
# 2012 CONSTRUCTION FORECAST

## Economy hits the "pause" button, but construction prospects are strong

BY JIM BARNES

It has been an ominous year for the economy. Natural disasters occurred around the world, including destructive flooding in Manitoba and widespread forest fires in Alberta. Global economic stability wobbled, with revolution in the Middle East, political turmoil in the U.S. and an ongoing sovereign debt crisis in Europe. Corporate and consumer confidence were shaken.

Despite all the bad news, though, the near-term health of construction in Canada seems strong.

### THE OPTIMISTS

The Royal Bank of Canada (RBC) is among the optimists. "As of early September, most of the shocks that knocked growth down this spring and summer either had already run their course or were well underway in doing so," it noted in its *Provincial Outlook* in September. Significant growth is expected in Q3 as production losses in industries such as automaking and the oil industry are reversed.

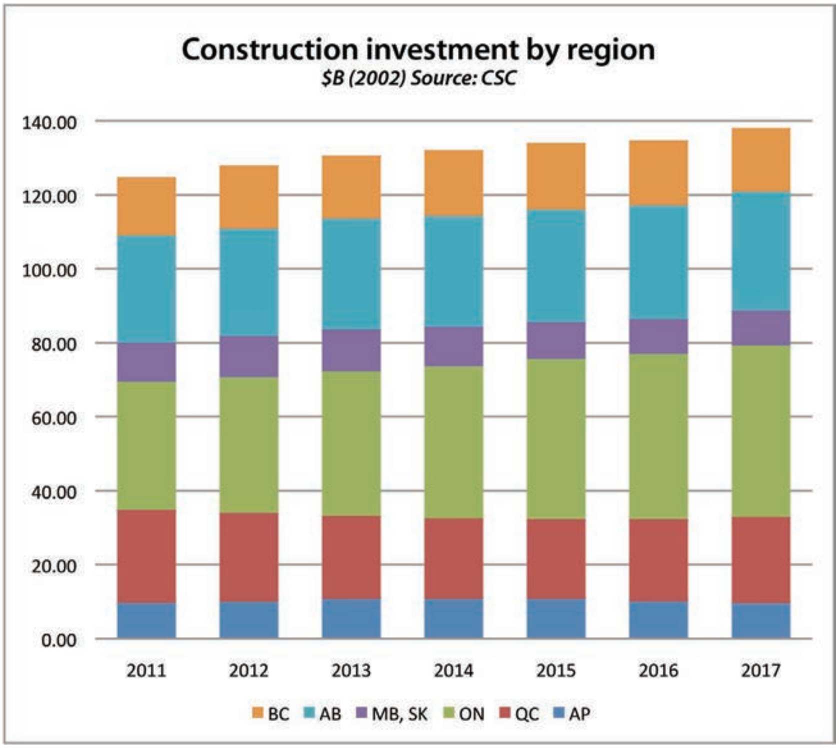
*Global Construction 2020*, published in May by Global Construction Perspectives and Oxford Economics and sponsored by consultants PwC, also predicts growth for Canadian construction—in fact, moving the country from seventh to fifth biggest construction market in the world by 2020. "Over the next decade, we expect infrastructure to be the fastest growing end-market in Canada and housing to be the slowest," noted Sal Bianco, national engineering and construction leader, PwC.

Michael Atkinson, president of the Canadian Construction Association in Ottawa, is also among the believers. "All the projections I'm seeing for the [non-residential] construction industry are extremely positive," he says.

Statistics Canada data shows overall construction investment in 2010 reached $232 billion. "That was a 13 per cent increase over 2009," notes Atkinson. "They predicted that 2011 would reach as high as $241 billion—a 3.6 per cent increase over 2010."

Employment is steady, too. Despite a drop in construction employment in October, just before the recession hit, construction employment was at an all-time high, at more than 1.6 million. "In the recession, we lost something like 130,000 jobs in the construction industry. A lot of that was in the residential sector. By June 2011, we were back to pre-recession levels," he says.

"Recovery is well underway in most of Canada's construction markets," noted the Construction Sector Council in the 2011 *Construction Looking Forward*, published in April. "Prompted by fiscal stimulus in 2009 and 2010, [construction] continues to be a leading growth industry across Canada... The national story is one of recovery by 2011–2012 and steady expansion later in the scenario period." The construction and maintenance industry will create demand for some 111,000 workers between 2011 and 2019. At the same time, nearly 208,000 workers leaving the industry will have to be replaced.




## THE MONEY

Despite economic constraints, the federal government has maintained support for infrastructure. In Budget 2011, it introduced legislation to formalize the Gas Tax Fund transfers to municipalities, currently valued at some $2 billion a year. It is also looking beyond the expiry of the Building Canada Plan.

"Public infrastructure should be a winner, despite all the belt-tightening that governments have been talking about," Atkinson says. "I think that governments understand that they can't abandon investment in infrastructure to control the fiscal situation. The two go hand-in-hand."

Signs of financial pressure in the industry are seen in surety loss ratios. The numbers have been up significantly for two years in a row. "That shows that even in what appears to be a relatively heated market, there have been failures," explains Atkinson.

"There have been a few defaults lately, mainly coming from out west—Alberta in particular," says David Bowcott, vice-president, AON Reed Stenhouse Inc. "We've had four or five major sub-trades and one general contractor go down."

He does not see this as a worrisome trend, though. "It's just the dynamic nature of the boom, bust and boom aspect of Alberta," he notes. With the Alberta defaults, "It just seems like some of those folks got in over their heads."

Public-private partnerships (P3s) should bloom in the current economy. "There's a bigger push by federal and provincial governments to get municipalities going down this road. And they are showing signs of embracing it," says Bowcott. "That will create mixed, mid-market opportunities for those contractors who are ahead of the curve."

## LOCATION, LOCATION, LOCATION

The recent economic turmoil has seen predictions for general economic growth in Canada scaled down. The International Monetary Fund (IMF) calls for approximately two per cent growth in both 2011 and 2012, on par with a recent forecast from the Bank of Canada (BoC). Both organizations are more positive about growth in 2013, with IMF calling for 2.6-per-cent growth and BoC forecasting 2.9-per-cent growth.

Canada is an economy of regions. In the RBC Provincial Outlook, researchers revised their GDP forecasts downwards for all provinces except Saskatchewan this year and for most provinces (except Manitoba and Alberta) next year.

**ATLANTIC –** Research from the Atlantic Provinces Economic Council (APEC) foresees weak growth in consumer spending and employment, and a slowing housing market across most of the region. Its Outlook for 2012, published in November, noted "Government spending is projected to decline while the outlook for exports is mixed, due to modest global demand growth and anticipated changes in Atlantic Canada's output of key products," noted the report.

In June, APEC's 2011 Major Projects Inventory gauged the region's potential major-project investment at $71 billion, comprising 354 projects this year—a bit off last year's $72 billion.

The bellwether in the area is Newfoundland and Labrador, where growth will rise 4.2 per cent this year, thanks to mining production and capital investment. However, lower oil output will offset gains in mining and continued strong investment, with real GDP growth forecast at a moderate 1.1 per cent in 2012.

**QUEBEC –** Four of Canada's 10 biggest infrastructure projects this year are in Quebec. Major projects include Hydro-Quebec projects, The Turcot Interchange in Montreal and the Centre hospitalier de l'universite de Montreal.

Statistics Canada says the sector generated just under $15 billion in 2010—almost six per cent of the provincial GDP. RBC has forecast real GDP growth at 1.7 per cent in 2011 and 2.1 per cent in 2012.

**ONTARIO –** "What I'm hearing is cautious optimism for 2012," says Clive Thurston, president of the Ontario General Contractors Association. "We're not seeing much coming from the commercial side or from the private sector, which is still the biggest problem," he adds. On the other hand, transit programs and the Pan-Am games are going to be major opportunities. "It's going to be fine, but it will be a little tighter than usual. You're going to be relying on public works," says Thurston.

RBC noted supply-chain disruptions in the auto sector and slow growth in the U.S. economy will affect Ontario in 2011 and 2012. It predicts real GDP growth of 2.3 per cent in 2011 and 2.4 per cent in 2012.

**PRAIRIES –** Commodities keep Saskatchewan and Manitoba in the spotlight.

According to Construction Specifications Canada (CSC), 2011 and 2012 will be peak years in Saskatchewan. A challenge will emerge after 2012 when known projects wind down. RBC forecasts real GDP growth of 4.3 per cent in 2011 and 4.1 per cent in 2012.

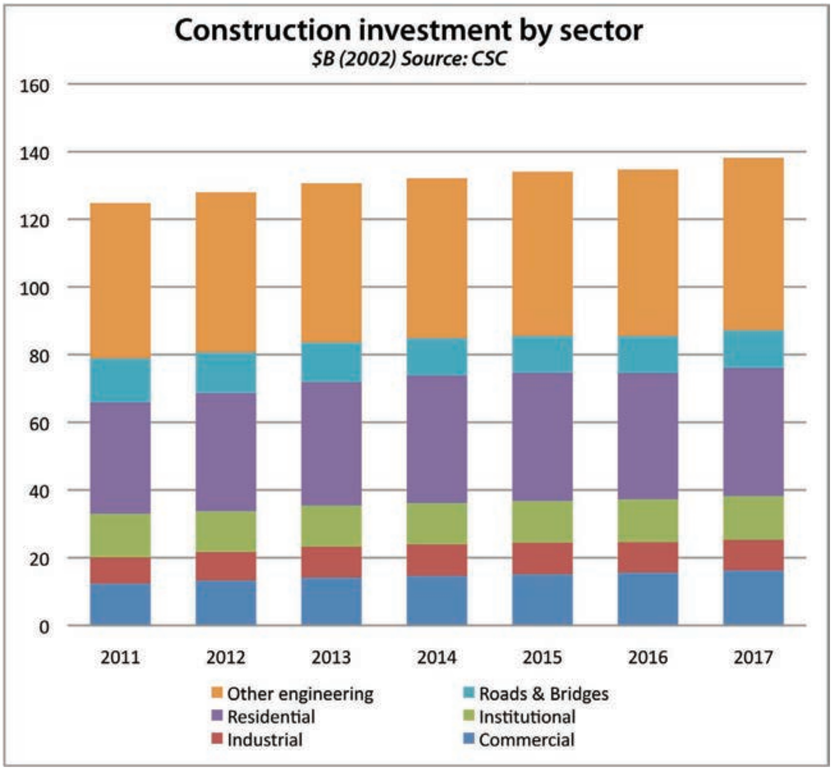
Major non-residential projects are underway or in planning in Manitoba, according to CSC. Large utility projects will peak in 2014, but employment should remain strong. RBC expects real GDP growth of 2.8 per cent in 2011 and 3.5 per cent in 2012.

**ALBERTA –** Recovery is coming quickly, taking Alberta back to levels of construction employment reached in 2008, says CSC. RBC expects real GDP growth of 3.7 per cent in 2011. Continued strength in energy-related sectors will further increase growth to 3.9 per cent in 2012.

**BRITISH COLUMBIA –** CSC predicts that an uneven pattern of expanding construction in 2015 will push the industry back towards 2007 numbers. RBC's predictions for real GDP growth are 2.1 per cent in 2011 and 2.3 per cent in 2012.

## SECTORS

Building permits have also been trending downwards lately. September, with $5.6 billion worth of building permits marking a 4.9-per-cent decline from the previous month, was the third




successive month of decreases, according to Statistics Canada.

Non-residential permits dropped 11 per cent to $2 billion, with declines in five provinces. Residential permits fell 1 per cent to $3.6 billion, following a 6-per-cent decline in August and decreasing in six provinces.

It is important to note engineering projects are not tracked in this data.

**INDUSTRIAL** – The strength of the industrial component of the non-residential building sector varies by sector and region. Anything tied into commodities should be a winner. In September, the value of permits rose 2.3 per cent to $388 million after a 4-per cent increase in August. Five provinces recorded advances, led by Ontario. "Manufacturing plants and utilities buildings were behind most of the gains," noted Statistics Canada.

**INSTITUTIONAL –** In this component, permits totalled $368 million, a 40.8-per-cent decline from August and the second monthly decrease in a row. This was the lowest level since January 2011, and institutional construction intentions fell in seven provinces. The largest decreases were in building permits for educational institutions in Ontario and B.C. and medical facilities in Alberta.

**COMMERCIAL –** In this sector, permits slipped 0.5 per cent to $1.3 billion in September, after a 19.6 per cent drop the previous month. "The decreases were partly offset by combined gains in office buildings and recreational facilities, primarily in Ontario," noted Statistics Canada.

**RESIDENTIAL –** Growth in housing in 2009 and 2010 was fuelled by stimulus and low interest rates, noted CSC, "But long-term demographic trends will limit the potential for new housing construction. The scenarios for most provinces include declining employment in residential construction across most of the scenario."

Canada Mortgage and Housing Corporation (CMHC) expects the real-estate market to stabilize this year and next. Housing should range from 170,900 to 199,900 units in 2011. That's comparable to the 189,930 units started in Canada last year, down from the peak hit in previous years.

In 2012, CMHC expects housing starts to be in the range of 161,650 to 206,350 units, with a point forecast of 186,750 units.

"2011 marked the transition into a period of more moderate building activity. A slowing in the Canadian housing market and an overbuilding in the condominium market is expected to be the main forces for a moderation in residential building," TD Economics noted in November.

## THE GOOD NEWS

The big news in Canadian construction in 2012 will be large engineering projects.

- Energy projects include the $6-billion Lower Churchill Development at Gull Island and Muskrat Falls, NL and the $7.9-billion Site C Clean Energy Project in B.C. among other sites;
- Mining projects such as the $3.5-billion Kemag Mining Project in Quebec and B.C.'s $2.9-billion Schaft Creek copper-gold-molybdenum-silver deposit project, among others in the north and Quebec;
- Oil-patch projects include Suncor's $10-billion heavy-oil processing plant, the $3.6-billion Firebag 4 oil sands project in Alberta and Chevron's $10-billion Hebron oil refinery in Newfoundland;
- More than a $1 billion in construction is slated for the 2015 Pan American Games in Toronto, as well as a $1-billion extension to the Toronto-York Region Spadina Subway Extension;
- And finally a massive investment in shipbuilding, as the federal government launches a $33-billion program to build 116 small naval vessels. The two major contractors will be Seaspan Marine Corp. in North Vancouver, B.C. and Irving Shipbuilding Inc. of Halifax, N.S. Substantial additions and upgrades to the shipbuilding infrastructure in both cities will be required.

"I think the story is still our natural resources—in both the private and public infrastructure markets," says Atkinson. Positioning your firm to align with the country's strengths, and finding partners involved in those markets, is always a sound strategy. ■



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