WWEMA
Water & Wastewater Equipment Manufacturers Association Inc.

A Look at Design-Build & Contract Operations

Presented By:

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Overview

- Market Drivers & Effects
- Regionalization Vs. Decentralization
- Contract Operations/Utility Outsourcing
- Design-Build-Operate
- Market Outlook
- Legislative Initiatives
- Implications for Water/Wastewater Equipment Manufacturers
- Questions & Answers

Market Drivers & Effects

Driver

- Aging Infrastructure
- System Expansion
- Regulatory Mandates
- Water Scarcity
- Security Requirements

Mitigation Option

- Pursue Government Assistance (Grants, Loans, Regulatory Relief)

Enhance System Efficiencies

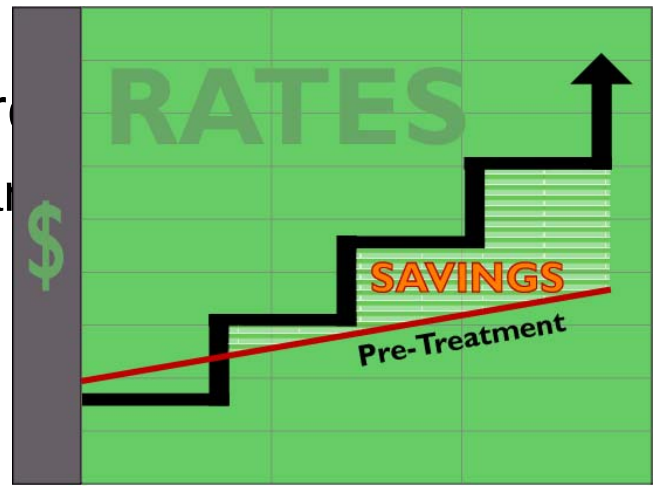
- Regionalize/Decentralize
- Lower Operating Costs/Improve Efficiencies
- Lower Capital Costs Related to Expansion/Replacement

Regionalization vs. Independence

- Effective Method of Capturing Scale Economics
  - Florida: Small Private Systems/Large Municipal
  - Pennsylvania: Small Municipal Systems/Large Private

But…

- Large/Bulk Wastewater Customers Ar
  - Significantly Affected by Rate Increases a
  - Can Build Their Own Systems to:
    - Save Money
    - Gain Independence
    - Improve Predictability



Decentralized Systems Will Play A Role in the Future

Improving Operational Efficiency:
Contract Operations/Utility Outsourcing

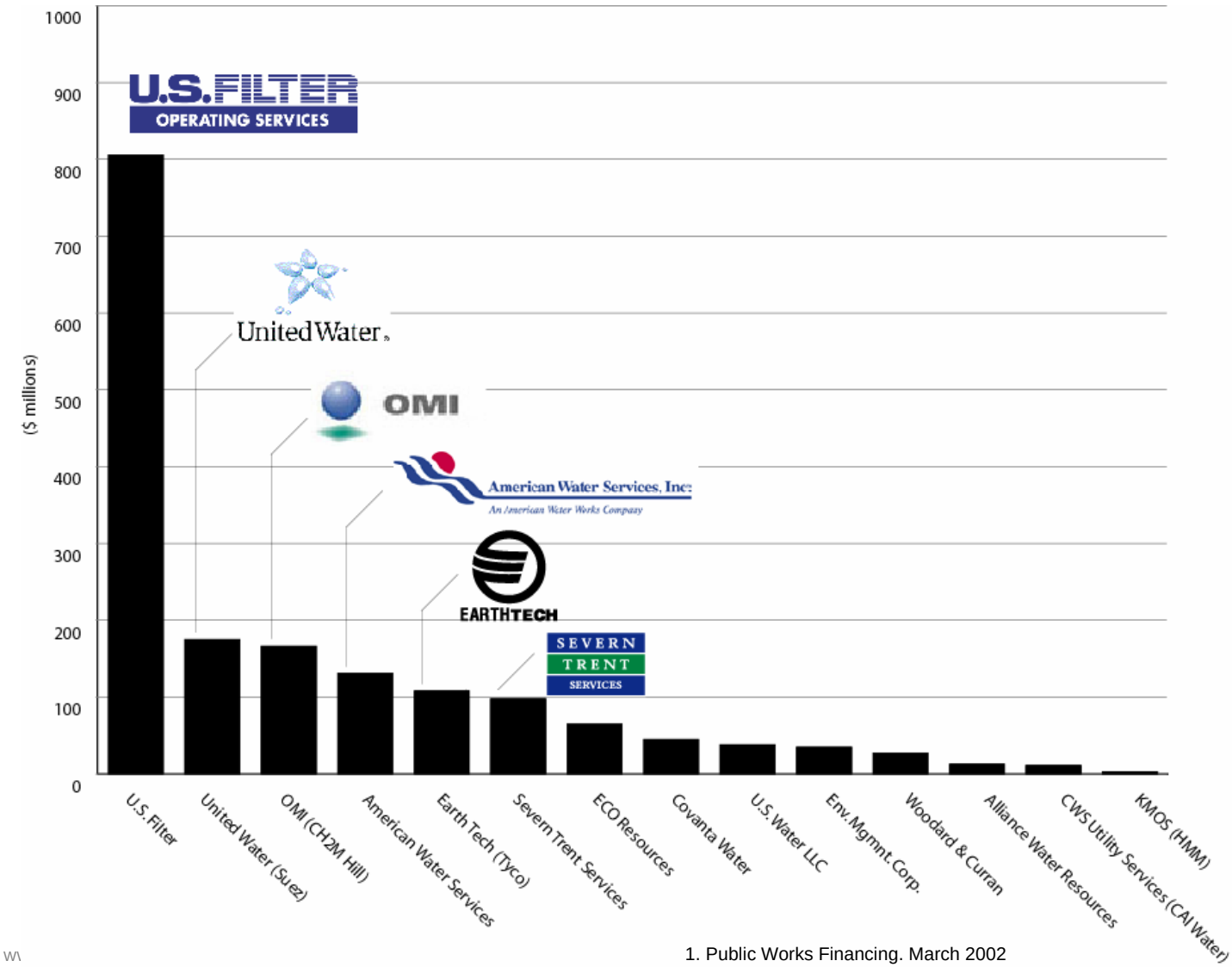
Growth Drivers

- Compelling Need to Improve Efficiency
- Lower Operating Costs (20%-40%)
- Risk Transfer (Under Operator's Control)
- Technical Expertise
- Improved Revenue Capture (Metering)

Growth Restraints

- Often Highly Political
- Organized Labor
- Lost Expertise/Control
- Monitoring Requirements
- Municipal Re-Engineering
- Cannibalistic Competition

Competitive Landscape: Contract Operations[1]



1. Public Works Financing. March 2002

Industry Characteristics/Trends

- Performance Characteristics

Project Gross Margins:	10% to 20%
Term:	5 Years – 20 Years
Opportunities for Margin Improvement:	Add-On Work & Learning Curve Efficiencies
Contract Renewal Rate:	~ 80%

- Risk Assumption During Operations
  - Maintenance Deductible
  - Fine Protection Unless:
    - Excessive Flows or Loadings
    - System Design Constraints
    - Force Majeure
  - Cost Certainty Over Contract Term (Barring Change-In-Law)

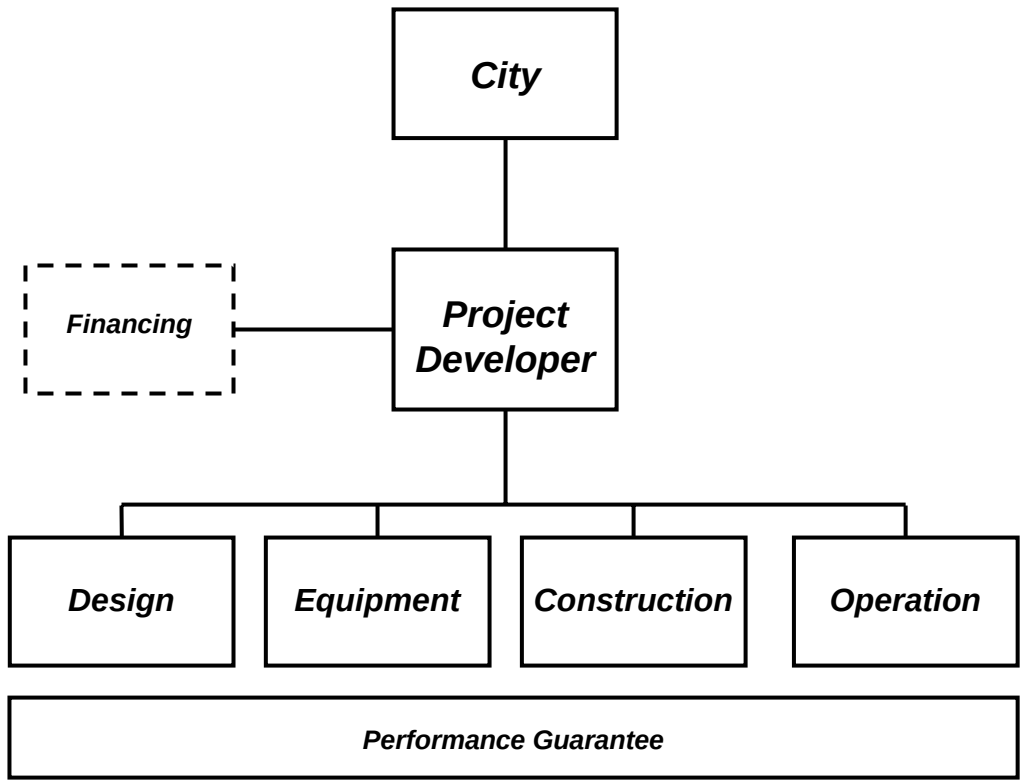
Design-Build-Operate

Growth Drivers

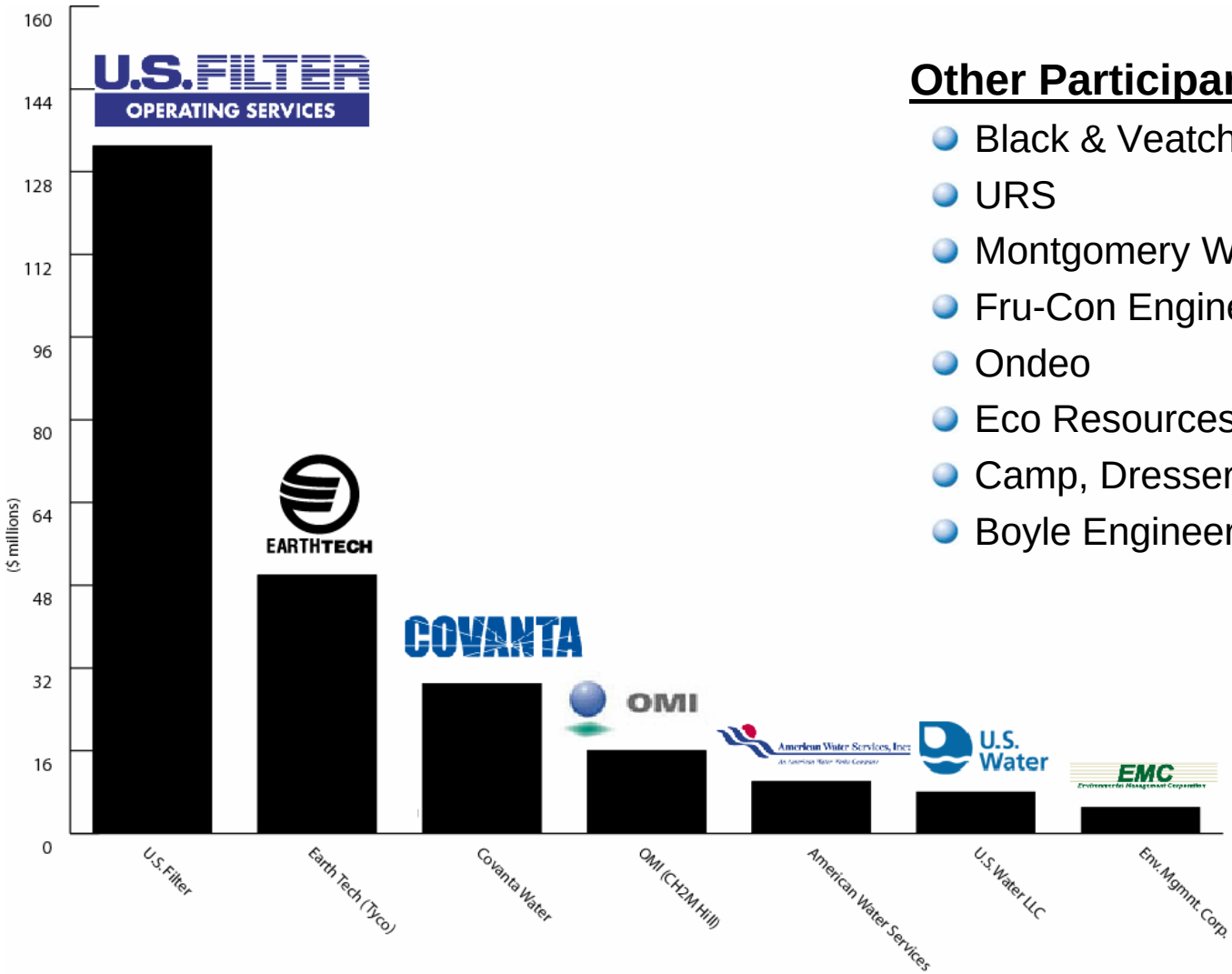
- Single Point of Accountability
- Private Sector Risk Assumption
- Acceleration of Project Delivery
- Reduced Lifecycle Costs

Growth Restraints

- Less Discretion in Design & Change Orders
- Requires More Planning for Procurement
- Output Oriented
- Legal Systems Need to Adapt
- Developer Financial Health is Important



Competitive Landscape: Design-Build Revenues[1]



Other Participants

- Black & Veatch
- URS
- Montgomery Watson - Harza
- Fru-Con Engineering
- Ondeo
- Eco Resources
- Camp, Dresser & McKee
- Boyle Engineering

1. Public Works Financing. March 2002

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Industry Characteristics/Trends

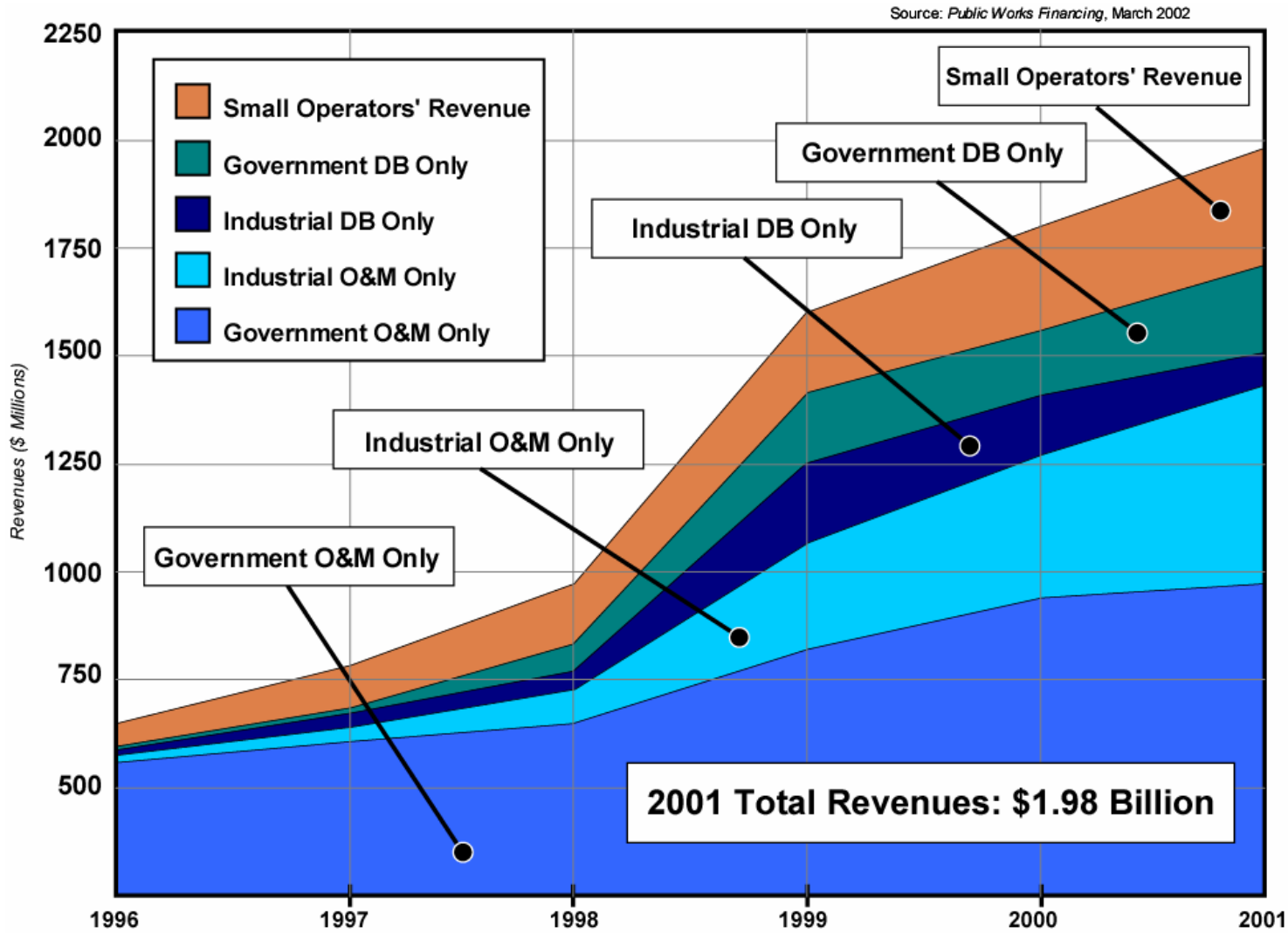
- Performance Characteristics

Target Margins:	3-10%
Growth in Number of Projects/Year:	<5 Completed in 1995 >25 Completed in 2002 (~$5 Billion Total[1])
Average Size:	73% < $50 Million[1]
Capital Cost Savings:	39%[2]

- Risk Assumption During Construction
  - Cost, Schedule, Performance
  - Liquidated Damages for Short-Falls
  - Secured by Bonds, Letters of Credit & Corporate Guarantees

1. Molenaar. 2002
2. Eisenhardt. 2002

Market Growth



Contract Operations/D-B-O

Market Outlook

- Less Competition/Improved Margins Due to Improved Project Screening & Consolidation
- Rationalized Risk Transfer
- Sustained Growth in Contract Operations
- Faster Growth in Design-Build
- Contract Operations to Experience Additional Consolidation
- Top 5 or 6 Will Offer Integrated D-B-O Package

Legislative Initiatives

Proposed Options	Impact on DBO/Contract Ops Market
Federal Grant Program	***Negative*** – Creates Market Distortions/Inefficiencies
Loans & Credit Enhancements	***Positive*** – Provides Small Communities Access to Needed Capital
Remove Cap on Private Activity Bonds	***Positive*** – Affords Greater Flexibility in Financing
Economic Stimulus Bill	***Positive*** – Particularly for Industrial Systems

Job Creation & Worker's Assistance Act - Background

- Signed into Law on March 9, 2002
- Provision for 30% Depreciation on Qualified Property
- Must Be New & Placed in Service Between 9/01 & 9/04
- 30% is Calculated on the Original Cost of the Asset Price and is Deducted in the Year Placed in Service
- Basis for MACRS = Original Cost – 30% Deduction
- Some States Have Not Signed onto New Treatment

For Example:

WWTP = $10,000,000
1st Year Deduction = $ 3,000,000
+ MACRS (7,000,000 x .05) = 350,000

Year 1 Total Deduction = $ 3,350,000

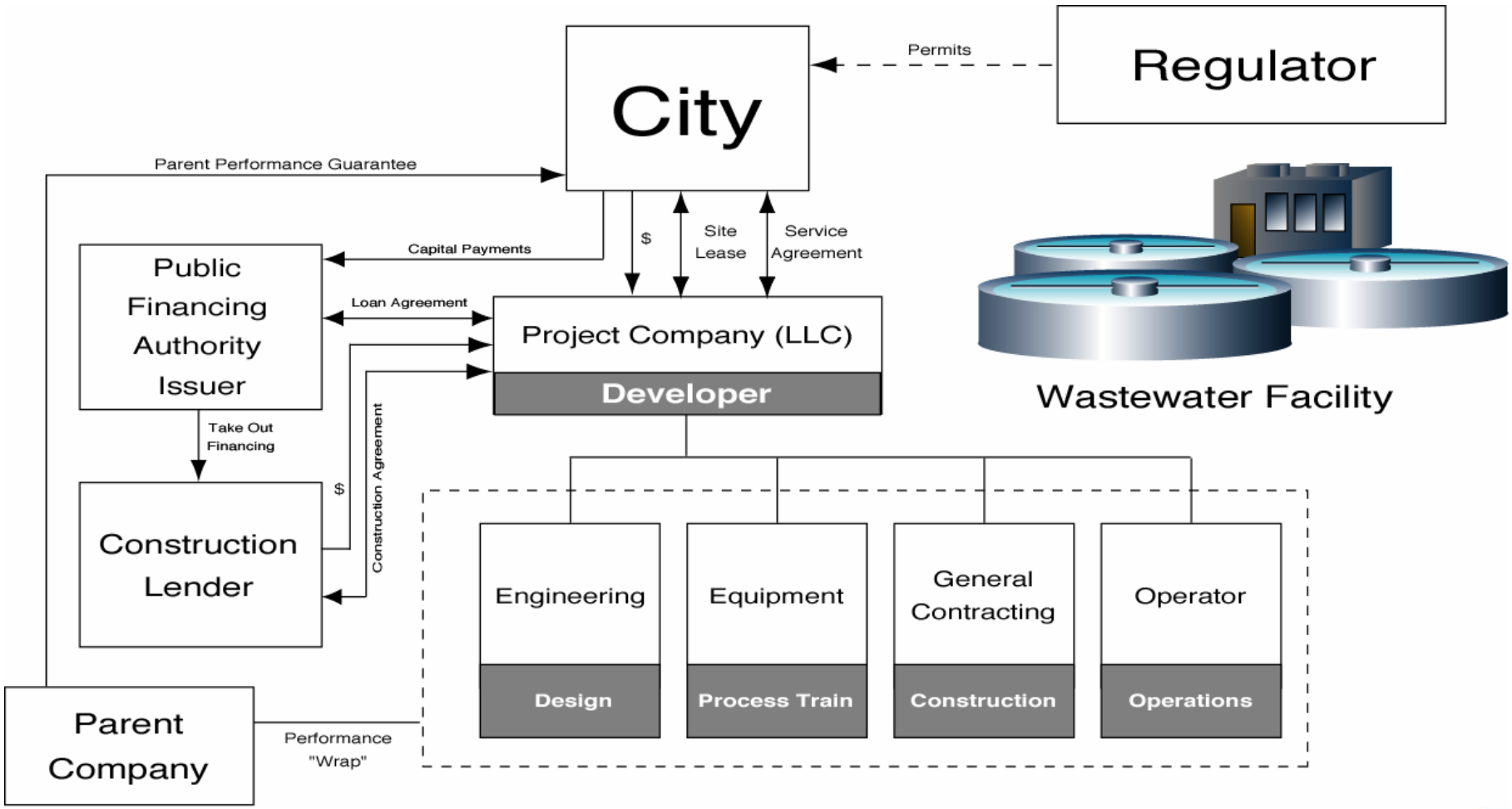
Implications For Water & Wastewater Equipment Manufacturers

- Evolving Path to Market
- Process Warranties Important
- Vertical Integration Strategies by Larger Rivals Not Proven Yet
- Vendor-Engineered Solutions Could Significantly Affect Design-Build

→ Equipment Represents Key Element of D-B-O Package

Implications For Water & Wastewater Equipment Manufacturers:

Delivering Value Instead of Low Bid



Questions & Answers