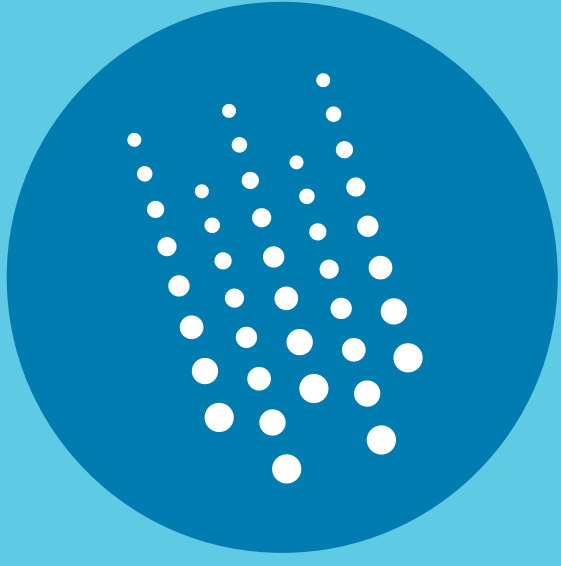
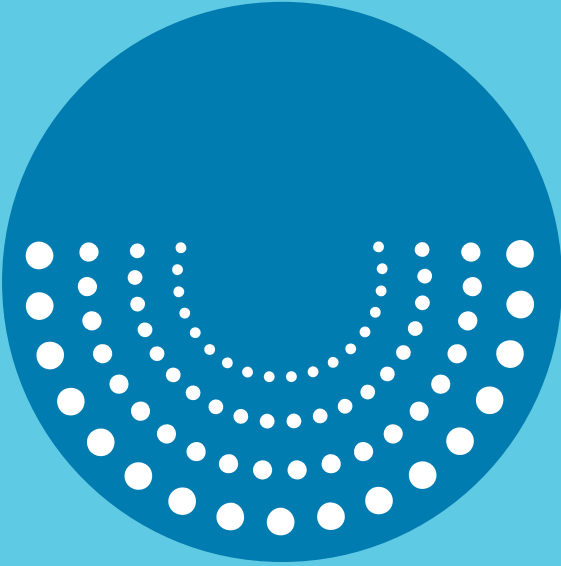
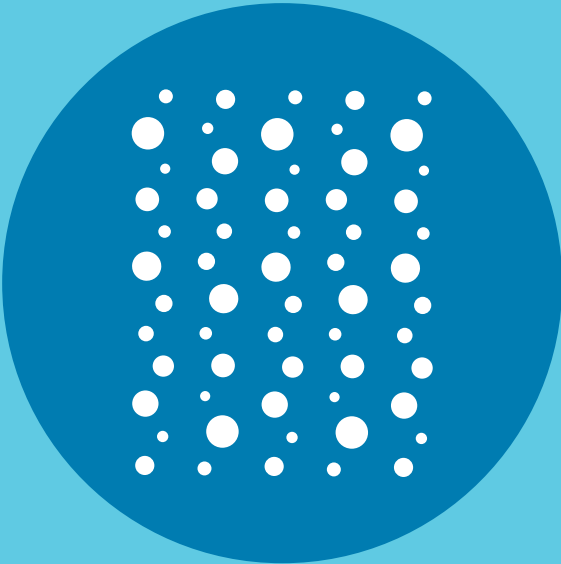
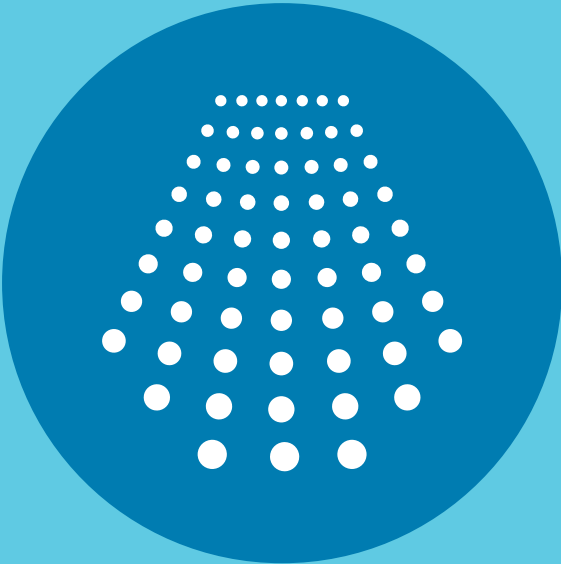


SouthWest Water Company
2007 Annual Report



SouthWest Water Company (NASDAQ: SWWC) provides essential water, wastewater and related services to more than 2 million people across the US. We have two operating businesses, our utility business and our services business. Our utility business owns and manages over 100 regulated water and wastewater systems representing more than 160,000 connections in six states. Our services business has nearly 700 contracts in ten states to assist cities, utility districts and private companies, including our utility business, with operations and management of utility systems. SouthWest Water Company was established in 1954 and employs approximately 1,400 people.

Water exists in many forms. It falls as rain, sleet or snow. It freezes as ice, and evaporates as steam.

Over the years, SouthWest Water Company has also existed in many forms and has operated under many different names in the South and the West. We have now consolidated under a single name, reflecting our common purpose of providing good stewardship for our most precious natural resource: water.

By unifying all of our operations, we are enhancing our efficiencies and implementing best business practices across our enterprise. We have reorganized our business to better focus on our core customers' needs, and we are investing in the systems we need to be able to effectively handle a large amount of growth.

Water is an essential and limited resource, and our business model positions us to participate in the opportunities this presents. We have all the fundamentals, and in 2007 we took significant steps toward building a solid, sustainable, unified company positioned for the future. We are pleased to introduce you to the new SouthWest Water Company:



SouthWest Water Company

A circle—a classic symbol of unity—signifies we are a full-service company, united in our dedication to provide safe and reliable water to our customers across the country.

The cascading drops symbolize water in its natural state. We are proud of the responsibility entrusted to us by our customers to manage and preserve their water supply.

Blue is a soothing color, which symbolizes the peace of mind that we bring to our customers every day by safeguarding this vital resource.

DEAR FELLOW SHAREHOLDERS,

2007 was a transitional year for SouthWest Water, with financial results that were far from acceptable. Management focused its efforts on improving operational performance. At the same time, we addressed critical issues that needed immediate attention, and as timing and luck would have it, we faced two external factors that also impacted results—the severe housing market slowdown and unusually heavy rains in Texas, which is one of our biggest markets.

Despite these formidable challenges, the company's foundation remains rock solid. Our core utility business performed well during 2007, and we made significant strides improving the operations and enhancing efficiencies of our services business. During the year, we also began the implementation of a company-wide systems integration project, Cornerstone, which will dramatically transform the way we operate and pave the way for the next phase of growth.

FINANCIAL OVERVIEW

While we finished the year with revenues of \$217.3 million, down slightly from last year's \$218.8 million, we incurred two large, non-cash charges that led to an \$8.0 million, or \$0.33 per share, net loss.

Despite formidable challenges during 2007, the company's underlying operations remain rock solid.

The first, a result of testing under SFAS 142, was a \$17.2 million goodwill impairment charge associated with our Texas utility business, reducing the carrying value of the Texas utility assets because of lower projected growth reflecting the current housing market, an increase in required capital expenditures and slower recovery through rate increases. We remain confident that these utilities can generate a solid return over time, and we will pursue recovering our capital expenditures through future rate increases.

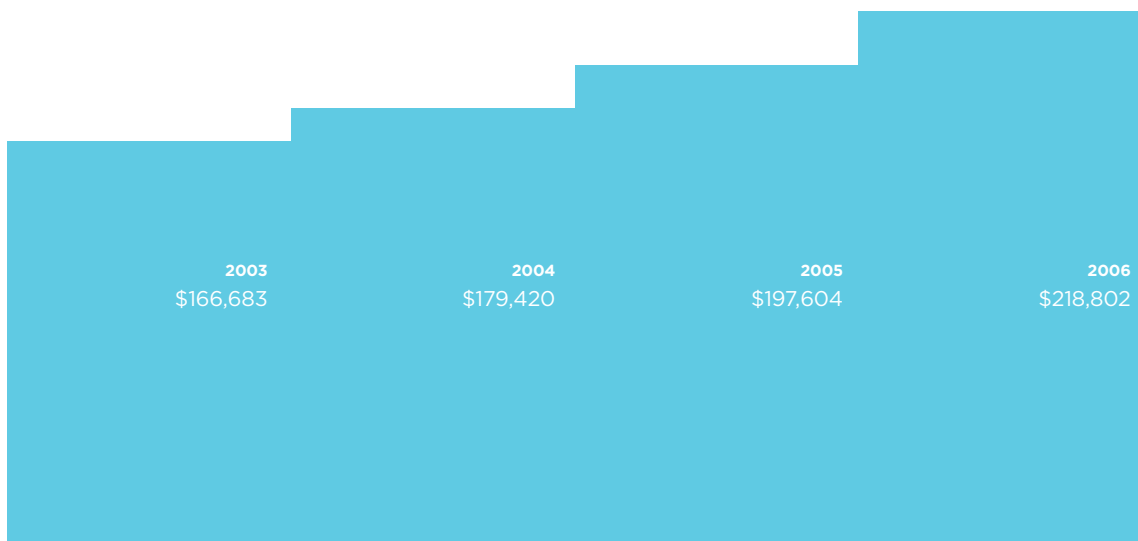
In addition, we incurred a \$3.4 million charge associated with the decision to divest our Texas-based wholesale water and wastewater business, which has now been accounted for as a discontinued operation. When this project was conceived in 2002, it was designed to support new developments, which at the time had projections for rapid population growth. While the business generated modest cash flow, it has been a drain on the earnings of our services business by more than \$1 million pretax per year. By divesting this underperforming asset, we can redeploy the proceeds in new opportunities that better meet our investment return goals.

2007 Revenue

\$217,347

Heavy rains in Texas reduced construction-related service work and water consumption at our utilities. However, the drought in California increased consumption and revenues. Our geographic diversification helps offset the impact of local weather.

(in thousands)



Without the impairment charge, income from continuing operations* was \$8.2 million, equal to \$0.34 per diluted share, for 2007, versus \$10.0 million, or \$0.43 per diluted share, in 2006.

UTILITIES

Our consolidated utility division generated \$93.4 million in revenues for 2007, up 8% from \$86.3 million the prior year, as a result of rate increases and acquisitions. Operating income, excluding the impairment charge*, was \$32.6 million, up \$2.4 million for the year, primarily due to the strong results of our California and Alabama operations.

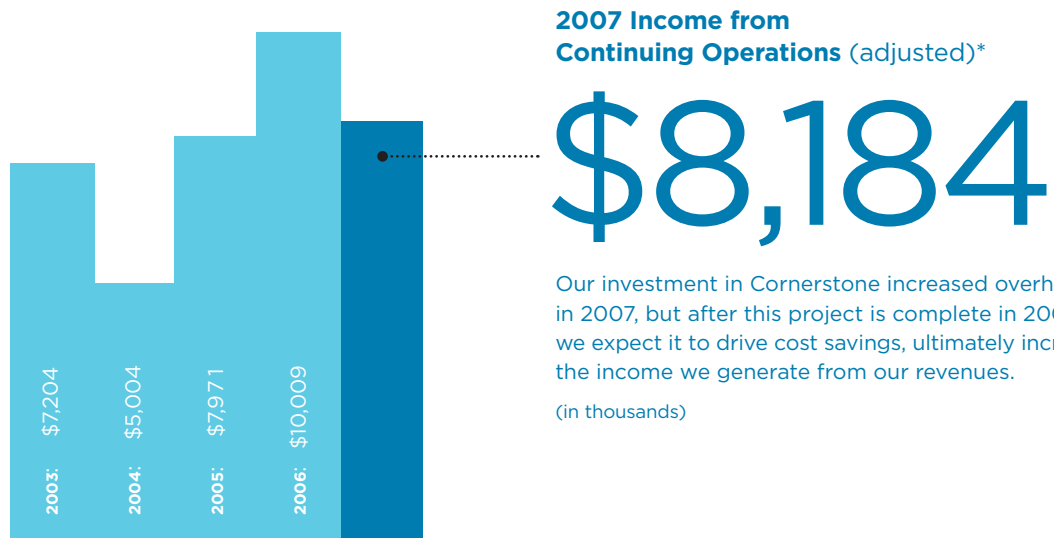
We implemented a rate increase at the beginning of the year at our Alabama utility, a step increase at our California utility in the third quarter and interim rates in the fourth quarter at several of our Texas utilities. We acquired four utilities during the year—one in northern Mississippi in the first quarter, two near San Antonio, Texas, in the second quarter, and a wastewater utility in northern Alabama in the fourth quarter.

We invest in our utilities to upgrade our level of service and continuously maintain our infrastructure. We work with state regulators to recapture these investments through rate increases.

* This is a non-GAAP financial measure. A reconciliation of all non-GAAP measures discussed in this letter to comparable GAAP measures can be found on page 14.

One of our primary growth strategies has been to purchase utility assets in areas of population growth. While this has served us well historically as we experienced organic growth from continued housing construction in these areas, the downturn in the housing market resulted in a significant reduction in the number of new connections from this source in 2007.

Because the housing slowdown may still be in its early stages, we anticipate lower organic growth at least through 2008. However, we are beginning to see favorable opportunities for acquiring quality utility assets. For example, we purchased a large wastewater system in Birmingham, Alabama, in January 2008. We are excited about this acquisition, which represents the second largest transaction consummated by SouthWest Water, since it serves more than 12,000 residents. It is located in a growth area that serves a major commercial corridor. Moreover, it is adjacent to our Shelby County wastewater system, which will allow us to realize cost efficiencies through cross-connections and by combining the operations of the two systems.



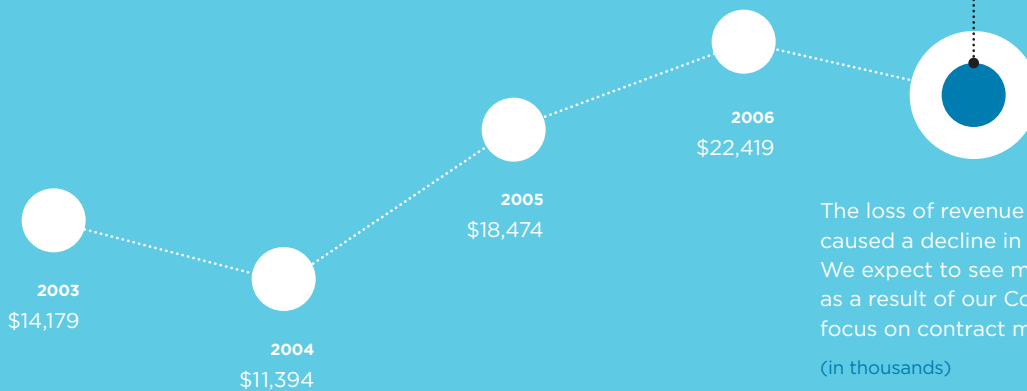
CONTRACT SERVICES

Revenues from our services division amounted to \$150.7 million for 2007, compared with \$166.0 million in 2006, with the decline principally due to heavy rains in Texas, the housing market slowdown in both Texas and New Mexico, and the loss of revenues from contracts that were not renewed in the Southeast at the end of 2006. Wet weather typically reduces our ability to perform construction and repair projects. In the Houston area, for example, rainfall in 2007 was one and a half times that city's 30-year average. The bad news about weather is that it is outside of our control. But the good news is it changes every year, and we hope for more normal weather patterns this year.

The housing slowdown in Texas and New Mexico decreased revenues related to the new home construction tapping and inspection services that we provide to clients in these markets. Our basic services, which include operations, maintenance, billing and customer care, are stable and not impacted by the housing slowdown. We expect to grow our service business by winning new contracts and improving the terms on our current contracts as they come up for renewal.

2007 Operating Income (adjusted)*

\$20,074



The loss of revenue related to new home construction caused a decline in our services margins in 2007. We expect to see margins improve in this business as a result of our Cornerstone efforts and increased focus on contract management.

(in thousands)

The majority of revenues generated by our services business comes from basic services such as operations and maintenance of facilities, meter reading, and billing services. These are stable income streams that are not affected by the current housing market dynamics.

In late 2006, we made management changes in our southeastern services region. As a result, six contracts were not renewed, which reduced 2007 revenues by about \$9 million as compared with 2006. Our new management team in the region has reduced operating costs considerably, resulting in improved operating margins, and already has won new, more profitable contracts, representing about \$2 million in revenues. I am confident that this team will make this region a winner.

Operating income for the consolidated services business was \$3.4 million, down \$2.2 million from last year, primarily because of the slowdown in construction projects from the weather and the housing slowdown. In addition, the services business incurred two smaller non-recurring charges related to legacy issues. The first was a \$650,000 reserve recorded in the third quarter in anticipation of a settlement on fines from violations that occurred at a customer's system that SouthWest Water operated prior to 2006. The second was an \$800,000 severance charge associated with a staff reduction.

Cornerstone is building a scalable foundation for SouthWest Water. When these systems are fully implemented, we will have the capacity to significantly increase the size of our business.

The services business serves three distinct groups of customers: the Texas Municipal Utility Districts, or MUDs; municipal clients that we serve through operations and maintenance contracts; and SouthWest Water's own utility business.

We restructured the services business in early 2008 to better serve the unique demands of each customer base, focus our business development efforts and eliminate structural redundancies. We flattened and simplified this division by removing one full layer of management. Today, each of the three customer groups has a business leader reporting directly to David Stanton, our chief operating officer. We eliminated 12 management/supervisory positions and 27 support positions, or approximately 3% of the services business employee base. These actions represent about \$2.6 million of salary and related cost savings going forward.

CORNERSTONE

In mid-2007, we launched a major corporate initiative, Cornerstone, to implement a single, integrated support platform across the company. Since SouthWest Water grew through acquisitions, we have been operating on numerous disconnected systems that are inefficient, are costly to operate and make data consolidation time-consuming. After a series of evaluations, we made the decision to proceed with a single integrated platform that will put SouthWest Water and all of its operating units on a shared financial and operational system. We selected an

Oracle-based system that includes an Oracle Financials foundation and an integrated Oracle Utilities operational platform for billing, customer service, dispatch, workforce management and asset management.

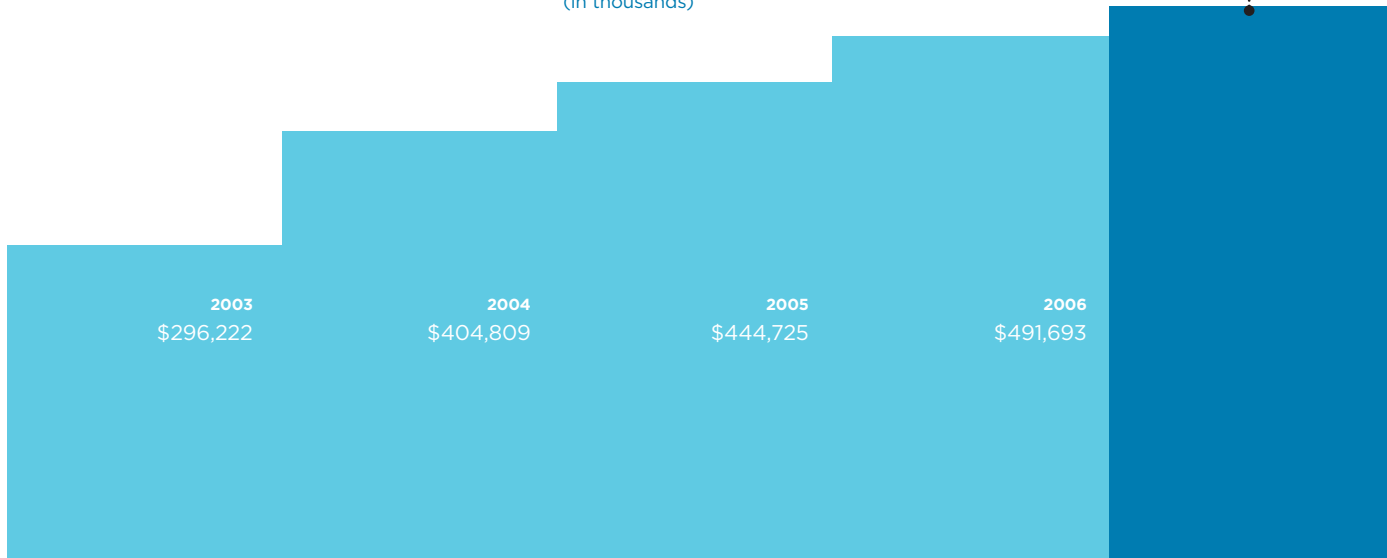
Cornerstone will require a significant investment and take more than two years to fully implement. The comprehensive system will allow us to employ best business practices across the entire company, enhance customer service in our utilities and create a competitive advantage for our services business. This project is imperative for both sustaining our existing business and positioning us for future growth.

2007 Assets

\$516,409

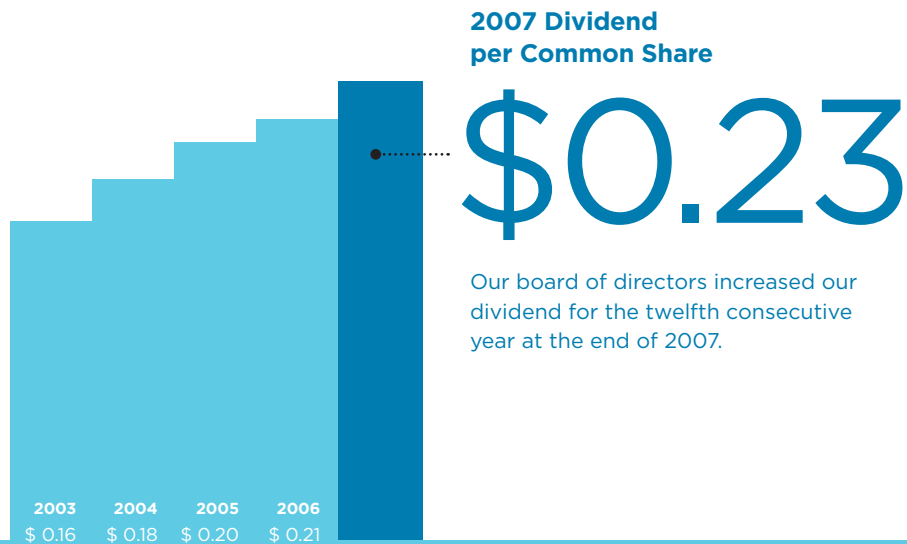
Our asset base increases through utility acquisitions and capital investments. In 2007 we purchased four utilities and invested \$30 million in utility capital improvements.

(in thousands)



We accomplished a number of critical Cornerstone activities in 2007. The company's information technology backbone was totally revamped, and we established secure redundant data centers to assure business continuity. These changes alone have already significantly improved performance, improved security and generated cost savings. We also consolidated three call centers into one location on a single modern call center platform. The new call center is scalable and capable of expanding to meet the demands of future growth.

In January 2008, we went live with our new Oracle financial platform for the entire company. This is the first time that SouthWest Water has been on a single, consolidated financial accounting system. We are now combining all of our back-office functions into one Financial Services Center, which will be in place by the end of 2008.



We are proactively investing in our business intelligence systems to gain efficiencies. The more efficient we make our operations, the more profit we will generate.

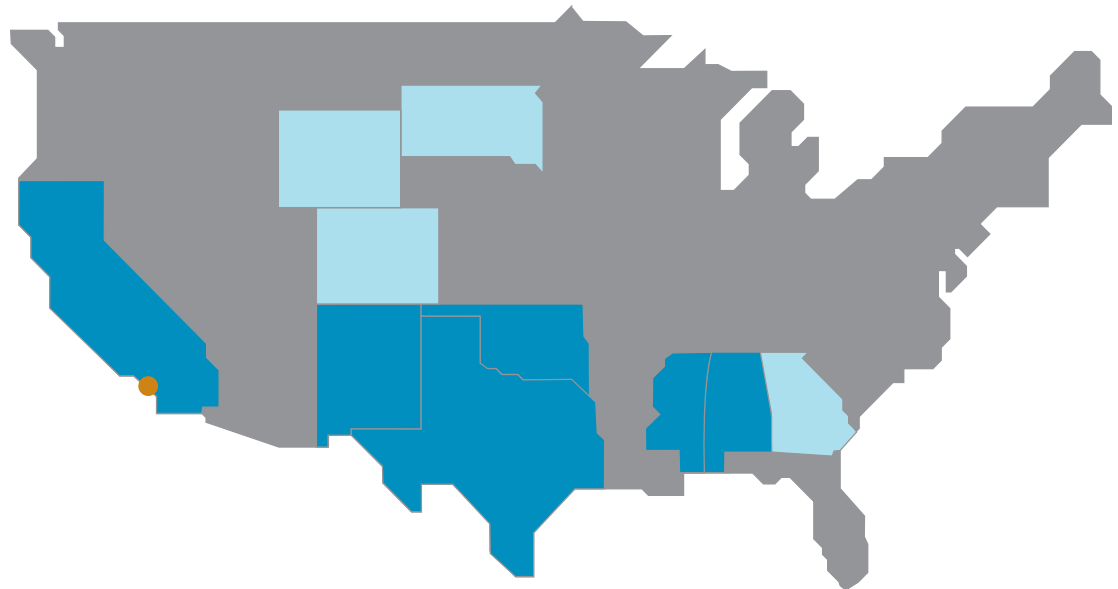
In 2007 we capitalized \$10.1 million for Cornerstone and expensed another \$1.9 million, which was reflected in increased corporate overhead. Because other phases of Cornerstone, such as customer care and billing, work and asset management, and mobile workforce management, are not scheduled to be fully implemented across the company until the end of 2009, our overhead expenses will continue to be at a higher level than our historic trends through 2009. We expect to get a portion of this investment back in rates across our owned utility portfolio as a result of improved customer service. The rest of the investment will drive additional cost savings and enhanced efficiencies in the services business, resulting in improved margins and reduced SG&A costs across the company.

POSITIONING FOR THE FUTURE

We are excited about being in the water business. Water is an essential and limited resource, and our business model positions us to participate in the opportunities this presents—both through utility ownership and through the operation and management of municipal utilities.

The company's operations are in the South and the West, which puts us in the heart of the nation's water issues. We are eager to be a part of the solution to problems associated with drought and pollution, which will continue to grow in these regions, and we have the expertise and the people to help. We have all the fundamentals—the know-how, the experience and the positioning—and we are putting into place the smooth-running engine we need to leverage our position into a nationwide powerhouse.

During the past year, we took several necessary steps toward a vision of building a solid, successful company positioned for growth. We are implementing Cornerstone to upgrade and integrate all of our financial and operational systems across the company; we have redesigned our service contract pricing model and continue our systematic approach for contract renewal; we restructured our services business around



- Utility ownership & contract services
- Contract services only
- Los Angeles corporate headquarters

We have all the fundamentals—the know-how, the experience and the positioning—and we are putting into place the smooth-running engine we need to leverage our position into a nationwide powerhouse.

its three distinct customer bases; we are divesting non-core and underperforming assets; we dealt with several large legacy issues; and in early 2008, we successfully increased our revolving credit line to \$150 million, which reflects the underlying strength of the company, even in this current period of economic challenges.

On behalf of our board of directors and management team, I thank our shareholders, employees and customers for their loyalty and support during this period of transition. While much hard work is still ahead, I am confident we are on the right track and are taking the right steps to create the kind of sustainable growth that, in turn, will help us meet our collective goal of enhancing shareholder value.



Mark Swatek

A handwritten signature in black ink, appearing to read "Mark Swatek". The signature is fluid and cursive.

Chairman and Chief Executive Officer

FINANCIAL HIGHLIGHTS						
(in thousands except per share)	2003	2004	2005	2006	2007	CAGR***
Revenues	\$166,683	\$179,420	\$197,604	\$218,802	\$217,347	12%
Operating income*	14,179	11,394	18,474	22,419	20,074	14%
Income from continuing operations*	7,204	5,004	7,971	10,009	8,184	6%
Diluted earnings per share**	0.44	0.26	0.37	0.43	0.34	(3%)
Dividend per common share	0.16	0.18	0.20	0.21	0.23	9%
Total assets	296,222	404,809	444,725	491,693	516,409	14%

* Excludes one-time impairment charge in 2007

** Continuing operations, excluding impairment charge in 2007

*** Compounded Annual Growth Rate over the 5-year period

RECONCILIATION OF NON-GAAP INCOME FROM CONTINUING OPERATIONS

(unaudited and in thousands except per share)	YEAR ENDED DECEMBER 31, 2007
Pretax loss from continuing operations (GAAP)	\$(4,225)
Add Back: Impairment charges	17,215
Pretax income from continuing operations (adjusted)	12,990
Provision for income taxes (37%)	4,806
Income from continuing operations (adjusted)	\$ 8,184
Earnings per diluted share	\$ 0.34

RECONCILIATION OF NON-GAAP OPERATING INCOME

(unaudited and in thousands)	YEAR ENDED DECEMBER 31, 2007
Utility business operating income	\$ 15,339
Services business operating income	3,415
Corporate	(15,895)
Operating income (GAAP)	2,859
Add Back: Impairment charges	17,215
Operating income (adjusted)	\$ 20,074

RECONCILIATION OF NON-GAAP UTILITY BUSINESS OPERATING INCOME

(unaudited and in thousands)	YEAR ENDED DECEMBER 31, 2007
Utility business operating income (from above table)	\$ 15,339
Add Back: Impairment charges	17,215
Operating income (adjusted)	\$ 32,554

DIRECTORS

Mark A. Swatek, P.E.
Chairman and
Chief Executive Officer

Anton C. Garnier
Executive Vice Chairman

H. Frederick Christie
Consultant; Retired President
and Chief Executive Officer
of the Mission Group,
a subsidiary of SCECorp
(now Edison International)^{2, 3, 4}

Linda Griego
Founder and Managing General Partner
of Engine Company No. 28^{1, 3}

Donovan D. Huennekens
Partner, HQT Homes, a real estate
development company^{2, 4}

Thomas Iino
Chairman of the Board of
Los Angeles-based Pacific
Commerce Bank^{1, 2}

William D. Jones
President, Chief Executive Officer
and owner of CityLink Investment
Corporation^{2, 3, 4}

Maureen A. Kindel
Senior Managing Director of
Global Consulting Group Rose & Kindel,
a public affairs firm^{3, 4}

Richard G. Newman
Founder, Chairman and Director of
AECOM Technology Corporation^{1, 4}

¹ Member of Financial Planning and
Investment Committee (R. G. Newman, Chair)

² Member of Audit Committee
(D. D. Huennekens, Chair)

³ Member of Nominating/Governance Committee
(Linda Griego, Chair)

⁴ Member of Compensation and Organization
Committee (H. F. Christie, Chair)

Forward-Looking Statements

This Annual Report contains "forward-looking statements" as defined under the Private Securities Litigation Reform Act of 1995. With the exception of historical information, the matters discussed in this report are forward-looking statements that involve risks and uncertainties. Although the Company believes that its expectations are based on reasonable assumptions, it can give no assurance that its goals will be achieved. Important factors that could cause actual results to differ materially from those in the forward-looking statements herein include, but are not limited to: competition, weather conditions, water contamination, environmental risks, government regulations, and other risks described in Item 1A of our Annual Report on Form 10-K, a copy of which is included in this publication.

OFFICERS AND EXECUTIVE MANAGEMENT

Mark A. Swatek, P.E.
Chairman and
Chief Executive Officer

David B. Stanton
Chief Operating Officer

Cheryl L. Clary
Chief Financial Officer

William K. ("Ken") Dix
Vice President, General Counsel
and Corporate Secretary

DeLise L. Keim
Vice President
Corporate Communications

James E. Mann
Vice President, Controller

Mark G. Rodriguez
Vice President, Human Resources

Walter J. Bench
Treasurer

OPERATIONS MANAGING DIRECTORS

James C. Brown
Texas MUDs

Charles W. Profilet, Jr., P.E.
Texas Utilities

Michael O. Quinn
Western Utilities

VICE PRESIDENTS

Daniel N. Evans
Suburban Water Systems

Robert L. Kelly
Regulatory Affairs

Chris A. Malinowski
Safety and Compliance

Mark W. Minter
Eastern Region, O&M

Thomas J. O'Neill
Western Region, O&M

Ben C. Smith
Financial Services Center

Marlea A. Tichy
Business Planning

Gregg W. Young
Customer Service

OUTSIDE COUNSEL

Musick Peeler & Garrett LLP
Los Angeles, California

2007 AUDITORS

KPMG LLP
Los Angeles, California

REGISTRAR, TRANSFER AGENT AND DIVIDEND DISBURSING AGENT

BNY Mellon Shareowner Services
P.O. Box 358013
Pittsburg, PA 15252
800.850.3119

Stockholders can access their
accounts on-line through Mellon
Investor Services' website:
www.melloninvestor.com

COMMON STOCK

The company's common stock
is traded on the NASDAQ Stock
Market—symbol SWWC.

ANNUAL MEETING

The Annual Meeting of Shareholders
of SouthWest Water Company will be
held on Tuesday, May 20, 2008, at
10:00 a.m., Pacific Time, at the Biltmore
Millennium Hotel, 506 South Grand
Avenue, Los Angeles, California 90071.

DIRECT STOCK PURCHASE AND DIVIDEND REINVESTMENT PLAN

Shares of SouthWest Water Company
common stock can be purchased directly
from the company without a broker fee
through our transfer agent by means of
our Direct Stock Purchase Plan (DSPP).
The plan is also a Dividend Reinvestment
Plan (DRIP), which gives shareholders an
opportunity to reinvest their dividends
at a discount to market price. For more
information and a prospectus, please
contact our transfer agent, BNY Mellon
Shareowner Services, via the contact
information listed on this page or visit the
Investor Relations section of our website at
www.swwc.com.

CORPORATE OFFICE

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e-mail: swwc@swwc.com

INVESTOR RELATIONS CONTACT

DeLise Keim
VP, Corporate Communications
tel: 213.929.1846
e-mail: dkeim@swwc.com



**SouthWest
Water Company**

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