Western State Water Resources Infrastructure Needs and Strategies

Public/Private Sector Roles in Financing/Building

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RBC Capital Markets®

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Industry Overview

Key Industry Themes

Fragmented Market	▪ The U.S. water and wastewater industry is highly fragmented with approximately 52,000 water systems and 16,000 wastewater facilities ▪ 56% of the water systems serve a population of 500 or less
High Barriers to Entry	▪ There are significant market barriers to entry that limit competition, they operate as pure monopolies, and demand for water services is relatively inelastic ▪ Water and wastewater systems are capital intensive with large fixed costs
Aging Infrastructure in Need of Modernization	▪ The EPA estimate that ~$335 billion of water capital spending and $390 billion of wastewater capital spending will be necessary between 2007 and 2026 to replace aging infrastructure and to comply with standards ▪ Investment needs continue to escalate and current funding trends continue to fall short of the needs
Industry Dominated by Municipalities Facing Economic Challenges	▪ Government owned systems make up the vast majority of the U.S. water and wastewater utility segment, accounting for approximately 84% of all water systems and 98% of wastewater systems ▪ Municipalities are facing budget deficits and are unable to meet the growing capital needs which has been further exacerbated by the end of the water stimulus package in 2009
Increased Private Sector Involvement	▪ Have greater access to capital enabling the provision of mandated and other necessary infrastructure upgrades to both water and wastewater systems ▪ Utilities with large customer bases spread across broad geographic regions may more easily absorb the impact of significant variations in precipitation and temperature ▪ Centralized operations allow the private enterprise to benefit from economies of scale
Water Cost Represents a Relatively Low Proportion of Household Expenditure	▪ Water and wastewater rates in the U.S. are among the lowest rates in developed countries ▪ For most U.S. consumers, water and wastewater bills make up a relatively small percentage of household expenditures compared to other utility services
Increased Regulations to Improve Water Quality and the Management of Wastewater	▪ The Clean Water Act in 1972 and the Safe Drinking Water Act in 1974 paved the trend for increasing regulation in the water sector ▪ The United States Environmental Protection Agency has recently become more stringent on regulations

Fragmented Market with High Barriers to Entry

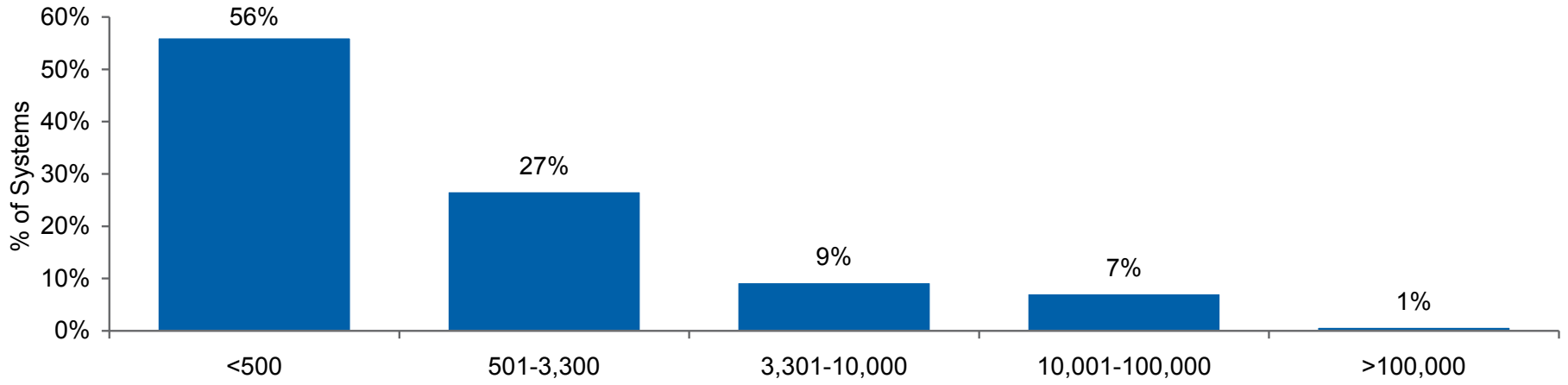
Fragmented Market

- The U.S. water and wastewater industry is highly fragmented with approximately 52,000 water systems and 16,000 wastewater facilities
  - Of the 52,000 water systems, over 92% support a population size of less than 10,000
- This large number of relatively small, fragmented water systems and wastewater facilities results in inefficiencies in the marketplace
  - Municipalities may not have the scale to allow the operating, financial and technological capabilities of larger utilities

High Barriers to Entry

- The water and wastewater industry has high barriers to entry driven by the following factors
  - Substantial capital requirements
  - Long regulatory approval process which often involves obtaining relevant operating approvals (including certificates of public convenience and necessity)
- These high barriers to entry create a natural monopoly for the entity that owns or operates the system
- Combined with the fact that the operations are relatively predictable, inelastic, necessary to sustain life, and do not depend on discretionary spending make it a very attractive and predictable industry in which to operate

Water Systems Measured by Population Size

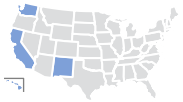


Source: United States Environmental Protection Agency

Increased Private Sector Involvement

- The private sector currently only constitutes 16% of all clean water systems and 2% of wastewater systems
- This ownership mix coupled with struggling local governments create increased opportunities for the private sector
- The municipal bond market is constrained and some of these entities are reluctant to use their limited debt capacity to fund these types of projects
- This has led to an increased amount of privatizations and partnerships with the private sector

Key Industry Players

Company	Key Geographies	Revenue (mm)	Customers[1] (mm)	Description
AMERICAN WATER		$2,666	3.1	▪ Established in 1886, American Water is the largest publicly traded water and wastewater utility company in the U.S. (NYSE: AWK) ▪ Provides services to more than 30 states and Canada
United Water		N/A	2.1	▪ Established in 1869, United Water is a subsidiary of Suez Environment (EPA: SEV) ▪ Provides services to 22 states
AQUA		$712	0.9	▪ Established in 1886, Aqua America is a publicly traded water and wastewater utility company in the U.S. (NYSE: WTR) ▪ Provides services to 10 states
VEOLIA WATER		$961	n/a	▪ Veolia Water, a subsidiary of Veolia Environment (NYSE: VE), a leading global provider of environmental management services ▪ Provides water service to 103mm people and wastewater to 73mm
California Water Service Group		$502	0.5	▪ Established in 1926, California Water Service Group is a publicly- traded water utility company in the U.S. (NYSE: CWT) ▪ Provides services to 4 states throughout the western U.S.
American States Water Company		$419	0.3	▪ Established in 1998, American States Water Co. is a publicly-traded water utility company in the U.S. (NYSE: AWR) ▪ Serves 3 segments: water, electric and contracted services
SJW Corp.		$239	0.2	▪ Established in 1985, SJW Corp. is a publicly- traded water utility company in the U.S. (NYSE: CWT) ▪ Provides water service to more than one million people in California

(1) As of December 31, 2011

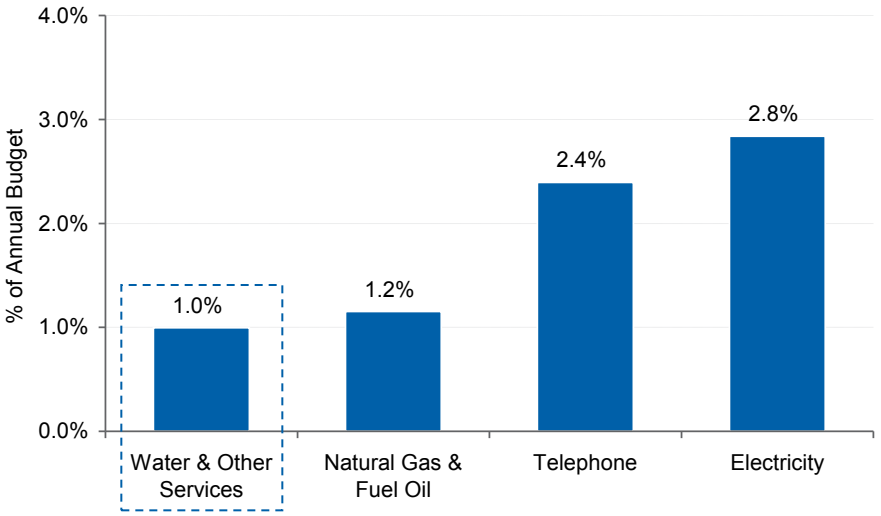
Source: Company filings and websites.

Water Cost Represents a Low Proportion of Household Expenditure

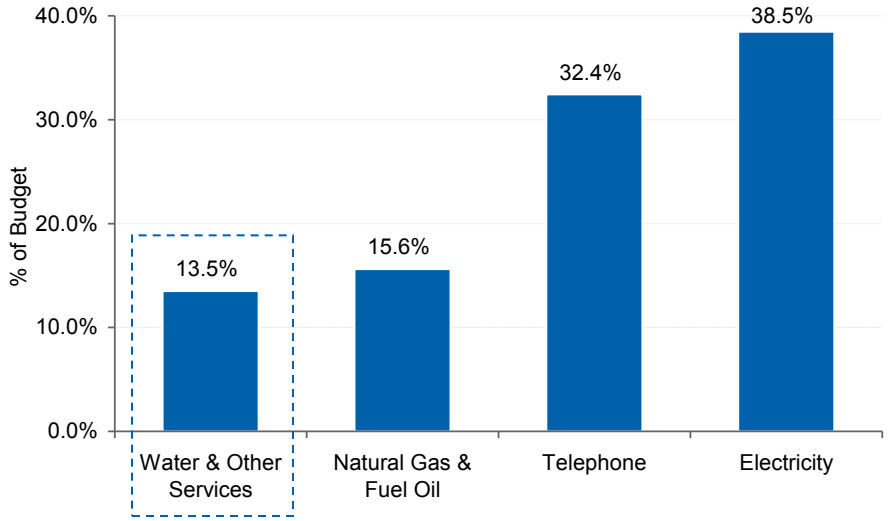
Average Household Expenditure

- Water and wastewater rates in the United States are among the lowest rates in developed countries
  - Compared with other developed countries, the United States has the lowest burden for water/wastewater bills when measured as a percentage of household income
- For most U.S. consumers, water and wastewater bills make up a relatively small percentage of household expenditures compared to other utility services
  - In 2010, the American household spends, on average, only $630 on water and other services, in contrast to an average of $1,796 on electricity

Percent of Annual Household Budget(1)



Percent of Household Utilities Budget(1)



(1) Source: BLS – Consumer Expenditures Survey, September, 2011 (assumes four person household)

Recent Activity in the U.S. Water Market

Current Water Market Performance

- Water market is expected to continue to grow internationally, with approximately 16% of the world's population expected to be serviced by private companies by 2015 (up from 11% in 2007)
- Demand for infrastructure assets remains strong and is expected to continue to grow in the immediate future
- Water sector has consistently outperformed the S&P 500
  - Water utilities have outperformed the S&P 500 by ~30 percentage points since the index peaked in October 2007

Water Sector vs. S&P 500 – Total Returns

Recent Material Headlines

- As of August 2012, 1,584 counties in 32 states had been designated as primary disaster areas by the U.S. Department of Agriculture due to the summer's extreme dryness and heat
- On Feb. 12, 2012 Highstar Capital announced it had entered into a definitive agreement to sell Utilities, Inc. to Corix Utilities for an undisclosed amount
- In November 2011, the California's Class A water utilities and Division of Ratepayer Advocates announced a settlement in the latest cost of capital proceeding. Agreement would set ROE's at 9.99% and is subject to CPUC approval
- On November 21, 2011, Lower Colorado River Authority voted to move forward with a deal to sell 18 water and wastewater systems to Corix Utilities
- On September 20, 2011, Aqua America (NYSE: WTR) announced the formation of a JV with Penn Virginia Resource Partners, an oil and gas gathering and pipeline company, to design, build, and operate a freshwater supply pipeline network for energy companies drilling in the Marcellus Shale
- On July 27, 2011, Connecticut Water Service, Inc. (NASDAQ: CTWS) announced that it entered into an agreement to purchase Aqua Maine, a subsidiary of Aqua America (NYSE: WTR) that owns 11 water systems in Maine, for a total consideration of $53.5 million (including the assumption of $17.7 million of long term debt). The acquisition price represents an EV/RAB of approximately 1.58x
- In February 2011, bcIMC acquired an additional 33.3% indirect stake in Aquarion from Macquarie Essential Assets Partnership for an undisclosed price

Source: FactSet, Market data as of September 12, 2012.
Water Index: American Water Works, Aqua America, California Water Service Group, Consolidated Water Co., American States Water and SJW Corp. Equally weighted.

Water Utilities Exhibit a Highly Attractive Investment Profile

Water utilities have the most favorable dynamics among the U.S. regulated utility sectors

Water Utility Characteristics	Implications
▪ Capital projects focused on maintaining public health and safety standards	▪ Regulators supportive of prudent projects ▪ Favorable capital expenditure provisions continue to be developed at the PUC level
▪ Water bills constitute a low portion of household budget ▪ Essential product – no substitutes	▪ Demand is more price inelastic than electric or gas
▪ Raw input costs (i.e. water and chemicals) are typically less volatile than other utility commodity costs (i.e. coal and natural gas)	▪ More stable rates for customers ▪ Cost forecasting and regulatory lag is more manageable
▪ M&A primarily comprised of small “tuck-in” acquisitions enabling targets to meet health & safety standards	▪ Regulators generally support the strengthening of water systems via M&A
▪ Water storage more feasible and cheaper than electricity or gas storage	▪ Water utilities can be more cost efficient and responsive to demand fluctuations

Case Study: Bayonne Water

Asset Overview

Water System

- The Authority owns and operates a water transmission aqueduct and distribution system that serves the City
- The Water System consists solely of the distribution system and associated existing metering equipment (no pumping stations or storage tanks)
- Water is supplied from the North Jersey District Water Supply Commission and transported to Bayonne through the main aqueduct
- The water distribution system exceeds 96 miles of mains including valves and fire hydrants
- Several interconnections exist to provide alternate means of supply if the aqueduct must be taken out of service

Wastewater System

- Wastewater flows from the City are conveyed to the Passaic Valley Sewerage Commission ("PVSC") by a force main owned jointly by them, the Authority, and the Kearny Municipal Utilities Authority
- It consists of over 83 miles of combined sewers, two interceptor sewers, 12 pumping stations, 55 CSO Control structures, and a total of 29 combined sewer outfalls
- No treatment is required under the Concession Agreement, this is the responsibility of the PVSC
- The system has a total system capacity of 17.6 million of gallons per day

Project Location

1 Monksville Reservoir
2 Wanaque Reservoir
3 Belleville
4 Kearny Water Distribution System
5 City of Bayonne
6 PVSC Facility

Source: Draft Concession Agreement Posted for public record; BMUA Annual Report, News Releases.

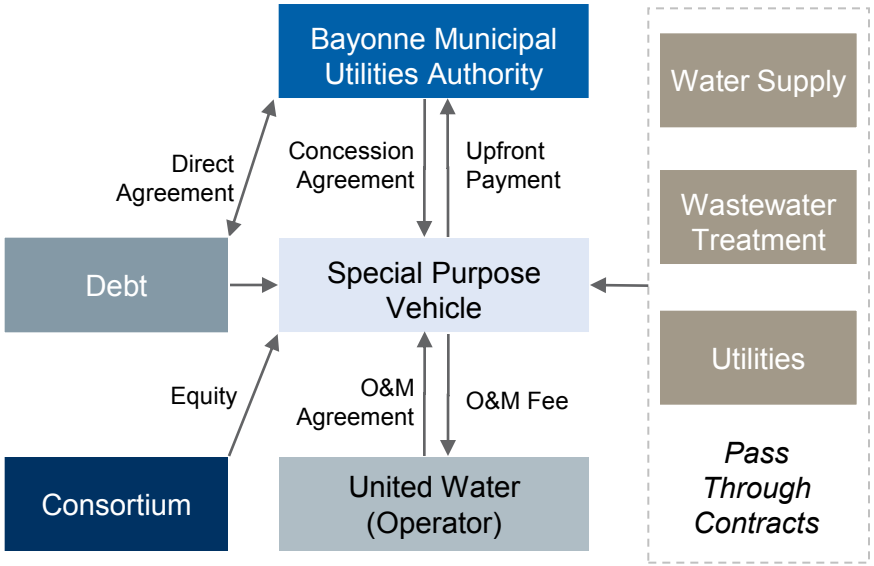
Case Study: Bayonne Water

Transaction Overview

Overview

- Transaction involves the concession of the water, wastewater, storm water and combined sewer overflow systems of the City of Bayonne for a period of 40 years
- KKR and United Water will purchase the interest in the Concession for an up-front consideration of $150 million and an ongoing annual payment to the Authority
  - Will allow full defeasance of the Authority's debt and provided additional cash for general city purposes
- Consortium will have the ability to collect all revenues generated by the System, but will be required to perform all necessary O&M and predetermined annual capital upgrades
- Modest rate increases set out in the Concession, with no ability for Sponsors to increase rates outside of what is stipulated in the agreement
- The transaction will be financed with taxable bonds and sponsor equity

Organizational Structure



Sponsor Overview

Sponsor	Description
KKR	▪ KKR is one of the world's largest global alternative asset managers, with over $62.3 billion in AUM ▪ KKR has a long history of investing in market-leading infrastructure businesses and currently has over $2 billion in dedicated funds for infrastructure investment
United Water	▪ United Water provides water and wastewater services to ~5.7 million people across 22 states in the U.S. ▪ In addition to owning and operating 20 regulated utilities, United Water operates about 100 municipal systems through public-private partnerships and contract agreements ▪ Founded in 1869, United Water is a subsidiary of Suez Environment

Source: Draft Concession Agreement Posted for public record.

Case Study: Bayonne Water

Key Transaction Advantages

1. Defeasance of existing debt and additional capital to be used for general City purposes
2. Maintain ownership of the asset via a long term concession structure
3. Structured to have a rate freeze period during the initial few years with modest rate increases throughout the life of the project
4. Require private entity to perform investment in the system to replace aging infrastructure
5. Improved level of customer service available from a large private entity
6. Proven structure with successful market precedents