

INDUSTRY OUTLOOK

Engineering & Construction Industry (Canada) Q4 2021

Executive Summary

The Engineering and Construction industry continued to perform well in the fourth quarter of 2021 (4Q-2021) despite the continued impact of the COVID-19 pandemic. The fundamentals remain strong, with growing investment in non-residential and commercial construction, despite a decrease in the number of housings starts and overall investment in construction, which was on account of seasonality.

The overall investment in the Canadian construction industry has continued to grow year over year over the last four years, representing a +6% CAGR. This growth was notably the highest in 2021 with a +19% increase compared to the +3% in 2020¹.

The industry reached and surpassed pre-pandemic gross domestic product (GDP) levels by 1Q-2021 after exhibiting lowest GDP levels in the last eight years in 2Q-2020². Subsequently, 2Q-2021 marked the industry's record-high GDP levels before returning to pre-pandemic levels in 3Q and 4Q-2021³.

Despite the positive outlook, the industry faces considerable challenges – some new, but many well-known. Among the major ones are rising cost of materials and equipment, labor shortages, and supply chain disruptions, which collectively continue to impair industry margins. Besides these, adapting to the next-generation digital technologies, integrating data and analytics into workstreams, and implementing end-to-end digitized construction capabilities are receiving increasing attention and importance from executives⁴.

The opportunities for mergers and acquisitions (“M&A”) in this industry are limitless, especially with the prominent drive towards digitization of the industry. A recent example is Tetra Tech Inc.'s acquisition of Axiom Data Science (March 2022), an informatics and software development firm and an industry leader in the management and analysis of oceanic and ecological data associated with climate change⁵, which was driven by Tetra Tech's objective to expand its analytics capabilities in oceans and ecosystems.

2021 saw the highest deal count and capital invested within Canada, making it the busiest year for Canadian deals in the last century. In Q4 2021, there were 117 private equity deals in Canada, representing CAD\$15.9B of capital invested in transactions, and a total of 376 M&A deals, representing CAD\$65.5B of capital invested in transactions.

Despite the near-term challenges in certain construction sectors, the medium to long term growth outlook of the Canadian construction industry remains intact.

Operating Environment Overview



Key stats in Q4 2021 compared to Q3 2021⁶

Metric	% increase/decrease	
Investment in non-residential construction	↑	3.9% QoQ
Investment in commercial construction	↑	5.7% QoQ
Investment in residential construction	↓	10.0% QoQ
Overall investment in building construction	↓	6.7% QoQ
Housing starts	↓	0.2% QoQ
Wages and salaries	↑	3.6% QoQ
Household consumption expenditure	↑	1.3% QoQ

E&C industry – 4Q-2021 vs 3Q-2021

- The **construction industry** employs over 1.4 million people in Canada and generates about \$141 billion to the economy annually, accounting for 7.5% of Canada's gross domestic product (GDP)⁷.
- **Residential building construction costs** increased 3.8% in the fourth quarter of 2021, following a similar rise in the third quarter. Non-residential building construction costs were up 2.7% in the fourth quarter, decelerating slightly from the previous quarter⁸.
- Despite the increased pandemic-related infections and containment measures in Q4 2021, Canadian corporations reported a quarterly increase of 3.8% in **net income before taxes (NIBT)** in the quarter. This increase was led by the non-financial sector (+7.7%) while the non-financial sector saw a decline in NIBT of 2.7% during the quarter⁹.
- Adverse weather events accompanied by severe flooding in British Columbia affected business activity in the fourth quarter; **the market for wood products** was among the most impacted¹⁰.
- **Investment in non-residential construction** was up ~4% to \$15 billion, representing the largest quarterly increase since the third quarter of 2017¹¹. The gains were led by the commercial component (+4.9%), which represents its fourth consecutive quarterly increase.
- **Investment in residential construction** was down by 10% compared with the third quarter.

Market Growth

Industry trends

Supply chain disruption, increasing digital revolution, and legal changes likely to affect project delivery and margins

Industry Shapers

While the construction sector forecasts strong growth in the coming years, one of the biggest challenges in the recent past has been availability of *skilled labour* and *raw materials* to meet the growing demand.

Similarly, material shortages have impacted projects at all levels. Steel and other metals are in scarce supply on account of the global pandemic and delayed transportation.

Import-export backlogs have been evident with ocean ports experiencing severe unload times on account of changing demands during the pandemic¹².

While *digital revolution* has been embraced by nearly every industry, Canada's construction industry is behind the curve. A survey by the Canadian Construction Association (2020) showed that three-quarters of construction companies in Canada rate their digital maturity as "fairly low".

The industry is beginning to increasingly rely on digital solutions such as artificial intelligence, blockchain and smart contracts, building information modelling, building automation, and wireless monitoring to complete projects.

“The slow pace of change in the industry offers tremendous opportunities for tech companies that can provide innovative products and services.”

— May 2021: Lauren Lake, Chief Operating Officer, Bridgit (a software company focused on the construction industry)

New Construction

The total value of building permits in Q4 2021 was relatively flat, falling 0.6% relative to Q3 2021. This cyclicity is expected as the industry went into the Winter. However, relative to Q4 2020, the total value of building permits in Q4 2021 was up 21% year-over-year¹³.

Interest Rates

Since March 2020, interest rates have dropped to an all-time low due to COVID-19, with the policy interest rate currently at 0.25%. However, due to the current high inflation environment (i.e., 4.8% in December 2021), interest rate hikes have begun in 2022¹⁴.

Legal Changes

Prompt payment and mandatory adjudication legislation is being enacted across Canada to alleviate perceived payment delays down the construction pyramid.

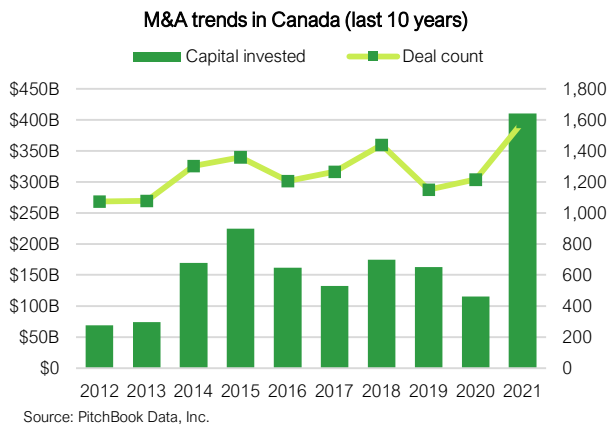
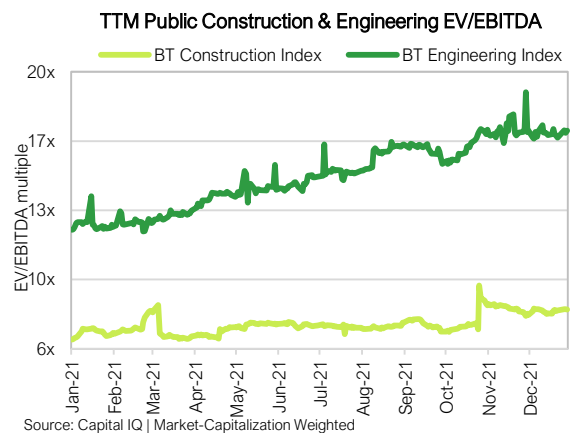
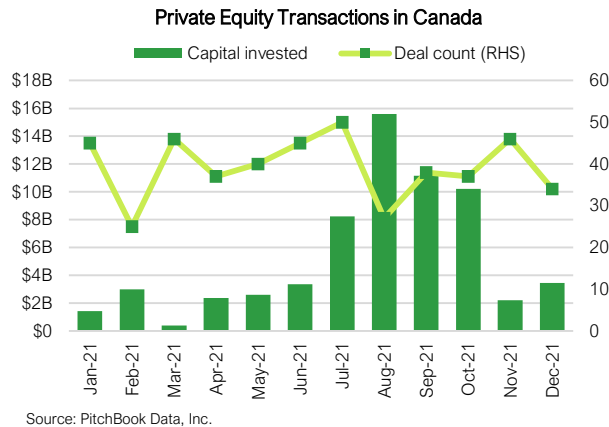
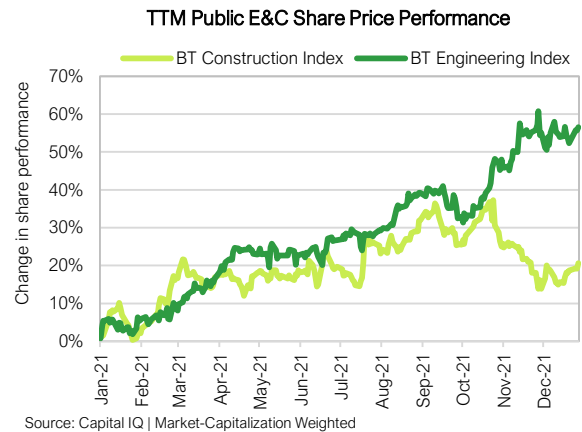
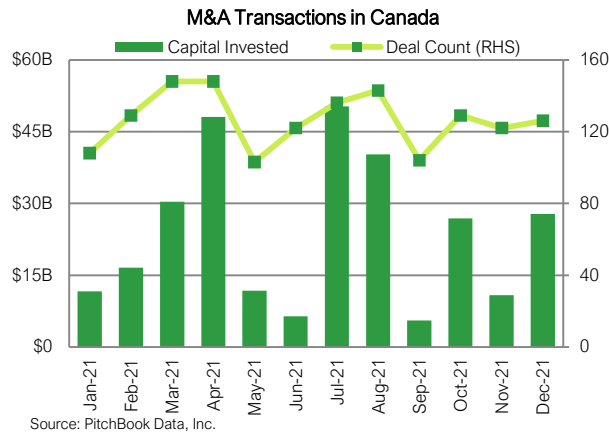
According to a report by law firm, Dentons (October 2021), changes to prompt payment and adjudication legislation are being implemented federally and in several Canadian provinces.

Collectively, the new legislative schemes set out timelines for payment and disputes, amend adjudication requirements, and changes in lien mechanics. The new Ontario and Québec regimes are currently in force, and the amendments to the Alberta, Nova Scotia and Saskatchewan legislation have received royal assent. Additionally, British Columbia, Manitoba and New Brunswick have recently published reports that propose changes to their existing legislative schemes¹⁵.

Industry Valuations

Mergers and Acquisitions (M&A)

2021 saw the highest deal count and capital invested within Canada, making it the busiest year for Canadian deals in the last century. In 4Q-2021, there were 117 private equity deals in Canada, representing CAD\$15.9B of capital invested in transactions, and a total of 376 M&A deals, representing CAD\$65.5B of capital invested in transactions. *Note: Private company multiples may vary significantly lower from those of public traded companies.*



BT Engineering Companies Index: Aecom, IBI Group Inc., Stantec Inc., and WSP Global Inc.

BT Construction Companies Index: Aecon Group Inc. and Bird Construction Inc.

Recent M&A Transactions

Select transactions

Notable E&C transactions in Canada over the past one-year include¹⁶:

Companies	Deal Date	Deal Type	Investors
 Axiom DATA SCIENCE	08-Mar-2022	M&A	 TETRA TECH
 PITEAU ASSOCIATES GEO TECHNICAL AND WATER MANAGEMENT CONSULTANTS	03-Mar-2022	M&A	 TETRA TECH
 Cordy Environmental Inc.	25-Feb-2022	M&A	 VERTEX
 VASPAC Power Automation Consulting	22-Feb-2022	M&A	 ATS
 PINCHIN	04-Feb-2022	Buyout/LBO	 KEYSTONE CAPITAL PM ENVIRONMENTAL
 IPS GREEN DRIVEN Integrated Pallet Management Solution	01-Feb-2022	M&A	 PARAMOUNT PALLET
 ENERGERE	21-Jan-2022	M&A	 AINSWORTH
 POWERLINE PLUS Ltd.	04-Jan-2022	M&A	 MYR GROUP
 austin	01-Jan-2022	M&A	 BBA
 BLS CONSTRUCTION	23-Dec-2021	M&A	Phil Bergen, Seamus Carroll, and Brent Smith
 MASKIMO	17-Dec-2021	M&A	 ROXBORO
 ecosystem recovery inc. PROFESSIONAL ENGINEERS	16-Dec-2021	M&A	 Matrix Solutions Inc. ENVIRONMENT & ENGINEERING
 MPE	02-Dec-2021	M&A	 Englobe
 RYKO TELECOMMUNICATIONS	01-Dec-2021	M&A	 Exchange Income Corporation
 NORTHERN	22-Nov-2021	M&A	 VINCI
 BOGDONOV PAO ASSOCIATES Structural Engineers	18-Nov-2021	M&A	 CIM+
 PLATINUM TRACK SERVICES INC.	14-Nov-2021	M&A	 GCF GENERALE COSTRUZIONI FERROVIARIE S.p.A
 PROTOSTATIX	20-Oct-2021	M&A	 Englobe

Pitchbook Definition:

M&A: A company acquires at least a controlling position in another company.

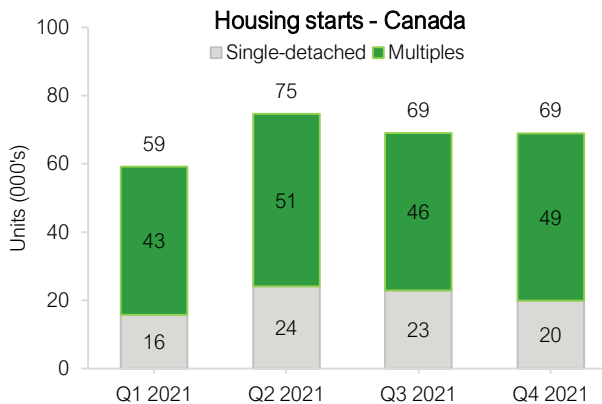
Buyout/LBO: A private equity firm acquires at least a controlling position in another company.

Key Findings

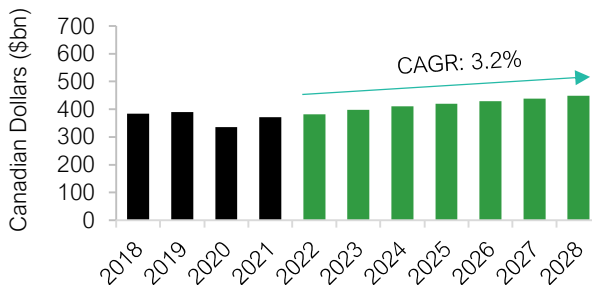
Industry snapshot

Despite the setbacks arising from the pandemic, the industry is expected to continue on an overall upward growth trajectory in the coming years.

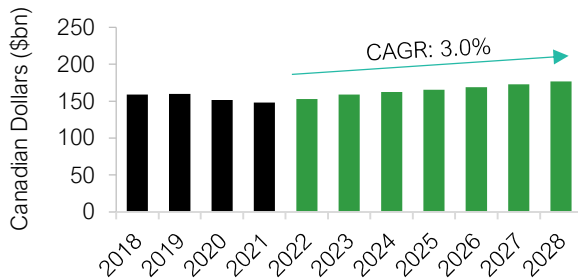
Current and Prospective Performance



Aggregate Private Investment



Value of Nonresidential Construction



Looking Forward

About 90% of builders have suffered from shortages of appliances, lumber, plywood, windows, and doors¹⁷.

The delta variant of the virus, along with natural disasters, set back supply chains for several materials and these supply chain disruptions are expected to continue in 2022.

Under the Investing in Canada Plan, the Plan has invested over CAD\$118 billion in over 78,000 projects to date. However, there are still billions of dollars earmarked for infrastructure investment¹⁸.

In October 2020, the government launched a CA\$10 billion “Growth Plan” for Canada Infrastructure Bank (“CIB”) in order to invest and attract investment from private sector and institutional investors. Green energy projects in particular have been established as a core investment area, with the push towards renewable energy sources.

Industry Outlook

“ We expect demand for our services to remain healthy for the foreseeable future, as the federal government and provincial governments across Canada have identified investment in infrastructure as a key source of stimulus as part of the economic recovery plan and an essential part of the transition to a net zero carbon economy through more sustainable infrastructure. ”

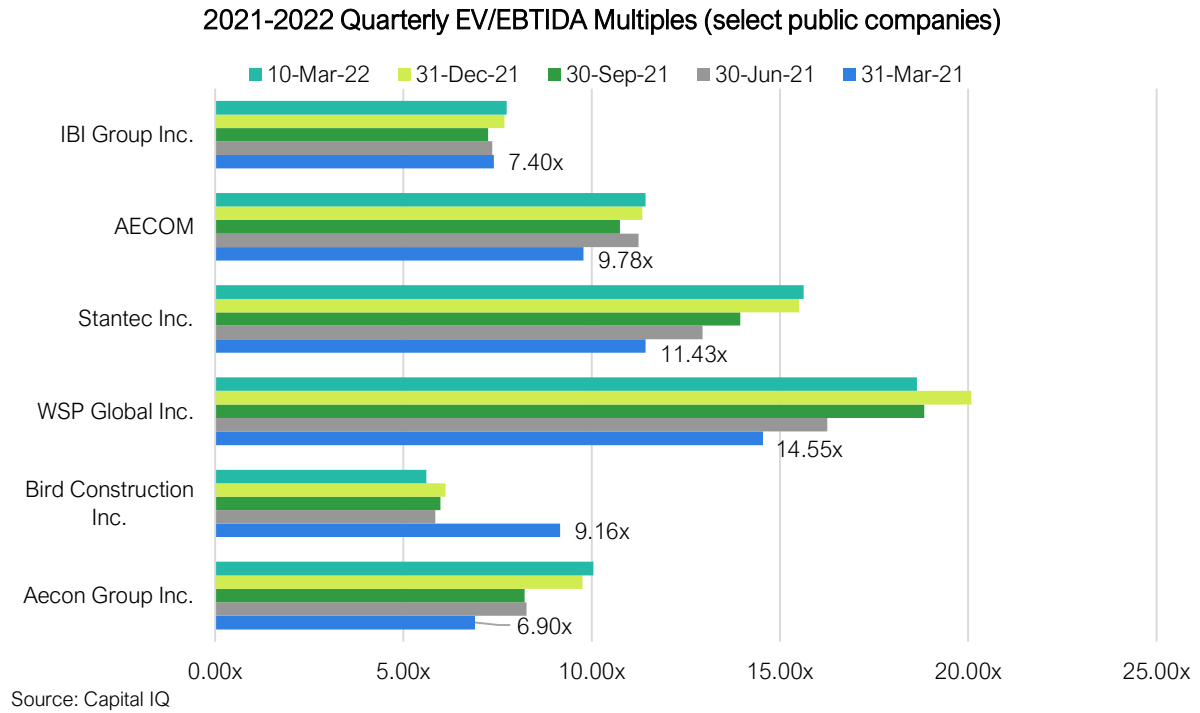
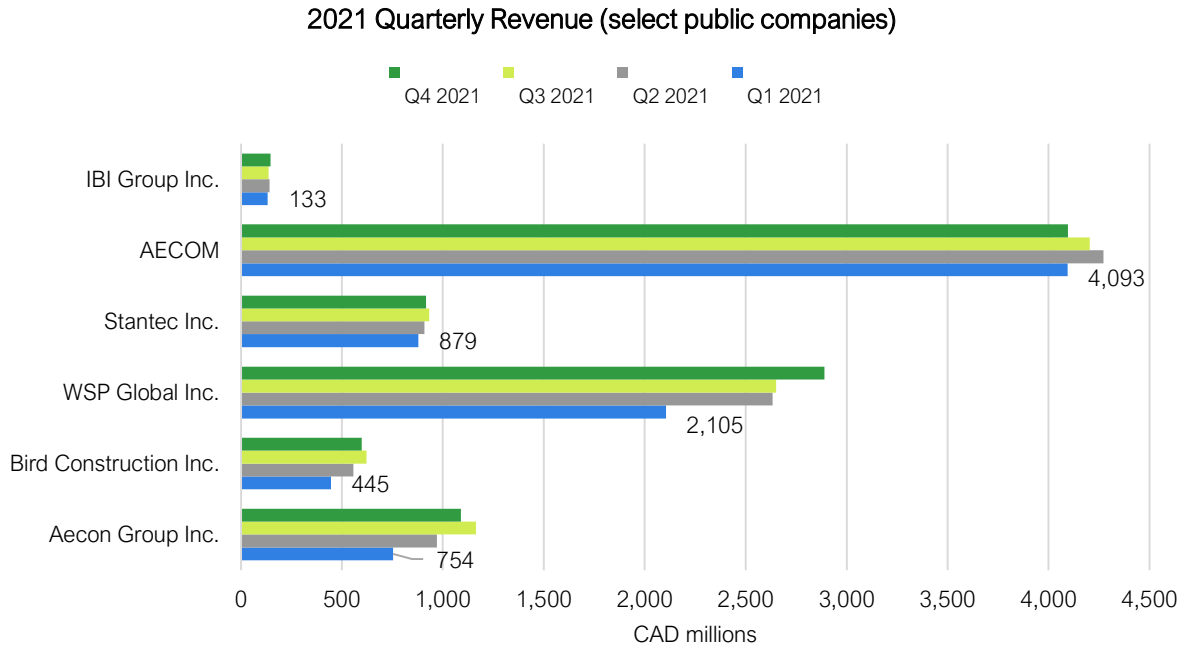
— March 2022: Jean-Louis Servranckx, President and Chief Executive Officer, Aecon Group Inc.

Conclusion

As the E&C industry continues to recover from the pandemic and exhibit an upward growth trajectory. Resilience in managing and navigating supply chain risk, labour shortages, and financial uncertainties will be crucial in companies’ ability to capitalize on the emerging opportunities.

Key Findings (continued)

TTM performance of key industry players – 4Q-2021



Select M&A Transactions

Select Engagement Highlights

Jacob Bros Construction

(Buy-side engagement)



Founded in 2008, Jacob Bros is a leading general contractor specializing in civil and building's construction. Headquartered in Surrey, British Columbia, Jacob Bros has delivered a diverse portfolio of projects for public and private clients across Western Canada.

Continental Chain and Rigging ("Continental") is a supplier of chain and rigging products including wire rope products, tire chains, synthetic slings, fall protection equipment, and much more. With headquarters in Edmonton, Alberta, Continental offers their products and services throughout Western Canada by using its robust distributor relationships.

Continental was growing impressively and achieving record results. This made agreeing on a purchase price challenging as financial results were improving more than expected every month the deal moved towards close.

Once the purchase price and terms were agreed, the parties needed a mechanism to address growing net working capital. The concern was the potential for a large purchase price adjustment post-close based on unprecedented working capital levels. Minority shareholder added complexity and required additional agreements to be finalized at close.

To provide price certainty, a "lock box" mechanism was established for working capital, which fixed the purchase price adjustments related to net working capital on agreed terms and at the "lock box date". The structure of the purchase and sale was negotiated to provide all shareholders a tax efficient transaction now and in the future. A minority stake in Continental was acquired at mutually agreeable terms. Management of Continental remain in place, while the Jacob brothers will join the board and act as advisors for Continental.

“We are excited to be partners in the ownership of Continental Chain and Rigging. They are good people and we see clear opportunities for both parties to benefit from this partnership. The Baker Tilly team did a great job of negotiating the fine details and pushing the transaction across the line.”

— Scott Jacob, President & CEO of Jacob Bros Construction

CCMET Group

(Sell-side engagement)



Founded in 1987, CCMET Group ("CCMET") grew to become the leading engineering materials testing company in Western Canada. With 275+ employees, CCMET continues to deliver a full range of services including materials testing, materials engineering, geotechnical engineering, concrete restoration, environmental engineering and TQM. Its scale, reliability and quality of work makes it a key partner in many of the Canada's largest infrastructure projects.

As an employee-owned business, the rationale for the transaction was twofold: Form a partnership to provide resources to fuel future growth and liquidity for the transition of several senior employees.

Roster of 40+ potential purchasers was developed → 20+ reviewed the CIM and received offers from 5 parties. Accepted LOI to transaction closing took 97 days.

70% of CCMET was successfully sold to Equicapita, a Calgary-based private equity fund that has a history of acquiring and growing industrial companies.

Transaction valued the enterprise at \$47.5M, which was substantially above the target price agreed upon with the client.

Baker Tilly Canada Corporate Finance Inc. acted as exclusive financial advisor to CCMET Group in structuring and negotiating this transaction.

“Renaissance Mergers & Acquisitions [now Baker Tilly Canada Corporate Finance] facilitated the transaction from initial concept to the very end where they literally pushed it over the final goal line. [They] exceeded our expectations by over 100% and I could not be more pleased with the results and the new partnership.”

— Harry Watson, President, CCMET



End notes

Sources

1. Statistics Canada, 2022
2. Ibid.
3. Ibid.
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5. Deloitte, [2022 engineering and construction industry outlook](#)
6. Statistics Canada, 2022
7. Canadian Construction Association
8. Statistics Canada (2022), [Building construction price indexes, fourth quarter 2021](#)
9. Statistics Canada (2022), [Quarterly financial statistics for enterprises, fourth quarter 2021](#)
10. Ibid.
11. Ibid.
12. Dentons (October 2021), [Canada's construction industry in 2021: key trends and developments](#)
13. Statistics Canada, [Table 34-10-0066-01 Building permits, by type of structure and type of work \(x 1,000\)](#)
14. Statistics Canada, [Consumer price index portal](#)
15. Dentons (October 2021), [Canada's construction industry in 2021: key trends and developments](#)
16. S&P Capital IQ
17. Wall Street Journal, [Builders Hunt for Alternatives to Materials in Short Supply](#)
18. Infrastructure Canada, [Government of Canada](#)

Corporate Finance

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<ul style="list-style-type: none"> - Financial and Tax Due Diligence - Focused scope on issues that are most important to you 	<ul style="list-style-type: none"> - Deal strategy and origination - Negotiation and structuring advice - Preparation of Term Sheet - SPA advice - End-to-end project management 	<ul style="list-style-type: none"> - Modelling - Valuation - Purchase Price Allocation 	<ul style="list-style-type: none"> - Tax structuring planning and implementation - Tax structuring advice 	<ul style="list-style-type: none"> - Operational due diligence - Commercial due diligence - Synergy assessment - Post-acquisition integration

Ongoing transaction project management

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