.7	4.9	5.0	5.3	5.4	5.6
Total Expenses	85.9	102.3	109.7	98.5	97.7	112.8	119.3	108.9
Income from Operations	9.7	24.8	39.7	18.6	13.4	29.7	45.7	23.7
Operating Margin	10.2%	19.5%	26.6%	15.9%	12.0%	20.9%	27.7%	17.8%
Other Income & Expenses (net)	0.5	1.0	1.0	1.0	0.5	1.0	1.0	1.0
Gain (loss) on sale of non-util property								
EBIT	10.2	25.8	40.7	19.6	13.9	30.7	46.7	24.7
EBIT (%)	10.7%	20.3%	27.3%	16.8%	12.5%	21.6%	28.3%	18.6%
Interest Expense	6.3	6.4	6.4	6.4	6.7	6.8	7.0	7.2
Income Before Taxes	3.9	19.5	34.3	13.2	7.2	23.9	39.7	17.5
Provision for Income Taxes	1.5	7.5	13.2	5.1	2.8	9.2	15.3	6.7
Implied Tax Rate	38.5%	38.5%	38.5%	38.5%	38.5%	38.5%	38.5%	38.5%
Net Income	2.4	12.0	21.1	8.1	4.4	14.7	24.4	10.7
Preferred Dividends	-	-	-	-	-	-	-	-
Net Income	2.4	12.0	21.1	8.1	4.4	14.7	24.4	10.7
EPS (fully diluted)	0.11	0.56	0.96	0.36	0.20	0.65	1.08	0.47
Weighted Avg. Shares	21.2	21.6	22.0	22.4	22.5	22.6	22.7	22.8
Financial Summary (values in %)								
Revenue Growth	10.4%	8.9%	7.4%	9.5%	16.2%	12.2%	10.4%	13.2%
Operations & Maintenance/Revenue	74.1%	68.8%	62.9%	70.5%	73.4%	67.6%	62.2%	69.4%
Gen. taxes/Revenue	4.7%	3.4%	3.1%	4.2%	4.5%	3.7%	3.3%	4.2%
EBIT (% of rev.)	10.7%	20.3%	27.3%	16.8%	12.5%	21.6%	28.3%	18.6%
EBIT/Interest expense	1.6	4.1	6.3	3.1	2.1	4.5	6.7	3.4
EPS growth	-2.6%	-4.6%	2.2%	17.0%	72.8%	17.5%	12.0%	29.8%

Source: Company reports, Longbow estimates

LONGBOW Research

March 15, 2010

California Water Service Group — Annual Earnings Statement
Garik Shmois\Vishal Khetriwal, CFA
Longbow Research
216-525-8414

(dollars in millions, except per share data)

FY Ends December 31	FY04	FY05	FY06	FY07	FY08	FY09	FY10E	FY11E
Total Revenue	**315.6**	**320.7**	**334.7**	**367.1**	**410.3**	**449.4**	**489.2**	**551.2**
Water Production Costs	119.1	115.7	124.3	138.9	146.6	159.5	173.6	196.3
Administrative & General	47.1	48.8	52.8	54.3	59.4	75.2	77.6	79.3
Other Operations	39.9	40.0	42.9	46.3	51.2	56.6	64.7	73.7
Maintainence	13.2	15.2	15.6	18.3	19.0	18.5	19.0	23.0
Operations & Maintenance	219.4	219.7	235.6	257.8	276.2	309.8	334.9	372.3
Depreciation and Amortization	26.1	28.7	30.7	33.6	37.3	39.8	43.0	45.1
General Taxes	11.5	12.6	12.9	13.7	14.8	16.8	18.3	21.3
Total Expenses	**257.0**	**261.0**	**279.1**	**305.0**	**328.3**	**366.4**	**396.3**	**438.7**
Income from Operations	**58.6**	**59.7**	**55.6**	**62.1**	**82.0**	**82.9**	**92.9**	**112.4**
Operating Margin	**18.6%**	**18.6%**	**16.6%**	**16.9%**	**20.0%**	**18.5%**	**19.0%**	**20.4%**
Other Income & Expenses (net)	2.4	3.0	3.4	4.4	(0.5)	3.2	3.5	3.5
Gain (loss) on sale of non-util property	0.0	2.3	0.3	2.5	0.0	0.6	0.0	0.0
EBIT	**61.0**	**64.9**	**59.4**	**69.0**	**81.5**	**86.7**	**96.4**	**115.9**
EBIT (%)	**19.3%**	**20.2%**	**17.7%**	**18.8%**	**19.9%**	**19.3%**	**19.7%**	**21.0%**
Interest Expense	17.8	17.7	17.0	17.1	17.2	21.3	25.5	27.7
Income Before Taxes	43.1	47.2	42.4	51.9	64.3	65.4	70.9	88.2
Provision for Income Taxes	**17.1**	**20.0**	**16.8**	**20.7**	**24.5**	**24.8**	**27.3**	**34.0**
Implied Tax Rate	**39.6%**	**42.4%**	**39.7%**	**39.9%**	**38.1%**	**38.0%**	**38.5%**	**38.5%**
Net Income	26.0	27.2	25.6	31.2	39.8	40.6	43.6	54.3
Preferred Dividends	-	-	-	-	-	-	-	-
Net Income	**26.0**	**27.2**	**25.6**	**31.2**	**39.8**	**40.6**	**43.6**	**54.3**
EPS (fully diluted)	**1.46**	**1.47**	**1.34**	**1.50**	**1.90**	**1.95**	**2.00**	**2.40**
Weighted Avg. Shares	17.7	18.4	18.9	20.7	20.7	20.8	21.8	22.6
Financial Summary (values in %)								
Revenue Growth	13.9%	1.6%	4.4%	9.7%	11.8%	9.5%	8.9%	12.7%
Operations & Maintenance/Revenue	69.5%	68.5%	70.4%	70.2%	67.3%	68.9%	68.5%	67.6%
(Dep + Amort)/Net Fixed Assets	3.4%	3.6%	3.6%	3.6%	3.7%	3.6%	3.6%	3.6%
Gen. taxes/Revenue	3.6%	3.9%	3.9%	3.7%	3.6%	3.7%	3.7%	3.9%
EBIT (% of rev.)	19.3%	20.2%	17.7%	18.8%	19.9%	19.3%	19.7%	21.0%
Interest Expense/Revenue	5.7%	5.5%	5.1%	4.7%	4.2%	4.7%	5.2%	5.0%
EBIT/Interest expense	3.4	3.7	3.5	4.0	4.7	4.1	3.8	4.2
Net Income Growth	34.0%	4.6%	-6.0%	21.8%	27.7%	1.9%	7.6%	24.4%
EPS growth	20.4%	0.7%	-8.8%	11.9%	26.7%	2.8%	2.6%	19.7%
Average ROE	9.7%	9.3%	7.5%	8.1%	10.1%	9.9%	10.0%	11.7%

Source: Company reports, Longbow estimates

Aqua America - Annual Income Statement
Garik Shmois/ Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09	1Q10E	2Q10E	3Q10E	4Q10E	1Q11E	2Q11E	3Q11E	4Q11E
Total Operating Revenue	139.3	150.8	177.1	159.8	154.5	167.3	180.8	167.9	163.5	178.4	211.8	182.9	177.8	192.7	226.1	197.2
Operation & Maintenance	64.3	65.1	66.7	65.9	67.0	68.5	68.5	66.0	70.8	71.4	78.1	69.5	73.1	74.8	85.5	77.1
Depreciation	21.5	20.6	22.8	23.9	26.4	25.0	25.4	26.2	26.6	27.2	28.3	29.1	29.4	29.6	29.9	31.2
Amortization	1.2	1.0	1.8	1.5	2.8	3.1	3.0	3.1	3.2	3.2	3.2	3.2	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	12.3	12.5	12.7	12.8	13.3	13.5	13.6	13.8
Recovery of restructuring costs																
Total Expenses	99.1	97.6	102.5	102.0	107.7	108.5	109.4	107.5	112.9	114.3	122.4	114.6	119.2	121.3	132.3	125.5
Income from Operations	40.2	53.1	74.6	57.9	46.8	58.9	71.5	60.4	50.6	64.2	89.4	68.2	58.6	71.4	93.8	71.7
Operating Margin (%)	28.9%	35.2%	42.1%	36.2%	30.3%	35.2%	39.5%	36.0%	31.0%	36.0%	42.2%	37.3%	33.0%	37.1%	41.5%	36.3%
All. for Borrowed Funds Used in Const.	1.0	1.1	1.0	0.6	0.6	0.6	0.7	0.9	0.7	0.7	0.8	0.8	0.8	0.8	0.8	0.8
Gain (loss) on sale of other assets		0.6	0.5	0.5	0.1	0.1	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Other																
EBIT	41.2	54.8	76.1	59.0	47.5	59.5	72.4	61.4	51.4	65.0	90.3	69.2	59.5	72.3	94.7	72.6
EBIT (%)	29.6%	36.3%	43.0%	36.9%	30.8%	35.6%	40.0%	36.6%	31.5%	36.4%	42.7%	37.8%	33.4%	37.5%	41.9%	36.8%
Interest Expense	17.1	17.1	17.0	17.4	16.6	16.8	17.3	17.9	18.2	18.6	18.9	19.1	19.5	20.0	20.4	21.0
Income Before Taxes	24.0	37.7	59.1	41.7	30.9	42.7	55.1	43.5	33.2	46.4	71.4	50.1	39.9	52.3	74.2	51.6
Provision for Income Taxes	9.7	15.2	23.7	16.0	12.5	16.9	21.6	16.8	13.3	18.6	28.6	19.5	16.0	20.9	29.7	20.1
Implied Tax Rate	40.4%	40.2%	40.1%	38.4%	40.5%	39.5%	39.3%	39.5%	40.0%	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	19.9	27.9	42.9	30.6	24.0	31.4	44.5	31.5
Reclassification adj. for gains reported in net income			(0.2)			0.0										
Unrealized gain on securities																
Unrealized holding gain on investments	-	0.2	0.0		0.0	0.2	(0.1)	0.2								
Minimum pension liability adjustment																
Comprehensive Income	14.3	22.7	35.2	25.7	18.4	26.1	33.3	26.8	19.9	27.9	42.9	30.6	24.0	31.4	44.5	31.5
Diluted Net Income Per Share	0.11	0.17	0.26	0.19	0.14	0.19	0.25	0.20	0.15	0.20	0.31	0.22	0.17	0.23	0.32	0.23
Weighted Avg. Shares	134.0	134.1	135.3	135.6	135.9	135.9	136.3	136.5	136.8	137.3	137.7	138.2	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%	5.8%	6.6%	17.1%	8.9%	8.7%	8.0%	6.8%	7.8%
Operations & Maintenance/Revenue	46.2%	43.2%	37.7%	41.2%	43.4%	41.0%	37.9%	39.3%	43.3%	40.0%	36.9%	38.0%	41.1%	38.8%	37.8%	39.1%
EBIT (% of rev.)	29.6%	36.3%	43.0%	36.9%	30.8%	35.6%	40.0%	36.6%	31.5%	36.4%	42.7%	37.8%	33.4%	37.5%	41.9%	36.8%
General taxes as % of revenue	8.7%	7.2%	6.3%	6.7%	7.5%	7.1%	6.9%	7.3%	7.5%	7.0%	6.0%	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	81.2	95.4	121.8	101.5	92.2	105.3	128.0	107.2
Net Income Growth	-15.0%	-5.0%	19.9%	3.0%	28.3%	14.6%	-5.4%	3.9%	8.4%	7.8%	28.1%	14.6%	20.3%	12.7%	3.9%	3.0%
EPS Growth	-15.5%	-5.3%	18.6%	1.8%	26.5%	13.0%	-6.1%	3.2%	7.7%	6.8%	26.7%	13.2%	19.2%	11.6%	2.9%	2.0%

Source: Company reports and Longbow estimates

Aqua America - Annual Income Statement
Garik Shmois/ Vishal Khetriwal, CFA
Longbow Research
216-525-8414
(dollars in millions, except per share data)

FY ends December 31	FY04A	FY05A	FY06A	FY07A	FY08A	FY09A	FY10E	FY11E
Total Operating Revenue	**442.0**	**496.8**	**533.5**	**602.5**	**627.0**	**670.5**	**736.5**	**793.7**
Operation & Maintenance	178.3	203.1	219.6	253.1	262.1	270.1	289.8	310.4
Depreciation	54.6	60.7	70.9	83.2	88.8	103.0	111.2	120.1
Amortization	4.3	4.7	4.1	4.8	5.5	11.9	12.8	13.6
General Taxes	27.6	31.7	33.3	45.4	44.7	48.1	50.3	54.2
	-		-					
Total Expenses	**264.8**	**300.3**	**327.9**	**386.5**	**401.2**	**433.1**	**464.1**	**498.3**
Income from Operations	**177.2**	**196.5**	**205.6**	**216.0**	**225.8**	**237.5**	**272.4**	**295.4**
Operating Margin (%)	**40.1%**	**39.6%**	**38.5%**	**35.9%**	**36.0%**	**35.4%**	**37.0%**	**37.2%**
Allow. for Borrowed Funds Used in Const.	2.3	2.4	3.9	3.0	3.7	2.9	3.1	3.1
Gain (loss) on sale of other assets	1.3	1.2	1.2	3.5	1.6	0.5	0.5	0.5
Other	-	-	-	-				
EBIT	**180.8**	**200.1**	**210.7**	**222.5**	**231.1**	**240.8**	**275.9**	**299.0**
EBIT (%)	**40.9%**	**40.3%**	**39.5%**	**36.9%**	**36.9%**	**35.9%**	**37.5%**	**37.7%**
Interest Expense	48.7	52.1	58.4	66.9	68.6	68.6	74.8	80.9
Income Before Taxes	132.1	148.1	152.3	155.5	162.5	172.2	201.1	218.1
Provision for Income Taxes	**52.1**	**56.9**	**60.2**	**60.5**	64.6	67.8	80.0	86.7
Implied Tax Rate	**39.4%**	**38.4%**	**39.6%**	**38.9%**	**39.7%**	**39.4%**	**39.8%**	**39.8%**
Net income	80.0	91.2	92.0	95.0	97.9	104.4	121.2	131.4
Reclassification adj. for gains reported in net incom	(0.2)	-	-	(1.3)	(0.2)			
Unrealized gain on securities	0.1	-	-	-				
Unrealized holding gain on investments	-	-	0.2	1.1	0.2	0.3	-	-
Minimum pension liability adjustment	(1.7)	(1.3)	3.1		-	-	-	-
Comprehensive Income	**78.1**	**89.8**	**95.3**	**94.8**	**97.9**	**104.7**	**121.2**	**131.4**
Diluted Net Income Per Share	**0.64**	**0.71**	**0.70**	**0.71**	**0.73**	**0.77**	**0.88**	**0.95**
Weighted Avg. Shares	125.7	129.2	131.8	133.6	134.7	136.1	137.5	138.8
Financial Summary (values in %)								
Revenue Growth	20.4%	12.4%	7.4%	12.9%	4.1%	6.9%	9.8%	7.8%
Operations & Maintenance/Revenue	40.3%	40.9%	41.2%	42.0%	41.8%	40.3%	39.3%	39.1%
Dep/Net Fixed Asset	3.0%	2.9%	3.1%	3.3%	3.2%	3.4%	3.5%	3.5%
Depreciation Growth	12.5%	11.3%	16.7%	17.3%	6.7%	16.0%	8.0%	8.0%
General taxes as % of revenue	6.2%	6.4%	6.2%	7.5%	7.1%	7.2%	6.8%	6.8%
Interest Exp/Average Net Debt	5.6%	5.3%	5.8%	5.9%	5.2%	5.3%	5.3%	5.4%
Interest Expense/Revenue	11.0%	10.5%	11.0%	11.1%	10.9%	10.2%	10.2%	10.2%
EBITDA	239.7	265.6	285.7	310.5	325.4	355.7	400.0	432.7
Net income growth	13.0%	13.9%	0.9%	3.3%	3.1%	6.6%	16.1%	8.4%
Average ROE	11.4%	11.7%	10.6%	10.0%	9.6%	9.7%	10.7%	11.0%
EPS Growth (ex special items and FAS 123)	7.0%	10.9%	-1.0%	1.9%	2.2%	5.5%	15.0%	7.4%

Source: Company reports and Longbow estimates

LONGBOW Research — March 15, 2010

WATER INDUSTRY PEER VALUATION

($ in millions, except per share data)

							52 Week				Earnings per Share			P/E		Dividend	Price/
Company	Ticker	FY End	Rating	Target	% Upside	Share Price	Hi	Lo	Mkt Cap	Revenue Last FY	Last FY	Current FY	Next FY	Current FY	Next FY	Rate	Book
U.S. WATER UTILITIES																	
American Water Works	**AWK**	**Dec.**	**BUY**	**$24**	**15%**	**$ 20.96**	**$23.77**	**$16.42**	**$ 3,672**	**$ 2,337**	**1.25**	**1.40**	**1.60**	**14.9x**	**13.1x**	**4.0%**	**1.3x**
Aqua America	**WTR**	**Dec.**	**Neutral**			**$ 16.88**	**$20.37**	**$15.39**	**$ 2,295**	**$ 671**	**0.77**	**0.88**	**0.95**	**19.1x**	**17.8x**	**3.4%**	**2.2x**
American States Water	**AWR**	**Dec.**	**Neutral**			**$ 32.50**	**$38.79**	**$29.92**	**$ 625**	**$ 361**	**1.63**	**1.71**	**2.08**	**19.1x**	**15.6x**	**3.1%**	**1.8x**
California Water Service Group	**CWT**	**Dec.**	**BUY**	**$43**	**18%**	**$ 36.55**	**$44.06**	**$33.49**	**$ 762**	**$ 449**	**1.95**	**2.00**	**2.40**	**18.2x**	**15.2x**	**3.2%**	**1.8x**
Artesian Resources Corporation	ARTNA	Dec	NR			$ 18.08	$18.85	$12.95	$ 139	$ 61	0.97	*1.12*	*n/a*	16.1x	*n/a*	4.0%	1.3x
Consolidated Water Co	CWCO	Dec	NR			$ 14.50	$21.29	$6.35	$ 209	$ 60	0.65	*0.8*	*0.8*	18.1x	18.1x	2.1%	1.5x
Connecticut Water Service	CTWS	Dec	NR			$ 23.99	$26.44	$17.57	$ 205	$ 61	1.23	*1.2*	*1.44*	20.0x	16.7x	3.8%	1.9x
Middlesex Water Company	MSEX	Dec	NR			$ 17.58	$18.00	$12.16	$ 235	$ 91	0.72	*0.8*	*0.89*	22.0x	19.8x	4.1%	1.7x
Pennichuck Corporation	PNNW	Dec	NR			$ 21.01	$24.80	$18.50	$ 99	$ 33	0.55	*0.74*	*0.79*	28.4x	26.6x	3.4%	1.8x
York Water Company	YORW	Dec	NR			$ 14.02	$17.95	$11.12	$ 179	$ 37	0.64	*0.72*	*0.72*	19.5x	19.5x	3.6%	2.0x
U.S. Water Utility Average														19.5x	18.0x	3.5%	1.7x
EQUIPMENT/FILTRATION/TREATMENT SECTOR																	
Calgon Carbon Corp.	CCC	Dec.	NR			$ 16.36	$19.31	$10.93	$ 885	$ 412	0.69	*0.80*	*0.96*	20.5x	17.0x	0.0%	2.5x
Danaher	DHR	Dec.	NR			$ 78.12	$78.13	$51.18	$ 25,146	$ 11,185	3.53	*4.08*	*4.63*	19.1x	16.9x	0.2%	2.1x
ITT Technologies	ITT	Dec.	NR			$ 53.01	$56.95	$34.25	$ 9,678	$ 10,905	3.78	*4.06*	*4.49*	13.1x	11.8x	1.9%	2.3x
Layne Christensen	LAYN	Jan.	NR			$ 29.63	$35.14	$15.69	$ 577	$ 1,008	0.85	*0.95*	*1.45*	31.2x	20.4x	0.0%	0.7x
Mueller Water Products	MWA	Sept	NR			$ 4.67	$5.93	$2.14	$ 748	$ 1,428	-0.29	*0.02*	*0.15*	NM	31.1x	1.4%	1.9x
Nalco	NLC	Dec.	NR			$ 23.68	$26.63	$11.02	$ 3,250	$ 3,747	0.95	*1.36*	*1.65*	17.4x	14.4x	0.6%	7.5x
Pall Corp.	PLL	Jul.	NR			$ 38.87	$41.82	$18.20	$ 4,774	$ 2,329	1.77	*2.28*	*2.28*	17.0x	17.0x	1.6%	3.2x
Pentair	**PNR**	**Dec.**	**BUY**	**$37**	**19%**	**$ 34.16**	**$34.88**	**$18.33**	**$ 3,373**	**$ 2,692**	**1.47**	**1.85**	**2.28**	**18.5x**	**15.0x**	**2.2%**	**1.6x**
Watts Water Technologies	**WTS**	**Dec.**	**Neutral**			**$ 31.18**	**$32.96**	**$16.27**	**$ 1,146**	**$ 1,234**	**1.54**	**1.60**	**1.88**	**19.5x**	**16.6x**	**1.4%**	**1.3x**
Equipment/Filtration/Treatment Average (*ex BWTR and CCC)														19.5x	17.8x	1.0%	2.6x
WATER RESOURCES/ INFRASTRUCTURE																	
Insituform Technologies	INSU		NR			$ 27.18	$27.47	$12.86	$ 1,061	$ 727	1.04	*1.48*	*1.73*	18.4x	15.8x	0.0%	1.5x
Lindsay Manufacturing	LNN		NR			$ 43.47	$47.45	$22.31	$ 531	$ 336	1.11	*1.35*	*1.82*	27.9x	25.9x	0.7%	2.5x
Tetra Tech	TTEK		NR			$ 20.88	$32.00	$19.51	$ 1,293	$ 2,287	1.22	*1.14*	*1.32*	18.5x	15.8x	0.0%	2.5x
Water Resources/ Infrastructure Average														21.6x	19.2x	0.2%	2.2x
Relevant Indices						**Share Price**											
Dow Jones Industrials	DJ30					$ 10,625											
S&P 500	SPX					$ 1,150											
Nasdaq Composite	NDX					$ 1,924											

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.

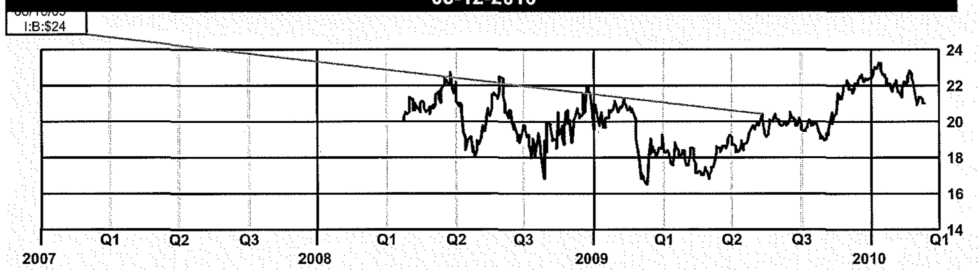
LONGBOW Research

March 15, 2010

G. Shmois
216-525-8414

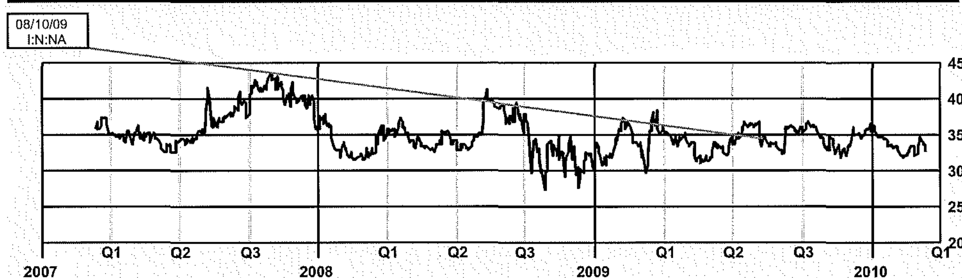
V. Khetriwal, CFA
216-525-8469

Rating and Price Target History for: American Water Works Company, Inc. (AWK) as of 03-12-2010



Created by BlueMatrix

Rating and Price Target History for: American States Water Company (AWR) as of 03-12-2010



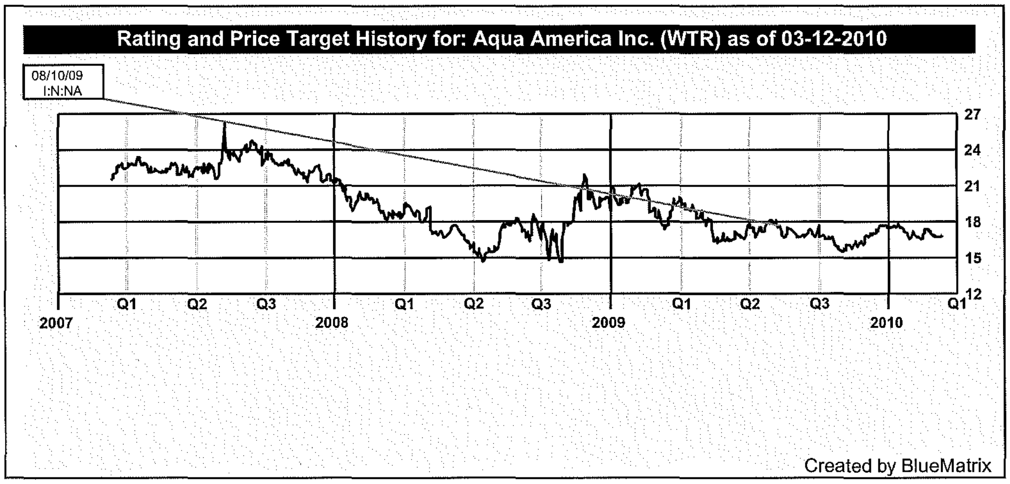
Created by BlueMatrix

Rating and Price Target History for: California Water Service Group (CWT) as of 03-12-2010

Created by BlueMatrix

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469



APPENDIX

IMPORTANT DISCLOSURES

REGULATION ANALYST CERTIFICATION ("REG AC"): The Research Analyst(s) who prepared this research report hereby certifies that the views expressed in the research report accurately reflect the analyst(s) personal views about the subject companies and their securities. The Research Analyst(s) also certifies that the Analyst(s) have not been, are not, and will not be receiving direct or indirect compensation for expressing the specific recommendation(s) or view(s) in this report.

GENERAL DISCLOSURES: Longbow Securities does not make a market in any securities, nor does it hold a principal position in any security. Security prices in this report may either reflect the previous day's closing price or an intraday price, depending on the time of distribution. Consensus estimates are derived from either Thomson/Reuters, Bloomberg or Baseline. Designated trademarks and brands are the property of their respective owners.

SPECIFIC DISCLOSURES:

- Longbow Securities does not make a market in the securities of any company mentioned in this report, and is not a market maker in any securities. Nor does the firm hold a principal position in any security.

- As of the date of this report, no officer, director or stockholder of Longbow Securities, or any member of their immediate families, holds securities of any company mentioned in the report. In the event such persons purchase, hold or sell securities of a company mentioned in the report for their own account, any subsequent report shall disclose the fact of any such ownership or transactions.

- As of the date of this report, no employee of Longbow Securities serves on the Board of Directors of the subject security or any other security mentioned in this report.

- As of the date of this report, neither the Research Analyst nor a member of the Research Analyst's household has a financial interest in the securities of the subject company or any other security mentioned in this report.

- As of the date of this report, neither the Research Analyst nor a member of the Research

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

Analyst's household serves on the Board of Directors of the subject company or any other security mentioned in this report.

- As of the date of this report, neither Longbow Securities nor its affiliates beneficially own 1% or more of an equity security of the subject company or any other security mentioned in this report.

RATINGS DISTRIBUTIONS FOR LONGBOW RESEARCH:

Rating Category	Count	Percent
Buy	86	38.6%
Neutral	135	60.5%
Sell	2	0.9%

RATING SYSTEM:

"Buy" means that Longbow Securities expects total return to exceed 20% over a 12-month period.

"Neutral" means that Longbow Securities expects total return to be within a range of plus or minus 20% over a 12-month period.

"Sell" means that Longbow Securities expects total return to be negative by greater than 20% over a 12-month period.

Longbow Research's full research universe and related applicable disclosures can be obtained by calling (216) 986-0700 or via postal mail at: Editorial Department, Longbow Research, 6000 Lombardo Center, Suite #500, Independence, Ohio 44131.

G. Shmois
216-525-8414

V. Khetriwal, CFA
216-525-8469

Macquarie Research
Equities (USA)

MACQUARIE

UNITED STATES

American Water Works

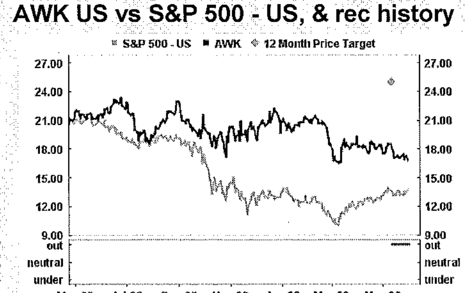
3 June 2009

AWK US		**Outperform**
Stock price as of 02 Jun 09	US$	17.06
12-month target	US$	25.00
12-month TSR	%	+51.3
Valuation	US$	22.45
- PER		
GICS sector		utilities
Market cap	US$m	2,730
30-day avg turnover	US$m	0.0
Number shares on issue	m	160.0

Investment fundamentals

Year end 31 Dec		2008A	2009E	2010E	2011E
Sales revenue	m	2,336.9	2,487.7	2,676.3	2,869.1
EBIT	m	562.7	639.9	706.7	779.3
Reported profit	m	176.1	-227.4	250.6	284.0
Adjusted profit	m	176.1	215.6	250.6	284.0
Gross cashflow	m	442.3	496.9	547.8	596.4
CFPS	US$	2.76	2.96	3.07	3.30
CFPS growth	%	7.1	7.0	3.8	7.7
PGCFPS	x	6.2	5.8	5.6	5.2
EPS adj	US$	1.10	1.28	1.40	1.57
EPS adj growth	%	10.6	16.6	9.4	12.1
PE adj	x	15.5	13.3	12.2	10.8
Total DPS	US$	0.40	0.80	0.84	0.88
Total div yield	%	2.3	4.7	4.9	5.2
ROA	%	4.3	4.8	5.1	5.4
ROE	%	4.1	5.3	6.0	6.6
EV/EBITDA	x	9.6	8.8	8.3	7.6
Net debt/equity	%	128.9	133.2	135.7	136.0
Price/book	x	0.7	0.7	0.7	0.7

AWK US vs S&P 500 - US, & rec history



Source: FactSet, Macquarie Capital (USA), June 2009
(all figures in USD unless noted)

Analyst
Angie Storozynski
1 212 231 2569 angie.storozynski@macquarie.com

Better safe than sorry

Event

- On 1 June, American Water Works announced an equity offering of 26m shares, which includes 14.5m of newly issued shares and 11.5m of existing shares being sold by AWK's largest shareholder, RWE AG. The offering includes an over-allotment option of 3.9m shares owned by RWE.

Impact

- **RWE divestiture – no surprise**: Following the expiration of the 180-day lock-up period after AWK's IPO in October 2008, we expected RWE to continue to shed its stake in AWK. On 1 May 2009, AWK filed a mixed shelf registration, which provided for sales by existing security holders. Following the sale of shares and the additional equity issuance, RWE will hold 85.2m shares (81.3m with the over-allotment), representing 49% (47%) of shares outstanding, and thus RWE would no longer be a majority shareholder of AWK. The divestiture should increase the liquidity of AWK's stock and remove some overhang on the stock associated with the anticipated equity transaction. We await further divestitures.
- **New equity – opportunistic issuance:** While the sale of AWK shares by RWE was long overdue, the new share issuance by AWK was somewhat surprising to us. While AWK's equity-to-capitalization fell to c40% post the 1Q09 goodwill impairment, we believed its equity mix would stabilize and improve organically with rapid earnings growth. We understand, however, that the low equity ratio could have hurt AWK in some of its pending rate cases, which in turn would have triggered attention from credit agencies. Following the offering, we estimate that AWK's 09E equity ratio should improve by 255 bp to 42.8%, which is still below the company's longer-term goal of 45%, but an acceptable level, in our opinion. Net proceeds from the issuance will be used for debt repayments.

Earnings revision

- Our 2009/2010/2011 EPS decline 4%/4%/5% to US$1.28/$1.40/$1.57, reflecting the increase in shares outstanding partially offset by lower interest expense.

Price catalyst

- 12-month price target: US$25.00 based on a combination of PER and DDM methodology.
- Catalyst: Further divestitures by RWE, quarterly earnings and regulatory rate case updates.

Action and recommendation

- We continue to recommend AWK as we see regulatory catch-up translating to accelerated earnings growth through 2012 and capex extending earnings and dividend growth longer term. The sale of shares by RWE is another step towards its goal of fully divesting its ownership of AWK; however, with a sizable stake still remaining, some overhang on stock should remain, we believe.

Valuation and risks

Our 12-month target price of US$25 is an average of our PER and DDM valuations below.

- 16x 2010E PER valuation of US$22.45. Our 16x multiple is based on a historical 18% discount to our regulated water utility base/anchor multiple of 19x.
- Dividend discount model of US$27. Our key assumptions are 5-8% dividend growth from 2009 to 2015, 4% long-term dividend growth and a payout ratio of 40-60%.

Fig 1 Dividend discount model (US$)

	2009E	2010E	2011E	2012E	2013E	2014E	2015E	Terminal
Earnings per share	1.28	1.40	1.57	1.76	1.96	2.21	2.46	
Dividend per share	0.80	0.84	0.88	0.92	0.98	1.06	1.14	37.3
Dividend payout ratio	63%	60%	56%	52%	50%	48%	46%	
Dividend yield	4.6%	4.9%	5.1%	5.3%	5.7%	6.1%	6.6%	
Return on equity	7.2%	7.2%	7.2%	7.2%	7.2%	7.2%	7.2%	7.2%
Long term dividend growth rate								4.0%
Number of years to present	0.5	1.5	2.5	3.5	4.5	5.5	6.5	7.5
Present value of dividends	0.77	0.76	0.74	0.72	0.72	0.72	0.73	22.21
Appraised share price	27.37							

Source: Macquarie Capital (USA), June 2009

Rising 10-year Treasury yields could reduce valuations of regulated utilities

We use the DDM valuation in determining our 12-month target price. Our key assumptions include a beta of 0.65, risk free rate of 4.3% and risk premium of 4.5%. An increase to our long-term risk free rate assumption of 100bps would reduce our DDM valuation by -24% to US$20.75, from US$27.37.

RWE divestiture could have implications on the share price

The pending RWE divestiture carries two potential risks: the near-term overhang of a large-sized offering and potential post-offering valuation dilution. High valuation multiples relative to the broader market and other utility industries could reflect the relatively small market capitalization of the water utility industry (ie, a scarcity premium). Other potential issues include expiration of two regulatory approvals for the divestiture in April 2010 and April 2011, and the Illinois state PUC approval that has been appealed; however, we do not believe that either will impede the RWE sale.

Adequate regulatory recovery is not assured

Public utility commissions and similar state regulatory bodies regulate utility rates and ROEs. The timing and outcome of regulatory proceedings create uncertainty and potential delays (ie, regulatory lag) in cost recovery. In the past, AWK has typically received 50–70% of requested rate increases. Risk of condemnation (ie, acquisition) by governmental entities exists. Lastly, stricter environmental standards could result in significant higher operating costs.

Capital intensity creates execution and financing risk

American Water estimates capital spending of US$4.0–4.5bn for 2009–13. The ability to recover and earn a return on invested capital could materially affect the company's financial position and cash flows. Moreover, completion of capital investment projects is subject to construction and development risks, including availability of capital, complying with permits, meeting budgets and satisfying operating and environmental performance standards.

Goodwill impairment could have negative credit implications and trigger equity needs

As of 31 March 2008, AWK has recorded US$1.3bn of goodwill on its balance sheet, primarily related to the RWE acquisition. The company may be required to impair goodwill in the future if it fails certain valuations tests. Any impairment could have a negative financial (not economic or cashflow) impact and reduce total capitalization. Credit rating agencies could downgrade AWK's credit ratings, which could impede the company's ability to access debt markets for capital. Goodwill impairment charges were US$385m, US$222m, US$509m, US$750m and US$450m in 2005, 2006, 2007, 2008 and 2009, respectively.

Financials

Fig 2 Income statement (US$m, except per share)

	2006	2007	2008	2009E	2010E	2011E	2012E
Sales	2,093	2,214	2,337	2,488	2,676	2,869	3,067
Operating expenses	1,360	1,430	1,503	1,561	1,667	1,772	1,877
Operational EBITDA	733	784	834	926	1,009	1,097	1,190
Depreciation	259	267	271	286	302	317	337
Operational EBIT	474	517	563	640	707	779	853
Net interest expense	368	285	283	303	312	329	343
Ordinary Profit Before Tax	113	254	299	356	414	470	530
Income tax	45	95	123	141	164	186	209
Net group profit of continuing operations	68	159	176	216	251	284	321
Weighted average number of shares (m)	160	160	160	169	179	181	183
Diluted EPS	0.42	1.00	1.10	1.28	1.40	1.57	1.76
Gross dividend per share	NA	NA	0.40	0.80	0.84	0.88	0.92
Dividend payout ratio	NA	NA	36%	63%	60%	56%	52%

Source: Macquarie Capital (USA), June 2009

Fig 3 Cashflow statement (US$m)

	2006	2007	2008	2009E	2010E	2011E	2012E
Net income	-162	-343	-562	-227	251	284	321
D&A, goodwill amortisation	259	267	271	286	302	317	337
Other non cash elements	323	532	943	545	112	129	148
Funds from operations	420	457	652	604	665	731	805
Decrease (increase) in non-cash working capital	(97)	17	(100)	7	(7)	(7)	(8)
Operating cash flow	324	474	552	610	658	724	798
Net investments in fixed assets	(692)	(750)	(1,009)	(930)	(850)	(850)	(850)
Net investments in financial assets	0	4	(25)	0	0	0	0
Free cash flow before dividends	(368)	(273)	(481)	(320)	(192)	(126)	(52)
Dividends paid (group + minorities)	0	0	(64)	(135)	(150)	(159)	(168)
Free cash flow after dividends	(368)	(273)	(546)	(455)	(342)	(285)	(220)
Increase or (repayment) of capital and subsidies	291	977	297	153	292	235	170
Increase or (repayment) of financial debt	(1)	(1,750)	1	302	50	50	50
Adjustment for minorities / miscellaneous	42	1,030	244	0	0	0	0
Increase in cash	(35)	(16)	(4)	0	0	0	(0)

Source: Macquarie Capital (USA), June 2009

Fig 4 Balance sheet ($USm)

	2006	2007	2008	2009E	2010E	2011E	2012E
Cash and cash equivalents	30	13	10	10	10	10	10
Financial and Operating Receivables	185	193	199	211	227	244	261
Inventory	23	27	29	29	31	33	35
Other short-term assets	175	196	180	194	209	223	238
Goodwill	2,962	2,457	1,700	1,250	1,250	1,250	1,250
Other-long term assets	688	729	991	991	991	991	991
Property, plant, and equipment	8,721	9,318	10,124	10,768	11,315	11,848	12,361
Total assets	12,783	12,934	13,232	13,453	14,033	14,599	15,145
Financial liabilities	1,007	317	655	655	655	655	655
Operating liabilities	141	169	150	169	180	191	202
Other liabilities	216	289	300	300	300	300	300
Deferred credits and other regulatory liabilities	2,727	2,914	3,372	3,481	3,608	3,752	3,914
Long-term debt	3,096	4,675	4,624	4,777	5,075	5,316	5,493
Shareholders' equity	5,596	4,571	4,131	4,071	4,215	4,384	4,581
Total liabilities and equity	12,783	12,934	13,232	13,453	14,033	14,599	15,145

Source: Macquarie Capital (USA), June 2009

Important disclosures:

Recommendation definitions

Macquarie - Australia/New Zealand
Outperform – return >5% in excess of benchmark return
Neutral – return within 5% of benchmark return
Underperform – return >5% below benchmark return

Macquarie – Asia/Europe
Outperform – expected return >+10%
Neutral – expected return from -10% to +10%
Underperform – expected return <-10%

Macquarie First South - South Africa
Outperform – expected return >+10%
Neutral – expected return from -10% to +10%
Underperform – expected return <-10%

Macquarie - Canada
Outperform – return >5% in excess of benchmark return
Neutral – return within 5% of benchmark return
Underperform – return >5% below benchmark return

Macquarie - USA
Outperform (Buy) – return >5% in excess of benchmark return (Russell 3000)
Neutral (Hold) – return within 5% of benchmark return (Russell 3000)
Underperform (Sell)– return >5% below benchmark return (Russell 3000)

Recommendations – 12 months

Note: Quant recommendations may differ from Fundamental Analyst recommendations

Volatility index definition*

This is calculated from the volatility of historical price movements.

Very high–highest risk – Stock should be expected to move up or down 60–100% in a year – investors should be aware this stock is highly speculative.

High – stock should be expected to move up or down at least 40–60% in a year – investors should be aware this stock could be speculative.

Medium – stock should be expected to move up or down at least 30–40% in a year.

Low–medium – stock should be expected to move up or down at least 25–30% in a year.

Low – stock should be expected to move up or down at least 15–25% in a year.
* Applicable to Australian/NZ/Canada stocks only

Financial definitions

All "Adjusted" data items have had the following adjustments made:
Added back: goodwill amortisation, provision for catastrophe reserves, IFRS derivatives & hedging, IFRS impairments & IFRS interest expense
Excluded: non recurring items, asset revals, property revals, appraisal value uplift, preference dividends & minority interests

EPS = adjusted net profit / efpowa*
ROA = adjusted ebit / average total assets
ROA Banks/Insurance = adjusted net profit /average total assets
ROE = adjusted net profit / average shareholders funds
Gross cashflow = adjusted net profit + depreciation
*equivalent fully paid ordinary weighted average number of shares

All Reported numbers for Australian/NZ listed stocks are modelled under IFRS (International Financial Reporting Standards).

Recommendation proportions – For quarter ending 31 March 2009

	AU/NZ	Asia	RSA	USA	CA	EUR	
Outperform	40.44%	49.55%	44.83%	38.49%	67.19%	43.84%	(for US coverage by MCUSA, 1.19% of stocks followed are investment banking clients)
Neutral	38.60%	15.57%	39.66%	46.43%	28.12%	39.04%	(for US coverage by MCUSA, 0.25% of stocks followed are investment banking clients)
Underperform	20.96%	34.88%	15.52%	15.08%	4.69%	17.12%	(for US coverage by MCUSA, 0.69% of stocks followed are investment banking clients)

The analyst primarily responsible for the preparation of this research report did not provide the certifications specified in 17 CFR 242.502(a) for the second quarter of 2008.

Analyst Certification: The views expressed in this research accurately reflect the personal views of the analyst(s) about the subject securities or issuers and no part of the compensation of the analyst(s) was, is, or will be directly or indirectly related to the inclusion of specific recommendations or views in this research. The analyst principally responsible for the preparation of this research receives compensation based on overall revenues of Macquarie Group Ltd ABN 94 122 169 279 (AFSL No. 318062)(MGL) and its related entities (the Macquarie Group) and has taken reasonable care to achieve and maintain independence and objectivity in making any recommendations.
Disclaimers: Macquarie Securities (Australia) Ltd; Macquarie Capital (Europe) Ltd; Macquarie Capital Markets Canada Ltd; Macquarie Capital Markets North America Ltd; Macquarie Capital (USA) Inc; Macquarie Capital Securities Ltd; Macquarie Capital Securities (Singapore) Pte Ltd; Macquarie Securities (NZ) Ltd; and Macquarie First South Securities (Pty) Limited are not authorised deposit-taking institutions for the purposes of the Banking Act 1959 (Commonwealth of Australia), and their obligations do not represent deposits or other liabilities of Macquarie Bank Limited ABN 46 008 583 542 (MBL) or MGL. MBL does not guarantee or otherwise provide assurance in respect of the obligations of any of the above mentioned entities. MGL provides a guarantee to the Monetary Authority of Singapore in respect of the obligations and liabilities of Macquarie Capital Securities (Singapore) Pte Ltd for up to SGD 35 million. This research has been prepared for the general use of the wholesale clients of the Macquarie Group and must not be copied, either in whole or in part, or distributed to any other person. If you are not the intended recipient you must not use or disclose the information in this research in any way. Nothing in this research shall be construed as a solicitation to buy or sell any security or product, or to engage in or refrain from engaging in any transaction. In preparing this research, we did not take into account the investment objectives, financial situation and particular needs of the reader. Before making an investment decision on the basis of this research, the reader needs to consider, with or without the assistance of an adviser, whether the advice is appropriate in light of their particular investment needs, objectives and financial circumstances. There are risks involved in securities trading. The price of securities can and does fluctuate, and an individual security may even become valueless. International investors are reminded of the additional risks inherent in international investments, such as currency fluctuations and international stock market or economic conditions, which may adversely affect the value of the investment. This research is based on information obtained from sources believed to be reliable but we do not make any representation or warranty that it is accurate, complete or up to date. We accept no obligation to correct or update the information or opinions in it. Opinions expressed are subject to change without notice. No member of the Macquarie Group accepts any liability whatsoever for any direct, indirect, consequential or other loss arising from any use of this research and/or further communication in relation to this research.
Other Disclaimers: In Canada, securities research is prepared, approved and distributed by Macquarie Capital Markets Canada Ltd, a participating organisation of the Toronto Stock Exchange, TSX Venture Exchange & Montréal Exchange. Macquarie Capital Markets North America Ltd., which is a registered broker-dealer and member of FINRA, accepts responsibility for the contents of reports issued by Macquarie Capital Markets Canada Ltd in the United States and to US persons and any person wishing to effect transactions in the securities described in the reports issued by Macquarie Capital Markets Canada Ltd should do so with Macquarie Capital Markets North America Ltd. Securities research is issued and distributed by Macquarie Securities (Australia) Ltd (AFSL No. 238947) in Australia, a participating organisation of the Australian Securities Exchange; Macquarie Securities (NZ) Ltd in New Zealand, a licensed sharebroker and New Zealand Exchange Firm; Macquarie Capital (Europe) Ltd in the United Kingdom, which is authorised and regulated by the Financial Services Authority (No. 193905); Macquarie Capital Securities Ltd in Hong Kong, which is licensed and regulated by the Securities and Futures Commission; Macquarie Capital Securities (Japan) Limited in Japan, a member of the Tokyo Stock Exchange, Inc., Osaka Securities Exchange Co. Ltd, and Jasdaq Securities Exchange, Inc. (Financial Instruments Firm, Kanto Financial Bureau(kin-sho) No. 231, a member of Japan securities Dealers Association and Financial Futures Association of Japan); Macquarie First South Securities (Pty) Limited in South Africa, a member of the JSE Limited and in Singapore, Macquarie Capital Securities (Singapore) Pte Ltd (Company Registration Number: 198702912C), a Capital Markets Services licence holder under the Securities and Futures Act to deal in securities and provide custodial services in Singapore. Pursuant to the Financial Advisers (Amendment)

Regulations 2005, Macquarie Capital Securities (Singapore) Pte Ltd is exempt from complying with sections 25, 27 and 36 of the Financial Advisers Act. Clients should contact analysts at, and execute transactions through, a Macquarie Group entity in their home jurisdiction unless governing law permits otherwise. Macquarie Capital (USA) Inc., which is a registered broker-dealer and member of FINRA, accepts responsibility for the content of each research report prepared by one of its non-US affiliates when the research report is distributed in the United States by Macquarie Capital (USA) Inc. Macquarie Capital (USA) Inc. affiliate research reports and affiliate employees are not subject to the disclosure requirements of FINRA rules. Any persons receiving this report directly from Macquarie Capital (USA) Inc. and wishing to effect a transaction in any security described herein should do so with Macquarie Capital (USA) Inc. The information contained in this document is confidential. If you are not the intended recipient, you must not disclose or use the information in this document in any way. If you received it in error, please tell us immediately by return e-mail and delete the document. We do not guarantee the integrity of any e-mails or attached files and are not responsible for any changes made to them by any other person. MGL has established and implemented a conflicts policy at group level (which may be revised and updated from time to time) (the "Conflicts Policy") pursuant to regulatory requirements (including the FSA Rules) which sets out how we must seek to identify and manage all material conflicts of interest. Important disclosure information regarding the subject companies covered in this report are available at www.macquarie.com/research/disclosures, or contact your registered representative at 1-888-MAC-STOCK, or write to the Supervisory Analysts, Research Department, Macquarie Securities, 125 W.55th Street, New York, NY 10019. © Macquarie Group

Auckland Tel: (649) 377 6433	**Bangkok** Tel: (662) 694 7999	**Calgary** Tel: (1 403) 218 6650	**Hong Kong** Tel: (852) 2823 3588	**Jakarta** Tel: (62 21) 515 1818	**Johannesburg** Tel: (2711) 583 2000	**Kuala Lumpur** Tel: (60 3) 2059 8833
London Tel: (44 20) 3037 4400	**Manila** Tel: (63 2) 857 0888	**Melbourne** Tel: (613) 9635 8139	**Montreal** Tel: (1 514) 925 2850	**Mumbai** Tel: (91 22) 6653 3000	**Perth** Tel: (618) 9224 0888	**Seoul** Tel: (82 2) 3705 8500
Shanghai Tel: (86 21) 6841 3355	**Singapore** Tel: (65) 6231 1111	**Sydney** Tel: (612) 8232 9555	**Taipei** Tel: (886 2) 2734 7500	**Tokyo** Tel: (81 3) 3512 7900	**Toronto** Tel: (1 416) 848 3500	**New York** Tel: (1 212) 231 2500

Available to clients on the world wide web at www.macquarie.com/research and through Thomson Financial, FactSet, Reuters and Bloomberg.

Electric Utilities and Competitive Power

Reinstatement of Coverage

Equity | United States | Electric Utilities
16 December 2009

Attractive for income, but commodity headaches

Bank of America Merrill Lynch

Steve Fleishman +1 646 855-2906
Research Analyst
MLPF&S
steven.fleishman@baml.com

Ameet I. Thakkar +1 713 247 6037
Research Analyst
MLPF&S
a.thakkar@ml.com

Alex Kania +1 646 855 3753
Research Analyst
MLPF&S
alex.kania@baml.com

Regulated utilities - attractive income vehicle

With an average yield of 4.6% and projected 3.4% dividend growth, traditional regulated utility stocks provide a favorable tax-advantaged income alternative, particularly relative to the shrinking yields on utility bonds. With the recent sector rally, however, some of our best investment ideas are Underperforms.

The competitive power sector - "Flat is the new up"

Hedging largely protected the competitive power sector from the recent collapse in power prices. That said, earnings are heading down as favorable hedges roll off. Companies are essentially trying to run up a downward escalator.

Power market pressures - more than just the economy

The oversupply of natural gas (thanks to shale) and major government support for renewable power and energy efficiency are secular trends that will likely keep a lid on any economy driven power market recovery.

Clean power is long-term winner - the question is timing

We anticipate new environmental requirements on coal generation over the next several years, either through EPA or Congress. These would lead to a shut down of inefficient coal plants and help to reduce the current power supply glut. Nuclear and scrubbed coal will benefit.

Regulateds: CMS, NU, PCG, WEC for growth; ED, TE for yield

We prefer companies with an attractive mix of current yield and dividend growth, a constructive regulatory situation, limited equity financing needs, and strong managements. For higher current yields, ED and TE provide 5% yields with dividend growth potential.

Regulated Underperforms - SO, DUK, DPL, NVE, POR

Our Underperform-rated stocks either have high valuations (SO, DUK), significant external financing needs (SO, POR), or near-term risk to consensus estimates (SO, NVE). For DUK and DPL, we are concerned about the sustainability of their above market rates in Ohio.

Competitive power: prefer ETR over EXC

Within the cleaner power space, we view ETR as undervalued and one of the few companies where earnings should be on an upward trend. Alternatively, we see EXC as fully valued and earnings on a significant downward trend post 2011.

Long-term power recovery plays - FE, NRG, PPL

These companies appear attractively valued in the current low power markets even with stripping out their hedges. We see significant upside if power markets recover. We would avoid those with high valuations and exposure to at-risk coal assets such as DYN and RRI.

Table 1: Stock Ratings and Price Objectives

Buy-rated	Ticker	Rating	PO
American Water Works	AWK	B-1-7	$24
CMS Energy	CMS	B-1-7	$19
Consolidated Edison	ED	A-1-7	$49
Entergy Corp.	ETR	B-1-7	$95
FirstEnergy	FE	B-1-7	$50
Northeast Utilities	NU	A-1-7	$28
NRG Energy	NRG	B-1-9	$29
PG&E Corp.	PCG	A-1-7	$49
PPL Corp	PPL	B-1-7	$35
TECO Energy	TE	B-1-7	$17
Wisconsin Energy	WEC	A-1-7	$53
Neutral-rated	**Ticker**	**Rating**	**PO**
Alliant Energy	LNT	B-2-7	$30
Calpine	CPN	C-2-9	$12
Dominion Resources	D	B-2-7	$38
Edison International	EIX	B-2-7	$38
FPL Group	FPL	B-2-7	$55
Hawaiian Electric	HE	B-2-8	$20
NSTAR	NST	A-2-7	$36
Pinnacle West Capital	PNW	B-2-7	$36
Progress Energy	PGN	A-2-7	$42
SCANA Corp.	SCG	B-2-7	$39
Xcel Energy	XEL	A-2-7	$21
Underperform-rated	**Ticker**	**Rating**	**PO**
DPL Inc.	DPL	B-3-7	$27
DTE Energy	DTE	B-3-7	$44
Duke Energy	DUK	A-3-7	$16
Dynegy	DYN	C-3-9	$1.5
Exelon Corp.	EXC	B-3-7	$44
NV Energy	NVE	B-3-7	$12
Portland General	POR	B-3-7	$20
RRI Energy	RRI	C-3-9	$5
Southern Company	SO	A-3-7	$33

Source: BofA Merrill Lynch Global Research

Refer to important disclosures on page 36 to 38. Analyst Certification on Page 34. Price Objective Basis/Risk on page 28.

Utility sector

Part bond, part commodity

The sector is essentially composed of two diverging stories right now: 1) the regulated utilities which are largely stable bond-like alternatives for investors; and 2) the competitive power companies which are a back-door commodity play

We are resuming coverage of the electric utility and competitive power sector. The sector is essentially composed of two diverging stories right now: 1) the regulated utilities which are largely stable bond-like alternatives for investors; and 2) the competitive power companies which are a back-door commodity play. Investors have been attracted to both bonds and commodities in the current market environment, which would seem to be a plus for utility stocks. However, competitive utilities are highly correlated to the only commodities that remain in a bear market – natural gas and power.

Investment highlights:
1. Attractive income alternatives
2. A contrarian play
3. Supportive state regulation
4. Recovery could be a surprise in 2010
5. Clean power growth opportunities
6. Robust rate base growth despite economy

Investment highlights

1) Attractive income alternatives

Electric utilities provide current yield of 4.6% and we project 3.4% dividend growth. This is superior to owning investment grade utility bonds, particularly on an after-tax basis. These yields are also among the highest among traditional equities and well above S&P 500 levels. Importantly, we do not see any obvious utility dividends at risk of cuts at this point in time.

2) A contrarian play

Utilities have meaningfully underperformed the broader stock market in 2009, rising 1.5% vs. a 23% gain in the S&P 500. Moreover, the recent BofA Merrill Lynch fund manager survey showed utilities at a 40% underweight versus their benchmark, the lowest of any sector.

3) State utility regulation supportive for the most part

Despite the tough economy, utilities have received reasonable rate case outcomes

Despite the tough economy, utilities have received reasonable rate case outcomes. As more utilities update their rates to reflect lower sales forecasts, earned rates of return should rise from current low levels.

4) Economic recovery could be a surprise in 2010

Most utilities have been very cautious about the outlook for economic recovery. We are generally assuming flat to slightly up sales in 2010. If the recovery proves stronger than expected, it could lead to upside to our 2010 estimates. From a power market standpoint, a stronger than expected recovery could spur higher than expected natural gas and power prices, which could help lift some of the down-in-the-dumps competitive power companies.

5) Clean power creates growth opportunities

While the mandated move to cleaner power could depress overall power prices, it does present growth opportunities for the companies positioned to benefit. Growth areas include renewable projects (wind, solar, biomass, etc) and transmission. FPL, NU and NRG are companies that have positioned to grow in these areas. Moreover, the potential upside of carbon cap and trade could be meaningful for those with low-carbon emitting power plants such as ETR and EXC.

6) Rate base growth profile strong despite economy

Utilities continue to grow their capital base at 5-10% annually despite the economic slowdown

Utilities continue to grow their capital base at 5-10% annually despite the economic slowdown. Assuming constructive regulation, this ratebase growth drives earnings growth. Key areas of regulated capital investment include environmental controls, renewables, transmission, new nuclear, smart grid and normal T&D system improvements.

Investment concerns:
1. Competitive power earnings on downward escalator
2. Secular pressures cap economy-driven power recovery
3. Environmental mandates could be the end of old coal
4. Dependence on external funding
5. Dividend tax uncertainty

Investment concerns

1) Competitive power earnings on a downward escalator

We project earnings for the competitive power sector to be trending downward over the next 3-5 years as favorable hedges and capacity payments roll off. Our models assume that natural gas stays in the $6.50 area longer-term, which is well below the level where most hedges were put on. This fall-off in earnings could create more rating agency pressures and also limits the potential for future dividend growth and/or share buybacks. We do not believe that consensus estimates have appropriately reflected how poor the outlook looks at this point in time. The one silver lining is that 2011-2012 is still a bit away so there is time for companies to cross their fingers and hope that power markets improve by then.

Power prices are under pressure from an oversupply of natural gas and unprecedented growth in renewables and energy efficiency

2) Secular pressures cap economy-driven power recovery

The abundance of shale gas has dramatically altered the supply dynamics of the natural gas market. We expect long-term natural gas prices to stay in the $6.50-area. Since natural gas is the marginal fuel in most regions of the US, the low natural gas prices will likely keep power prices depressed as well. Power markets themselves are facing oversupply. The federal stimulus bill combined with state mandates support an unprecedented level of new renewable development and demand reduction programs (ie, energy efficiency) that could meaningfully extend out the time line for supply/demand balance even with a likely economic recovery in 2010.

The costs of retrofitting even the newer plants could eat into the cash flow of coal generators

3) Environmental mandates could be the end of old coal

We anticipate there will be significant new environmental requirements on coal generation over the next five to ten years – SOx, NOx, mercury, ash, and carbon – either through EPA or Congress. While many of the newer, efficient coal plants have been retrofitted, we believe that it will prove uneconomic for many older, smaller coal plants to survive. Companies with large old coal fleets such as EIX's Edison Mission and RRI could be hurt. Moreover, the costs of retrofitting even the newer plants could eat into the cash flow of coal generators.

4) Dependence on external funding

The regulated utility business is heavily reliant on external debt and equity funding particularly given the current high mandated capex requirements of most utilities. While capital markets have rallied strongly from their lows, the crisis last year highlighted the utility model can be at risk in difficult financial markets. If utilities issue equity below book value, it essentially makes their ratebase growth dilutive instead of accretive. This is the reason we are more favorable toward companies that can internally finance their capex plan. Table 2 shows the expected external equity issuers through 2013 based on our financial models.

Table 2: Expected Equity Issuances 2010-2013

Company	Ticker	2010E	2011E	2012E	2013E
Alliant Energy	LNT			250	
CMS Energy	CMS			100	150
Consolidated Edison	ED	200	200	200	200
Dominion Resources	D	150			
DTE Energy	DTE	100			
Edison International	EIX		500	500	500
FPL Group	FPL	200	100		
Northeast Util.	NU			300	
PG&E Corporation	PCG		100	300	
Pinnacle West	PNW	200	100	75	80
Portland General	POR		150		
Progress Energy	PGN		200		
SCANA Corp.	SCG	140	190	340	150
Southern Company	SO	640	660		

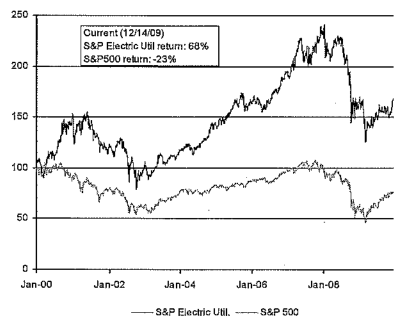
Source: BofA Merrill Lynch Global Research

Dividend tax issue could linger as a big overhang for most of 2010 until it is resolved

5) Dividend taxes - what will happen in 2010?

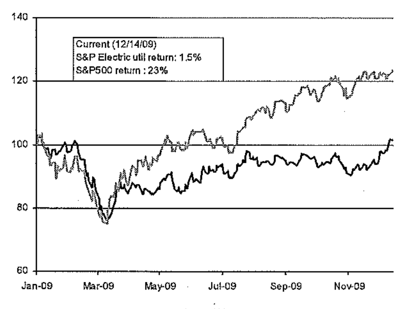
The 15% tax rate on corporate dividends expires at the end of 2010. If no action is taken, taxes on dividends would revert back to ordinary income rates which could be 35% or higher for top tax brackets. The current low dividend tax rate has favored utility stocks versus other income instruments such as corporate and government bonds, which are taxed an at ordinary income rate. If the rate were to go back to ordinary income levels, we expect investors would seek other tax-efficient means for income. The good news is that the Obama administration's proposal on this issue is to raise taxes on dividends to 20% from 15%. We do not believe this would have a noticeable impact on utility valuations as the sector would retain its more favorable tax treatment to bonds. We see some risk that a highly partisan Congress and the fact that 2010 is a mid-term election year could result in no bill getting done. Moreover, this issue could linger as a big overhang for most of 2010 until it is resolved.

Chart 1: S&P Electric Utilities Index v. S&P 500 (January 2000 - Present)



Source: Factset

Chart 2: S&P Electric Utilities Index v. S&P 500 (YTD 2009)



Source: Factset

Stock price performance

For the first time in six years, utilities are underperforming the S&P 500, and by a wide margin. The S&P Utilities Index is up 1.5% versus the 23% gain in the S&P 500. See Chart 1 (S&P Utilities vs S&P 500 2000 to present) and 2 (S&P Utilities vs S&P 500 YTD). We attribute this to end of the safety rally in late 2008 and early 2009 that lifted many regulated utility stocks. Moreover, utilities have not been as immune to the recession as some initially thought. Finally, competitive utilities are most sensitive to the one commodity that has not rallied out of the recession – natural gas.

Valuations

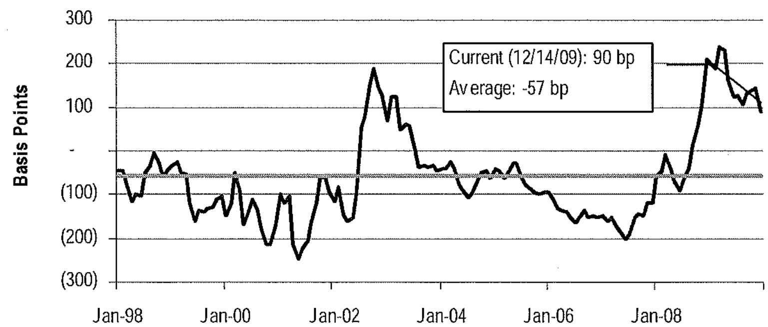
Electric utilities still present attractive income alternative with average dividend yields of 4.6%, projected 3% dividend growth and relatively low P/E valuations of 13x 2010 earnings estimates. Investment grade utility bonds now yield 4.7%, or 3.1% on a 35% federal taxed basis. Even assuming an increase in taxes on dividends to 20% proposed by the Obama administration, utility stocks yield 3.7% after-tax – 60bp above the after-tax yield on corporate bonds. Given fears over inflationary pressures in the future, the growth in utility dividends provides some level of inflation protection which is not provided by bonds. While the sector saw a couple of dividend cuts during the financial crisis (Ameren, Great Plains and Constellation Energy), we see limited risk of dividend cuts in the sector in the near term.

Utility stocks are current trading at a near record spread to utility bonds and at a highly elevated spread to Treasuries. Chart 3 shows that the current yield spread between utility dividend yields and 10-year Treasuries is 90 basis points (utility dividends above Treasuries). The historic average shows that utility dividend yields have usually traded at a 57bp lower yield than Treasuries. While well above average, the spread is still below the 200bp level seen during the market crisis peak in early 2009.

The utility dividend yield versus investment grade utility debt is near record levels today

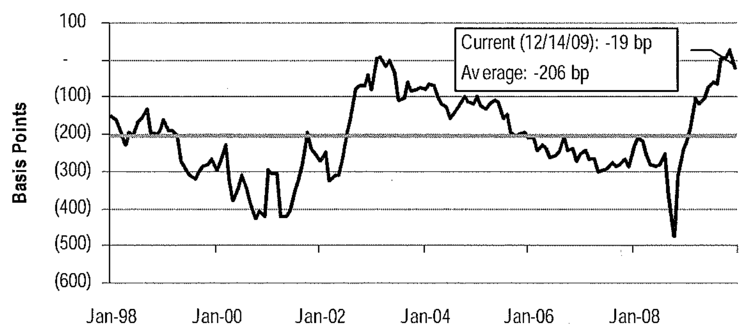
The utility dividend yield versus investment grade utility debt is near record levels today as shown in Chart 4. Utility stocks yield 19bp below utility bonds today. Historically, they have traded at a 206bp discount to utility bond yields. We believe this is the most telling valuation positive for utility stocks at the present time.

Chart 3: S&P Utilities Dividend Index vs. 10-Yr Treasury Yield



Source: Factset

Chart 4: S&P Utilities Index Dividend Yield v. ML Investment Grade Utility Bond Index



Source: Factset and Bloomberg

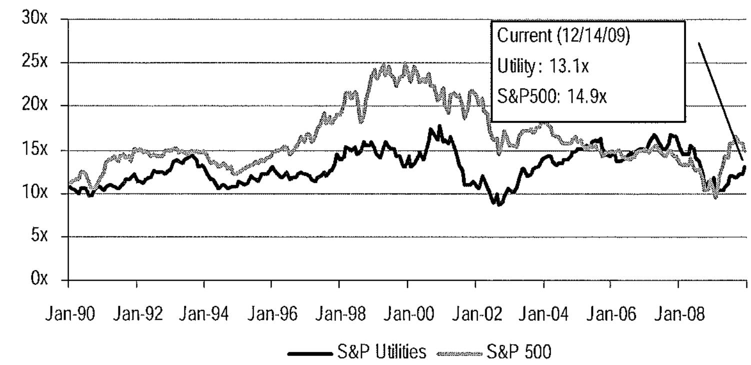
Valuation vs S&P 500 and other income sectors

Utility earnings valuations look slightly above normal compared to the S&P 500, particularly after their recent rally. The group is trading at a relative P/E of 88.1% of the S&P 500, above its historic average of 82.4%. See Charts 5 and 6 (Utility P/E vs. S&P 500 P/E on 2010 estimates – historic relation over time).

Overall, utilities provide a nice mix of current yield plus moderate growth with reasonable valuation

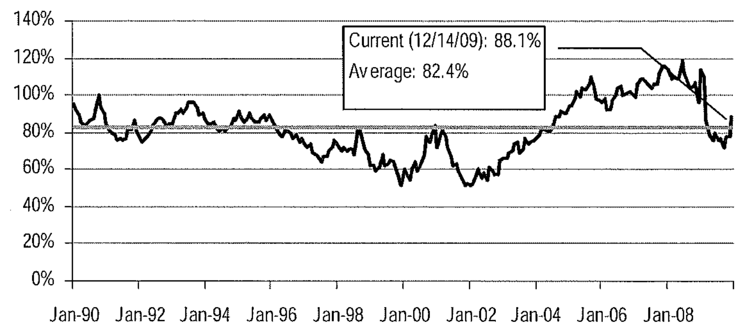
In Table 3, we compare utility P/E, dividend yield and earnings/dividend growth with other income-oriented sectors. Utility P/Es are near the low end of the group and yield is near the high end. While utility earnings and dividend growth is moderate, it is better than comparable sectors such as REITs where both are projected to be down. Telecom looks more attractive on a yield basis, but these companies have much greater competitive threats than the average electric utility. The growth profile of food and staples is superior to utilities, but their current yields are 100bp-200bp lower. Overall, utilities provide a nice mix of current yield plus moderate growth with reasonable valuation.

Chart 5: Utilities Sector and S&P 500 1-Year Forward P/E (January 1990 – Present)



Source: Factset

Chart 6: Utilities Sector P/E Relative to the S&P 500 (January 1990 – Present)



Source: Factset

Table 3: Electric Utilities Valuation v. S&P 500 and Other Income-Oriented Sectors

	P/E			Current	3 Yr EPS	3 Yr DPS
	2009E	2010E	2011E	Div. Yield	CAGR (08-11E)	CAGR (08-11E)
Electric Utilities	12.5	11.8	11.4	4.80%	1.40%	3.50%
S&P 500	17.4	15.0	13.2	2.10%	7.40%	-1.50%
Other Income-Oriented Sectors:						
Diversified Telecommunication Services	12.6	12.5	12.0	6.30%	0.50%	3.80%
REITs	15.3	16.3	17.0	5.00%	-7.70%	-11.90%
Pharmacuticals	11.6	10.9	10.5	3.60%	1.70%	0.40%
Food Products	15.0	14.1	13.4	3.30%	3.70%	5.90%
Consumer Staples	15.4	14.6	13.9	2.80%	3.00%	8.50%

Source: BofA Merrill Lynch Global Research; Bloomberg

Spurred by a lower power price outlook, many competitive utilities have declining eanings profiles that are resulting in a halt to dividend growth and share repurchases

A complication for the utility sector is the declining fortunes of the integrated utilities with large competitive power businesses – Exelon, FirstEnergy, etc. Spurred by a lower power price outlook, many of these companies have declining earnings profiles that are resulting in a halt to dividend growth and share repurchases. Since these companies comprise many of the larger market caps in the sector, they could negatively affect investor views of the whole.

Stock themes

Our Buy-rated names can be bucketed into four themes

Our Buy-rated stocks tend to have lower than average current yield, but well above average dividend growth

1) Regulated income and growth - CMS, NU, PCG, WEC

We prefer companies with an attractive mix of current yield and dividend growth, a constructive regulatory situation, limited equity financing needs, and strong managements. Our Buy-rated stocks tend to have lower than average current yield, but well above average dividend growth.

2) Yield Plays - ED and TE

Both companies have current yields around 5% with modest dividend growth potential.

3) Clean Power and Transmission plays - ETR, NU

ETR is one of the most attractively valued generators but is also a potential upside beneficiary of carbon legislation given its all-nuclear generation fleet. NU is a play on transmission growth as it continues to build out new projects in New England to improve reliability and bring more clean power into the region.

While we are cautious on the power markets, we view FE, NRG and PPL, together with ETR, as attractively valued stocks in the current depressed power markets

4) Long-term power market recovery plays - FE, NRG, PPL

While we are cautious on the power markets, we view FE, NRG and PPL, together with ETR, as attractively valued stocks in the current depressed power markets and significant beneficiaries if power markets improve.

Underperform-rated stocks have four themes as well

While viewed as high quality companies, both SO and DUK have very little growth potential in the near term

1) Regulateds: SO, DUK, NVE, POR

While viewed as high quality companies, both SO and DUK have very little growth potential in the near term. For SO, consensus forecasts look too high and we see need for a lot of external equity issuances. For DUK, our concern is valuation and potential downsides in Ohio. For NVE, our near term estimates are well below consensus. Our concern for POR is regulatory risk and equity needs.

2) Ohio companies with higher rates - DPL and DUK

Both these companies are operating under constructive rate plans until 2011/2012. However, under Ohio law, new electric security plans need to be better than market and both companies could face significant downward earnings to get rates closer to market.

3) Competitive Power downward earnings stories - EXC

We believe the market is not reflecting the downside risk of EXC as above market hedges roll-off.

DYN and RRI are highly valued on current power markets. While leveraged to a power market recovery, they could face increased environmental risks and plant closures over time

4) Coal exposure - DYN and RRI

DYN and RRI are highly valued on current power markets. While leveraged to a power market recovery, they could face increased environmental risks and plant closures over time.

Tables 4-6 display estimates for our Regulated Utilities, Diversified Utilities and Competitive Power coverage versus consensus. Tables 7-9 provide our valuations by sub-industry.

Table 4: EPS Estimates for our Regulated Utilities Coverage v. Consensus

Company Name	Ticker	2010E BofA ML	2010E Cons	2011E BofA ML	2011E Cons	2012E BofA ML	2012E Cons	2013E BofA ML	2013E Cons
Alliant	LNT	$2.49	$2.56	$2.77	$2.91	$2.71	NA	$2.79	NA
CMS Energy	CMS	1.35	1.35	1.39	1.48	1.43	1.57	1.54	NA
ConEd	ED	3.51	3.32	3.73	3.44	3.79	3.48	3.86	3.55
DPL Inc.	DPL	2.37	2.51	2.50	2.66	2.51	NA	1.98	NA
DTE Energy	DTE	3.42	3.37	3.52	3.51	3.65	3.71	3.72	3.94
Duke	DUK	1.31	1.29	1.34	1.35	1.35	1.39	1.42	1.42
Hawaiian	HE	1.16	1.65	1.82	1.79	1.98	NA	2.08	NA
Northeast Util.	NU	1.95	1.93	2.18	2.16	2.31	2.35	2.56	2.61
NSTAR	NST	2.60	2.51	2.77	2.64	2.86	2.75	2.94	2.95
NV Energy	NVE	0.94	1.10	0.98	1.12	1.35	1.24	1.38	NA
PG&E	PCG	3.41	3.40	3.73	3.70	3.90	3.83	4.14	3.91
Pinnacle West	PNW	2.98	2.93	2.87	2.93	3.20	3.41	3.46	3.55
Portland Gen.	POR	1.56	1.58	1.76	1.88	1.82	1.94	1.88	2.00
Progress	PGN	3.09	3.18	3.30	3.29	3.45	3.41	3.69	3.50
SCANA	SCG	2.86	2.94	3.21	3.29	3.35	3.39	3.54	3.51
Southern	SO	2.32	2.43	2.53	2.61	2.64	2.76	2.73	2.94
TECO	TE	1.29	1.29	1.35	1.41	1.42	1.45	1.49	1.48
Wisconsin	WEC	3.58	3.75	4.07	4.04	4.27	4.32	4.52	4.46
Xcel	XEL	1.63	1.63	1.72	1.73	1.82	1.86	1.96	1.98

Source: BofA Merrill Lynch Global Research; Factset; Reuters

Table 5: EPS Estimates for our Diversified Utilities Coverage v. Consensus

Company Name	Ticker	2010E BofA ML	2010E Cons	2011E BofA ML	2011E Cons	2012E BofA ML	2012E Cons	2013E BofA ML	2013E Cons
Dominion	D	$3.18	$3.26	$3.09	$3.25	$3.16	$3.36	$3.18	$3.61
Edison Intl.	EIX	3.35	3.34	3.21	3.37	3.31	3.31	3.19	3.99
Entergy	ETR	6.81	6.74	6.99	7.11	7.04	7.41	6.94	7.35
Exelon	EXC	3.70	3.90	4.05	4.37	3.39	3.64	3.34	3.84
FirstEnergy	FE	3.68	3.54	4.01	4.20	3.98	4.33	3.98	4.04
FPL Group	FPL	4.61	4.57	4.64	4.86	4.80	4.97	5.02	5.33
PPL Corp.	PPL	3.42	3.28	3.21	3.17	3.09	3.18	2.81	3.22

Source: BofA Merrill Lynch Global Research; Factset; Reuters

Table 6: EBITDA Estimates for our Competitive Power Producers Coverage v. Consensus

Company Name	Ticker	2010E BofA ML	2010E Cons	2011E BofA ML	2011E Cons	2012E BofA ML	2012E Cons	2013E BofA ML	2013E Cons
Calpine	CPN	1,510	1,455	1,487	1,529	1,534	1,413	1,538	1,387
Dynegy	DYN	425	490	523	614	547	591	571	583
NRG Energy	NRG	2,218	2,295	1,720	2,101	1,918	2,137	1,781	2,004
RRI Energy	RRI	350	423	393	479	421	282	409	NA

Source: BofA Merrill Lynch Global Research; Factset; Reuters

Table 7: Regulated Utilities Comparables

Company Name	Ticker	Current Price	BofA ML Rating	Mkt Cap ($M)	P/E 2010E	P/E 2011E	P/E 2012E	P/E 2013E	Div Yield	Div Growth (E)	Payout Ratio	Price/ Book	09 Equity Ratio
Alliant	LNT	$30.49	B-2-7	$3,356	12.3x	11.0x	11.3x	10.9x	4.9%	2.0%	80.7%	1.2x	52%
CMS Energy	CMS	15.46	B-1-7	3,594	11.4x	11.1x	10.8x	10.1x	3.2%	13.1%	40.2%	1.4	29%
ConEd	ED	45.03	A-1-7	12,350	12.8x	12.1x	11.9x	11.7x	5.2%	1.7%	74.0%	1.1	48%
DPL Inc.	DPL	28.58	B-3-7	3,253	12.1x	11.4x	11.4x	14.4x	4.0%	3.3%	56.2%	3.0	43%
DTE Energy	DTE	43.94	B-3-7	7,255	12.8x	12.5x	12.0x	11.8x	4.8%	2.5%	64.9%	1.2	41%
Duke	DUK	17.65	A-3-7	22,722	13.5x	13.2x	13.1x	12.4x	5.4%	2.0%	80.8%	1.0	57%
Hawaiian	HE	20.77	B-2-8	1,757	18.0x	11.4x	10.5x	10.0x	6.0%	0.0%	121.2%	1.5	50%
Northeast Util.	NU	25.83	A-1-7	4,393	13.3x	11.9x	11.2x	10.1x	3.7%	4.9%	53.7%	0.9	40%
NSTAR	NST	35.21	A-2-7	3,761	13.5x	12.7x	12.3x	12.0x	4.3%	6.1%	63.2%	1.4	39%
NV Energy	NVE	12.49	B-3-7	2,930	13.2x	12.8x	9.2x	9.1x	3.2%	8.8%	49.1%	0.9	37%
PG&E	PCG	45.14	A-1-7	17,348	13.2x	12.1x	11.6x	10.9x	3.7%	6.0%	53.2%	1.7	50%
Pinnacle West	PNW	37.44	B-2-7	3,786	12.6x	13.0x	11.7x	10.8x	5.6%	1.2%	90.6%	1.1	48%
Portland Gen.	POR	21.01	B-3-7	1,534	13.5x	11.9x	11.5x	11.2x	4.8%	3.5%	73.4%	1.0	47%
Progress	PGN	41.51	A-2-7	11,721	13.5x	12.6x	12.0x	11.3x	6.0%	0.0%	81.9%	1.2	45%
SCANA	SCG	37.49	B-2-7	4,574	13.1x	11.7x	11.2x	10.6x	5.0%	2.1%	70.2%	0.9	41%
Southern	SO	34.10	A-3-7	27,042	14.7x	13.5x	12.9x	12.5x	5.1%	2.1%	75.3%	1.8	42%
TECO	TE	15.90	B-1-7	3,380	12.4x	11.8x	11.2x	10.7x	5.0%	2.4%	81.2%	1.6	38%
Wisconsin	WEC	47.87	A-1-7	5,658	13.4x	11.8x	11.2x	10.6x	2.8%	12.3%	43.5%	1.6	40%
Xcel	XEL	21.48	A-2-7	9,807	13.2x	12.5x	11.8x	11.0x	4.6%	3.0%	66.2%	1.3	45%
Average					**13.3x**	**12.2x**	**11.5x**	**11.2x**	**4.6%**	**3.4%**	**69.4%**	**1.4x**	**44%**

Source: BofA Merrill Lynch Global Research; Pricing as of 12/15/09 close

Table 8: Diversified Utilities Comparables

Company Name	Ticker	Current Price	BofA ML Rating	Mkt Cap ($M)	P/E 2010E	P/E 2011E	P/E 2012E	P/E 2013E	Implied Genco EV / EBITDA 2010E	2011E	2012E	2013E	FCF / Yield 2010E	2011E	2012E	2013E	Div Yield
Dominion	D	$39.25	B-2-7	$23,233	12.3x	12.7x	12.4x	12.3x	7.0x	8.1x	8.3x	8.9x	(3.2%)	(0.5%)	2.5%	3.2%	4.5%
Edison Intl.	EIX	36.12	B-2-7	11,811	10.8x	11.2x	10.9x	11.3x	7.1x	7.9x	7.9x	10.4x	(16%)	(14%)	(17%)	(13%)	3.4%
Entergy	ETR	83.00	B-1-7	16,198	12.2x	11.9x	11.8x	12.0x	5.7x	5.5x	5.5x	5.9x	11%	11%	12%	12%	3.6%
Exelon	EXC	51.05	B-3-7	33,757	13.8x	12.6x	15.1x	15.3x	8.0x	7.3x	9.5x	10.0x	8%	3%	2%	2%	4.1%
FirstEnergy	FE	47.24	B-1-7	14,390	12.8x	11.8x	11.9x	11.9x	8.7x	7.9x	7.8x	7.8x	4%	4%	3%	2%	4.7%
FPL Group	FPL	55.40	B-2-7	22,437	12.0x	11.9x	11.6x	11.0x	7.9x	8.7x	9.1x	9.4x	(5%)	(9%)	(7%)	(6%)	3.4%
PPL Corp.	PPL	32.38	B-1-7	12,183	9.5x	10.1x	10.5x	11.5x	5.9x	6.4x	6.8x	7.7x	3%	0%	2%	3%	4.3%
Average					**11.9x**	**11.7x**	**12.0x**	**12.2x**	**7.2x**	**7.4x**	**7.8x**	**8.6x**	**0.3%**	**(0.7%)**	**(0.4%)**	**0.4%**	**4.0%**

Source: BofA Merrill Lynch Global Research; Pricing as of 12/15/09 close

Table 9: Competitive Power Producers Comparables

Company Name	Ticker	Current Price	BofA ML Rating	Mkt Cap ($M)	EBITDA (unadjusted) 2010E	2011E	2012E	2013E	EV/EBITDA (unadjusted) 2010E	2011E	2012E	2013E	Free Cash Flow Yield (unadjusted) 2010E	2011E	2012E	2013E
Calpine	CPN	$11.43	C-2-9	$5,551	1,510	1,487	1,534	1,538	10.3x	10.6x	9.4x	9.0x	6.9%	7.6%	8.5%	9.0%
Dynegy	DYN	$1.91	C-3-9	$1,608	425	523	547	571	14.7x	12.0x	11.4x	10.8x	(11.3%)	(3.7%)	2.3%	6.4%
NRG Energy	NRG	$25.85	B-1-9	$7,005	2,218	1,720	1,918	1,781	6.1x	7.9x	7.1x	7.6x	9.4%	4.6%	8.8%	7.5%
RRI Energy	RRI	$5.60	C-3-9	$1,966	350	393	421	409	9.2x	7.9x	7.0x	6.7x	4.6%	6.9%	8.6%	9.1%
Average									**10.1x**	**9.6x**	**8.7x**	**8.5x**	**2.4%**	**3.8%**	**7.1%**	**8.0%**

Source: BofA Merrill Lynch Global Research; Pricing as of 12/15/09 close

Financial models

We are introducing in-depth financial models of our coverage including:

1. **Full subsidiary financial statements.**

2. **Detailed analysis of cash flows** between the subsidiaries and holding company.

3. **Plant by plant generation models** for the competitive power companies

Regulated utilities assumptions

We generally assume 0-1% sales growth for 2010 and 1-2% in 2011 and beyond

We generally assume 0-1% sales growth for 2010 and 1-2% in 2011 and beyond. Our models include detailed assumptions on future rate cases with a focus on the factors that could cause continued regulatory lag. We also model each regulated utility within a company separately so that we are careful to determine which subsidiaries are underearning or overearning. Finally, we do a detailed cash flow model of each subsidiary to see how much capital is available to dividend to the parent. Given that many utilities are in large capital spending programs, dividends to the parent are generally lower these days. This is why many utilities need external equity in order to fund their dividend to shareholders and keep the consolidated balance sheet in good position.

Regulated utilities valuation

We value regulated utilities at an average P/E of 12x our 2011 earnings estimates

From a valuation standpoint, we value regulated utilities at an average P/E of 12x our 2011 earnings estimates. We adjust this valuation to reflect premiums for certain higher quality regulation and companies (eg, PCG, SO, etc) as well as higher growth business such as transmission (NU). We then use an S-O-P methodology to capture other factors such as NOLs, non-regulated businesses, cash on hand, etc.

Competitive power assumptions

Our current estimates reflect power prices that are close to current market forwards on companies unhedged power positions

For our financial models, we use a consistent deck of power prices for each regional power market. Our current estimates reflect power prices that are close to current market forwards on companies unhedged power positions. Our long-term gas price assumption is $6.50, which is slightly below the current market at $6.80 in 2012 and also consistent with the BofA Merrill Lynch fundamental natural gas price expectations in the $6.00 area.

For capacity, we use the results of the recent PJM and NEPOOL auctions. For the May 2010 PJM auction for 2013/2014 capacity, we are assuming an RTO price of $75/MW-day. This is up from the last auction at $16/MW-day, but well below prior auctions that came in over $100/MW-day.

Power prices can vary dramatically based on location and product. We have been diligent in our models about making sure these differences are included. For location, we make sure that any relevant basis spreads to key trading hubs are reflected in our forecasts. On product, we look carefully at how companies sell their power – retail vs. wholesale; full requirements vs. block power. The margins on these different products can vary meaningfully so we have spent considerable time addressing this situation.

Competitive power valuation

We use a multiple of 8x 2011 adjusted EBITDA for the competitive business

From a valuation standpoint, we use a multiple of 8x 2011 adjusted EBITDA for the competitive business. We think this multiple is a relatively generous number, but it is also reflective of EBITDA that we believe is currently closer to cyclical lows than highs. We adjust our EBITDA for the value of hedges that are in or out of the money, so that it reflects more of a sustainable EBITDA level. We then add back the hedge value as an offset to debt. We believe this creates a better framework for comparability among the companies.

For carbon, we do an additional valuation assuming a $10/ton carbon price in our adjusted EBITDA

For carbon, we do an additional valuation assuming a $10/ton carbon price in our adjusted EBITDA. We then give a 25% weighting to the resulting price target reflecting the uncertainty over timing and levels of carbon cap and trade.

Competitive power companies

The downward escalator problem

Given the negative supply/demand dynamics discussed in more detail below, the competitive power business is facing significant pressures. Hedging has masked much of these pressures for the time being, but they are likely to come to roost over the next couple of years.

For 2009-2011, many companies have hedged energy revenues that were locked in when power prices were meaningfully higher. Thus, their hedged power prices are much higher than the open power prices.

Competitive power revenues typically come from three sources – hedged energy revenues, unhedged or open energy revenues, and capacity revenues. For 2009-2011, many companies have hedged energy revenues that were locked in when power prices were meaningfully higher. Thus, their hedged power prices are much higher than the open power prices.

Open power prices are very low, but they are in contango in every region, which means that forward power prices are higher in 2010 than 2009 and higher in 2011 than 2010.

Additionally, capacity revenues in the centralized capacity markets in the PJM and New England regions were initially very high due to expected tight supply/demand conditions. However, the impact of the economy and increased energy efficiency programs has caused capacity revenues to be set at lower levels in future years.

For most companies, the roll-off of high hedged energy revenues and high capacity revenues creates substantial earnings pressure over the next 3-5 years

For most companies, the roll-off of high hedged energy revenues and high capacity revenues creates substantial earnings pressure over the next 3-5 years. The fact that open power prices rise over this period is helpful, but the 2011-2013 open prices are still well below most companies' hedge prices. To give an example of this, Table 10 shows Exelon's hedge prices, open prices, and capacity prices and then summarizes what happens to overall revenues. The table shows that Midwest prices fall to $41.14/mwh by 2013 from $47.15/mwh in 2010. Beyond 2013, there are even more favorable hedges that roll-off afterward.

Table 10: EXC Hedged, Open and Capacity Prices

	2009E	2010E	2011E	2012E	2013E
NI Hub					
Hedged price	$47.00	$46.50	$44.50	$46.00	$53.48
Open price	24.39	28.30	34.41	36.54	37.29
Capacity price	3.15	4.33	4.16	1.69	1.54
NI Hub (Capacity+Energy)	$46.57	$47.15	$43.95	$40.61	$41.14
PJM-West					
Hedged price	$40.00	$40.00	$59.00	$52.50	$59.00
Open price	36.23	43.27	50.12	52.22	52.52
Avg. Capacity price	4.81	5.52	4.16	3.76	4.09
PJM-East					
Hedged price	$50.44	$50.36	$60.50	$52.75	$0.00
Open price	39.37	46.30	54.21	56.46	57.06
Avg. Capacity price	5.28	5.52	4.16	3.87	4.17
Mid-Atlantic (Capacity+Energy)	$49.30	$49.41	$65.51	$62.30	$64.11

Source: Company presentations, PJM Interconnection, and BofA Merrill Lynch Global Research estimates

For nuclear utilities like EXC, carbon could significantly raise power prices while not impacting their costs

Exelon provides a good example of one factor that could change this cycle, which is carbon cap and trade. For nuclear generators like EXC, carbon could significantly raise power prices while not impacting their costs. Assuming a $10 carbon price in 2013, we estimate EXC could see a $5/MWh increase in their realized prices in Table 10. Nonetheless, carbon would only bring EXC earnings back to 2011 levels given the imbedded pressures from hedges rolling off.

In Table 11, we show the hedge profile of all the competitive power companies in our coverage universe.

Table 11: Hedge Power Profile of Competitive Power Companies

Company name	Ticker	Region	Plant Type	2009E	2010E	2011E	2012E	2013E
Dominion Resources	D							
		NEPOOL	Coal	94%	65%	13%	8%	5%
		NEPOOL	Nuclear	91%	70%	25%	10%	10%
		PJM	Coal	94%	77%	49%	20%	10%
Edison International	EIX							
		PJM	Coal	34%	30%	0%	0%	0%
		Midwest	Coal	38%	65%	3%	0%	0%
Entergy Corp	ETR							
		Various	Nuclear	86%	88%	63%	25%	18%
Exelon Corp	EXC							
		NI Hub	Nuclear	99%	90%	68%	44%	12%
		PJM-East	Nuclear	96%	93%	59%	19%	0%
		PJM-West	Various	99%	87%	70%	33%	24%
FirstEnergy	FE							
		Midwest	Various	100%	67%	25%	0%	0%
FPL Group	FPL							
		Various	Various	95%	82%	85%	73%	68%
PPL Corporation	PPL							
		PJM-West	Various	99%	100%	90%	55%	30%
		Mid-C	Various	96%	90%	83%	73%	30%

Source: Company presentations

Table 12 also shows the realized power prices – hedged plus unhedged plus capacity that we project for each company as well.

Table 12: Expected Realized Power Prices and Capacity Revenues for Competitive Power Companies

Company name	Ticker		Region/Type	2009E	2010E	2011E	2012E	2013E
Dominion Resources	D							
		Realized Power Prices ($/MWh)	NEPOOL	$75.52	$64.60	$62.54	$63.35	$63.23
		Total Capacity Revenue ($M)		297	348	310	236	210
Edison International	EIX							
		Realized Power Prices ($/MWh)	PJM MAAC	47.47	49.24	43.12	45.22	45.52
			NI Hub	41.19	47.76	39.81	41.33	42.18
		Total Capacity Revenue ($M)		296	384	328	179	175
Entergy Corp	ETR							
		Realized Power Prices ($/MWh)	Nuclear	57.63	55.65	55.17	55.73	55.08
		Total Capacity Revenue ($M)		124	150	148	130	119
Exelon Corp	EXC							
		Realized Power Prices ($/MWh)	NI Hub	46.69	44.60	41.24	40.68	39.17
			PJM-East	50.00	50.08	57.94	55.75	57.06
			PJM-West	39.98	40.43	56.36	52.31	54.10
		Total Capacity Revenue ($M)		117	622	986	620	617
FirstEnergy	FE							
		Realized Power Prices ($/MWh)	Various	55.49	53.92	60.10	63.62	63.19
		Total Capacity Revenue ($M)		28	35	29	20	21
FPL Group	FPL							
		Realized Power Prices ($/MWh)	Various	52.14	53.49	57.46	56.39	56.91
		Total Capacity Revenue ($M)		181	169	136	101	84
PPL Corporation	PPL							
		Realized Power Prices ($/MWh)	PJM-West	47.91	63.00	62.01	60.60	58.36
			Mid-C	46.39	49.05	54.76	55.37	53.18
		Total Capacity Revenue ($M)		63	557	428	374	402

Source: BofA Merrill Lynch Global Research estimates

Visualizing this, most competitive power companies are trying to go up a downward escalator. They will need to work very hard just to stay where they are.

Competitive power industry

Ugh!

The economic recession combined with unfavorable weather drove down power prices to record lows

The competitive power market was a mess in 2009. The economic recession combined with unfavorable weather drove down power prices to record lows. Overall, power demand is down 4.7% year to date through August – the largest decline ever recorded in the US.

Hedging is good news today....

The good news is that most competitive power companies came into the year heavily hedged, which is typical for the industry. As a result, companies captured power prices that were dramatically higher than the current spot market. Many companies also have favorably priced hedges that extend into 2010 and 2011.

...but leads to future earnings cliffs.

This hedge profile sets the stage for potential earnings cliffs as hedges roll off and companies are more exposed to the current forward power curves that are much lower than the past.

The bad news is that this hedge profile sets the stage for potential earnings cliffs as hedges roll off and companies are more exposed to the current forward power curves that are much lower than the past.

Won't recovery bring power prices back?

Not likely

We expect there will be some recovery in power prices, but there are secular pressures that have arisen in the power sector that will likely put a lid on it

We expect there will be some recovery in power prices, but there are secular pressures that have arisen in the power sector that will likely put a lid on it. We discuss these secular pressures in more detail below.

Natural gas oversupply - blame it on the shale!

While demand will come back, the shale gas has ample room to expand and marginal costs of production are low (less than $5/Mcf)

Just two years ago, the US looked to be in a chronically short natural gas position. The only potential savior then was LNG, but even LNG faced high global demand and price spikes. Brewing under the surface, new technology had revived gas reserves in shale rock in areas like the Barnett in Texas. As this technology proved out, shale rock became the new gusher from Haynesville to Fayetteville and then to the large Marcellus shale in PA and NY. The shale gas has proven to be more plentiful than anyone initially imagined and the wells also produce prolifically. This new shale gas has been coming to market at the same time that gas demand has been hurt by the recession, particularly industrial demand. While demand will come back, the shale gas has ample room to expand and marginal costs of production are low (less than $5/Mcf).

The result is that the near to intermediate term natural gas outlook now looks like an oversupplied market with limited chance of price spikes above the $7/Mcf area

The result is that the near to intermediate term natural gas outlook now looks like an oversupplied market with limited chance of price spikes above the $7/Mcf area. This scenario can change – for example, shale gas has quick decline rates and can have potential environmental impacts (water and risk of ground instability). Natural gas use in the power sector will also continue to rise if prices stay this low. Nonetheless, Shale gas has been a game changer for natural gas prices. We use long-term natural gas prices of $6.50/Mcf in our valuations.

Why do natural gas prices matter so much?

The introduction of shale gas and resulting lower natural gas prices have had a very negative impact on power prices

Well, natural gas prices set the marginal price of power in most regions of the US during peak hours. In fact, natural gas plants are on the margin in the West, New England and Texas during most hours. To that end, the introduction of shale gas and resulting lower natural gas prices have had a very negative impact on power prices.

The renewables boom - on the come

Actions by the Obama administration combined with state mandates for renewable standards are supporting a sizable increase in renewables power supply

Actions by the Obama administration combined with state mandates for renewable standards are supporting a sizable increase in renewables power supply, irrespective of whether the power is needed or not. The tax credits in the 2009 Stimulus Bill were well beyond anything this tax driven industry had seen before. Not only was the production tax credit (PTC) extended to 2012, but a new investment tax credit (ITC) and convertible ITC was introduced. The ITC allows a company to get 30% of its investment back in a renewable project while it is essentially being constructed. Finally, the Bill also provided DOE loan support for renewable projects.

ITC expiration in 2012 could spur a flood of renewables

The impact of the Stimulus Bill has been mitigated in 2009 by the recession and investment uncertainty as the DOE tax credit rules were not finalized until the summer. However, we believe there could be a virtual boom in renewable project additions in the 2010-2012 period. One of the biggest drivers is the deadline for the convertible ITC. A project must have started construction by YE 2010 and achieve operation by YE 2012 to obtain the 30% ITC. This will create tremendous pressure to get projects moving in this time frame. This timing also dovetails with state renewable mandates increasing in the 2012-2015 period.

Both the tax credits and state mandates make this renewable build almost inevitable, regardless of the current economics (which do not look very good at $6-$7/Mcf natural gas).

The bottom line is that renewable additions could add over 10,000MWs per year over the next 3-5 years, or nearly 5% to overall supply

The bottom line is that renewable additions could add over 10,000MWs per year over the next 3-5 years, or nearly 5% to overall supply. While this is tempered by the fact that renewables are not firm power (particularly wind typically operates only 35% capacity factors), this is still a meaningful supply increase at a time when demand growth has been pushed out.

Energy efficiency = lower demand

The utility industry is implementing its most aggressive demand reduction initiatives in history

At the same time that renewables are increasing supply, the utility industry is implementing its most aggressive demand reduction initiatives in history. This is again a function of federal support as well as state requirements for energy efficiency. Table 13 shows demand reduction targets of some key states.

Table 13: State Energy Efficiency Targets*

State	Approx. Annual Savings Target	Year of Implementation
Delaware	2.5%	2009
Massachusetts	2.4%	2008
Vermont	2.0%	2000
Indiana	2.0%	2010
New York	1.9%	2011
Maryland	1.5-1.8%	2008
Iowa	1.5%	2008
Minnesota	1-1.5%	2010
Ohio[1]	1.3%	2009
Illinois[2]	1.2%	2008
Hawaii	1.0%	2004
Connecticut	1.0%	2007
Colorado	1.0%	2009
Pennsylvania	1.0%	2009
Washington	1.0%	2010
California	0.9%	2004
North Carolina	0.8%	2012
Nevada	0.6%	2007
New Mexico[2]	0.7%	2008
Michigan[3]	0.3%	2008
Texas	0.3%	2009

* Energy is electric and natural gas; 1. Target is average through 2025; 2. Target is average through 2020; 3. Target ramps up to 1% in 2012
Sources: "The 2009 State Energy Efficiency Scorecard," American Council for an Energy-Efficient Economy, October 2009; and state regulatory commissions

Energy efficiency has been discussed for years, but it has generally been a case of all talk, no action. We believe it is different this time for a few reasons:

- **Several states are mandating it** and utilities tend to follow what their local regulators and politicians tell them to do.
- **Many states have set up favorable regulatory mechanisms** to make it more attractive for utilities to do it, such as revenue decoupling and direct incentive fees.
- **Smart grid implementation** will provide better information to allow for utilities and customers to help shave peak power usage.

Bottom line: power is in a bear market

The intermediate trends in the competitive power sector are negative

To sum it up, the intermediate trends in the competitive power sector are negative. Supply is rising thanks to renewables as well as some new fossil generation. Demand growth will be slower than before due to serious energy efficiency plans. Finally, the price of the marginal fuel – natural gas – is likely to stay depressed in the near-term thanks to an abundance of shale gas. While further in the future, we also believe that the push for new nuclear plants is real and will also be a potential long-term supply threat.

Potential game changers

There are a couple of trends that could change the power supply/demand outlook meaningfully over the LT; 1) the shutdown of old, dirty coal plants; 2) the potential for new electric usage for technologies such as electric cars

Our experience tells us that when things look bleakest, it is time to look for silver linings. There are a couple of trends that could change the power supply/demand outlook meaningfully over the long term. On the supply side, the shutdown of old, dirty coal plants is inevitable – it's just a matter of time as we discuss below. On the demand side, the potential for new electric usage for technologies such as electric cars could be impactful. This will take time, but the more power prices stay low, the more pressure there will be for new uses.

Environmental - a matter of time

The utility industry and investors have been bracing for increased environmental controls for some time. If anything, that time has been extended due to the temporary court overturning of the CAIR rule (SOx and NOx reduction) and the delay in cap and trade legislation on carbon.

EPA

Increased environmental controls on coal plants are just a matter of time

Nonetheless, increased environmental controls on coal plants are just a matter of time. We expect the EPA to propose a new CAIR rule for SOx and NOx by early next year and implement by 2011. The general scuttlebutt has been that the new rule may be tougher than the old one. Moreover, the EPA is working on new rules for mercury reduction and for control of coal ash ponds. The EPA is also working on a carbon reduction requirement even as Congress is debating cap and trade.

Carbon

No carbon bill does not mean no carbon reduction; the EPA will move forward in regulating carbon under the Clean Air Act on its own

The potential for Congress to pass a cap and trade bill in 2010 is still very much up in the air. Most companies in the utility industry would like to see a carbon bill as it would provide investment certainty and reduce the role of EPA in setting the carbon rules. However, the devil of the bill is in the details and every allowance that goes into one side hand creates a problem for other sides. If Congress does not pass a carbon bill, the EPA will move forward in regulating carbon under the Clean Air Act on its own. Recent court rulings have given the EPA this authority and it plans to fully use it. Thus, no carbon bill does not mean no carbon reduction.

Timing uncertain; outcome not in doubt

While timing remains very fluid, the ultimate outcomes of future environmental mandates are pretty clear in our opinion:

- **Coal plants that are smaller, less efficient and dirty (ie unscrubbed) will be shut down** over time unless they are specifically needed for local reliability reasons.
- **Remaining coal plants will have higher costs**. Even natural gas plants will have higher costs if carbon is implemented.

- **Electric supply will shrink** with the shut down of old coal plants.
- **Power prices will go up**.
- **Low-cost and clean power sources will be winners** – nuclear, renewables and to a lesser extent natural gas and fully-scrubbed, efficient coal plants.

Prefer clean generators

Given this direction, we have a strong strategic preference to cleaner power generators such as ETR, FPL and EXC (at the right price)

Given this direction, we have a strong strategic preference to cleaner power generators such as ETR, FPL and EXC (at the right price). In the event that a generator has a lot of coal plants, we prefer those that have added environmental controls already, such as PPL, FE and NRG versus those that have not.

Transmission - highly impactful/slow to come

Electric transmission is a very popular area in the electric business right now for four reasons.

1. **Reliability** – the historic reason transmission was built. NU's Southwest Connecticut and NEEWS projects are examples of reliability-driven transmission.
2. **Bringing renewables to market** – Transmission is a critical piece of the strategy to allow new renewables to access the higher demand areas. For example, the wind blows hardest in west Texas zone, but the people are primarily in the north and south Texas zones. Thus, FPL's recent Lone Star line and the Texas CREZ project would help make this happen. Same with ITC's proposed Green Power Express in the Midwest and NU's HydroQuebec line.
3. **Power market economics** – connecting low-price regions with high-price regions. AYE and AEP's PATH line would help connect the lower-priced western PJM markets to the higher priced eastern PJM market. The HQ line could do the same in New England as it would bring down lower-priced hydro power from Canada.
4. **FERC incentive regulation –** The FERC regulates the transmission business and has generally provided both attractive ROEs, meaningful incentives for important new projects, and timely cost recovery.

The FERC regulates the transmission business and has generally provided both attractive ROEs

With all of these factors, one would think that transmission would be a sure thing as it can help consumers as well as provide attractive returns to the companies. However, reality is much more complicated for two reasons:

1. **Cost allocation** – transmission lines have typically been shared across the regional power market. However, companies and regulators do not want to pay for regional transmission that does not benefit their customers or in fact hurts their customers. As a result, we are starting to see more proposals for participant-funded transmission (ie, lines paid for by only those customers who benefit).
2. **Siting** – Transmission remains difficult to permit thanks to the local siting requirements and NIMBY. The FERC currently has backstop authority to site a line in the event that a state does not act on a site permitting. However, FERC cannot overturn a state siting decision. Strong federal siting authority over transmission is one of the key issues in pending energy legislation.

Benefit to renewables & companies in low priced markets

Over time, the impact of transmission build will be more renewables reaching load centers and a flattening of prices within regional power markets

Despite these hurdles, we expect transmission to be built. Over time, the impact will be more renewables reaching load centers and a flattening of prices within regional power markets. Thus, companies that are currently mired in low-priced power markets may see more long-term upside than those in high priced power markets.

Electric car

The best thing for electric utilities since air conditioning?

Despite the hurdles, the electric car is another potential game changer and one that could be a much-needed demand driver for the power sector.

While it is fun to postulate about electric cars, the reality is still many years away in terms of a meaningful impact on power supply/demand

The advent of the electric car is receiving a lot of press as well as a lot of attention in the electric power industry. Electric cars would use batteries charged at home or at external charging stations. These batteries could lead to substantially increased electricity usage over time. That said, the goal is to charge electric cars overnight during off-peak periods when many power plants are not running at the present time – this would limit any impact on peak demand. In fact, electric car batteries could act as storage devices that could be used to sell power during peak periods at some point in time.

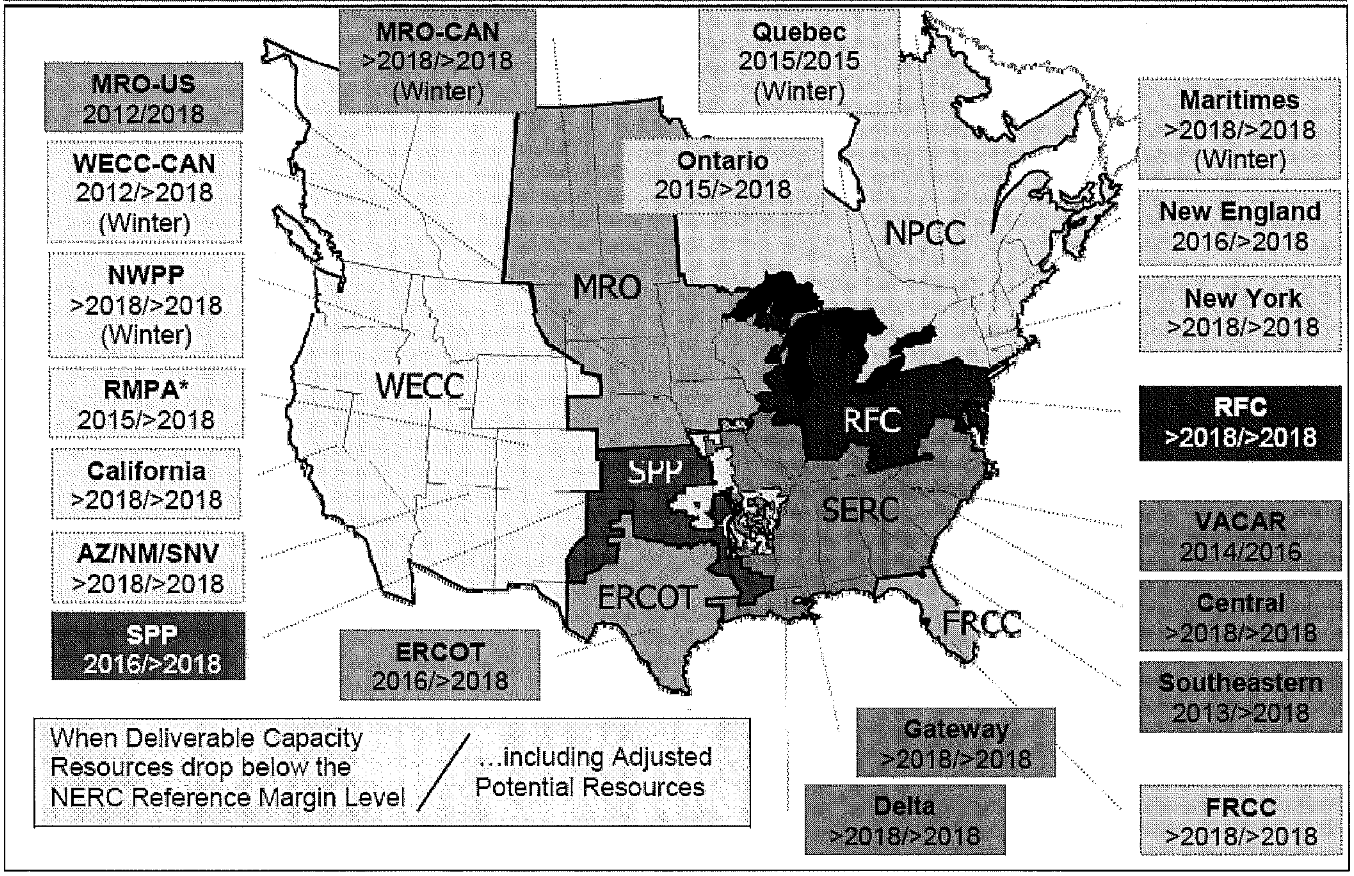
While it is fun to postulate about electric cars, the reality is still many years away in terms of a meaningful impact on power supply/demand. It will take a long time for enough electric cars to be sold and for the infrastructure to be in place to service the industry. One issue that PG&E mentioned at a power conference is that the distribution system is not set up for the electric car. If three people in a neighborhood were charging their electric cars at once, it would collapse the local distribution system. There may need to be significant new infrastructure added to allow households to charge electric cars.

Supply/demand outlook

NERC does not see reserve margins falling below targeted levels until 2015 and beyond in most major market areas

The latest North American Reliability Council data highlight the widening supply/demand gap in the power markets. As shown in Chart 7, NERC does not see reserve margins falling below targeted levels until 2015 and beyond in most major market areas. The only exception is the upper Midwest, MRO region, but this is a largely regulated market where utilities will be the likely provider of new supply.

Chart 7: Prospective and Adjusted Potential Reserve Margins Compared to NERC's Reference Margin Level



Source: "2009 Long-Term Reliability Assessment 2009-2018," North American Electric Reliability Corporation, October 2009, Figure 2

The NERC data also highlights a continued reduction in peak demand growth over the last several years

The NERC data also highlights a continued reduction in peak demand growth over the last several years. The 2009 report shows 10-year peak demand growth projected at 14.8%. The 2008 report had peak demand growth of 16.8%. See details in Table 14.

Table 14: Net Internal Demand and Energy Growth

NERC Long-Term Reliability Assessment	Peak Demand Growth (%)	Energy Growth (%)
2005 Report - (2005 to 2014)	19.8	18.2
2006 Report - (2006 to 2015)	19.0	17.2
2007 Report - (2007 to 2016)	17.7	16.9
2008 Report - (2008 to 2017)	16.8	15.7
2009 Report - (2009 to 2018)	14.8	14.5

Source: "2009 Long-Term Reliability Assessment 2009-2018," North American Electric Reliability Corporation, October 2009, Table 2

Opportunities

It is pretty clear that the future NERC forecast is highly dependent on new renewable generation. The variable nature of this generation, particularly wind, will create more variability in prices.

Looking more closely at the NERC data, it is pretty clear that the future forecast is highly dependent on new renewable generation – 260,000MWs. The variable nature of this generation, particularly wind, will create more variability in prices with potential for lower lows when the wind is blowing and higher highs when it is not. This could create opportunities for generators, such as flexible natural gas plants, that are not obvious when looking at just overall supply/demand.

The NERC data does not assume any major reduction in coal fired generation. If power prices remain low, coal will likely shutdown. We believe this is the most likely factor that will drive a recovery in power markets.

Additionally, the NERC data does not assume any major reduction in coal fired generation. If power prices remain low, it will be very hard for coal plants to make an economic decision to spend capex for retrofits. The result will be a round of plant shutdowns and some recovery in power prices. We believe this will take time to play out, but it is probably the most likely factor that will drive a recovery in power markets.

Key drivers for regulated utilities

Many regulated utilities are underearning

Many utilities have faced lower earned returns on common equity and associated regulatory lag than seen since the major nuclear construction days of the 1980s

While the regulated utility outlook has been more stable than most other sectors during the recent recession and potential recovery, there have been some unprecedented pressures. Industrial sales for many utilities fell 20% starting in Q4 2008. Customer growth turned negative in states like Florida. The weaker sales came at the same time that many regulated utilities are pursuing sizeable capital programs for investments in a range of mandates – environmental controls, renewables, smart meters, etc. The result is that many utilities have faced lower earned returns on common equity and associated regulatory lag than seen since the major nuclear construction days of the 1980s. Table 15 displays this trend by showing the variety of earned returns we are projecting for our utility coverage.

Table 15: Projected Regulated Returns on Equity

Ticker	Utility	2009E	2010E	2011E	2012E	2013E
CMS	Consumers Electric	10.7%	10.5%	10.5%	10.4%	10.5%
DPL	Dayton Power & Light	17.2%	18.7%	18.1%	18.6%	14.3%
DTE	Detroit Edison	10.0%	10.6%	10.4%	10.4%	10.3%
DUK	Duke Energy	9.7%	10.5%	10.0%	10.6%	10.5%
ED	Con Ed of New York	9.3%	9.9%	10.2%	10.1%	10.1%
HE	Hawaiian Electric Co.	5.5%	6.5%	8.5%	8.8%	9.0%
LNT	Interstate Power & Light	7.5%	9.2%	10.0%	9.7%	9.8%
	Wisconsin Power & Light	6.5%	9.7%	9.9%	9.9%	9.9%
NST	NSTAR Electric	12.2%	12.6%	12.5%	12.5%	12.4%
NU	Connecticut Light & Power Co.	8.2%	8.6%	10.5%	9.0%	9.0%
	Public Service Co. of New Hampshire	7.6%	8.8%	9.0%	9.0%	9.0%
	Western Massachusetts Electric Co.	7.9%	8.6%	8.9%	9.0%	9.0%
	NU Transmission Segment	12.1%	12.2%	12.4%	12.5%	13.0%
NVE	Nevada Power Co.	6.6%	7.6%	6.1%	9.2%	9.1%
	Sierra Pacific Power Co.	6.0%	5.5%	10.1%	10.1%	10.2%
PCG	Pacific Gas & Electric Co.	11.4%	11.5%	11.5%	11.5%	11.5%
PNW	Arizona Public Service	6.6%	8.5%	8.2%	8.9%	9.3%
POR	Portland General Electric Co.	7.4%	7.8%	9.2%	9.4%	9.5%
PGN	Progress Energy Carolinas	10.1%	9.7%	9.1%	9.1%	9.1%
	Progress Energy Florida	9.7%	10.0%	10.5%	10.5%	10.5%
SCG	South Carolina Electric & Gas	8.7%	9.0%	9.9%	10.1%	10.0%
SO	Alabama Power Co.	14.6%	13.7%	13.6%	13.5%	13.4%
	Georgia Power Co.	11.2%	11.5%	12.5%	12.6%	12.6%
	Gulf Power Co.	11.9%	11.8%	11.8%	11.8%	11.7%
	Mississippi Power Co.	13.5%	13.5%	13.5%	13.5%	13.5%
TE	Tampa Electric	9.4%	11.2%	10.9%	11.2%	11.2%
WEC	Wisconsin Electric Power Co.	10.9%	10.3%	10.4%	10.5%	10.8%
XEL	Northern States Power - MN Electric	10.4%	10.2%	10.1%	10.1%	10.5%
	Public Service Co. of Colorado Electric	6.9%	8.6%	8.7%	9.0%	9.2%
Average		**9.6%**	**10.2%**	**10.6%**	**10.7%**	**10.7%**

Source: BofA Merrill Lynch Global Research estimates

State regulatory policies a critical variable

These trends have made the quality of state utility regulation as important as ever. It's not just about allowed rates of return on equity these days – if a company is allowed an 11% ROE but is able to earn 7-8% actual ROEs is not a good outcome. Key diffentiators include:

- **Forward vs historic test years** (forward is good to get new capex into rates on a timely basis)
- **Timeliness of rate relief** and rate case process
- **Decoupling of sales** to protect against economy risk and/or conservation risk
- **Cost trackers** such as pension and uncollectibles.
- **Investment trackers** to allow timely recovery of new capex for large capex programs.

Potential for earnings recovery

The good news is that the regulatory model typically allows utilities to catch-up from periods of underearning

The good news is that the regulatory model typically allows utilities to catch-up from periods of underearning. If sales loads are lower now due to the economy, this can get adjusted through a lower actual sales number (in a historic test year) or a lower sales forecast (forward test year). The same is true for cost increases such as pensions or bad debts. Thus, as new rate plans catch-up with the new economic reality, we should see utility earned returns on equity improve.

State regulation reasonable despite the weak economy

Many states are viewing their local utility as one of bastions of local job growth and investment and are in fact creating more supportive regulation as a result

The one caveat is the political aspect of regulation – voters don't like electric rate increases. We have seen rate increases become a political football recently in Florida where Governor Crist came out against FPL and PGN rate hikes and forced a change-out of 2 of the 5 commissioners. Surprisingly, this politicization of utility regulation has been more the exception than the rule during the recession. Many states are viewing their local utility as one of bastions of local job growth and investment and are in fact creating more supportive regulation as a result. Examples here are numerous – decoupling and uncollectible trackers in Michigan; CWIP recovery for new nuclear in SC, FL and Georgia; higher allowed ROEs in NY; special recovery clauses and rate riders for new investments in Virginia; and new multi-year rate settlements in Arizona.

The regulated utility model - ratebase growth

Despite the weakness in the economy, utility ratebase growth is still relatively high as a result of a number of clean power mandates

Regulated utilities are allowed to earn a reasonable return on the capital that they invest in the business. The ratebase is essentially the net capital (after depreciation) that is invested. When a utility files a rate case, it files its proposed ratebase for the relevant test year and also files for the appropriate capital structure (equity ratio) and allowed rate of return (ROE). Under this traditional regulation, the ratebase growth essentially drives the growth in earnings power for the company. Despite the weakness in the economy, utility ratebase growth is still relatively high as a result of a number of clean power mandates – environmental controls, renewable standards, transmission, smart meters, energy efficiency, etc.

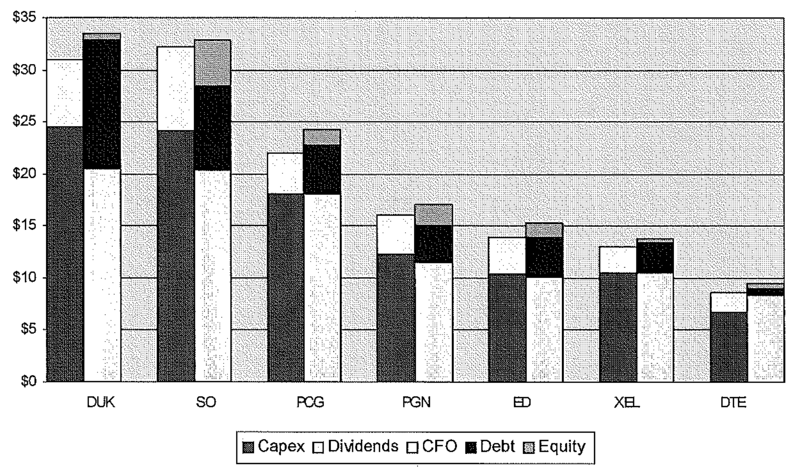
Most utilities remain in large capital spending plans despite the recession. This can be a good thing, as capex growth drives the ratebase growth which ultimately drives utility earnings growth potential.

It's all about capital spending and how to fund it

The regulated utility model is heavily dependent on capital spending and how that spending is financed. We tend to favor utilities that have the ability to fund their growth internally through strong cash flow from operations, moderate dividend payouts, cash flows from non-utility businesses, or tax shields. Examples include WEC and CMS. Many utilities require substantial external equity to fund their growth such as POR, SO, PGN. This slows the rate of earnings per share growth and more importantly can become a real economic hindrance if their stock prices fall below regulatory book value. Issuing equity below book creates permanent economic value loss for utilities. This is less of a problem now that capital markets have recovered.

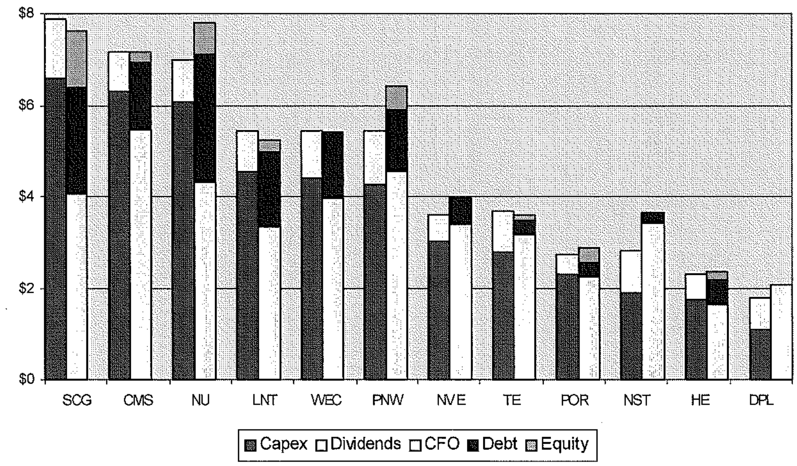
Charts 8 and 9 highlight regulated utility capital plans and our projections on how they will be funded.

Chart 8: Expected Financing of Capex and Dividends in 2009-2013 by Large Utilities ($ Billions)



Source: Company presentations and financial filings; BofA Merrill Lynch Global Research estimates

Chart 9: Expected Financing of Capex and Dividends in 2009-2013 by Small Utilities ($ Billions)



Source: Company presentations and financial filings; BofA Merrill Lynch Global Research estimates

We are projecting modest earnings growth for regulated utilities over the next five years of 5.6%

With this backdrop, we are projecting modest earnings growth for regulated utilities over the next five years of 5.6%.

With a current payout ratio for the sector of 69%, we are also forecasting dividend growth of 3.4%. We do not see any current candidates for likely dividend cuts. With a current yield of 4.6% and dividend growth of 3.4%, we like the total return profile and relatively low risk of the regulated utilities for investors seeking income and growth.

Investment thesis

Alliant Energy

While LNT has above-average potential ratebase growth opportunities and a solid dividend yield, the outlook is tempered by uncertain regulatory outcomes in IA and WI. LNT will also need to file another round of rate cases in 2010.

American Water Works

As the largest public traded water utility, AWK is a pureplay on the growth prospects for the water utility business, which include the need for substantial capex spend to upgrade an aging system and the potential consolidation or outsourcing of the government-owned share of the water sector. AWK is also a turnaround story, making great strides in improving earned returns at its regulated business. AWK is positioned to grow EPS by 10% and its dividend by 5% per year over the next few years.

Calpine

CPN is differentiated from other generation companies by its modern, efficient and largely natural-gas fired fleet. While we like CPN's asset position and see potential for longer-term upside, particularly as environmental regulations continue to become more stringent, we believe these factors are largely priced into CPN shares at current levels. We rate CPN as Neutral.

CMS Energy

CMS has an attractive utility growth story, but trades at a significant discount to peers. We see 5-6% EPS growth and 13% div growth over the next 5 years. An improved regulatory environment in MI also reduces the risk of CMS. Growth will be driven by investments at the core utility in renewables, energy efficiency, AMI, and new generation. We also project above average dividend growth since management reinstated the dividend in 2007 and intends to increase the payout to the sector average.

Consolidated Edison

ED is a pure distribution utility providing electric, gas and steam service in New York City and its northern suburbs. ED pays an attractive yield relative to its large cap peers with projected dividend growth of 1-2%. The company just announced a new three-year rate agreement with the NYPSC staff and other parties that should provide greater certainty and slightly higher return potential.

Dominion Resources

We like the fundamental growth story of Dominion, particularly its regulated segments, such as the regulated utility VEPCO, Dominion Transmission, and Dominion Cove Point. VEPCO earns premier ROEs and has a robust ratebase growth profile. Dominion also has a large merchant generation business, with the largest generation fleet in New England. Our Neutral rating reflects weaker merchant generation earnings due to low commodity prices offsetting higher growth at the regulated segments.

DPL Inc.

DPL enjoys a high degree of earnings certainty through 2012 through its rate plan. However, generation rates in the plan appear to be above market, and the combination of potentially lower generation rates and fewer barriers to competitive shopping suggests earnings downside risk in 2013.

DTE Energy

DTE combines regulated electric and gas utilities in Michigan with a portfolio of non-regulated assets. While we like DTE's long-term fundamental story, we believe it is fully reflected in the current stock price. Year to date, DTE has outperformed the UTY meaningfully. While we appreciate the company's improved regulatory environment, we do not see much upside for DTE beyond what it has already achieved.

Duke Energy

Duke benefits from constructive regulation in the Carolinas and the Midwest, strong ratebase growth opportunities, and a strong balance sheet. However, DUK's generation rates in OH are above market and a set to rise higher in 2010 and 2011, leading to the potential for increased shopping and lower rates in 2012. Roughly 30 percent of company earnings are from the International and Commercial segments, with riskier earnings. DUK also trades at a significant premium to the group.

Dynegy

Although we like the fuel and dispatch diversity of DYN's assets, exposure to very weak Midwest power markets remains an issue. In the absence of a significant recovery in Midwest power prices we believe DYN shares will underperform other generation leveraged companies. In addition, a potential equity overhang from LS Power's shares and future increases in coal supply costs could dampen any recovery related gains. We rate DYN shares as Underperform.

Edison International

Edison International's (EIX) utility, Southern California Edison (SCE), is a top growing utility in a constructive regulatory environment. This growth is currently muddled by a volatile and deteriorating earnings situation at Edison Mission Energy (EME), EIX's power generation company. As a result, we see very little earnings growth at EIX over the next five years and only modest dividend growth.

Entergy

ETR stock is the most attractively valued way to pay clean power, in our opinion. ETR compares favorably with its diversified peers in a few ways: 1) Earnings will be on a flat to upward trend in the current depressed power markets, 2) ETR will be repurchasing shares in 2010, and 3) ETR is the one of the few clear beneficiaries of potential carbon legislation.

Exelon

We rate EXC shares at Underperform as we estimate that the company's earnings power will fall nearly 20% in 2012-2014, but continues to trade at a premium relative to other diversified utilities. The company's nuclear generation fleet is well positioned for potential carbon legislation, but in our view consensus EPS and estimates for potential carbon upside are too high. In addition, we see limited potential for future dividend increases or share repurchases under current market conditions.

FirstEnergy

FE has nearly completed the transition of its generation to market, and is now focused on optimizing its generation sales mix through wholesale and retail sales. Earnings should be flat to up in the current market price environment but the high dividend yield allows investors to be paid to wait for a market rebound.

FPL Group

FPL is one of the best strategically positioned companies to benefit from the increased national emphasis on low-carbon and renewable generation. FPL should be able to add at least 1,000 MW of renewable generation per year and see earnings upside despite depressed market power prices. The utility also has the potential for above-average ratebase growth. However, these upsides already appear priced in the stock.

Hawaiian Electric Industries

HE was hit on both sides in 2009, as its bank subsidiary suffered higher loan loss provisions and asset writedowns. Its utilities felt the brunt of a weak economy, rising costs and the lack of timely rate relief. Although the core business is improving, HE needs its utility returns to improve, which requires a reasonable decoupling order or an accelerated rate case process. The PUC has no set a deadline to rule on decoupling.

Northeast Utilities

Aside from ITC, NU is one of the only ways to play transmission growth in the US. We project its transmission earnings will grow by more than 70% over the next five years. Since the transmission business is generally accorded a higher multiple by investors, the consolidated P/E of NU should improve. We also see an opportunity for NU on the distribution side to improve on its current 8% earned ROE. Overall, we project earnings growth of 8% and dividend growth of 5-6% during the next five years.

NRG Energy

We see several favorable aspects to the NRG story that differentiate it relative to its peers. NRG offers investors exposure to an integrated retail/wholesale generation strategy, well positioned baseload generation assets in Texas, attractive growth opportunities and a commitment to return captial to shareholders. While power market conditions remain tough, we believe NRG remains structurally advantaged relative to its peers and rate the company as a Buy.

NSTAR

NST is a high-quality regulated utility with 1) strong balance sheet, cash flow and credit ratings, 2) rate certainty through 2012, 3) visible earnings growth drivers, 4) transmission investment opportunities, and 5) good management. We project 5% EPS growth and 6-7% dividend growth through 2012. The one overhang on NST is what happens after the current rate agreement expires. In our opinion, NST will likely fashion a reasonable new agreement just as it did under similar circumstances in 2005.

NV Energy

We are using a premium P/E of 12.5x our 2011E of $0.98 in our $12 P.O. The biggest risk to our outlook would be a stronger than expected sales recovery in Nevada. Another upside would be political or regulatory initiatives to reduce regulatory lag.

PG&E Corporation

PCG offers a compelling regulated growth story with well below average risk. PCG benefits from very supportive state regulation in CA. Key positive CA regulatory mechanisms include revenue decoupling, cost of capital adjustment mechanism, and a pension balancing account. We project earnings growth of 6-

7% over the next 5 years driven by a 10% growth in ratebase, through investments in transmission and distribution and generation. We expect PCG to increase the dividend as earnings grow.

Pinnacle West

Although we are still cautious of the future regulatory environment in AZ, PNW has successfully negotiated a reasonable settlement in its Arizona Public Service rate case giving investors visibility and stability around future earnings. The settlement helps APS maintain an investment grade rating and supports PNW's dividend. Renewables and transmission projects will provide growth in the interim.

Portland General Electric Company

We like the fundamental ratebase story of POR, but find it a little too risky to like for a regulated utility. Risk issues include: 1) Power cost adjustment mechanism has a wide bandwidth, 2) Sales decoupling does not offer protection from weather or industrial sales, and 3) Senate Bill 408 corporate tax legislation causes tax swings that amplify earnings upsides and downsides. POR may slow or temporarily stop its dividend growth in 2010 as the payout ratio is higher than management's target.

PPL Corporation

We rate PPL as a Buy. The company's quality generation portfolio and highly hedged position through 2012 make it a safe place to wait for a potential power recovery. An above-average 4.3% dividend yield is also attractive. Even after adjusting for the benefits of the company's in the money power hedges, PPL's valuation appears compelling.

Progress Energy

PGN is one of the largest pure-play regulated utilities. The utilities have strong ratebase growth prospects going forward and cash flows support the high dividend yield. However, dividend growth appears limited and the company will need external equity to fund its growth.

RRI Energy

We rate RRI Energy with our Underperform rating. A disproportionately large amount (45%) of RRI's EBITDA is dependent on potentially costly environmental upgrades needed at several of its plants. We estimate the NPV of likely environmental spending to be approximately $800-$900 million. Combined with its greater exposure (unhedged) to weak near-term power fundamentals we see better value elsewhere in the sector.

SCANA Corp.

SCG is building two new nuclear 1,117MW plants scheduled to reach operations in 2016 and 2019, respectively. SCG has a regulatory framework for the new nuclear plants, providing up-front prudence decisions and real-time cost recovery. Despite these protections, we see a higher risk profile for SCG given 1) the new technology nature of new nuclear, 2) the risk of rising construction costs and delays, and 3) the high concentration of its growth focused on one asset.

Southern Company

In our view Southern may disappoint investors in coming months for 3 reasons: 1) Consensus earnings are too high for 2010, 2) Stock issuance will remain elevated, and 3) Dividend growth is likely to slow. An important GA rate case will be an overhang for most of 2010 as well. We project SO will issue about $1.1B of new shares annually in 2009-2011. In our view the 2010 dividend growth will either slow down to the 2.5% area or even take a temporary breather.

TECO Energy
TECO combines a high dividend yield with earnings upside over the next few years. It has secured a constructive rate outcome in Florida in advance of the recent politicization of the regulatory process, and coal margins appear set to improve off 2009 lows.

Xcel Energy
We like XEL's strong ratebase wind program and multi-state utility model, but find the stock fairly valued at current levels. XEL also earnings growth of 6-7% per year driven by ratebase growth. Xcel operates utilities in CO, MN, WI, ND,SD, NM, and TX, giving it the benefit of geographically diverse service territories. Investments in wind generation provide solid growth. XEL's challenges will be translating these opportunities into EPS growth by managing cash flow and regulatory lag.

Price objective basis & risk
Alliant Energy (LNT)
Our $30 price objective uses 11x multiples on the earnings from IP&L and WP&L. This is a discount to current sector averages mainly due to the lingering regulatory uncertainty in both states. Including parent losses, utility EPS of $2.31 would be worth $23/share. We use a premium 13x multiple on 2011E ATC earnings of $0.24 due to the stability of FERC regulation and solid rate base growth opportunities. Finally, as the earnings stream from Resources is difficult to forecast, we use a 9x multiple on 2011E EPS of $0.22. This totals to a value of $30/sh. Risks to our price objective are regulatory outcomes, the potential for additional equity, and management execution.

American Water Works (AWK)
Our $24 price objective is based on a P/E of 16x 2011 earnings of $1.51. This P/E is a 5-10% discount to the 17x P/E for the comps including the other larger name, Aqua America. In our opinion, this discount conservatively reflects a more leveraged balance sheet and a need to prove out its strategic plan. Risks to our price objective are regular reviews of $1.25B in goodwill on the balance sheet, regular future equity needs, and the importance of successful rate relief in various jurisdictions.

Calpine (CPN)
Our $12 price objective is primarily based on our sum-of-the-parts-valuation, which uses an 8x EBITDA multiple to our adjusted 2012 EBITDA estimate. Our EBITDA estimate used in our sum of-the-parts valuation adjusts downward for our estimate for CPN's in-the-money hedges. Our valuation treats the NPV of the company's remaining NOL balance as an offset to net debt. Downside risks to our price objective are CPN's exposure to volatile natural gas and power prices, a delay in implementation of proposed environmental regulations, energy efficiency related demand declines, and expiration of favorable power supply contracts or tolling agreements. Risks to the upside are a sooner-than-expected recovery in power demand, more stringent environmental legislation.

CMS Energy (CMS)
Our price objective of $19 assumes a slight premium P/E of 12.5x 2011 utility and parent earnings, or $17/share. We also value CMS post 2011 NOLs at about

$1/share. Finally, the non-regulated business is worth about $0.75/share. Risks to our price objective are: 1) the pending gas rate case, 2) the parent balance sheet is more levered than peers, 3) Michigan regulation needs to stay balanced.

Consolidated Edison (ED)

In our view, ED stock deserves a premium valuation given the certainty from the new settlement and the companies low risk profile. Based on a premium valuation of 13x our 2011E of $3.73, our price objective is $49. Risks to our price objective are approval of the rate settlement and the ability to manage costs to be able to earn the allowed ROE.

Dominion Resources (D)

Our price objective of $38 is derived from our sum-of-the-parts valuation. We apply a premium 13x multiple to 2011 earnings for VEPCO and an 8x multiple to merchant generation EBITDA. Our sum of parts includes value for the E&P business including Marcellus acreage. Downside risk is a negative outcome of VEPCO rate case. Upside risk is power market recovery.

DPL Inc. (DPL)

Our price objective of $27 uses an 11x multiple on 2011 earnings of $2.50/sh, a discount to the regulated average of 12x. We believe this discount is appropriate for a few reasons. First, we see earnings downside risk of about $0.60/sh all else equal in 2013, as its current rate plan expires and rates shift closer to market. DPL will also be more exposed to competitive generation in its service territory in 2013. Second, given the long-term exposure to market, we see its risk profile as higher than a traditional fully integrated electric utility. Upside risks to our price objective are a rebound in power and capacity prices and its ability to negotiate a similarly favorable rate plan beyond 2012.

DTE Energy (DTE)

Our price objective is $44. We apply a 12.5x multiple to our 2011 EPS estimate for Detroit Edison and MichCon, a slight premium to the average multiple for regulated utility companies due to improved MI regulation. Risks are worse/better-than-expected outcomes at the rate cases, and slower/faster-than-expected economic recovery boosts utility and power and industrial sales.

Duke Energy (DUK)

Our price objective is $16. In our view, the regulated utility businesses deserve a slight premium valuation to the sector, while the Commercial Power and International merit a slight discount. We value the utility at 12.5x 2011E EPS of $0.88 (net of parent losses) which equates to $10.12 pershare. For the non-regulated operations, we use 10.5x 2011E EPS of $0.46, or $4.83 per share. The sum-of-the-parts is then $16. We also looked at the non-regulated valuations on EBITDA using the typical 8x multiple we use for competitive generators. Even keeping Commercial Power at the ESP price (ie, no opening up of hedges), we come to a $4.14/share for the non-regulateds or a SOTP value for DUK of just under $16. Risks to our price objective are a strong turnaround in the power markets that serves to fix some of our concerns at Commercial Power. Both the shopping risk and post ESP roll-off risk are a function of the current low-priced power market. Additionally, DUK is trying to move Ohio further toward re-regulation and may try to address the 2012 price risk in that context.

Dynegy (DYN)

Our $1.50 price objective is primarily derived from our sum-of-the-parts analysis and employs an 8.00x adjusted EBITDA multiple to our 2012 unhedged EBITDA estimate for DYN's generation businesses, consistent with other competitive generators in our coverage universe. We assume DYN is largely unhedged in 2012. That said, DYN's low-cost coal supply to its Illinois coal plants is largely the result of a deep in-the-money coal transportation contract that expires at the end of 2013. We expect the company's coal transportation costs to increase at that point. We adjust our EBITDA and free cash flow estimates for this contract in our adjusted EV/EBITDA and adjusted FCF Yield analysis, which we use to round out our valuation of competitive generation companies. Upside risks are a sooner-than-expected recovery in Midwest power prices, potential delays in carbon legislation. Downside risks are further deterioration in already weak Midwest power prices, unplanned outages of the company's baseload generation facilities, and credit rating agency downgrades.

Edison International (EIX)

Our EIX price ojective is $38. We value SCE at $38/share, based on 13x 2011 earnings, a premium to the industry average. We see zero equity value at EME at current power prices even before adding environmental capex at the coal plants. For EME, in our view, the company cannot be worth negative value to EIX, but we also see a slim chance of material positive value barring a dramatic power market recovery. The biggest downside risk for EIX would be an unforeseen negative turn in California regulation. On the upside, a strong power market recovery could cause EME to be worth more than we currently expect.

Entergy (ETR)

Our price objective for ETR is $95. We use an average utility multiple of 12x 2011 utility earnings and 8x 2011 adjusted EBITDA for nuclear. In addition we give ETR $1.90/share in benefit for carbon, assuming a 25% chance legislation is in effect by 2011. For carbon, we assume an initial price of $10/ton. We estimate that this will raise power prices by about $5/mwh and provide an EBITDA uplift of $170 for ETR. Downside risks: 1) longer-than-expected economic recession, 2) falling commodity prices and power prices, 3) regulatory risk in operating states, and 4) delays in relicensing for Vermont Yankee and Indian Point. Upside risks: 1) faster-than-expected economic recovery, 2) faster-than-expected power price recovery, and 3) better-than-expected regluatory actions.

Exelon (EXC)

Our $44 price objective is based on our sum-of-the-parts valuation where we assume a 12x P/E multiple for our 2011 EPS estimates for EXC's regulated utility businesses. We value EXC's generation business in our sum-of-the-parts analysis using an 8x EBITDA multiple for our 2011 adjusted EBITDA estimate for the generation business, which adjusts for the company's in the money hedges. Our valuation also includes $1.5 billion in potential carbon value. Upside risks to our price objective and rating are a stronger- and sooner-than-expected turnaround in Midwest and MidAtlantic power prices. In addition a more stringent and quicker passage of potential carbon legislation would also pose an upside risk to our price objective and rating. Downside risks to our $44 EXC price objective are operational and regulatory risks. EXC's generation fleet largely consists of nuclear power plants with their operations subject to strict regulatory oversight. Any extended and unplanned outage at EXC's nuclear generation assets either due to an operational issue or at the behest of government regulatory authorities could pressure EXC shares.

FirstEnergy (FE)

Our $50 price objective is based on 8x 2011 adjusted EBITDA for generation and 12x 2011 utility earnings. Both of these reflect industry average valuations. In contrast to most other generators, FE does not have any above market hedges in 2011. In fact, what is there is just slightly below market. As a result, our adjusted EBITDA is pretty close to actual EBITDA with the caveat of adjustments for operating leases (these leases are added as debt). We do not make any adjustment for carbon in our valuation, but believe that FE would see a marginal benefit if it were implemented. Risks to our price objective is a further downturn in power markets for 2011 and 2012 as its hedge position is relatively low, executing on the retail strategy and sustaining cost controls.

FPL Group (FPL)

Our price objective is $55/share. Key assumptions in our analysis include a slight premium multiple of 12.5x (vs. the average of 12x) 2011 utility earnings of $2.49, 8x 2011 adjusted EBITDA for the conventional generation business. Our 2011 EBITDA is adjusted down by $115M to reflect lingering above market hedges, mainly in New England. We add hedge value back as an offset to net debt. For wind, we use a 10x 2011 EBITDA multiple reflecting a special renewable growth premium. We also add a DCF of PTC and ITC tax credits using a 6% discount rate. This comes to $3.8B, or 9.30 per share. Risks to our objective are a negative rate order in Florida. Every 100bp change in earned ROE is worth $0.21 per share to EPS. Other risks are executing on the wind growth plan, dependence on tax credits and energy trading exposure.

Hawaiian Electric Industries (HE)

Our valuation is based on an average utility P/E of 12x 2011 earnings of $1.43 and parent losses of $0.26. The utility net of parent is worth $14/share. After discussing American Savings Bank (ASB) metrics with the BofA Merrill Lynch thrift analyst, the appropriate valuation is in line with the thrift industry average of 1.5x tangible book value. This is a lower value than its neighbor, Bank of Hawaii (BOH), but BOH returns on equity are far superior to ASB. The bank is worth approximately $6/share, thus our $20 price objective. Risks to our price objective are a negative decoupling order that causes utility earned returns to remain very low. HE ultimately needs a path to higher earned returns to keep the dividend. The other risk would be further unexpected write-offs or loan losses at ASB.

Northeast Utilities (NU)

Our $28 price objective is based on an average P/E of 12x 2011 distribution earnings (net of parent drag) of $1.20/share. For transmission, our valuation is based on 14x 2011 earnings of $0.98. This 14x multiple is in between the average utility and the 16x pure P/E for ITC Holdings. NU is currently trading at a discount P/E of 11.9x 2011E earnings, which is below the average regulated of 12.2x. We believe this is too low given its transmission component and superior overall growth outlook. The greatest risk to our outlook is either the NEEWS or HQ lines are meaningfully delayed or cancelled. While we cannot rule this out, NU has shown a continued ability to bring new projects to the table.

NRG Energy (NRG)

Our $29 price objective is primarily based on our sum-of-the- parts- valuation, which uses an 8.0x EBITDA multiple to our adjusted 2012 EBITDA estimate. Our EBITDA estimate used in our sum of-the-parts valuation adjusts downward for NRG's in the money hedges. Our valuation also adjusts for the impact of potential carbon legislation and our estimates for the company's remaining environmental spending needs. Downside risks to our PO are NRG's exposure to volatile natural gas and power prices. In addition, an earlier or more stringent-than-expected implantation of carbon or other environmental legislation currently being contemplated would be likely to negatively affect NRG shares.

NSTAR (NST)

Respecting its high-quality attributes, we believe NST deserves an 8-10% premium P/E to the average utility due to 1) strong balance sheet, cash flow and credit ratings, 2) rate certainty through 2012, 3) visible earnings growth drivers, 4) transmission investment opportunities, and 5) good management. Our $36 price objective is based on 13x our 2011 EPS of $2.77. The risk to our price objective is the uncertainty of potential regulatory outcomes post 2012.

NV Energy (NVE)

In our view, investors can value NVE at either a premium multiple to 2011 earnings (pre rate relief) or a discount multiple to 2012 (post rate relief). We are using a premium P/E of 12.5x our 2011E of $0.98 in our $12 P.O. to account for the stock's meaningful post rate relief earnings pick up in 2012 and 2013. Upside risks to our price objective would be a stronger than expected sales recovery in Nevada, and political or regulatory initiatives to reduce regulatory lag. Downside risks are: 1) longer-than-expected economic recession, 2) worse than expected outcomes in rate cases, 3) timing delays on construction projects exacerbating regulatory lag.

PG&E Corporation (PCG)

Our $49 price objective assumes a premium P/E of 13x 2011 earnings to account for above average growth and high quality earnings. Risks to our price objective are: 1) outstanding 2011 general rate case and 2) Any unforeseen changes to California regulation.

Pinnacle West (PNW)

Our price objective for PNW is $36. We value PNW utility and parent and other earnings at 11.5x 2012E of $3.20 (net). We value PNW off 2012 earnings to reflect the improved earnings expected in 2012-2013. Upside risks are faster-than-expected economic recovery. Downside risks are a longer-than-expected economic recession.

Portland General Electric Company (POR)

We arrive at our $20 price objective by applying an average11.5x multiple to 2011e earnings of $1.76 per share. We apply a discounted multiple to account for higher earnings volatility. Upside risks to our price objective are a faster-than-expected economic recovery and better-than-expected outcome in the 2011 rate case. Downside risks are: 1) a longer-than-expected economic recession, 2) lower-than-expected hydro conditions, and 3) regulatory risk in Oregon.

PPL Corporation (PPL)

We arrive at our $35 price objective on PPL using our sum-of-the-parts valuation, Our sum-of-the-parts utilizes an 8x multiple to our 2011E adjusted EBITDA. Our adjusted EBITDA is adjusted downward for the company's in the money hedges. We apply a 12x P/E multiple to our 2011 earnings estimate for PPL's Pennsylvania based utility, in-line with its peers. We apply a 13.5x P/E multiple to our 2011 earnings estimate for PPL's UK based utility, which relfects this businesses lower degree of regulatory risk. Risks are sensitivity to power prices, the next PJM capacity auction, and any potential credit rating downgrades.

Progress Energy (PGN)

Our $42 price objective is based on a sum of the parts valuation for PGN. We value the utilities at a slight premium of 12.5x 2011 earnings $3.30 (utility net of parent losses). This totals slightly under $41. We then add $1.25/share of value for deferred tax benefits post 2011 that PGN retain from its old synfuel business. The biggest risk to our price objective is that the Florida rate case comes out poorly resulting in much lower earnings power than we project. This could also put some strain on the dividend if PGN cannot fix it in a follow-up case. On the other hand, a constructive FL rate order and a better-than-expected economic recovery could provide upside to our estimates.

RRI Energy (RRI)

Our price objective of $5 is derived from our sum-of-the parts valuation, which uses an 8x multiple to our adjusted 2012 EBITDA estimate, in line with its competitive power peers. We add the NPV of future environmental capex as additional debt and include approximately $100M related to potential carbon legislation in our base case. Upside risks to our Underperform rating are a faster-than-expected power market recovery and a delay in potential environmental mandates that would allow RRI to delay environmental upgrades at several of its coal generation facilities. Downside risks are a further deterioration of power market conditions in the PMJ-W region where many of the company's larger coal-generation assets are located. In addition, installation of advanced environmental controls at many of the company's coal-generation facilities are subject to potential delays and cost over-runs that could exceed our estimates.

SCANA Corp. (SCG)

Our $39 price objective is based on an average utility P/E of 12x 2011 earnings of $3.21. One could argue SCG merits a discount as a result of the new nuclear concentration risk. Alternatively, one could argue the certainty provided by BLRA and an estimate of 6-7% earnings growth merit a premium. Our take is that the current average valuation is on the mark. The risk to our price objective is some event that puts the new nuclear build at risk in some way. To the upside, a strong economic recovery could lead to upside sales at the utility business.

Southern Company (SO)

We value SO at a premium to reflect its high quality history. Our price objective is $33 based on 13x 2011 utility earnings and 8x 2011 EBITDA at Southern Power. Upside risks to our price objective are 1) a stronger economic recovery and 2) higher power prices that boost real-time pricing margins in Georgia. Downside risks are: 1) lower than expected power prices resulting in a continued decline in RTP pricing, 2) worse than expected outcome in GA rate case, 3) longer than expected economic recession.

TECO Energy (TE)

Our $17 price objective is based on a sum-of-parts valuation. We use a premium 12.5x multiple on 2011 electric and gas earnings of $1.03. This premium is warranted given their already completed rate case and ability to earn their allowed ROE. For Guatemala, we use an 11x multiple on earnings of $0.16. We do not assume a favorable outcome over the value-added distribution (VAD) tariff dispute. For TECO Coal, we use a 6.5x multiple on 2011 EBITDA of $153M. We assume an average coal price of $74.43/ton and a pretax margin of $9.50/ton, and overall production of 10.5 million tons. We then subtract $900M of unallocated parent debt and add the NPV of NOLs (about $476M) to come to an overall value of $17/sh. Risks are volatility of coal earnings and the long-term regulatory outlook in Florida.

Wisconsin Energy (WEC)
Our $53 price objective is based on current sector multiples and a clearer look on 2011E earnings. We value the utility operations and Power the Future at 13x 2011 earnings of $3.74, coming to a value of $48. This is a premium to the group average as the company will continue to have above-average rate base growth opportunities even after Power the Future. Moreover, the Power the Future earnings profile is embedded in the lease structure with a high ROE that cannot be changed by future regulatory action. We value the transmission operation at 14x 2011E earnings of $0.33 based on the premium valuation given to transmission-heavy utilities owing to the advantages of Federal Energy Regulatory Commission (FERC) regulation and continued need from transmission infrastructure investment. Risks to our price objective are some additional regulatory uncertainty stemming from the recent rate case decision, and state economic conditions.

Xcel Energy (XEL)
Our price objective for XEL is $21. We use a sum of the parts valuation for XEL. We value the utilities at a slight premium of 12.5x 2011E earnings $1.72 to account for the quality ratebase growth and clean power investments. Risks are changes in regulatory environments in operating states. Upside risks are a faster-than-expected economic recovery.

Analyst Certification
We, Steve Fleishman, Alex Kania and Ameet I. Thakkar, hereby certify that the views each of us has expressed in this research report accurately reflect each of our respective personal views about the subject securities and issuers. We also certify that no part of our respective compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Electric Utilities/Competitive Power Coverage Cluster

Investment rating	Company	BofAML ticker	Bloomberg symbol	Analyst
BUY				
	American Water Works	AWK	AWK US	Steve Fleishman
	CMS Energy	CMS	CMS US	Steve Fleishman
	Consolidated Edison	ED	ED US	Steve Fleishman
	Entergy	ETR	ETR US	Steve Fleishman
	FirstEnergy	FE	FE US	Steve Fleishman
	Northeast Utilities	NU	NU US	Steve Fleishman
	NRG Energy	NRG	NRG US	Ameet I. Thakkar
	PG&E Corporation	PCG	PCG US	Steve Fleishman
	PPL Corporation	PPL	PPL US	Steve Fleishman
	TECO Energy	TE	TE US	Steve Fleishman
	Wisconsin Energy	WEC	WEC US	Alex Kania
NEUTRAL				
	Alliant Energy	LNT	LNT US	Steve Fleishman
	Calpine	CPN	CPN US	Ameet I. Thakkar
	Dominion Resources	D	D US	Steve Fleishman
	Edison International	EIX	EIX US	Steve Fleishman
	FPL Group	FPL	FPL US	Steve Fleishman
	Hawaiian Electric Industries	HE	HE US	Steve Fleishman
	NSTAR	NST	NST US	Steve Fleishman
	Pinnacle West	PNW	PNW US	Steve Fleishman
	Progress Energy	PGN	PGN US	Steve Fleishman
	SCANA Corp.	SCG	SCG US	Steve Fleishman
	Xcel Energy	XEL	XEL US	Steve Fleishman
UNDERPERFORM				
	DPL Inc.	DPL	DPL US	Steve Fleishman
	DTE Energy	DTE	DTE US	Steve Fleishman
	Duke Energy	DUK	DUK US	Steve Fleishman
	Dynegy	DYN	DYN US	Ameet I. Thakkar
	Exelon	EXC	EXC US	Steve Fleishman
	NV Energy	NVE	NVE US	Steve Fleishman
	Portland General Electric Company	POR	POR US	Steve Fleishman
	RRI Energy	RRI	RRI US	Ameet I. Thakkar
	Southern Company	SO	SO US	Steve Fleishman

Important Disclosures

Investment Rating Distribution: Utilities Group (as of 12 Nov 2009)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	59	42.14%	Buy	30	56.60%
Neutral	40	28.57%	Neutral	14	38.89%
Sell	41	29.29%	Sell	11	32.35%

Investment Rating Distribution: Global Group (as of 12 Nov 2009)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1629	50.37%	Buy	842	57.51%
Neutral	821	25.39%	Neutral	455	62.33%
Sell	784	24.24%	Sell	357	49.31%

* Companies in respect of which MLPF&S or an affiliate has received compensation for investment banking services within the past 12 months. For purposes of this distribution, a stock rated Underperform is included as a Sell.

FUNDAMENTAL EQUITY OPINION KEY: Opinions include a Volatility Risk Rating, an Investment Rating and an Income Rating. *VOLATILITY RISK RATINGS*, indicators of potential price fluctuation, are: A - Low, B - Medium and C - High. *INVESTMENT RATINGS* reflect the analyst's assessment of a stock's: (i) absolute total return potential and (ii) attractiveness for investment relative to other stocks within its *Coverage Cluster* (defined below). There are three investment ratings: 1 - Buy stocks are expected to have a total return of at least 10% and are the most attractive stocks in the coverage cluster; 2 - Neutral stocks are expected to remain flat or increase in value and are less attractive than Buy rated stocks and 3 - Underperform stocks are the least attractive stocks in a coverage cluster. Analysts assign investment ratings considering, among other things, the 0-12 month total return expectation for a stock and the firm's guidelines for ratings dispersions (shown in the table below). The current price objective for a stock should be referenced to better understand the total return expectation at any given time. The price objective reflects the analyst's view of the potential price appreciation (depreciation).

Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where BofAML Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

***INCOME RATINGS*, indicators of potential cash dividends, are: 7 - same/higher (dividend considered to be secure), 8 - same/lower (dividend not considered to be secure) and 9 - pays no cash dividend.** *Coverage Cluster* is comprised of stocks covered by a single analyst or two or more analysts sharing a common industry, sector, region or other classification(s). A stock's coverage cluster is included in the most recent BofAML Comment referencing the stock.

Price charts for the securities referenced in this research report are available at http://www.ml.com/research/pricecharts.asp, or call 1-888-ML-CHART to have them mailed.

MLPF&S or one of its affiliates acts as a market maker for the equity securities recommended in the report: Alliant, American Water, Calpine Corp., CMS Energy, Consol Edison, Dominion Resourc, DPL Inc., DTE Energy, Duke Energy, Dynegy, Edison Intl, Entergy, Exelon Corp., FirstEnergy Corp, FPL Group, Hawaiian Electric, Northeast Util, NRG Energy, Inc., NSTAR, NV Energy, PG&E Corp., Pinnacle West, POR, PPL Corp., Progress, Reliant Energy, SCANA Corp., Southern Company, TECO Energy, Wisconsin Energy, Xcel Energy.

MLPF&S or an affiliate was a manager of a public offering of securities of this company within the last 12 months: Alliant, American Water, Calpine Corp., CMS Energy, Dominion Resourc, Duke Energy, Edison Intl, FirstEnergy Corp, FPL Group, Northeast Util, NRG Energy, Inc., NSTAR, POR, PPL Corp., Progress, SCANA Corp., Southern Company.

The company is or was, within the last 12 months, an investment banking client of MLPF&S and/or one or more of its affiliates: Alliant, American Water, Calpine Corp., CMS Energy, Consol Edison, Dominion Resourc, DPL Inc., DTE Energy, Duke Energy, Dynegy, Edison Intl, Entergy, Exelon Corp., FirstEnergy Corp, FPL Group, Hawaiian Electric, Northeast Util, NRG Energy, Inc., NSTAR, NV Energy, PG&E Corp., Pinnacle West, PPL Corp., Progress, Reliant Energy, SCANA Corp., Southern Company, TECO Energy, Wisconsin Energy, Xcel Energy.

MLPF&S or an affiliate has received compensation from the company for non-investment banking services or products within the past 12 months: Calpine Corp., Consol Edison, Dominion Resourc, DTE Energy, Duke Energy, Edison Intl, Entergy, Exelon Corp., FPL Group, Hawaiian Electric, NRG Energy, Inc., NSTAR, PG&E Corp., PPL Corp., Progress, Reliant Energy, Southern Company.

The company is or was, within the last 12 months, a non-securities business client of MLPF&S and/or one or more of its affiliates: Alliant, American Water, CMS Energy, Consol Edison, Dominion Resourc, DTE Energy, Duke Energy, Dynegy, Edison Intl, Entergy, Exelon Corp., FirstEnergy Corp, FPL Group, Hawaiian Electric, NRG Energy, Inc., NSTAR, PG&E Corp., Pinnacle West, PPL Corp., Progress, Reliant Energy, SCANA Corp., Southern Company, TECO Energy, Wisconsin Energy, Xcel Energy.

MLPF&S or an affiliate has received compensation for investment banking services from this company within the past 12 months: Alliant, American Water, Calpine Corp., CMS Energy, Consol Edison, Dominion Resourc, DTE Energy, Duke Energy, Dynegy, Edison Intl, Entergy, Exelon Corp., FirstEnergy Corp, FPL Group, Hawaiian Electric, Northeast Util, NRG Energy, Inc., NSTAR, NV Energy, PG&E Corp., Pinnacle West, PPL Corp., Progress, Reliant Energy, SCANA Corp., Southern Company, TECO Energy, Wisconsin Energy, Xcel Energy.

MLPF&S or an affiliate expects to receive or intends to seek compensation for investment banking services from this company or an affiliate of the company within the next three months: Alliant, American Water, Calpine Corp., CMS Energy, Consol Edison, Dominion Resourc, DPL Inc., DTE Energy, Duke Energy, Dynegy, Edison Intl, Exelon Corp., FirstEnergy Corp, FPL Group, Hawaiian Electric, Northeast Util, NRG Energy, Inc., NSTAR, NV Energy, PG&E Corp., Pinnacle West, PPL Corp., Progress, Reliant Energy, SCANA Corp., Southern Company, TECO Energy, Wisconsin Energy, Xcel Energy.

MLPF&S together with its affiliates beneficially owns one percent or more of the common stock of this company. If this report was issued on or after the 10th day of the month, it reflects the ownership position on the last day of the previous month. Reports issued before the 10th day of a month reflect the ownership position at the end of the second month preceding the date of the report: CMS Energy, DPL Inc., Entergy, Exelon Corp., FPL Group, Northeast Util, PG&E Corp., Wisconsin Energy, Xcel Energy.

MLPF&S or one of its affiliates is willing to sell to, or buy from, clients the common equity of the company on a principal basis: Alliant, American Water, Calpine Corp., CMS Energy, Consol Edison, Dominion Resourc, DPL Inc., DTE Energy, Duke Energy, Dynegy, Edison Intl, Entergy, Exelon Corp., FirstEnergy Corp, FPL Group, Hawaiian Electric, Northeast Util, NRG Energy, Inc., NSTAR, NV Energy, PG&E Corp., Pinnacle West, POR, PPL Corp., Progress, Reliant Energy, SCANA Corp., Southern Company, TECO Energy, Wisconsin Energy, Xcel Energy.

The company is or was, within the last 12 months, a securities business client (non-investment banking) of MLPF&S and/or one or more of its affiliates: Alliant, American Water, Calpine Corp., CMS Energy, Consol Edison, Dominion Resourc, DTE Energy, Duke Energy, Edison Intl, Entergy, Exelon Corp., FirstEnergy Corp, FPL Group, Hawaiian Electric, NRG Energy, Inc., NSTAR, PG&E Corp., Pinnacle West, PPL Corp., Progress, Reliant Energy, SCANA Corp., Southern Company, TECO Energy, Wisconsin Energy, Xcel Energy.

The analyst(s) responsible for covering the securities in this report receive compensation based upon, among other factors, the overall profitability of Bank of America Corporation, including profits derived from investment banking revenues.

Merrill Lynch is affiliated with an NYSE Designated Market Maker (DMM) that specializes in one or more securities issued by the subject companies. This affiliated NYSE DMM makes a market in, and may maintain a long or short position in or be on the opposite side of orders executed on the Floor of the NYSE in connection with one or more of the securities issued by these companies: DPL Inc., NSTAR, PG&E Corp., POR, Reliant Energy, Wisconsin Energy

Other Important Disclosures

BofA Merrill Lynch (BofAML) Research refers to the combined Global Research operations of Merrill Lynch and BAS.

Officers of MLPF&S or one or more of its affiliates (other than research analysts) may have a financial interest in securities of the issuer(s) or in related investments.

Merrill Lynch Research policies relating to conflicts of interest are described at http://www.ml.com/media/43347.pdf.

"Merrill Lynch" includes Merrill Lynch, Pierce, Fenner & Smith Incorporated ("MLPF&S") and its affiliates, including BofA (defined below). "BofA" refers to Banc of America Securities LLC ("BAS"), Banc of America Securities Limited ("BASL"), Banc of America Investment Services, Inc ("BAI") and their affiliates. Investors should contact their Merrill Lynch or BofA representative if they have questions concerning this report.

Information relating to Non-US affiliates of Merrill Lynch and Distribution of Affiliate Research Reports:

MLPF&S, BAS, BAI, and BASL distribute, or may in the future distribute, research reports of the following non-US affiliates in the US (short name: legal name): Merrill Lynch (France): Merrill Lynch Capital Markets (France) SAS; Merrill Lynch (Frankfurt): Merrill Lynch International Bank Ltd, Frankfurt Branch; Merrill Lynch (South Africa): Merrill Lynch South Africa (Pty) Ltd; Merrill Lynch (Milan): Merrill Lynch International Bank Limited; MLPF&S (UK): Merrill Lynch, Pierce, Fenner & Smith Limited; Merrill Lynch (Australia): Merrill Lynch Equities (Australia) Limited; Merrill Lynch (Hong Kong): Merrill Lynch (Asia Pacific) Limited; Merrill Lynch (Singapore): Merrill Lynch (Singapore) Pte Ltd; Merrill Lynch (Canada): Merrill Lynch Canada Inc; Merrill Lynch (Mexico): Merrill Lynch Mexico, SA de CV, Casa de Bolsa; Merrill Lynch (Argentina): Merrill Lynch Argentina SA; Merrill Lynch (Japan): Merrill Lynch Japan Securities Co, Ltd; Merrill Lynch (Seoul): Merrill Lynch International Incorporated (Seoul Branch); Merrill Lynch (Taiwan): Merrill Lynch Securities (Taiwan) Ltd.; DSP Merrill Lynch (India): DSP Merrill Lynch Limited; PT Merrill Lynch (Indonesia): PT Merrill Lynch Indonesia; Merrill Lynch (KL) Sdn. Bhd.: Merrill Lynch (Malaysia); Merrill Lynch (Israel): Merrill Lynch Israel Limited; Merrill Lynch (Russia): Merrill Lynch CIS Limited, Moscow; Merrill Lynch (Turkey): Merrill Lynch Yatirim Bankasi A.S.; Merrill Lynch (Dubai): Merrill Lynch International, Dubai Branch; MLPF&S (Zürich rep. office): MLPF&S Incorporated Zürich representative office; Merrill Lynch (Spain); Merrill Lynch Capital Markets Espana, S.A.S.V.

This research report has been approved for publication in the United Kingdom by Merrill Lynch, Pierce, Fenner & Smith Limited and BASL, which are authorized and regulated by the Financial Services Authority; has been considered and distributed in Japan by Merrill Lynch Japan Securities Co, Ltd and Banc of America Securities - Japan, Inc., registered securities dealers under the Financial Instruments and Exchange Law in Japan; is distributed in Hong Kong by Merrill Lynch (Asia Pacific) Limited and Banc of America Securities Asia Limited, which are regulated by the Hong Kong SFC and the Hong Kong Monetary Authority; is issued and distributed in Taiwan by Merrill Lynch Securities (Taiwan) Ltd.; is issued and distributed in Malaysia by Merrill Lynch (KL) Sdn. Bhd., a licensed investment adviser regulated by the Malaysian Securities Commission; is issued and distributed in India by DSP Merrill Lynch Limited; and is issued and distributed in Singapore by Merrill Lynch International Bank Limited (Merchant Bank), Merrill Lynch (Singapore) Pte Ltd (Company Registration No.'s F 06872E and 198602883D respectively) and Bank of America Singapore Limited (Merchant Bank). Merrill Lynch International Bank Limited (Merchant Bank), Merrill Lynch (Singapore) Pte Ltd and Bank of America Singapore Limited (Merchant Bank) are regulated by the Monetary Authority of Singapore. Merrill Lynch Equities (Australia) Limited (ABN 65 006 276 795), AFS License 235132 provides this report in Australia in accordance with section 911B of the Corporations Act 2001 and neither it nor any of its affiliates involved in preparing this research report is an Authorised Deposit-Taking Institution under the Banking Act 1959 nor regulated by the Australian Prudential Regulation Authority. No approval is required for publication or distribution of this report in Brazil.

This research report has been prepared and issued by MLPF&S and/or one or more of its non-US affiliates. MLPF&S is the distributor of this research report in the US and accepts full responsibility for research reports of its non-US affiliates distributed to MLPF&S clients in the US. Any US person (other than BAS, BAI and their respective clients) receiving this research report and wishing to effect any transaction in any security discussed in the report should do so through MLPF&S and not such foreign affiliates.

BAS distributes this research report to its clients and to its affiliate BAI and accepts responsibility for the distribution of this report in the US to BAS clients, but not to the clients of BAI. BAI is a registered broker-dealer, member of FINRA and SIPC, and is a non-bank subsidiary of Bank of America, N.A. BAI accepts responsibility for the distribution of this report in the US to BAI clients. Transactions by US persons that are BAS or BAI clients in any security discussed herein must be carried out through BAS and BAI, respectively.

General Investment Related Disclosures:

This research report provides general information only. Neither the information nor any opinion expressed constitutes an offer or an invitation to make an offer, to buy or sell any securities or other financial instrument or any derivative related to such securities or instruments (e.g., options, futures, warrants, and contracts for differences). This report is not intended to provide personal investment advice and it does not take into account the specific investment objectives, financial situation and the particular needs of any specific person. Investors should seek financial advice regarding the appropriateness of investing in financial instruments and implementing investment strategies discussed or recommended in this report and should understand that statements regarding future prospects may not be realized. Any decision to purchase or subscribe for securities in any offering must be based solely on existing public information on such security or the information in the prospectus or other offering document issued in connection with such offering, and not on this report.

Securities and other financial instruments discussed in this report, or recommended, offered or sold by Merrill Lynch, are not insured by the Federal Deposit Insurance Corporation and are not deposits or other obligations of any insured depository institution (including, Bank of America, N.A.). Investments in general and, derivatives, in particular, involve numerous risks, including, among others, market risk, counterparty default risk and liquidity risk. No security, financial instrument or derivative is suitable for all investors. In some cases, securities and other financial instruments may be difficult to value or sell and reliable information about the value or risks related to the security or financial instrument may be difficult to obtain. Investors should note that income from such securities and other financial instruments, if any, may fluctuate and that price or value of such securities and instruments may rise or fall and, in some cases, investors may lose their entire principal investment. Past performance is not necessarily a guide to future performance. Levels and basis for taxation may change.

This report may contain a short-term trading idea or recommendation, which highlights a specific near-term catalyst or event impacting the company or the market that is anticipated to have a short-term price impact on the equity securities of the company. Short-term trading ideas and recommendations are different from and do not affect a stock's fundamental equity rating, which reflects both a longer term total return expectation and attractiveness for investment relative to other stocks within its Coverage Cluster. Short-term trading ideas and recommendations may be more or less positive than a stock's fundamental equity rating.

Foreign currency rates of exchange may adversely affect the value, price or income of any security or financial instrument mentioned in this report. Investors in such securities and instruments, including ADRs, effectively assume currency risk.

UK Readers: The protections provided by the U.K. regulatory regime, including the Financial Services Scheme, do not apply in general to business coordinated by Merrill Lynch entities located outside of the United Kingdom. These disclosures should be read in conjunction with the BASL general policy statement on the handling of research conflicts, which is available upon request.

Officers of MLPF&S or one or more of its affiliates (other than research analysts) may have a financial interest in securities of the issuer(s) or in related investments.

Merrill Lynch is a regular issuer of traded financial instruments linked to securities that may have been recommended in this report. Merrill Lynch may, at any time, hold a trading position (long or short) in the securities and financial instruments discussed in this report.

Merrill Lynch, through business units other than BofAML Research, may have issued and may in the future issue trading ideas or recommendations that are inconsistent with, and reach different conclusions from, the information presented in this report. Such ideas or recommendations reflect the different time frames, assumptions, views and analytical methods of the persons who prepared them, and Merrill Lynch is under no obligation to ensure that such other trading ideas or recommendations are brought to the attention of any recipient of this report.

Copyright and General Information regarding Research Reports:

Materials prepared by Merrill Lynch research personnel are based on public information. Facts and views presented in this material have not been reviewed by, and may not reflect information known to, professionals in other business areas of Merrill Lynch, including investment banking personnel. Merrill Lynch has established information barriers between BofAML Research and certain business groups. As a result, Merrill Lynch does not disclose certain client relationships with, or compensation received from, such companies in research reports.

To the extent this report discusses any legal proceeding or issues, it has not been prepared as nor is it intended to express any legal conclusion, opinion or advice. Investors should consult their own legal advisers as to issues of law relating to the subject matter of this report. Merrill Lynch research personnel's knowledge of legal proceedings in which any Merrill Lynch entity and/or its directors, officers and employees may be plaintiffs, defendants, co-defendants or co-plaintiffs with or involving companies mentioned in this report is based on public information. Facts and views presented in this material that relate to any such proceedings have not been reviewed by, discussed with, and may not reflect information known to, professionals in other business areas of Merrill Lynch in connection with the legal proceedings or matters relevant to such proceedings.

This report has been prepared independently of any issuer of securities mentioned herein and not in connection with any proposed offering of securities or as agent of any issuer of any securities. None of MLPF&S, any of its affiliates or their research analysts has any authority whatsoever to make any representation or warranty on behalf of the issuer(s). Merrill Lynch policy prohibits research personnel from disclosing a recommendation, investment rating, or investment thesis for review by an issuer prior to the publication of a research report containing such rating, recommendation or investment thesis.

Any information relating to the tax status of financial instruments discussed herein is not intended to provide tax advice or to be used by anyone to provide tax advice. Investors are urged to seek tax advice based on their particular circumstances from an independent tax professional.

The information herein (other than disclosure information relating to Merrill Lynch and its affiliates) was obtained from various sources and we do not guarantee its accuracy. This report may contain links to third-party websites. Merrill Lynch is not responsible for the content of any third-party website or any linked content contained in a third-party website. Content contained on such third-party websites is not part of this report and is not incorporated by reference into this report. The inclusion of a link in this report does not imply any endorsement by or any affiliation with Merrill Lynch. Access to any third-party website is at your own risk, and you should always review the terms and privacy policies at third-party websites before submitting any personal information to them. Merrill Lynch is not responsible for such terms and privacy policies and expressly disclaims any liability for them.

Subject to the quiet period applicable under laws of the various jurisdictions in which we distribute research reports and other legal and Merrill Lynch policy-related restrictions on the publication of research reports, fundamental equity reports are produced on a regular basis as necessary to keep the investment recommendation current.

Certain outstanding reports may contain discussions and/or investment opinions relating to securities, financial instruments and/or issuers that are no longer current. Always refer to the most recent research report relating to a company or issuer prior to making an investment decision.

In some cases, a company or issuer may be classified as Restricted or may be Under Review or Extended Review. In each case, investors should consider any investment opinion relating to such company or issuer (or its security and/or financial instruments) to be suspended or withdrawn and should not rely on the analyses and investment opinion(s) pertaining to such issuer (or its securities and/or financial instruments) nor should the analyses or opinion(s) be considered a solicitation of any kind. Sales persons and financial advisors affiliated with BAS, BAI, MLPF&S or any of their affiliates may not solicit purchases of securities or financial instruments that are Restricted or Under Review and may only solicit securities under Extended Review in accordance with firm policies.

Neither Merrill Lynch nor any officer or employee of Merrill Lynch accepts any liability whatsoever for any direct, indirect or consequential damages or losses arising from any use of this report or its contents.

American Water Works

Go with the flow; reinstate coverage at Buy

Reinstatement of Coverage **BUY**

Equity | United States | Hydro-Electric Utilities
16 December 2009

Bank of America Merrill Lynch

Steve Fleishman +1 646 855-2906
Research Analyst
MLPF&S
steven.fleishman@baml.com

Reinstate coverage with a Buy rating and $24 P.O.

We view American Water Works (AWK) as an attractive way to participate in the growth potential of the regulated water sector. We forecast 10% EPS growth through 2011 driven by improving returns at AWK's underearning utilities, new capital investment in the system, and opportunities for M&A and non-regulated growth. AWK has a current yield of 3.8% and forecast dividend growth prospects of at least 5%. NJ-based AWK is the largest public US water utility serving 3.3 million customers in 20 states.

Scarcity of water plays

The entire publicly traded US water sector totals just 1/3 of the market cap of Southern Company. In our view this creates scarcity value for stocks in a market with attractive growth potential. Water utilities have significant capital investment opportunities to upgrade their aging equipment. In addition, more than 80% of the water business is owned by government entities, many of which may look to sell or outsource in coming years.

A turnaround story

AWK suffered from deteriorating returns under the recent ownership of RWE. RWE sold its final stake in the company last month. AWK is pursuing a multi-year rate plan to improve ROE from the current 6.5% area to a more normal 9-10%.

$24 price objective

Our valuation is based on 16x 2011E earnings of $1.51. This P/E is a 5-10% discount to the water utility comps. The valuation is a large premium to electric utilities, but we think is merited by higher growth potential and lower risk. Risks to our objective include $1.25B of remaining goodwill, the importance of incremental rate relief and the need for future equity issuance.

Stock Data

Price	US$22.49
Price Objective	US$24.00
Date Established	16-Dec-2009
Investment Opinion	B-1-7
Volatility Risk	MEDIUM
52-Week Range	US$16.22-22.50
Mrkt Val / Shares Out (mn)	US$3,925 / 174.5
BofAML Ticker / Exchange	AWK / NYS
Bloomberg / Reuters	AWK US / AWK.N
ROE (2009E)	5.3%
Total Dbt to Cap (Sep-2009A)	57.8%
Est. 5-Yr EPS / DPS Growth	9.5% / 4.8%

Estimates (Dec)

(US$)	2007A	2008A	2009E	2010E	2011E
EPS	1.00	1.10	1.26	1.39	1.51
GAAP EPS	(2.14)	(3.52)	(1.37)	1.39	1.51
EPS Change (YoY)	156.4%	10.0%	14.5%	10.3%	8.6%
Consensus EPS (Bloomberg)			1.28	1.44	1.58
Dividend Rate	0	0.40	0.84	0.86	0.90

Valuation (Dec)

	2007A	2008A	2009E	2010E	2011E
P/E	22.5x	20.4x	17.8x	16.2x	14.9x
GAAP P/E	NM	NM	NM	16.2x	14.9x
Dividend Yield	0%	1.8%	3.7%	3.8%	4.0%
EV / EBITDA*	11.5x	10.9x	9.8x	9.0x	8.3x
Free Cash Flow Yield*	-7.3%	-12.0%	-6.9%	-7.2%	-7.8%

* For full definitions of *iQmethod*SM measures, see page 10.

Refer to important disclosures on page 12 to 14. Analyst Certification on Page 10. Price Objective Basis/Risk on page 10.

iQprofile℠ American Water Works

iQmethod℠ – Bus Performance*

(US$ Millions)	2007A	2008A	2009E	2010E	2011E
Return on Capital Employed	0.1%	-1.3%	1.4%	3.2%	3.4%
Return on Equity	3.8%	4.1%	5.3%	6.0%	6.2%
Operating Margin	0.7%	-8.0%	7.9%	27.2%	28.1%
Free Cash Flow	(285)	(471)	(270)	(281)	(306)

iQmethod℠ – Quality of Earnings*

(US$ Millions)	2007A	2008A	2009E	2010E	2011E
Cash Realization Ratio	3.0x	3.1x	2.5x	2.3x	2.3x
Asset Replacement Ratio	2.8x	3.8x	2.7x	2.7x	2.8x
Tax Rate	NM	NM	NM	39.5%	39.5%
Net Debt-to-Equity Ratio	110.0%	128.9%	136.0%	128.8%	123.0%
Interest Cover	0.1x	-0.7x	0.7x	2.3x	2.3x

Income Statement Data (Dec)

(US$ Millions)	2007A	2008A	2009E	2010E	2011E
Sales	2,214	2,337	2,480	2,620	2,769
% Change	5.8%	5.5%	6.1%	5.6%	5.7%
Gross Profit	968	1,033	1,143	1,236	1,330
% Change	5.4%	6.8%	10.7%	8.1%	7.7%
EBITDA	799	843	937	1,022	1,110
% Change	7.7%	5.5%	11.2%	9.1%	8.6%
Net Interest & Other Income	(271)	(264)	(282)	(298)	(314)
Net Income (Adjusted)	**159**	**176**	**213**	**250**	**281**
% Change	**158.3%**	**10.6%**	**20.8%**	**17.6%**	**12.2%**

Free Cash Flow Data (Dec)

(US$ Millions)	2007A	2008A	2009E	2010E	2011E
Net Income from Cont Operations (GAAP)	(342)	(562)	(230)	250	281
Depreciation & Amortization	267	271	292	311	331
Change in Working Capital	17	6	0	0	0
Deferred Taxation Charge	40	94	99	113	127
Other Adjustments, Net	491	744	369	(105)	(105)
Capital Expenditure	(759)	(1,023)	(800)	(850)	(940)
Free Cash Flow	**-285**	**-471**	**-270**	**-281**	**-306**
% Change	**22.0%**	**-65.4%**	**42.6%**	**-4.0%**	**-8.8%**

Balance Sheet Data (Dec)

(US$ Millions)	2007A	2008A	2009E	2010E	2011E
Cash & Equivalents	13	10	80	0	70
Trade Receivables	148	149	149	149	149
Other Current Assets	269	259	259	259	259
Property, Plant & Equipment	9,318	10,124	10,657	11,221	11,855
Other Non-Current Assets	3,186	2,690	2,329	2,441	2,554
Total Assets	**12,934**	**13,232**	**13,474**	**14,071**	**14,887**
Short-Term Debt	221	479	279	179	279
Other Current Liabilities	458	450	450	450	450
Long-Term Debt	4,796	4,824	5,224	5,402	5,566
Other Non-Current Liabilities	2,914	3,372	3,533	3,707	3,895
Total Liabilities	**8,387**	**9,125**	**9,486**	**9,737**	**10,191**
Total Equity	**4,547**	**4,107**	**3,988**	**4,333**	**4,696**
Total Equity & Liabilities	**12,934**	**13,232**	**13,474**	**14,071**	**14,887**

* For full definitions of *iQmethod*℠ measures, see page 10.

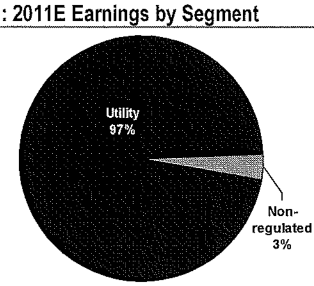
Company Description

American Water is headquartered in New Jersey and provides regulated water service in 20 states. New Jersey and Pennsylvania are the two largest states with each representing 20-25% of revenues. American Water Enterprises is the non-regulated business and represents a modest 5% of total earnings. The non-regulated business lines include 1) water service contracts with military bases, 2) homeowner repair, 3) contract operations for large cities, 4) water reuse, and 5) desalination.

Investment Thesis

As the largest public traded water utility, AWK is a pureplay on the growth prospects for the water utility business, which include the need for substantial capex spend to upgrade an aging system and the potential consolidation or outsourcing of the government-owned share of the water sector. AWK is also a turnaround story, making great strides in improving earned returns at its regulated business. We expect AWK to grow EPS by 10% and its dividend by 5% per year over the next few years.

Chart 1: 2011E Earnings by Segment



Source: BofA Merrill Lynch Global Research

Stock Data

Average Daily Volume	2,780,360

Quarterly Earnings Estimates

	2008	2009
Q1	0.04A	0.19A
Q2	0.28A	0.32A
Q3	0.55A	0.52A
Q4	0.23A	0.23E

Two stories in one

American Water is both a growth story and a turnaround story

As the largest public traded water utility, AWK is a pure play on the attractive growth prospects for the water utility business. Growth opportunities include the need for substantial capex spend to upgrade an aging system and the potential consolidation or outsourcing of the 80% share of the water business that is government-owned.

At the same time, AWK is also a turnaround story. Under the ownership of German utility RWE, the company's returns collapsed and state regulatory relations deteriorated. New management came in three years ago and made great strides in improving the regulatory situation. That said, AWK is still only earning a 6.5-7% ROE and we think still has plenty of room for upside improvement. In November, RWE sold out of its remaining 23% stake in AWK, which removed a multi-year stock overhang on AWK.

Between this ROE turnaround story and the capital investment opportunities, AWK is positioned to grow EPS by 10% per year the next few years, in our view. We also project a minimum of 5% dividend growth. Our price objective is $24, or 16x our 2011E of $1.51. This target multiple is still a 5-10% discount to the water sector comps shown below, including the closest comp, Aqua America. Risks to our price objective include the $1.25B of RWE-related goodwill still on AWK's books, the importance of incremental rate relief, and the need for future equity issuance.

Pick a state

AWK is headquartered in New Jersey and provides regulated water service to 3.3 million customers in 20 states. New Jersey and Pennsylvania are the two largest states with each representing 20-25% of revenues. The next largest are Illinois, Missouri, and Indiana. American Water Enterprises is the non-regulated business and represents a modest 5% of total earnings. The non-regs have several business lines including: 1) long-term water service contracts with military bases, 2) homeowner repair services, 3) contract operations for large cities such as Buffalo, 4) design, build and operate agreements for large water projects; 5) water reuse, and 6) desalination.

Table 1: Water Utility Comparables

						Price/EPS			Firm Value/EBITDA						
Water Utilities	Ticker	Price	Equity Value	Firm Value	Price/ Book	2009E	2010E	2011E	2009E	2010E	2011E	5-Year EPS Growth	Dividend Yield	Debt/ Cap	2009 P/E / Total Return
Aqua America, Inc.	WTR	$17.37	$2,361	$3,743	2.1x	21.7x	19.3x	17.7x	10.5x	9.5x	8.6x	8.6%	3.4%	56.4%	1.8x
California Water Service Group	CWT	37.58	780	1,130	1.8	19.0	17.8	15.6	8.9	8.3	7.3	6.0%	3.1%	48.7%	2.1
American States Water Company	AWR	34.99	647	955	1.8	19.7	17.1	16.3	8.6	7.6	N/A	4.0%	3.0%	47.3%	2.8
SJW Corp.	SJW	22.22	411	660	1.6	27.8	19.0	17.9	N/A	N/A	N/A	5.4%	2.9%	49.7%	3.3
Middlesex Water Company	MSEX.O	16.88	228	402	1.6	24.1	21.1	19.0	16.4	14.6	N/A	8.0%	4.2%	54.3%	2.0
Connecticut Water Service, Inc.	CTWS.O	24.57	209	320	2.0	20.6	22.8	N/A	17.9	18.7	N/A	6.6%	3.7%	51.0%	2.0
			Mean		1.8x	22.1x	19.5x	17.3x	12.5x	11.7x	8.0x	6.4%	3.4%	51.2%	2.3x
			Median		1.8	21.2	19.1	17.7	10.5	9.5	8.0	6.3%	3.2%	50.4%	2.0
American Water Works (BofA ML Est.)	AWK	$22.06	$3,851	$9,358	0.9x	17.4x	15.9x	14.7x	10.0x	9.2x	8.4x	10.0%	3.8%	58.0%	1.3x

Source: BofA Merrill Lynch Global Research; Pricing as of 12/15/09 close

Investment highlights

Highlights include:

1. Scarcity value of publicly traded water companies
2. Higher expected ROE
3. Rate base growth
4. Consolidation and non-regulated opportunities
5. Robust earnings and dividend growth

1) Scarcity value of water companies

AWK and Aqua America are the only US water utilities with a market cap over $1B. The entire publicly traded US water utility industry has a market cap of $8-$9B. This is only 1/3 of the market cap of Southern Company, which is just one of more than 100 publicly traded electric utilities. For a sector with attractive growth fundamentals, there are only a few ways to participate. We believe this scarcity could keep multiples in the water sector at elevated levels.

2) An ROE turnaround story

Under RWE management, AWK agreed to multi-year rate moratoriums and also cut back on some of its local regulatory presence. The result was disastrous as earned ROEs collapsed to low single digits and regulatory relations deteriorated. When the rate moratoriums expired and new management came in, the company beefed up its local presence again in order to improve regulatory relations. These efforts have started to pay off. In 2008, AWK filed for $310M of rate increases across its states and received $206M of actual rate relief. YTD 2009, AWK has sought $312M of rate relief and has received $103M. Pending rate cases total $218M across eight states. We believe AWK has plenty of room remaining for improvement as earned ROEs are still hovering in the 6.5-7% range, which is well below the typical allowed ROEs of 10-11%.

3) Rate base growth opportunities

AWK plans to spend $800M-1B in annual capex to replace aging equipment, enhance reliability and add new capacity. We estimate rate base will grow 5-6% based on this level of capex.

4) Consolidation and non-regulated opportunities

AWK is the largest public water company, but only represents 2.2% of the market

The water business is highly fragmented. AWK is the largest public company but only represents 2.2% of the market. More than 80% of the business is owned by government entities, such as municipalities. Given the increasing strains on local governments, the concept of privatizing or outsourcing the water system is growing more popular. With its national scope, AWK is well positioned to take advantage of this in both the regulated and non-regulated businesses. At its recent analyst conference, AWK highlighted public-private partnership structures as potentially an attractive way to facilitate these partnerships with government entities.

5) Strong earnings and dividend growth

We project 10% earnings growth and 5% dividend growth

We see 10% earnings growth over the next couple of years thanks to rate relief helping to lift earned returns. We are not including meaningful M&A transactions or any big non-regulated growth drivers. AWK recently raised its dividend by 5% to $0.84, or a 3.8% yield. With the payout ratio of 67% within the company's target of 50-70%, we expect dividend growth can be sustained in the 5% area for some time.

6) New management - back in place

Several top AWK management left the company after the RWE acquisition but decided to come back to help fix the situation. This includes the current CFO Ellen Wolf. CEO Don Correll spent most of his career in the water industry and was CEO of two other water utilities. In our view the management team is highly capable and passionate about the water business.

Investment concerns

Concerns include:
1. Writedowns of goodwill
2. Regulatory risk of imputing parent debt ratios into state rate cases
3. Regulatory lag on rate cases
4. Premium multiple over electric utilities

1) Goodwill balance sheet issues...

AWK still has $1.25B of goodwill on its parent balance sheet. This goodwill is essentially the premium RWE paid in its acquisition of AWK in 2003. Under GAAP, this goodwill was pushed down onto AWK's balance sheet. AWK recorded goodwill writedowns in 2008 and 2009 totaling $1.2B as its stock price highlighted the value of the goodwill was too high. The latest write-off occurred when AWK's stock reached a low of $16.53 in early 2009. AWK reviews its goodwill annually in November. In our opinion, goodwill is now at a sustainable and fair level, but there is a risk of further write-downs if the stock price or industry fundamentals weaken.

2)...related equity needs and potential regulatory risk

As a result of the goodwill write-downs, AWK's equity ratio is at 42%, which is below its long-term target of 45-50%. To reach the low end of this target, we project that AWK will need to issue approximately $250M of equity in both 2010 and 2011. AWK management stated after their June offering that the next one would not be for at least 12 months. Thus, we expect the next common offering in second half 2010. In the event of further goodwill write-downs, equity needs could increase.

From a regulatory standpoint, AWK currently has a more leveraged capital structure at the parent than at the utility subsidiaries, which generally have 50/50 debt/equity capital structures. Some have been concerned the more leveraged parent ratios could be imputed into the state rate cases. After several rounds of rate cases the last two years, this has not been a problem. The regulators understand the goodwill write-downs have created this issue and the company is taking actions to improve its parent balance sheet. Importantly, there is no RWE goodwill included in any state's ratebase.

3) Rate cases and regulatory lag

AWK has been focused on improving its presence in each of the 20 states in which it operates

AWK typically has 10 rate cases pending at any given time. Some of these will not go as well as planned and could create negative catalysts. That said, the diversity of AWK's business (20 states) mitigates the risk of one state turning rogue. To the flip side, this diversity could make it harder for AWK to develop the local relations to be effective in state regulation. New management has been focused on improving AWK's state-by-state presence with a president and regulatory head dedicated to each state.

Regulatory lag has been a big problem for AWK as most of its states use historic test years for rate cases. This means there can be a long lag time between the timing of capex and its ultimate recovery, which causes AWK to earn below its allowed ROE. AWK management is highly focused on reducing this lag given the company is currently earning 200-300bp below its allowed returns. One mechanism several states have adopted is a distribution system infrastructure charge (DSIC), which provides real-time recovery of capital additions. The more AWK can move states to this system, the better chance the company has to earn its allowed returns. At present, there is a natural lag of 50-100bp even once some of the turnaround issues are fixed.

4) Should water trade at such a premium to electrics?

The water utility sector trades at 17x 2011E earnings versus the regulated electric utilities at 12x. Is this 40% premium deserved? On the surface, it appears a bit extreme. However, we project the water utility sector to grow EPS at high single digits, which is double our growth expectations for regulated electrics. Moreover, water does not face the fuel and purchased power volatility that can entangle electrics and also does not have the extent of major environmental overhangs such as carbon. We believe water has massive consolidation potential and outsourcing from the large government ownership, something that is nearly impossible to achieve in the electric business. Finally, water utilities are scarce. There are less than 10 companies and the entire industry market cap is less than $9B. Electric investors have a wealth of investment choices. Given these factors, we believe the current high premium of water utilities to electrics is likely to be sustained.

Table 2: Financial Summary

Financial Summary	2009E	2010E	2011E
EPS	$1.26	$1.39	$1.51
Diluted Shares Outstanding	168	180	186
Dividends Per Share (indicated)	$0.84	$0.86	$0.90
Dividend Yield	3.8%	3.9%	4.1%
Dividend Payout Ratio	66%	62%	60%
Equity ratio	42%	44%	45%
FFO/Net Debt	10%	10%	11%
Valuation Metrics			
P/E	17.4x	15.9x	14.7x
P/B	1.0x	0.9x	0.9x
Segment EPS			
Utility	$1.37	$1.50	$1.64
Non-regulated	0.06	0.06	0.06
Parent/Other	(0.17)	(0.17)	(0.19)
Total EPS	$1.26	$1.39	$1.51
Utility			
Realized ROE	7.03%	7.76%	8.20%
Average Rate Base	$7,526	$8,018	$8,561

Source: BofA Merrill Lynch Global Research

Table 3: Model Assumptions

	2009E	2010E	2011E
Investing and Financing ($M)			
Capex	$800	$850	$940
Equity Issued/(Repurchased)	250	250	250
Debt Issued/(Repurchased)	552	223	200
Utility			
Customer Growth	0.0%	0.3%	0.3%
Usage Losses	(2.5%)	(0.5%)	(0.6%)

Source: BofA Merrill Lynch Global Research

$24 price objective

Our valuation is based on a P/E of 16x 2011E earnings of $1.51. This P/E is a 5-10% discount to the 17x P/E for the comps including the other larger name, Aqua America. We believe this discount conservatively reflects AWK's more leveraged balance sheet and their need to prove out their strategic plan. Risks to our price objective include regular reviews of the $1.25B goodwill on the balance sheet, regular future equity needs, and the importance of successful rate relief.

Table 4: Sum of Parts Valuation

			Low Case		Base Case		High Case	
Business Segment	Valuation Metric	2011E	Valuation Multiple	Value	Valuation Multiple	Value	Valuation Multiple	Value
Utility	EPS	$1.64	15x	$25	16x	$26	17x	$28
Non-regulated	EPS	0.06	15x	1	16x	1	17x	1
Parent/Other	EPS	(0.19)	15x	(3)	16x	(3)	17x	(3)
AWK Equity Value per Share				**$23**		**$24**		**$26**

Source: BofA Merrill Lynch Global Research

Financials

Earnings outlook

Our estimates are slightly below consensus

AWK management does not provide any annual earnings guidance, but states an intention to grow EPS 7-10% over the long term. Our 2009E is $1.26, which is slightly below the consensus of $1.28. The 2009 earnings have been pressured by weak sales due to unfavorable weather (a rainy summer), conservation and the weak economy. AWK has offset some of these pressures with cost cutting. With a return to normal weather and incremental rate relief in 2010, we see earnings improvement to $1.39/share, slightly below the $1.44 consensus. Our 2011 estimate is $1.51 is also below the consensus of $1.58.

Key assumptions in our model include:

- Rate relief of $162M in 2009, $109M in 2010 and $122M in 2011
- DSIC revenues of $15-$20M incrementally per year
- Customer growth of 0 to 0.5%. Usage losses of 2.5% in 2009 and 0.5% in 2010 and 2011
- $250M in annual equity issuance
- No material growth from acquisitions

Balance sheet, cash flow and dividends

We believe AWK will raise its equity ratio from 42% to 45% by YE 2011

AWK's current equity ratio is about 42% after the $450M goodwill write-off earlier this year and the $242M equity issuance in June. Management is targeting a 45-50% equity ratio over the long-term, which has been characterized as 3-5 years. We are assuming $250M equity issuances in 2010 and 2011 and that takes AWK to the low end of the target range, 45%, by year-end 2011.

AWK's capex plan is $800M-$1B per year. The company will be near the low end of this in 2009, and then rise toward the high end in 2011. We project internal cash flow of roughly $550M in 2009 growing to $650M in 2011. The remainder of the capex and the dividend will need to be funded with debt and equity issuances.

AWK recently raised its dividend to $0.84 annually from $0.80, a 5% dividend increase. The company is targeting a payout ratio of 50-70% and the current payout is 67%. With 10% earnings growth potential, we see room for AWK to sustain 5% dividend growth and bring the payout ratio down relatively quickly.

Table 5: AWK Income Statement

	2007A	2008A	2009E	2010E	2011E
Operating Revenues	2,214	2,337	2,480	2,620	2,769
O&M	(1,246)	(1,304)	(1,337)	(1,384)	(1,438)
General Taxes	(183)	(199)	(206)	(213)	(221)
Other Operating Expenses (Income)	7	0	0	0	0
EBITDA	**792**	**834**	**937**	**1,022**	**1,110**
Depreciation & Amortization	(267)	(271)	(292)	(311)	(331)
EBIT	**524**	**563**	**645**	**711**	**778**
Other Income	13	21	16	17	18
Interest Expense	(283)	(285)	(298)	(315)	(332)
Impairment Charges	(509)	(750)	(450)	0	0
Pre-Tax Income	**(256)**	**(451)**	**(87)**	**413**	**464**
Income Taxes	(87)	(112)	(143)	(163)	(183)
Income (Loss) From Continuing Operations	**(342)**	**(562)**	**(230)**	**250**	**281**
Income from Discontinued Operations	1	0	0	0	0
Reported GAAP Income	**(342)**	**(562)**	**(230)**	**250**	**281**
After-tax Adjustments	502	738	443	0	0
Adjusted Net Income	**159**	**176**	**213**	**250**	**281**
Average Shares - Diluted	*160*	*160*	*168*	*181*	*186*
Operating EPS	**$1.00**	**$1.10**	**$1.26**	**$1.39**	**$1.51**

Source: BofA Merrill Lynch Global Research

Table 6: AWK Cash Flow Statement

	2007A	2008A	2009E	2010E	2011E
Net Income - Before Preferred	(343)	(562)	(230)	250	281
Extraordinary Items	509	750	450	0	0
Depreciation & Amortization	267	271	292	311	331
Deferred Taxes	42	96	100	114	128
Other Operating Cash	(19)	(8)	(82)	(107)	(107)
Gross Operating Cash	**457**	**547**	**530**	**569**	**634**
Common Stock Dividends	0	(64)	(138)	(155)	(168)
Working Capital	17	6	0	0	0
Operating Cash After Divs.	**474**	**488**	**392**	**414**	**466**
Capital Expenditure	(759)	(1,023)	(800)	(850)	(940)
Other Investment Cash	12	(8)	(31)	(31)	(31)
Investing Cash Flow	**(747)**	**(1,031)**	**(831)**	**(881)**	**(971)**
Change in Net Debt	956	271	180	58	245
Stock Issuance (Buyback)	0	1	250	250	250
Capital Contribution	967	245	0	0	0
Other Financing Cash Flow	(1,666)	25	80	80	80
Financing Cash Flow	**257**	**542**	**510**	**388**	**575**
Net Change in Cash	**(16)**	**(1)**	**71**	**(80)**	**70**

Source: BofA Merrill Lynch Global Research

Table 7: AWK Balance Sheet

	2007A	2008A	2009E	2010E	2011E
Cash & Equivalents	13	10	80	0	70
Accounts Receivable	148	149	149	149	149
Inventories	27	29	29	29	29
Other Current Assets	242	230	230	230	230
Current Assets	**430**	**418**	**488**	**408**	**479**
Net PP&E	9,318	10,124	10,657	11,221	11,855
Goodwill	2,457	1,700	1,250	1,250	1,250
Other L-T Assets	729	991	1,079	1,192	1,304
Total Assets	**12,934**	**13,232**	**13,474**	**14,071**	**14,887**
S-T Debt	221	479	279	179	279
Current L-T Debt	96	176	45	35	50
Accounts Payable	169	150	150	150	150
Other Current Liabilities	289	300	300	300	300
Current Liabilities	**774**	**1,105**	**774**	**664**	**779**
L-T Debt	4,699	4,648	5,179	5,366	5,516
Contributions in Aid of Construction	818	911	971	1,031	1,091
Other L-T Liabilities	2,095	2,461	2,561	2,676	2,804
Preferred Equity	5	5	5	5	5
Shareholders' Equity	4,542	4,101	3,984	4,329	4,692
Total Liabilities & Equity	**12,934**	**13,231**	**13,474**	**14,071**	**14,887**

Source: BofA Merrill Lynch Global Research

Price objective basis & risk

American Water Works (AWK)

Our $24 price objective is based on a P/E of 16x 2011 earnings of $1.51. This P/E is a 5-10% discount to the 17x P/E for the comps including the other larger name, Aqua America. In our opinion, this discount conservatively reflects a more leveraged balance sheet and a need to prove out its strategic plan. Risks to our price objective are regular reviews of $1.25B in goodwill on the balance sheet, regular future equity needs, and the importance of successful rate relief in various jurisdictions.

Analyst Certification

I, Steve Fleishman, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Electric Utilities/Competitive Power Coverage Cluster

Investment rating	Company	BofAML ticker	Bloomberg symbol	Analyst
BUY				
	American Water Works	AWK	AWK US	Steve Fleishman
	CMS Energy	CMS	CMS US	Steve Fleishman
	Consolidated Edison	ED	ED US	Steve Fleishman
	Entergy	ETR	ETR US	Steve Fleishman
	FirstEnergy	FE	FE US	Steve Fleishman
	Northeast Utilities	NU	NU US	Steve Fleishman
	NRG Energy	NRG	NRG US	Ameet I. Thakkar
	PG&E Corporation	PCG	PCG US	Steve Fleishman
	PPL Corporation	PPL	PPL US	Steve Fleishman
	TECO Energy	TE	TE US	Steve Fleishman
	Wisconsin Energy	WEC	WEC US	Alex Kania
NEUTRAL				
	Alliant Energy	LNT	LNT US	Steve Fleishman
	Calpine	CPN	CPN US	Ameet I. Thakkar
	Dominion Resources	D	D US	Steve Fleishman
	Edison International	EIX	EIX US	Steve Fleishman
	FPL Group	FPL	FPL US	Steve Fleishman
	Hawaiian Electric Industries	HE	HE US	Steve Fleishman
	NSTAR	NST	NST US	Steve Fleishman
	Pinnacle West	PNW	PNW US	Steve Fleishman
	Progress Energy	PGN	PGN US	Steve Fleishman
	SCANA Corp.	SCG	SCG US	Steve Fleishman
	Xcel Energy	XEL	XEL US	Steve Fleishman
UNDERPERFORM				
	DPL Inc.	DPL	DPL US	Steve Fleishman
	DTE Energy	DTE	DTE US	Steve Fleishman
	Duke Energy	DUK	DUK US	Steve Fleishman
	Dynegy	DYN	DYN US	Ameet I. Thakkar
	Exelon	EXC	EXC US	Steve Fleishman
	NV Energy	NVE	NVE US	Steve Fleishman
	Portland General Electric Company	POR	POR US	Steve Fleishman
	RRI Energy	RRI	RRI US	Ameet I. Thakkar
	Southern Company	SO	SO US	Steve Fleishman

*iQmethod*SM Measures Definitions

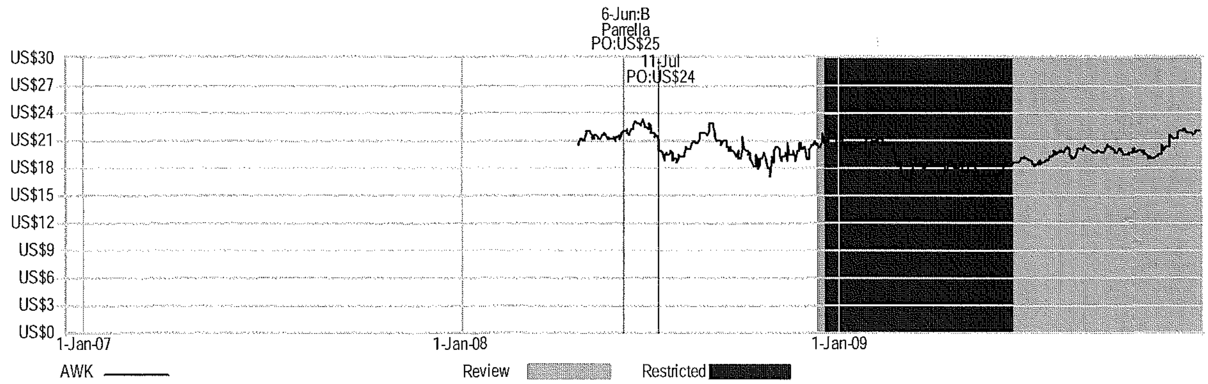
Business Performance	Numerator	Denominator
Return On Capital Employed	NOPAT = (EBIT + Interest Income) * (1 - Tax Rate) + Goodwill Amortization	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	EV = Current Share Price * Current Shares + Minority Equity + Net Debt + Other LT Liabilities	Sales
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

*iQmethod*SM is the set of BofA Merrill Lynch standard measures that serve to maintain global consistency under three broad headings: Business Performance, Quality of Earnings, and validations. The key features of iQmethod are: A consistently structured, detailed, and transparent methodology. Guidelines to maximize the effectiveness of the comparative valuation process, and to identify some common pitfalls.

iQdatabase® is our real-time global research database that is sourced directly from our equity analysts' earnings models and includes forecasted as well as historical data for income statements, balance sheets, and cash flow statements for companies covered by BofA Merrill Lynch.

Important Disclosures

AWK Price Chart



B : Buy, N : Neutral, S : Sell, U : Underperform, PO : Price objective, NA : No longer valid

"Prior to May 31, 2008, the investment opinion system included Buy, Neutral and Sell. As of May 31, 2008, the investment opinion system includes Buy, Neutral and Underperform. Dark Grey shading indicates that a security is restricted with the opinion suspended. Light grey shading indicates that a security is under review with the opinion withdrawn. The current investment opinion key is contained at the end of the report. Chart is current as of November 30, 2009 or such later date as indicated.

BofAML price charts do not reflect analysts' coverage of the stock at prior firms. Historical price charts relating to companies covered as of December 31, 2008 by former Banc of America Securities LLC (BAS) analysts are available to BAS clients on the BAS website."

Investment Rating Distribution: Utilities Group (as of 12 Nov 2009)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	59	42.14%	Buy	30	56.60%
Neutral	40	28.57%	Neutral	14	38.89%
Sell	41	29.29%	Sell	11	32.35%

Investment Rating Distribution: Global Group (as of 12 Nov 2009)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1629	50.37%	Buy	842	57.51%
Neutral	821	25.39%	Neutral	455	62.33%
Sell	784	24.24%	Sell	357	49.31%

* Companies in respect of which MLPF&S or an affiliate has received compensation for investment banking services within the past 12 months. For purposes of this distribution, a stock rated Underperform is included as a Sell.

FUNDAMENTAL EQUITY OPINION KEY: Opinions include a Volatility Risk Rating, an Investment Rating and an Income Rating. *VOLATILITY RISK RATINGS*, indicators of potential price fluctuation, are: A - Low, B - Medium and C - High. *INVESTMENT RATINGS* reflect the analyst's assessment of a stock's: (i) absolute total return potential and (ii) attractiveness for investment relative to other stocks within its *Coverage Cluster* (defined below). There are three investment ratings: 1 - Buy stocks are expected to have a total return of at least 10% and are the most attractive stocks in the coverage cluster; 2 - Neutral stocks are expected to remain flat or increase in value and are less attractive than Buy rated stocks and 3 - Underperform stocks are the least attractive stocks in a coverage cluster. Analysts assign investment ratings considering, among other things, the 0-12 month total return expectation for a stock and the firm's guidelines for ratings dispersions (shown in the table below). The current price objective for a stock should be referenced to better understand the total return expectation at any given time. The price objective reflects the analyst's view of the potential price appreciation (depreciation).

Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where BofAML Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

***INCOME RATINGS*, indicators of potential cash dividends, are: 7 - same/higher (dividend considered to be secure), 8 - same/lower (dividend not considered to be secure) and 9 - pays no cash dividend.** *Coverage Cluster* is comprised of stocks covered by a single analyst or two or more analysts sharing a common industry, sector, region or other classification(s). A stock's coverage cluster is included in the most recent BofAML Comment referencing the stock.

MLPF&S or one of its affiliates acts as a market maker for the equity securities recommended in the report: American Water.
MLPF&S or an affiliate was a manager of a public offering of securities of this company within the last 12 months: American Water.
The company is or was, within the last 12 months, an investment banking client of MLPF&S and/or one or more of its affiliates: American Water.
The company is or was, within the last 12 months, a non-securities business client of MLPF&S and/or one or more of its affiliates: American Water.
MLPF&S or an affiliate has received compensation for investment banking services from this company within the past 12 months: American Water.

MLPF&S or an affiliate expects to receive or intends to seek compensation for investment banking services from this company or an affiliate of the company within the next three months: American Water.

MLPF&S or one of its affiliates is willing to sell to, or buy from, clients the common equity of the company on a principal basis: American Water.

The company is or was, within the last 12 months, a securities business client (non-investment banking) of MLPF&S and/or one or more of its affiliates: American Water.

The analyst(s) responsible for covering the securities in this report receive compensation based upon, among other factors, the overall profitability of Bank of America Corporation, including profits derived from investment banking revenues.

Other Important Disclosures

BofA Merrill Lynch (BofAML) Research refers to the combined Global Research operations of Merrill Lynch and BAS.

Officers of MLPF&S or one or more of its affiliates (other than research analysts) may have a financial interest in securities of the issuer(s) or in related investments.

Merrill Lynch Research policies relating to conflicts of interest are described at http://www.ml.com/media/43347.pdf.

"Merrill Lynch" includes Merrill Lynch, Pierce, Fenner & Smith Incorporated ("MLPF&S") and its affiliates, including BofA (defined below). "BofA" refers to Banc of America Securities LLC ("BAS"), Banc of America Securities Limited ("BASL"), Banc of America Investment Services, Inc ("BAI") and their affiliates. Investors should contact their Merrill Lynch or BofA representative if they have questions concerning this report.

Information relating to Non-US affiliates of Merrill Lynch and Distribution of Affiliate Research Reports:

MLPF&S, BAS, BAI, and BASL distribute, or may in the future distribute, research reports of the following non-US affiliates in the US (short name: legal name): Merrill Lynch (France): Merrill Lynch Capital Markets (France) SAS; Merrill Lynch (Frankfurt): Merrill Lynch International Bank Ltd, Frankfurt Branch; Merrill Lynch (South Africa): Merrill Lynch South Africa (Pty) Ltd; Merrill Lynch (Milan): Merrill Lynch International Bank Limited; MLPF&S (UK): Merrill Lynch, Pierce, Fenner & Smith Limited; Merrill Lynch (Australia): Merrill Lynch Equities (Australia) Limited; Merrill Lynch (Hong Kong): Merrill Lynch (Asia Pacific) Limited; Merrill Lynch (Singapore): Merrill Lynch (Singapore) Pte Ltd; Merrill Lynch (Canada): Merrill Lynch Canada Inc; Merrill Lynch (Mexico): Merrill Lynch Mexico, SA de CV, Casa de Bolsa; Merrill Lynch (Argentina): Merrill Lynch Argentina SA; Merrill Lynch (Japan): Merrill Lynch Japan Securities Co, Ltd; Merrill Lynch (Seoul): Merrill Lynch International Incorporated (Seoul Branch); Merrill Lynch (Taiwan): Merrill Lynch Securities (Taiwan) Ltd.; DSP Merrill Lynch (India): DSP Merrill Lynch Limited; PT Merrill Lynch (Indonesia): PT Merrill Lynch Indonesia; Merrill Lynch (KL) Sdn. Bhd.: Merrill Lynch (Malaysia); Merrill Lynch (Israel): Merrill Lynch Israel Limited; Merrill Lynch (Russia): Merrill Lynch CIS Limited, Moscow; Merrill Lynch (Turkey): Merrill Lynch Yatirim Bankasi A.S.; Merrill Lynch (Dubai): Merrill Lynch International, Dubai Branch; MLPF&S (Zürich rep. office): MLPF&S Incorporated Zürich representative office; Merrill Lynch (Spain); Merrill Lynch Capital Markets Espana, S.A.S.V.

This research report has been approved for publication in the United Kingdom by Merrill Lynch, Pierce, Fenner & Smith Limited and BASL, which are authorized and regulated by the Financial Services Authority; has been considered and distributed in Japan by Merrill Lynch Japan Securities Co, Ltd and Banc of America Securities - Japan, Inc., registered securities dealers under the Financial Instruments and Exchange Law in Japan; is distributed in Hong Kong by Merrill Lynch (Asia Pacific) Limited and Banc of America Securities Asia Limited, which are regulated by the Hong Kong SFC and the Hong Kong Monetary Authority; is issued and distributed in Taiwan by Merrill Lynch Securities (Taiwan) Ltd.; is issued and distributed in Malaysia by Merrill Lynch (KL) Sdn. Bhd., a licensed investment adviser regulated by the Malaysian Securities Commission; is issued and distributed in India by DSP Merrill Lynch Limited; and is issued and distributed in Singapore by Merrill Lynch International Bank Limited (Merchant Bank), Merrill Lynch (Singapore) Pte Ltd (Company Registration No.'s F 06872E and 198602883D respectively) and Bank of America Singapore Limited (Merchant Bank). Merrill Lynch International Bank Limited (Merchant Bank), Merrill Lynch (Singapore) Pte Ltd and Bank of America Singapore Limited (Merchant Bank) are regulated by the Monetary Authority of Singapore. Merrill Lynch Equities (Australia) Limited (ABN 65 006 276 795), AFS License 235132 provides this report in Australia in accordance with section 911B of the Corporations Act 2001 and neither it nor any of its affiliates involved in preparing this research report is an Authorised Deposit-Taking Institution under the Banking Act 1959 nor regulated by the Australian Prudential Regulation Authority. No approval is required for publication or distribution of this report in Brazil.

This research report has been prepared and issued by MLPF&S and/or one or more of its non-US affiliates. MLPF&S is the distributor of this research report in the US and accepts full responsibility for research reports of its non-US affiliates distributed to MLPF&S clients in the US. Any US person (other than BAS, BAI and their respective clients) receiving this research report and wishing to effect any transaction in any security discussed in the report should do so through MLPF&S and not such foreign affiliates.

BAS distributes this research report to its clients and to its affiliate BAI and accepts responsibility for the distribution of this report in the US to BAS clients, but not to the clients of BAI. BAI is a registered broker-dealer, member of FINRA and SIPC, and is a non-bank subsidiary of Bank of America, N.A. BAI accepts responsibility for the distribution of this report in the US to BAI clients. Transactions by US persons that are BAS or BAI clients in any security discussed herein must be carried out through BAS and BAI, respectively.

General Investment Related Disclosures:

This research report provides general information only. Neither the information nor any opinion expressed constitutes an offer or an invitation to make an offer, to buy or sell any securities or other financial instrument or any derivative related to such securities or instruments (e.g., options, futures, warrants, and contracts for differences). This report is not intended to provide personal investment advice and it does not take into account the specific investment objectives, financial situation and the particular needs of any specific person. Investors should seek financial advice regarding the appropriateness of investing in financial instruments and implementing investment strategies discussed or recommended in this report and should understand that statements regarding future prospects may not be realized. Any decision to purchase or subscribe for securities in any offering must be based solely on existing public information on such security or the information in the prospectus or other offering document issued in connection with such offering, and not on this report.

Securities and other financial instruments discussed in this report, or recommended, offered or sold by Merrill Lynch, are not insured by the Federal Deposit Insurance Corporation and are not deposits or other obligations of any insured depository institution (including, Bank of America, N.A.). Investments in general and, derivatives, in particular, involve numerous risks, including, among others, market risk, counterparty default risk and liquidity risk. No security, financial instrument or derivative is suitable for all investors. In some cases, securities and other financial instruments may be difficult to value or sell and reliable information about the value or risks related to the security or financial instrument may be difficult to obtain. Investors should note that income from such securities and other financial instruments, if any, may fluctuate and that price or value of such securities and instruments may rise or fall and, in some cases, investors may lose their entire principal investment. Past performance is not necessarily a guide to future performance. Levels and basis for taxation may change.

This report may contain a short-term trading idea or recommendation, which highlights a specific near-term catalyst or event impacting the company or the market that is anticipated to have a short-term price impact on the equity securities of the company. Short-term trading ideas and recommendations are different from and do not affect a stock's fundamental equity rating, which reflects both a longer term total return expectation and attractiveness for investment relative to other stocks within its Coverage Cluster. Short-term trading ideas and recommendations may be more or less positive than a stock's fundamental equity rating.

Foreign currency rates of exchange may adversely affect the value, price or income of any security or financial instrument mentioned in this report. Investors in such securities and instruments, including ADRs, effectively assume currency risk.

UK Readers: The protections provided by the U.K. regulatory regime, including the Financial Services Scheme, do not apply in general to business coordinated by Merrill Lynch entities located outside of the United Kingdom. These disclosures should be read in conjunction with the BASL general policy statement on the handling of research conflicts, which is available upon request.

Officers of MLPF&S or one or more of its affiliates (other than research analysts) may have a financial interest in securities of the issuer(s) or in related investments.

Merrill Lynch is a regular issuer of traded financial instruments linked to securities that may have been recommended in this report. Merrill Lynch may, at any time, hold a trading position (long or short) in the securities and financial instruments discussed in this report.

Merrill Lynch, through business units other than BofAML Research, may have issued and may in the future issue trading ideas or recommendations that are inconsistent with, and reach different conclusions from, the information presented in this report. Such ideas or recommendations reflect the different time frames, assumptions, views and analytical methods of the persons who prepared them, and Merrill Lynch is under no obligation to ensure that such other trading ideas or recommendations are brought to the attention of any recipient of this report.

Copyright and General Information regarding Research Reports:

Materials prepared by Merrill Lynch research personnel are based on public information. Facts and views presented in this material have not been reviewed by, and may not reflect information known to, professionals in other business areas of Merrill Lynch, including investment banking personnel. Merrill Lynch has established information barriers between BofAML Research and certain business groups. As a result, Merrill Lynch does not disclose certain client relationships with, or compensation received from, such companies in research reports.

To the extent this report discusses any legal proceeding or issues, it has not been prepared as nor is it intended to express any legal conclusion, opinion or advice. Investors should consult their own legal advisers as to issues of law relating to the subject matter of this report. Merrill Lynch research personnel's knowledge of legal proceedings in which any Merrill Lynch entity and/or its directors, officers and employees may be plaintiffs, defendants, co-defendants or co-plaintiffs with or involving companies mentioned in this report is based on public information. Facts and views presented in this material that relate to any such proceedings have not been reviewed by, discussed with, and may not reflect information known to, professionals in other business areas of Merrill Lynch in connection with the legal proceedings or matters relevant to such proceedings.

This report has been prepared independently of any issuer of securities mentioned herein and not in connection with any proposed offering of securities or as agent of any issuer of any securities. None of MLPF&S, any of its affiliates or their research analysts has any authority whatsoever to make any representation or warranty on behalf of the issuer(s). Merrill Lynch policy prohibits research personnel from disclosing a recommendation, investment rating, or investment thesis for review by an issuer prior to the publication of a research report containing such rating, recommendation or investment thesis.

Any information relating to the tax status of financial instruments discussed herein is not intended to provide tax advice or to be used by anyone to provide tax advice. Investors are urged to seek tax advice based on their particular circumstances from an independent tax professional.

The information herein (other than disclosure information relating to Merrill Lynch and its affiliates) was obtained from various sources and we do not guarantee its accuracy. This report may contain links to third-party websites. Merrill Lynch is not responsible for the content of any third-party website or any linked content contained in a third-party website. Content contained on such third-party websites is not part of this report and is not incorporated by reference into this report. The inclusion of a link in this report does not imply any endorsement by or any affiliation with Merrill Lynch. Access to any third-party website is at your own risk, and you should always review the terms and privacy policies at third-party websites before submitting any personal information to them. Merrill Lynch is not responsible for such terms and privacy policies and expressly disclaims any liability for them.

Subject to the quiet period applicable under laws of the various jurisdictions in which we distribute research reports and other legal and Merrill Lynch policy-related restrictions on the publication of research reports, fundamental equity reports are produced on a regular basis as necessary to keep the investment recommendation current.

Certain outstanding reports may contain discussions and/or investment opinions relating to securities, financial instruments and/or issuers that are no longer current. Always refer to the most recent research report relating to a company or issuer prior to making an investment decision.

In some cases, a company or issuer may be classified as Restricted or may be Under Review or Extended Review. In each case, investors should consider any investment opinion relating to such company or issuer (or its security and/or financial instruments) to be suspended or withdrawn and should not rely on the analyses and investment opinion(s) pertaining to such issuer (or its securities and/or financial instruments) nor should the analyses or opinion(s) be considered a solicitation of any kind. Sales persons and financial advisors affiliated with BAS, BAI, MLPF&S or any of their affiliates may not solicit purchases of securities or financial instruments that are Restricted or Under Review and may only solicit securities under Extended Review in accordance with firm policies.

Neither Merrill Lynch nor any officer or employee of Merrill Lynch accepts any liability whatsoever for any direct, indirect or consequential damages or losses arising from any use of this report or its contents.

American Water Works

Story heading upstream; recent management meetings

Company Update **BUY**

Equity | United States | Hydro-Electric Utilities
15 March 2010

Bank of America Merrill Lynch

Steve Fleishman +1 646 855-2906
Research Analyst
MLPF&S
steven.fleishman@baml.com

David A. Paz +1 646 855 1470
Research Analyst
MLPF&S
david.paz@baml.com

Meetings with CEO and CFO; 7-10% growth intact

AWK stock has suffered since management gave little color supporting its $1.30-$1.40 guidance for 2010. At meetings with management last week, they were confident on achieving the 7-10% earnings growth target. We believe fundamental growth drivers of rate relief and ratebase growth are intact. Over time, we expect management will get more accustomed to how it can better communicate earnings guidance drivers without pre-judging rate cases.

Regulatory updates promising

AWK posted an approximate 6.3% regulated ROE in 2009. This leaves tremendous room for earnings improvement with fair rate relief. Every 100bp improvement in ROE would worth $0.20/share of EPS. The company has $250M of cases pending – a recent ALJ position in IL was supportive. Support by the new NJ Governor's task force for a water infrastructure rider was also a positive signal.

Index opportunity?

With no more foreign RWE ownership and a $3.7B market cap, AWK is now eligible to be a member of either the S&P 500 or 400. This would bring in index buyers if it happens. On the other hand, we also expect AWK to issue new equity later this year to fund its ratebase growth.

Multiple growth drivers; cheap vs water peers

By narrowing its under-earning situation and continuing to grow its core ratebase, we believe AWK can meet its 7-10% growth target. We see additional opportunity through consolidation and privatization of the water sector, where activity has picked up. AWK trades at a 15% discount to the peer group. Our price objective is $24, or 16x our 2011E, in line with the water peers. Risks to our price objective are regular reviews of $1.25B in goodwill on the balance sheet, regular future equity needs, and the importance of successful rate relief in various jurisdictions.

Stock Data

Price	US$20.96
Price Objective	US$24.00
Date Established	11-Jul-2008
Investment Opinion	B-1-7
Volatility Risk	MEDIUM
52-Week Range	US$16.42-23.77
Mrkt Val / Shares Out (mn)	US$3,658 / 174.5
BofAML Ticker / Exchange	AWK / NYS
Bloomberg / Reuters	AWK US / AWK.N
ROE (2010E)	5.9%
Total Dbt to Cap (Dec-2009A)	56.8%
Est. 5-Yr EPS / DPS Growth	8.7% / 4.5%

Estimates (Dec)

(US$)	2008A	2009A	2010E	2011E	2012E
EPS	1.10	1.25	1.37	1.49	1.60
GAAP EPS	(3.52)	(1.39)	1.37	1.49	1.60
EPS Change (YoY)	10.0%	13.6%	9.6%	8.8%	7.4%
Consensus EPS (Bloomberg)			1.38	1.52	1.58
DPS	0.40	0.84	0.86	0.90	0.94

Valuation (Dec)

	2008A	2009A	2010E	2011E	2012E
P/E	19.1x	16.8x	15.3x	14.1x	13.1x
GAAP P/E	NM	NM	15.3x	14.1x	13.1x
Dividend Yield	1.9%	4.0%	4.1%	4.3%	4.5%
EV / EBITDA*	10.6x	9.8x	8.8x	8.1x	7.4x
Free Cash Flow Yield*	-12.9%	-5.5%	-7.4%	-7.7%	-4.6%

* For full definitions of *iQmethod*SM measures, see page 6.

Merrill Lynch does and seeks to do business with companies covered in its research reports. As a result, investors should be aware that the firm may have a conflict of interest that could affect the objectivity of this report. Investors should consider this report as only a single factor in making their investment decision.

Refer to important disclosures on page 7 to 9. Analyst Certification on Page 5. Price Objective Basis/Risk on page 5. 10919826

iQprofile℠ American Water Works

iQmethod℠ – Bus Performance*

(US$ Millions)	2008A	2009A	2010E	2011E	2012E
Return on Capital Employed	-1.3%	1.2%	3.3%	3.4%	3.6%
Return on Equity	4.1%	5.2%	5.9%	6.3%	6.7%
Operating Margin	-8.0%	7.1%	27.5%	28.7%	29.8%
Free Cash Flow	(471)	(201)	(269)	(283)	(167)

iQmethod℠ – Quality of Earnings*

(US$ Millions)	2008A	2009A	2010E	2011E	2012E
Cash Realization Ratio	3.1x	2.8x	2.3x	2.3x	2.3x
Asset Replacement Ratio	3.8x	2.7x	2.9x	3.0x	2.7x
Tax Rate	NM	NM	39.0%	39.0%	39.0%
Net Debt-to-Equity Ratio	128.9%	136.4%	129.3%	123.3%	117.5%
Interest Cover	-0.7x	0.6x	2.2x	2.4x	2.5x

Income Statement Data (Dec)

(US$ Millions)	2008A	2009A	2010E	2011E	2012E
Sales	2,337	2,441	2,604	2,752	2,913
% Change	5.5%	4.4%	6.7%	5.7%	5.9%
Gross Profit	1,033	1,116	1,224	1,325	NA
% Change	6.8%	8.1%	9.6%	8.3%	NA
EBITDA	843	918	1,012	1,108	1,208
% Change	5.5%	8.9%	10.3%	9.4%	9.1%
Net Interest & Other Income	(264)	(285)	(309)	(320)	(338)
Net Income (Adjusted)	**176**	**210**	**248**	**287**	**324**
% Change	**10.6%**	**19.2%**	**18.2%**	**15.6%**	**13.1%**

Free Cash Flow Data (Dec)

(US$ Millions)	2008A	2009A	2010E	2011E	2012E
Net Income from Cont Operations (GAAP)	(562)	(233)	248	287	324
Depreciation & Amortization	271	294	297	317	339
Change in Working Capital	6	(42)	0	0	0
Deferred Taxation Charge	94	139	110	127	144
Other Adjustments, Net	744	438	(74)	(74)	(74)
Capital Expenditure	(1,023)	(797)	(850)	(940)	(900)
Free Cash Flow	**-471**	**-201**	**-269**	**-283**	**-167**
% Change	**-65.4%**	**57.4%**	**-34.2%**	**-5.1%**	**40.8%**

Balance Sheet Data (Dec)

(US$ Millions)	2008A	2009A	2010E	2011E	2012E
Cash & Equivalents	10	22	14	50	134
Trade Receivables	149	149	149	149	149
Other Current Assets	259	327	327	327	327
Property, Plant & Equipment	10,124	10,677	11,255	11,903	12,464
Other Non-Current Assets	2,690	2,276	2,370	2,464	2,558
Total Assets	**13,232**	**13,453**	**14,116**	**14,893**	**15,633**
Short-Term Debt	479	119	119	119	119
Other Current Liabilities	450	434	434	434	434
Long-Term Debt	4,824	5,366	5,516	5,741	5,941
Other Non-Current Liabilities	3,372	3,528	3,699	3,887	4,092
Total Liabilities	**9,125**	**9,447**	**9,768**	**10,181**	**10,587**
Total Equity	**4,107**	**4,005**	**4,348**	**4,712**	**5,046**
Total Equity & Liabilities	**13,232**	**13,453**	**14,116**	**14,893**	**15,633**

* For full definitions of *iQmethod*℠ measures, see page 6.

Company Description

American Water is headquartered in New Jersey and provides regulated water service in 20 states. New Jersey and Pennsylvania are the two largest states with each representing 20-25% of revenues. American Water Enterprises is the non-regulated business and represents a modest 5% of total earnings. The non-regulated business lines include 1) water service contracts with military bases, 2) homeowner repair, 3) contract operations for large cities, 4) water reuse, and 5) desalination.

Investment Thesis

As the largest public traded water utility, AWK is a pureplay on the growth prospects for the water utility business, which include the need for substantial capex spend to upgrade an aging system and the potential consolidation or outsourcing of the government-owned share of the water sector. AWK is also a turnaround story, making great strides in improving earned returns at its regulated business. AWK is positioned to grow EPS by 7-10% and its dividend by 5% per year over the next few years.

Stock Data

Average Daily Volume	1,291,975

Quarterly Earnings Estimates

	2009	2010
Q1	0.19A	NA
Q2	0.32A	NA
Q3	0.52A	NA
Q4	0.22A	NA

Highlights of management meetings

We hosted investors meetings with AWK's CEO and CFO in Boston last week. The meetings came a week after AWK reported 2009 results and provided forward earnings guidance for the first time. The 2010 guidance of $1.30-$1.40 was below the then-consensus of $1.44, though in line with management's stated 7-10% growth rate target. More concerning to some was management's unwillingness to provide any color on the assumptions baked into this guidance range. The bottom line from our recent meetings is that management remains confident in achieving its 7-10% growth target. We would not view the lack of guidance color as a sign of weakening business fundamentals, but rather a management team that is grappling with how to provide guidance when the earnings outlook is heavily driven by pending regulatory orders. Below we address topics of discussion as well as some recent developments.

Guidance

Management's key target is 7-10% earnings growth. This is the most important measure for incentive comp. Consensus estimates had risen above this target range, and we believe this may have been one of the reasons management provided the $1.30-$1.40 guidance for 2010. With respect to guidance drivers, management is concerned about giving too much information, particularly on the topic of rate case outcomes which are one of the most important earnings factors. Management does not want to be in a position of pre-judging pending rate cases. While we can understand the sensitivity around this, we have seen electric utilities find ways to handle this balance over time. We expect AWK will as well. Most importantly, we sensed nothing fundamentally concerning that caused management to limit its guidance commentary.

Regulatory updates

AWK has about $250M of pending rate relief requested in 11 different cases. The largest of those cases is a $58.5M request in Illinois. On February 22, an administrative law judge issued a proposed decision recommending a $44.7M rate hike based on a 10.38% ROE and 47.33% equity ratio (the company was seeking a 10.7%-11.1% ROE and a 48.63% equity ratio). We view this ALJ proposal as constructive. A final ICC order is expected over the next few months.

More recently in Missouri, the PSC staff recommended a $22M rate hike versus the company's $49M request. The staff position is based on a 9.25% ROE, 46.21% equity ratio and $759M ratebase versus the company at 11.6% ROE, 48.94% equity and $792M ratebase. Given our knowledge of the Missouri PSC staff on the electric side, we would view this as better than normal. That said, we would hope for a better ROE in the final order.

Finally, AWK continues to work on implementing an infrastructure charge in its largest state, New Jersey. A task force for the new governor recently recommended that the Board of Public Utilities should support such a rider, known as a DSIC. While it is not clear how the BPU will proceed or the timing, a DSIC mechanism in NJ would be a significant positive for AWK as it would allow timely recovery of new investment. This in turn would meaningfully reduce regulatory lag and help AWK have a better chance to earn its allowed return. AWK has a DSIC in place in its second largest state: PA. Success with a DSIC in NJ could serve as templates for other states to consider.

S&P index potential

AWK is not currently a member of any S&P index due to the foreign ownership of the company by RWE. With RWE fully exiting in November, there are no limitations on them becoming part of one of the indexes. With a $3.7B market cap, it is not clear if AWK would go into the S&P 500 or the S&P 400 (midcap). Either way, we believe there would be significant index buying of the stock. In discussing this with a BofAML index analyst, there could be 17M shares to buy if AWK entered the S&P 500 and 12M shares for the S&P 400. On the other hand, AWK also plans to issue new equity this year. We are assuming $250M in the second half of 2010.

Earned ROEs and sales

Excluding parent interest, we estimate AWK only earned a 6.3% regulatory ROE in 2009. This is well below the typical allowed returns of 10%. While regulatory lag will likely always result in maybe 100bp of underearning, AWK appears to have substantial room to improve its earned returns. Every 100bp of better earned returns would worth roughly $0.20/share to EPS.

One of the reasons AWK earned so poorly in 2009 was weak sales which were down over 5%. It is hard for management to break down this weakness between the economy, conservation and unfavorable weather. Nonetheless, we believe it is important for investors to understand that the regulatory process allows AWK a chance to catch up with this. The 2009 sales become the base for the historical test year for upcoming rate cases. AWK should be able to seek rate relief to cover a lower sales level so it can earn a fair return. However, such rate relief might not actually be implemented until 2011 (file rate case in 2010 based on the 2009 test year – implement final order by early 2011).

Privatization and M&A

One of the long-term themes in the water sector is the potential for privatization since 85% of the water business is still owned by government entities. With rising capex needs and worsening municipal woes, the conditions for this seem to be ripening. Interestingly, the city of Indianapolis just announced a potential sale of its water and sewage operations to Citizen Energy, a non-profit company. While AWK did not win this, it is a signal that this trend might be heating up.

Separately, a small public water company Southwest Water was recently acquired by a group of infrastructure funds. Valuations of this deal appeared quite attractive at roughly 2.3x book value.

Price objective basis & risk

American Water Works (AWK)

Our $24 price objective is based on a P/E of 16x 2011E earnings of $1.49. This P/E is around the average multiple for other water utilities. Risks to our price objective are regular reviews of $1.25B in goodwill on the balance sheet, regular future equity needs, and the importance of successful rate relief in various jurisdictions.

Analyst Certification

I, Steve Fleishman, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers.
I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Electric Utilities/Competitive Power Coverage Cluster

Investment rating	Company	BofAML ticker	Bloomberg symbol	Analyst
BUY				
	American Water Works	AWK	AWK US	Steve Fleishman
	CMS Energy	CMS	CMS US	Steve Fleishman
	Entergy	ETR	ETR US	Steve Fleishman
	Northeast Utilities	NU	NU US	Steve Fleishman
	PG&E Corporation	PCG	PCG US	Steve Fleishman
	PPL Corporation	PPL	PPL US	Steve Fleishman
	TECO Energy	TE	TE US	Steve Fleishman
	Wisconsin Energy	WEC	WEC US	Alex Kania
NEUTRAL				
	Alliant Energy	LNT	LNT US	Steve Fleishman
	Calpine	CPN	CPN US	Ameet I. Thakkar
	Consolidated Edison	ED	ED US	Steve Fleishman
	Dominion Resources	D	D US	Steve Fleishman
	Edison International	EIX	EIX US	Steve Fleishman
	FirstEnergy	FE	FE US	Steve Fleishman
	FPL Group	FPL	FPL US	Steve Fleishman
	NRG Energy	NRG	NRG US	Ameet I. Thakkar
	NSTAR	NST	NST US	Steve Fleishman
	Pinnacle West	PNW	PNW US	Steve Fleishman
	Progress Energy	PGN	PGN US	Steve Fleishman
	SCANA Corp.	SCG	SCG US	Steve Fleishman
	Xcel Energy	XEL	XEL US	Steve Fleishman
UNDERPERFORM				
	DPL Inc.	DPL	DPL US	Steve Fleishman
	DTE Energy	DTE	DTE US	Steve Fleishman
	Duke Energy	DUK	DUK US	Steve Fleishman
	Dynegy	DYN	DYN US	Ameet I. Thakkar
	Exelon	EXC	EXC US	Steve Fleishman
	Hawaiian Electric Industries	HE	HE US	Steve Fleishman
	NV Energy	NVE	NVE US	Steve Fleishman
	Portland General Electric Company	POR	POR US	Steve Fleishman
	RRI Energy	RRI	RRI US	Ameet I. Thakkar
	Southern Company	SO	SO US	Steve Fleishman

*iQmethod*SM Measures Definitions

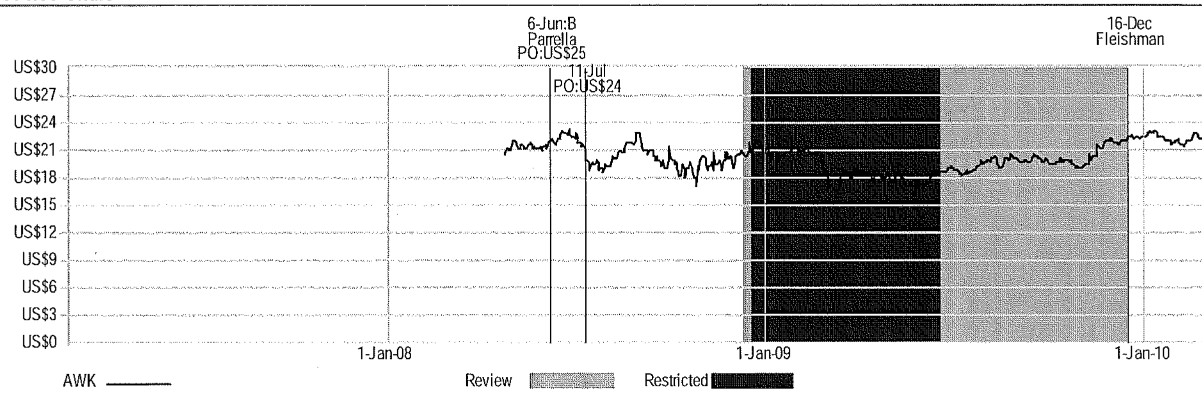
Business Performance	Numerator	Denominator
Return On Capital Employed	NOPAT = (EBIT + Interest Income) * (1 - Tax Rate) + Goodwill Amortization	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	EV = Current Share Price * Current Shares + Minority Equity + Net Debt + Other LT Liabilities	Sales
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

*iQmethod*SM is the set of BofA Merrill Lynch standard measures that serve to maintain global consistency under three broad headings: Business Performance, Quality of Earnings, and validations. The key features of iQmethod are: A consistently structured, detailed, and transparent methodology. Guidelines to maximize the effectiveness of the comparative valuation process, and to identify some common pitfalls.

iQdatabase® is our real-time global research database that is sourced directly from our equity analysts' earnings models and includes forecasted as well as historical data for income statements, balance sheets, and cash flow statements for companies covered by BofA Merrill Lynch.

Important Disclosures

AWK Price Chart



B : Buy, N : Neutral, S : Sell, U : Underperform, PO : Price objective, NA : No longer valid

"Prior to May 31, 2008, the investment opinion system included Buy, Neutral and Sell. As of May 31, 2008, the investment opinion system includes Buy, Neutral and Underperform. Dark Grey shading indicates that a security is restricted with the opinion suspended. Light grey shading indicates that a security is under review with the opinion withdrawn. The current investment opinion key is contained at the end of the report. Chart is current as of February 28, 2010 or such later date as indicated.

BofAML price charts do not reflect analysts' coverage of the stock at prior firms. Historical price charts relating to companies covered as of December 31, 2008 by former Banc of America Securities LLC (BAS) analysts are available to BAS clients on the BAS website."

Investment Rating Distribution: Utilities Group (as of 01 Jan 2010)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	70	41.18%	Buy	45	70.31%
Neutral	48	28.24%	Neutral	24	54.55%
Sell	52	30.59%	Sell	17	37.78%

Investment Rating Distribution: Global Group (as of 01 Jan 2010)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1699	50.78%	Buy	904	58.82%
Neutral	841	25.13%	Neutral	491	65.03%
Sell	806	24.09%	Sell	368	49.80%

* Companies in respect of which MLPF&S or an affiliate has received compensation for investment banking services within the past 12 months. For purposes of this distribution, a stock rated Underperform is included as a Sell.

FUNDAMENTAL EQUITY OPINION KEY: Opinions include a Volatility Risk Rating, an Investment Rating and an Income Rating. *VOLATILITY RISK RATINGS*, indicators of potential price fluctuation, are: A - Low, B - Medium and C - High. *INVESTMENT RATINGS* reflect the analyst's assessment of a stock's: (i) absolute total return potential and (ii) attractiveness for investment relative to other stocks within its *Coverage Cluster* (defined below). There are three investment ratings: 1 - Buy stocks are expected to have a total return of at least 10% and are the most attractive stocks in the coverage cluster; 2 - Neutral stocks are expected to remain flat or increase in value and are less attractive than Buy rated stocks and 3 - Underperform stocks are the least attractive stocks in a coverage cluster. Analysts assign investment ratings considering, among other things, the 0-12 month total return expectation for a stock and the firm's guidelines for ratings dispersions (shown in the table below). The current price objective for a stock should be referenced to better understand the total return expectation at any given time. The price objective reflects the analyst's view of the potential price appreciation (depreciation).

Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where BofAML Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

***INCOME RATINGS*, indicators of potential cash dividends, are: 7 - same/higher (dividend considered to be secure), 8 - same/lower (dividend not considered to be secure) and 9 - pays no cash dividend.** *Coverage Cluster* is comprised of stocks covered by a single analyst or two or more analysts sharing a common industry, sector, region or other classification(s). A stock's coverage cluster is included in the most recent BofAML Comment referencing the stock.

MLPF&S or one of its affiliates acts as a market maker for the equity securities recommended in the report: American Water.
MLPF&S or an affiliate was a manager of a public offering of securities of this company within the last 12 months: American Water.
The company is or was, within the last 12 months, an investment banking client of MLPF&S and/or one or more of its affiliates: American Water.
MLPF&S or an affiliate has received compensation from the company for non-investment banking services or products within the past 12 months: American Water.
The company is or was, within the last 12 months, a non-securities business client of MLPF&S and/or one or more of its affiliates: American Water.
MLPF&S or an affiliate has received compensation for investment banking services from this company within the past 12 months: American Water.
MLPF&S or an affiliate expects to receive or intends to seek compensation for investment banking services from this company or an affiliate of the company within the next three months: American Water.
MLPF&S or one of its affiliates is willing to sell to, or buy from, clients the common equity of the company on a principal basis: American Water.
The company is or was, within the last 12 months, a securities business client (non-investment banking) of MLPF&S and/or one or more of its affiliates: American Water.
The analyst(s) responsible for covering the securities in this report receive compensation based upon, among other factors, the overall profitability of Bank of America Corporation, including profits derived from investment banking revenues.

Other Important Disclosures

BofA Merrill Lynch (BofAML) Research refers to the combined Global Research operations of Merrill Lynch and BAS.
Officers of MLPF&S or one or more of its affiliates (other than research analysts) may have a financial interest in securities of the issuer(s) or in related investments.
Merrill Lynch Research policies relating to conflicts of interest are described at http://www.ml.com/media/43347.pdf.
"Merrill Lynch" includes Merrill Lynch, Pierce, Fenner & Smith Incorporated ("MLPF&S") and its affiliates, including BofA (defined below). "BofA" refers to Banc of America Securities LLC ("BAS"), Banc of America Securities Limited ("BASL") and their affiliates. Investors should contact their Merrill Lynch or BofA representative if they have questions concerning this report.
Information relating to Non-US affiliates of Merrill Lynch and Distribution of Affiliate Research Reports:
MLPF&S, BAS, and BASL distribute, or may in the future distribute, research reports of the following non-US affiliates in the US (short name: legal name): Merrill Lynch (France): Merrill Lynch Capital Markets (France) SAS; Merrill Lynch (Frankfurt): Merrill Lynch International Bank Ltd, Frankfurt Branch; Merrill Lynch (South Africa): Merrill Lynch South Africa (Pty) Ltd; Merrill Lynch (Milan): Merrill Lynch International Bank Limited; MLPF&S (UK): Merrill Lynch, Pierce, Fenner & Smith Limited; Merrill Lynch (Australia): Merrill Lynch Equities (Australia) Limited; Merrill Lynch (Hong Kong): Merrill Lynch (Asia Pacific) Limited; Merrill Lynch (Singapore): Merrill Lynch (Singapore) Pte Ltd; Merrill Lynch (Canada): Merrill Lynch Canada Inc; Merrill Lynch (Mexico): Merrill Lynch Mexico, SA de CV, Casa de Bolsa; Merrill Lynch (Argentina): Merrill Lynch Argentina SA; Merrill Lynch (Japan): Merrill Lynch Japan Securities Co, Ltd; Merrill Lynch (Seoul): Merrill Lynch International Incorporated (Seoul Branch); Merrill Lynch (Taiwan): Merrill Lynch Securities (Taiwan) Ltd.; DSP Merrill Lynch (India): DSP Merrill Lynch Limited; PT Merrill Lynch (Indonesia): PT Merrill Lynch Indonesia; Merrill Lynch (Israel): Merrill Lynch Israel Limited; Merrill Lynch (Russia): Merrill Lynch CIS Limited, Moscow; Merrill Lynch (Turkey): Merrill Lynch Yatirim Bankasi A.S.; Merrill Lynch (Dubai): Merrill Lynch International, Dubai Branch; MLPF&S (Zürich rep. office): MLPF&S Incorporated Zürich representative office; Merrill Lynch (Spain): Merrill Lynch Capital Markets Espana, S.A.S.V.; Merrill Lynch (Brazil): Banco Merrill Lynch de Investimentos S.A.
This note has been approved for publication in the United Kingdom by Merrill Lynch, Pierce, Fenner & Smith Limited and BASL, which are authorized and regulated by the Financial Services Authority; has been considered and distributed in Japan by Merrill Lynch Japan Securities Co, Ltd and Banc of America Securities – Japan, Inc., registered securities dealers under the Financial Instruments and Exchange Law in Japan; is distributed in Hong Kong by Merrill Lynch (Asia Pacific) Limited and Banc of America Securities Asia Limited, which are regulated by the Hong Kong SFC and the Hong Kong Monetary Authority; is issued and distributed in Taiwan by Merrill Lynch Securities (Taiwan) Ltd.; is issued and distributed in India by DSP Merrill Lynch Limited; and is issued and distributed in Singapore by Merrill Lynch International Bank Limited (Merchant Bank), Merrill Lynch (Singapore) Pte Ltd (Company Registration No.'s F 06872E and 198602883D respectively) and Bank of America Singapore Limited (Merchant Bank). Merrill Lynch International Bank Limited (Merchant Bank), Merrill Lynch (Singapore) Pte Ltd and Bank of America Singapore Limited (Merchant Bank) are regulated by the Monetary Authority of Singapore. Merrill Lynch Equities (Australia) Limited (ABN 65 006 276 795), AFS License 235132 provides this note in Australia in accordance with section 911B of the Corporations Act 2001 and neither it nor any of its affiliates involved in preparing this note is an Authorised Deposit-Taking Institution under the Banking Act 1959 nor regulated by the Australian Prudential Regulation Authority. No approval is required for publication or distribution of this note in Brazil.
This research report has been prepared and issued by MLPF&S and/or one or more of its non-US affiliates. MLPF&S is the distributor of this research report in the US and accepts full responsibility for research reports of its non-US affiliates distributed to MLPF&S clients in the US. Any US person (other than BAS, BAI and their respective clients) receiving this research report and wishing to effect any transaction in any security discussed in the report should do so through MLPF&S and not such foreign affiliates.
BAS distributes this research report to its clients and accepts responsibility for the distribution of this report in the US to BAS clients. Transactions by US persons that are BAS clients in any security discussed herein must be carried out through BAS.
General Investment Related Disclosures:
This research report provides general information only. Neither the information nor any opinion expressed constitutes an offer or an invitation to make an offer, to buy or sell any securities or other financial instrument or any derivative related to such securities or instruments (e.g., options, futures, warrants, and contracts for differences). This report is not intended to provide personal investment advice and it does not take into account the specific investment objectives, financial situation and the particular needs of any specific person. Investors should seek financial advice regarding the appropriateness of investing in financial instruments and implementing investment strategies discussed or recommended in this report and should understand that statements regarding future prospects may not be realized. Any decision to purchase or subscribe for securities in any offering must be based solely on existing public information on such security or the information in the prospectus or other offering document issued in connection with such offering, and not on this report.

Securities and other financial instruments discussed in this report, or recommended, offered or sold by Merrill Lynch, are not insured by the Federal Deposit Insurance Corporation and are not deposits or other obligations of any insured depository institution (including, Bank of America, N.A.). Investments in general and, derivatives, in particular, involve numerous risks, including, among others, market risk, counterparty default risk and liquidity risk. No security, financial instrument or derivative is suitable for all investors. In some cases, securities and other financial instruments may be difficult to value or sell and reliable information about the value or risks related to the security or financial instrument may be difficult to obtain. Investors should note that income from such securities and other financial instruments, if any, may fluctuate and that price or value of such securities and instruments may rise or fall and, in some cases, investors may lose their entire principal investment. Past performance is not necessarily a guide to future performance. Levels and basis for taxation may change.

This report may contain a short-term trading idea or recommendation, which highlights a specific near-term catalyst or event impacting the company or the market that is anticipated to have a short-term price impact on the equity securities of the company. Short-term trading ideas and recommendations are different from and do not affect a stock's fundamental equity rating, which reflects both a longer term total return expectation and attractiveness for investment relative to other stocks within its Coverage Cluster. Short-term trading ideas and recommendations may be more or less positive than a stock's fundamental equity rating.

Foreign currency rates of exchange may adversely affect the value, price or income of any security or financial instrument mentioned in this report. Investors in such securities and instruments, including ADRs, effectively assume currency risk.

UK Readers: The protections provided by the U.K. regulatory regime, including the Financial Services Scheme, do not apply in general to business coordinated by Merrill Lynch entities located outside of the United Kingdom. These disclosures should be read in conjunction with the BASL general policy statement on the handling of research conflicts, which is available upon request.

Officers of MLPF&S or one or more of its affiliates (other than research analysts) may have a financial interest in securities of the issuer(s) or in related investments.

Merrill Lynch is a regular issuer of traded financial instruments linked to securities that may have been recommended in this report. Merrill Lynch may, at any time, hold a trading position (long or short) in the securities and financial instruments discussed in this report.

Merrill Lynch, through business units other than BofAML Research, may have issued and may in the future issue trading ideas or recommendations that are inconsistent with, and reach different conclusions from, the information presented in this report. Such ideas or recommendations reflect the different time frames, assumptions, views and analytical methods of the persons who prepared them, and Merrill Lynch is under no obligation to ensure that such other trading ideas or recommendations are brought to the attention of any recipient of this report.

In the event that the recipient received this report pursuant to a contract between the recipient and MLPF&S for the provision of research services for a separate fee, and in connection therewith MLPF&S may be deemed to be acting as an investment adviser, such status relates, if at all, solely to the person with whom MLPF&S has contracted directly and does not extend beyond the delivery of this report (unless otherwise agreed specifically in writing by MLPF&S). MLPF&S is and continues to act solely as a broker-dealer in connection with the execution of any transactions, including transactions in any securities mentioned in this report.

Copyright and General Information regarding Research Reports:

Materials prepared by Merrill Lynch research personnel are based on public information. Facts and views presented in this material have not been reviewed by, and may not reflect information known to, professionals in other business areas of Merrill Lynch, including investment banking personnel. Merrill Lynch has established information barriers between BofAML Research and certain business groups. As a result, Merrill Lynch does not disclose certain client relationships with, or compensation received from, such companies in research reports.

To the extent this report discusses any legal proceeding or issues, it has not been prepared as nor is it intended to express any legal conclusion, opinion or advice. Investors should consult their own legal advisers as to issues of law relating to the subject matter of this report. Merrill Lynch research personnel's knowledge of legal proceedings in which any Merrill Lynch entity and/or its directors, officers and employees may be plaintiffs, defendants, co-defendants or co-plaintiffs with or involving companies mentioned in this report is based on public information. Facts and views presented in this material that relate to any such proceedings have not been reviewed by, discussed with, and may not reflect information known to, professionals in other business areas of Merrill Lynch in connection with the legal proceedings or matters relevant to such proceedings.

This report has been prepared independently of any issuer of securities mentioned herein and not in connection with any proposed offering of securities or as agent of any issuer of any securities. None of MLPF&S, any of its affiliates or their research analysts has any authority whatsoever to make any representation or warranty on behalf of the issuer(s). Merrill Lynch policy prohibits research personnel from disclosing a recommendation, investment rating, or investment thesis for review by an issuer prior to the publication of a research report containing such rating, recommendation or investment thesis.

Any information relating to the tax status of financial instruments discussed herein is not intended to provide tax advice or to be used by anyone to provide tax advice. Investors are urged to seek tax advice based on their particular circumstances from an independent tax professional.

The information herein (other than disclosure information relating to Merrill Lynch and its affiliates) was obtained from various sources and we do not guarantee its accuracy. This report may contain links to third-party websites. Merrill Lynch is not responsible for the content of any third-party website or any linked content contained in a third-party website. Content contained on such third-party websites is not part of this report and is not incorporated by reference into this report. The inclusion of a link in this report does not imply any endorsement by or any affiliation with Merrill Lynch. Access to any third-party website is at your own risk, and you should always review the terms and privacy policies at third-party websites before submitting any personal information to them. Merrill Lynch is not responsible for such terms and privacy policies and expressly disclaims any liability for them.

Subject to the quiet period applicable under laws of the various jurisdictions in which we distribute research reports and other legal and Merrill Lynch policy-related restrictions on the publication of research reports, fundamental equity reports are produced on a regular basis as necessary to keep the investment recommendation current.

Certain outstanding reports may contain discussions and/or investment opinions relating to securities, financial instruments and/or issuers that are no longer current. Always refer to the most recent research report relating to a company or issuer prior to making an investment decision.

In some cases, a company or issuer may be classified as Restricted or may be Under Review or Extended Review. In each case, investors should consider any investment opinion relating to such company or issuer (or its security and/or financial instruments) to be suspended or withdrawn and should not rely on the analyses and investment opinion(s) pertaining to such issuer (or its securities and/or financial instruments) nor should the analyses or opinion(s) be considered a solicitation of any kind. Sales persons and financial advisors affiliated with BAS, MLPF&S or any of their affiliates may not solicit purchases of securities or financial instruments that are Restricted or Under Review and may only solicit securities under Extended Review in accordance with firm policies.

Neither Merrill Lynch nor any officer or employee of Merrill Lynch accepts any liability whatsoever for any direct, indirect or consequential damages or losses arising from any use of this report or its contents.

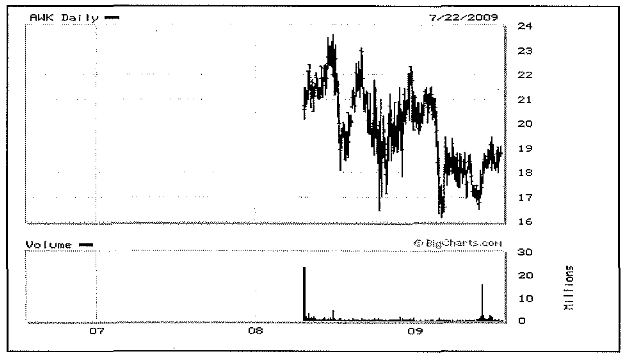
American Water Works Company, Inc. (AWK-$19.26) BUY

Initiation of Coverage **Target: $27**

Christian Bradbury (212) 894-3337 (cbradbury@sidoti.com) **July 24, 2009**

Market Cap (Mil)	$3,082	Price to Book Value	0.8x
Avg. Daily Trading Volume	1,112,600	Return on Equity (2010E)	6.2%
Shares Out (Mil)	160.030	LT Debt-to-Total Capital	56%
Float Shares (Mil)	85.280	5-Year EPS Growth Rate Projection	11%
Institutional Holdings	34%	52-Week Range (NYSE)	24-16
Dividend	$0.80	Russell 2000	546
Dividend Yield	4.2%	Short Interest (Mil)	2.680

	2007	2008	2009E	2010E
Mar.	$0.02	$0.05	$0.18A	$0.20
June	0.29	0.28	0.33	0.37
Sept.	0.47	0.55	0.58	0.63
Dec.	0.17	0.24	0.26	0.28
Cal.	**$0.95**	**$1.12**	**$1.35**	**$1.48**
P/E (Cal.)			**14.3x**	**13.0x**



Note: Exclude impairment charges of $3.09 for 2007, $4.64 for 2008 and $2.76 for 1Q:09. 2008-2010E includes $0.03 annual stock-based compensation expense. Sum of quarterly EPS may not equal full-year total due to changes in share count and/or rounding. AWK is in the S&P 400 MidCap Index. NC=Not covered by Sidoti & Company, LLC.

Year	2001	2002	2003	2004	2005	2006	2007	2008	2009E	2010E
Rev.(Mil.)	N/A	N/A	N/A	$2017.9	$2136.7	$2093.1	$2214.2	$2336.9	$2523.9	$2700.6
GAAP EPS	N/A	N/A	N/A	$0.37	$(1.72)	$(0.97)	$(2.14)	$(3.52)	$(1.41)	$1.48
Dividend	N/A	N/A	N/A	N/A	N/A	N/A	N/A	$0.40	$0.80	$0.84

* AWK completed an initial public offering on April 28, 2008 with the sale of 58 million shares at $21.50 each.

Description: American Water Works Company, Inc. (www.amwater.com) owns and operates regulated water and wastewater systems. Through its subsidiaries, the company provides drinking water, wastewater and water-related services to approximately 15 million people in 32 states across the U.S. and Ontario, Canada. Headquarters are in Voorhees, NJ.

Initiate Coverage Of American Water Works Co., Inc., With A BUY Rating And $27 Price Target

- **We admit that America's largest investor-owned utility is not without problems...** The acquisition of American Water Company by RWE AG in 2003 was met with tremendous criticism, and the German company's grandiose designs on the U.S. market proved ill-fated. Since April 2008, RWE has unloaded 53% of its American Water stake (the stock traded from 1947 to 2003 as an independent entity) and plans to sell its remaining 47% holding by April 2010. However, the market downturn puts the timing in doubt, in our view, and perhaps dampens investor sentiment. In addition, American Water, under new management since late-2006, continues to work through goodwill write-downs (impairment charges of $1.7 billion from 2007-1Q:09, and $1.25 billion of goodwill remains) primarily associated with RWE's acquisition in 2003.

- **...but suggest investors have been overly hard on AWK shares.** Notwithstanding apparent investor misgivings about an S&P downgrade (the debt of peers cited in Exhibit 1 on page 5 is all rated "A" by S&P) and goodwill comprising almost 10% of total assets, we argue that AWK is well undervalued versus the peer group. We calculate annual cash from operations of $575 million, on average, is sustainable through 2010 after a 17% increase in 2008 to $552 million, and we find the debt-to-equity ratio on par with peers. With water utility peers currently trading at 19x consensus 2010 EPS estimates, we consider AWK inexpensive at just 13x our 2010 adjusted EPS estimate based on the company's earnings potential as the largest U.S. regulated investor-owned water-utility, with its monopoly of more than 15 million customers. This base is well ahead of No. 2 player Aqua America, Inc.'s (NYSE: WTR, BUY) 3 million customers).

- **Our compound annual EPS growth target of 11% factors steady rate increases and acquisitions.** The five-year rate-freeze concession by RWE to curry regulatory favor for the American Water acquisition in 2003 has expired, and American Water will continue to seek steep rate hikes despite the recession, in our view. State regulators awarded the company approximately $200 million of increases in 2008, with the largest in New Jersey ($72.1 million), Missouri ($34.5 million) and Illinois ($21.6 million). We expect AWK to file for an additional $300 million of rate relief in 2009 to recover higher operating expenses and infrastructure investments related to the acquisition of distressed municipal utilities, on the order of the $75 million purchase of four systems in Trenton, N.J., which were in need of a quick fix for a $28 million budget deficit. We expect the recession to create similar situations across the U.S. and target California as the biggest opportunity for AWK.

- **AWK's large geographic presence is a competitive advantage, in our view, and its balance sheet is in line with industry averages.** American Water is the largest and most geographically diverse investor-owned water utility in the U.S., providing drinking water and wastewater services across 32 states and Ontario, Canada, and the monopolistic status of investor-owned water utilities keeps them largely free of direct competition. We are confident that write-downs will not impair cash flow, but admit an impairment charge could diminish book value and boost the company's leverage ratios. Although American Water is already highly leveraged (i.e., the consequence of significant capital investment), we find its capital ratios in line with other publicly traded companies in the sector. Also, we are not too concerned about a debt-rating downgrade, particularly since American Water's recent $80 million tax-exempt debt issue at a favorable 6.2% coupon was rated "A" by S&P and "A3" by Moody's (upper-medium grades on both fronts).

- **We initiate coverage of American Water Works Company, Inc. with a BUY rating and $27 price target.** AWK shares are down 8% for 2009, versus an 8% rise in the S&P 400 MidCap Index. We attribute the weakness to the overhang of RWE's eventual sale of its 47% stake, deterring shareholders from buying the stock until this large position is liquidated. Nonetheless, at the current quote we find the valuation attractive, offering investors the opportunity to buy into the largest U.S. investor-owned water utility at a steep discount and capture an attractive (currently 4.2%) dividend yield as well. We derive our $27 target by applying a multiple of 18x to our 2010 EPS estimate of $1.48. (This multiple represents a discount of approximately 20% to our average target multiple for the peer group of 22x, given the RWE overhang.) With a potential one-year total return above 40%, we initiate coverage of AWK with a BUY rating.

Company Overview

American Water Works Company, Inc., was formed in 1886 to build and purchase water systems in Pennsylvania. The company restructured in 1935 into a utility holding company, which increased its opportunities to expand in other states and into nonregulated businesses. The company first listed on the New York Stock Exchange in 1947 under the ticker symbol "AWK".

In 2003, the New Jersey-based company was acquired by German multi-utility RWE for $7.6 billion, or nearly 3x its book value. Despite the significant premium to shareholders, the deal was widely criticized amid concern about foreign control over domestic water supplies. RWE, responding to U.S. pushback, agreed with some state regulators to freeze rates for a period of time; the freeze has since expired, but it largely explains American Water's $1 billion outlay for capital improvements (i.e., to replace underground water pipes) in 2008 and in our view, the $800 million in annual expenditures planned through 2010.

RWE, in a quick about-face, decided to unwind American Water to focus on its core electric utility business, but put the kibosh on a 2007 sale due to poor performance and weak growth prospects. Notwithstanding apparent investor disinterest in the water utility sector, on April 28, 2008 RWE spun 40% of its American Water stake through an IPO of 58 million AWK shares at $21.50 apiece, for proceeds of about $1.2 billion. Subsequent to the IPO the underwriters exercised an option to purchase 5.2 million shares.

At the end of 2008, 63 million shares of AWK were publicly traded, with the remaining 60% of outstanding shares still in RWE's hands. More recently, in June 2009, RWE lowered its ownership position further to 47% from 60%, by selling 15.4 million of its shares to a group of underwriters for approximately $250 million. American Water's 2008 10-K filing notes RWE's intent to sell its entire ownership of American Water by April 2010 through additional offerings, but given the havoc in global equity markets, we figure that RWE's divesture plans will be delayed so as not to disrupt the stock price. We attribute the outsize selling pressure on AWK (relative to other U.S. water utility stocks) to the RWE overhang that deters investors from purchasing the stock.

Regulated Operations

American Water's regulated business involves the ownership and operation of water and wastewater systems serving 15 million customers in 32 U.S. states and Ontario, Canada. In 2008, 89% of American Water revenue derived from such regulated activities, relatively flat versus 2007. Most of the company's regulated systems are in the Northeast (Pennsylvania, New Jersey and New York) and the Midwest (Missouri, Illinois and Indiana). American Water's utilities face no direct competition but are subject to regulation by their respective state Public Utility Commissions (PUCs) to ensure customers are charged reasonable rates.

Water utilities are natural monopolies and water prices must be regulated. A state regulator or PUC is responsible for ensuring that water customers receive reliable service at reasonable rates. At the same time, the PUC ensures that water utilities earn a rate of return on investment as well as maintain financial stability to obtain necessary financing. In Pennsylvania, American Water's largest service area, the Pennsylvania Public Utility Commission (PPUC) consists of three members appointed by the governor and confirmed by the state's senate. These commissioners represent the general public interest and participate in rate-case hearings.

Although some state regulators approve increases in water rates to help American Water keep up with higher operating expenses and the need for infrastructure upgrades, others are reluctant to grant requested amounts. For instance, in Chattanooga, TN, Tennessee Regulatory Authority (TRA) approved only 21% of a requested $7.6 million rate case, failing to provide sufficient revenue for American Water to cover the cost of providing service. States like Tennessee rely on elected officials, as opposed to appointed officials, which we suggest makes them more susceptible to political pressure when setting rates and therefore may compromise American Water's profitability.

In 2008, regulators in AWK's states approved rates designed to generate $206 million additional revenue on an annual basis. The largest increases were approved by New Jersey ($72.1 million), Missouri ($34.5 million) and Illinois ($21.6 million). American Water and other water utilities at large need rate relief to meet high operating expenses and higher capital investments in infrastructure replacement for new construction to serve growing populations and maintain safe, reliable water quality. In 2008, AWK spent $1 billion, up 33% from 2007, largely to replace deteriorated underground pipes. The regulated utility model makes rate relief a primary growth determinant. In 2008, operating revenue for AWK's regulated segment increased 4.8%, primarily as a result of rate increases.

Nonregulated Operations

American Water's activities here include the operation and management of municipal or government-owned water and wastewater utility systems, as well as pipe replacements, laboratory testing and other related services. Nonregulated business accounted for 11.7% of AWK's operating revenue in 2008, up from 10.9% in 2007. Our model assumes nonregulated revenue will hold flat through 2010.

Military Privatization. In 1997, the Department of Defense (DoD) developed a plan to privatize 1,700 water, electric and natural gas utility systems at U.S. Army, Navy and Air Force installations. Military privatization entails the sale of a government-owned utility system under a 50-year contract to an investor-owned water utility to manage day-to-day operations and rebuild the system. Historically, U.S. military installations have been unable to receive adequate funding to upgrade and maintain utilities, so investor-owned entities like American Water offer easier access to financing and improved efficiencies.

The most recent contract, worth an estimated $348 million of revenue to American Water through 2058, was awarded in September 2008 at Fort Polk, TX. As part of the contract, AWK will provide necessary improvements, upgrades, repairs, expansions, investments, and facility replacements, as well as continue to operate and maintain the water and wastewater systems. Price adjustments for a contract such as this typically occur after the first two years and every three years thereafter. The Fort Polk pact followed AWK contracts at Fort Hood, TX, Fort Hill, VA, Fort Bragg, NC, Fort Sill, OK, Fort Leavenworth, KS, Scott Air Force Base, IL and Fort Rucker, AL. The company has outstanding bids for more military contracts that could augment revenue, but note that contract awards can take a long time largely due to the solicitation and contracting process. Although these bids may lead to more deals, we expect nonregulated activities to remain a consistently low percentage of revenue.

The Industry Trend Toward Privatization

Privatization of water utilities is becoming more common in the U.S., with roughly 15% of 54,000 drinking water systems run by an investor-owned water utility. The remaining 85% of systems are owned by municipalities or local water authorities. Looming required capital investment, coupled with increasing budget deficits, in our view, will force publicly owned utilities to sell their systems to private companies. Although not yet finalized, Milwaukee, WI recently floated the idea of privatizing its water system in an effort to stem rising property taxes. As a result, we think the percentage of systems owned by publicly traded water utilities will grow to almost 50% over the next two decades.

American Water is in the process of acquiring 625 miles of water pipes and infrastructure, including several water towers, from Trenton (N.J.) Water Works for $75 million, a 36% premium to estimated book value of $55 million. The city is looking to pare debt from past infrastructure projects and plug a $28 million budget deficit. The acquisition will increase American Water's customer base by 40,000.

In addition, regulators will allow AWK to include the full amount of the acquisition in its rate base, which means the company will recover its full cost, plus a rate of return. We expect the transaction to close sometime in 2H:09. The Trenton deal is a good example of how the financial difficulties of municipalities are driving privatization, as we see it.

AWK's Growth Strategy

Capital Investment. As a regulated utility, American Water is entitled to recover a return on its rate base (i.e., its invested capital); the rate base essentially represents "net utility plant" and other investments required to provide reliable service to customers. In 2008 AWK spent more than $1 billion on such investments, and we expect additional expenditures totaling $1.6 billion over the next two years. At the end of 1Q:09, net utility plant, or the implied market value of AWK's physical regulated utility assets, was $10.1 billion, which we estimate will grow to $11.6 billion by the end of 2010. The growth in net utility plant suggests, to us, further expansion of the company's rate base, which will provide a source of earnings growth.

In its estimates of required long-term infrastructure investments, the Environmental Protection Agency (EPA) in 2007 projected that U.S. water utilities would need to invest $335 billion through 2027, up from a 2003 forecast of $277 billion, to add, replace and/or maintain water pipes and mains to be compliant with state and federal water quality standards. This massive $335 billion in expenditures suggest, to us, that water tariffs will soar over the next two decades. We find plenty of room for higher rates, despite customers' impressions that water should be free.

However, water bills make up a relatively small percentage of household budgets compared to other utility bills. According to the most recent report by the Bureau of Labor Statistics, water utility bills comprised less than 1% of the U.S. household budget.

Acquisitions. As the nation's largest investor-owned water utility, we find that AWK is more likely to rely on acquisitions for growth. In the last decade alone, the company acquired more than 100 water and wastewater systems for approximately $200 million. The vast majority were small systems serving fewer than 10,000 customers and operating within the company's existing service areas. Since American Water has been a serial acquirer over the last decade, our model reflects that "tuck-in" acquisitions will provide less than a percentage point of revenue growth in 2009 and 2010.

The water utility industry is largely fragmented, and we argue consolidation will remain part of a long-term trend that favors AWK, particularly since local municipalities own and operate 85% of the nation's water systems and many of those that are cash-strapped, much like Trenton, may reach out to investor-owned water utilities that can afford to upgrade systems and provide a quick fix to budgetary gaps. Other territories faced with significant budgetary deficits include California and New York. Industry fragmentation otherwise will allow American Water to extend its evolution over the last decade from a little-known Pennsylvania company to the largest publicly traded U.S. water utility.

AWK will continue to expand across the U.S., in our view, targeting safe, reliable water supplies, first-rate regulatory environments and high population growth areas. We can assume further acquisitions of small water and wastewater systems, particularly in Pennsylvania and New Jersey.

In addition, we would target California, backed by a supportive regulatory environment and strong population growth (more than 13% between 2000 and 2008 versus the national average of 8%). Through the acquisition of small water and wastewater systems, AWK will save on costs relative to a municipality's operating expense, while lowering SG&A and increasing the company's earnings, in our opinion.

Risks

The biggest risk to AWK's earnings growth is **regulatory lag**, which is the time between when costs are incurred and when costs are included in new rates. We find that, in an inflationary environment, water rates often lag the accurate cost of providing service. For example, as a result of a sharp increase in chemical costs in 2008, AWK filed for rate increases, but current regulatory process can take up to two to three years to recover costs. Although recent rate increases are expected to provide some progress in the recovery of rising operating costs, we still anticipate some time lag for AWK in 2010.

Eminent Domain. Distressed over service interruption and spiking utility rates, the city of Felton, CA forced a buyout of a water system owned by AWK through the use of eminent domain. In California, eminent domain proceedings involve a "right to take" hearing, which determines whether a purchase serves the public interest, and a "valuation" hearing, which determines the fair market value of the property. Following a court decision that established the takeover was in the best interest of the public, Felton, CA paid American Water $13.4 million ($10.5 million cash, $2.9 million assumed liabilities) for the assets. Residents in Scottsdale, AZ are also exploring this option as AWK seeks to raise water rates by 22%.

In 1Q:09 AWK logged a $450 million **goodwill impairment charge** related to the acquisition of American Water by RWE in 2003. At the end of 1Q:09 AWK still had a $1.25 billion (or 10% of assets) of goodwill on its books. The company is required to test for impairment at the end of each year. We suggest that goodwill could be further impaired in the future but note that an impairment charge will not hurt cash flows. Still, we see risks in the potential destruction of book value and an increase in the company's leverage ratios.

Financing. We forecast that American Water over the next two years will need to raise in excess of $1 billion to meet cap-ex requirements and fund acquisitions, and warn that further economic and credit market weakness puts such funding at risk. With AWK already having raised nearly $300 million since January 2009, we remain optimistic about the company's access to financing. In the event American Water cannot tap outside funds, however, we suggest management will have to reduce capital spending plans, which could hamper projected earnings growth.

Recent Results

American Water's non-cash impairment charge related to the acquisition of AWK by RWE in 2003 totaled $2.76 per share In 1Q:09. Despite the write-down, we view the quarterly performance favorably, especially in light of the difficult operating conditions. Excluding the charge, EPS surged to $0.18, versus $0.05 in 1Q:08.

Revenue of $550.2 million grew 8.6% year over year, fueled by $43.5 million of rate increases that more than offset lower consumption. Operating margin improved 510 basis points to 20.8%, even as AWK's operations and maintenance costs grew due to higher chemicals, pension and postretirement, and bad-debt expense. These costs were largely offset by lower contract service expense.

Earnings Outlook

Our 2009 forecast of revenue growth of 8% to $2.52 billion includes approved rate increases of $150 million for several of the company's core service areas. We anticipate operating margin expansion of 190 basis points to 26.0% on top of significant rate relief. Excluding impairment charges and one-time asset sales, we forecast EPS will expand 21% to $1.35 in 2009, factoring dilution from a $250 million follow-on offering in June 2009. Our view compares to First Call consensus for $2.51 billion in revenue and EPS of $1.32.

For 2010 we project 7% revenue growth to $2.70 billion and $150 million in rate increases, 50% of the amount expected to be requested given the more difficult operating environment. We forecast operating margin expansion of 160 basis points to 27.6% on top of more rate relief and cost reductions. We expect EPS to rise 9% to $1.48, which also factors in dilution from an anticipated $250 million follow-on offering. First Call revenue and EPS estimates are $2.68 billion and $1.45.

Financial Condition and Cash Flows

At first glance, AWK may appear to have significant financial risk, as the company holds little cash on its books and has a substantial amount of debt; however, we contend this is normal for a regulated water utility. At the end of 1Q:09, AWK had $8.5 million in cash and equivalents. Total debt approached $5.3 billion, or 60% of total capital, versus the company's 55% target ratio. Short-term debt increased 35% from 4Q:08 and constituted about 12% of the total as AWK responded to the frozen credit markets. Under its $840 million credit facility the water utility had $195 million available at the end of 1Q:09 with additional funds expected to be available as the company refinances short-term borrowings with long-term debt. Since the beginning of 2009, AWK has raised $350 million via separate issues at a weighted average cost of 6.85%.

The company's primary source of cash is the sale of water to customers, weighted toward the second and third calendar quarters. Given the vital need for water, we expect AWK's cash flows from operations to remain reliable. American Water netted $552.2 million of cash ($3.45 per share) from operations for 2008, up 17% primarily due to rate increases. For 2009 and 2010 we forecast respective operating cash of $552.2 million ($3.30 per share) and $575.3 million ($3.14 per share).

Generally, water utilities exhaust internally generated funds on capital improvements, forcing them to rely on secondary sources of cash. Our forecast through 2010 assumes $800 million annual cap-ex and $100 million of tuck-in acquisitions, mainly in 2009. Considering AWK's robust cap-ex, acquisition history and plans to reduce short-term borrowings, we project the company will need to raise more than $1 billion through the debt and equity markets. In 2009, our model assumes AWK issues $350 million in long-term debt and $250 million of common stock. For 2010, we anticipate the company will raise $500 million through long-term borrowings and the issuance of common stock.

Dividend Outlook

In 3Q:08 the board of directors approved the company's first quarterly dividend payment ($0.20) since the 2008 IPO. The annual dividend yields above 4% and underscores the company's well-being, in our view, as we model the payout will remain between 50% and 60% of adjusted net income. In 2H:09 we project American Water will raise the quarterly dividend to $0.21. We consider the balance sheet strong enough to support investments and dividend payments, even in an economic slowdown.

Valuation

AWK shares are down 8% in 2009, versus an 8% rise in the S&P MidCap 400 Index. Defensive sectors, including water utilities, did not participate in the recent market rally as investors moved funds into financial and technology stocks, betting on an economic recovery. But despite the sector weakness, the share underperformance is primarily due to RWE's presumed spin-off of its 47% holdings in AWK. This scenario poses a huge overhang, in our opinion, in that it discourages investors from taking positions in the stock knowing a large block trade is coming to market.

While we acknowledge the market overhang, we find AWK's valuation too attractive to ignore. At the current price, the stock trades at 13x our 2010 EPS estimate and 0.8x book value of $22.90 per share (includes goodwill), both big discounts to the peer group averages (See Exhibit 1: Peer P/E Valuation). Given a lack of historical trading information, it is impossible to draw a useful trailing comparison, but historically, water utilities have typically traded at 15x and 35x forward EPS and 1.5x and 2.5x book value. We find that these high valuations are supported by highly regulated businesses, with consistent revenue and earnings growth, and decent dividend yields as well.

We calculate shares currently trade at a 45% discount to the peer average P/E multiple on 2010 EPS. Over the next two years, we expect that valuation gap to narrow as the uncertainty related to the RWE overhang is lifted. Applying a 20% discount to our average target multiple for the peer group of 22x on 2010 EPS, our $27 price target is based on 18x our 2010 EPS estimate of $1.48. At the current price quote our target implies 40% upside—and nearly 45% total return, factoring in the above-peer-average dividend yield of 4.2%. As such, we initiate coverage of American Water Works, Inc. with a BUY rating.

Exhibit 1. Peer P/E Valuation

Company	Ticker	Rating	7/23/09 Close Price	Market Cap. ($ Mil)	52-Week Range	Shares Out.	EPS Estimates 2009E	EPS Estimates 2010E	Price/ Earnings 2009E	Price/ Earnings 2010E	Div. Yield	P/ BV	Debt/Cap
Aqua America	WTR	BUY	$17.82	$2,413	22-12	135.4	$0.84	$0.92	21.2	19.4	3.0%	2.3	56%
California Water	CWT	BUY	$36.78	$763	48-28	20.7	$2.06	$2.13	17.9	17.3	3.2%	1.9	46%
American States Water	AWR	BUY	$36.24	$628	42-27	17.3	$1.65	$1.87	22.0	19.4	2.8%	2.0	54%
SJW Corp.	SJW	BUY	$23.09	$427	32-20	18.5	$0.99	$1.25	23.3	18.5	2.9%	1.7	49%
Middlesex Water	MSEX	NC	$15.13	$203	19-12	13.4	$0.76	$0.78	19.9	19.4	4.7%	1.5	54%
AVERAGE									**20.9**	**18.8**	**3.3%**	**1.9**	**52%**
American Water Works	AWK	BUY	$19.26	$3,082	24-16	160.0	$1.35	$1.48	14.3	13.0	4.2%	0.8	59%

Source: First Call, Sidoti & Company, LLC estimates

AMERICAN WATER WORKS COMPANY

Table 1: American Water Works Company, Inc., Income Statement
(000's, except where noted)

	2007	Mar	Jun	Sep	Dec	2008	Mar A	Jun	Sep	Dec	2009 E	Mar	Jun	Sep	Dec	2010 E
Revenue	**$2,214,215**	**$506,815**	**$589,369**	**$672,193**	**$568,551**	**$2,336,928**	**$550,170**	**$623,399**	**$719,306**	**$631,007**	**$2,523,882**	**$586,020**	**$664,336**	**$783,161**	**$667,037**	**$2,700,554**
Operation and maintenance	1,246,479	311,261	330,575	342,226	319,735	1,303,797	314,402	343,493	352,460	353,364	1,363,719	331,101	359,406	379,833	370,872	1,441,213
Depreciation and Amortization	267,335	63,916	67,307	68,376	71,662	271,261	68,843	71,067	74,089	78,876	292,875	70,322	73,077	78,316	80,044	301,760
General taxes	183,253	52,066	49,629	49,380	48,065	199,140	52,497	49,872	53,948	53,636	209,952	52,742	49,825	54,821	54,030	211,418
Operating Income	**517,148**	**79,572**	**141,858**	**212,211**	**129,089**	**562,730**	**114,428**	**158,967**	**238,810**	**145,132**	**657,336**	**131,855**	**182,028**	**270,190**	**162,090**	**746,163**
EBITDA	**784,483**	**143,488**	**209,165**	**280,587**	**200,751**	**833,991**	**183,271**	**230,034**	**312,898**	**224,007**	**950,211**	**202,177**	**255,105**	**348,506**	**242,134**	**1,047,923**
Interest expense	283,165	69,968	70,066	72,684	72,437	285,155	71,979	74,611	74,611	74,611	295,812	78,361	78,361	78,361	78,361	313,444
Allowance for funds used during construction	(7,759)	(2,541)	(3,387)	(4,442)	(4,127)	(14,497)	(3,343)	(3,740)	(4,316)	(3,786)	(15,185)	(3,516)	(3,986)	(4,699)	(4,002)	(16,203)
Allowance for borrowed funds used during construction	(3,449)	(1,368)	(1,725)	(2,970)	(2,108)	(8,171)	(1,872)	(1,870)	(2,158)	(1,893)	(7,793)	(1,172)	(1,329)	(1,566)	(1,334)	(5,401)
Amortization of debt expense	4,867	1,318	1,441	1,601	1,535	5,895	1,488	1,558	1,798	1,578	6,422	1,172	1,329	1,566	1,334	5,401
Impairment charge	509,345	750,000	-	-	-	750,000	450,000	-	-	-	450,000	-	-	-	-	-
Gain (loss) on sale of assets	(7,326)	(70)	(800)	457	39	(374)	(202)	-	-	-	(202)	-	-	-	-	-
Preferred dividends of subsidiaries	223	56	56	55	56	223	-	-	-	-	-	-	-	-	-	-
Other	(6,401)	(1,205)	543	(881)	(3,365)	(4,908)	(1,114)	(623)	(719)	(631)	(3,088)	(586)	(664)	(783)	(667)	(2,701)
Pretax Income	**(255,517)**	**(736,586)**	**75,664**	**145,707**	**64,622**	**(450,593)**	**(402,508)**	**89,031**	**169,594**	**75,253**	**(68,630)**	**57,596**	**108,318**	**197,312**	**88,398**	**451,623**
Income taxes	86,756	(4,102)	30,166	57,549	28,215	111,828	10,571	35,613	67,837	30,101	144,122	23,038	43,327	78,925	35,359	180,649
Income from continuing operations	(342,273)	(732,484)	45,498	88,158	36,407	(562,421)	(413,079)	53,419	101,756	45,152	(212,752)	34,557	64,991	118,387	53,039	270,974
Discontinued operations	(807)	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Net Income	**(343,080)**	**(732,484)**	**45,498**	**88,158**	**36,407**	**(562,421)**	**(413,079)**	**53,419**	**101,756**	**45,152**	**(212,752)**	**34,557**	**64,991**	**118,387**	**53,039**	**270,974**
Diluted EPS	**($2.14)**	**($4.58)**	**$0.28**	**$0.55**	**$0.23**	**($3.52)**	**($2.58)**	**$0.33**	**$0.58**	**$0.26**	**($1.41)**	**$0.20**	**$0.37**	**$0.63**	**$0.28**	**$1.48**
Diluted Average Shares Outstanding (Mil.)	160,000	160,000	160,000	160,000	160,045	159,967	160,011	160,000	174,500	174,500	167,253	174,500	174,500	187,000	187,000	183,000
Dividends / share	N/A	N/A	0.200	0.200	0.200	0.600	0.200	0.200	0.200	0.200	0.800	0.210	0.210	0.210	0.210	0.840
Payout ratio	N/A	N/A	71.6%	36.7%	82.9%	53.5%	112.8%	59.9%	34.3%	77.3%	59.1%	106.0%	56.4%	33.2%	74.0%	56.7%
Adjusted EPS																
Income before taxes	(255,517)	(736,586)	75,664	145,707	64,622	(450,593)	(402,508)	89,031	169,594	75,253	(68,630)	57,596	108,318	197,312	88,398	451,623
Adjustments:																
Gain on sale of assets	(7,326)	(70)	(800)	457	39	(374)	(202)	-	-	-	(202)	-	-	-	-	-
Impairment charges	509,345	750,000	-	-	-	750,000	450,000	-	-	-	450,000	-	-	-	-	-
Adjusted income before taxes	246,502	13,344	74,864	146,164	64,661	299,033	47,290	89,031	169,594	75,253	381,168	57,596	108,318	197,312	88,398	451,623
Income taxes	95,150	5,378	30,170	58,904	26,058	119,613	18,916	35,613	67,837	30,101	152,467	23,038	43,327	78,925	35,359	180,649
Adjusted Net Income	151,352	7,966	44,694	87,260	38,603	179,420	28,374	53,419	101,756	45,152	228,701	34,557	64,991	118,387	53,039	270,974
Adjusted Diluted EPS	**$0.95**	**$0.05**	**$0.28**	**$0.55**	**$0.24**	**$1.12**	**$0.18**	**$0.33**	**$0.58**	**$0.26**	**$1.35**	**$0.20**	**$0.37**	**$0.63**	**$0.28**	**$1.48**
Profitability Analysis																
EBITDA Margin	35.4%	28.3%	35.5%	41.7%	35.3%	35.7%	33.3%	36.9%	43.5%	35.5%	37.6%	34.5%	38.4%	44.5%	36.3%	38.8%
O&M Expense As % Revenue	56.3%	61.4%	56.1%	50.9%	56.2%	55.8%	57.1%	55.1%	49.0%	56.0%	54.0%	56.5%	54.1%	48.5%	55.6%	53.4%
D&A Expense As % Revenue	12.1%	12.6%	11.4%	10.2%	12.6%	11.6%	12.5%	11.4%	10.3%	12.5%	11.6%	12.0%	11.0%	10.0%	12.0%	11.2%
Operating Margin	23.4%	15.7%	24.1%	31.6%	22.7%	24.1%	20.8%	25.5%	33.2%	23.0%	26.0%	22.5%	27.4%	34.5%	24.3%	27.6%
Pretax Margin	11.1%	2.6%	12.7%	21.7%	11.4%	12.8%	8.6%	14.3%	23.6%	11.9%	15.1%	9.8%	16.3%	25.2%	13.3%	16.7%
Net Margin	6.8%	1.6%	7.6%	13.0%	6.8%	7.7%	5.2%	8.6%	14.1%	7.2%	9.1%	5.9%	9.8%	15.1%	8.0%	10.0%
Year-Over-Year % Change																
Revenue	5.8%	8.2%	5.5%	6.2%	2.7%	5.5%	8.6%	5.8%	7.0%	11.0%	8.0%	6.5%	6.6%	8.9%	5.7%	7.0%
Operating Income	9.0%	8.4%	-2.3%	12.9%	16.9%	8.8%	43.8%	12.1%	12.5%	12.4%	16.8%	-76.6%	14.5%	13.1%	11.7%	13.5%
EBITDA	-17.9%	3.9%	1.0%	-43.9%	-54.5%	6.3%	27.7%	10.0%	11.5%	11.6%	13.9%	10.3%	10.9%	11.4%	8.1%	10.3%
Net Income	123.6%	NM	-2.0%	19.6%	48.4%	18.5%	NM	18.9%	16.0%	16.4%	27.5%	21.8%	21.7%	16.3%	17.5%	18.5%
Diluted EPS	123.6%	NM	-4.8%	16.3%	44.2%	18.6%	NM	19.5%	6.9%	7.3%	20.6%	11.7%	11.6%	8.6%	9.6%	9.4%

Source: Company reports, Sidoti & Company, LLC estimates.

AMERICAN WATER WORKS COMPANY

Table 2: American Water Works Company, Inc., Statement of Cash Flows
(000's, except where noted)

	Mar	Jun	Sep	Dec	2007	Mar	Jun	Sep	Dec	2008	Mar A	2009 E	2010 E
Operating Activities													
Net income	2,685	49,178	(160,117)	(234,572)	(342,826)	(732,484)	45,498	88,158	36,407	(562,421)	(413,079)	(212,752)	270,974
Gain (loss) on sale of businesses	-	-	-	-	-	-	-	-					
Depreciation and amortization	64,627	68,137	69,699	64,872	267,335	63,916	67,307	68,376	71,662	271,261	68,843	292,875	301,760
Impairment charges	-	-	243,345	266,000	509,345	750,000	-	-	-	750,000	450,000	450,000	-
Amortization of removal costs net of salvage	9,018	6,793	6,765	15,866	38,442	10,553	10,661	10,583	9,718	41,515	10,009	-	-
Provision for deferred taxes	4,736	11,085	(17,470)	43,567	41,918	5,474	16,486	54,782	18,901	95,643	31,627	-	-
Amortization of deferred investment tax credits	(406)	(407)	(448)	(249)	(1,510)	(404)	(404)	(405)	(125)	(1,338)	(401)	-	-
Provision for losses on utility accounts receivable	2,657	3,897	4,519	6,480	17,553	836	5,532	6,982	3,917	17,267	5,298	-	-
Allowance for other funds used during construction	(1,658)	(1,511)	(2,028)	(2,562)	(7,759)	(2,541)	(3,387)	(4,442)	(4,127)	(14,497)	(3,343)	-	-
Employee benefit expenses greater (less) than funding	-	-	-	-	-	-	-	-	-	-	-	-	-
Gain (loss) on sale of assets	106	(6,219)	(708)	(505)	(7,326)	(70)	(800)	457	39	(374)	(202)	-	-
Gain on early extinguishment of debt	(7,064)	7,064	-	(13,113)	(13,113)	-	-	-	-	-	-	-	-
Amortization of deferred charges	-	-	-	-	-	-	-	-	-	-	-	-	-
Other, net	(15,579)	(1,654)	(18,065)	71,426	36,128	(31,033)	(27,808)	12,642	100,842	54,643	23,234	-	-
Changes in assets and liabilities	(4,911)	(54,393)	68,240	7,834	(64,475)	21,144	(57,201)	14,505	(77,978)	(99,530)	(29,487)	22,087	2,520
Net Cash From Operations	**54,211**	**81,970**	**193,732**	**225,044**	**473,712**	**85,391**	**55,884**	**251,638**	**159,256**	**552,169**	**142,499**	**552,210**	**575,254**
Investing Activities													
Construction expenditures	(166,115)	(138,442)	(202,680)	(251,332)	(758,569)	(188,437)	(237,523)	(288,599)	(294,247)	(1,008,806)	(196,178)	(800,000)	(800,000)
Allowance for other funds used in construction	-	-		7,759	7,759	-	-	-	-	-	-	-	-
Acquisitions	-	(217)	(727)	(14,933)	(15,877)	-	(248)	(7,773)	(4,491)	(12,512)	-	(80,000)	(20,000)
Proceeds from the sale of assets and securities	1,145	14,055	388	758	16,346	82	716	11,361	445	12,604	204	-	-
Proceeds from sale of discontinued operations	-	9,660	-	-	9,660	-	-	-	-	-	-	-	-
Removal costs from property, plant, equipment retirements	(1,880)	1,392	(4,538)	(4,826)	(9,852)	(1,714)	(3,143)	(12,433)	(7,503)	(24,793)	(5,031)	-	-
Receivables from affiliate	-	-	-	-	-	-	-	-	-	-	-	-	-
Restricted funds	1,633	(672)	4,048	820	5,829	2,364	289	1,484	(1,680)	2,457	(26)	-	-
Investment in equity investee	-	-	-	(1,874)	(1,874)	-	-	-	(2,617)	(2,617)	-	-	-
Other	-	-	-	-	-	-	-	-	-	-	(1,250)	-	-
Net Cash From (Used In) Investing	**(165,217)**	**(114,224)**	**(203,509)**	**(263,628)**	**(746,578)**	**(187,705)**	**(239,909)**	**(295,960)**	**(310,093)**	**(1,033,667)**	**(202,281)**	**(880,000)**	**(820,000)**
Financing Activities													
Proceeds from long-term debt	617,253	197	1,750,112	1,501,547	3,869,109	-	201,546	283	78,112	279,941	75,000	350,000	250,000
Repayment of long-term debt	(266,553)	(171,330)	(54,308)	(1,858,534)	(2,350,725)	(35,915)	(155,604)	(8,136)	(41,845)	(241,500)	(150,451)	-	-
Net borrowings (repayments) under short-term debt agreements	(555,578)	(23,000)	4,833	32,122	(541,623)	166,740	(129,967)	87,805	134,106	258,684	189,940	(150,000)	(125,000)
Proceeds from employee stock plan issuances	-	-	-	-	-	-	-	-	-	836	526	-	-
Advances and contributions for construction, net of refunds	13,097	2,645	9,903	10,201	35,846	(13,673)	15,842	1,035	(126)	3,078	2,608	10,000	25,000
Change in cash in overdraft account	-	-	-	42,198	42,198	(19,117)	(13,869)	(4,038)	36,836	(188)	(23,858)	-	-
Proceeds from issuing common stock	-	-	-	-	-	-	-	-	-	-	-	250,000	250,000
Capital contributions	550,000	1,092	150,000	266,000	967,092	-	264,117	-	(19,117)	245,000	-	-	-
Debt issuance costs	(3,054)	358	(815)	(11,405)	(14,916)	-	(1,314)	277	(2,971)	(4,008)	(2,937)	-	-
Redemption from preferred stocks	(150)	(26)	(1,750,134)	(78)	(1,750,388)	-	(14)	(137)	(78)	(229)	-	-	-
Dividends paid	-	-	-	-	-	-	-	(31,992)	(32,063)	(64,055)	(32,072)	(133,802)	(153,720)
Net Cash From (Used In) Financing	**355,015**	**(190,064)**	**109,591**	**(17,949)**	**256,593**	**98,035**	**180,737**	**45,097**	**152,854**	**477,559**	**58,756**	**326,198**	**246,280**
Increase (Decrease) In Cash	244,009	21,691	121,505	64,972	(16,273)	(4,279)	(7,567)	(6,792)	(4,775)	(3,939)	(1,026)	(1,593)	1,534
Beginning Cash Balance	29,754	29,754	29,754	29,754	29,754	13,481	13,481	13,481	13,481	13,481	9,542	9,542	7,949
Ending Cash Balance	**273,763**	**51,445**	**151,259**	**94,726**	**13,481**	**9,202**	**5,914**	**6,689**	**8,706**	**9,542**	**8,516**	**7,949**	**9,483**
OCF / Share	$0.34	$0.51	$1.21	$1.41	$2.96	$0.53	$0.35	$1.57	$1.00	$3.45	$0.89	$3.30	$3.14
FCF	(111,904)	(56,472)	(8,948)	(26,288)	(284,857)	(103,046)	(181,639)	(36,961)	(134,991)	(456,637)	(53,679)	(247,790)	(224,746)
FCF / Share	($0.70)	($0.35)	($0.06)	($0.16)	($1.78)	($0.64)	($1.14)	($0.23)	($0.84)	($2.85)	($0.34)	($1.48)	($1.23)

Source: Company reports, Sidoti & Company, LLC estimates.

AMERICAN WATER WORKS COMPANY

Table 3: American Water Works Company, Inc., Balance Sheet
(000's, except where noted)

	2007	Mar	Jun	Sep	2008	Mar A	2009 E	2010 E
Assets								
Cash and cash equivalents	$13,481	$9,202	$5,914	$6,689	$9,542	$8,516	$7,949	$9,483
Restricted funds	3,258	2,149	1,874	902	454	1,446	1,446	1,446
Utility customer accounts receivable	147,640	136,261	158,886	172,421	149,198	142,386	148,909	156,632
Allowance for uncollectible accounts	(20,923)	(17,576)	(18,144)	(19,669)	(18,644)	(18,766)	(20,191)	(21,604)
Unbilled utility revenue	134,326	122,431	141,043	150,912	134,204	130,035	133,766	135,028
Non-regulated trade and other receivables, net	66,540	62,812	62,528	75,222	68,877	67,603	68,145	70,214
Materials and supplies	23,111	23,111	23,908	32,530	28,948	32,811	35,334	37,808
Assets in discontinued operations	27,458	28,961	31,679	32,949	-	-	-	-
Other	35,463	47,523	50,984	45,268	45,096	56,557	46,739	51,311
Total Current Assets	**430,354**	**414,874**	**458,672**	**497,224**	**417,675**	**420,588**	**422,097**	**440,317**
Utility plant, net	9,199,909	9,296,315	9,497,176	9,742,671	9,991,783	10,102,399	10,874,395	11,598,823
Nonutility plant, net	118,052	119,740	124,415	128,920	132,145	134,918	138,814	148,530
Regulatory assets	628,039	626,093	631,497	628,050	919,654	938,397	946,456	958,697
Restricted funds	10,252	8,997	8,983	8,471	10,599	9,633	12,619	13,503
Goodwill	2,456,952	1,706,952	1,706,675	1,704,310	1,699,517	1,249,839	1,249,839	1,249,839
Other	90,514	95,033	99,264	71,086	60,445	51,470	75,716	75,616
Total Assets	**12,934,072**	**12,268,004**	**12,526,682**	**12,780,732**	**13,231,818**	**12,907,244**	**13,719,937**	**14,485,325**
Liabilities								
Short-term debt	220,514	368,137	243,418	327,185	479,010	645,092	495,092	365,092
Current portion of long-term debt	96,455	90,188	80,534	95,836	175,822	62,499	126,194	135,028
Accounts payable	168,886	119,209	137,303	160,518	149,795	115,066	176,672	189,039
Taxes accrued, including federal income	56,002	56,536	58,174	65,928	52,488	70,630	63,097	67,514
Interest accrued	50,867	85,248	53,720	91,271	53,629	90,905	73,193	75,616
Liabilities of discontinued operations	-	-	-	-	-	-	-	-
Other	181,765	152,156	168,090	196,752	194,016	185,016	222,102	237,649
Total Current Liabilities	**774,489**	**871,474**	**741,239**	**937,490**	**1,104,760**	**1,169,208**	**1,156,349**	**1,069,937**
Long-term debt	4,674,837	4,642,315	4,696,260	4,669,502	4,624,063	4,659,806	4,974,063	5,224,063
Redeemable preferred stock at redemption	24,296	24,296	24,333	24,217	24,150	24,153	24,153	24,153
Advances for construction	655,375	652,536	656,914	629,058	622,227	611,618	630,971	621,127
Contributions in aid of construction	818,387	833763	866,480	878,298	911,415	922,652	933,836	985,702
Deferred income taxes	638,918	644,343	658,481	720,569	705,587	719,872	731,926	756,155
Deferred investment tax credits	35,361	34,957	34,553	34,148	34,023	33,622	35,334	37,808
Regulatory liabilities	192,650	202,019	209,963	197,910	307,324	313,342	353,344	378,078
Accrued pension expense	290,722	275,536	260,391	253,244	502,062	501,983	479,538	459,094
Accrued postretirement benefit expense	158,552	156,178	153,975	151,899	241,193	239,294	239,769	243,050
Other	123,871	116,596	116,631	117,483	48,456	46,796	45,430	49,960
Total Liabilities	**8,387,458**	**8,454,013**	**8,419,220**	**8,613,818**	**9,125,260**	**9,242,346**	**9,604,712**	**9,849,127**
Shareholder's Equity								
Common shareholders' equity	4,542,046	3,809,423	4,102,902	4,162,357	4,102,001	3,660,341	4,110,668	4,631,642
Preferred stock	4,568	4,568	4,560	4,557	4,557	4,557	4,557	4,557
Total Shareholder's Equity	**4,546,614**	**3,813,991**	**4,107,462**	**4,165,214**	**4,106,558**	**3,664,898**	**4,115,225**	**4,636,199**
Total Liabilities and Shareholders' Equity	**12,934,072**	**12,268,004**	**12,526,682**	**12,779,032**	**13,231,818**	**12,907,244**	**13,719,937**	**14,485,326**
Balance Sheet Analysis								
Current Ratio (excludes ST Debt)	0.777	0.824	0.921	0.815	0.667	0.802	0.638	0.625
Cash / Share	$0.084	$0.058	$0.037	$0.042	$0.060	$0.053	$0.048	$0.052
BV / Share	28.416	23.837	25.672	26.033	25.666	22.899	24.605	25.334
Tangible BV / Share	13.060	13.169	15.005	15.381	15.044	15.090	17.132	18.505
LT Debt / Capital	51%	55%	54%	53%	54%	56%	55%	54%
Debt / Capital	52%	57%	55%	55%	56%	59%	58%	55%
ROE (ttm)	3.6%	N/A	N/A	N/A	4.1%	5.3%	5.6%	6.2%
ROA (ttm)	1.2%	N/A	N/A	N/A	1.4%	1.6%	1.7%	1.9%

Source: Company reports, Sidoti & Company, LLC estimates.

IMPORTANT DISCLOSURES

The Sidoti & Company, LLC Equity Research rating system consists of BUY and NEUTRAL recommendations. BUY suggests capital appreciation of at least 25% from initiation of coverage over the next 12 months, while NEUTRAL denotes that a stock is not likely to provide similar gains over a 12-month period. As of 07/24/09, Sidoti & Company, LLC provides research on 531 companies, of which 325 (61%) are rated BUY and 204 (39%) are rated NEUTRAL. Of the BUYS, Sidoti & Company, LLC has received investment banking income from 8 companies (2.46%). Of the NEUTRALS, 142 trade above our price targets. Any estimates or forecasts may not be met. Information contained herein is based on sources we believe to be reliable but we do not guarantee their accuracy. Prices and opinions concerning the composition of market sectors included in this report reflect the judgments as of this date and are subject to change without notice. This report is for information purposes only and is not intended as an offer to sell or a solicitation to buy securities. **Reprints of Sidoti & Company, LLC reports are prohibited without permission.** The research analyst certifies that this report accurately reflects his/her personal views about the subject securities and issuers and that none of the research analyst's compensation was, is or will be directly or indirectly related to the analyst's specific recommendations or views contained in this research report. Occasionally, Sidoti & Company, LLC may receive a fee, directly or indirectly, at the time of an underwriting for an individual company already under research coverage, for which the covering analyst will not be compensated. Sidoti & Company, LLC does NOT own securities of the issues described herein. Sidoti & Company, LLC policy does not allow any analyst to own shares in any company he/she covers. No employee or household member thereof, serves as an officer or director of a covered company. Sidoti & Company, LLC does not make a market in any securities. Additional information is available upon request.

Smith,Moore&Co.
Established 1913

Equity Analysis
SM Research & Perspective
Water Utilities

American Water Works (AWK-NYSE: $21.62 - Outperform)

May 18, 2008

	2006A	2007A	2008E	2009E	2010E
EPS*	$0.41	$0.99	$1.15	$1.25	$1.40
P/E		21.8x	18.8x	17.3x	15.4x
ROE*	5.2%	7.5%	8.7%	9.2%	10.0%

(* Excludes items Smith, Moore believes to be non-recurring)

American Water Works; Nation's Largest Water Utility Returns to the Market

- We have initiated coverage of American Water Works with an Outperform rating and a $25 price objective. American Water Works (AWK) is the largest investor-owned water and wastewater utility company in the United States.

- We regard AWK as a high quality conservative utility with unique growth opportunities. AWK shares offer investors a competitive 3.7% dividend yield, the likelihood of consistent annual dividend increases and, more importantly, earnings growth through rate base additions and consolidation/privatization opportunities.

- AWK will materially benefit from public and regulatory support of significant investment in water and wastewater infrastructure. In addition, the company's national presence, diverse geographic footprint, technical expertise, operating reputation and financial resources favorably position it to consolidate and privatize the extremely fragmented and municipally-dominated water and wastewater industry.

- We expect the rate relief to lead to a period of accelerated EPS growth over the 2007-2010 period. With roughly 90% of earnings generated from the low-risk regulated water utility business, we assume reasonable regulatory treatment results in EPS power of $1.40 by 2010, which results in a 10% return on common equity. Our 2008 and 2009 EPS estimates are $1.15 and $1.25, respectively.

- AWK received rate increases totaling $158.9 million annually in 2007, which compares to $41 million in 2006 and $35 million in 2005. In the first three months of 2008, AWK subsidiaries implemented $26.0 million in annual revenue increases and filed rate requests in the states of New Jersey, California, Virginia, Tennessee and Missouri, requesting approximately $231.1 million in increased annualized revenues.

Fundamental Data	
Est. 3 year CAGR	12.2%
Book Value Per Share (3/08)	$13.14
Common Equity Total Capital	28%
S&P Debt Rating	A-
Current Annual Dividend	$0.80
Current Yield	3.7%
Payout Ratio	70%

Market Data	
Shares Outstanding (millions)	160.0
Market Capitalization (millions)	$3,459
Avg. daily share volume (000)	NMF
52-Week Range	$20-22
Institutional Ownership	NA%
Short Interest	NA%

Valuation Data	
Price/Book	165%
Relative/PE	120%

Contacts

Analyst
Timothy M. Winter, CFA
314-446-1617
twinter@smithmoore.com

Sales / Trading
George F. Grimes
314-446-1663
ggrimes@smithmoore.com

Disclosure / Certification found in Page 19

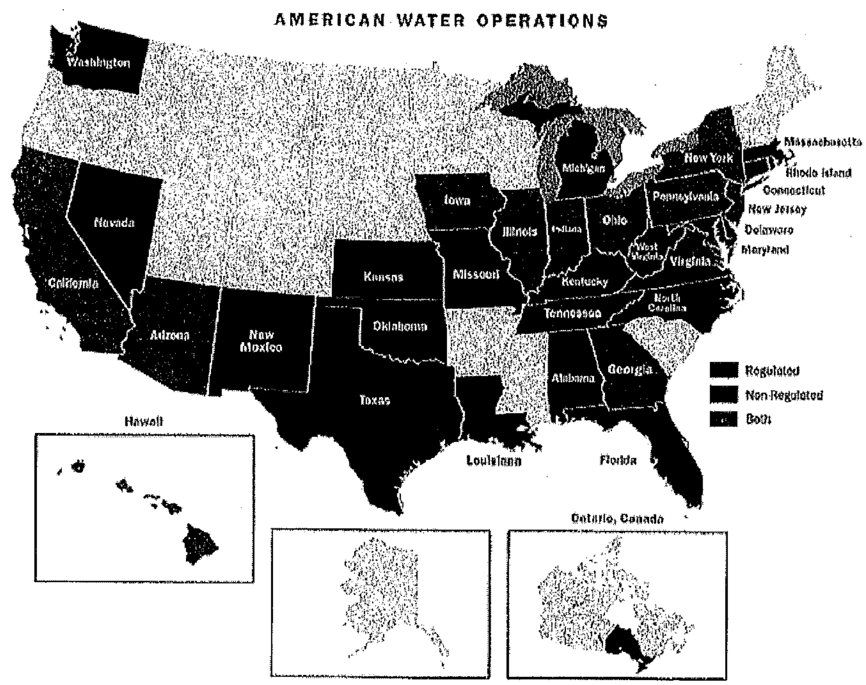
Investment Summary

We have initiated coverage of American Water Works with an Outperform rating and a $25 price objective. American Water Works (AWK) is the largest investor-owned water and wastewater utility company in the United States. The company provides water and wastewater services to approximately 15.6 million people in 32 states and Ontario, Canada.

AWK's primary business is the ownership of regulated utilities that provide water and wastewater services to residential, commercial and industrial customers. Its regulated utilities operate in approximately 1,625 communities spread out across 375 individual service areas in 20 states in the United States. AWK is organized as a holding company with subsidiaries in each of the 20 states it serves. Each regulated subsidiary is subject to economic regulation by state Public Utility Commissions (PUCs) in the states in which they operate. In 2007, regulated operations generated $1.988 billion in revenues, or roughly 89% of consolidated revenues.

We have initiated coverage of American Water Works with an Outperform rating and a $25 price objective.

Non-regulated businesses include Contract Operations Group, Applied Water Management Group and Homeowner Services Group. In 2007, non-regulated businesses generated $242.7 million in operating revenue, or roughly 11% of consolidated revenues.



We regard AWK as a high quality conservative utility with unique growth opportunities. AWK shares offer investors a competitive 3.7% dividend yield, the likelihood of consistent annual dividend increases and, more importantly, earnings growth through rate base additions and consolidation/privatization opportunities. AWK is the largest water utility in the United States and will materially benefit from public and regulatory support of significant investment in water and wastewater infrastructure. In addition, the company's national presence, diverse geographic footprint, technical expertise, operating reputation and financial resources favorably position it to consolidate and privatize the extremely fragmented and municipally-dominated water and wastewater industry.

We regard AWK as a high quality conservative utility with unique growth opportunities.

Following an initial public offering of 58 million shares, or 36% of total shares outstanding, the storied water company has reinstated a strategic focus on earning returns on its regulated utility business, profitably consolidating the fragmented water and wastewater sector and pursuing opportunities throughout North America.

The company was purchased by the German multi-utility RWE in 2003 and experienced a challenging 5-year period. During this period, AWK's earnings and strategy were hampered by regulatory rate stay-out

AWK is the largest water utility in the United States and will materially benefit from public and regulatory support of significant investment in water and wastewater infrastructure.

provisions and patriotic attitudes from regulators, interveners and smaller private and municipal water utilities. In addition, we believe RWE management lacked a full comprehension of the U.S. water industry dynamics and the savoir-faire necessary to operate in the local politics. As a result, earnings and customer growth suffered.

Over the past eighteen-months, AWK has diligently focused efforts on requesting and implementing rate recognition of investments in its business and earning reasonable returns on equity at its subsidiaries.

The current executive management team is headed by President and CEO Don Correll, with roughly 30-years of experience managing large water utilities, and CFO Ellen Wolf, who was CFO of AWK prior to the RWE acquisition. Over the past eighteen-months, AWK has diligently focused efforts on requesting and implementing rate recognition of investments in its business and earning reasonable returns on equity at its subsidiaries. The company received rate increases totaling $158.9 million annually in 2007, which compares to $41 million in 2006 and $35 million in 2005. In the first three months of 2008, AWK subsidiaries implemented $26.0 million in annual revenue increases and filed rate requests in the states of New Jersey, California, Virginia, Tennessee and Missouri, requesting approximately $231.1 million in increased annualized revenues. As of March 31, 2008 AWK was awaiting final orders for one general rate case that was filed in 2006, requesting $7.0 million in annual revenues and five general cases that were filed in 2007, requesting $58.2 million in total additional annual revenues.

We expect the rate relief to lead to a period of accelerated EPS growth over the 2007-2010 period. With roughly 90% of earnings generated from the low-risk regulated water utility business, we assume reasonable regulatory treatment results in EPS power of $1.40 by 2010, which results in a 10% return on common equity. Our 2008 and 2009 EPS estimates are $1.15 and $1.25, respectively. Water utility allowed returns on equity have averaged roughly 10-10.5% over the past few years. In addition, management has instilled the growth-through-acquisition culture that marked the "Water Works" of yore and we expect an acceleration of growth opportunities.

AWK Subsidiaries 2007

Subsidiary	Regulated Operating Revenue (millions)	%	Regulated Customers	%
New Jersey	$ 505	25.4	634,957	19.2
Pennsylvania	$ 416	20.9	644,720	19.5
Missouri	$ 180	9.1	465,087	14.0
Illinois	$ 179	9.0	306,740	9.3
Indiana	$ 147	7.4	283,088	8.5
California	$ 124	6.3	171,445	5.2
West Virginia	$ 106	5.3	167,744	5.1
Top Seven States	$ 1,657	83.4	2,673,781	80.7
Other	$ 331	16.6	638,847	19.3
	$ 1,988	100.0	3,312,628	100.0
Source: Company documents				
Non-regulated business	$ 242.70			

We expect the rate relief to lead to a period of accelerated EPS growth over the 2007-2010 period.

The Water Utility Sector

The U.S. water and wastewater sector is characterized by three major features: (1) it is municipally-dominated, (2) extremely fragmented and (3) infrastructure in need of repair or improvement. Government-owned systems make up the vast majority of the United States water and wastewater utility segment, accounting for approximately 84% of all United States community water systems and approximately 98% of all United States community wastewater systems. Nearly every major city in the United States is owned and operated by the local government. Investor-owned water and wastewater systems account for the remainder and are generally economically regulated by the state PUCs in the states in which they operate. The federal government and the states also regulate environmental, health and safety and water quality matters for both investor-owned and government-owned water and wastewater utilities.

The U.S. water and wastewater sector is characterized by three major features: (1) it is municipally-dominated, (2) extremely fragmented and (3) infrastructure in need of repair or improvement.

As of 2005, the Environmental Protection Agency's (EPA) most recent data, there were roughly 53,000 separate community water systems in the United States with roughly 49,000-plus serving population bases of less than 3,300 people. Notably, 80-to 85% of the nation is served by 24,000 municipally-owned and operated systems, including most of the major cities and population bases. There are tens of thousands of private utilities ranging in size from small single utilities, including many owned by developers and families, to large companies, operating hundreds of separate utilities in multiple states. As shown in the charts below, the majority of the approximately 53,000 community water systems are very small, serving a population of 500 or less. As mentioned, American Water Works is the largest and most geographically diverse water utility in the United States.

2005 Water System Inventory				
	Very Small 0-500	Small 501-3,300	Medium 3,300-10,000	Large Over 10,000
Number of Systems	29,666	14,389	4,748	4,034
Population Served	4,926	20,851	27,515	229,053
% of Population	2	7	10	81

\ Safe Drinking Water Information System

The aging water and wastewater infrastructure in the United States is in constant need of modernization and facilities replacement. Increased regulations to improve water quality and the management of wastewater discharges, which began with passage of the Clean Water Act in 1972 and the Safe Drinking Water Act in 1974, have been among the primary drivers. The EPA estimates that approximately $277 billion of capital spending will be necessary between 2003 and 2022 to replace aging infrastructure and to comply with quality standards to ensure quality water systems across the United States. In addition, the EPA estimates that approximately $388 billion of capital spending will be necessary between 2000 and 2019 to replace aging infrastructure and ensure quality wastewater systems across the United States.

Strategy

The American Water Works's strategy includes: (1) prudent investment in regulated water and wastewater infrastructure (2) earning a healthy return on these investments from state PUCs; (3) the acquisition of smaller water/wastewater systems and water/wastewater companies; and (4) pursuit of public/private partnerships, including water/wastewater O&M contracts with municipalities, military bases and industrial customers.

Competitive Advantages

With a presence in 23 states, AWK has established beach-heads in most regions to pursue privatization or acquisition growth prospects.

1) Size. American Water Works is the largest investor-owned water and wastewater utility company in the United States. The company provides water and wastewater services to approximately 15.6 million people in 32 states and Ontario, Canada. Given its size, AWK is able to spread overhead expenses over a large customer base. Since many administrative and support activities can be efficiently centralized to gain economies of scale and sharing of best practices, companies that participate in industry consolidation have the potential to improve operating efficiencies, lower unit costs and improve service. The ability to create economies of scale are evident in the two national customer service centers, with personnel located in Alton, Illinois and Pensacola, Florida that process telephone calls from customers across all service areas. The company's large size and scope allows the ability to undertake small and large opportunities and projects.

2) Geographic diversity and footprint. With a presence in 23 states, AWK has established beach-heads in most regions to pursue privatization or acquisition growth prospects. In addition, the geographic diversity insulates the consolidated company against adverse state regulatory decisions/environments and/or adverse weather conditions.

geographic diversity insulates the consolidated company against adverse state regulatory decisions/environments and/or adverse weather conditions.

3) Resources. With over 7,000 employees, including technical, engineering and managerial professionals at 23 subsidiaries, AWK employs among the more sophisticated and experienced people in the industry and can employ best practices across the company. As an example, AWK established a formal research and development program in 1981 with personnel located at two facilities: the regional center in Voorhees, New Jersey and the research laboratory in Delran, New Jersey. In addition, the quality control and testing laboratory in Belleville, Illinois supports research through sophisticated testing and analysis. Since its inception, AWKs research and development program has evolved to become a leading water-related research program, achieving advancements in the science of drinking water, including sophisticated water testing procedures and desalination technologies.

4) Reputation. As the largest waster utility with a history dating back to 1886, AWK is well-known as the industry leader with an excellent operating track record of quality service. Its reputation materially benefits its strategy of acquiring water systems and partnering with local governments. Examples of the quality reputation include its numerous awards. (Tampa Bay Desalination Plant named Desalination Plant of the Year by Global Water Intelligence and contract with city of Buffalo named 2008 Public/Private Partnership by U.S. Conference of Mayors)

As the largest waster utility with a history dating back to 1886, AWK is well-known as the industry leader with an excellent operating track record of quality service.

These competitive advantages benefit AWK in many ways, including the ability to shape issues on the regulatory and legislative front, ability to receive rate recognition of investments and the ability to participate in water and wastewater infrastructure growth opportunities and projects of various sizes and in various regions.

AWK's relationship with the EPA and its renowned treatment laboratories has provided early insight into emerging regulatory issues and initiatives. As the largest or among the larger regulated water utilities in many of the states in which it operates, AWK subsidiaries proactively work to implement constructive regulatory policies. Given that 90% of its business is regulated, constructive regulation is key to AWK's ability to earn a reasonable return on investment. Examples of constructive regulatory policy shaped or influenced by AWK and its subsidiaries are discussed in detail later in this report.

Given the history, reputation and resources, politicians as well as private water and wastewater owners and managers can transfer ownership or operations with confidence that service will be maintained or improved. States and municipalities can look to AWK to solve regional water and wastewater issues or partner with on large projects. AWK actively participates in the general services segment, which includes engineering and consulting companies and numerous other fee-for-service businesses. These include the building and operating of water and wastewater utility systems, system repair services, lab services, sale of water infrastructure and distribution products (such as pipes) and other specialized services.

These competitive advantages are important as the privatization business is characterized by aggressive competition and market-driven growth and profit margins. In addition, AWK competes with other regulated utilities, as well as strategic and financial buyers, for acquisition opportunities, including tuck-ins.

We believe the water and wastewater industry is ripe for new rounds of consolidation and privatization as the sector is in the early stages of an extended period of restructuring.

Eventual Restructuring

We believe the water and wastewater industry is ripe for new rounds of consolidation and privatization as the sector is in the early stages of an extended period of restructuring. The large number of relatively small water and wastewater utilities results in inefficiencies as smaller utilities often do not have the operating expertise, financial and technological capability or economies of scale to provide services or raise capital as efficiently as larger utilities. Economic logic suggests that these inefficiencies will lead to future consolidation.

We believe the restructuring of the $500 billion sector has the potential for significant value-creation. We contend that a "handful" of publicly-traded water utilities possess strategically positioned assets, outstanding operating track records and reputations, managerial and professional talent and are poised to capitalize on the eventual restructuring of the industry. The larger privately-owned companies often operate more efficiently and benefit from economies of scale, including managerial, professional, technical and technological expertise. The larger utilities have greater access to capital and are more capable of making mandated and other necessary infrastructure upgrades.

With roughly 12 publicly-traded water utilities, including American Water Works, with market capitalizations over $100 million, the current market capitalization of the group is a mere $10 billion.

With roughly 12 publicly-traded water utilities, including American Water Works, with market capitalizations over $100 million, the current market capitalization of the group is a mere $10 billion. However, these publicly-traded utilities are among the larger players in the industry with the capabilities to capitalize on the industry's unique characteristics. The key driver to the industry's restructuring (consolidation and privatization) and the unique growth opportunity for American Water Works is the massive amount of investment required to maintain and upgrade infrastructure. It is driving rate base growth and will lead to the acceleration of consolidation and privatization.

We suggest water utility investors exercise patience. Economic logic reasons that water/wastewater infrastructure restructuring offers significant value-creation opportunity and long-term growth potential, but the process could take decades to play-out. The massive inefficiency of the multi-hundred-billion dollar sector has been largely neglected primarily due to comparatively low residential water utility bills. With minimal impact on the individual consumer's "pocketbook" and an absence of public health emergencies, the water and wastewater business has been "out of sight and out of mind" to most of the general public.

However, we believe a storm is slowly brewing in the form of growing public awareness of the following:

(1) An infrastructure network in dire need of repair, replacement or improvement;
(2) The ability to avoid large rate increases, and
(3) Social responsibility to optimize the world's most valuable resource.

In other industries, similar situations would be readily and immediately capitalized on by private-equity or other financial predators, but there are limited investment vehicles with the technical expertise, financial resources, shareholder discipline and diplomatic savoir-faire to take advantage of the politically-charged, emotionally sensitive and challenging water environment.

We believe AWK is the poised to capitalize on the eventual restructuring of the industry.

We believe AWK is the poised to capitalize on the eventual restructuring of the industry. We believe that the political and public environment is growing ever-more amenable, if not outright eager, toward allowing substantial capital investment in water/wastewater infrastructure and that economic logic suggests that the best way to accomplish "society's" goal is to consolidate and privatize. This long-term process provides the opportunity for "above-average" earnings growth for the foreseeable future. As we will discuss in greater detail, the combination of well below-average risk premiums and long-term growth potential not only justify existing valuation multiples, but could argue for even higher multiples for a few well-managed and strategically-positioned companies.

Water Infrastructure Needs

Type of Investment	Estimate Cost ($ billions)	% of Total
Distribution	183.6	66
Treatment	53.2	19
Storage	24.8	9
Source	12.8	5
Other	2.3	>1
Total	**276.7**	**100**

Source: EPA

Company	Symbol	Market Data: Price	Px. Chg. 2008	Tot. Ret. 2007	Market Cap. (mil.)	Daily Volume	Inst. Holdings	Valuation Data: P/E 2006A	P/E 2007A	P/E 2008E	P/E 2009E	Enterp/ Share	EBITDA/ Share	EV/ EBITDA	Price/ Book
		$	%	%	$	(000)	%	X	X	X	X	$	$	X	X
American States Water	AWR	34.23	(9)	1	589	144	58	23.8	22.1	19.6	18.0	34.23	5.82	5.9	1.96
Aqua America	WTR	17.00	(20)	(4)	2,259	1,178	48	24.3	23.6	22.1	19.1	26.55	2.29	11.6	2.33
Artesian Water Resources	ARTNA	18.29	(3)	0	133	7	23	18.9	20.8	19.7	18.9	30.65	2.91	10.5	1.58
California Water Service Gp.	CWT	36.87	(3)	(5)	743	176	51	27.5	24.6	21.7	18.9	50.72	4.75	10.7	2.01
Connecticut Water Service	CTWS	24.41	4	8	205	9	25	30.1	23.0	21.0	20.2	36.25	2.95	12.3	2.05
Consolidated Water Co.	CWCO	16.62	(34)	2	241	91	66	28.2	21.3	18.5	16.3	15.58	1.19	13.1	2.01
Middlesex Water	MSEX	18.24	(4)	6	242	19	28	22.2	21.0	19.8	18.8	29	2.4	12.1	1.82
Pennichuck Water	PNNW	22.24	(17)	36	94	4	45	76.7	26.2	24.4	23.9	35.41	2.88	12.3	2.08
SJW Corp.	SJW	30.64	(12)	(9)	563	124	49	25.5	29.5	25.1		42.94	3.74	11.5	2.37
Southwest Water Company	SWWC	11.24	(16)	(7)	259	159	50	24.4	36.3	22.9	22.5	16.55	1.02	16.3	1.74
York Water	YORW	15.08	(3)	(10)	169	9	17	26.0	26.5	22.8	22.5	21.52	1.52	14.2	2.53
Average			**(11)**	**2**	**500**		**42**	**29.8**	**25.0**	**21.6**	**19.9**			**11.9**	**2.04**
Median			**(9)**	**0**	**242**		**48**	**25.5**	**23.6**	**21.7**	**19.0**			**12.1**	**2.01**

Company	Symbol	Financial Performance: EPS 2006A	EPS 2007A	EPS 2008E	EPS 2009E	Oper. CFPS (TTM)	ROE (TTM)	Dividends: Current Annual Rate	Current Yield	Payout 2008E EPS	Div. as % of Book	1-yr. Growth Rate @	Balance Sheet: Book Value P/S	Equity/ Capital 12/2007'	Debt Rating
		$	$	$	$	$	%	$	%	%	%	%	$	%	
American States Water	AWR	1.44	1.55	1.75	1.90	3.23	6.20	1.00	2.9	57	5.7	6.4	17.43	50	A
Aqua America	WTR	0.70	0.72	0.77	0.89	1.37	9.80	0.50	2.9	65	6.8	8.7	7.30	43	A+
Artesian Water Resources	ARTNA	0.97	0.88	0.93	0.97	1.54	8.20	0.71	3.9	77	6.2	7.5	11.59	48	N/R
California Water Service Gp.	CWT	1.34	1.50	1.70	1.95	3.13	7.90	1.17	3.2	69	6.4	0.6	18.34	55	A+
Connecticut Water Service	CTWS	0.81	1.06	1.16	1.21	1.93	9.30	0.87	3.6	75	7.3	1.2	11.93	50	A
Consolidated Water Co.	CWCO	0.59	0.78	0.90	1.02	1.06	8.40	0.26	1.6	29	3.2	8.3	8.25	83	N/R
Middlesex Water	MSEX	0.82	0.87	0.92	0.97	1.51	9.00	0.70	3.8	76	7.0	1.4	10.03	48	A-
Pennichuck Water	PNNW	0.29	0.85	0.91	0.93	1.78	8.10	0.66	3.0	73	6.2	0	10.67	41	N/R
SJW Corp.	SJW	1.20	1.04	1.22	-	2.34	8.40	0.65	2.1	53	5.0	7.1	12.95	51	N/R
Southwest Water Company	SWWC	0.46	0.31	0.49	0.50	0.74	4.10	0.24	2.1	49	3.7	4.2	6.47	52	N/R
York Water	YORW	0.58	0.57	0.66	0.67	0.85	9.50	0.48	3.2	73	8.1	2.5	5.96	48	A-
Average							**8.08**		**2.9**	**63**	**6.0**	**4.4**		**52**	
Median							**8.40**		**3.0**	**69**	**6.2**	**4.2**		**50**	

** Estimates for AWR, CWT, and WTR are from Smith, Moore; Others from First Call.*
** Figures exclude items Smith, Moore believes to be non-recurring.*
Sources: Smith, Moore, Baseline, and company filings.

EPS Outlook

We expect recent and pending rate relief to lead to a period of accelerated EPS growth over the 2007-2010 period.

We expect recent and pending rate relief to lead to a period of accelerated EPS growth over the 2007-2010 period. Our 2008, 2009 and 2010 EPS estimates are $1.15, $1.25 and $1.40, respectively. During the 2001-2007 period, AWK's earnings and strategy were hampered by regulatory rate "stay-out" provisions and patriotic attitudes from regulators, interveners and smaller private and municipal water utilities. In addition, we believe RWE management lacked a full comprehension of the U.S. water industry dynamics and the savoir-faire necessary to operate in the local politics. As a result, earnings and customer growth suffered.

In the first three months of 2008, AWK subsidiaries filed rate requests in the states of New Jersey, California, Virginia, Tennessee and Missouri, requesting approximately $231.1 million in increased annualized revenues.

Over the past eighteen-months, AWK has diligently focused efforts on requesting and implementing rate recognition of investments in the business as well as earning reasonable returns on equity at its subsidiaries. The company received rate increases totaling $159 million annually in 2007, which compares to $41 million in 2006 and $35 million in 2005. In the first three months of 2008, AWK subsidiaries implemented $26.0 million in annual revenue increases and filed rate requests in the states of New Jersey, California, Virginia, Tennessee and Missouri, requesting approximately $231.1 million in increased annualized revenues. As of March 31, 2008, the company was awaiting final orders for one general rate case that was filed in 2006, requesting $7.0 million in total additional annual revenues, and five general cases that were filed in 2007, requesting $58.2 million in total additional annual revenues.

Annualized Rate Increases Granted			
State	**2005**	**2006**	**2007**
	$	$	$
New Jersey			56.2
Pennsylvania	5.8	8	40.6
Missouri		6.8	24
Illinois		0.9	1.7
Indiana	0.9	1.8	14
California	8.4	15.1	0.5
West Virgini	10		
Other	9.9	8.7	21.9
Total	**$35.0**	**$41.3**	**$158.9**

Source: Company Prospectus

In addition to normal customer growth and/or operating cost controls, AWK, similar to most water utilities, has three basic methods of EPS growth: (1) rate base growth, (2) consolidation and (3) privatization. We conservatively estimate AWK's long-term EPS growth rate at 5-to-7% per year for the foreseeable future.

With roughly 90% of earnings generated from the low-risk regulated water utility business, we assume reasonable regulatory treatment results in EPS power of $1.40 by 2010, which results in an estimated 10% return on common equity.

With roughly 90% of earnings generated from the low-risk regulated water utility business, we assume reasonable regulatory treatment results in EPS power of $1.40 by 2010, which results in an estimated 10% return on common equity. Water utility allowed returns on equity have averaged roughly 10-10.5% over the past few years. We estimate American Works regulated rate base at roughly $7.1 billion at year-end 2007 and an assumed 40% equity ratio would result in roughly $2.86 billion of equity rate base. A 10% earned ROE would result in roughly $1.78 of EPS power on 160 million shares outstanding. We note that the difference between actual "EPS power" and AWKs actual 2007 EPS results of $0.99 is the result of regulatory lag and a 28% common equity ratio (excludes goodwill). AWKs March 31, 2008, equity value per share (excluding goodwill) was $13.14 per share, which indicates EPS of $1.31 assuming a 10% earned return on equity.

Assuming a conservative 10% allowed ROE, we use the following simple equation as a starting point for projected rate base EPS growth for 2011 and beyond.

Financial Theory EPS Growth Rate				
EPS Growth	=	ROE*	X	Retention Rate**
EPS Growth	=	10%	X	(1 minus 50-to-70%)
3-to-5%	=	10%	X	(30-to-50%)

***ROE: return on equity**

**** Retention rate: earnings retained following dividend payout**

The assumed 3-to-5% EPS growth rate can be improved upon by increasing prudent infrastructure investment, which requires external capital raises, or by lowering the dividend payout ratio. We emphasize that the greater the multiple of book value that equity is issued, the lower the cost of capital and the greater the return on investment.

In addition to the 3-to-5% rate base growth, water utilities can enhance EPS growth via the consolidation of smaller systems.

In addition to the 3-to-5% rate base growth, water utilities can enhance EPS growth via the consolidation of smaller systems. During 2005, 2006 and 2007, AWK spent $5.0 million, $12.5 million and $15.9 million, respectively, for acquisitions of regulated water and wastewater systems. We consider such a level of acquisition activity to be minimal given AWKs size and the nation's potential opportunities. We attribute the lack of growth activity to an undetermined focus from the parent company, RWE. New AWK management has instilled the growth-through-acquisition culture that marked the "Water Works" of yore and we expect an acceleration of growth opportunities. A "tuck-in" is the acquisition of a water and wastewater utility serving less than 10,000 customers in areas contiguous with existing operations. Tuck-in opportunities allow AWK to integrate and manage acquired systems using existing management to achieve efficiencies. Historically, pursuing tuck-ins has been a fundamental part of AWKs growth strategy.

Throughout its long history, AWK has executed numerous large acquisitions, including several over the past 10 years.

Throughout its long history, AWK has executed numerous large acquisitions, including several over the past 10 years.

- In 1996 Pennsylvania American acquired the regulated water utility operations of Pennsylvania Gas and Water Company, a subsidiary of Pennsylvania Enterprises Inc., for approximately $409.4 million.
- In 1999, AWK acquired the privately held National Enterprises Inc., in a transaction valued at $700.0 million.
- In 2002, AWK acquired the water and wastewater facilities in six states from Citizens Communications Company for an aggregate purchase price of $979.8 million.

On December 21, 2007, New Jersey-American Water, signed an agreement with the city of Trenton, New Jersey to purchase the assets of the city's water system located in Ewing, Hamilton, Hopewell and Lawrence townships, which serve 39,000 customers. The purchase price is $100 million, and the agreement was approved by the Trenton City Council. The agreement requires approval by various regulatory agencies, including the New Jersey Board of Public Utilities.

Customer growth in the regulated businesses is driven by organic population growth within franchised service areas. We consider AWKs regulated business to be less-sensitive to economic cycles than other business. Residential customers account for approximately 91% of the total regulated customers and approximately 58% of total regulated operating revenue and residential water usage tends to be stable. Residential customers consume water for daily health and sanitary needs regardless of economic or other external factors. In addition, residential customers generally do not have the option of switching to another service provider.

We believe investors should be aware of a general trend toward declining residential per customer water usage.

However, we believe investors should be aware of a general trend toward declining residential per customer water usage. Increased water conservation, including growing use of more efficient household fixtures and appliances, combined with declining household sizes, has contributed to this trend. The average annual change in residential water usage per customer from January 1998 through December 2007 (as a percentage of January 1998 usage) in the larger subsidiaries and have ranged from 0.66% per year in New Jersey at the low end to as high as 1.63% per year in West Virginia. Declining usage could have a negative impact on revenues between rate cases in most states where revenue de-coupling regulatory principles are not allowed. Normally, a general rate case will reset sales levels to test year levels.

Regulatory lag refers to rising capital and operating costs that can hamper earnings results in the periods between rate cases.

Finally, regulatory lag is a significant challenge for AWK as well other water utilities. Regulatory lag refers to rising capital and operating costs that can hamper earnings results in the periods between rate cases. PUCs normally use an historical test year to set rates which incorporate historical capital and operating costs. As costs rise following a rate increases, AWKs earnings are challenged. Rising operating costs include labor, energy, taxes and treatment chemicals. We note and discuss numerous unique constructive water utility regulatory principles which have been designed to constructively deal with this issue, including distribution improvement surcharges, forward test years, revenue de-coupling and construction work in progress rate increases.

Non-regulated businesses include Contract Operations Group, Applied Water Management Group and Homeowner Services Group. In 2007, non-regulated businesses generated $242.7 million in operating revenue, or roughly 11% of consolidated revenues. As noted, the privatization business is highly competitive and has historically resulted in low margins. None-the-less, we anticipate the privatization market to grow at stronger rate than the regulated business and that AWK will be a leading player. We discuss AWK's non-regulated businesses in greater detail later in this report.

Capital Intensive Business:

We consider the water and wastewater utility business to be the most capital intensive of all the utility businesses.

We consider the water and wastewater utility business to be the most capital intensive of all the utility businesses. In 2007, AWK expended $758.6 million to add, replace and maintain property, plant and equipment. 2007 construction expenditures rose $69.7 million, or 10.1%, over 2006 driven by infrastructure replacements and upgrades to treatment facilities at several plants including Joplin, Missouri, Maricapa County, Arizona, Franklin Township, New Jersey and Champaign, Illinois. 2006 construction expenditures rose $130.4 million, or 23.4%, over 2005. These increases occurred due to re-focused efforts to invest in the regulated utility business.

Over the next five years, AWKs capital budget totals approximately $4.0- $4.5 billion and is expected to range between $770 and $950 million per year. The 5-year budget includes approximately $1.7 billion to replace aging infrastructure including mains, meters, and supply and treatment facilities, $1.3 billion for facilities to serve new customer growth and $700 million for compliance with quality standards and other regulatory requirements. Projects to enhance system reliability, security, and efficiency or to meet other needs are projected to total an additional $500 million.

Over the next five years, AWKs capital budget totals approximately $4.0- $4.5 billion and is expected to range between $770 and $950 million per year.

Operating cash flow totaled $473 million in 2007 including $140 million from Pennsylvania-Amerian and $123 million from New Jersey American. Subsidiary dividend policy requires all regulated subsidiaries to pay quarterly dividends of 75% of their net income in the previous quarter. Construction expenditures are partially offset by customer advances and contributions for construction (net of refunds) of $35.8 million, $47.4 million and $52.0 million for the years ended December 31, 2007, 2006 and 2005, respectively. Customer advances and contributions are reflected in net cash flows from financing activities.

We estimate operating cash of roughly $550 million per year over the 2007-2010 period generated primarily from net income, depreciation and advance from customers. With common dividends totaling roughly $125-150 million per year and construction expenditures of roughly $800 million, we project AWK will need to externally finance roughly $400-450 million per year.

Capital Structure

As of March 31, 2008, common equity represented 43% of total capitalization (includes short-term debt), including roughly 19% goodwill. Common equity excluding goodwill was 28%. As a condition to some PUC approvals of the IPO, AWK is required to maintain a capital structure which included a minimum of 45% equity (includes preferred equity). As of March 31, 2008, equity represented 46% of common equity for purposes of this calculation.

Goodwill and First Quarter 2008 Impairment Charge

On May 14, AWK took an event-driven impairment charge of $750 million due to the market price of the company's common stock (both as of the IPO date as well as the market price during subsequent trading) being less than what was anticipated at the completion of the 2007 annual test. On May 13, 2008, RWE transferred $245.0 million to the company to ensure that the regulatory requirements were met. At March 31, 2008, goodwill totaled $1.707 billion. The goodwill is associated primarily with the acquisition of American Water by an affiliate of RWE in 2003 and the acquisition of E'town Corporation in 2001, representing the excess of the purchase price the purchaser paid over the fair value of the net tangible and intangible assets acquired. Annual impairment reviews are performed in the fourth quarter. AWK recorded goodwill impairment in the amounts of $396.3 million in 2005, $227.8 million in 2006 and $509.3 million in 2007. We exclude goodwill from our calculation of capitalization ratios, book value, rate base and hypothetical EPS projections.

On May 13, 2008, RWE transferred $245.0 million to the company to ensure that the regulatory requirements were met.

The annual goodwill impairment test is conducted during the fourth quarter. During the third quarter of 2007, as a result of debt being placed on review for a possible downgrade and the anticipated sale of a portion of the Company, management determined at that time that it was appropriate to update its valuation analysis before the next scheduled annual test and recorded an impairment charge in the amount of $243.3 million in the third quarter of 2007. In the fourth quarter of 2007, AWK recorded an additional goodwill impairment charge of $266.0 million

Credit Ratings

Securities	Moody's	Standard & Poor's
Senior unsecured debt	Baa2	A–
Commercial paper	P2	A2

Standard and Poor's ratings on American Water and AWCC remain on CreditWatch with negative implications. Moody's rating outlook is stable.

Water Rate Increases the Key To Earnings Growth

Privately owned utilities are subject to economic regulation at the state level by independent state Public Utility Commissions (PUCs). Water utility rates are set on a cost-of-service or rate-base/rate-of-return methodology where utilities are given the opportunity to earn a fair return on their investment. Allowed returns on investment are set by the PUC's to allow utility equity and debt investors the opportunity to earn a fair return on investment while balancing the needs of customers. Over the past several years, allowed returns on equity have ranged between 9% and 12% and are highly correlated to interest rates. Each individual PUC has differing methods of auditing and determining a utility's capital and operating costs and differing regulatory mechanisms to balance the needs of consumers and water providers.

Frequent rate increases are often needed to allow a water utility to earn close to its allowed ROE.

Frequent rate increases are often needed to allow a water utility to earn close to its allowed ROE. As a result, numerous regulatory principles have been developed to deal with the unique needs of water utilities. Favorable mechanisms include quarterly distribution improvement charges, acquisition adjustments, balancing account mechanisms or other automatic adjustment mechanisms. While rate cases are generally viewed negatively in the electric and gas utility businesses, water rate cases and frequent increase grants are a general "way of life" for water utilities. Water rate increase requests are generally more frequent and acceptable.

Utility rate increases are never publicly and politically popular, but we do not expect resistance or price elasticity to be an issue for the foreseeable future. Water utility bills across the U.S. are extremely low. In fact, many household water bills are billed quarterly rather than monthly given their insignificance to the monthly consumer budget. Willingness to pay for "high-quality" water is readily evident in the prices paid for bottled water. Should one extend the price the consumer is willing to pay at the convenience store to the residential tap, a typical residential household water bill would total in excess of $50,000 per month. This compares to average-household water bills of roughly $30-to-$45 per month and other utility bills of roughly $100 for cable television, cell phone, electricity and heating services.

Water utility bills across the U.S. are extremely low.

Knowledgeable utility regulatory commissions loathe to describe water rate increases in terms of percentages given the headline grabbing attention that say a 15% rate increase can have when in fact a 15% increase on a $30/per month bill is $4.50 per month. Our observation is that constructive PUCs and regulatory relationships develop in states where larger and more pro-active water utilities operate. We consider Pennsylvania, Indiana, Ohio California and Illinois to be among the more currently constructive regulatory PUC's. A number of state public utility commissions have adopted constructive rate policies, including some form of single tariff pricing (uniform rates across a service territory), forward-looking test years, pass-through provisions or infrastructure surcharges.

One of the more constructive regulatory principles designed to deal with water utility-specific issues is an infrastructure surcharge mechanism (ISM). An ISM (each state has its own acronym) was designed to encourage pipe replacement by allowing immediate returns on investment. The mechanism allows rate adjustments outside of a general rate proceeding for specific capital expenditures to replace aging infrastructure (pipe replacement). These constructive regulatory mechanisms encourage a steady capital expenditure program to repair and improve water and wastewater systems as needed by reducing the regulatory lag on the recovery of prudent expenditures. Currently, Pennsylvania, Illinois, Missouri, Indiana, New York, California and Ohio have allowed the use of these infrastructure surcharges.

Some states have permitted use of some form of forecast or forward looking test **year** instead of historical data to set rates. Examples of these states include Hawaii, Illinois, Kentucky, Ohio, Pennsylvania, New York and California. In addition, a number of states have allowed the utility to update historical data for some changes that occur for some limited period of time subsequent to the historical test year. This allows the utility to take account of some more current costs or capital investments in the rate-setting process. Examples of these states include New Mexico, Texas, Missouri, Iowa, Virginia, Maryland, Tennessee, West Virginia, New Jersey and Arizona.

Another regulatory mechanism to address issues of regulatory lag includes the ability, in some circumstances, to recover in rates a return on utility plant before it is actually in service, instead of capitalizing an allowance for funds used during construction. Examples of states that have allowed such recovery include Texas, Pennsylvania, Ohio, Kentucky and California.

Uniform rates: Pennsylvania, New Jersey, West Virginia, Ohio, Indiana and Illinois have adopted a full or partial single rate policy. The single tariff structure is based on costs that are determined on a statewide basis, thereby moderating the impacts of periodic fluctuations in local costs and lowering administrative costs.

Selected Recent Rate Activity

On November 30, 2007, the Pennsylvania Public Utility Commission (PUC) approved a settlement calling for a $36 million (8.9 percent) annual revenue increase. The company's original proposal increased water rates by about $59.2 million (14.7 percent). The Commission voted 4-0 to approve the settlement, which was reached between the company and the state's Office of Consumer Advocate, the state's Office of Small Business Advocate, the PUC's Office of Trial Staff and consumers who had filed formal complaints. Under the settlement, the company may not file for a rate increase until April 24, 2009.

On January, 14 2008, New Jersey-American filed for a 23.35 percent rate increase with the New Jersey Board of Public Utilities. New Jersey American Water will have spent more than $350 million on investments to replace and upgrade its facilities, infrastructure and sources of supply state-wide since its last rate case. Investments include the replacement of hundreds of miles of water and sewer mains and the expansion of the Company's Canal Road Water Treatment Plant. In 2007, New Jersey American Water broke ground on a project to expand the production of water at the Canal Road Water Treatment Plant from 60 million gallons a day to 80 million gallons a day. The Company has also absorbed increasing operations costs including labor, energy, taxes and treatment chemicals.

On March 31, 2008, the Missouri-American Water Company filed a rate request with the Missouri Public Service Commission seeking to increase annual water operating revenues by approximately $49.6 million .

On March 18, 2008, the Public Service Commission of West Virginia approved a settlement of West Virginia-American rate case that was filed in mid-2007. The settlement calls for an increase of $14.5 million, or 15%. The last rate case was decided in July of 2005. Since 2004, the company invested more than $63.8 million in its facilities.

Non-Regulated Business.

AWK's Contract Operations Group (COG) generated revenue of $139.0 million in 2007, representing 57.3% of consolidated non-regulated revenues. COG provides services to systems with over 3,000 customers (and in many cases far larger) as distinguished from the O&M services provided by Applied Water Management Group usually to systems with less than 3,000 customers.

COG is party to more than 45 contracts across the United States and Canada, with contracts ranging in term from two to 20 years. The services provided vary in size and scope with annual operating revenue per contract ranging from $0.26 million to $9.0 million per contract. For instance, 25 of the O&M contracts are purely operational in nature and do not involve the design or construction of the facilities.

COG is an active participant in the Department of Defense's recently adopted Utility Privatization Program, or UPP. In 2003 it was awarded 50-year contracts for the operation and maintenance of the water and wastewater systems at Forts Leavenworth, Sill and Rucker and in September 2007 was awarded 50-year contracts for the operation and maintenance of the water and wastewater systems at Fort A.P. Hill and Scott Air Force Base worth approximately $160.0 million in total. Responsibilities under these contracts include system project management, regulatory and environmental compliance, planning and long-term operations and maintenance. Additionally, under a three-year contract awarded in 2006, COG was selected by Harnett County and the City of Fayetteville, North Carolina to operate, maintain and manage the existing water and wastewater treatment plants at Fort Bragg for an interim period until construction of new connections to the Harnett County and City of Fayetteville systems were completed.

The Applied Water Management Group (AWG) works with customers to design, build and operate smaller-scale water and wastewater treatment plants (typically serving up to 3,000 customers). Typical customers are real estate developers, industrial companies and new or expanding communities. Applied Water Management Group generated revenue of $33.3 million in 2007, representing 13.7% of revenue for our Non-Regulated Businesses.

AWG currently serves the AWK customer base primarily in the Northeastern United States and was responsible for the design, construction and operation of advanced wastewater treatment recycling systems for sites as varied as residential buildings in Battery Park City in New York City and Gillette Stadium in Foxborough, Massachusetts. Approximately 30% of AWGs business involves operating and maintaining smaller-scale water and wastewater plants, made up of a mixture of facilities that we designed and built, and some which we only operate.

The Homeowner Services Group provides services to domestic homeowners to protect against the cost of repairing broken or leaking pipes inside and outside their homes. AWK initially offered these services within territories covered by its regulated subsidiaries, but has expanded to enable other utilities outside our territories to offer the services to their customers. Homeowner Services Group generated revenue of $40.4 million in 2007, representing 16.6% of non-regulated businesses. In addition, Service Line Protection Programs offer customers various service contracts for a monthly fee that cover repair of water line leaks and breaks, sewer line clogs and blockages and emergency in-home plumbing

Recent Earnings Results

On May 13, 2008, AWK reported first quarter 2008 EPS results of $0.04, excluding an impairment charge compared with earnings of $2.7 million, or $0.02 per share, in the first quarter of 2007.

Operating revenues increased 8.2 percent to $506.8 million, compared to $468.5 million in the prior year period. The rise in operating revenues was due primarily to rate increases of approximately $33.0 million obtained mainly through general rate cases in New Jersey, Pennsylvania, Missouri and Indiana. This increase was offset by a $4.7 million decrease in revenues related to unusually wet weather, mainly in states in the western region of the United States. Total volume of water sold decreased 2.9 percent for the three months ended March 31, 2008, to 87.0 billion gallons, from 89.6 billion gallons for the same period in 2007.

Non-regulated Businesses' revenues increased by $7.9 million for the three months ended March 31, 2008, compared to the same period in 2007. The net increase was primarily attributable to higher revenues in the Contract Operations Group and the Homeowner Services Group, partially offset by decreased revenues in its Applied Water Management Group due to the weakness in the United States housing market.

Operating expenses excluding impairment charge for the three months ended March 31, 2008, increased $31.9 million over the prior year. The increase resulted primarily from an increase in the number of employees, as well as higher wage and benefit expenses. Non-regulated Businesses' increased expenses correspond with their increased revenues.

Valuation

AWK currently trades at 18.8X and 17.3X our 2008 and 2009 EPS estimates and 165% of tangible book value (excludes goodwill). The sector recently traded at valuation multiples averaging 21.6X 2008 EPS estimates, 19.0X 2009 EPS estimates and 201% of book value. We believe AWK shares warrant at least an industry average multiple. On the one hand, AWKs premier national franchise and associated growth opportunities justify a premium valuation. However, the RWE ownership and leveraged balance sheet warrant discounted multiples.

While we believe price-to-earnings and price-to-book value ratios are helpful measures in our valuation assessment, our $25 price objective range is derived using a dividend discount model (DDM). We prefer the DDM for water utility valuation given the unique features of a water utility and their application to the model, including frequent setting of allowed ROE's, long-standing dividend policies and predictability of earnings streams. Importantly, a DDM places significant value on risk premium in determining present value.

Our $25 price objective range is achieved by applying a 3.0% risk premium to the 30-year treasury yield of 4.75%, a 12% near-term EPS growth rate and a 4.5% long-term growth rate.

American Water Works

Period	Annual Dividend	Discount Rate	PV of Dividends
0	$0.80		
1	$0.84	0.93	$0.78
2	$0.88	0.86	$0.76
3	$0.92	0.80	$0.73
4	$0.96	0.74	$0.71
5	$1.00	0.69	$0.69
	Sum of PV of Dividends		**$3.67**
6	$1.04	0.90	
ROR	**7.80%**	**LT Growth Rate**	**4.5%**
	Terminal Value		**$21.38**

Present Value of the Stock	**$25.05**
Price Objective	**$25.00**
Current Share Price	**$21.62**
Discount	**15.63%**

Water utilities possess many characteristics of the traditional regulated electric or gas utility but are differentiated by unique features often neglected by those reluctant to look any further than relatively-high valuations. Water utilities warrant premium multiples to the electric and gas utility industries for two reasons: lower risk and stronger long-term growth potential.

Low Risk. We believe water utilities warrant among the lower risk premiums of any sector in the market based on the following features:

- a monopoly service territory,
- high barriers to entry,
- no alternative product,
- price inelasticity,
- public and regulatory support for price increases,
- regulated rates of return and
- strong financial conditions.

Stronger long-term growth potential through rate base growth, consolidation and privatization opportunities.

Rate Base Growth. Cost of Service and/or Rate Base-Rate of Return regulation permits rate adjustments to give utilities the opportunity to earn a fair return on investment in infrastructure. The more cash a utility prudently invests in infrastructure or "plows back into the business", the greater rate base and earnings grow. According to the EPA and various other organizations, water utilities must invest billions of dollars in water infrastructure to maintain quality service, rehabilitate existing systems, comply with ever-increasing quality standards and build new projects. In recent periods, water utility allowed returns on common equity (ROE's) have been set at reasonable ranges between 9-to-12%.

Assuming a conservative 10% allowed ROE, we assume projected rate base EPS growth of 3-to-5%. The assumed 3-to-5% growth rate can be improved upon by increasing prudent infrastructure investment, which requires external capital raises, or by lowering the dividend payout ratio. We emphasize that the greater the multiple of book value that equity is issued, the lower the cost of capital and the greater the return on investment.

Electric and gas utilities also have the opportunity to grow EPS through investment in rate base and over the next decade or so electric utilities have substantial opportunity to grow through base load generation additions and transmission investments. However, we believe this growth is cyclical in that the industry goes through baseload boom-bust periods. Water and wastewater infrastructure investments appear to be needed for the foreseeable future. In addition, water utility rate increases normally do not face the controversy of an electric or gas utility rate increase primarily due to relatively low cost of water. For most consumers, water and wastewater bills make up a relatively small percentage of household expenditures compared to other utility services.

We expect rate base growth to continue for the foreseeable future given that capital expenditures are required, the regulatory environment is supportive and customer rates are relatively low and price inelastic.

(2) Consolidation. In addition to the 3-to-5% rate base growth, water utilities can enhance EPS growth via the consolidation of smaller systems. The water utility industry is the most fragmented of the utility industries with approximately 53,000 community water systems in the U.S. and nearly 45,000 systems serving customer bases of less than 3,300. AWK pursues the addition of customers through tuck-ins of small water and/or wastewater systems, typically serving fewer than 10,000 customers, in close geographic proximity to existing regulated operations. However, AWK will pursue large acquisition in both contiguous and non-contiguous service areas. Acquisitions are accretive as long as the purchase price is reasonable, cost cutting achievable, profitability enhanced and/or the share price, if trading at a multiple of book, is used as currency to fund the proposed purchase.

(3) Privatization activity. Water utilities can also grow revenues, customers and EPS without significant capital investment and regulatory oversight by partnering with the nation's "24,000 or so" municipal water and wastewater systems. Privatization activity can range anywhere from the "outright sale" of municipal assets to a private company to a contract for the outsourcing of a particular function, such as billing or meter reading. Public-private partnerships or contract arrangements generally consist of a private firm operating/managing all or part of a municipally-owned system under contract. The private company benefits from the opportunity to generate revenues and cash flow with minimal capital investment, while the municipality benefits from better quality service, technical expertise and potential lower costs. The municipality owns the system, sets the rates and makes the long-term capital investment decisions. There are currently several thousands of contracts of varying sizes and degrees between municipalities and private water operators. The great majority of these contracts are between smaller towns and municipalities where the politics of privatization are less challenging. We note that contracts with larger cities have generally proven difficult to negotiate and have often resulted in thin or negative profit margins for the private operator.

Intangible Value. We argue that water utilities possess an intangible and unquantifiable value related to existing infrastructure, water resources, and rights and expertise to the further development of infrastructure. We expect this intangible value to be realized over a period of decades through the regulatory framework, but could be realized quicker through a takeover and/or in the unlikely event of deregulation or development of a competitive water resource market.

We argue that water utilities possess an intangible and unquantifiable value related to existing infrastructure, water resources, and rights and expertise to the further development of infrastructure.

We liken water supply and "water rights" in a theoretically-unregulated water environment to a nuclear power plant in today's competitive power markets. With tight supply-demand margins and limited base-load generation competition (variable costs well-below natural gas or coal and the extremely-long time frame of adding new nuclear plants), nuclear power plants have the potential to earn "excessive" profits for the foreseeable future. However, unlike a nuclear plant, water supply is finite and has absolutely no substitute. In addition, water consumption (demand) is a necessity for life. As a result, the price of water could theoretically become completely price-inelastic, or in many ways, the ultimate commodity. In our opinion, the social and political ramifications of such a scenario are too great and will ensure water resources are always heavily regulated.

While the resource will never be competitively traded like oil, gold or diamonds, we believe certain elements of the water distribution value-add-chain are "competitive" assets and subject to market prices. These assets include: the technical expertise to treat and distribute water, managerial ability to construct and operate long-term water infrastructure projects and the "savoir-faire" to navigate a politically-charged water and wastewater environment.

Accepting the real value of a water utility stock requires one to accept that the growth potential may not occur in the next one-to-five years.

Accepting the real value of a water utility stock requires one to accept that the growth potential may not occur in the next one-to-five years. Value and growth potential lies not only in the existing hard assets in the ground but also in the "rights expertise" to maintain and grow infrastructure. We believe many larger companies have considered this value when acquiring water utilities over the last several years. The water utility sector has undergone considerable consolidation over the past decade-or-so as major players attempt to strategically position themselves to capitalize on the eventual consolidation and privatization of the industry. Takeover multiples have generally been in the 200-300% of book value and 20-30X EPS multiple ranges.

Given high absolute valuation levels relative to the market and utility peer groups and the relatively small market capitalization size of the sector, the addition of American Water increases the market capitalization of the group by as much as 40% and could lead to sector valuation dilution. On the other hand, the entrance of another large publicly-traded water utility, like American Water, on professional money managers "radar screens" could increase the interest in the sector and generate additional investment consideration.

Water utility share prices are inversely correlated with interest rates due to the relatively stable nature of earnings, cash flow and dividend streams. Should interest rates rise, water utility share prices would likely come under pressure. However, we note that allowed returns on common equity are also highly correlated with interest rates and higher rates typically result in larger rate increases and higher authorized allowed returns on common equity.

Control issues and additional shares to come public. RWE, the large German multi-utility, owns approximately 102 million, or 64%, of the 160 million shares of common stock outstanding. As a result, RWE has the potential to significantly influence all matters submitted to a vote of stockholders, including the election of directors. Following the expiration of a 180-day lock-up period, which ends October 23, the remaining 102 million common shares will be eligible for future sale. RWE intends to fully divest its ownership of American Water as soon as reasonably practicable, subject to market conditions.

As a result, RWE has the potential to significantly influence all matters submitted to a vote of stockholders, including the election of directors.

History as a Public Company. AWK was founded in 1886 as the American Water Works & Guarantee Company, for the purposes of building and purchasing water systems in McKeesport, Pennsylvania. In 1935, the Company was reorganized under its current name, and in 1947 the common stock of the Company became publicly traded on the New York Stock Exchange. Prior to being acquired by RWE in 2003, AWK was the largest publicly traded water utility company in the United States.

In 2003, AWK was acquired by RWE and became a private company. The RWE acquisition resulted in many structural changes. Operations and management were managed through Thames Water, a subsidiary of RWE. In addition, many of AWKs subsidiaries agreed not to file rate cases for specified periods of time as a condition of the acquisition. In 2005, RWE decided to divest American Water. In March 2006, RWE decided to divest American Water through the sale of shares in one or more public offerings.

American Water Works

Financial Statements (2005-2010)
(In $ millions unless otherwise noted)

Income Statement	2005A	2006A	2007A	2008E	2009E	2010E
Operating revenues	2,137	2,093	2,214	2,270	2,326	2,384
Rate increases				187	300	402
Operating revenues	2,137	2,093	2,214	2,457	2,626	2,786
Operating expenses						
Operation & maintenance	1,201	1,175	1,249	1,324	1,390	1,459
Depreciation & amortization	261	259	267	283	300	318
General taxes	183	185	183	189	194	200
Gain on sale of assets	(7)	0	(7)			
Impairment charge	385	222	509	750		
Total operating expenses	2,025	1,841	2,201	2,546	1,885	1,978
Operating income	112	253	13	(89)	742	808
Operating income excl. impairment	491	474	515	661	742	808
Other income						
Interest	345	366	281	300	300	301
New interest expense				26	50	74
Other	(10)	(5)	(12)	29	59	59
Total other income	336	361	269	354	409	434
Income from continuing operations	155	113	245	306	333	375
Provision for income taxes	51	47	86	122	133	150
Tax rate	0	0	0	0	0	0
Net income	(275)	(156)	(343)	(566)	200	225
Net income, excluding impairment	104	66	159	184	200	225
Shares outstanding	160	160	160	160	160	161
EPS	($1.72)	($0.97)	($2.14)	($3.54)	$1.25	$1.40
EPS excluding non-recurring	$0.65	$0.41	$0.99	$1.15	$1.25	$1.40

Cash Flow Statement	2005A	2006A	2007A	2008E	2009E	2010E
Net income	(275)	(156)	(343)	(566)	200	225
Depreciation	261	259	267	283	300	318
Other	539	220	549	850	75	75
Operating cash flow	525	324	474	567	575	618
Capital expenditures	(558)	(689)	(759)	(800)	(800)	(800)
Other	28	3	12			
Investing cash flow	(530)	(691)	(747)	(800)	(800)	(800)
Debt issuance				425	400	400
Common dividends				(128)	(134)	(141)
Other						
Financing cash flow				297	266	259

Balance sheet	2005A	2006A	2007A	2008E	2009E	2010E
Common equity	2,805	3,817	4,543	3,848	3,914	3,998
Goodwill	3,188	2,966	2,457	1,709	1,709	1,709
Preferred equity	1,779	1,779	29	29	29	29
Short-term debt	0	0	317	317	317	317
Long-term debt	5,030	4,104	4,675	5,100	5,500	5,900
Total capitalization	12,802	12,666	12,020	11,003	11,468	11,952

Smith, Moore Compliance Disclosure

Disclosures:

I certify that:
1) The views expressed in this research report accurately reflect my personal views about the subject security; and
2) No part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by me in this research report.

Chief risks to (American Water Works/AWK-NYSE) shares include potential adverse regulatory decisions, undertaking unprofitable growth ventures, and deterioration in its premium to the industry multiple.

In addition:
1) Neither the analyst nor Smith, Moore & Co owns any shares of the above mentioned security.
2) Smith, Moore & Co does not make a market in the subject security.
3) Neither the analyst nor member knows or has reason to know of any material conflict of interest regarding the subject security.
4) Neither the analyst nor any member of the analyst's household is an officer, director or advisory board member of the subject company.

And finally:
1) Smith, Moore & Co. does not compensate its research analysts based on specific investment banking transactions. Smith, Moore & Co research analysts receive compensation that is based upon and impacted by the overall profitability and revenue of the firm, which includes, but is not limited to investment banking revenue, and
2) Smith, Moore & Co has not received compensation for any investment banking services from the subject security or any affiliated entities of the subject security during the past 12 months, including no involvement as either a manager or co-manager of a public offering of equity or equity related securities during the same period of time.

Security/Stock Rating Definitions:

O = Outperform:SM Research & Perspective expects the risk-adjusted return of the security to exceed the risk-adjusted return of its peer group over the next 12 to 18 months.
M = Market Perform:SM Research & Perspective expects the risk-adjusted return of the security to be in-line with the risk-adjusted return of its peer group over the next 12 to 18 months.
U = Underperform:SM Research & Perspective expects the risk-adjusted return of the security to be less than the risk-adjusted return of its peer group over the next 12 to 18 months.
TB = Trading Buy:SM Research & Perspective expects a near-term identifiable catalyst to potentially cause the select security to exhibit abnormal upside price movement over the near term.
TS = Trading Sell:SM Research & Perspective expects a near-term identifiable catalyst to potentially cause the select security to exhibit abnormal downside price movement over the near term.

As of (date of publication)
(86%) of companies covered by SM Research & Perspective are rated Outperform.
(14%) of companies covered by SM Research & Perspective are rated Market Perform.
(0%) of companies covered by SM Research & Perspective are rated Underperform.

Smith, Moore & Co. has provided investment banking services for 0% of all companies under current research coverage.

18/02/2009

SOCIETE GENERALE
Cross Asset Research

Equity Research

Water Utilities (United States)

PREVIEW

AMERICAN WATER WORKS

Quarterly results Details on financing cost and the stimulus plan

Buy (12m)

Price 17/02/09	12m target
$20.8	$22.0

Sector
Weighting
Underweight
Preferred stock
EDF
Least preferred stock
Scottish & Southern Energy

Headline numbers

	Q4 07	Q4 08e	yoy (%)	Reuters
Revenues ($m)	554	572	+3.2	617
EBITDA ($m)	175	190	+8.4	224
EBIT ($m)	-156	120	Ns	162
EBIT margin (%)	Ns	20.9		26.2
Reported net income ($m)	247	68	-72.5	43

SG Equity Research sentiment

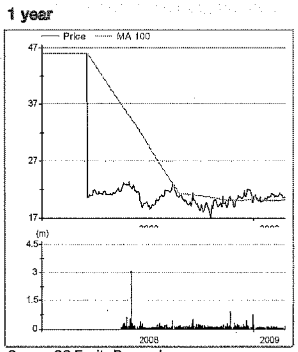
	--/-/0/+/++
Visibility/Confidence	0
Publication vs consensus	0
Market reaction	0
Company new guidance	0
Chg. in sector perception	0

- **Calendar** American Water is to report FY08 results (Q4 08) on 26 February 2009 at 9 am US Eastern Time). A conference call is scheduled; dial-in +1 800 230 1059 (US) and +1 612 234 9959 (outside US); access code #982411. The conference call can also be followed online: www.amwater.com.

- **Watch out for** Management's comments on the US stimulus plan and the expected impact thereof. William D. Patterson has been appointed as Senior Vice-President of corporate and business development to further the group's plans to penetrate the public/private partnership segments, services to the US military, and operating and maintenance contracts (all mentioned in Obama's plan). We also think that management could discuss the financing situation in depth (and financing cost) in the light of the current crisis. The group has already announced payment of a dividend of $0.2 per share. Note that the group is expected to report a FY loss of an estimated $531m following asset writedowns ($750m) in Q1 08.

- **Potential market reaction** We believe that the consensus could react positively to announcements on group development in the non-regulated market with possible contract signatures (note that American Water already has strong positions in water treatment with the US army). Management is likely to announce no change to the dividend payout policy, of $0.2/quarter. If the dividend is not maintained, the consensus is likely to take a dim view.

1 year



Source: SG Equity Research

American Water Works
on,www.sgresearch.socgen.com

Share data			
RIC AWK.N, **Bloom** AWK US			
52-week range			23.4-17.2
EV 08 ($m)			8,958
Market cap. ($m)			3,333
Free float (%)			40.0
Performance (%)	**1m**	**3m**	**12m**
Ordinary shares	1.9	6.5	na
Rel. S&P 500	9.7	14.9	na

Financial data	12/07	12/08e	12/09e	12/10e
Revenues ($bn)	2.21	2.34	2.43	2.55
EBIT margin (%)	23.4	23.6	23.7	23.9
Rep. net inc. ($m)	139	-531	181	180
EPS (adj.) ($)	0.99	1.09	1.13	1.12
Dividend/share ($)	0.00	0.60	0.80	0.88
Payout (%)	0.0	nm	70.9	78.4
Interest cover (x)	1.8	1.8	1.7	1.7
Net debt/equity (%)	110.0	135.0	145.0	154.5

Ratios	12/07	12/08e	12/09e	12/10e
P/E (x)	21.1	19.2	18.5	18.5
FCF yield (/EV) (%)	0.0	-2.2	-0.8	-0.1
Dividend yield (%)	0.0	2.9	3.8	4.2
Price/book value (x)	0.7	0.8	0.8	0.8
EV/revenues (x)	3.76	3.83	3.89	3.89
EV/EBIT (x)	16.1	16.2	16.4	16.3
EV/IC (x)	0.6	0.6	0.6	0.6
ROIC/WACC (x)	0.5	0.5	0.5	0.5

CAGR 07-10e,: +4.4%


John Honore
(33) 1 42 13 51 55
john.honore@sgcib.com


Didier Laurens
(33) 1 42 13 50 78
didier.laurens@sgcib.com

SG acted as co-manager in American Water Works' IPO

IMPORTANT DISCLOSURES

American Water Works	SG acted as co-manager in American Water Works' IPO
British Energy	SG acted as Mandated Lead Arranger and Bookrunner of the acquisition facilities set up by EDF for the acquisition of British Energy
EDF	SG acted as joint-lead manager and joint-bookrunner of EDF Energies Nouvelles capital increase
EDF	SG acted as Mandated Lead Arranger and Bookrunner of the acquisition facilities set up by EDF for the acquisition of British Energy
EDF Energies Nouvelles	SG acted as joint-lead manager and joint-bookrunner of EDF Energies Nouvelles capital increase

US THIRD PARTY FOREIGN AFFILIATE RESEARCH DISCLOSURES:

SG and its affiliates beneficially own 1% or more of any class of common equity of British Land Co.
SG and its affiliates beneficially own 1% or more of any class of common equity of EDF Energies Nouvelles.
SG or its affiliates expect to receive or intend to seek compensation for investment banking services in the next 3 months from American Water Works.
SG or its affiliates expect to receive or intend to seek compensation for investment banking services in the next 3 months from EDF.
SG or its affiliates expect to receive or intend to seek compensation for investment banking services in the next 3 months from EDF Energies Nouvelles.
SG or its affiliates have received compensation for investment banking services in the past 12 months of American Water Works.
SG or its affiliates have received compensation for investment banking services in the past 12 months of EDF.
SG or its affiliates have received compensation for investment banking services in the past 12 months of EDF Energies Nouvelles.
SG or its affiliates managed or co-managed in the past 12 months a public offering of securities of American Water Works.
SG or its affiliates managed or co-managed in the past 12 months a public offering of securities of EDF.

IMPORTANT DISCLAIMER: The information herein is not intended to be an offer to buy or sell, or a solicitation of an offer to buy or sell, any securities and including any expression of opinion, has been obtained from or is based upon sources believed to be reliable but is not guaranteed as to accuracy or completeness although Société Générale ("SG") believe it to be clear, fair and not misleading. SG, and their affiliated companies in the SG Group, may from time to time deal in, profit from the trading of, hold or act as market-makers or act as advisers, brokers or bankers in relation to the securities, or derivatives thereof, of persons, firms or entities mentioned in this document or be represented on the board of such persons, firms or entities. Employees of SG, and their affiliated companies in the SG Group, or individuals connected to then, other than the authors of this report, may from time to time have a position in or be holding any of the investments or related investments mentioned in this document. Each author of this report is not permitted to trade in or hold any of the investments or related investments which are the subject of this document. SG and their affiliated companies in the SG Group are under no obligation to disclose or take account of this document when advising or dealing with or for their customers. The views of SG reflected in this document may change without notice. To the maximum extent possible at law, SG does not accept any liability whatsoever arising from the use of the material or information contained herein. This research document is not intended for use by or targeted at retail customers. Should a retail customer obtain a copy of this report they should not base their investment decisions solely on the basis of this document but must seek independent financial advice.
Important notice: The circumstances in which materials provided by SG Fixed & Forex Research, SG Commodity Research, SG Convertible Research, SG Technical Research and SG Equity Derivatives Research have been produced are such (for example because of reporting or remuneration structures or the physical location of the author of the material) that it is not appropriate to characterise it as independent investment research as referred to in European MIF directive and that it should be treated as a marketing material even if it contains a research recommendation («,recommandation d'investissement à caractère promotionnel,»). However, it must be made clear that all publications issued by SG will be clear, fair, and not misleading.
Analyst Certification: Each author of this research report hereby certifies that (i) the views expressed in the research report accurately reflect his or her personal views about any and all of the subject securities or issuers and (ii) no part of his or her compensation was, is, or will be related, directly or indirectly, to the specific recommendations or views expressed in this report.
Notice to French Investors: This publication is issued in France by or through Société Générale ("SG") which is authorised by the CECEI and regulated by the AMF (Autorité des Marchés Financiers).
Notice to UK investors: This publication is issued in the United Kingdom by or through Société Générale ("SG") London Branch which is regulated by the Financial Services Authority ("FSA") for the conduct of its UK business.
Notice To US Investors: This report is intended only for major US institutional investors pursuant to SEC Rule 15a-6. Any US person wishing to discuss this report or effect transactions in any security discussed herein should do so with or through SG Americas Securities, LLC ("SGAS") 1221 Avenue of the Americas, New York, NY 10020. (212)-278-6000. THIS RESEARCH REPORT IS PRODUCED BY SOCIETE GENERALE AND NOT SGAS.
Notice to Japanese Investors: This report is distributed in Japan by Société Générale Securities (North Pacific) Ltd., Tokyo Branch, which is regulated by the Financial Services Agency of Japan. The products mentioned in this report may not be eligible for sale in Japan and they may not be suitable for all types of investors.
Notice to Australian Investors: Société Générale Australia Branch (ABN 71 092 516 286) (SG) takes responsibility for publishing this document. SG holds an AFSL no. 236651 issued under the Corporations Act 2001 (Cth) ("Act"). The information contained in this newsletter is only directed to recipients who are wholesale clients as defined under the Act.
IMPORTANT DISCLOSURES: Please refer to our website: http://www.sgresearch.socgen.com

SOCIETE GENERALE
Cross Asset Research

Equity Research

United States
Target price downgrade

26 February 2009

A GLOBAL VIEW FROM EUROPE

Water Utilities

AMERICAN WATER WORKS

Q4 08 better than we expected despite lower volumes

Buy (12m)

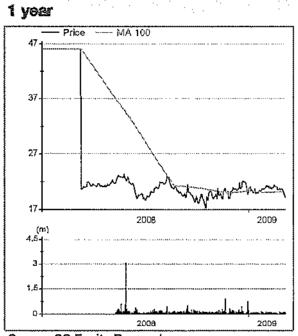
Price 25/02/09	12m target
$19.2	$21.0

Sector
Weighting
Underweight
Preferred stock
EDF
Least preferred stock
Scottish & Southern Energy

- **Update** The group reported Q4 08 operating profit slightly higher than we had expected ($129m vs SGe: $120m) and just lagging the consensus ($136m). American Water Works observed a decline in volumes of more than 5% owing to the uncertain economic backdrop, in line with trends seen in the previous three quarters. Note that the group managed to benefit from tariff increases (rate base) of close to $206m over 2008, which amounts to 10% of regulated revenues and should support future growth (for 2009e and beyond). Furthermore, the group also managed to secure part of its financing via confirmed credit lines and a capital injection of $245m.

- **Impact** We have adjusted our EPS forecasts (-5.6%) to take account of: 1) trends in operating multiples, and 2) what we see as an increase in financing costs. Note that the group indicated that it had suffered an increase in its costs (pensions, chemical treatment products, etc.) which we believe it should manage to keep under control in the coming months.

1 year



Source: SG Equity Research

- **Target price & rating** Based on our new estimates, we are revising our DCF-based target price to $21 per share (from $22). Our DCF approach uses a WACC of 5.1% (unchanged beta at 0.6), growth to perpetuity of 1%, but intermediate growth (over 2014e-2019e) of 5% (vs 6% previously). We apply an unchanged normalised operating margin of 30% (SGe: 23% for 2009e) which reflects the entire tariff increase the group could expect under less uncertain market conditions. We reiterate our Buy on the share as we view the share as a way of gaining protection against unfavourable economic trends (even though downtrending volumes can be attributed to less dynamic economic growth). Our forecast for group revenues is based on returns allocated by local regulators (see our 24 November 2008 report) which we see as particularly resilient. The share's recent decline (15% over one month) is, in our view, a good entry point to take positions on President Obama's stimulus package (see our note from 20 February 2009).

- **Next events & catalysts** The group is to detach its upcoming dividend ($0.2/sh.) around 2 March 2009. Q1 09 results should be released around end-April 2009. Furthermore, the group's annual report should be available in the next few days via the SEC site.

American Water Works
on www.sgresearch.socgen.com

Share data			
RIC AWK.N, Bloom AWK US			
52-week range			23.4-17.2
EV 09 ($m)			9,213
Market cap. ($m)			3,353
Free float (%)			40.0
Performance (%)	**1m**	**3m**	**12m**
Ordinary shares	-7.6	-7.7	na
Rel. S&P 500	0.5	3.4	na

Financial data	12/08	12/09e	12/10e	12/11e
Revenues ($bn)	2.34	2.39	2.46	2.55
EBIT margin (%)	24.1	23.3	22.6	22.8
Rep. net inc. ($m)	-562	172	158	158
EPS (adj.) ($)	1.05	0.99	0.90	0.90
Dividend/share ($)	0.60	0.80	0.80	0.80
Payout (%)	nm	81.1	88.7	88.5
Interest cover (x)	2.0	1.7	1.6	1.7
Net debt/equity (%)	135.9	139.5	144.7	149.5
Prev. EPS change (26/02/09)		1.13	1.12	na

Ratios	12/08	12/09e	12/10e	12/11e
P/E (x)	18.2	19.5	21.3	21.2
FCF yield (/EV) (%)	-2.7	2.4	2.0	2.2
Dividend yield (%)	3.1	4.2	4.2	4.2
Price/book value (x)	0.8	0.8	0.8	0.8
EV/revenues (x)	3.86	3.85	3.85	3.80
EV/EBIT (x)	16.0	16.5	17.0	16.7
EV/IC (x)	0.6	0.6	0.6	0.6
ROIC/WACC (x)	0.5	0.5	0.5	0.5
CAGR 08-11e: -5.0%				

John Honore
(33) 1 42 13 51 55
john.honore@sgcib.com

Didier Laurens
(33) 1 42 13 50 78
didier.laurens@sgcib.com

SG acted as co-manager in American Water Works' IPO

Q4 08 key figures – Estimates and published

In $m	Q4 07	Q4 08 SGe	Q4 08 Reuters estimates	Q4 08 Published
Sales	554	572	600	569
EBITDA	175	190	208	201
EBIT	-156	120	136	129
Margin (%)	ns	21.0	22.7	22.7
Net profit	247	68	43	36

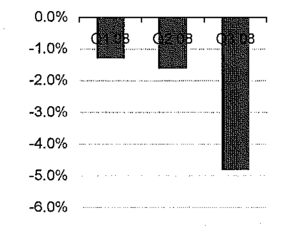
Source: SG Equity Research / Reuters / American Water

Old and new EPS estimates

$ per share	2008	2009e	2010e	2011e
New EPS*	Published: 1.10	1.08	0.99	1.00
Old EPS	1.09	1.13	1.12	n/a
Change	0.9%	-4.4%	-11.6%	-

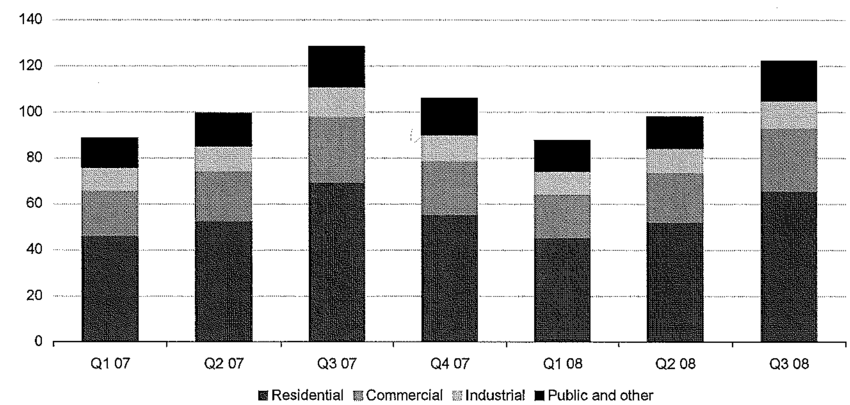
Source: SG Equity Research * Includes a 9% increase in shares outstanding after a refinancing-related rights issue

Quarterly change in consumption Q/Q N-1



Source: SG Equity Research

Quarterly consumption (bn gallons) Q1 07-Q3 08



Source: SG Equity Research / American Water

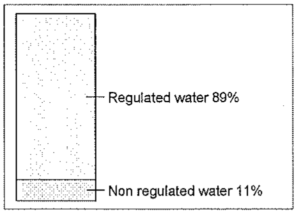
IMPORTANT DISCLOSURES

American Water Works	SG acted as co-manager in American Water Works' IPO
EDF	SG acted as joint-lead manager and joint-bookrunner of EDF Energies Nouvelles capital increase
EDF	SG acted as Mandated Lead Arranger and Bookrunner of the acquisition facilities set up by EDF for the acquisition of British Energy

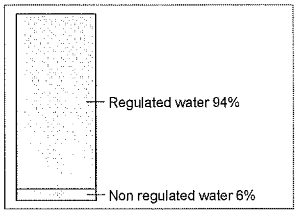
US THIRD PARTY FOREIGN AFFILIATE RESEARCH DISCLOSURES:

SG or its affiliates expect to receive or intend to seek compensation for investment banking services in the next 3 months from American Water Works.
SG or its affiliates expect to receive or intend to seek compensation for investment banking services in the next 3 months from EDF.
SG or its affiliates have received compensation for investment banking services in the past 12 months of American Water Works.
SG or its affiliates have received compensation for investment banking services in the past 12 months of EDF.
SG or its affiliates managed or co-managed in the past 12 months a public offering of securities of American Water Works.
SG or its affiliates managed or co-managed in the past 12 months a public offering of securities of EDF.

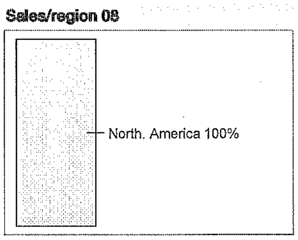
Sales/division 08



EBIT/division 08



Sales/region 08



Major shareholders (%)

RWE	60.0

Normalised data

EBITDA margin (%)	42.0
Normalised growth (%)	0.0

We have lowered our 2009 & 2010 EBITDA estimates by respectively 3% and 6%.

We believe the group is going to be very selective in its investment policy in 09 in light of current financial conditions.

Water Utilities (United States) — Price (25/02/09) $19.2 — 12m target $21.0

American Water Works

BUY

Valuation* ($m)	**12/04**	**12/05**	**12/06**	**12/07**	**12/08**	**12/09e**	**12/10e**	**12/11e**
Average nb of shares (diluted)	160.0	160.0	160.0	160.0	167.3	174.5	174.5	174.5
Share price (average)					20.68	19.21	19.21	
Average market cap. (SG adjusted) (1)	0	0	0	0	3,312	3,353	3,353	0
Restated net debt (-)/cash (+) (2)	-7,048	-6,740	-5,848	-5,003	-5,663	-5,860	-6,102	-6,333
Value of minorities (3)	0	0	0	0	0	0	0	0
Value of financial investments (4)	0	0	0	0	0	0	0	0
Other adjustment (5)	0	0	0	0	0	0	0	0
EV = (1) - (2) + (3) - (4) + (5)	na	na	na	na	8,974	9,213	9,455	na
P/E (x)	na	na	na	na	19.6	19.5	21.3	na
Price/cash flow (x)	na	na	na	na	7.6	7.3	7.3	na
Price/free cash flow (x)	nm	nm	nm	nm	nm	nm	nm	nm
Price/book value (x)	na	na	na	na	0.9	0.8	0.8	na
EV/revenues (x)	na	na	na	na	3.84	3.85	3.85	na
EV/EBITDA (x)	na	na	na	na	10.8	11.0	11.1	na
Dividend yield (%)	na	na	na	na	2.9	4.2	4.2	na
Per share data ($)								
SG EPS (adj.)	0.98	0.85	0.89	0.99	1.05	0.99	0.90	0.90
Cash flow	2.87	3.28	2.02	2.96	2.73	2.62	2.64	2.71
Book value	19.59	17.56	23.89	28.42	23.87	24.06	24.16	24.27
Dividend	0.00	0.00	0.00	0.00	0.60	0.80	0.80	0.80
Income statement ($m)								
Revenues	2,018	2,137	2,093	2,214	2,337	2,394	2,458	2,546
Gross income	726	752	733	785	836	844	854	891
EBITDA	726	752	733	785	834	840	850	887
Depreciation and amortisation	-225	-261	-259	-267	-271	-282	-295	-307
EBIT	501	491	474	517	563	558	555	580
Impairment losses	-79	-385	-222	-509	-750	0	0	0
Net interest income	-305	-336	-362	-271	-264	-312	-324	-337
Exceptional & non-operating items	9	7	0	7	0	0	0	0
Taxation	-65	-49	-46	88	-112	-74	-74	-85
Minority interests	0	0	0	0	0	0	0	0
Reported net income	138	110	66	139	-562	172	158	158
SG adjusted net income	158	137	143	158	176	172	158	158
Cash flow statement ($m)								
EBITDA	726	752	733	785	834	840	850	887
Change in working capital	-37	51	-97	17	-25	-20	-15	-15
Other operating cash movements	-231	-278	-313	-328	-352	-363	-375	-399
Cash flow from operating activities	458	525	324	474	457	458	460	473
Net capital expenditure	-546	-558	-689	-759	-984	-558	-606	-606
Free cash flow	-88	-33	-365	-285	-527	-100	-146	-133
Cash flow from investing activities	22	12	21	10	5	5	5	5
Cash flow from financing activities	74	7	309	259	518	348	348	298
Net change in cash resulting from CF	8	-14	-35	-16	-4	253	207	170
Balance sheet ($m)								
Total long-term assets	11,756	12,104	12,420	12,562	12,388	12,664	12,975	13,275
of which intangible	0	0	0	0	0	0	0	0
Working capital	-207	-105	-23	-99	-39	-36	-32	-27
Employee benefit obligations	300	399	460	449	414	414	414	414
Shareholders' equity	3,134	2,809	3,822	4,547	4,167	4,200	4,217	4,236
Minority interests	0	0	0	0	0	0	0	0
Provisions	0	0	0	0	0	0	0	0
Net debt (-)/cash (+)	-7,048	-6,740	-5,848	-5,003	-5,663	-5,860	-6,102	-6,333
Accounting ratios								
ROIC (%)	na	2.9	2.6	2.6	2.6	2.4	2.4	2.4
ROE (%)	na	3.7	2.0	3.3	-12.9	4.1	3.7	3.7
Gross income/revenues (%)	36.0	35.2	35.0	35.4	35.8	35.3	34.7	35.0
EBITDA margin (%)	36.0	35.2	35.0	35.4	35.7	35.1	34.6	34.8
EBIT margin (%)	24.8	23.0	22.7	23.4	24.1	23.3	22.6	22.8
Revenue yoy growth (%)	na	5.9	-2.1	5.8	5.5	2.4	2.7	3.6
Rev. organic growth (%)	5.0	5.0	5.0	5.8	5.5	2.4	2.7	3.6
EBITDA yoy growth (%)	na	3.6	-2.5	7.0	6.3	0.8	1.1	4.3
EBIT yoy growth (%)	na	-2.0	-3.4	9.1	8.8	-0.8	-0.5	4.4
EPS (adj.) yoy growth (%)	na	-13.3	4.3	10.8	6.7	-6.3	-8.6	0.2
Dividend growth (%)	na	na	na	na	na	33.3	0.0	0.0
Cash conversion (%)	58.5	73.7	9.8	-17.4	-23.1	53.6	47.9	52.2
Net debt/equity (%)	224.9	239.9	153.0	110.0	135.9	139.5	144.7	149.5
FFO/net debt (%)	5.1	5.4	5.6	12.0	8.1	7.8	7.4	7.3
Dividend paid/FCF (%)	nm	nm	nm	nm	nm	nm	nm	nm

*** Valuation ratios for past years are based on average historical prices and market capitalisations**

SOCIETE GENERALE
Cross Asset Research

7 January 2010

Equity

Water Utilities

www.sgresearch.socgen.com

12m target upgrade

A GLOBAL VIEW FROM EUROPE

United States

AMERICAN WATER WORKS

Increasing prospects

Buy (12m)

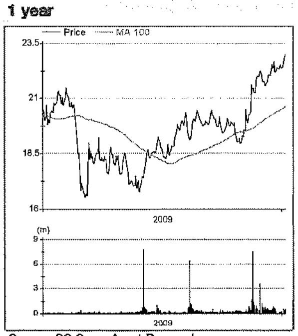
Price 06/01/10	12m target
$23.0	$25.5

Sector
Weighting
Overweight
Preferred stock
Veolia Environnement
Least preferred stock
Scottish & Southern Energy

Type of investment

Value	✓
Investor Day	✓
SG conference	✓

1 year



Source: SG Cross Asset Research

Update At its investors' meeting in New York, the US-based firm gave a presentation on the prospects offered by the North American water market. The US water market was worth an estimated $154bn in 2002, and the Environmental Protection Agency (EPA) now estimates it at $335bn, representing underlying market growth of over 11% per year.

Impact As the leading player with 2009e sales of $2.5bn, American Water Works (AWW) could seize a number of opportunities in this market. AWW is once again totally independent as German firm RWE (Hold, TP €69.3) has definitively exited its share capital, giving it more freedom to focus on three major areas of development: at the organic level, on existing contracts, at the external growth level, on the awarding of new municipal contracts, and lastly, on expanding the non-regulated business, which accounted for 11% of 2008 sales and 5% of EBITDA. The company said that it might tap the market to finance its future growth, but that doing so did not seem necessary in the short term. We have raised our investment spending assumptions for the 2010-13e period to $800m per year, in line with management's projections (vs c.$600m previously). This increases our EPS estimates slightly (+2.6% for 2010/2011e).

Target price & rating TP $25.5 (vs $22.5). Our TP is derived from a DCF. The main changes to the assumptions underpinning our TP include long-term rates, the risk premium and medium-term normalised growth, which we have raised to 5%, from 3.5% previously. The impact of the latter on our valuation is +$2. We have lifted our MT growth assumption due to the water industry's increasing needs and to prevailing economic policies in North America that are more conducive to municipal investments. Consensus ratings on the stock tend to be positive: Buy 75% and Hold 25% (Source: Factset).

Next events & catalysts AWW's management is expected to participate in SG's Utilities conference in Paris on 14 January. We expect the company to continue to expand with a focus on PPPs. This would be perfectly suitable to the market, with American Water bringing optimal management experience to the table and municipalities financing the necessary investments.

Share data			
RIC AWK.N, Bloom AWK US			
52-week range			23.0-16.5
EV 09 ($m)			8,985
Market cap. ($m)			4,014
Free float (%)			100.0
Performance (%)	**1m**	**3m**	**12m**
Ordinary shares	5.5	17.9	12.2
Rel. S&P 500	2.6	9.4	-7.7

Financial data	12/08	12/09e	12/10e	12/11e
Revenues ($bn)	2.34	2.45	2.57	2.69
EBIT margin (%)	24.1	25.5	25.7	26.1
Rep. net inc. ($m)	-562	-235	236	255
EPS (adj.) ($)	1.10	1.29	1.35	1.46
Dividend/share ($)	0.60	0.82	0.84	0.86
Payout (%)	nm	nm	62.1	58.9
Interest cover (x)	2.0	2.2	2.3	2.4
Net debt/equity (%)	128.9	133.3	136.2	137.7
Prev. EPS change (06/01/10)		1.29	1.32	1.42

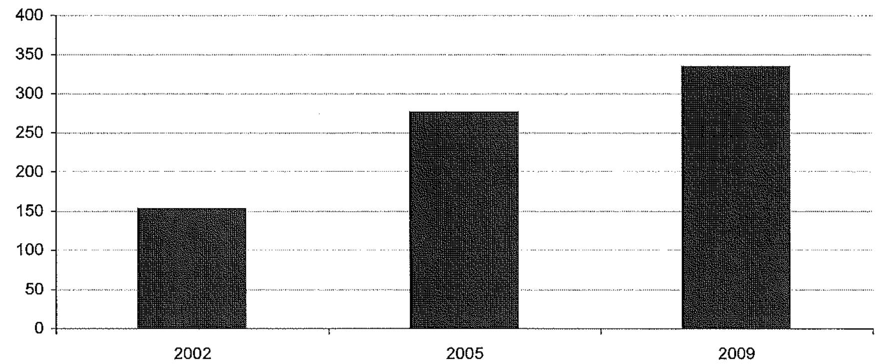
Ratios	12/08	12/09e	12/10e	12/11e
P/E (x)	20.9	17.9	17.0	15.7
FCF yield (/EV) (%)	-0.7	4.5	2.1	2.6
Dividend yield (%)	2.6	3.6	3.7	3.7
Price/book value (x)	0.9	1.1	1.1	1.0
EV/revenues (x)	3.98	3.67	3.59	3.50
EV/EBIT (x)	16.5	14.4	14.0	13.4
EV/IC (x)	0.6	0.6	0.6	0.6
ROIC/WACC (x)	0.5	0.5	0.5	0.5
CAGR 08-11e: +9.9%				


John Honore
(33) 1 42 13 51 55
john.honore@sgcib.com


Thierry Bros
(33) 1 58 98 11 70
thierry.bros@sgcib.com

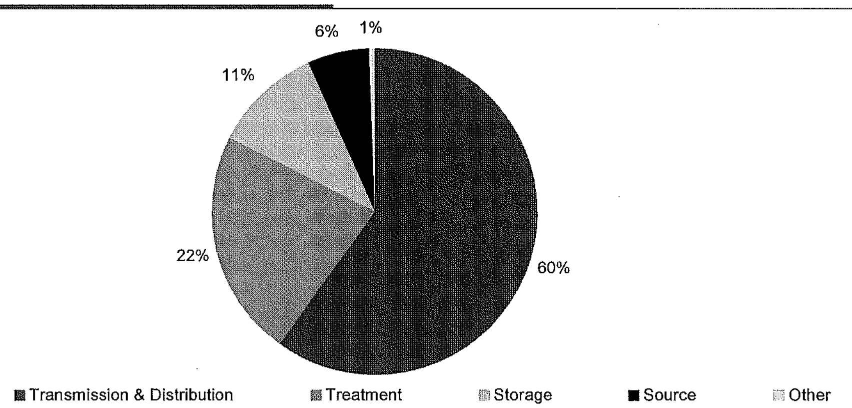

Didier Laurens
(33) 1 42 13 50 78
didier.laurens@sgcib.com

US EPA estimated 20-year total needs of US public water systems



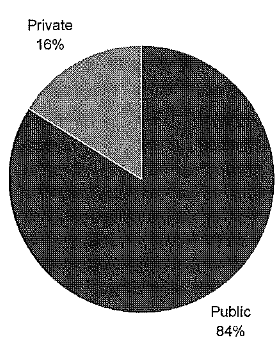
Source: SG Cross Asset Research, American Water, EPA

Breakdown of 2009 US estimated 20-year total needs ($335bn)

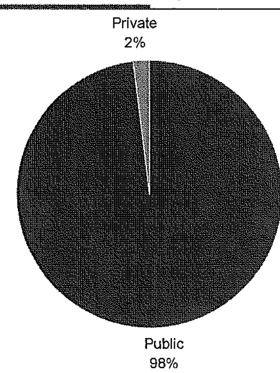


Source: SG Cross Asset Research, American Water, EPA

Water treatment under private management



Wastewater under private management



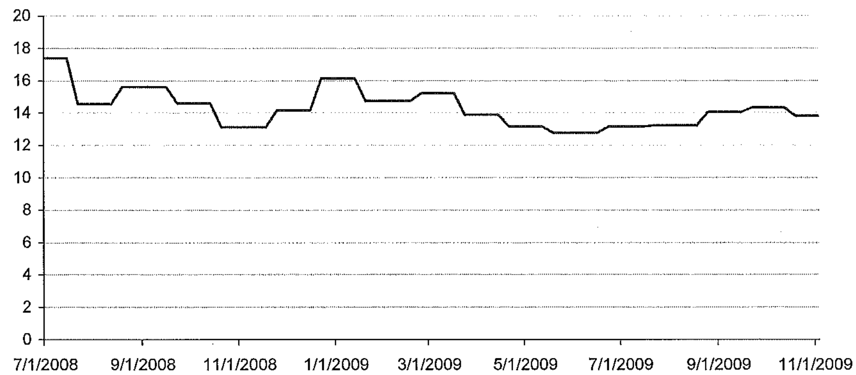
Source: SG Cross Asset Research, American Water, EPA

Change in estimated EPS

$/share	2009e	2010e	2011e	CAGR
New EPS	1.29	1.35	1.46	6.5%
Old EPS	1.29	1.32	1.42	5.0%
Change	0.0%	2.4%	2.9%	

Source: SG Cross Asset Research

12M forward P/E



Source: SG Cross Asset Research, Datastream

IMPORTANT DISCLOSURES

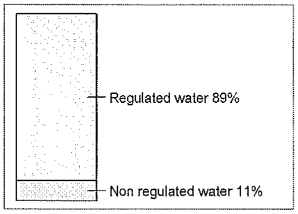
American Water Works	SG acted as co-manager in American Water Works' equity raising.
American Water Works	SG acted as co-manager in the secondary offering of American Water Works shares by RWE
American Water Works	SG acted as co-manager in the secondary offering of American Water Works shares by RWE and in the capital increase of American Water Works.
RWE	SG acted as co-manager in the secondary offering of American Water Works shares by RWE
RWE	SG is one of the Mandated Lead Arranger in the acquisition financing of RWE's bid for Essent
Veolia Environnement	SG is acting as financial advisor to CDC for the merger of Transdev with Veolia Transport.
Veolia Environnement	SG acted as joint bookrunner in the VEOLIA Environnement's senior bond issue.

US THIRD PARTY FOREIGN AFFILIATE RESEARCH DISCLOSURES:

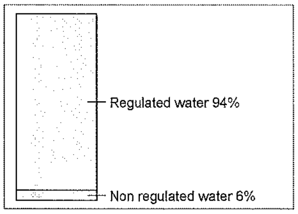
SG and its affiliates beneficially own 1% or more of any class of common equity of Veolia Environnement.
SG or its affiliates act as market maker or liquidity provider in the equities securities of Veolia Environnement.
SG or its affiliates expect to receive or intend to seek compensation for investment banking services in the next 3 months from RWE.
SG or its affiliates expect to receive or intend to seek compensation for investment banking services in the next 3 months from Veolia Environnement.
SG or its affiliates have received compensation for investment banking services in the past 12 months from American Water Works.
SG or its affiliates have received compensation for investment banking services in the past 12 months from RWE.
SG or its affiliates have received compensation for investment banking services in the past 12 months from Veolia Environnement.
SG or its affiliates managed or co-managed in the past 12 months a public offering of securities of American Water Works.
SG or its affiliates managed or co-managed in the past 12 months a public offering of securities of RWE.
SG or its affiliates managed or co-managed in the past 12 months a public offering of securities of Veolia Environnement.

IMPORTANT DISCLAIMER: The information herein is not intended to be an offer to buy or sell, or a solicitation of an offer to buy or sell, any securities and including any expression of opinion, has been obtained from or is based upon sources believed to be reliable but is not guaranteed as to accuracy or completeness although Société Générale ("SG") believe it to be clear, fair and not misleading. SG, and their affiliated companies in the SG Group, may from time to time deal in, profit from the trading of, hold or act as market-makers or act as advisers, brokers or bankers in relation to the securities, or derivatives thereof, of persons, firms or entities mentioned in this document or be represented on the board of such persons, firms or entities. Employees of SG, and their affiliated companies in the SG Group, or individuals connected to then, other than the authors of this report, may from time to time have a position in or be holding any of the investments or related investments mentioned in this document. Each author of this report is not permitted to trade in or hold any of the investments or related investments which are the subject of this document. SG and their affiliated companies in the SG Group are under no obligation to disclose or take account of this document when advising or dealing with or for their customers. The views of SG reflected in this document may change without notice. To the maximum extent possible at law, SG does not accept any liability whatsoever arising from the use of the material or information contained herein. This research document is not intended for use by or targeted at retail customers. Should a retail customer obtain a copy of this report they should not base their investment decisions solely on the basis of this document but must seek independent financial advice.
Important notice: The circumstances in which materials provided by SG Fixed & Forex Research, SG Commodity Research, SG Convertible Research, SG Technical Research and SG Equity Derivatives Research have been produced are such (for example because of reporting or remuneration structures or the physical location of the author of the material) that it is not appropriate to characterise it as independent investment research as referred to in European MIF directive and that it should be treated as a marketing material even if it contains a research recommendation (« recommandation d'investissement à caractère promotionnel »). However, it must be made clear that all publications issued by SG will be clear, fair, and not misleading.
Analyst Certification: Each author of this research report hereby certifies that (i) the views expressed in the research report accurately reflect his or her personal views about any and all of the subject securities or issuers and (ii) no part of his or her compensation was, is, or will be related, directly or indirectly, to the specific recommendations or views expressed in this report.
Notice to French Investors: This publication is issued in France by or through Société Générale ("SG") which is authorised by the CECEI and regulated by the AMF (Autorité des Marchés Financiers).
Notice to UK investors: This publication is issued in the United Kingdom by or through Société Générale ("SG") London Branch which is regulated by the Financial Services Authority ("FSA") for the conduct of its UK business.
Notice To US Investors: This report is intended only for major US institutional investors pursuant to SEC Rule 15a-6. Any US person wishing to discuss this report or effect transactions in any security discussed herein should do so with or through SG Americas Securities, LLC ("SGAS") 1221 Avenue of the Americas, New York, NY 10020. (212)-278-6000. THIS RESEARCH REPORT IS PRODUCED BY SOCIETE GENERALE AND NOT SGAS.
Notice to Japanese Investors: This report is distributed in Japan by Société Générale Securities (North Pacific) Ltd., Tokyo Branch, which is regulated by the Financial Services Agency of Japan. The products mentioned in this report may not be eligible for sale in Japan and they may not be suitable for all types of investors.
Notice to Australian Investors: Société Générale Australia Branch (ABN 71 092 516 286) (SG) takes responsibility for publishing this document. SG holds an AFSL no. 236651 issued under the Corporations Act 2001 (Cth) ("Act"). The information contained in this newsletter is only directed to recipients who are wholesale clients as defined under the Act.
IMPORTANT DISCLOSURES: Please refer to our website: http://www.sgresearch.socgen.com

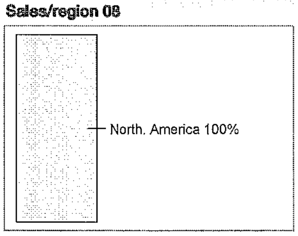
Sales/division 08



EBIT/division 08



Sales/region 08



Major shareholders (%)

RWE	23.5

Normalised data

EBITDA margin (%)	42.0
Normalised growth (%)	0.1

We have increased our investment expectations from $600m pa to $800m pa as stated by the management at investors' day.

Debt should increase as the company is overinvesting in our view, but gearing should remain below 140% on our estimates.

Water Utilities (United States) — Price (06/01/10) $23.0 — 12m target $25.5

American Water Works — BUY

Valuation* ($m)	12/04	12/05	12/06	12/07	12/08	12/09e	12/10e	12/11e
Nb. of shares basic year end/outstanding	160.0	160.0	160.0	160.0	160.0	174.5	174.5	174.5
Share price (average)					20.68	19.50	23.00	23.00
Average market cap. (SG adjusted) (1)	0	0	0	0	3,308	3,404	4,014	4,014
Restated net debt (-)/cash (+) (2)	-7,048	-6,740	-5,848	-5,003	-5,294	-4,971	-5,202	-5,402
Value of minorities (3)	0	0	0	0	0	0	0	0
Value of financial investments (4)	0	0	0	0	0	0	0	0
Other adjustment (5)	0	0	0	0	0	0	0	0
EV = (1) - (2) + (3) - (4) + (5)	na	na	na	na	8,602	8,375	9,216	9,416
P/E (x)	na	na	na	na	18.8	15.1	17.0	15.7
Price/cash flow (x)	na	na	na	na	5.0	4.9	5.6	5.4
Price/free cash flow (x)	nm	nm	nm	nm	nm	29.0	nm	nm
Price/book value (x)	na	na	na	na	0.8	0.9	1.1	1.0
EV/revenues (x)	na	na	na	na	3.68	3.42	3.59	3.50
EV/EBITDA (x)	na	na	na	na	10.3	9.2	9.6	9.3
Dividend yield (%)	na	na	na	na	2.9	4.2	3.7	3.7
Per share data ($)								
SG EPS (adj.)	0.98	0.85	0.89	0.99	1.10	1.29	1.35	1.46
Cash flow	2.87	3.28	2.02	2.96	4.11	4.01	4.08	4.28
Book value	19.59	17.56	23.89	28.42	25.67	21.37	21.88	22.48
Dividend	0.00	0.00	0.00	0.00	0.60	0.82	0.84	0.86
Income statement ($m)								
Revenues	2,018	2,137	2,093	2,214	2,337	2,451	2,568	2,694
Gross income	726	752	733	785	834	910	961	1,021
EBITDA	726	752	733	785	834	906	957	1,017
Depreciation and amortisation	-225	-261	-259	-267	-271	-282	-298	-314
EBIT	501	491	474	517	563	624	659	703
Impairment losses	-79	-385	-222	-509	-750	-450	0	0
Net interest income	-305	-336	-362	-271	-264	-271	-266	-278
Exceptional & non-operating items	9	7	0	7	0	0	0	0
Taxation	-65	-49	-46	88	-112	-137	-157	-170
Minority interests	0	0	0	0	0	0	0	0
Reported net income	138	110	66	139	-562	-235	236	255
SG adjusted net income	158	137	143	158	176	215	236	255
Cash flow statement ($m)								
EBITDA	726	752	733	785	834	906	957	1,017
Change in working capital	-37	51	-97	17	6	-20	-15	-15
Other operating cash movements	-231	-278	-313	-328	-182	-216	-230	-255
Cash flow from operating activities	458	525	324	474	658	671	712	747
Net capital expenditure	-546	-558	-689	-759	-1,009	-558	-800	-800
Free cash flow	-88	-33	-365	-285	-351	113	-88	-53
Cash flow from investing activities	22	12	21	10	0	5	5	5
Cash flow from financing activities	74	7	309	259	452	547	302	248
Net change in cash resulting from CF	8	-14	-35	-16	101	665	219	200
Balance sheet ($m)								
Total long-term assets	11,756	12,104	12,420	12,562	12,859	12,685	13,186	13,672
of which intangible	0	0	0	0	0	0	0	0
Working capital	-207	-105	-23	-99	-87	-80	-74	-66
Employee benefit obligations	300	399	460	449	743	743	743	743
Shareholders' equity	3,134	2,809	3,822	4,547	4,107	3,729	3,818	3,923
Minority interests	0	0	0	0	0	0	0	0
Provisions	0	0	0	0	0	0	0	0
Net debt (-)/cash (+)	-7,048	-6,740	-5,848	-5,003	-5,294	-4,971	-5,202	-5,402
Accounting ratios								
ROIC (%)	na	2.9	2.6	2.6	2.6	2.7	2.7	2.8
ROE (%)	na	3.7	2.0	3.3	-13.0	-6.0	6.3	6.6
Gross income/revenues (%)	36.0	35.2	35.0	35.4	35.7	37.1	37.4	37.9
EBITDA margin (%)	36.0	35.2	35.0	35.4	35.7	37.0	37.3	37.8
EBIT margin (%)	24.8	23.0	22.7	23.4	24.1	25.5	25.7	26.1
Revenue yoy growth (%)	na	5.9	-2.1	5.8	5.5	4.9	4.8	4.9
Rev. organic growth (%)	5.0	5.0	5.0	5.8	5.5	4.9	4.8	4.9
EBITDA yoy growth (%)	na	3.6	-2.5	7.0	6.3	8.7	5.6	6.2
EBIT yoy growth (%)	na	-2.0	-3.4	9.1	8.8	10.8	5.6	6.6
EPS (adj.) yoy growth (%)	na	-13.3	4.3	10.8	11.6	16.9	5.0	8.0
Dividend growth (%)	na	na	na	na	na	36.7	2.4	2.4
Cash conversion (%)	58.5	73.7	9.8	-17.4	8.1	86.5	53.8	58.9
Net debt/equity (%)	224.9	239.9	153.0	110.0	128.9	133.3	136.2	137.7
FFO/net debt (%)	5.1	5.4	5.6	12.0	8.7	10.0	10.3	10.5
Dividend paid/FCF (%)	nm	nm	nm	nm	nm	127.0	nm	nm

*** Valuation ratios for past years are based on average historical prices and market capitalisations**

STURDIVANT & CO.

Mid-Atlantic Institutional Research

American Water Works Co., Inc. (NYSE: AWK - $18.16)
Reports Strong Q1 Results.....Bulls on Parade

May 7, 2009

Richard A. Verdi
(856) 751-1331 x109
rverdi@sturdivant-co.com

Long Term Rating: Market Outperform
Long Term Target Price: $26

Investment Summary: *Our bullish outlook continued its stampede this quarter as American Water crushed our earnings estimate. The company reported robust bottom-line results in a weak economic climate as a result of operating income upside. Revenue was essentially in-line with our estimate confirming our thesis that the company's healthy pipeline of rate case relief should come to fruition and in our view, drive earnings growth over the coming years. We believe American Water is a good defensive stock market recovery play. With the shares down approximately 13% year-to-date and lagging the S&P 500 which is up approximately 1.0% for 2009, we believe the stock should outperform relative to the market given AWK's more predictable revenue stream. If any rally in the market turns south, we believe the stock's defensive style should help it outperform the broad market on the downside. As such, we recommend investors accumulate shares at current trading levels and for new investors to establish core positions now. Reiterate Market Outperform and raise target by $1 to $26. Upside to price target—approximately 40%.*

Key Points

- **Earnings results crushed our estimate.** American Water Works reported first quarter diluted EPS on a non-GAAP basis of $0.19, $0.09 higher than our estimate. Earnings outperformance was driven by better than expected operating income.

- **Operating margin was well ahead of our estimate and led to earnings upside.** Revenue was essentially in-line with our forecast. The company reported sales of $550.2 million, our projection was $1.2 million higher. EBITDA margin of 33.3% was up a whopping 500 basis points yr/yr—well ahead of our estimate of 31.9%. The margin beat reflected lower than estimated operating and maintenance expenses. General taxes were $2.5 million above our estimate of $50.0 million.

- **In April, the company filed rate requests seeking more than $115 million—supporting growth through 2010.** Continuing its momentum from 2008, AWK filed for approximately $118 million in rate case relief in April 2009. By our estimates, this should add approximately $67 million in revenue on top of our 2009 sales estimate—providing for a more predictable earnings outlook in 2010. We believe the rate case relief will come to fruition 9-12 months after the filings and we assume a 57% success rate.

- **We remain bullish on the company and were pleased with results.** We believe the near– and medium-term outlook for American Water appears to be stable given its current pipeline of rate case relief requests and our conservative operating expense forecast. In the long-run, it appears as though business is firming up with the company's recent rate case relief announcement.

- **Reiterate Market Outperform and lifting one-year price target to $26.** We are reiterating our Market Outperform rating on American Water. AWK reported robust first quarter earnings well ahead of our estimates in a challenging environment. We believe the stage is set for continued earnings growth and believe stock price appreciation should follow. Our price target is based on the stock trading at 18.5x our forward four-quarter diluted EPS estimate of $1.39. Risks to achieving our price target include: regulatory lag, unfavorable weather conditions, declining water usage and acquisition risk. If the company is able to overcome one or all of these issues, it may provide a catalyst for the stock.

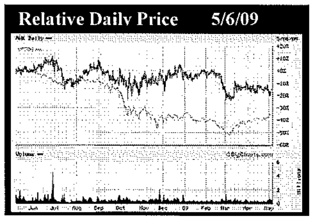
Share Information	
Price 5/6	$18.16
52 Wk Lo-Hi	$16.22-$23.65
Div Yield	4.50%
Avg. Volume	404,968
Insiders Own	60.5%
S&P 500	919.53

Financial Statistics	
Equity Mkt. Cap.	$2.9B
'08 LTD/Cap.	53.1%
Ent. Value	$8.2B
10 Yr. Treasury	3.15%
'08 FCF Yield	N/A

EPS	EPS	P/E
2007A	-	-
2008A	$1.10	16.5x
2009E	$1.38	13.2x
2010E	$1.56	11.6x

EBITDA	EBITDA	EV/ EBITDA
2007A	-	-
2008A	$0.8B	10.3x
2009E	$1.0B	8.5x
2010E	$1.0B	7.9x

Relative Daily Price 5/6/09



Source: BigCharts, Company Reports and Sturdivant & Co. Estimates.

Additional Discussion

Quarterly Earnings Review

American Water reported first quarter revenue increased 8.6% yr/yr to $550.2 million compared to $506.8 million a year ago—our estimate was $551.2 million. On a segment basis, Regulated Business revenue increased by $47.8 million primarily as a result of rate case awards, but was also fueled slightly by organic growth and tuck-in acquisitions. We found comfort in the quarter due to the rate case relief which confirmed our thesis. Turning the to the company's other segment, AWK's Non-Regulated Business revenue declined by $3.6 million as the company is prudently selecting appropriate O&M contracts. Companywide water sales volume did fall yr/yr by 3 billion gallons or 3.5%. Dissecting it further, residential, commercial and industrial volumes decreased 1.5%, 3.6% and 12.9%, respectively. We are not concerned with the volume shortfall since we have already modeled for decreased consumption.

Non-GAAP operating expenses rose $8.4 million or 2.0% yr/yr to $435.5 million, we estimated $449.0 million. OpEx for the company's Regulated Business was $12.0 million higher than Q108's $378.0 million. Non-Regulated OpEx fell $3.6 million due to decreased business and cost control. Making up the lion's share of OpEx, employee-related expenses increased approximately $6.0 million. The main driver was pension expense. While alarming at first glance, American Water and other utilities have begun discussions with regulators about the appropriate treatment for these costs in order to minimize regulatory lag between incurring expenses and any recovery of the cost. Operating income was $114.6 million and pre-tax margin was 8.6%, our estimate was 4.8%. AWK's first quarter tax rate was 36.9% and on the bottom-line, American Water earned $0.19 per diluted share—$0.09 ahead of our estimate.

Industry Outlook

Our outlook for the water utility industry over the short-term is positive. We expect investors to build positions in water utilities (investor-owned utilities or IOUs) because of their predictable earnings, defensive style and attractive dividends. Over the medium- to long-term we are bullish on the space. In our view, the aging water and wastewater infrastructure in the United States needs modernization/replacement and will require water utilities to invest in infrastructure. Rate hikes should follow translating into top- and bottom-line growth. In addition, we expect water utilities to benefit from acquisitions despite the weak economy and the housing slowdown. The majority of water systems are owned by municipalities, that have less tax revenue to finance infrastructure projects, and therefore they may sell their systems to IOUs, thus allowing water utilities to grow their customer base.

Earnings Outlook

As a result of the first quarter upside, we are raising our 2009 diluted EPS forecast to $1.38 from $1.33. The remaining 2009 assumptions are essentially unchanged. For the year, we estimate revenue of $2.5 billion or 8.7% higher yr/yr. Our sales forecast is predicated on American Water receiving approximately $186.0 million in revenue from rate case relief. In addition, we estimate the company to receive $9.0 million in acquisition revenue and $9.0 million from its Non-Regulated segment. Our O&M expense for 2009 is $1.4 billion or 4.0% higher than 2008. The rise in the line-item is based on normal increased expenses attributable to growth throughout the company. We are forecasting depreciation and amortization expense to be approximately $295.0 million and we project the company to pay approximately $200.0 million in general taxes leading to our operating margin forecast of 26.7%, 260 basis points higher than 2008. Below the line, we estimate pre-tax margin to be 15.3% and our tax rate is 39.6%.

Figure 1: Valuation Analysis

P/E Multiple	Fwd 4 Qtr EPS	Implied Share Price	Price as of 5/6/2009	Upside
18.5x	$1.39	$26	$18.16	41%

EV/EBITDA Multiple	Fwd 4 Qtr EBITDA	Enterprise Value	Net Debt	Market Capitalization	Implied Share Price	Price as of 5/6/2009	Upside
9.5x	$995,026	$9,452,752	$4,675,443	$4,777,309	$26	$18.16	45%

Source: Sturdivant & Company Equity Research

Conclusion and Recommendation

We believe American Water Works is a desirable investment due to its stable and predictable top-line growth, steadily expanding customer base, diverse geographic footprint, strong management team and its current valuation. In our view, American Water Works has the potential to experience near- and long-term price appreciation as the company's rate case filings come to fruition and AWK grows its rate base.

We believe AWK should be appointed an 18.5x P/E multiple that when applied to our forward four-quarter earnings estimate of $1.39 generates a price target of $26. There could be upside to our target if American Water Works is awarded additional rate case relief above our estimates. Furthermore, we believe the company has the potential to experience long-term price appreciation as Wall Street recognizes the growth potential in the water sector and the company exploits its potential for growth.

We are reiterating our Market Outperform rating and raising our price target to $26. We advise investors to establish core positions now.

Investment Thesis

American Water is a geographically diverse water utility company that capitalizes on its top-notch earnings growth strategy. We consider AWK to be one of the more compelling stocks in the water space based on its highly predictable earnings and a valuation below its peers. In our view, American Water is positioned to benefit from a substantial pipeline of rate case relief. Furthermore, the company is positioned to benefit from strong customer growth and acquisitions. With a weak U.S. economy, we recommend companies with favorable government mandates/regulations, a significant position in its respective area and a strong track record – in our view, American Water Works satisfies these requirements. We reiterate our Market Outperform rating and raise our price target to $26.

Investment Risks

If the company experiences any or all of the following risk factors, as well as others, the company's stock price may be affected.

- American Water's utility operations are heavily regulated. Decisions by state PUCs and other regulatory agencies can significantly affect the company's business and results of operations.
- AWK's operations and quality of water they provide are subject to environmental laws and regulations.
- Changes in laws and regulations can significantly effect American Water's business and financial results.
- Weather conditions, natural hazards, availability of water supplies and competing uses may interfere with the company's sources of water, demand of water services and AWK's ability to supply water to customers.
- Declining residential per customer water usage may reduce the company's revenue, financial condition and results of operations.

Figure 2: Comparable Companies

Comparable Companies

				Revenue & Valuation Measures			Trading Multiples		
Company Name	Ticker	Stock Price 5/6/09	Period Date	Revenue LTM	Market Cap	Enterprise Value	TEV/Rev LTM	TEV/EBITDA LTM	P/E LTM
American Water Works Compan	**AWK**	**18.16**	**12/31/2008**	**2,336.9**	**2,906.2**	**8,204.0**	**3.5x**	**9.8x**	**NM**
Aqua America Inc.	WTR	18.24	12/31/2008	627.0	2,474.2	3,797.4	6.1x	12.1x	25.1x
Artesian Resources Corp.	ARTN.A	14.25	12/31/2008	56.2	105.6	232.9	4.1x	10.5x	16.5x
California Water Service Group	CWT	36.80	3/31/2009	424.0	763.4	1,100.2	2.6x	8.9x	18.3x
Consolidated Water Co. Ltd.	CWCO	13.00	12/31/2008	65.7	188.9	177.0	2.7x	12.3x	26.2x
Middlesex Water Co.	MSEX	14.21	12/31/2008	91.0	190.7	352.8	3.9x	10.8x	15.9x
Pennichuck Corp.	PNNW	20.95	12/31/2008	31.0	89.1	154.3	5.0x	10.3x	18.9x
York Water Co.	YORW	14.11	12/31/2008	32.8	160.5	252.8	7.7x	13.8x	24.8x
Max							*7.7x*	*13.8x*	*26.2x*
Median							*4.0x*	*10.7x*	*18.9x*
Min							*2.6x*	*8.9x*	*15.9x*
Mean							*4.4x*	*11.1x*	*20.8x*

				Operating Stats (%)			Returns (%)		
Company Name	Ticker	Stock Price 5/6/09	Period Date	Gross Margin LTM	EBIT LTM	EBITDA LTM	ROA LTM	ROE LTM	ROIC LTM
American Water Works Compan	**AWK**	**18.16**	**12/31/2008**	**45.2**	**24.1**	**35.7**	**2.7**	**-13.0**	**3.7**
Aqua America Inc.	WTR	18.24	12/31/2008	58.2	36.0	50.2	4.2	9.6	6.0
Artesian Resources Corp.	ARTN.A	14.25	12/31/2008	45.1	29.1	39.4	3.2	7.4	5.1
California Water Service Group	CWT	36.80	3/31/2009	62.1	19.8	29.2	4.0	10.7	7.3
Consolidated Water Co. Ltd.	CWCO	13.00	12/31/2008	28.7	15.4	25.4	4.2	6.0	4.4
Middlesex Water Co.	MSEX	14.21	12/31/2008	46.3	26.4	35.8	3.6	8.8	5.2
Pennichuck Corp.	PNNW	20.95	12/31/2008	33.4	23.9	37.5	2.7	10.1	4.1
York Water Co.	YORW	14.11	12/31/2008	79.4	44.9	55.9	4.1	9.4	6.1
Max				*79.4*	*44.9*	*55.9*	*4.21*	*10.74*	*7.32*
Median				*45.7*	*25.2*	*36.6*	*3.81*	*9.08*	*5.15*
Min				*28.7*	*15.4*	*25.4*	*2.69*	*-13.01*	*3.71*
Mean				*49.8*	*27.4*	*38.6*	*3.58*	*6.13*	*5.24*

Source: Capital IQ

Figure 3: Income Statement

American Water Works Company, Inc. (AWK)
Income Statement
(Non-GAAP)
(in millions except per share data)

Sturdivant & Co.
Richard Verdi; 856.751.1331

December Fiscal Year	FY 2008					FY 2009					FY 2010
	1Q08	**2Q08**	**3Q08**	**4Q08**	**Year**	**1Q09**	**2Q09E**	**3Q09E**	**4Q09E**	**Year**	**Year**
Revenue	**$506.8**	**$589.4**	**$672.2**	**$568.6**	**$2,336.9**	**$550.2**	**$618.8**	**$729.3**	**$642.5**	**$2,540.8**	**$2,678.6**
Operating & Maintenance	311.3	330.6	342.2	319.7	1303.8	314.4	347.1	359.3	335.7	1356.6	1424.4
Depreciation & amortization	63.9	67.3	68.4	71.7	271.3	68.8	75.0	75.0	75.0	293.8	300.0
General taxes	52.1	49.6	49.4	48.1	199.1	52.5	53.0	53.0	53.0	211.5	212.0
Loss (gain) on sales of assets	(0.1)	(0.8)	0.5	0.0	(0.4)	(0.2)	0.0	0.0	0.0	(0.2)	0.0
Impairment charges	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Operating Income	**79.6**	**142.7**	**211.8**	**129.1**	**563.1**	**114.6**	**143.7**	**242.0**	**178.7**	**679.1**	**742.2**
Interest Expense, Net	(70.0)	(70.1)	(72.7)	(72.4)	(285.2)	(72.0)	(78.0)	(78.0)	(78.0)	(306.0)	(280.0)
Allowance for other funds used during construction	2.5	3.4	4.4	4.1	14.5	3.3	3.4	3.4	3.4	13.4	13.4
Allowance for borrowed funds used during construction	1.4	1.7	3.0	2.1	8.2	1.9	1.9	1.9	1.9	7.4	7.4
Amortization of debt expense	(1.3)	(1.4)	(1.6)	(1.5)	(5.9)	(1.5)	(1.5)	(1.5)	(1.5)	(6.0)	(6.0)
Preferred dividends of subsidiaries	(0.1)	(0.1)	(0.1)	(0.1)	(0.2)	0.0	0.0	0.0	0.0	0.0	0.0
Other, net	1.2	(0.5)	0.9	3.4	4.9	1.1	0.0	0.0	0.0	1.1	0.0
Income Before Taxes	13.4	75.7	145.7	64.6	299.4	47.5	69.4	167.7	104.4	389.1	477.0
Income Taxes	7.4	30.2	57.5	28.2	123.4	17.5	27.8	67.1	41.8	154.2	190.8
Net Income	**6.0**	**45.5**	**88.2**	**36.4**	**176.1**	**29.9**	**41.7**	**100.6**	**62.7**	**234.9**	**286.2**
Diluted EPS	**$0.04**	**$0.28**	**$0.55**	**$0.23**	**$1.10**	**$0.19**	**$0.25**	**$0.58**	**$0.35**	**$1.38**	**$1.56**
Diluted Shares Outstanding	160.0	160.0	160.0	160.0	160.0	160.0	167.0	174.0	181.0	170.5	183.5
Margin Analysis											
Operating & Maintenance	61.4%	56.1%	50.9%	56.2%	55.8%	57.1%	56.1%	49.3%	52.3%	53.4%	53.2%
Depreciation & amortization	12.6%	11.4%	10.2%	12.6%	11.6%	12.5%	12.1%	10.3%	11.7%	11.6%	11.2%
General taxes	10.3%	8.4%	7.3%	8.5%	8.5%	9.5%	8.6%	7.3%	8.2%	8.3%	7.9%
Operating Income	15.7%	24.2%	31.5%	22.7%	24.1%	20.8%	23.2%	33.2%	27.8%	26.7%	27.7%
Income Before Taxes	2.6%	12.8%	21.7%	11.4%	12.8%	8.6%	11.2%	23.0%	16.3%	15.3%	17.8%
Income Taxes	55.3%	39.9%	39.5%	43.7%	41.2%	36.9%	40.0%	40.0%	40.0%	39.6%	40.0%
Net Income	1.2%	7.7%	13.1%	6.4%	7.5%	5.4%	6.7%	13.8%	9.8%	9.2%	10.7%
Growth Rates yr/yr											
Revenue	-	-	-	-	5.5%	8.6%	5.0%	8.5%	13.0%	8.7%	5.4%
Operating Income	-	-	-	-	3622.0%	43.9%	0.8%	14.3%	38.5%	20.6%	9.3%
Income Before Taxes	-	-	-	-	-217.2%	254.0%	-8.2%	15.1%	61.6%	29.9%	22.6%
Net Income	-	-	-	-	-151.4%	399.8%	-8.4%	14.1%	72.1%	33.4%	21.9%
Diluted EPS	-	-	-	-	-151.4%	399.8%	-12.3%	4.9%	52.2%	25.2%	13.0%

Source: Company Reports, Sturdivant & Co. Estimates

Figure 4: Key Ratios

American Water Works Company, Inc. (NYSE:AWK)
Key Ratios

	Dec-31-2002	Dec-31-2004	Dec-31-2005	Dec-31-2006	Dec-31-2007	Dec-31-2008
Profitability						
Return on Assets %	3.6%	NA	NA	2.3%	2.5%	2.7%
Return on Capital %	4.8%	NA	NA	3.1%	3.4%	3.7%
Return on Equity %	8.1%	NA	NA	(3.1%)	(6.8%)	(13.0%)
Margin Analysis						
Gross Margin %	45.9%	46.0%	45.4%	44.8%	44.7%	45.2%
SG&A Margin %	NA	1.6%	1.6%	0.9%	1.0%	1.0%
EBITDA Margin %	37.7%	36.0%	35.2%	35.0%	35.4%	35.7%
EBIT Margin %	24.3%	24.8%	24.0%	22.7%	23.4%	24.1%
Net Income Margin %	8.6%	(3.2%)	(15.2%)	(7.8%)	(15.5%)	(24.1%)
Short Term Liquidity						
Current Ratio	0.4x	NA	0.2x	0.3x	0.6x	0.4x
Quick Ratio	0.4x	NA	0.2x	0.2x	0.5x	0.3x
Long Term Solvency						
Total Debt/Equity	225.5%	NA	109.8%	73.7%	109.9%	128.7%
Total Debt/Capital	68.9%	NA	52.3%	42.3%	52.2%	56.1%
LT Debt/Equity	192.6%	NA	65.8%	55.6%	102.9%	112.7%
LT Debt/Capital	58.8%	NA	31.3%	31.9%	48.9%	49.1%
Total Liabilities/Total Assets	76.7%	NA	63.5%	56.5%	64.9%	69.0%
EBITDA / Interest Exp.	2.8x	2.3x	2.1x	1.9x	2.5x	2.8x
(EBITDA-CAPEX) / Interest Exp.	0.9x	0.6x	0.6x	0.1x	0.1x	NM
Total Debt/EBITDA	6.3x	NA	6.7x	5.6x	6.4x	6.3x
Net Debt/EBITDA	6.2x	NA	6.6x	5.6x	6.3x	6.3x
Total Debt/(EBITDA-CAPEX)	20.3x	NA	25.2x	81.1x	148.2x	NM
Net Debt/(EBITDA-CAPEX)	20.2x	NA	24.9x	80.5x	147.8x	NM
Growth Over Prior Year						
Total Revenue	19.2%	NA	5.9%	(2.0%)	5.8%	5.5%
Gross Profit	1.8%	NA	4.6%	(3.4%)	5.6%	6.7%
EBITDA	0.3%	NA	3.6%	(2.4%)	7.0%	6.3%
EBIT	(9.3%)	NA	2.3%	(7.4%)	9.0%	8.8%
Earnings from Cont. Ops.	(10.6%)	NA	NM	NM	NM	NM
Net Income	(8.9%)	NA	NM	NM	NM	NM
Diluted EPS before Extra	(11.0%)	NA	NM	NM	NM	NM

Source: Capital IQ

Sturdivant & Co.'s
Businessman's Approach to Value Philosophy

Sturdivant & Co. uses the businessman's approach to evaluating stocks. This philosophy is predicated on looking at a company as a prudent man would were he to consider making a reasoned investment in a business. We focus on a company's strategy, the competitive position a company has versus its peers, quality of management, risk factors, its prospect for growth, as well as critical catalysts and milestones as evidence of progress. Finally, of course, we look at a company's valuation to determine where we feel the stock is priced attractively.

Chairman

Albert A. Sturdivant
Asturdivant@sturdivant-co.com
856-751-1331 *ext.* 108

Fundamental Research

Richard A. Verdi
Rverdi@sturdivant-co.com
856-751-1331 *ext.* 109
Industrials
Utilities

Beth Ann Loewy, CFA
Bloewy@sturdivant-co.com
856-751-1331 *ext.* 114
Food
Consumer Staples
Retail

Brian Bolan
Bbolan@sturdivant-co.com
312-345-1534
Technology

Institutional Sales

Carl R. Gibbs, Jr.
Cgibbs@sturdivant-co.com
856-751-1331 *ext.* 107

Terry Williams
Twilliams@sturdivant-co.com
856-751-1331 *ext.* 101

Institutional Trading

Harvey R. de Krafft
Hdekrafft@sturdivant-co.com
800-486-1515 or
856-751-1331 *ext.* 112

Debra L. Bailey
Dbailey@sturdivant-co.com
800-486-1515 or
856-751-1331 *ext.* 110

James Campanella
Jcampanella@sturdivant-co.com
800-486-1515 or
856-751-1331 *ext.* 115

	Date	Price	Rating	Target
AWK	10/15/08	$18.10	Market Outperform	$25.00
	11/06/08	$18.93	Market Outperform	$25.00
	03/24/09	$18.09	Market Outperform	$25.00
	05/06/09	$18.16	Market Outperform	$26.00

Total Industrial Group

Outperform	Marketperform	Underperform
60% (6)	40% (4)	0

Investment Banking Relationship

Outperform	Marketperform	Underperform
0%	0%	0%

US - Industrial Services and Utilities

Investment Rating	Company	Ticker Symbol	Initial Coverage Date	Research Analyst
Market Outperform				
	American Water Works	AWK	10/16/2008	Richard Verdi
	Aqua America, Inc.	WTR	6/25/2008	Richard Verdi
	Artesian Resources Corp.	ARTNA	2/11/2009	Richard Verdi
	Met-Pro Corp.	MPR	5/29/2007	Richard Verdi
	Middlesex Water Co.	MSEX	1/29/2009	Richard Verdi
	Tyco International Ltd.	TYC	1/29/2009	Richard Verdi
Market Perform				
	Ametek, Inc.	AME	3/26/2008	Richard Verdi
	Badger Meter	BMI	7/11/2007	Richard Verdi
	Echelon Corp.	ELON	12/6/2007	Richard Verdi
	Itron Inc.	ITRI	9/13/2007	Richard Verdi
Market Underperform				
	N/A			

Member: FINRA and SIPC

STURDIVANT & CO.

Mid-Atlantic Institutional Research

American Water Works Co., Inc. (NYSE: AWK - $20.00)

Strong Q2 Results. Well-Positioned in '09 & Stage is Set for '10
Reiterate Market Outperform

August 6, 2009

Richard A. Verdi
(856) 751-1331 x109
rverdi@sturdivant-co.com

Long Term Rating: Market Outperform
Long Term Target Price: $27

Investment Summary: *American Water reported another strong quarter confirming our view that the company not only has water running through its pipes, but it also has bulls. AWK reported Q2 results well ahead of our estimate despite unfavorable weather during the quarter and the challenging economic environment. Although the economic downturn is negatively impacting the top-line, the company is still producing solid revenue growth as a result of rate relief and its maintaining its margins due to improved cost control which was evident in the quarter. Trading at 13.9x our forward four-quarter diluted EPS estimate of $1.44, we believe the shares represent a compelling entry level for investors. We are reiterating our Market Outperform rating on the stock and lifting our one-year price target of $27.*

Key Points

- **Blow-out quarter.** American Water beat our estimate once again on solid revenue growth and firm cost control. Diluted earnings on a non-GAAP basis were $0.32 versus our estimate of $0.25. Revenue of $612.7 million was slightly lower than our estimate of $618.8 million which was not surprising due to the unusually wet weather in the Mid-Atlantic region during the second quarter. Weather negatively impacted the top-line by $24.0 million and cost the company $0.08 per diluted shares on the bottom-line. Operating and maintenance expense (O&M) of $330.6 million was well below our forecast of $347.1 million - O&M growth was flat yr/yr. Other line-items on the P&L were all generally in-line with our estimates. In our view, it appears that the company continues to execute well through the downturn of the economy.
- **Revenue remains solid and the outlook is bullish.** Overall Q2 revenue growth of $23.3 million was fueled by rate relief. The increase in revenue due to rate authorizations in the quarter was $46.5 million. Surcharges and balancing accounts contributed $1.4 million. Acquisitions increased sales by $1.6 million. Offsetting the growth, a drop in water consumption decreased the top-line by $24.0 million and a decrease in the Contract Operations group caused revenue to drop by $3.0 million. During the quarter, AWK received authorizations for additional annualized revenue from general rate cases of $12.5 million, this brings the total 1H09 to $17.7 million. The company also filed rate applications during the quarter in Indiana, Iowa, Ohio, Pennsylvania, Maryland and Illinois, requesting approximately $182.6 million in increased annualized revenue.
- **Reiterate Market Outperform.** American Water remains one of our top picks under of coverage umbrella. We expect the company to continue to deliver on both the top– and bottom-lines due its rate relief which should result in stock price appreciation. Additionally, as RWE continues to divest its AWK shares and the smoke clears from the overhang associated with RWE ownership, the stock should benefit from multiple expansion. On that note, our view is that the 2010 stage is set for growth in American Water stock. For 2009, we are adjusting our diluted earnings estimate on a non-GAAP basis downward to $1.31 from $1.38 and we are increasing our 2010 estimate to $1.58 from $1.56. The majority of the changes to our estimates reflect our updated rate relief revenue model. We have also adjusted our O&M expense estimate to more accurately reflect historic and current trends. Previously we modeled 5.0% yr/yr growth in the line-item, we believe 3.75% yr/yr growth is more appropriate - in our view, our prior O&M estimates were too conservative. Our price target is now $27.

Share Information

Price 8/5	$20.00
52 Wk Lo-Hi	$16.22-$23.12
Div Yield	4.00%
Avg. Volume	1,121,360
Insiders Own	55.5%
S&P 500	1,002.72

Financial Statistics

Equity Mkt. Cap.	$3.1B
'08 LTD/Cap.	53.1%
Ent. Value	$8.6B
10 Yr. Treasury	3.76%
'08 FCF Yield	N/A

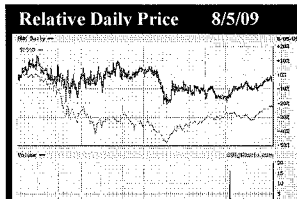
EPS

	EPS	P/E
2007A	-	-
2008A	$1.10	18.2x
2009E	$1.31	15.3x
2010E	$1.58	12.7x

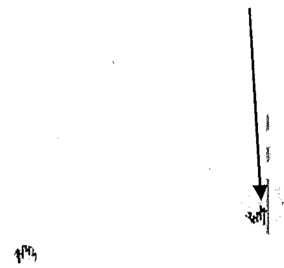
EBITDA

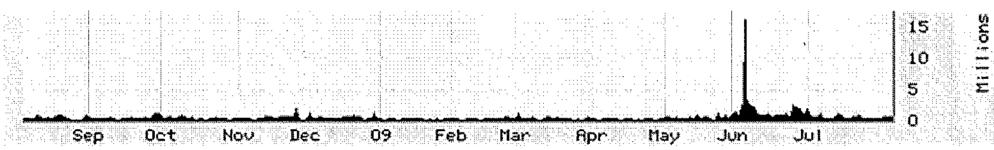
	EBITDA	EV/ EBITDA
2007A	-	-
2008A	$0.8B	9.8x
2009E	$0.9B	8.9x
2010E	$1.0B	8.0x

Relative Daily Price 8/5/09



Source: BigCharts, Company Reports and Sturdivant & Co. Estimates.




15
10
5
0
Millions
Sep
Oct
Nov
Dec
09
Feb
Mar
Apr
May
Jun
Jul

Additional Discussion

Quarterly Earnings Review

American Water reported second quarter revenue increased 4.0% yr/yr to $612.7 million compared to $589.4 million a year ago—our estimate was $618.8 million. On a segment basis, Regulated Business revenue increased by $28.7 million despite unusually wet weather in the quarter primarily as a result of rate case awards. We found comfort in the quarter due to the company's ability to overcome the negative impact of unfavorable weather via rate case relief pipeline. Turning the to the company's other segment, AWK's Non-Regulated Business revenue declined by $2.8 million yr/yr which was attributable to lower revenues in the Contract Operations Group and Applied Water Management Group. This was partially offset by an increase in revenue in the Homeowner Services unit which entered its 16th state during the quarter. Companywide water sales volume did fall yr/yr by 5.4 billion gallons or 5.5%. Dissecting it further, residential, commercial, industrial and public volumes decreased 4.8%, 4.9%, 16.8% and 0.8%, respectively. We are not concerned with the volume shortfall since we have already modeled for decreased consumption.

Non-GAAP operating expenses rose $8.0 million or 1.8% yr/yr to $455.5 million, we estimated $475.1 million. OpEx for the company's Regulated Business was $15.5 million higher yr/yr due to increased O&M and depreciation expense, as well as higher general taxes in the unit during the quarter. Non-Regulated OpEx fell $4.4 million due to lower revenue and cost control. Making up the lion's share of OpEx, depreciation and amortization increased approximately $5.9 million, production costs were $4.6 million higher due primarily to higher chemical costs and employee related costs grew $1.7 million in the quarter. Growth in employee costs were mainly fueled by greater pension expenses. The company is in discussions with regulators about the appropriate treatment of this issue in order to minimize regulatory lag between incurring the cost and recovery of the expense Operating income was $157.2 million and pre-tax margin was 14.1%, our estimate was 11.2%. AWK's second quarter tax rate was 39.6% and on the bottom-line, American Water earned $0.32 per diluted share—$0.07 ahead of our estimate.

Industry Outlook

Our outlook for the water utility industry over the short-term is positive. We expect investors to build positions in water utilities (investor-owned utilities or IOUs) because of their predictable earnings, defensive style and attractive dividends. Over the medium- to long-term we are bullish on the space. In our view, the aging water and wastewater infrastructure in the United States needs modernization/replacement and will require water utilities to invest in infrastructure. Rate hikes should follow translating into top- and bottom-line growth. In addition, we expect water utilities to benefit from acquisitions despite the weak economy and the housing slowdown. The majority of water systems are owned by municipalities, that have less tax revenue to finance infrastructure projects, and therefore they may sell their systems to IOUs, thus allowing water utilities to grow their customer base.

Earnings Outlook

As a result of our updated rate relief revenue model and our less conservative O&M estimates, we are decreasing our 2009 diluted EPS forecast to $1.31 from $1.38. The remaining 2009 assumptions are essentially unchanged. For the year, we estimate revenue of $2.5 billion or 5.9% higher yr/yr. Our sales forecast is predicated solely on American Water's rate relief and does not take into account tuck-in acquisitions which would provide upside to our forecast. Our O&M expense for 2009 is now $1.3 billion, down from our prior estimate of $1.4 billion . We are forecasting depreciation and amortization expense to be approximately $295.0 million and we project the company to pay approximately $210.0 million in general taxes leading to our operating margin forecast of 25.9%, 180 basis points higher than 2008. Below the line, we estimate pre-tax margin to be 14.6% and our tax rate is 39.5%. Our 2010 earnings estimate is now $1.58, up from our previous estimate of $1.56. Like our 2009 adjustments, our 2010 increase is due to our updated rate relief model and our less conservative O&M estimate. For a copy of our revenue model, please contact your respective sales representative.

Figure 1: Valuation Analysis

P/E Multiple	Fwd 4 Qtr EPS	Implied Share Price	Price as of 8/5/2009	Upside
18.5x	$1.44	$27	$20.00	33%

EV/EBITDA Multiple	Fwd 4 Qtr EBITDA	Enterprise Value	Net Debt	Market Capitalization	Implied Share Price	Price as of 8/5/2009	Upside
10.0x	$988,029	$9,880,290	$4,997,054	$4,883,236	$28	$20.00	39%

Source: Sturdivant & Company Equity Research

Conclusion and Recommendation

We believe American Water Works is a desirable investment due to its stable and predictable top-line growth, steadily expanding customer base, diverse geographic footprint, strong management team and its current valuation. In our view, American Water Works has the potential to experience near- and long-term price appreciation as the company's rate case filings come to fruition and AWK grows its rate base.

We believe AWK should be appointed an 18.5x P/E multiple that when applied to our forward four-quarter earnings estimate of $1.44 generates a price target of $27. There could be upside to our target if American Water Works is awarded additional rate case relief above our estimates. Furthermore, we believe the company has the potential to experience long-term price appreciation as Wall Street recognizes the growth potential in the water sector and the company exploits its potential for growth.

We are reiterating our Market Outperform rating and raising our price target to $27. We advise investors to establish core positions now.

Investment Thesis

American Water is a geographically diverse water utility company that capitalizes on its top-notch earnings growth strategy. We consider AWK to be one of the more compelling stocks in the water space based on its highly predictable earnings and a valuation below its peers. In our view, American Water is positioned to benefit from a substantial pipeline of rate case relief. Furthermore, the company is positioned to benefit from strong customer growth and acquisitions. With a weak U.S. economy, we recommend companies with favorable government mandates/regulations, a significant position in its respective area and a strong track record – in our view, American Water Works satisfies these requirements. We reiterate our Market Outperform rating and raise our price target to $27.

Investment Risks

If the company experiences any or all of the following risk factors, as well as others, the company's stock price may be affected.

- American Water's utility operations are heavily regulated. Decisions by state PUCs and other regulatory agencies can significantly affect the company's business and results of operations.
- AWK's operations and quality of water they provide are subject to environmental laws and regulations.
- Changes in laws and regulations can significantly effect American Water's business and financial results.
- Weather conditions, natural hazards, availability of water supplies and competing uses may interfere with the company's sources of water, demand of water services and AWK's ability to supply water to customers.
- Declining residential per customer water usage may reduce the company's revenue, financial condition and results of operations.

Figure 2: Income Statement

American Water Works Company, Inc. (AWK)
Income Statement
(Non-GAAP)
(in millions except per share data)

Sturdivant & Co.
Richard Verdi; 856.751.1331

December Fiscal Year	FY 2008					FY 2009					FY 2010
	1Q08	2Q08	3Q08	4Q08	Year	1Q09	2Q09	3Q09E	4Q09E	Year	Year
Revenue	**$506.8**	**$589.4**	**$672.2**	**$568.6**	**$2,336.9**	**$550.2**	**$612.7**	**$712.3**	**$600.3**	**$2,475.6**	**$2,622.2**
Operating & Maintenance	311.3	330.6	342.2	319.7	1303.8	314.4	330.6	355.1	331.7	1331.8	1381.7
Depreciation & amortization	63.9	67.3	68.4	71.7	271.3	68.8	73.2	75.0	75.0	292.1	300.0
General taxes	52.1	49.6	49.4	48.1	199.1	52.5	51.7	53.0	53.0	210.2	212.0
Loss (gain) on sales of assets	(0.1)	(0.8)	0.5	0.0	(0.4)	0.0	0.0	0.0	0.0	0.0	0.0
Impairment charges	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Operating Income	**79.6**	**142.7**	**211.8**	**129.1**	**563.1**	**114.4**	**157.2**	**229.3**	**140.6**	**641.5**	**728.5**
Interest Expense, Net	(70.0)	(70.1)	(72.7)	(72.4)	(285.2)	(72.0)	(73.7)	(75.0)	(75.0)	(295.7)	(280.0)
Allowance for other funds used during construction	2.5	3.4	4.4	4.1	14.5	3.3	3.6	3.5	3.5	13.9	14.0
Allowance for borrowed funds used during construction	1.4	1.7	3.0	2.1	8.2	1.9	2.0	1.9	1.9	7.6	7.4
Amortization of debt expense	(1.3)	(1.4)	(1.6)	(1.5)	(5.9)	(1.5)	(1.5)	(1.6)	(1.6)	(6.1)	(6.2)
Preferred dividends of subsidiaries	(0.1)	(0.1)	(0.1)	(0.1)	(0.2)	0.0	0.0	0.0	0.0	0.0	0.0
Other, net	1.2	(0.5)	0.9	3.4	4.9	1.1	(1.4)	0.0	0.0	(0.3)	0.0
Income Before Taxes	13.4	75.7	145.7	64.6	299.4	47.3	86.1	158.1	69.4	360.9	463.7
Income Taxes	7.4	30.2	57.5	28.2	123.4	17.5	34.1	63.2	27.8	142.7	185.5
Net Income	**6.0**	**45.5**	**88.2**	**36.4**	**176.1**	**29.7**	**52.0**	**94.8**	**41.6**	**218.2**	**278.2**
Diluted EPS	**$0.04**	**$0.28**	**$0.55**	**$0.23**	**$1.10**	**$0.19**	**$0.32**	**$0.56**	**$0.24**	**$1.31**	**$1.58**
Diluted Shares Outstanding	160.0	160.0	160.0	160.0	160.0	160.0	163.3	168.3	173.3	166.2	175.8
Margin Analysis											
Operating & Maintenance	61.4%	56.1%	50.9%	56.2%	55.8%	57.1%	54.0%	49.8%	55.3%	53.8%	52.7%
Depreciation & amortization	12.6%	11.4%	10.2%	12.6%	11.6%	12.5%	12.0%	10.5%	12.5%	11.8%	11.4%
General taxes	10.3%	8.4%	7.3%	8.5%	8.5%	9.5%	8.4%	7.4%	8.8%	8.5%	8.1%
Operating Income	15.7%	24.2%	31.5%	22.7%	24.1%	20.8%	25.7%	32.2%	23.4%	25.9%	27.8%
Income Before Taxes	2.6%	12.8%	21.7%	11.4%	12.8%	8.6%	14.1%	22.2%	11.6%	14.6%	17.7%
Income Taxes	55.3%	39.9%	39.5%	43.7%	41.2%	37.1%	39.6%	40.0%	40.0%	39.5%	40.0%
Net Income	1.2%	7.7%	13.1%	6.4%	7.5%	5.4%	8.5%	13.3%	6.9%	8.8%	10.6%
Growth Rates yr/yr											
Revenue	-	-	-	-	5.5%	8.6%	4.0%	6.0%	5.6%	5.9%	5.9%
Operating Income	-	-	-	-	3622.0%	43.7%	10.2%	8.3%	8.9%	13.9%	13.6%
Income Before Taxes	-	-	-	-	-217.2%	252.5%	13.8%	8.5%	7.4%	20.5%	28.5%
Net Income	-	-	-	-	-151.4%	396.5%	14.3%	7.6%	14.4%	24.0%	27.5%
Diluted EPS	-	-	-	-	-151.4%	396.4%	12.0%	2.3%	5.6%	19.3%	20.4%

Source: Company Reports, Sturdivant & Co. Estimates

Sturdivant & Co.'s
Businessman's Approach to Value Philosophy

Sturdivant & Co. uses the businessman's approach to evaluating stocks. This philosophy is predicated on looking at a company as a prudent man would were he to consider making a reasoned investment in a business. We focus on a company's strategy, the competitive position a company has versus its peers, quality of management, risk factors, its prospect for growth, as well as critical catalysts and milestones as evidence of progress. Finally, of course, we look at a company's valuation to determine where we feel the stock is priced attractively.

Chairman

Albert A. Sturdivant
Asturdivant@sturdivant-co.com
856-751-1331 *ext.* 108

Fundamental Research

Richard A. Verdi
Rverdi@sturdivant-co.com
856-751-1331 *ext.* 109
Industrials
Utilities

Beth Ann Loewy, CFA
Bloewy@sturdivant-co.com
856-751-1331 *ext.* 114
Food
Consumer Staples
Retail

Institutional Sales

Carl R. Gibbs, Jr.
Cgibbs@sturdivant-co.com
856-751-1331 *ext.* 107

Terry Williams
Twilliams@sturdivant-co.com
856-751-1331 *ext.* 101

Institutional Trading

Harvey R. de Krafft
Hdekrafft@sturdivant-co.com
800-486-1515 or
856-751-1331 *ext.* 112

Debra L. Bailey
Dbailey@sturdivant-co.com
800-486-1515 or
856-751-1331 *ext.* 110

James Campanella
Jcampanella@sturdivant-co.com
800-486-1515 or
856-751-1331 *ext.* 115

	Date	Price	Rating	Target
AWK	10/15/08	$18.10	Market Outperform	$25.00
	11/06/08	$18.93	Market Outperform	$25.00
	03/24/09	$18.09	Market Outperform	$25.00
	05/06/09	$18.16	Market Outperform	$26.00
	08/05/09	$20.00	Market Outperform	$27.00

Total Industrial Group

Outperform	Marketperform	Underperform
64% (7)	36% (4)	0

Investment Banking Relationship

Outperform	Marketperform	Underperform
100%	0%	0%

US - Industrial Services and Utilities

Investment Rating	Company	Ticker Symbol	Initial Coverage Date	Research Analyst
Market Outperform				
	American Water Works	AWK	10/16/2008	Richard Verdi
	Aqua America, Inc.	WTR	6/25/2008	Richard Verdi
	Artesian Resources Corp.	ARTNA	2/11/2009	Richard Verdi
	Calgon Carbon Corp.	CCC	7/27/2009	Richard Verdi
	Met-Pro Corp.	MPR	5/29/2007	Richard Verdi
	Middlesex Water Co.	MSEX	1/29/2009	Richard Verdi
	Tyco International Ltd.	TYC	1/29/2009	Richard Verdi
Market Perform				
	Ametek, Inc.	AME	3/26/2008	Richard Verdi
	Badger Meter	BMI	7/11/2007	Richard Verdi
	Echelon Corp.	ELON	12/6/2007	Richard Verdi
	Itron Inc.	ITRI	9/13/2007	Richard Verdi
Market Underperform				
	N/A			

Member: FINRA and SIPC

STURDIVANT & CO.

Mid-Atlantic Institutional Research

American Water Works Co., Inc. (NYSE: AWK - $20.50)

Tough Quarter on Unfavorable Weather Conditions Creates Buying Opportunity
Stage is Set for Strong 2010 & 2011 Earnings Growth...Reiterate Market Outperform

November 10, 2009

Richard A. Verdi
(856) 751-1331 x109
rverdi@sturdivant-co.com

Long Term Rating: Market Outperform
Long Term Target Price: $27

Investment Summary: *American Water Works reported Q309 results below our estimate on a softer than expected top-line that resulted from the negative impact of unfavorable weather conditions during the quarter. The U.S. Weather Service reported that the summer of 2009 was the eighth wettest summer in that last 137 years in southeastern Pennsylvania and New Jersey and with AWK deriving 47% of its revenue from this region, we were not surprised nor concerned with this quarter's results. Transitioning from the past to the future, in the short-term, we believe AWK is in a sweet spot for buying as we are modeling for earnings to ramp in 2010 and beyond, and we expect the stock price should follow. In the longer term, we believe the company is positioned to benefit nicely from a sustainable period of increased revenue due to its rate case relief pipeline and its potential for solid customer growth. Trading at 12.7x our 2010 diluted EPS estimate of $1.62, we believe the company should trade at 18.5x which is more consistent with the group's historic trading range, however, the multiple accounts for the RWE overhang. With a PEG ratio of 0.5x and 32% upside to our price target from current trading levels, we are reiterating our Market Outperform rating on American Water and recommend investors accumulate shares of the stock.*

Key Points

- **Earnings shortfall.** AWK reported Q309 earnings of $0.52, $0.04 below our estimate on softer than expected sales. Revenue for the quarter of $680.0 million was 1.2% higher than the same quarter a year ago, but the company fell short of our estimate by $32.4 million. The sales miss resulted from the negative impact of unfavorable weather conditions during the summer months in the Mid-Atlantic region. Operating and maintenance expense fell $1.4 million yr/yr to $340.9 million compared to our estimate of $355.1 million. Peeking inside O&M, increased employee and production costs were offset by lower operational and accounting expenses. We are impressed with management's control of the line-item since this is the third consecutive quarter that AWK has reported essentially flat yr/yr growth in O&M. D&A met our forecast of $75.0 million and general taxes of $50.6 million was below our estimate by $2.4 million. Below EBIT, Q3 line-items were essentially in-line and the tax rate of 35.4% was below our forecast of 40.0% as the company benefitted from state tax law changes at one of its subsidiaries. Net income for the quarter was $91.6 million, our estimate as $94.9 million.

- **Adjusting estimates and maintaining $27 price target.** Following American Water's Q309 results we are tweaking our 2009 and 2010 estimates. For 2009, we estimate the company to earn $1.24 per diluted share on $2.4 billion in revenue compared to our previous estimates of $1.31 and $2.5 billion. Our 2010 top-line estimate is $2.63 billion compared to our prior estimate of $2.62 billion. In turn, our 2010 diluted EPS estimate rose by $0.04 to $1.62. The increase is attributable to AWK's recent rate case relief request which it filed in August 2009, as well as adjustments to the P&L to reflect current trends in the company's line-items. We are maintaining our $27 price target which is based on a blended approach of P/E and EV/EBITDA valuation analysis.

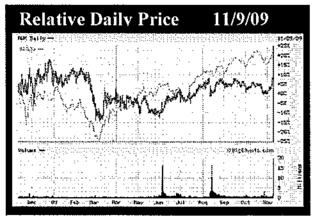
Share Information	
Price 11/9	$20.50
52 Wk Lo-Hi	$16.22-$22.35
Div Yield	4.30%
Avg. Volume	1,316,830
Insiders Own	55.5%
S&P 500	1,093.08

Financial Statistics	
Equity Mkt. Cap.	$3.6B
'08 LTD/Cap.	53.1%
Ent. Value	$8.8B
10 Yr. Treasury	3.49%
'08 FCF Yield	N/A

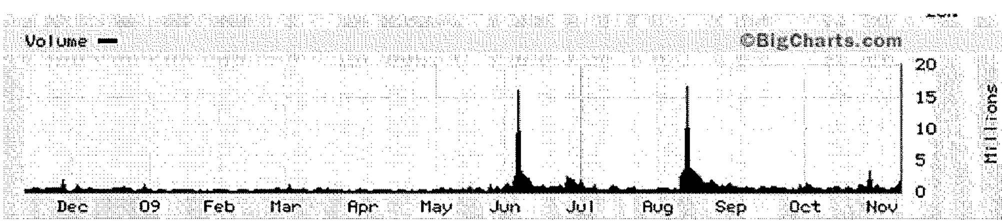
EPS	EPS	P/E
2007A	-	-
2008A	$1.10	18.6x
2009E	$1.24	16.5x
2010E	$1.62	12.7x

EBITDA	EBITDA	EV/ EBITDA
2007A	-	-
2008A	$0.8B	11.0x
2009E	$0.9B	9.8x
2010E	$1.1B	8.0x

Relative Daily Price 11/9/09



Source: BigCharts, Company Reports and Sturdivant & Co. Estimates.


Volume
©BigCharts.com
20
15
10
5
0
Millions
Dec
09
Feb
Mar
Apr
May
Jun
Jul
Aug
Sep
Oct
Nov

Additional Discussion

Quarterly Earnings Review

American Water reported third quarter revenue increased 1.2% yr/yr to $680.0 million compared to $672.2 million a year ago—our estimate was $712.3 million. The top-line miss was attributable to the negative impact of unfavorable weather conditions during the quarter. On a segment basis, Regulated Business revenue increased by $17.6 million or 2.9% over Q308 primarily as a result of rate case awards. Water usage volume decreased 7.4% yr/yr as a result of the unfavorable weather conditions. This drop in volume resulted in a $44.2 million decrease in revenue and $0.14 per diluted share. Turning to the company's other segment, AWK's Non-Regulated Business revenue declined by $8.6 million yr/yr which was attributable to lower revenues in the Contract Operations Group reflecting decreased sales associated with the company's design and build contracts. Total operating expenses rose $5.1 million or 1.1% yr/yr to $465.6 million, we estimated $483.1 million. Dissecting OpEx further, O&M expense was $340.9 million, falling 40 basis points yr/yr—we estimated the O&M line to grow 3.75% over Q308. Figures 1 and 2 below display how management has been able to produce a solid operating margin by leveraging top-line growth through keeping O&M yr/yr growth below the industry run rate of 3.5% to 4.0%. Depreciation and amortization increased approximately $6.5 million, production costs were $2.6 million higher due primarily to higher chemical costs and employee related costs grew $12.2 million in the quarter. Growth in employee costs were mainly fueled by the net increase in the expenses of salaries, wages, pensions and post-retirement benefits. Operating income was $214.4 million compared to our forecast of $229.3 million and pre-tax margin was 20.9%, our estimate was 22.2%. AWK's third quarter tax rate was 35.4% and on the bottom-line, American Water earned $0.52 per diluted share—$0.04 below our estimate.

Figure 1: Historic Revenue (Q109-Q309)

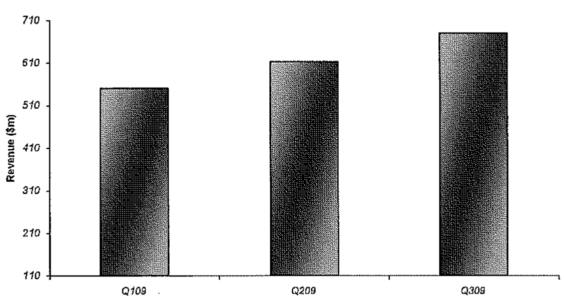
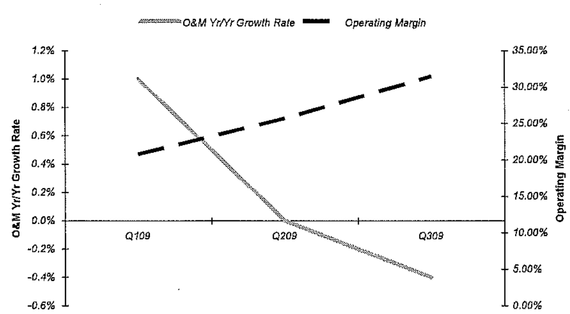


Figure 2: O&M & EBIT Margin Trends (Q109-Q309)



Source: Company Reports, Sturdivant & Co. Equity Research

Industry Outlook

Our outlook for the water utility industry over the short-term is positive. We expect investors to build positions in water utilities (investor-owned utilities or IOUs) because of their predictable earnings, defensive style and attractive dividends. Over the medium- to long-term we are bullish on the space. In our view, the aging water and wastewater infrastructure in the United States needs modernization/replacement and will require water utilities to invest in infrastructure. Rate hikes should follow translating into top- and bottom-line growth. In addition, we expect water utilities to benefit from acquisitions despite the weak economy and the housing slowdown. The majority of water systems are owned by municipalities, that have less tax revenue to finance infrastructure projects, and therefore they may sell their systems to IOUs, thus allowing water utilities to grow their customer base. More specific for AWK, while there may be multiple contraction in the group as investors rotate out of defensive areas and into more cyclical growth names, we believe American Water's multiple will expand and eventually trade in-line with the group's historic range of 20.0x-25.0x. This would be attributable to AWK coming out from underneath the RWE overhang and as Wall Street begins to recognize the earnings growth potential for the company.

Earnings Outlook

As a result of AWK's recent rate relief request, as well as the company's Q3 results, we are adjusting our model as follows—for 2010, we estimate American Water to report $2.6 billion in sales. Our sales forecast is predicated solely on rate relief. We are not modeling for any additional revenue from acquisitions, customer growth or a contribution from the Non-Regulated segment. In our view, this is a conservative revenue model since any contribution from these other potential top-line contributors would generate upside to our sales forecast. Our O&M expense projection for is $1.4 billion or 3.75% higher yr/yr which is the midpoint of the industry average growth range of 3.5% to 4.0%. We note that American Water has been reporting essentially flat yr/yr growth in the line-item and if this continues, there may be upside to our earnings estimates. In 2010, our D&A estimate is $300.0 million and our forecast for general taxes is $204.0 million—both are based on current trends on the P&L. In turn, we estimate operating margin expansion of 330 basis points to 29.0%. Below the line, our pre-tax margin is 18.7% and our tax-rate is 40.0%. On the bottom-line, we estimate American Water Works Company to earn $1.62 per diluted share for 2010.

Figure 3: Income Statement

American Water Works Company, Inc. (AWK)
Income Statement
(Non-GAAP)
(in millions except per share data)

Sturdivant & Co.
Richard Verdi; 856.751.1331

December Fiscal Year	FY 2008					FY 2009					FY 2010
	1Q08	2Q08	3Q08	4Q08	Year	1Q09	2Q09	3Q09	4Q09E	Year	Year
Revenue	**$506.8**	**$589.4**	**$672.2**	**$568.6**	**$2,336.9**	**$550.2**	**$612.7**	**$680.0**	**$600.3**	**$2,443.2**	**$2,633.8**
Operating & Maintenance	311.3	330.6	342.2	319.7	1303.8	314.4	330.6	340.9	331.7	1317.6	1367.0
Depreciation & amortization	63.9	67.3	68.4	71.7	271.3	68.8	73.2	74.9	75.0	291.9	300.0
General taxes	52.1	49.6	49.4	48.1	199.1	52.5	51.7	50.6	51.0	205.8	204.0
Loss (gain) on sales of assets	(0.1)	(0.8)	0.5	0.0	(0.4)	0.0	0.0	(0.8)	0.0	(0.8)	0.0
Impairment charges	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Operating Income	**79.6**	**142.7**	**211.8**	**129.1**	**563.1**	**114.4**	**157.2**	**214.4**	**142.6**	**628.6**	**762.8**
Interest Expense, Net	(70.0)	(70.1)	(72.7)	(72.4)	(285.2)	(72.0)	(73.7)	(74.1)	(75.0)	(294.8)	(280.0)
Allowance for other funds used during construction	2.5	3.4	4.4	4.1	14.5	3.3	3.6	2.3	3.0	12.2	12.0
Allowance for borrowed funds used during construction	1.4	1.7	3.0	2.1	8.2	1.9	2.0	1.7	1.6	7.1	6.4
Amortization of debt expense	(1.3)	(1.4)	(1.6)	(1.5)	(5.9)	(1.5)	(1.5)	(2.1)	(2.2)	(7.3)	(8.6)
Preferred dividends of subsidiaries	(0.1)	(0.1)	(0.1)	(0.1)	(0.2)	0.0	0.0	0.0	0.0	0.0	0.0
Other, net	1.2	(0.5)	0.9	3.4	4.9	1.1	(1.4)	(0.3)	0.0	(0.6)	0.0
Income Before Taxes	13.4	75.7	145.7	64.6	299.4	47.3	86.1	141.8	70.0	345.3	492.6
Income Taxes	7.4	30.2	57.5	28.2	123.4	17.5	34.1	50.2	32.9	134.8	197.0
Net Income	**6.0**	**45.5**	**88.2**	**36.4**	**176.1**	**29.7**	**52.0**	**91.6**	**37.1**	**210.5**	**295.6**
Diluted EPS	**$0.04**	**$0.28**	**$0.55**	**$0.23**	**$1.10**	**$0.19**	**$0.32**	**$0.52**	**$0.21**	**$1.24**	**$1.62**
Diluted Shares Outstanding	160.0	160.0	160.0	160.0	160.0	160.0	163.3	174.7	179.7	169.4	182.2
Margin Analysis											
Operating & Maintenance	61.4%	56.1%	50.9%	56.2%	55.8%	57.1%	54.0%	50.1%	55.3%	53.9%	51.9%
Depreciation & amortization	12.6%	11.4%	10.2%	12.6%	11.6%	12.5%	12.0%	11.0%	12.5%	11.9%	11.4%
General taxes	10.3%	8.4%	7.3%	8.5%	8.5%	9.5%	8.4%	7.4%	8.5%	8.4%	7.7%
Operating Income	15.7%	24.2%	31.5%	22.7%	24.1%	20.8%	25.7%	31.5%	23.8%	25.7%	29.0%
Income Before Taxes	2.6%	12.8%	21.7%	11.4%	12.8%	8.6%	14.1%	20.9%	11.7%	14.1%	18.7%
Income Taxes	55.3%	39.9%	39.5%	43.7%	41.2%	37.1%	39.6%	35.4%	47.0%	39.0%	40.0%
Net Income	1.2%	7.7%	13.1%	6.4%	7.5%	5.4%	8.5%	13.5%	6.2%	8.6%	11.2%
Growth Rates yr/yr											
Revenue	-	-	-	-	5.5%	8.6%	4.0%	1.2%	5.6%	4.5%	7.8%
Operating Income	-	-	-	-	3622.0%	43.7%	10.2%	1.3%	10.5%	11.6%	21.3%
Income Before Taxes	-	-	-	-	-217.2%	252.5%	13.8%	-2.7%	8.4%	15.3%	42.7%
Net Income	-	-	-	-	-151.4%	396.5%	14.3%	3.9%	2.0%	19.6%	40.4%
Diluted EPS	-	-	-	-	-151.4%	396.4%	12.0%	-4.8%	-9.2%	12.9%	30.4%

Source: Company Reports, Sturdivant & Co. Estimates

Investment Risks

If the company experiences any or all of the following risk factors, as well as others, the company's stock price may be affected.

- American Water's utility operations are heavily regulated. Decisions by state PUCs and other regulatory agencies can significantly affect the company's business and results of operations.
- AWK's operations and quality of water they provide are subject to environmental laws and regulations.
- Changes in laws and regulations can significantly effect American Water's business and financial results.
- Weather conditions, natural hazards, availability of water supplies and competing uses may interfere with the company's sources of water, demand of water services and AWK's ability to supply water to customers.
- Declining residential per customer water usage may reduce the company's revenue, financial condition and results of operations.

Sturdivant & Co.'s
Businessman's Approach to Value Philosophy

Sturdivant & Co. uses the businessman's approach to evaluating stocks. This philosophy is predicated on looking at a company as a prudent man would were he to consider making a reasoned investment in a business. We focus on a company's strategy, the competitive position a company has versus its peers, quality of management, risk factors, its prospect for growth, as well as critical catalysts and milestones as evidence of progress. Finally, of course, we look at a company's valuation to determine where we feel the stock is priced attractively.

Chairman

Albert A. Sturdivant
Asturdivant@sturdivant-co.com
856-751-1331 *ext.* 108

Fundamental Research

Richard A. Verdi
Rverdi@sturdivant-co.com
856-751-1331 *ext.* 109
Industrials
Utilities

Beth Ann Loewy, CFA
Bloewy@sturdivant-co.com
856-751-1331 *ext.* 114
Food
Consumer Staples
Retail

Institutional Sales

Carl R. Gibbs, Jr.
Cgibbs@sturdivant-co.com
856-751-1331 *ext.* 107

Terry Williams
Twilliams@sturdivant-co.com
856-751-1331 *ext.* 101

Institutional Trading

Harvey R. de Krafft
Hdekrafft@sturdivant-co.com
800-486-1515 or
856-751-1331 *ext.* 112

Debra L. Bailey
Dbailey@sturdivant-co.com
800-486-1515 or
856-751-1331 *ext.* 110

James Campanella
Jcampanella@sturdivant-co.com
800-486-1515 or
856-751-1331 *ext.* 115

	Date	Price	Rating	Target
AWK	10/15/08	$18.10	Market Outperform	$25.00
	11/06/08	$18.93	Market Outperform	$25.00
	03/24/09	$18.09	Market Outperform	$25.00
	05/06/09	$18.16	Market Outperform	$26.00
	08/05/09	$20.00	Market Outperform	$27.00
	11/09/09	$20.50	Market Outperform	$27.00

Total Industrial & Utilities Group

Outperform	Marketperform	Underperform
73% (8)	27% (3)	0

Investment Banking Relationship

Outperform	Marketperform	Underperform
100%	0%	0%

US - Industrial Services and Utilities

Investment Rating	Company	Ticker Symbol	Initial Coverage Date	Research Analyst
Market Outperform				
	American Water Works	AWK	10/16/2008	Richard Verdi
	Aqua America, Inc.	WTR	6/25/2008	Richard Verdi
	Artesian Resources Corp.	ARTNA	2/11/2009	Richard Verdi
	Calgon Carbon Corp.	CCC	7/27/2009	Richard Verdi
	Itron Inc.	ITRI	9/13/2007	Richard Verdi
	Met-Pro Corp.	MPR	5/29/2007	Richard Verdi
	Middlesex Water Co.	MSEX	1/29/2009	Richard Verdi
	Tyco International Ltd.	TYC	1/29/2009	Richard Verdi
Market Perform				
	Ametek, Inc.	AME	3/26/2008	Richard Verdi
	Badger Meter	BMI	7/11/2007	Richard Verdi
	Echelon Corp.	ELON	12/6/2007	Richard Verdi
Market Underperform				
	N/A			

Member: FINRA and SIPC

WACHOVIA

A publication of
WACHOVIA CAPITAL MARKETS, LLC

Equity Research

American Water Works Company, Inc.

AWK: A Tale Of Two Stories

Market Perform / V
Sector: Water Utilities, Market Weight
February 26, 2009

- AWK reported ongoing 08 EPS of $1.10, below our $1.13 and the consensus $1.15 estimates, compared to $0.99 in 07. Mgmt indicated poor weather and lower usage resulted in a ($0.19) impact. While it is understandably difficult to separate the weather vs. declining usage vs. economic impact, the lower sales trends cause us concern as they accelerated in the less discretionary-use Q4. For the year, volumes were (4.4%) whereas Q4 was (6.7%) including an (11.6%) industrial decline.
- Operationally we are encouraged by the progress made in regards to rate case filings, growing rate base, tuck-in acquisitions and improving returns. Rate relief received over the last 3 years has increased steadily from $41 mm in 06 to $159 mm in 07 and $206 mm in 08. Rate cases pending total another $104 mm with plans to file additional cases in 09. AWK's 08 success rate (granted vs. requested) has averaged 60-65% with authorized ROE's in the 10-10.5% range.
- Balance sheet and capital markets position remains relatively weak. We believe the disruptions in the capital markets have prevented RWE from divesting additional shares following the IPO despite its outstanding secondary registration. We est. a $400-450mm offering is being contemplated such that RWE's ownership will drop below 50% and AWK can capitalize some of its recent investments. With avg. daily volume of ~440k, an offering of this size presents a formidable challenge.
- Mgmt forecasts 09 capex at the lower end of its $0.8-1.0B range though we believe further reductions may be necessary. Debt needs are unclear, however we believe cash flow could be at a premium. Recent debt issuances at 8.25-10% have been above AWK's historical costs reflective of the BBB+ rating and difficult credit markets. We expect weak sales volumes to continue in 09 combined with pension costs that "could increase substantially" such that AWK may have to continue to rely heavily on its credit facilities and the CP market, when available, to fund the capex budget. As of 2/23, AWK had ~$180 mm of outstanding CP and ~$500 mm of available capacity under its $840 mm credit facility.
- Long-term thesis intact. We believe upper single digit EPS growth is achievable, especially once the credit disruption passes. 2009 Stimulus Bill seems to recognize the dire need for water/wastewater infrastructure investment and AWK's regulators understand this as well as the need to offer a fair return on capital. Our 2009-11E EPS remain $1.40, $1.52 and $1.60 though we believe downside risk exists.

Earnings Reported

	2008A	2009E		2010E	
EPS		**Curr.**	**Prior**	**Curr.**	**Prior**
Q1 (Mar.)	$0.04	NE		NE	
Q2 (June)	0.28	NE		NE	
Q3 (Sep.)	0.55	NE		NE	
Q4 (Dec.)	0.23	NE		NE	
FY	$1.10	$1.40	NC	$1.52	
CY	$1.10	$1.40		$1.52	
FY P/E	16.8x	13.2x		12.2x	
Rev.(MM)	$2,336.9	$2,576.0		NE	

Source: Company Data, Wachovia Capital Markets, LLC estimates, and Reuters
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful

Ticker	AWK
Price (02/26/2009)	$18.50
52-Week Range:	$16-24
Shares Outstanding: (MM)	160.0
Market Cap.: (MM)	$2,960.0
S&P 500:	752.83
Dividend/Yield:	$0.80/4.3%
LT Debt: (MM)	$4,648.2
LT Debt/Total Cap.:	49.4%
ROE:	5.0%
3-5 Yr. Est. Growth Rate:	9.0%
CY 2009 Est. P/E-to-Growth:	1.5x
Last Reporting Date:	02/25/2009 *After Close*

Source: Company Data, Wachovia Capital Markets, LLC estimates, and Reuters

Valuation Range: $18 to $20
Our relative P/E multiple (applying a 5-10% premium to the electric utility 2009E median multiple of 10.5X to our 2010E) and DDM analyses indicate a 12-18 month fair value range of $18-20 per share. Chief risks to AWK shares include execution risk, regulatory risk, capital market risk and RWE follow-on share overhang.

Investment Thesis:
We rate shares Market Perform. We believe AWK is well-positioned to capitalize on favorable industry dynamics such as significant infrastructure investment, stringent EPA water quality standards and the trend towards consolidation. Our rating reflects valuation considerations, capital markets risk and above average execution risk.

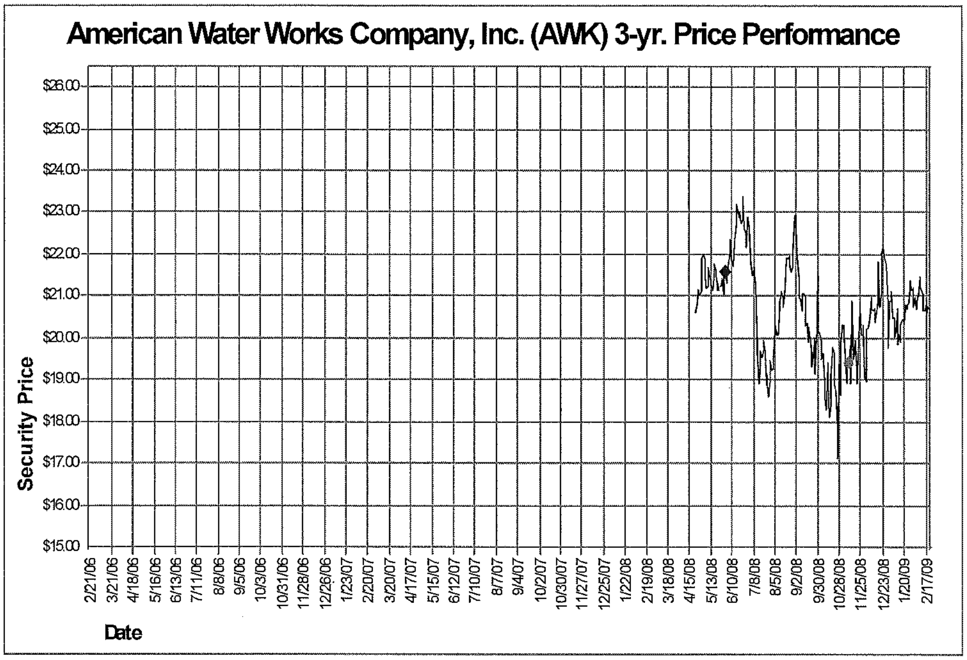
Utilities

Neil Kalton, CFA, Senior Analyst
(314) 955-5239 / neil.kalton@wachovia.com
Jonathan Reeder, Associate Analyst
(314) 955-2462 / jonathan.reeder@wachovia.com
Sarah Akers, Associate Analyst
(314) 955-6209 / sarah.akers@wachovia.com

Please see page 3 for rating definitions, important disclosures and required analyst certifications.

Company Description:
Headquartered in Voorhees, NJ, American Water Works Company, Inc. (AWK) is the largest and most geographically diversified of the investor-owned U.S. water and wastewater services providers. The company has operations in 32 states and Ontario, Canada serving approximately 15.6 million people, including its regulated utilities which serve 3.3 million customers across 20 states. Approximately 90% of revenues are derived from regulated operations. While AWK's regulated revenues are diversified across 20 states, the utility operations are most heavily concentrated in the following states: New Jersey (24%), Pennsylvania (21.7%), Illinois (9.2%), Missouri (9.2%), Indiana (7.4%), California (6.3%) and West Virginia (5.5%). As is typical for water utilities, the majority of AWK's regulated customer base are residential customers (91%), which can be characterized as a fairly predictable/inelastic demand source, and comprise more than 60% of regulated operating revenues. AWK's non-regulated businesses contribute roughly 10% to consolidated revenues and mainly include the operation and maintenance of water and wastewater systems for municipal governments and the U.S. military. Other segments beyond the Contract Operations Group include the Applied Water Management Group and Homeowner Services Group.

Required Disclosures



	Date	Publication Price ($)	Rating Code	Val. Rng. Low	Val. Rng. High	Close Price ($)
	6/2/2008		Kalton			
◆	6/2/2008	21.50	2	21.00	23.00	21.60
●	11/10/2008	19.26	2	19.00	21.00	19.43

Source: Wachovia Capital Markets, LLC estimates and Reuters data

Symbol Key
- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Valuation Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ☐ Split Adjustment

Rating Code Key
- 1 Outperform/Buy
- 2 Market Perform/Hold
- 3 Underperform/Sell
- SR Suspended
- NR Not Rated
- NE No Estimate

Additional Information Available Upon Request

I certify that:
1) All views expressed in this research report accurately reflect my personal views about any and all of the subject securities or issuers discussed; and
2) No part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by me in this research report.

- Wachovia Capital Markets, LLC or its affiliates managed or comanaged a public offering of securities for American Water Works Company, Inc. within the past 12 months.
- Wachovia Capital Markets, LLC or its affiliates intends to seek or expects to receive compensation for investment banking services in the next three months from American Water Works Company, Inc.
- Wachovia Capital Markets, LLC or its affiliates received compensation for investment banking services from American Water Works Company, Inc. in the past 12 months.
- American Water Works Company, Inc. currently is, or during the 12-month period preceding the date of distribution of the research report was, a client of Wachovia Capital Markets, LLC. Wachovia Capital Markets, LLC provided investment banking services to American Water Works Company, Inc.

Chief risks to AWK shares include execution risk, regulatory risk, capital market risk and RWE follow-on share overhang.

Wachovia Capital Markets, LLC does not compensate its research analysts based on specific investment banking transactions. WCM's research analysts receive compensation that is based upon and impacted by the overall profitability and revenue of the firm, which includes, but is not limited to investment banking revenue.

STOCK RATING

1 = **Outperform:** The stock appears attractively valued, and we believe the stock's total return will exceed that of the market over the next 12 months. BUY

2 = **Market Perform:** The stock appears appropriately valued, and we believe the stock's total return will be in line with the market over the next 12 months. HOLD

3 = **Underperform:** The stock appears overvalued, and we believe the stock's total return will be below the market over the next 12 months. SELL

SECTOR RATING

O = **Overweight:** Industry expected to outperform the relevant broad market benchmark over the next 12 months.

M = **Market Weight:** Industry expected to perform in-line with the relevant broad market benchmark over the next 12 months.

U = **Underweight:** Industry expected to underperform the relevant broad market benchmark over the next 12 months.

VOLATILITY RATING

V = A stock is defined as volatile if the stock price has fluctuated by +/-20% or greater in at least 8 of the past 24 months or if the analyst expects significant volatility. All IPO stocks are automatically rated volatile within the first 24 months of trading.

As of: February 26, 2009

40% of companies covered by Wachovia Capital Markets, LLC Equity Research are rated Outperform.	Wachovia Capital Markets, LLC has provided investment banking services for 38% of its Equity Research Outperform-rated companies.
55% of companies covered by Wachovia Capital Markets, LLC Equity Research are rated Market Perform.	Wachovia Capital Markets, LLC has provided investment banking services for 28% of its Equity Research Market Perform-rated companies.
5% of companies covered by Wachovia Capital Markets, LLC Equity Research are rated Underperform.	Wachovia Capital Markets, LLC has provided investment banking services for 30% of its Equity Research Underperform-rated companies.

Important Disclosure for International Clients

The securities and related financial instruments described herein may not be eligible for sale in all jurisdictions or to certain categories of investors. For certain non-U.S. institutional reader (including readers in the EEA), this report is distributed by Wachovia Securities International Limited ("WSIL"). For the purposes of Section 21 of the UK Financial Services and Markets Act 2000 ("the Act"), the content of this report has been approved by WSIL a regulated person under the Act. WSIL does not deal with retail clients as defined in the Markets in Financial Instruments Directive 2007. This research is not intended for, and should not be relied upon, by retail clients.

Important Information for Australian Recipients

Wachovia Capital Markets, LLC ("WCM") is exempt from the requirements to hold an Australian financial services license in respect of the financial services it provides to wholesale clients in Australia. WCM is a registered broker-dealer registered with the U.S. Securities and Exchange Commission, and a member of the New York Stock Exchange, the Financial Industry Regulatory Authority, and the Securities Investor Protection Corp. WCM is regulated under U.S. laws which differ from Australian laws. Any offer or documentation provided to you by WCM in the course of providing the financial services will be prepared in accordance with the laws of the United States and not Australian laws.

Important Information for Recipients in the Hong Kong Special Administrative Region of the People's Republic of China ("Hong Kong")

For recipients resident in Hong Kong, this research is issued and distributed in Hong Kong by Wachovia Securities Asia Limited. Wachovia Securities Asia Limited is a Hong Kong incorporated investment firm licensed and regulated by the Securities and Futures Commission to carry on types 1, 4, 6 and 9 regulated activities (as defined in the Securities and Futures Ordinance [the "SFO"]). This research is not intended for, and should not be relied on by, any person other than professional investors (as defined in the SFO). The securities and related financial instruments described herein are not intended for sale nor will be sold to any person other than professional investors (as defined in the SFO). Any sale of any securities or related financial instruments described herein will be made in Hong Kong by Wachovia Securities Asia Limited. Please consult your Wachovia Securities Asia Limited sales representative or the Wachovia Securities Asia Limited office in your area for additional information.

Important Information for Japanese Recipients

This material is distributed in Japan by Wachovia Securities (Japan) Co., Ltd., a foreign securities company registered with the Financial Services Agency in Japan.

Additional Disclosures

WCM is a U.S. broker-dealer registered with the U.S. Securities and Exchange Commission and a member of the New York Stock Exchange, the Financial Industry Regulatory Authority and the Securities Investor Protection Corp. Wachovia Securities International Limited is a U.K. incorporated investment firm authorized and regulated by the Financial Services Authority.

This report is for your information only and is not an offer to sell, or a solicitation of an offer to buy, the securities or instruments named or described in this report. Interested parties are advised to contact the entity with which they deal, or the entity that provided this report to them, if they desire further information. The information in this report has been obtained or derived from sources believed by Wachovia Capital Markets, LLC, to be reliable, but Wachovia Capital Markets, LLC, does not represent that this information is accurate or complete. Any opinions or estimates contained in this report represent the judgment of Wachovia Capital Markets, LLC, at this time, and are subject to change without notice. For the purposes of the U.K. Financial Services Authority's rules, this report constitutes impartial investment research. Each of Wachovia Capital Markets, LLC, and Wachovia Securities International Limited is a separate legal entity and distinct from affiliated banks.

WACHOVIA

A publication of
WACHOVIA CAPITAL MARKETS, LLC

Equity Research

American Water Works Company, Inc.

AWK: Goodwill Impairment Not Expected To Cause Upsized Offering

Market Perform / V

Sector: Water Utilities, Market Weight
May 6, 2009

Earnings Reported - First Look

	2008A	2009E		2010E	
EPS		**Curr.**	**Prior**	**Curr.**	**Prior**
Q1 (Mar.)	$0.04	$0.19 A		NE	
Q2 (June)	0.28	NE		NE	
Q3 (Sep.)	0.55	NE		NE	
Q4 (Dec.)	0.23	NE		NE	
FY	$1.10	$1.40	NC	$1.52	NC
CY	$1.10	$1.40		$1.52	
FY P/E	16.1x	12.6x		11.6x	
Rev.(MM)	$2,336.9	$2,576.0		NE	

Source: Company Data, Wachovia Capital Markets, LLC estimates, and Reuters
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful

- Excluding a $450MM goodwill impairment charge, AWK reported ongoing Q1 EPS of $0.19 ($0.13 Street) versus $0.04 in Q1 2008. Operationally, everything is progressing as expected. AWK is executing on its infrastructure investment plans and achieving largely constructive regulatory outcomes. Somewhat concerning to us was the 3.5% decline in overall sales, including a 12.9% drop in industrial sales. Q4 had similar declines, however, wet weather was to blame. We are interested to know what role weather played in the Q1 trends versus a change in usage patterns.
- We have heard some investor concern regarding the potential effect on equity needs due to the goodwill impairment. Somewhat surprising to us, management did not find a need to impair it during its annual Q4 test, though we would note there is some flexibility and room for interpretation in these impairment tests. However, the sustained decline of AWK stock since the Q4 test caused the triggering event.
- The potential need for an accelerated stock issuance to restore the equity ratio to an appropriate level was a concern we expressed to the company in the past; however, management cited understanding by its regulators that AWK had "inherited the sins of the former parent" and that a temporarily lower ratio due to goodwill impairment would not be viewed as an attempt at double leveraging thus the utility would not be penalized. Management seems to be singing a similar tune--regulators are willing to be patient with the company restoring a 45-50% equity ratio over time as earned ROEs improve and retained earnings increase the equity balance somewhat naturally as well as when the AWK raises additional capital to fund its capex.
- Interestingly enough, we believe the charge somewhat clears the way for AWK's much-anticipated secondary offering. The company had filed an S-1 in December indicating former parent RWE and AWK intended to sell $300MM of equity each. While jittery equity markets and a volatile share price prevented the deal thus far, we believe the recent impairment in combination with somewhat more-stable equity markets make it more likely that the deal is imminent. Of course share price reaction to the announcement will certainly play a role. We get the sense that RWE is willing to take a very patient approach rather than to try to force a deal that might require a substantial discount. Should RWE delay its part much longer, we believe AWK may have to raise roughly $300-400MM on its own.
- Conference call is at 9am ET. 1-800-762-8795 id # 4058090

Ticker	AWK
Price (05/05/2009)	$17.66
52-Week Range:	$16-24
Shares Outstanding: (MM)	160.0
Market Cap.: (MM)	$2,825.6
S&P 500:	903.80
Dividend/Yield:	$0.80/4.5%
LT Debt: (MM)	$4,684.0
LT Debt/Total Cap.:	51.7%
ROE:	5.0%
3-5 Yr. Est. Growth Rate:	9.0%
CY 2009 Est. P/E-to-Growth:	1.4x
Last Reporting Date:	05/05/2009 *After Close*

Source: Company Data, Wachovia Capital Markets, LLC estimates, and Reuters

Valuation Range: $18 to $20
Our relative P/E multiple (applying a 5-10% premium to the electric utility 2009E median multiple of 11X to our 2010E) and DDM analyses indicate a 12-18 month fair value range of $18-20 per share. Chief risks to AWK shares include execution risk, regulatory risk, capital market risk and RWE follow-on share overhang.

Investment Thesis:
We rate shares Market Perform. We believe AWK is well-positioned to capitalize on favorable industry dynamics such as significant infrastructure investment, stringent EPA water quality standards and the trend towards consolidation. Our rating reflects valuation considerations, capital markets risk and above average execution risk.

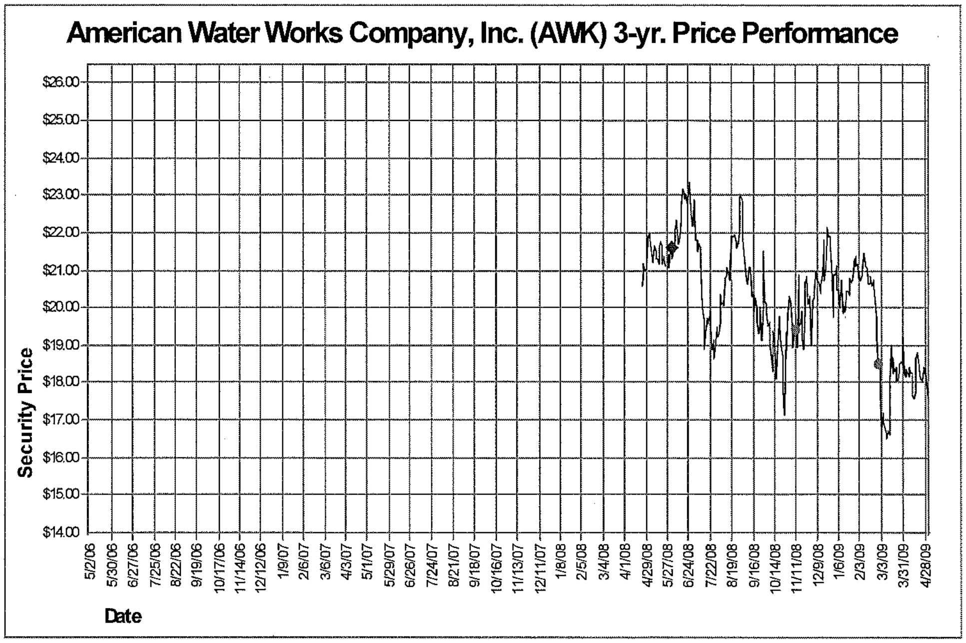
Utilities

Neil Kalton, CFA, Senior Analyst
(314) 955-5239 / neil.kalton@wachovia.com
Jonathan Reeder, Associate Analyst
(314) 955-2462 / jonathan.reeder@wachovia.com
Sarah Akers, Associate Analyst
(314) 955-6209 / sarah.akers@wachovia.com

Please see page 3 for rating definitions, important disclosures and required analyst certifications.

Company Description:
Headquartered in Voorhees, NJ, American Water Works Company, Inc. (AWK) is the largest and most geographically diversified of the investor-owned U.S. water and wastewater services providers. The company has operations in 32 states and Ontario, Canada serving approximately 15.6 million people, including its regulated utilities which serve 3.3 million customers across 20 states. Approximately 90% of revenues are derived from regulated operations. While AWK's regulated revenues are diversified across 20 states, the utility operations are most heavily concentrated in the following states: New Jersey (24%), Pennsylvania (21.7%), Illinois (9.2%), Missouri (9.2%), Indiana (7.4%), California (6.3%) and West Virginia (5.5%). As is typical for water utilities, the majority of AWK's regulated customer base are residential customers (91%), which can be characterized as a fairly predictable/inelastic demand source, and comprise more than 60% of regulated operating revenues. AWK's non-regulated businesses contribute roughly 10% to consolidated revenues and mainly include the operation and maintenance of water and wastewater systems for municipal governments and the U.S. military. Other segments beyond the Contract Operations Group include the Applied Water Management Group and Homeowner Services Group.

Required Disclosures



	Date	Publication Price ($)	Rating Code	Val. Rng. Low	Val. Rng. High	Close Price ($)
	6/2/2008		Kalton			
◆	6/2/2008	21.50	2	21.00	23.00	21.60
●	11/10/2008	19.26	2	19.00	21.00	19.43
●	2/26/2009	18.50	2	18.00	20.00	18.50

Source: Wachovia Capital Markets, LLC estimates and Reuters data

Symbol Key
- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Valuation Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ☐ Split Adjustment

Rating Code Key
- 1 Outperform/Buy
- 2 Market Perform/Hold
- 3 Underperform/Sell
- SR Suspended
- NR Not Rated
- NE No Estimate

Additional Information Available Upon Request

I certify that:
1) All views expressed in this research report accurately reflect my personal views about any and all of the subject securities or issuers discussed; and
2) No part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by me in this research report.

- Wachovia Capital Markets, LLC or its affiliates intends to seek or expects to receive compensation for investment banking services in the next three months from American Water Works Company, Inc.
- Wachovia Capital Markets, LLC or its affiliates received compensation for investment banking services from American Water Works Company, Inc. in the past 12 months.
- American Water Works Company, Inc. currently is, or during the 12-month period preceding the date of distribution of the research report was, a client of Wachovia Capital Markets, LLC. Wachovia Capital Markets, LLC provided investment banking services to American Water Works Company, Inc.

Chief risks to AWK shares include execution risk, regulatory risk, capital market risk and RWE follow-on share overhang.

Wachovia Capital Markets, LLC does not compensate its research analysts based on specific investment banking transactions. WCM's research analysts receive compensation that is based upon and impacted by the overall profitability and revenue of the firm, which includes, but is not limited to investment banking revenue.

STOCK RATING

1 = **Outperform:** The stock appears attractively valued, and we believe the stock's total return will exceed that of the market over the next 12 months. BUY

2 = **Market Perform:** The stock appears appropriately valued, and we believe the stock's total return will be in line with the market over the next 12 months. HOLD

3 = **Underperform:** The stock appears overvalued, and we believe the stock's total return will be below the market over the next 12 months. SELL

SECTOR RATING

O = **Overweight:** Industry expected to outperform the relevant broad market benchmark over the next 12 months.

M = **Market Weight:** Industry expected to perform in-line with the relevant broad market benchmark over the next 12 months.

U = **Underweight:** Industry expected to underperform the relevant broad market benchmark over the next 12 months.

VOLATILITY RATING

V = A stock is defined as volatile if the stock price has fluctuated by +/-20% or greater in at least 8 of the past 24 months or if the analyst expects significant volatility. All IPO stocks are automatically rated volatile within the first 24 months of trading.

As of: May 6, 2009

36% of companies covered by Wachovia Capital Markets, LLC Equity Research are rated Outperform.

Wachovia Capital Markets, LLC has provided investment banking services for 35% of its Equity Research Outperform-rated companies.

58% of companies covered by Wachovia Capital Markets, LLC Equity Research are rated Market Perform.

Wachovia Capital Markets, LLC has provided investment banking services for 30% of its Equity Research Market Perform-rated companies.

6% of companies covered by Wachovia Capital Markets, LLC Equity Research are rated Underperform.

Wachovia Capital Markets, LLC has provided investment banking services for 27% of its Equity Research Underperform-rated companies.

Important Disclosure for International Clients

The securities and related financial instruments described herein may not be eligible for sale in all jurisdictions or to certain categories of investors. For certain non-U.S. institutional reader (including readers in the EEA), this report is distributed by Wachovia Securities International Limited ("WSIL"). For the purposes of Section 21 of the UK Financial Services and Markets Act 2000 ("the Act"), the content of this report has been approved by WSIL a regulated person under the Act. WSIL does not deal with retail clients as defined in the Markets in Financial Instruments Directive 2007. This research is not intended for, and should not be relied upon, by retail clients.

Important Information for Australian Recipients

Wachovia Capital Markets, LLC ("WCM") is exempt from the requirements to hold an Australian financial services license in respect of the financial services it provides to wholesale clients in Australia. WCM is a registered broker-dealer registered with the U.S. Securities and Exchange Commission, and a member of the New York Stock Exchange, the Financial Industry Regulatory Authority, and the Securities Investor Protection Corp. WCM is regulated under U.S. laws which differ from Australian laws. Any offer or documentation provided to you by WCM in the course of providing the financial services will be prepared in accordance with the laws of the United States and not Australian laws.

Important Information for Recipients in the Hong Kong Special Administrative Region of the People's Republic of China ("Hong Kong")

For recipients resident in Hong Kong, this research is issued and distributed in Hong Kong by Wachovia Securities Asia Limited. Wachovia Securities Asia Limited is a Hong Kong incorporated investment firm licensed and regulated by the Securities and Futures Commission to carry on types 1, 4, 6 and 9 regulated activities (as defined in the Securities and Futures Ordinance [the "SFO"]). This research is not intended for, and should not be relied on by, any person other than professional investors (as defined in the SFO). The securities and related financial instruments described herein are not intended for sale nor will be sold to any person other than professional investors (as defined in the SFO). Any sale of any securities or related financial instruments described herein will be made in Hong Kong by Wachovia Securities Asia Limited. Please consult your Wachovia Securities Asia Limited sales representative or the Wachovia Securities Asia Limited office in your area for additional information.

Important Information for Japanese Recipients

This material is distributed in Japan by Wachovia Securities (Japan) Co., Ltd., a foreign securities company registered with the Financial Services Agency in Japan.

Additional Disclosures

WCM is a U.S. broker-dealer registered with the U.S. Securities and Exchange Commission and a member of the New York Stock Exchange, the Financial Industry Regulatory Authority and the Securities Investor Protection Corp. Wachovia Securities International Limited is a U.K. incorporated investment firm authorized and regulated by the Financial Services Authority.

This report is for your information only and is not an offer to sell, or a solicitation of an offer to buy, the securities or instruments named or described in this report. Interested parties are advised to contact the entity with which they deal, or the entity that provided this report to them, if they desire further information. The information in this report has been obtained or derived from sources believed by Wachovia Capital Markets, LLC, to be reliable, but Wachovia Capital Markets, LLC, does not represent that this information is accurate or complete. Any opinions or estimates contained in this report represent the judgment of Wachovia Capital Markets, LLC, at this time, and are subject to change without notice. For the purposes of the U.K. Financial Services Authority's rules, this report constitutes impartial investment research. Each of Wachovia Capital Markets, LLC, and Wachovia Securities International Limited is a separate legal entity and distinct from affiliated banks.

August 6, 2009

WELLS FARGO SECURITIES

Equity Research

American Water Works Company, Inc.

AWK: Well Positioned For Above-Average EPS Growth

Market Perform / V

- Reported 2Q09 EPS of $0.32, in-line with consensus, vs. $0.28 in 2Q08. AWK's diligent focus on pursuing rate recovery continues to drive earnings improvement. Q2 consumption trends were impacted by poor weather across the Northeast (NJ and PA are ~45% of consolidated revenues) which accelerated the sales decline from Q1. Residential and commercial volumes each decreased 5% while industrial was down 17% compared to deltas of 1.5%, 3.6% and 12.9%, respectively, in Q1. Though the cool, wet weather magnified the declines, we believe underlying usage declines have increased from the historical norm which reflects a combo of both current economic pressure and a longer-term behavioral shift as consumers begin to recognize the value and cost of water service.
- Our 2009-11E EPS remain $1.30, $1.43 and $1.56, respectively. The benefits from the smaller than expected mid-year equity raise and operating expense efficiencies were offset in our model by a downward adjustment to volumes and the push back of the Trenton acquisition closing. We now incorporate a 3-3.5% decrease in total water sales, down from a 1-1.5% decrease previously. We will once again revisit our assumptions following the weather sensitive Q3. We note our estimates continue to reflect $400 mm of equity financing needs in 2009.
- In June, AWK and RWE completed a long-awaited roughly $515 mm secondary offering. AWK raised net proceeds of $242.3 mm (14.5 mm shares) and RWE sold 15.4 mm shares, reducing its ownership position to 46.6% from 60%. Though the size of AWK's portion was less than expected, the utility will be a serial issuer of equity given the water utility business model and thus the size and timing of issuances will vary according to market conditions and RWE's divestment strategy. We would not rule out the possibility of another issuance in Q4. We project AWK will restore its common equity ratio within its 45-50% targeted range by 2012 (assumes no further goodwill impairments) as earned ROEs improve, net income increases and new equity is issued to fund CapEx.
- We continue to rate shares Market Perform given valuation considerations. Shares trade at a substantial P/E discount to the water utility industry multiple which largely reflects the RWE share overhang but are still at a premium to the regulated electric group, which we believe investors are using as a more appropriate comparable. Operationally, AWK has made substantial progress over the past few years including improving regulatory relationships, growing rate base and EPS power by investing heavily in its infrastructure and achieving largely constructive outcomes in its rate relief filings.

Valuation Range: $18.00 to $20.00 from $17.00 to $19.00
Our relative P/E multiple (applying a 10% premium to the electric utility '09E multiple of 12.5X to our '10E) and DDM analyses results in our 12-18 month fair value range. Risks to AWK shares include execution risk, regulatory risk, capital market risk and RWE follow-on share overhang.

Investment Thesis:
We believe AWK is well-positioned to capitalize on favorable industry dynamics such as significant infrastructure investment, stringent EPA water quality standards and the trend towards consolidation. Our Market Perform rating reflects valuation considerations, capital markets risk and above average execution risk.

Sector: Water Utilities
Market Weight

Earnings Reported

	2008A	2009E		2010E	
EPS		**Curr.**	**Prior**	**Curr.**	**Prior**
Q1 (Mar.)	$0.04	$0.19 A	NC	NE	
Q2 (June)	0.28	0.32 A		NE	
Q3 (Sep.)	0.55	NE		NE	
Q4 (Dec.)	0.23	NE		NE	
FY	$1.10	$1.30	NC	$1.43	NC
CY	$1.10	$1.30		$1.43	
FY P/E	17.8x	15.1x		13.7x	
Rev.(MM)	$2,337	$2,475		$2,677	

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful

Ticker	AWK
Price (08/06/2009)	$19.60
52-Week Range:	$16-24
Shares Outstanding: (MM)	174.5
Market Cap.: (MM)	$3,420.2
S&P 500:	993.40
Avg. Daily Vol.:	509,752
Dividend/Yield:	$0.84/4.3%
LT Debt: (MM)	$5,006.0
LT Debt/Total Cap.:	55.4%
ROE:	5.0%
3-5 Yr. Est. Growth Rate:	9.0%
CY 2009 Est. P/E-to-Growth:	1.7x
Last Reporting Date:	08/05/2009 *After Close*

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

Neil Kalton, CFA, Senior Analyst
(314) 955-5239 / neil.kalton@wachovia.com
Jonathan Reeder, Associate Analyst
(314) 955-2462 / jonathan.reeder@wachovia.com
Sarah Akers, Associate Analyst
(314) 955-6209 / sarah.akers@wachovia.com

Please see page 5 for rating definitions, important disclosures and required analyst certifications

Company Description:

Headquartered in Voorhees, NJ, American Water Works Company, Inc. (AWK) is the largest and most geographically diversified of the investor-owned U.S. water and wastewater services providers. The company has operations in 32 states and Ontario, Canada serving approximately 15.6 million people, including its regulated utilities which serve 3.3 million customers across 20 states. Approximately 90% of revenues are derived from regulated operations. While AWK's regulated revenues are diversified across 20 states, the utility operations are most heavily concentrated in the following states: New Jersey (24%), Pennsylvania (21.7%), Illinois (9.2%), Missouri (9.2%), Indiana (7.4%), California (6.3%) and West Virginia (5.5%). As is typical for water utilities, the majority of AWK's regulated customer base are residential customers (91%), which can be characterized as a fairly predictable/inelastic demand source, and comprise more than 60% of regulated operating revenues. AWK's non-regulated businesses contribute roughly 10% to consolidated revenues and mainly include the operation and maintenance of water and wastewater systems for municipal governments and the U.S. military. Other segments beyond the Contract Operations Group include the Applied Water Management Group and Homeowner Services Group.

Earnings Model ($ in millions, except per share data)	2006	2007	2008	2009E	2010E	2011E
Revenues	**2,093.1**	**2,214.2**	**2,336.9**	**2,474.5**	**2,677.2**	**2,870.9**
Operating Expenses						
Operation & Maintenance	1,174.5	1,246.5	1,303.8	1,326.6	1,386.3	1,455.6
Depreciation and Amortization	259.2	267.3	271.3	292.9	321.2	349.6
General Taxes and Other	185.1	175.9	198.8	207.9	219.6	230.5
Impairment charges	221.7	509.3	750.0	450.0	0.0	0.0
Total Operating Expenses	**1,840.6**	**2,199.1**	**2,523.8**	**2,277.4**	**1,927.0**	**2,035.7**
Operating Income	252.5	15.1	(186.9)	197.2	750.1	835.2
Operating Income, excl. impairment	**474.2**	**524.5**	**563.1**	**647.2**	**750.1**	**835.2**
EBITDA	511.7	282.5	84.4	490.0	1,071.3	1,184.8
EBITDA, excluding impairment	**733.4**	**791.8**	**834.4**	**940.0**	**1,071.3**	**1,184.8**
Other Income	6.9	13.9	19.2	24.4	23.2	21.4
Interest Expense	368.4	284.6	282.9	305.6	323.6	340.4
EBT	(108.9)	(255.5)	(450.6)	(84.1)	449.8	516.1
EBT, excluding impairment	112.7	253.8	299.4	365.9	449.8	516.1
Income Tax Expense	46.9	86.8	111.8	146.4	179.9	206.5
Tax Rate, excluding impairment	44%	36%	40%	40%	40%	40%
Income from Continuing Operations	(155.9)	(342.3)	(562.4)	(230.5)	269.9	309.7
Discontinued Ops, net	(6.4)	(0.6)	0.0	0.0	0.0	0.0
Reported Net Income	(162.2)	(342.8)	(562.4)	(230.5)	269.9	309.7
Ongoing Net Income	65.8	159.2	176.1	219.5	269.9	309.7
EPS, as reported	(1.01)	(2.14)	(3.52)	(1.36)	1.43	1.56
Adjustments	1.43	3.14	4.62	2.66	0.00	0.00
Ongoing Diluted EPS	**0.41**	**1.00**	**1.10**	**1.30**	**1.43**	**1.56**
Avg. Diluted Common Shares Out*	160.0	160.0	160.0	169.3	188.6	198.4
Dividends						
Dividends Paid Per Share	N/A	N/A	0.40	0.82	0.86	0.90
Payout Ratio	N/A	N/A	73%	63%	60%	58%
Statistics						
Year-end Tangible BVPS	5.34	13.03	15.02	15.78	16.55	17.41
Year-end BVPS	23.86	28.39	25.64	22.61	23.03	23.59
Average BVPS	20.69	26.12	27.01	24.12	22.82	23.31
Earned ROE, ongoing	**2.0%**	**3.8%**	**4.1%**	**5.4%**	**6.3%**	**6.7%**
EBITDA Per Share	3.20	1.77	0.53	2.89	5.68	5.97
Free CFPS	(2.30)	(1.71)	(3.41)	(3.26)	(2.89)	(1.81)
Free Cash Flow	(367.7)	(272.9)	(545.6)	(551.7)	(546.0)	(358.3)

* For comparison purposes, we utilize 2008 share count in presenting 2006 and 2007 per share data even though IPO did not occur until April 2008.

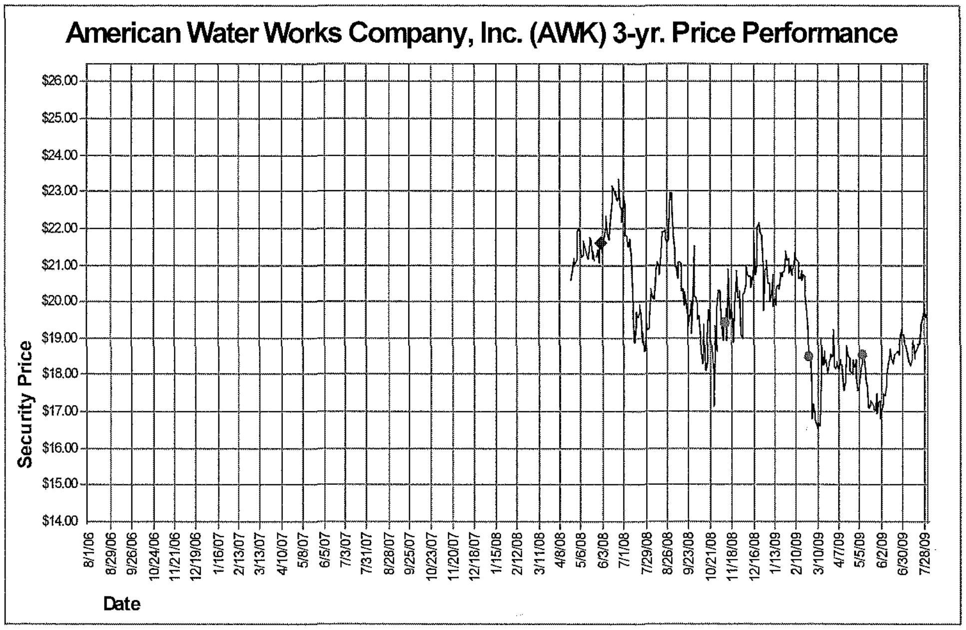
Source: Wells Fargo Securities, LLC estimates and company filings

Cash Flow Model ($ in millions)	2006	2007	2008	2009E	2010E	2011E
Operating Cash Flows						
Net Income	(162.2)	(342.8)	(562.4)	(230.5)	269.9	309.7
Depreciation and Amortization	259.2	267.3	271.3	292.9	321.2	349.6
Impairment Charges	227.8	509.3	750.0	450.0	0.0	0.0
Other	(1.0)	39.9	93.3	(30.8)	(35.3)	(25.1)
Net Cash Flows from Operations	**323.7**	**473.7**	**552.2**	**481.6**	**555.8**	**634.2**
Investing Cash Flows						
Capital Expenditures	(682.9)	(750.8)	(1,008.8)	(800.1)	(920.2)	(789.6)
Acquisitions	(12.5)	(15.9)	(12.5)	(95.0)	(20.0)	(25.0)
Other	4.0	20.1	(12.3)	0.0	0.0	0.0
Net Cash Flows from Investing	**(691.4)**	**(746.6)**	**(1,033.7)**	**(895.1)**	**(940.2)**	**(814.6)**
Financing Cash Flows						
Issuance of Long-term Debt	582.5	3,869.1	279.9	400.0	395.0	200.0
Repayment of Long-term Debt	(637.5)	(2,350.7)	(241.5)	(175.8)	(44.9)	(35.1)
Line of Credit (repayments) borrowings, net	345.7	(541.6)	258.7	(75.0)	0.0	0.0
RWE Capital Contributions	0.0	967.1	245.0	0.0	0.0	0.0
Common Stock Issuance	0.0	0.0	0.8	400.0	200.0	200.0
Redemption of Preferred Stock	(0.5)	(1,750.4)	(0.2)	0.0	0.0	0.0
Dividends on Common Stock	0.0	0.0	(64.1)	(138.2)	(161.5)	(177.8)
Other	42.2	63.1	(1.1)	(5.0)	(5.0)	(5.0)
Net Cash Flows from Financing	**332.4**	**256.6**	**477.6**	**406.0**	**383.6**	**182.1**
Net Change in Cash	(35.3)	(16.3)	(3.9)	(7.5)	(0.9)	1.7
Beginning of Year Balance	65.1	29.8	13.5	9.5	2.0	1.2
End of Year Balance	**29.8**	**13.5**	**9.5**	**2.0**	**1.2**	**2.8**

Capital Structure ($ in millions)	2006	2007	2008	2009E	2010E	2011E
Goodwill	2,962.5	2,457.0	1,699.5	1,249.5	1,249.5	1,249.5
Common Equity	3,817.4	4,542.0	4,102.0	4,133.3	4,441.7	4,773.6
Preferred Stock, w/o mandatory redemption	4.6	4.6	4.6	4.6	4.6	4.6
Long-term Debt	3,096.4	4,674.8	4,624.1	4,848.2	5,198.3	5,363.3
Redeemable Preferred Stock	1,774.5	24.3	24.2	24.2	24.2	24.2
Short-term Debt	1,007.1	317.0	654.8	579.8	579.8	579.8
Total Capitalization	**9,700.0**	**9,562.7**	**9,409.6**	**9,590.1**	**10,248.6**	**10,745.4**
% Common Equity	**39.4**	**47.5**	**43.6**	**43.1**	**43.3**	**44.4**
% Long-term Debt	31.9	48.9	49.1	50.6	50.7	49.9
% Other	28.7	3.6	7.3	6.3	5.9	5.7
Year-end Rate Base	**5,700.0**	**6,500.0**	**7,252.0**	**7,772.2**	**8,384.0**	**8,836.4**

Source: Wells Fargo Securities, LLC estimates and company filings

Required Disclosures



	Date	Publication Price ($)	Rating Code	Val. Rng. Low	Val. Rng. High	Close Price ($)
	6/2/2008		Kalton			
◆	6/2/2008	21.50	2	21.00	23.00	21.60
●	11/10/2008	19.26	2	19.00	21.00	19.43
●	2/26/2009	18.50	2	18.00	20.00	18.50
●	5/8/2009	18.58	2	17.00	19.00	18.55

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key
- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Valuation Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ☐ Split Adjustment

Rating Code Key
- 1 Outperform/Buy
- 2 Market Perform/Hold
- 3 Underperform/Sell
- SR Suspended
- NR Not Rated
- NE No Estimate

Additional Information Available Upon Request

I certify that:
1) All views expressed in this research report accurately reflect my personal views about any and all of the subject securities or issuers discussed; and
2) No part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by me in this research report.

- Wells Fargo Securities, LLC or its affiliates managed or comanaged a public offering of securities for American Water Works Company, Inc. within the past 12 months.
- Wells Fargo Securities, LLC or its affiliates intends to seek or expects to receive compensation for investment banking services in the next three months from American Water Works Company, Inc.
- Wells Fargo Securities, LLC or its affiliates received compensation for investment banking services from American Water Works Company, Inc. in the past 12 months.
- American Water Works Company, Inc. currently is, or during the 12-month period preceding the date of distribution of the research report was, a client of Wells Fargo Securities, LLC. Wells Fargo Securities, LLC provided investment banking services to American Water Works Company, Inc.

Risks to AWK shares include execution risk, regulatory risk, capital market risk and RWE follow-on share overhang.

Wells Fargo Securities, LLC does not compensate its research analysts based on specific investment banking transactions. Wells Fargo Securities, LLC's research analysts receive compensation that is based upon and impacted by the overall profitability and revenue of the firm, which includes, but is not limited to investment banking revenue.

STOCK RATING

1=Outperform: The stock appears attractively valued, and we believe the stock's total return will exceed that of the market over the next 12 months. BUY
2=Market Perform: The stock appears appropriately valued, and we believe the stock's total return will be in line with the market over the next 12 months. HOLD
3=Underperform: The stock appears overvalued, and we believe the stock's total return will be below the market over the next 12 months. SELL

SECTOR RATING

O=Overweight: Industry expected to outperform the relevant broad market benchmark over the next 12 months.
M=Market Weight: Industry expected to perform in-line with the relevant broad market benchmark over the next 12 months.
U=Underweight: Industry expected to underperform the relevant broad market benchmark over the next 12 months.

VOLATILITY RATING

V = A stock is defined as volatile if the stock price has fluctuated by +/-20% or greater in at least 8 of the past 24 months or if the analyst expects significant volatility. All IPO stocks are automatically rated volatile within the first 24 months of trading.

As of: August 6, 2009

38% of companies covered by Wells Fargo Securities, LLC Equity Research are rated Outperform.	Wells Fargo Securities, LLC has provided investment banking services for 36% of its Equity Research Outperform-rated companies.
56% of companies covered by Wells Fargo Securities, LLC Equity Research are rated Market Perform.	Wells Fargo Securities, LLC has provided investment banking services for 36% of its Equity Research Market Perform-rated companies.
6% of companies covered by Wells Fargo Securities, LLC Equity Research are rated Underperform.	Wells Fargo Securities, LLC has provided investment banking services for 30% of its Equity Research Underperform-rated companies.

Important Disclosure for International Clients

The securities and related financial instruments described herein may not be eligible for sale in all jurisdictions or to certain categories of investors. For certain non-U.S. institutional reader (including readers in the EEA), this report is distributed by Wells Fargo Securities International Limited ("WFSIL"). For the purposes of Section 21 of the UK Financial Services and Markets Act 2000 ("the Act"), the content of this report has been approved by WFSIL a regulated person under the Act. WFSIL does not deal with retail clients as defined in the Markets in Financial Instruments Directive 2007. This research is not intended for, and should not be relied upon, by retail clients.

Important Information for Australian Recipients

Wells Fargo Securities, LLC is exempt from the requirements to hold an Australian financial services license in respect of the financial services it provides to wholesale clients in Australia. Wells Fargo Securities, LLC is a registered broker-dealer registered with the U.S. Securities and Exchange Commission, and a member of the New York Stock Exchange, the Financial Industry Regulatory Authority, and the Securities Investor Protection Corp. Wells Fargo Securities, LLC is regulated under U.S. laws which differ from Australian laws. Any offer or documentation provided to you by Wells Fargo Securities, LLC in the course of providing the financial services will be prepared in accordance with the laws of the United States and not Australian laws.

Important Information for Recipients in the Hong Kong Special Administrative Region of the People's Republic of China ("Hong Kong")

For recipients resident in Hong Kong, this research is issued and distributed in Hong Kong by Wells Fargo Securities Limited. Wells Fargo Securities Limited is a Hong Kong incorporated investment firm licensed and regulated by the Securities and Futures Commission to carry on types 1, 4, 6 and 9 regulated activities (as defined in the Securities and Futures Ordinance [the "SFO"]). This research is not intended for, and should not be relied on by, any person other than professional investors (as defined in the SFO). The securities and related financial instruments described herein are not intended for sale nor will be sold to any person other than professional investors (as defined in the SFO). Any sale of any securities or related financial instruments described herein will be made in Hong Kong by Wells Fargo Securities Limited. Please consult your Wells Fargo Securities Limited sales representative or the Wells Fargo Securities Limited office in your area for additional information.

Important Information for Japanese Recipients

This material is distributed in Japan by Wells Fargo Securities (Japan) Co., Ltd., a foreign securities company registered with the Financial Services Agency in Japan.

Additional Disclosures

Wells Fargo Securities, LLC is a U.S. broker-dealer registered with the U.S. Securities and Exchange Commission and a member of the New York Stock Exchange, the Financial Industry Regulatory Authority and the Securities Investor Protection Corp. Wells Fargo Securities International Limited is a U.K. incorporated investment firm authorized and regulated by the Financial Services Authority.

This report is for your information only and is not an offer to sell, or a solicitation of an offer to buy, the securities or instruments named or described in this report. Interested parties are advised to contact the entity with which they deal, or the entity that provided this report to them, if they desire further information. The information in this report has been obtained or derived from sources believed by Wells Fargo Securities, LLC, to be reliable, but Wells Fargo Securities, LLC, does not represent that thisinformation is accurate or complete. Any opinions or estimates contained in this report represent the judgment of Wells Fargo Securities, LLC, at this time, and are subject to change without notice. For the purposes of the U.K. Financial Services Authority's rules, this report constitutes impartial investment research. Each of Wells Fargo Securities, LLC, and Wells Fargo Securities International Limited is a separate legal entity and distinct from affiliated banks.

SECURITIES: NOT FDIC-INSURED/NOT BANK-GUARANTEED/MAY LOSE VALUE

November 11, 2009

WELLS FARGO SECURITIES

Equity Research

American Water Works Company, Inc.

AWK: Potential Upside To Our EPS Outlook?

Market Perform / V

Sector: Water Utilities
Market Weight

Company Note

- **Summary.** 2009-11E EPS maintained. Believe upside could exist to our '10E and '11E but will reevaluate following analyst day. Reiterate Market Perform rating and increasing our valuation range to $20-21 from $18-20.
- **'09E Remains $1.30.** Despite downward sales pressures accelerating in Q3, it appears AWK's EPS remain on track to meet our '09E. While we adjusted our model on 8/6 to reflect lower 1H sales and a wet July, we had not forecast as steep of a Q3 decline. However, it appears that O&M cost containment and a modestly lower expected '09 effective tax rate have largely offset lower Q3 sales.
- **Upside to Our '10E and '11E?** Since 7/1/08, AWK has implemented rate increases intended to provide more than $210MM in annual revenues, including a $31MM PA increase effective 11/7/09; however, the YTD weather impact has blunted the full benefits from materializing. Based on a preliminary analysis of our model that among other things assumes normal weather and an economic stabilization, we believe there could be some upside to our '10E and '11E of $1.43 and $1.56. We intend to fully reevaluate our model and estimates following AWK's December 7 analyst day as we hope to gain greater insight into the appropriate level of O&M expenses going forward. With more than $250MM in rate requests currently pending and the need to continue to seek rate recognition of the utility's significant capital investment program, we believe AWK has the ability to grow EPS in the upper-single-digit range in the near term.
- **Equity Offerings.** Our model includes a small Q4 equity raise; however, we would not be surprised to see AWK roll it into a larger 1H10 offering that could also satisfy '10 equity needs. We believe AWK will look to replicate the combined offering in June during which AWK and RWE sold shares simultaneously. We believe the 23.5% RWE overhang could be completely lifted by mid-year 2010.
- **Q3 Recap.** Reported EPS of $0.52, in-line with consensus, vs. $0.55 in 3Q08. A 7.4% decline in Q3 sales and share dilution more than offset the benefits of rate relief and decreased O&M costs. Continuing AWK's 1H09 theme, Q3 sales were adversely impacted by weather, the economy and declining usage trends which mgmt estimates had a roughly ($0.14) effect. Residential and commercial volumes are each down ~5% YTD while industrial sales are nearly 15% lower. While the main culprit was extremely cool, wet weather across much of AWK's service territory, we believe underlying usage declines have accelerated from historical norms due to current economic pressures as well as a longer-term behavioral shift as consumers recognize the value and cost of water service.

EPS	2008A	2009E Curr.	2009E Prior	2010E Curr.	2010E Prior
Q1 (Mar.)	$0.04	$0.19 A	NC	NE	
Q2 (June)	0.28	0.32 A	NC	NE	
Q3 (Sep.)	0.55	0.52 A		NE	
Q4 (Dec.)	0.23	0.26		NE	
FY	$1.10	$1.30	NC	$1.43	NC
CY	$1.10	$1.30		$1.43	
FY P/E	18.3x	15.5x		14.1x	
Rev.(MM)	$2,337	$2,475		$2,677	

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful

Ticker	AWK
Price (11/11/2009)	$20.10
52-Week Range:	$16-23
Shares Outstanding: (MM)	174.6
Market Cap.: (MM)	$3,509.5
S&P 500:	1,098.16
Avg. Daily Vol.:	1,059,490
Dividend/Yield:	$0.84/4.2%
LT Debt: (MM)	$5,222.0
LT Debt/Total Cap.:	55.9%
ROE:	5.0%
3-5 Yr. Est. Growth Rate:	9.0%
CY 2009 Est. P/E-to-Growth:	1.7x
Last Reporting Date:	11/09/2009 *After Close*

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

Valuation Range: $20.00 to $21.00 from $18.00 to $20.00

Our relative P/E multiple (applying a 10% premium to the electric utility '10E multiple of 12X to our '11E) and DDM analyses results in our 12-18 month fair value range. Risks to AWK shares include execution risk, regulatory risk, capital market risk and RWE follow-on share overhang.

Investment Thesis:

We believe AWK is well-positioned to capitalize on favorable industry dynamics such as significant infrastructure investment, stringent EPA water quality standards and the trend towards consolidation. Our Market Perform rating reflects valuation considerations, capital markets risk and above average execution risk.

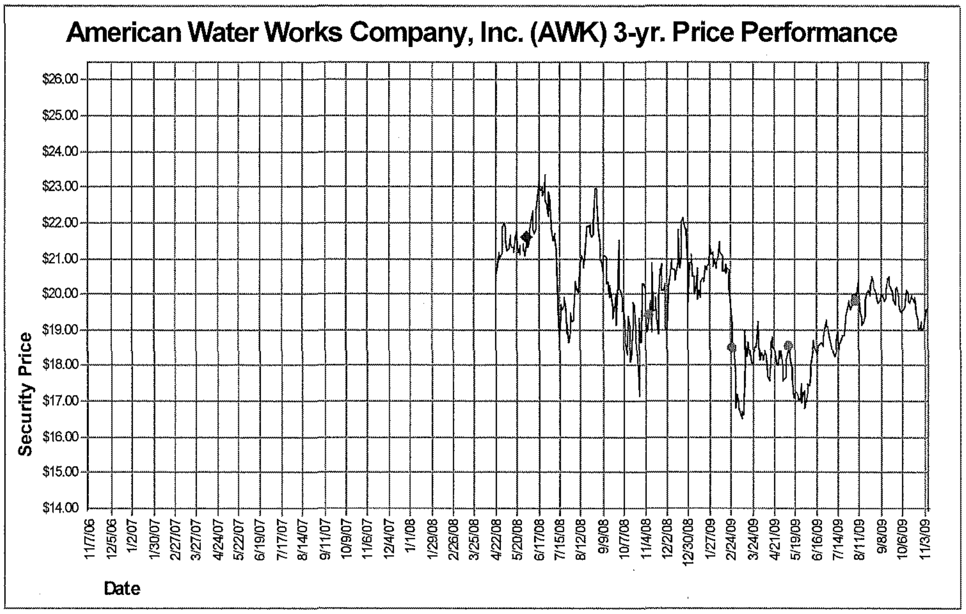
Neil Kalton, CFA, Senior Analyst
(314) 955-5239 / neil.kalton@wachovia.com
Jonathan Reeder, Associate Analyst
(314) 955-2462 / jonathan.reeder@wachovia.com
Sarah Akers, Associate Analyst
(314) 955-6209 / sarah.akers@wachovia.com

Please see page 3 for rating definitions, important disclosures and required analyst certifications

Company Description:

Headquartered in Voorhees, NJ, American Water Works Company, Inc. (AWK) is the largest and most geographically diversified of the investor-owned U.S. water and wastewater services providers. The company has operations in 32 states and Ontario, Canada serving approximately 15.6 million people, including its regulated utilities which serve 3.3 million customers across 20 states. Approximately 90% of revenues are derived from regulated operations. While AWK's regulated revenues are diversified across 20 states, the utility operations are most heavily concentrated in the following states: New Jersey (24%), Pennsylvania (21.7%), Illinois (9.2%), Missouri (9.2%), Indiana (7.4%), California (6.3%) and West Virginia (5.5%). As is typical for water utilities, the majority of AWK's regulated customer base are residential customers (91%), which can be characterized as a fairly predictable/inelastic demand source, and comprise more than 60% of regulated operating revenues. AWK's non-regulated businesses contribute roughly 10% to consolidated revenues and mainly include the operation and maintenance of water and wastewater systems for municipal governments and the U.S. military. Other segments beyond the Contract Operations Group include the Applied Water Management Group and Homeowner Services Group.

Required Disclosures



	Date	Publication Price ($)	Rating Code	Val. Rng. Low	Val. Rng. High	Close Price ($)
	6/2/2008		Kalton			
◆	6/2/2008	21.50	2	21.00	23.00	21.60
●	11/10/2008	19.26	2	19.00	21.00	19.43
●	2/26/2009	18.50	2	18.00	20.00	18.50
●	5/8/2009	18.58	2	17.00	19.00	18.55
●	8/6/2009	19.60	2	18.00	20.00	19.80

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key
- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Valuation Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- □ Split Adjustment

Rating Code Key
- 1 Outperform/Buy
- 2 Market Perform/Hold
- 3 Underperform/Sell
- SR Suspended
- NR Not Rated
- NE No Estimate

Additional Information Available Upon Request

I certify that:
1) All views expressed in this research report accurately reflect my personal views about any and all of the subject securities or issuers discussed; and
2) No part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by me in this research report.

- Wells Fargo Securities, LLC or its affiliates managed or comanaged a public offering of securities for American Water Works Company, Inc. within the past 12 months.
- Wells Fargo Securities, LLC or its affiliates intends to seek or expects to receive compensation for investment banking services in the next three months from American Water Works Company, Inc.
- Wells Fargo Securities, LLC or its affiliates received compensation for investment banking services from American Water Works Company, Inc. in the past 12 months.
- American Water Works Company, Inc. currently is, or during the 12-month period preceding the date of distribution of the research report was, a client of Wells Fargo Securities, LLC. Wells Fargo Securities, LLC provided investment banking services to American Water Works Company, Inc.

Risks to AWK shares include execution risk, regulatory risk, capital market risk and RWE follow-on share overhang.

Wells Fargo Securities, LLC does not compensate its research analysts based on specific investment banking transactions. Wells Fargo Securities, LLC's research analysts receive compensation that is based upon and impacted by the overall profitability and revenue of the firm, which includes, but is not limited to investment banking revenue.

STOCK RATING

1=Outperform: The stock appears attractively valued, and we believe the stock's total return will exceed that of the market over the next 12 months. BUY
2=Market Perform: The stock appears appropriately valued, and we believe the stock's total return will be in line with the market over the next 12 months. HOLD
3=Underperform: The stock appears overvalued, and we believe the stock's total return will be below the market over the next 12 months. SELL

SECTOR RATING

O=Overweight: Industry expected to outperform the relevant broad market benchmark over the next 12 months.
M=Market Weight: Industry expected to perform in-line with the relevant broad market benchmark over the next 12 months.
U=Underweight: Industry expected to underperform the relevant broad market benchmark over the next 12 months.

VOLATILITY RATING

V = A stock is defined as volatile if the stock price has fluctuated by +/-20% or greater in at least 8 of the past 24 months or if the analyst expects significant volatility. All IPO stocks are automatically rated volatile within the first 24 months of trading.

As of: November 11, 2009

42% of companies covered by Wells Fargo Securities, LLC Equity Research are rated Outperform.	Wells Fargo Securities, LLC has provided investment banking services for 35% of its Equity Research Outperform-rated companies.
53% of companies covered by Wells Fargo Securities, LLC Equity Research are rated Market Perform.	Wells Fargo Securities, LLC has provided investment banking services for 33% of its Equity Research Market Perform-rated companies.
6% of companies covered by Wells Fargo Securities, LLC Equity Research are rated Underperform.	Wells Fargo Securities, LLC has provided investment banking services for 36% of its Equity Research Underperform-rated companies.

Important Disclosure for International Clients

The securities and related financial instruments described herein may not be eligible for sale in all jurisdictions or to certain categories of investors. For certain non-U.S. institutional reader (including readers in the EEA), this report is distributed by Wells Fargo Securities International Limited ("WFSIL"). For the purposes of Section 21 of the UK Financial Services and Markets Act 2000 ("the Act"), the content of this report has been approved by WFSIL a regulated person under the Act. WFSIL does not deal with retail clients as defined in the Markets in Financial Instruments Directive 2007. This research is not intended for, and should not be relied upon, by retail clients.

Important Information for Australian Recipients

Wells Fargo Securities, LLC is exempt from the requirements to hold an Australian financial services license in respect of the financial services it provides to wholesale clients in Australia. Wells Fargo Securities, LLC is a registered broker-dealer registered with the U.S. Securities and Exchange Commission, and a member of the New York Stock Exchange, the Financial Industry Regulatory Authority, and the Securities Investor Protection Corp. Wells Fargo Securities, LLC is regulated under U.S. laws which differ from Australian laws. Any offer or documentation provided to you by Wells Fargo Securities, LLC in the course of providing the financial services will be prepared in accordance with the laws of the United States and not Australian laws.

Important Information for Recipients in the Hong Kong Special Administrative Region of the People's Republic of China ("Hong Kong")

For recipients resident in Hong Kong, this research is issued and distributed in Hong Kong by Wells Fargo Securities Limited. Wells Fargo Securities Limited is a Hong Kong incorporated investment firm licensed and regulated by the Securities and Futures Commission to carry on types 1, 4, 6 and 9 regulated activities (as defined in the Securities and Futures Ordinance [the "SFO"]). This research is not intended for, and should not be relied on by, any person other than professional investors (as defined in the SFO). The securities and related financial instruments described herein are not intended for sale nor will be sold to any person other than professional investors (as defined in the SFO). Any sale of any securities or related financial instruments described herein will be made in Hong Kong by Wells Fargo Securities Limited. Please consult your Wells Fargo Securities Limited sales representative or the Wells Fargo Securities Limited office in your area for additional information.

Important Information for Japanese Recipients

This material is distributed in Japan by Wells Fargo Securities (Japan) Co., Ltd., a foreign securities company registered with the Financial Services Agency in Japan.

Additional Disclosures

Wells Fargo Securities, LLC is a U.S. broker-dealer registered with the U.S. Securities and Exchange Commission and a member of the New York Stock Exchange, the Financial Industry Regulatory Authority and the Securities Investor Protection Corp. Wells Fargo Securities International Limited is a U.K. incorporated investment firm authorized and regulated by the Financial Services Authority.

This report is for your information only and is not an offer to sell, or a solicitation of an offer to buy, the securities or instruments named or described in this report. Interested parties are advised to contact the entity with which they deal, or the entity that provided this report to them, if they desire further information. The information in this report has been obtained or derived from sources believed by Wells Fargo Securities, LLC, to be reliable, but Wells Fargo Securities, LLC, does not represent that thisinformation is accurate or complete. Any opinions or estimates contained in this report represent the judgment of Wells Fargo Securities, LLC, at this time, and are subject to change without notice. For the purposes of the U.K. Financial Services Authority's rules, this report constitutes impartial investment research. Each of Wells Fargo Securities, LLC, and Wells Fargo Securities International Limited is a separate legal entity and distinct from affiliated banks.

SECURITIES: NOT FDIC-INSURED/NOT BANK-GUARANTEED/MAY LOSE VALUE