



COMPANY UPDATE / ESTIMATE CHANGE

Key Metrics

CWT - NYSE - as of	4/26/17	\$38.30
Price Target		--
52-Week Range	\$27.05 -	\$38.65
Shares Outstanding (mm)		48.0
Market Cap. (\$mm)		\$1,837.4
1-Mo. Average Daily Volume		185,978
Institutional Ownership		73.6%
LTD / Total Capital	Q1'17	44.5%
ROE--unadjusted	TTM	7.8%
Book Value / Share	Q1'17	\$13.57
Price / Book Value		2.8x
Dividend Yield		1.9%
EBITDA Margin		--

EPS FY 12/31

		Prior	Current	Prior	Current
	2016A	2017E	2017E	2018E	2018E
1Q	(\$0.02)	--	\$0.02	A --	--
2Q	\$0.24	\$0.39	\$0.39	--	--
3Q	*\$0.52	\$0.70	\$0.70	--	--
4Q	*\$0.23	\$0.23	\$0.26	--	--
Year	*\$0.97	\$1.39	\$1.37	\$1.49	\$1.49
P/E	39.5x		28.0x		25.7x

*excludes benefit from non-recurring tax gain

Net Revenue (\$MM; Rev - H2O Production Costs)

		Prior	Current	Prior	Current
	2016A	2017E	2017E	2018E	2018E
1Q	\$80.7	--	\$80.0	A --	--
2Q	\$94.9	\$107.0	\$107.2	--	--
3Q	\$114.1	\$130.5	\$130.7	--	--
4Q	\$99.8	\$105.7	\$105.9	--	--
Year	\$389.4	\$431.7	\$423.8	\$452	\$447

Company Description: *California Water Service Group is the third-largest publicly traded water utility in the United States by market capitalization. Its regulated public utilities serve approximately 500,000 customers. Overall, it provides water services to over two million people in 100 communities in California, Washington, New Mexico, and Hawaii.*

Water Utilities

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California Water Service Group

CWT – NYSE – Neutral-2

Positive Start to 2017 in Q1; Reiterating Neutral Rating.

Investment Highlights

- CWT reported Q1'17 EPS of \$0.02 versus (\$0.02) in Q1'16; consensus was looking for \$0.05 while we were a tad higher at \$0.07. We primarily attribute the growth to lower operating costs.
- Net revenue (rev – production costs) slipped 0.9%, as roughly +\$9MM of rate activity was offset by usage items. Accrued unbilled revenues represented a ~\$3MM yr/yr headwind, while wet conditions drove full quarter usage lower.
- We estimate drought memoranda spending at just \$200k in Q1, down from \$2MM in the year-ago period. More comprehensive, total Op Ex (G&A, Maintenance, Other) fell 10.7% yr/yr in Q1.
- CWT's WRAM balance (revenue to be recovered in the future) was \$48MM on 3/31, but up moderately from \$37MM at year-end 2016 due to low usage in Q1.
- Cal Water's CA Cost of Capital filing occurred in early-April. Risk here is to allowed returns (and the cap structure) for 2018.
- During Q & A, management spoke on the call this morning of a 'retooled' M&A team with a 'sharper focus.' We believe the pivot in narrative is worth noting, but do not make any changes to our model.
- Reflecting downside to our first quarter estimate, our 2017E EPS slides to \$1.37, but our outlook is substantially unchanged extending out thru 2018. Our 2018E EPS remains \$1.49.
- We are reiterating our Neutral rating. We are pleased with performance in Q1, and while a wet quarter held back results a bit, we nonetheless believe CWT is positioned for a strong 2017. Having said that, we believe shares are fairly priced in the market.

**Note Important Disclosures on Pages 5-6
Note Analyst Certifications on Page 5**

ADDITIONAL DISCUSSION—Q1 COMMENTS

California Water holds one of the least important ‘Q1s’ from an EPS perspective in the industry, and is consistently one of the more volatile earners across sequential quarters due to accrued unbilled accounting. With that in mind, we are unconcerned with CWT’s nickel miss to our EPS target for the quarter, and are more encouraged by what seems to be a clean implementation of the 2015 general rate case that was finalized in late-December of last year. Related to this, the alteration of a few underlying items in our model tied to the case (i.e. depreciation rates, AFUDC) do not seem to have delivered any major surprises.

ADDITIONAL DISCUSSION—MULTIPLE ITEMS

On April 7, Governor Brown in CA declared an official end to the drought emergency in 54 of 58 counties. Investors may recall that drought-driven surcharge rates were suspended in July of last year, which from a cash flow perspective probably had a bigger impact on CWT than the official proclamation. As CWT investors we have not ‘feared’ the drought for some time now, but we remain cognizant of weather concerns. Formulation of water use rules in CA remains ongoing, but implementation is still years away.

Our position on the Cost of Capital (CoC) filing has not changed much over the past ~2 months. Having a request to delay the CoC filing denied (as had been the case for several years) suggest to us some risk; however, we view the current ~9.5% ROE as fair, particularly with the narrative in interest rates having shifted to a hiking cycle. Proceedings should be concluded this year, but any changes will not impact 2017.

SUITABILITY

We assign CWT a suitability rating of ‘2.’ A complete description of our suitability scale is on page 5. We view Cal Water as a strong operator, with generally favorable regulatory constructs, and consistent cash flow predictability as an owner of regulated monopoly franchises. Size (smaller than most Utility sector peers) and high sensitivity to a single state (CA) are the primary factors that push CWT comfortably below our most conservative ‘1’ suitability rating. A strong history of returning capital to shareholders, exceedingly low cyclicalities under usual circumstances due to revenue decoupling, and industry-appropriate leverage keep the company above our more aggressive ‘3’ rating.

CONSIDERATIONS AND RISKS

We view all companies in the Water Utilities industry as being subject to significant regulatory and political risk. Utility operations are heavily regulated; negative rate-making climates and/or new environmental restrictions may affect the company’s ability to earn a sufficient return on invested capital. Weather, natural disaster, and availability of water supplies could negatively impact sources of water, demand for water services, and a utility’s ability to supply water to customers. Risks associated with the collection, treatment, and disposal of wastewater could also impose significant costs.

Significant capital expenditures are required to maintain infrastructure and expand rate base. Should the company suffer from the lack of ability to secure appropriate funding to make investments, or if delays are incurred in completing projects, operating results could be negatively affected. Contamination of water could result in service interruptions or cause enforcement actions. Water assets can be subject to condemnation through eminent domain. The company’s non-regulated businesses provide performance guarantees and have long-term contracts. Additionally, the company is subject to all other risks that result from operating as a publicly traded company.

Our Suitability rating is 2 on a 1-to-4 scale (1 = most conservative, 4 = most aggressive).

Additional information is available upon request.

California Water Service Group

Income Statements (000's)	FY'14	FY'15	Q1'16	Q2'16	Q3'16	Q4'16	FY'16	Q1'17	Q2'17E	Q3'17E	Q4'17E	FY'17E	FY'18E
Operating Revenue	\$597,499	\$588,368	\$121,727	\$152,445	\$184,268	\$150,930	\$609,370	\$122,036					
Water Production Costs	223,941	207,926	41,069	57,589	70,175	51,160	219,993	42,068					
Net Revenue--Water Ops	373,558	380,442	80,658	94,856	114,093	99,770	389,377	79,968	107,210	130,680	105,890	423,750	447,390
G & A	97,373	113,110	27,827	23,366	23,844	23,437	98,474	25,249	24,301	21,002	28,041	98,590	100,070
Other Op Exp	65,807	62,848	17,302	17,803	18,261	22,316	75,682	15,924	18,160	18,630	21,700	74,410	79,000
Drought Memorandum Acct		4,400	2,000	1,100	1,300	0	4,400	200	250	250	250	950	0
Maintenance	19,854	21,463	6,063	5,934	5,545	5,451	22,993	6,112	5,534	5,270	5,070	21,990	20,880
D & A	61,217	61,381	16,046	15,842	15,884	15,827	63,599	19,201	17,190	17,140	17,140	70,670	74,120
Income Tax	26,727	24,528	(925)	6,870	13,247	5,612	24,804	(884)	9,200	19,700	8,800	36,820	43,300
Property and Other Taxes	20,733	21,559	6,075	5,407	5,957	5,792	23,231	6,116	5,460	6,020	5,850	23,450	23,680
Other Op Exp	291,711	309,289	74,388	76,322	84,038	78,435	313,183	71,918	80,090	88,010	86,850	326,880	341,050
Net Operating Income	81,847	71,153	6,270	18,534	30,055	21,335	76,194	8,050	27,120	42,670	19,040	96,870	106,340
% of Net Rev	21.9%	18.7%	7.8%	19.5%	26.3%	21.4%	19.6%	10.1%	25.3%	32.7%	18.0%	22.9%	23.8%
Other Income and Exp:													
Total Other Inc / (Exp)	1,839	1,134	267	571	531	1,613	2,982	1,298	(36)	(203)	2,096	2,380	1,430
Income Before Interest	83,686	72,287	6,537	19,105	30,586	22,948	79,176	9,348	27,084	42,467	21,136	99,250	107,770
Interest Expense	28,483	29,185	8,065	8,434	8,485	8,482	33,466	8,710	8,990	9,530	9,570	36,800	38,870
Less: Capitalized Interest // AFUDC	1,535	1,915	730	837	774	624	2,965	494	750	750	750	2,744	3,000
Total Interest Expense	26,948	27,270	7,335	7,597	7,711	7,858	30,501	8,216	8,240	8,780	8,820	34,056	35,870
Net Income	\$56,738	\$45,017	(\$798)	\$11,508	\$22,875	\$15,090	\$48,675	\$1,132	\$18,844	\$33,687	\$12,316	\$65,194	\$71,900
EPS (FD)	\$1.19	\$0.94	(\$0.02)	\$0.24	\$0.48	\$0.31	\$1.01	\$0.02	\$0.39	\$0.70	\$0.26	\$1.37	\$1.49
Adjusted EPS (FD)					\$0.52	\$0.23	\$0.97						
Diluted Avg Shares	47,819	47,880	47,905	47,972	47,969	47,969	47,954	47,984	48,024	48,064	48,104	48,044	48,204
Dividend	\$0.650	\$0.670	\$0.1725	\$0.1725	\$0.1725	\$0.1725	\$0.690	\$0.1800	\$0.1800	\$0.1800	\$0.1800	\$0.720	\$0.740
Rate of Change Analysis:													
Net Revenue--Water Ops	4.3%	1.8%	5.0%	3.8%	-7.3%	11.9%	2.3%	-0.9%	13.0%	14.5%	6.1%	8.8%	5.6%
G & A	-0.7%	16.2%	0.5%	-12.3%	-22.4%	-16.4%	-12.9%	-9.3%	4.0%	-11.9%	19.6%	0.1%	1.5%
Operating Income	10.6%	-13.1%	-16.4%	12.4%	-6.7%	42.6%	7.1%	28.4%	46.3%	42.0%	-10.8%	27.1%	9.8%
EPS	20.2%	-20.7%	-150.6%	16.7%	-1.1%	77.7%	2.9%	nm	63.6%	35.1%	-18.6%	41.9%	8.6%
EBITDA	12.2%	-7.5%	-8.7%	11.6%	-5.8%	26.4%	4.8%	23.3%	29.7%	34.3%	5.2%	24.2%	9.5%
Margin Analysis:													
G & A / Net Rev	26.1%	29.7%	34.5%	24.6%	20.9%	23.5%	25.3%	31.6%	22.7%	16.1%	26.5%	23.3%	22.4%
Maintenance / Net Rev	5.3%	5.6%	7.5%	6.3%	4.9%	5.5%	5.9%	7.6%	5.2%	4.0%	4.8%	5.2%	4.7%
Net Income / Net Rev	15.2%	11.8%	-1.0%	12.1%	20.0%	15.1%	12.5%	1.4%	17.6%	25.8%	11.6%	15.4%	16.1%
Tax rate	33.0%	36.0%	48.2%	38.7%	37.3%	30.8%	35.5%	0.4%	33.3%	37.1%	42.2%	37.0%	38.0%
					*Adjusting out \$3.2MM capital charge							*+\$0.05 frm 2016 drgt mem (+\$0.01 y/y)	

Source: Company reports and Hilliard Lyons estimates

California Water Service Group

California Water Service Group													
Summary Balance Sheet	FY'14	FY'15	Q1'16	Q2'16	Q3'16	Q4'16	FY'16	Q1'17	Q2'17E	Q3'17E	Q4'17E	FY'17E	FY'18E
Cash	\$19,587	\$8,837	\$30,878	\$30,826	\$21,351	\$25,492	\$25,492	\$11,990	\$7,090	\$31,990	\$35,030	\$35,030	\$23,270
A/R--Customers	25,803	31,512	31,397	36,635	45,376	30,305	30,305	24,685	41,410	51,970	32,160	32,160	33,610
Regulatory Balance Acct	53,199	35,052	31,554	26,453	19,811	30,332	30,332	30,661	30,660	30,660	30,660	30,660	30,660
Other	55,535	52,177	54,692	65,086	64,589	55,940	55,940	60,869	68,340	67,820	58,740	58,740	61,680
Total CA	154,124	127,578	148,521	159,000	151,127	142,069	142,069	128,205	147,500	182,440	156,590	156,590	149,220
Net Utility Plant	1,590,431	1,701,768	1,739,679	1,785,077	1,817,751	1,859,277	1,859,277	1,888,005	1,925,820	1,968,680	2,001,540	2,001,540	2,142,420
Regulatory assets	390,331	361,893	361,249	363,321	363,597	355,930	355,930	367,476	367,476	367,476	367,476	367,476	367,576
Goodwill	2,615	2,615	2,615	2,615	2,615	2,615	2,615	2,615	2,615	2,615	2,615	2,615	2,615
Other	49,850	52,241	47,741	48,110	50,953	51,854	51,854	53,997	50,520	53,500	54,450	54,450	57,170
Total Assets	\$2,187,351	\$2,246,095	\$2,299,805	\$2,358,123	\$2,386,043	\$2,411,745	\$2,411,745	\$2,440,298	\$2,493,931	\$2,574,711	\$2,582,671	\$2,582,671	\$2,719,001
A/P	59,395	66,380	65,354	77,604	84,052	77,813	77,813	69,276	87,710	96,270	82,590	82,590	86,300
CP of LTD	6,607	6,600	6,113	6,133	6,130	26,208	26,208	36,139	20,000	12,730	12,730	12,730	100,000
ST Borrowings	79,115	33,615	34,500	75,100	57,100	97,100	97,100	130,100	70,100	80,100	90,100	90,100	156,100
Other	72,589	41,860	52,176	43,176	56,699	49,109	49,109	57,858	45,330	59,530	51,560	51,560	54,140
Total CL	217,706	148,455	158,143	202,013	203,981	250,230	250,230	293,373	223,140	248,630	236,980	236,980	396,540
LTD	419,233	512,287	557,849	555,787	555,536	531,745	531,745	521,715	652,740	660,020	660,020	660,020	573,650
Other LT liab	923,786	943,198	950,846	963,563	974,514	970,299	970,299	973,877	982,830	994,000	989,700	989,700	1,009,490
Shareholders' Equity	626,626	642,155	632,967	636,760	652,012	659,471	659,471	651,333	635,221	672,061	695,971	695,971	739,321
Total Liab & SE	\$2,187,351	\$2,246,095	\$2,299,805	\$2,358,123	\$2,386,043	\$2,411,745	\$2,411,745	\$2,440,298	\$2,493,931	\$2,574,711	\$2,582,671	\$2,582,671	\$2,719,001
Summary Cash Flow	FY'14	FY'15	Q1'16	Q2'16	Q3'16	Q4'16	FY'16	Q1'17E	Q2'17E	Q3'17E	Q4'17E	FY'17E	FY'18E
Net income	\$56,738	\$45,017	(\$798)	\$11,508	\$22,875	\$15,090	\$48,675	\$1,130	\$18,840	\$33,690	\$12,320	\$65,190	\$71,900
D&A	61,217	61,381	16,046	15,842	15,884	15,827	63,599	19,201	17,190	17,140	17,140	70,670	74,120
Deferred Tax	34,125	24,393	5,000	7,000	9,500	5,318	26,818	5,000	1,000	20,000	15,000	41,000	25,000
(Inc) / Dec in Wrk Cap	(2,430)	(7,948)	10,388	(7,281)	18,369	(630)	20,846	574	(18,289)	12,720	7,240	2,245	1,900
Operating CF	149,650	122,843	30,636	27,069	66,628	35,605	159,938	25,905	18,741	83,550	51,700	179,105	172,920
Cap Ex	(132,015)	(176,833)	(56,463)	(59,692)	(50,251)	(62,532)	(228,938)	(51,900)	(55,000)	(60,000)	(50,000)	(216,900)	(215,000)
Acquisitions	-	-	-	-	-	-	-	-	-	-	-	-	-
Dividends	(31,063)	(32,066)	(8,258)	(8,274)	(8,275)	(8,274)	(33,081)	(8,640)	(8,640)	(8,650)	(8,660)	(34,590)	(35,670)
Free Cash Flow	(13,428)	(86,056)	(34,085)	(40,897)	8,102	(35,201)	(102,081)	(34,635)	(44,899)	14,900	(6,960)	(72,385)	(77,750)
Issuance LTD	497	99,343	50,039	(216)	-	-	49,823	-	100,000	20,000	-	120,000	12,700
(Retirement) LTD	(8,705)	(7,003)	(254)	(2,209)	(402)	(4,131)	(6,996)	-	-	(20,000)	-	(20,000)	(12,700)
ST Debt Borrowings	117,300	94,303	54,500	48,600	2,000	40,000	145,100	-	40,000	10,000	10,000	60,000	76,000
ST Debt (Repayments)	(85,000)	(141,000)	(53,615)	(8,000)	(20,000)	-	(81,615)	9,900	(100,000)	-	-	(90,100)	(10,000)
Stock Issued	-	-	-	-	-	-	-	-	-	-	-	-	-
Contrib / (Refund) for Const	5,688	9,300	5,996	1,995	5,001	1,571	14,563	-	-	-	-	-	-
Net Cash Flow	16,352	(31,113)	22,581	(727)	(5,299)	2,239	18,794	(24,735)	(4,899)	24,900	3,040	(2,485)	(11,750)
EBITDA	169,791	157,062	21,391	41,246	59,186	42,774	164,597	26,367	53,510	79,510	44,980	204,360	223,760
EV / TTM EBITDA	9.3x	10.3x	11.7x	13.9x	13.4x	13.1x	13.1x	14.1x	13.8x	12.3x	12.1x	12.1x	11.2x
Selected Financial Statistics	FY'14	FY'15	Q1'16	Q2'16	Q3'16	Q4'16	FY'16	Q1'17E	Q2'17E	Q3'17E	Q4'17E	FY'17E	FY'17E
Book Value	\$13.10	\$13.41	\$13.21	\$13.27	\$13.59	\$13.75	\$13.75	\$13.57	\$13.23	\$13.98	\$14.47	\$14.47	\$15.32
Price / Book	1.9x	1.7x	2.0x	2.6x	2.4x	2.5x	2.5x	2.8x	2.9x	2.7x	2.6x	2.6x	2.5x
Net Indebtedness / Total Capital	43.6%	45.8%	47.3%	48.8%	47.8%	48.8%	48.8%	50.9%	53.7%	51.8%	51.1%	51.1%	52.2%
LTD / Total Capital	40.1%	44.4%	46.8%	46.6%	46.0%	44.6%	44.6%	44.5%	50.7%	49.5%	48.7%	48.7%	43.7%
ROE (TTM)	9.4%	7.1%	6.7%	7.0%	6.6%	7.6%	7.6%	7.8%	9.0%	10.5%	10.0%	10.0%	10.2%

Source: Company reports and Hilliard Lyons estimates

Analyst Certification

I, Spencer E. Joyce, CFA, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject company(ies) and its (their) securities. I also certify that I have not been, am not, and will not be receiving direct or indirect compensation in exchange for expressing the specific recommendation(s) in this report.

Important Disclosures

Hilliard Lyons' analysts receive bonus compensation based on Hilliard Lyons' profitability. They do not receive direct payments from investment banking activity.

Suitability Ratings

- 1** - A large cap, core holding with a solid history
- 2** - A historically secure company which could be cyclical, has a shorter history than a "1" or is subject to event driven setbacks
- 3** - An above average risk/reward ratio could be due to small size, lack of product diversity, sporadic earnings or high leverage
- 4** - Speculative, due to small size, inconsistent profitability, erratic revenues, volatility, low trading volume or a narrow customer or product base

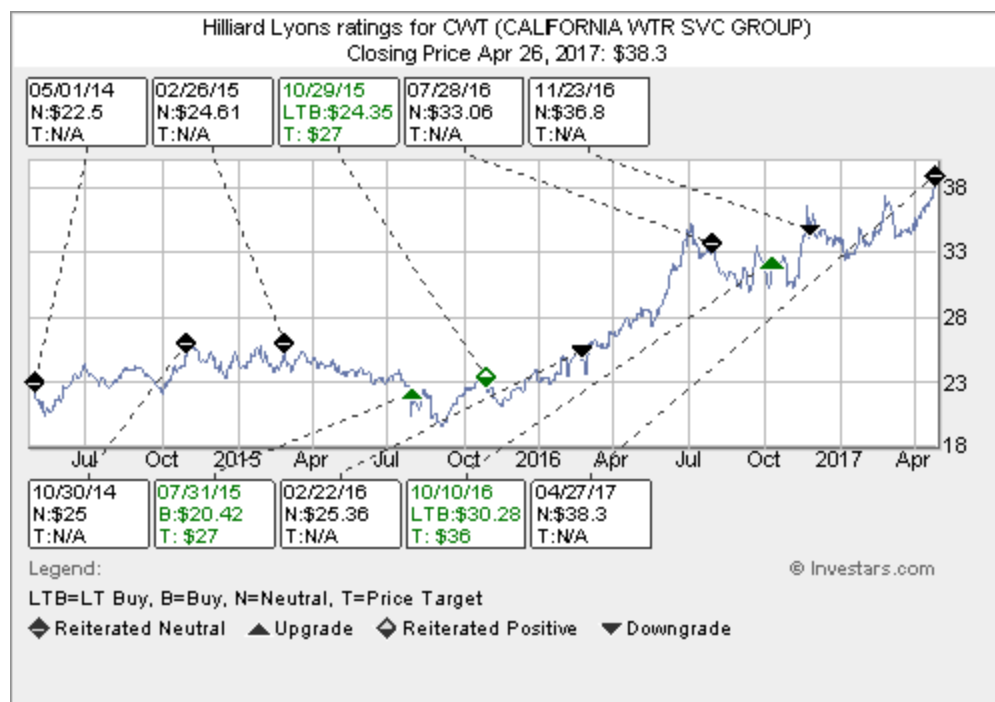
Investment Ratings

Buy - We believe the stock has significant total return potential in the coming 12 months.

Long-term Buy - We believe the stock is an above average holding in its sector, and expect solid returns to be realized over a longer time frame than our Buy rated issues, typically 2-3 years.

Neutral - We believe the stock is an average holding in its sector, is currently fully valued, and may be used as a source of funds if better opportunities arise.

Underperform - We believe the stock is vulnerable to a price setback in the next 12 months.



Hilliard Lyons Recommended Issues			Investment Banking Provided in Past 12 Mo.	
Rating	# of Stocks Covered	% of Stocks Covered	Banking	No Banking
Buy	36	30%	14%	86%
Hold/Neutral	71	58%	6%	94%
Sell	15	12%	7%	93%

As of 5 April 2017

Other Disclosures

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