

CONSTRUCTION INSIGHTS



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2022 Construction Outlook

LOOKING BACK: THE REVIVAL

The pandemic continued to wreak havoc on just about every aspect of daily life for much of the past year, however, Canada and Canadians showed remarkable resilience in adjusting to the upheaval and finding a way forward. In the business and economic landscape, there were even encouraging signs of a recovery, with economic activity bouncing back to pre-pandemic levels in Q3 2021, and the construction industry at the forefront of the revival.

The data bears this out. Growth in the construction sector in 2021, estimated at 6.5%, is expected to strongly outpace projected 4.5% growth in the general economy. New building permits surged, hitting not only their pre-pandemic level in Q2, but their highest level in several years. And Canadian surety industry results - as good a barometer as any of the health of the construction industry - saw a drop of almost 20% in surety claims at Q3 versus the prior year, reflective of a notable reduction in contractor defaults. All compelling indicators of a stable, if not thriving, construction economy in Canada in 2021.

What's particularly remarkable about the construction sector's progress is that it did so while facing a host of pandemic related challenges. Issues such as supply chain disruptions, labour shortages, extreme material price volatility, not to mention the difficulties of managing a largely front line, "essential" workforce through rigorous new safety protocols and restrictions, and the wrench this throws into productivity and scheduling.

Despite these hurdles, the construction industry showed remarkable resolve in getting the job done. And in so doing, once again validating our long-held view that construction contractors are amongst the most resourceful and dynamic entrepreneurs on the planet.

WE WELCOME READERS TO OUR 2022 NEWSLETTER



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BENEFIT FROM OUR SPECIALIZATION



LOOKING BACK: THE REVIVAL (CONT.)

To be clear, ascribing stability to the construction sector in 2021 is not to suggest it was a banner year for individual operators. Generally speaking, it wasn't. The reality is it was a hard fought year of mediocre results for many contractors. But on a relative basis - when measured against the economic collapse of the prior year and the prevailing continued weakness in many sectors - mediocrity stands out as a formidable achievement in 2021.

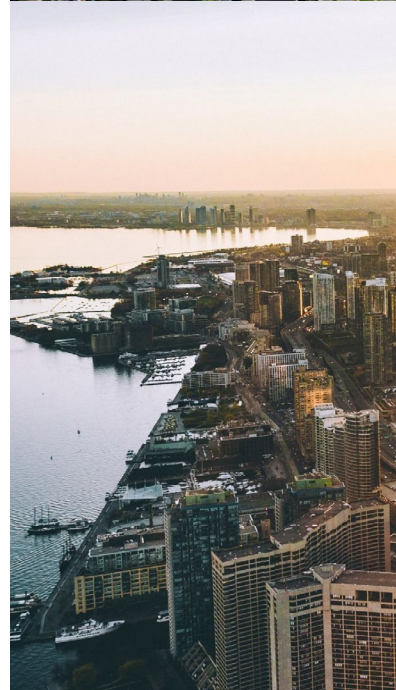
We must also acknowledge the elephant in the room at the time of writing, which is the unexpected end of year spike in pandemic cases, provoking an all too familiar sense of uncertainty with what lies ahead, and the prospect of a slower start to the year.

MOVING FORWARD: SOARING CLOSER TO THE SUN

Notwithstanding any setbacks early in the year, *our 2022 outlook for Canadian construction remains optimistic*. Non-residential (ICI) construction will continue to benefit from a confluence of new and pent-up demand for construction across just about every region in both the government and private sectors. The irrepressible Canadian housing market, buoyed by record new housing starts (and record immigration) in 2021, will take up massive building capacity over the coming years to execute on the pipeline of work. As it usually does, a strong housing sector will lift the entire construction economy as governments make the necessary public infrastructure investment to keep pace with growing cities.

Taking it a step further, we don't rule out an overheated construction market in some regions in 2022. At the same time, the supply chain, labour scarcity, and other pandemic induced problems that plague construction will not disappear overnight, and could conceivably worsen if surging demand further outstrips supply. *The result is the prospect of growing backlogs amidst a higher risk operating environment for contractors, a perilous combination*. It recalls the old maxim that contractors generally don't fail from lack of work, rather, over-extension is what most often delivers the knock-out punch: taking on too much work too quickly and ultimately running out of cash to resolve the bigger problems that typically accompany bigger volumes.

Our focus then turns to how best to maximize success and manage through a potential climate of both greater opportunity and higher risk. The solution lies in project selection, or more specifically, being especially thorough in recognizing and managing the inherent risks in new project opportunities, and selective in dedicating resources and focus to the ones that stand the best chance to generate a proper return. And having the discipline to either walk away from, or price accordingly, those jobs that pose more risk than you're comfortable taking on. They may be best left for the competition.





Our friends at the prominent construction consulting firm, FMI, had this to say on the issue:

Selecting the right work is one of the most important and consequential management activities in an at-risk construction business. Contractors' profit margins are greatly influenced by the quality of their project selection process and decision making. While it may be obvious that good backlog equates to good financial results, the downside risk of poor-quality decision making in project selection is asymmetric. That is, one or a few bad projects can wreck an otherwise profitable year. Contractors' most profitable years are often ones without any major project losses. Thus avoiding catastrophic projects is key to achieving best-in-class profitability, and requires the discipline to say no to opportunities with identifiable issues.



We at PWA are excited for what lies ahead in construction and look forward to continuing to work closely with contractors to help them navigate the choppy waters the industry is sure to bring in 2022.

Good luck out there!

INSURANCE MARKET UPDATE

Most of us are tired of the term “hard market” when discussing insurance, but the truth is, the market has been very challenging since early 2019.

Throughout 2021, insurers continued seeking increased rates, higher deductibles, and more restrictive coverage, and as we head into 2022, the Canadian insurance industry's discipline seems to have paid off with more respectable returns and a stabilizing, yet still somewhat fractured market.

Better managed, longer standing insurers who have realized improved results over the last 3 years will be in the best position to offer more competitive terms.

Having said that, insurers have noted a lull in claims activity, which they attribute to the social restrictions imposed on much of our population throughout the pandemic. As things start to return to a new normal, most expect claims activity to pick back up, especially automobile and general liability claims.

“Social inflation”, a term used to describe the increasing cost of settling claims over the past few years, is predicted to continue. Further, natural catastrophes continue to occur with greater frequency: of the 10 largest natural catastrophe insurance losses in Canadian insurance history, 8 have occurred within the last decade. Due to these factors, we envision the return to a more competitive insurance market will be more of a slow jog, and not a sprint.



INSURANCE MARKET UPDATE (CONT.)

So, what are the insurance challenges unique to contractors that we foresee for 2022?

Since the onset of the hard market, many insurers either stopped offering builders risk insurance or limited their capacity. It is now common for insurers to share builders risk policies with other insurers, requiring more time and effort to negotiate a policy. There is some new, opportunistic capacity entering the market, but it is not naïve, and is also exercising a cautious entrance or re-entrance to builders risk insurance. Builders risk deductibles have increased, and nearly all insurers demand significant deductibles for the specific peril of water damage, especially on multi-storey construction.

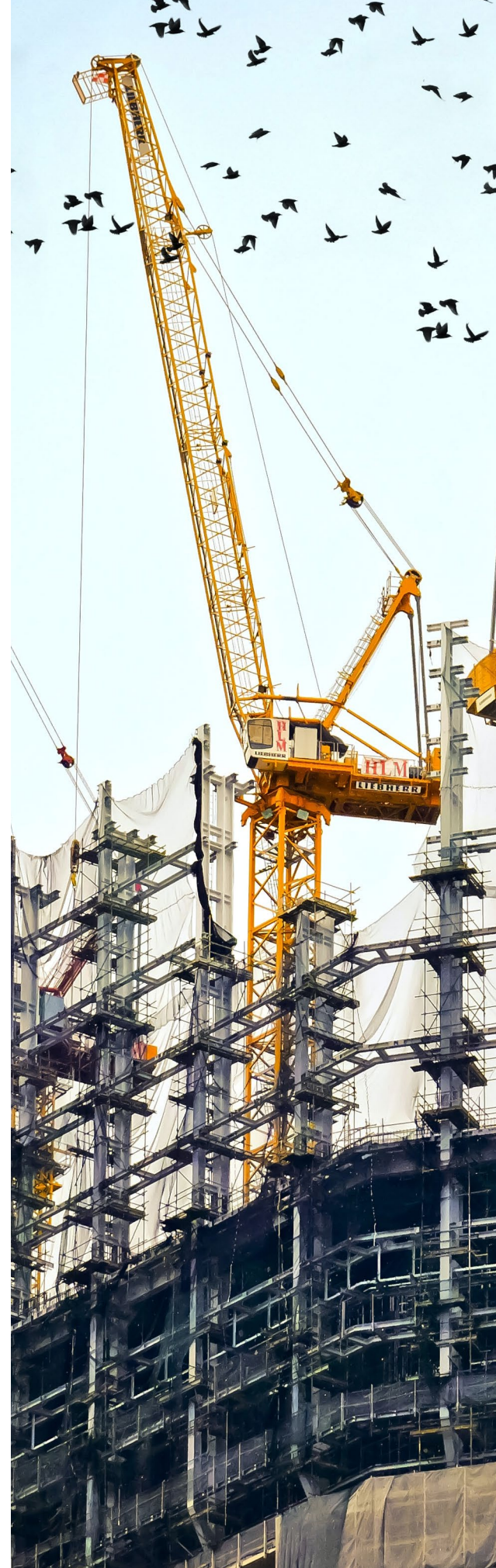
Rebuilding costs continue to escalate due to supply chain shortages. Budgets carried for projects in 2019 and 2020 may not have lined up with the realities of the strained supply chain in 2021, and could lead to some projects being underinsured and claims costing more than anticipated.

Finally, the passing of bill 118 is widely seen as a great step forward in limiting fraudulent slip and fall claims for winter maintenance contractors, however, insurers are waiting to see the long-term effects before changing their appetite or rates for this sector, which remains particularly challenging.

Our parting advice in last year's insurance market update was to partner with a construction specialist broker who can leverage their expertise and market relationships to deliver an improved overall insurance experience for contractors.

2021 statistics released by a large, international brokerage, referred to *"average rate increases upwards of 30% for construction insurance"*. We're pleased to report PWA clients fared considerably better, as our team of experts worked hard, and strategically, to deliver more advantageous results, an accomplishment we're proud of.

Entering 2022, our advice remains the same: having a construction specialist broker in your corner will continue to pay meaningful dividends over the near term and long run.





SURETY MARKET UPDATE

2021 will go down as a strong year for the surety industry, with results showing improvements in both total premiums and losses as of Q3, and these expected to hold for the full year. This comes as a surprise to many who believed the economic impact of COVID-19 would finally catch up to contractors in year two of the pandemic and lead to an increase in surety claims. While that has been true in some cases, results suggest contractors are weathering the storm better than expected, although, as mentioned earlier, as activity picks up there is concern associated with over-extension and depleted balance sheets not capable of withstanding the strain of a sharp uptick in backlog.

As much as the surety industry is in a healthy state and capacity remains robust, bonding company appetites are slightly more cautious and discerning, and while well-managed, better performing contractors continue to attract favourable terms (as always), there's a higher degree of scrutiny being applied across the board. As a result, even in this stable surety environment, underwriters are following up more diligently for financial reporting and asking more questions aimed at understanding how contractors are managing supply chain issues, which to date, show little sign of moderating.

There are some changes anticipated in the Canadian surety space in 2022, and the healthy market is attracting some new surety companies expected to be open for business this year, as well as some notable changes with established players. As a leading surety broker in Canada, PWA is well-connected to the senior decision makers of all Canadian sureties (including the impending new entrants), and we welcome any further inquiries in this regard.

For any contractor that imports materials into Canada, there is a new requirement pending that you obtain your own Canada Customs surety bond (previously, importers were covered by a bond placed by their customs broker). Some customs brokers have already started reaching out to contractors outlining this change. Be advised that while CBSA has tentatively set May 2022 as its "Go Live" date for the new security arrangements, there are ongoing discussions on the wording and amount for the bond. PWA can provide guidance and the required bonds.

BOND ORDERING PLATFORM

BONDLINE
NAVASURE™

We were very proud to roll out BondLine in 2021, our newly enhanced online bond ordering and management website! Offered *exclusively* to clients of PWA and Navacord, BondLine allows contractors to order bonds and insurance documents, track and manage outstanding bids, verify bond rates and premiums, and much more – all online with the click of a virtual button.

BondLine was the product of over 18 months of planning and investment by PWA, and has been very well received by our clients, who appreciate the convenience and speed that it offers. Stay tuned as we will be rolling out even more features in 2022!

PWA TEAM UPDATE

Flexibility and adaptation are key ingredients to success, and while 2020 was trial by fire, 2021 provided an opportunity for PWA to hone our operation to keep pace with the rapidly evolving professional services workplace.

We introduced a “hybrid work policy”, which has been very successful, enabling more flexible work arrangements for our team while maintaining a seamless service experience for our clients, and the team-based spirit and culture that are key to our success. The technology side of our business saw continued focus and investment, with the implementation of several IT initiatives aimed at improving the ease of doing business and overall experience for both staff and clients.

Our team continued to grow throughout 2021, with six important new additions to the PWA family.

At the head office in Toronto, Kristena Cvetanovski joined in Q1, and has provided much needed strong support to the always-buzzing Insurance Services team. In late spring, a familiar face, Kelli Leoen rejoined our insurance practice, picking up where she left off a few years back and adding to the seasoned bench with her extensive construction related experience and enthusiasm for the business. Also joining the insurance team over the summer were Joel Philip and Julia Park, who hit the ground running and have been an excellent addition to our team of Insurance Associates. In Sudbury, PWA's Northern Ontario office, the insurance team grew with the addition of Tara Trimmer, an industry veteran with a wealth of experience in the construction insurance segment. Finally, Jennifer Mahabir joined us in our Bond Services group, bringing a passion for the surety business and several years of related experience to the team.

Finally, more exciting news - we've outgrown our midtown Toronto office, where we've been situated since 2004, and will be moving to a new location in Q2 of 2022. Details to follow!



**WE CELEBRATED
IN 2021!**

MILLIE MACESIC

CHRIS CURRY

MARIANA DIMITROVA

ALEX MINO

15 YEARS

10 YEARS

5 YEARS

5 YEARS



LONDON & SOUTHWESTERN ONTARIO BRANCH UPDATE

PWA's London Branch continued to see consistent growth in the Southwestern Ontario region, as contractors continue to value our professional advice and guidance when it comes to managing tricky insurance renewals and/or seeking improvements to their bond programs.

After a pause due to the pandemic, our team was thrilled to be back participating in some local construction association events, including the LDCA Project Excellence Awards and the LDCA Christmas Lunch. It was great to see so many familiar faces again!

While 2021 presented challenges in many ways, it also brought forward opportunities for our firm. Joining the Navacord group of brokers is Ives Insurance Broker and McConville Omni Insurance Brokers which, combined with PWA and Selectpath, helps position us as a regional powerhouse within Southwestern Ontario, while still maintaining our construction focus and the attention to detail our clients have grown accustomed to over the years.

In closing, at the time of writing, the IHF just made the difficult decision to cancel the 2022 World Junior Hockey Championship: For all those hockey fans out there, we will have to buckle up and sit tight before watching Connor Bedard dazzle the fans again!



SUDBURY & NORTHERN ONTARIO BRANCH UPDATE

PWA's Sudbury operation has been building on its success since its establishment in 2020, and Northern Ontario contractors appear to be appreciating the benefits of working with a construction specialist brokerage firm as we continue to grow in the North. Our timing was good (pandemic aside) and the challenging insurance market in 2020 and 2021 has elevated the need with the region's contractors for a problem solving, construction specialist broker. PWA has responded by attracting outstanding talent to build the branch, and we appreciate the support we've received from the construction community.

We were delighted this year to welcome Tara Trimmer to the Northern Ontario team as Senior Insurance Account Manager, joining Jocelyn Horsfall, Sudbury branch leader, and are looking forward to further additions to the team in 2022.

Stay tuned as we continue to invest in our Northern Ontario branch and advocate for the specific needs of the region's contractors!



NAVACORD UPDATE

It's hard to believe that it's been 6 years since PWA became the first Navacord partner back in 2015, and we're thrilled to see such extraordinary progress during this time. Navacord is a top 5 broker in Canada, with total premiums of roughly \$2.5 billion, through 40 leading brokerages from coast to coast, and across various lines; commercial insurance (60%), personal insurance (25%) and life / group benefits (15%).

In 2021, Navacord welcomed several respected insurance brokerage businesses in Atlantic Canada, Ontario and Western Canada. We also made investments in our legal and financial infrastructure, with a large commitment to IT, an especially important investment given the current hostile climate of cyber crimes.

We put on very a successful virtual construction conference for our contracting clients in the Spring, and later in the year brought together 100 of Navacord's construction focused professionals for a virtual "Construction Summit", with technical learning sessions and forums designed to collaborate, share ideas and best practices, and enhance the value proposition for our construction and surety bonding clients from coast to coast.

Finally, Navacord's commitment to our people has been steadfast. In 2021, we are 2,000 exceptional employees, including 200 shareholders actively engaged in the business. Our people, and our broad shareholder base, stand out as strong differentiators in our industry, and a key ingredient to our customer-centric culture.

We hope this update was of interest and wish you a prosperous 2022.

Feel free to contact us if you have any questions about any of the information contained in this document.

BENEFIT FROM OUR SPECIALIZATION

Toronto
416.488.2522

London
519.439.7754

Sudbury
705.280.6554