



UNION SECURITIES LTD.

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## INFRASTRUCTURE – AN INVESTMENT THEME FOR 2009 AND BEYOND

February 25, 2009

- We believe Infrastructure will be one of the key investment themes in 2009 and beyond for several reasons:
  - (i) Governments in the U.S., Canada and several other countries around the world have announced economic stimulus programs, with infrastructure occupying a central role. In the U.S., the economic stimulus program is worth approximately US\$790 billion, (with infrastructure, including energy infrastructure, totaling approximately US\$200 billion) and in Canada, it is in excess of \$30 billion;
  - (ii) The systematic underspending in infrastructure assets over the last three decades in the U.S. and Canada has resulted in massive “infrastructure deficits” reaching crisis proportions (in the U.S. it is estimated at US\$1.6 trillion and in Canada at C\$123 billion), making infrastructure spending imperative;
  - (iii) The historically low correlation of infrastructure securities to other asset classes, offers the opportunity for portfolio diversification during a period of heightened stock market volatility;
  - (iv) Greater participation of the private sector in the ownership, operation and maintenance of infrastructure assets (P3 or public-private partnership) offers greater potential to bridge the infrastructure deficit and spur growth in the infrastructure space; and
  - (v) The potential for steady income and inflation protection from certain types of infrastructure stocks (e.g., pipelines, power generation etc).
- Key beneficiaries of the infrastructure spending in the US and Canada include companies in the civil construction, engineering services, electrical and alternative energy, water infrastructure services and industrial products sectors. In anticipation of the impending infrastructure spend, stocks leveraged to infrastructure have seen price appreciation with large capitalization infrastructure related stocks in Canada rebounding from the market lows seen last fall and outperforming the TSX.
- However, several small cap infrastructure related stocks have underperformed the TSX over the same time frame and trade at steep discounts to their historical trading ranges. We believe the overall weak market sentiment to the broader small cap space is the key reason for the weak relative performance of small cap infrastructure stocks. When market sentiment for this asset class (small cap stocks) improves, we expect small cap infrastructure stocks could rebound and for investors with a medium-term horizon (> 1 year), and the capacity to withstand volatility, small cap infrastructure stocks could provide solid returns over this time frame.

Please see important disclosures at the back of this report.

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## INFRASTRUCTURE – AN INVESTMENT THEME FOR 2009 AND BEYOND

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- (v) the potential for steady income and inflation protection from certain types of infrastructure stocks (e.g., pipelines, power generation etc).

There are two ways for investors to play the infrastructure theme:

- (i) **Infrastructure Operators** – they include capital intensive infrastructure assets with long lives, steady inflation-linked cash flow streams with relatively high barriers to entry. This includes utilities (pipelines, power generation), toll road/bridge operators, airports and ports, etc. Securities of infrastructure operators typically offer lower risk with moderate but consistent returns. In recent years, securities of infrastructure operators have found favor with large investors, for example, pension funds, given the predictability of their cash flow stream and consistency of returns;

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<sup>1</sup> American Society of Civil Engineers, 2005

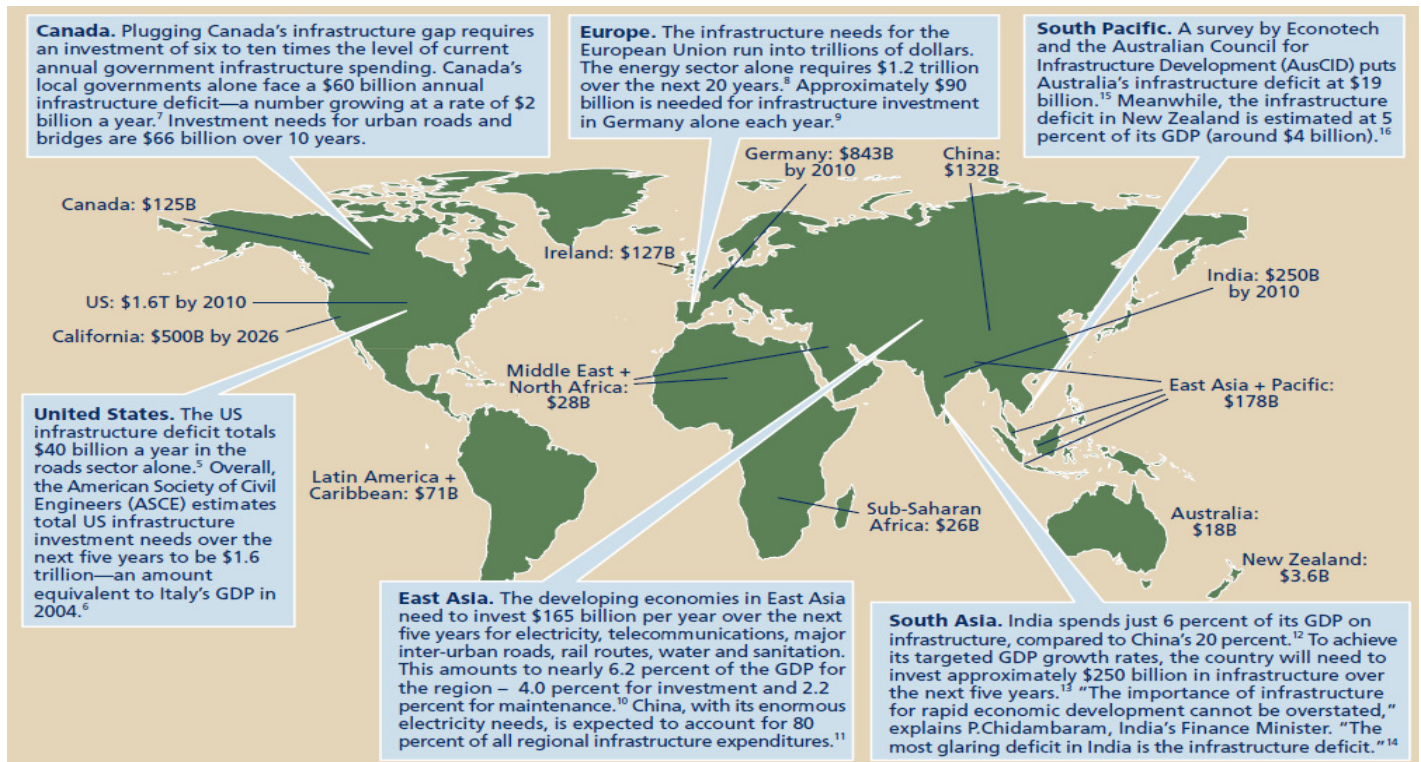
<sup>2</sup> Federation of Canadian Municipalities, 2007

(ii) **Infrastructure Suppliers** – they include companies that provide products and services to the utility-type infrastructure operators, Government owned and maintained infrastructure assets (highways/bridges, water treatment, wastewater management, power transmission, social infrastructure, etc) and include ancillary companies that are expected to benefit from the surge in infrastructure spending. Companies in this second category include large and small capitalization public companies, in addition to private companies. Our focus in this report will be on stocks that fall into the Infrastructure Suppliers category.

### **HOW SEVERE IS THE INFRASTRUCTURE PROBLEM?**

The problem appears quite severe. The broad definition of infrastructure encompasses assets that are used in the productive process (roads/bridges, ports, water supply, waste management, power generation, transit systems, etc.), as well as typically Government-owned social Infrastructure such as health systems, recreational and cultural facilities. Countries and Governments across the globe have had to face a chronic infrastructure deficit resulting from years of underspending due to a lack of sufficient funding. Exhibit 1 on the following page provides a snapshot of the glaring infrastructure deficits around the world and underscores the fact that infrastructure, as an investment theme, is likely to be an enduring one over the medium-term.

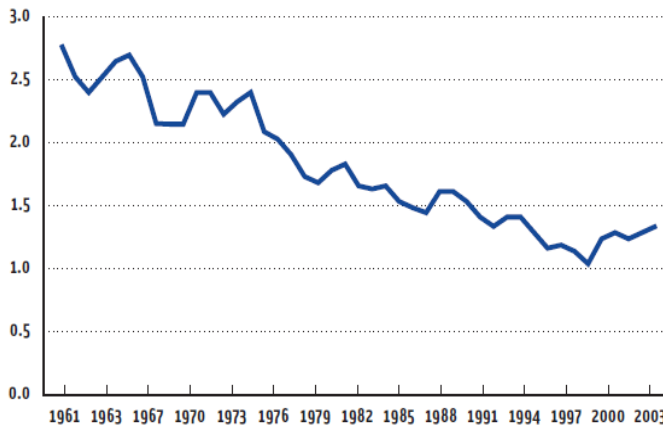
**Exhibit 1. Global Infrastructure Deficit**



Source: Deloitte & Touche

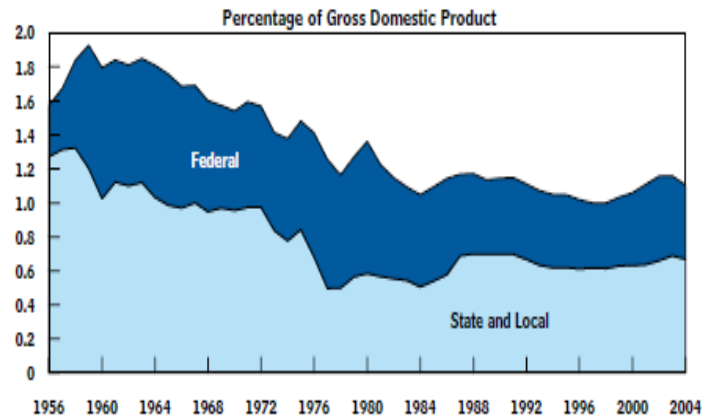
The focus of this report will be Canada and the U.S. After a period of sustained and growing spending on infrastructure during the sixties and early seventies, the subsequent decades have seen infrastructure related spending (as a % of GDP) decline. Exhibits 2 and 3 on the following page, highlight the trend of Infrastructure spending over the last several decades in Canada and the U.S., respectively, with spending peaking in the early sixties and beginning a steady decline thereafter.

**Exhibit 2. Canada Infra Spending (% of GDP)**



Source: Canada Department of Finance

**Exhibit 3. U.S. Transportation & Water Infra Spending (% of GDP)**

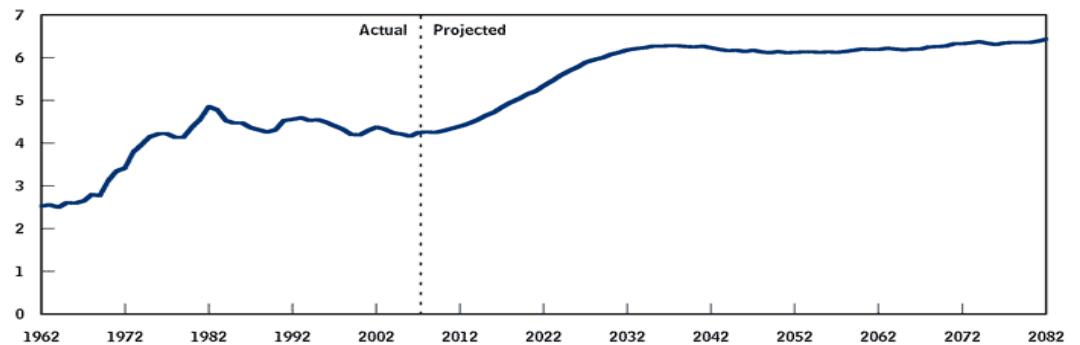


Source: Congressional Budget Office

The two key reasons for the neglect and under spending in infrastructure in the U.S. and Canada are listed below:

- (i) A gradual creep up in spending on social security payments including pensions, etc, has impacted the ability of federal governments in the U.S. and Canada to fund infrastructure investments; and

**Exhibit 4. U.S. Social Security Spending (% of GDP – past and projected)**

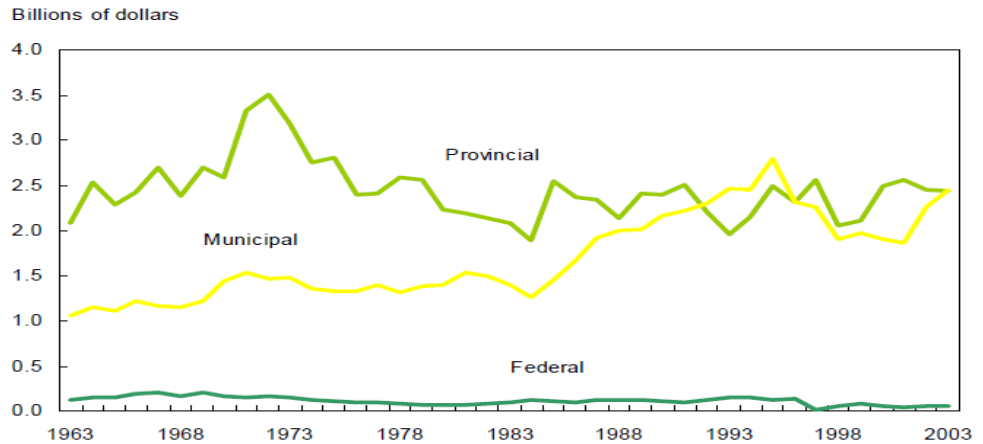


Source: Congressional Budget Office

- (ii) Federal and provincial/state governments in Canada and the U.S. are increasingly transferring responsibility for infrastructure assets to municipal governments. In the U.S., between 1956 and 1966, federal infrastructure spending, as a share of total non-defense federal expenditures, was approximately 10%. Since then, there has been an average steady decline of 3.5% - 4.0%, in each of the last two decades. In Canada, the value of municipal ownership of road infrastructure rose 226% between 1963 and 2003, while over the same period, provincial capital stock declined 79% and federal capital stock declined by 42%.

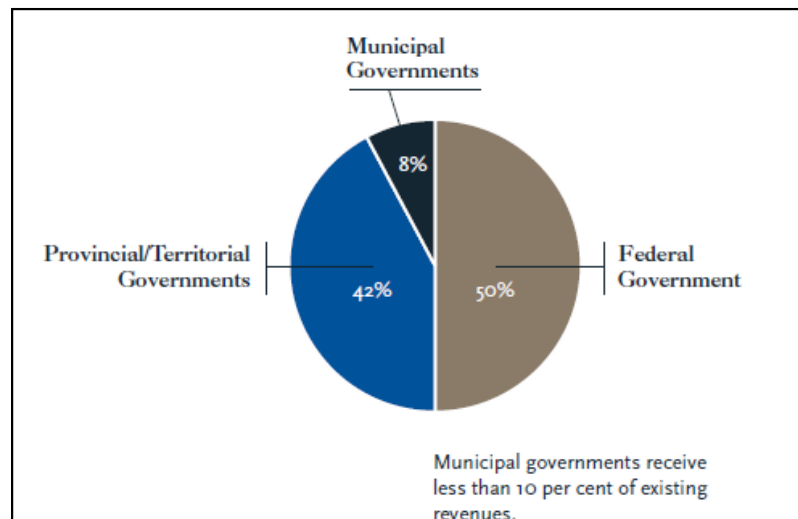
Municipal governments lack the taxation power and financial base that provincial and federal Governments possess which, coupled with reduced transfer payments from higher levels of government, has impeded their ability to finance infrastructure in a timely and adequate manner.

**Exhibit 5. Canada Road Infrastructure Investment – Levels of Government**



Source: Statistics Canada

**Exhibit 6. Municipal Government Tax Share (Canada)**



Source: Federation of Canadian Municipalities

## WHICH SEGMENTS WILL BENEFIT?

Our analysis and the recent stimulus packages in the US and Canada indicate that four broad segments will receive a material portion of the anticipated infrastructure spending. They include: (i) Transportation (roads, bridges, highways); (ii) Water Supply and Wastewater Treatment; (iii) Power Infrastructure/Alternative Energy (energy efficiency, etc); (iv) Social Infrastructure.

**Transportation.** This includes roads, highways, bridges and related capital stock. In Canada, highways and roads comprise the largest component of public assets listed above (59%) and were worth \$170 billion in 2007. Bridges and overpasses accounted for 8% of the total assets. Highways and roads have an average service life of 28.2 years<sup>3</sup> and in 2007 the average age of roads and highways in Canada was 14.9 years. Bridges and overpasses have an average life of 43.3 years and in 2007 the average age of bridges in Canada was 24.5 years. Net/net Canada's bridges have passed 57% of their useful life with roads at 53%, indicating renewed investment is necessary in these assets.

The situation in the U.S. is similar, with road and highway infrastructure consuming over 50% of annual infrastructure related investments. Although over US\$100 billion is invested each year in infrastructure, the U.S. Federal Highways Administration in 2005, estimated that at least an additional US\$20 billion over and above the existing spend is required to maintain infrastructure at current levels. Exhibit 7 highlights the details.

### Exhibit 7. Annual U.S. Spending of Transportation Infrastructure (2005)

US\$ billions	Current Spending	Spending to maintain current level of service
Highways	\$66.7	\$78.8
Mass Transit	\$15.5	\$15.8
Freight Railroads	\$6.4	\$10.7
Passenger Railroads	\$0.7	\$0.5
Aviation	\$14.4	\$17.9
Water Transportation	\$2.5	\$2.7
<b>Total</b>	<b>\$106.2</b>	<b>\$126.4</b>

Source: Congressional Budget Office

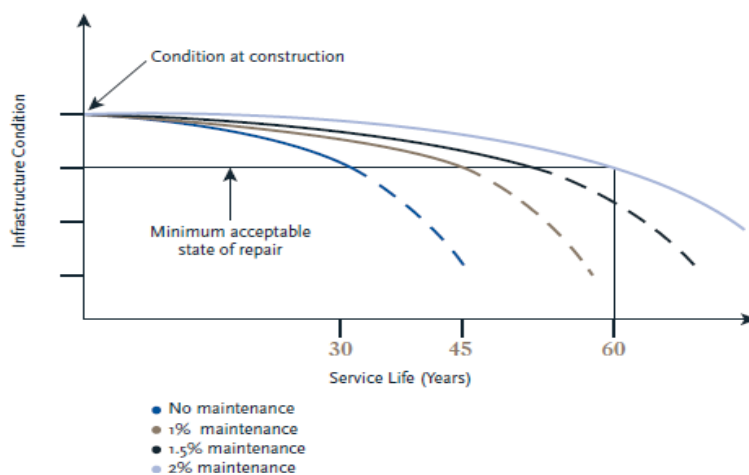
<sup>3</sup> Statistics Canada

In addition, given the job creation potential of highway/road construction projects and attendant productivity enhancements, transportation will continue to be a targeted segment for infrastructure spending. The American Automobile Association estimated that every US\$1 billion invested in transportation infrastructure, has the potential to generate 47,500 jobs and every dollar invested in highway construction generates US\$2.50 in GDP in the short-term.

**Water Supply and Wastewater Treatment.** This refers to water infrastructure, for example, water mains, distribution pipes, pumping stations, storage capacity, water meters, etc. In 2003, the Canadian Water Network estimated Canada's water infrastructure deficit at \$39 billion, to maintain already existing water supply and wastewater treatment systems. In a more recent study by the Federation of Canadian Municipalities, the water supply and wastewater infrastructure deficit was estimated at \$31 billion and requirements for new investments were estimated at approximately \$57 billion.

The situation is similar in the U.S. where the Environmental Protection Agency (EPA) estimates that over the next 20 years the investment deficit for wastewater will be over US\$270 billion. The Congressional Budget Office estimates the annual requirement for both waste and drinking water is between US\$20 and US\$40 billion. What has also compounded the problem in both the U.S. and Canada has been the deferral of maintenance and repair and rehabilitation during fiscally difficult times. Exhibit 8 highlights the impact of deferred maintenance on the longevity of infrastructure assets – with no maintenance or sporadic maintenance, the infrastructure deteriorates quite rapidly with considerable reduction in its service life.

#### Exhibit 8. Infrastructure Condition as Determined by Maintenance



Source: Federation of Canadian Municipalities

**Power Infrastructure/Alternative Energy.** Our analysis indicates the power sector (generation, transmission/distribution) including alternative energy and energy efficiency could continue to receive material investments. In Canada, after a period of underinvestment in the nineties, the current decade has witnessed a rebound in investment with capital investment reaching \$13 billion in 2006, a three-decade high. However, demand over the period between 1990 and 2005 grew 24% and is expected to grow at a rate of 1.5% annually. The Canada Electricity Authority estimates that between 2005 and 2030 an investment of \$190 billion would be required in Canada's power infrastructure.

Similarly, in the U.S., the North American Electric Reliability Corporation (NERC) estimates that over the next decade 135 gigawatts of new capacity will need to be added to meet demand, however, ongoing investments will be sufficient only in creating 57 gigawatts. The Brattle Group estimates that US\$1.5 trillion will need to be invested between 2010 and 2030 in the U.S. to maintain today's level of service. While new generating capacity has a gestation period of a few years, there are urgent investments needed in the Transmission & Distribution infrastructure. In the U.S., 70% of transmission lines are 25 years or older, 70% of power transformers are 25 years or older and 60% of all circuit breakers are more than 30 years old. The Obama administration has committed US\$11 billion in the recently passed economic stimulus package to modernize the electrical grid to improve efficiency and allow easier integration of renewable energy sources to the grid. The so-called 'smart grid' will introduce digital technologies that are expected to reduce waste and inefficiency, improve reliability and reduce emissions.

In October 2008, the U.S. Congress passed legislation renewing the solar investment tax credit ("ITC") by eight years, the production tax credit for wind projects by one year and geothermal by two years. They also eliminated the US\$2,000 cap on the residential ITC and eliminated the prohibition on utilities from obtaining the ITC. As credit conditions ease, the renewable energy sector could get a further boost. Renewable energy is also featured in the Obama administration's Infrastructure stimulus program. The recently passed US economic stimulus package has committed over US\$10 billion to various renewable energy initiatives.

**Social Infrastructure.** This includes schools, hospitals, universities, sports facilities, government buildings, etc. In the U.S., President Obama has stated that his American Recovery and Reinvestment Plan will include investments in schools, libraries and laboratories. In Canada, social infrastructure also occupies an important role in the infrastructure spending plans of the government. The budget for 2009 has allocated spending to the tune of approximately \$3.0 billion for social infrastructure.

## WHO ARE THE BENEFICIARIES GOING TO BE?

**Civil Construction.** These are companies that provide civil design, building services, construction management and procurement services. They include small local companies that provide construction services for buildings and roads to larger companies that undertake complex design and building work, including project management services. We believe these companies will be the earliest beneficiaries of infrastructure spending given the infrastructure deficit in the U.S. and Canada and their capacity to generate jobs. The U.S. Conference of Mayors recently submitted a report indentifying 5,000 “shovel ready” projects worth US\$96 billion and in Canada the Federation of Canadian Municipalities estimates there are \$13.7 billion worth of similar “ready-to-go” projects. Therefore, it is likely this group would be among the earliest to benefit from the infrastructure spending.

**Potential Beneficiaries** – Aecon (ARE), Bird Construction (BDT-UN), Churchill Corp (CUQ), Seaciff Construction (SDC), SNC-Lavalin (SNC), Canam Group (CAM), ADF Group (DRX), Lockerbie & Hole (LH).

**Engineering Services.** These companies provide specialized professional consulting, engineering, project management, surveying, environmental impact assessment services, etc. This segment is quite fragmented with companies serving only local markets co-existing with large companies that have a national footprint. We expect engineering services to benefit from infrastructure spending, although it is dependent on the sectors these companies have exposure to. For example, engineering firms that have more exposure to the mining and oil & gas industries are less likely to benefit than those with exposure to the public sector.

**Potential Beneficiaries** – Stantec (STN), Genivar (GNV-UN), and local private companies.

**Electrical & Alternative Energy.** They include companies that supply machinery, parts to the power generation, transmission and distribution sectors. Companies that supply products that improve the energy efficiency of buildings and provide alternative energy infrastructure are also likely to benefit.

**Potential Beneficiaries** – Hammond Power Solutions (HPS/A), Waterfurnace Renewable Energy (WFI), Day4 Energy (DFE), Electrovaaya (EFL), Microplanet Technologies (MP).

**Water Infrastructure Services.** Given the water supply and sewage systems infrastructure deficits in both the U.S. and Canada, water infrastructure is a focus area. Companies in this segment provide equipment for water treatment plants, supply pipelines, monitoring equipment, and storage facilities etc.

**Potential Beneficiaries** – GLV Inc. (GLA-A), Armtec Infrastructure (ARF-UN), ZCL Composites (ZCL), and Pure Technologies (PUR).

**Industrial Products & Construction Materials.** They include companies that provide construction equipment, construction aggregates (sand, gravel etc), and equipment distributors, etc.

**Potential Beneficiaries** – Polaris Minerals (PLS), Toromont (TIH), Wajax (WJX-UN), Rocky Mountain Dealership (RME), and Finning Intl (FTT).

## CANADA & U.S. – INFRASTRUCTURE SPENDING DETAILS

Recently, the Canadian federal government passed the 2009 budget, containing explicit provisions for infrastructure spending over and above ongoing infrastructure programs. The new infrastructure spending programs play a central role in the government's efforts at reflating the economy. The federal budget earmarks nearly \$12 billion in new infrastructure spending through end of 2011. When provincial contributions are added to this, the total adds up to \$21 billion. This announcement comes over and above the \$33 billion announced in the 2007 budget under the seven-year Building Canada program. Key highlights in the budget include:

- A two-year, \$4 billion infrastructure stimulus fund that will provide funding to renew infrastructure,
- \$1 billion over five years for a Green Infrastructure fund to support projects such as sustainable energy,
- Accelerating \$1 billion in payments over two years to expedite "ready-to-go" infrastructure projects,
- \$2 billion to repair, retrofit and expand facilities at post secondary institutions, and
- \$1.5 billion to build and renew federal public infrastructure.

**Exhibit 9. Canada Economic Action Plan Summary**

	2009	2010	Total
	<i>(mm - cash basis)</i>		
Action to Help Canadian and Stimulate Economy	5,880	6,945	12,825
Action to Stimulate Housing Construction	5,365	2,395	7,760
<i>Housing Leverage</i>	725	750	1,475
Immediate Action to Build Infrastructure	6,224	5,605	11,829
<i>Infrastructure leverage</i>	4,532	4,365	8,897
Action to Support Businesses and Communities	5,272	2,255	7,527
<i>Sectoral leverage</i>	1,300		1,300
Total Federal Stimulus	22,742	17,200	39,942
Total Stimulus (with leverage)	29,298	22,136	51,613
As a share of GDP (%)			
Total federal stimulus	1.5	1.1	2.5
Total stimulus (with leverage)	1.9	1.4	3.2

Source: Government of Canada

In the U.S., the new administration's American Recovery and Reinvestment Act 2009 (H.R.1), which was recently signed into law, is the vehicle that is expected to jumpstart the U.S. economy through fiscal stimulation, with infrastructure playing an important role. The act features several infrastructure related spending proposals aiming to reduce the infrastructure deficit in the U.S., as well as make investments necessary to prepare the economy for future requirements when energy from renewable sources such as solar, wind, and geothermal, etc. is expected to grow in importance. Key infrastructure related spending proposals include:

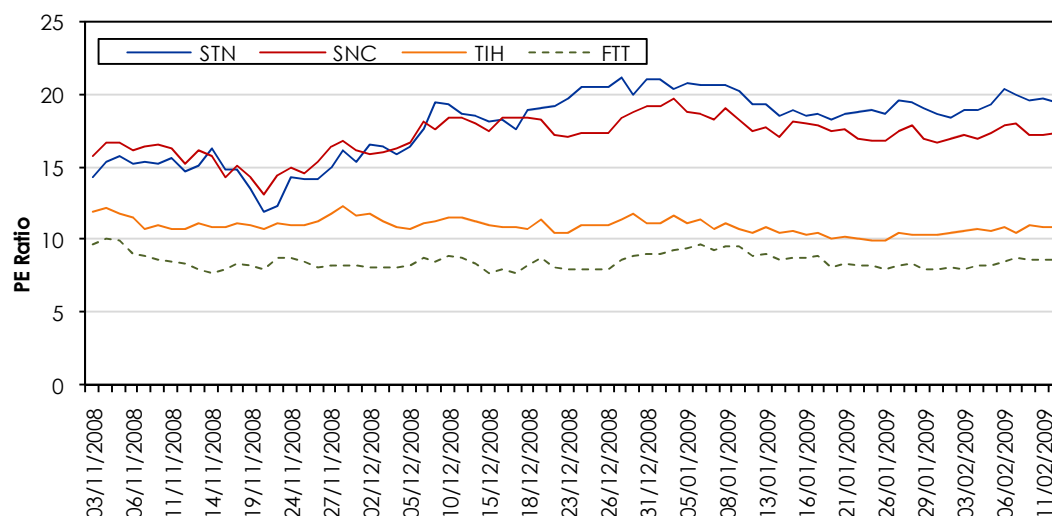
- US\$27.5 billion for highway construction, repair and maintenance;
- US\$20.5 billion for other transportation investment (rail, air, etc)
- US\$4.5 billion to modernize federal and other public infrastructure with investments that lead to long-term energy cost savings;
- US\$14.6 billion for clean water, flood control, and environmental restoration investments;
- US\$11 billion to revamp the nation's power transmission, distribution, and production systems;
- US\$6.25 billion to repair public housing and make key energy efficiency retrofits.

In addition to those mentioned above, there are several other proposals that cumulatively add up to a few hundred billion dollars of expenditures going towards infrastructure spending in the U.S.

## SMALL CAP VS. LARGE CAP INFRASTRUCTURE STOCKS

Given the buzz and hype surrounding infrastructure spending, stocks leveraged to the infrastructure sector have seen price appreciation with prominent large cap names (STN, SNC) in Canada, rebounding from the market lows seen last fall. In Exhibits 10 & 11 below, we highlight the Price Earnings ratios and consensus earnings per share expectation trend of some prominent large cap infrastructure names.

### Exhibit 10. PE Ratio - Large Cap Infrastructure Stocks



Source: Bloomberg, Union Securities

### Exhibit 11. EPS Consensus Trend – STN & SNC

	STN		SNC	
	F08E	F09E	F08E	F09E
31-Jan-09	1.89	2.19	2.06	2.19
31-Dec-08	1.90	2.17	2.07	2.20
30-Nov-08	1.89	2.15	2.07	2.20
31-Oct-08	1.80	2.06	1.99	2.30

Source: Bloomberg, Union Securities

Price Earnings multiples for both Stantec and SNC-Lavalin have held steady in spite of consensus EPS for F08 steadily climbing. In the case of SNC, they have held steady, notwithstanding a moderating of consensus F09 expectations.

However, in the small cap space there are several infrastructure related stocks that have not experienced the same valuation lift, largely, we believe, on account of overall weak market sentiment towards the broader small cap segment.

### Exhibit. 12. Small Cap Infrastructure Stocks - Canada

Company	Ticker	Industry	Market Cap (mm) *	52 Week Low/High *	Current Price *	Comments
<b>Civil Construction / Materials</b>						
ADF Group	DRX - T	Construction Services/Fabrication	\$64	\$1.01 / \$5.93	\$1.72	~ 90% of revenue in US; exposure to public infrastructure sector
Canam Corp.	CAM - T	Construction Design/Fabrication	\$313	\$3.73 / \$12.00	\$6.34	~ 50% revenues US; 74% market share in Canada; plants in US & Canada
Churchill Corp.	CUO - T	Construction/Industrial Services	\$152	\$4.45 / \$24.00	\$8.35	exposure to healthcare, education sectors & power generation; predominantly Canadian exposure
Seacliff Construction	SDC - T	Construction/Electrical contracting	\$150	\$3.85 / \$13.00	\$8.35	~ 50% of revenues from government, healthcare and education sectors
Polaris Minerals	PLS - T	Construction Aggregates	\$76	\$1.19 / \$10.35	\$1.43	~ 85% - 90% of revenues in US; long term supply contracts with customers
<b>Water Infrastructure / Services</b>						
GLV, Inc	GLV/A - T	Water Treatment	\$176	\$3.76 / 415.37	\$6.57	good exposure to municipal sector; ~ 47% of revenues from US; good international revenue diversification
Pure Technologies	PUR - T	Infrastructure Monitoring	\$116	\$2.00 / \$4.00	\$3.55	~ 36% of revenues in US, 53% intl; good exposure to municipal market
Armtec Infrastructure	ARF.UN-T	Water Drainage & Treatment	\$269	\$11.84 / \$27.84	\$17.31	over 90% of revenues in Canada; ~ 55% of revenues leveraged to infrastructure spending
ZCL Composites	ZCL - T	Water and wastewater storage	\$120	\$3.11 / \$9.89	\$4.60	~50% of revenues in US with US based ops; favorable regulatory environment
<b>Electrical &amp; Alternative Energy</b>						
Hammond Power Solutions	HPS/A - T	Electrical Equipment	\$82	\$5.74 / \$14.72	\$6.89	~60% of revenues in US with US based facilities; diversified revenue streams
Waterfurnace Renewable Energy	WFI - T	Geothermal Energy	\$345	\$19.44 / \$32.00	\$28.54	~ 80% of revenues in US; renewable energy tax credits favorable
Day4 Energy	DFE - T	Solar Panels	\$20	\$0.42 / \$6.51	\$0.51	~30% revenues in US; renewable energy tax credits favorable
<b>Industrial Products</b>						
Rocky Mountain Dealership	RME - T	Equipment Distributor	\$348	\$3.00 / \$16.70	\$5.00	74% of revenues from construction segment in Canada
Wajax	WJX.UN - T	Construction/Industrial Equipment	\$311	\$14.00 / \$35.75	\$17.62	~ 50% of revenues leveraged to construction

\*as of Feb. 18<sup>th</sup> close.

Source: Company reports, Bloomberg

## A QUICK NOTE ON P3

P3 stands for Public Private Partnership and refers to private sector financing, design, construction and operation of infrastructure assets. Increasingly, the P3 model is being adopted in financing infrastructure projects, although the level of use and extent of financial participation by the private sector varies by geography. The U.K. pioneered the use of P3 in infrastructure projects; approximately 13% of all infrastructure projects in the U.K. now use the P3 model<sup>4</sup>. In the U.S. and Canada, the P3 model is slowly gaining in ascendancy with appropriate policy and legal frameworks gradually being executed across federal, provincial and municipal jurisdictions. As governments at various levels look to bridge the infrastructure deficit, we believe P3 will play an increasingly important role in the years ahead, in helping bridge the infrastructure deficit for the following key reasons: (i) P3 projects typically allow projects to be brought

<sup>4</sup> Deloitte & Touche

forward by several years versus the conventional pay-as-you-go financing model for infrastructure projects; (ii) P3 projects have a track record of on time, on budget delivery; (iii) in the P3 model, risks are shared between the private partner and government, providing greater incentive for proper maintenance of assets. With the recent credit crunch, P3-based infrastructure projects could see a near-term slowdown as, unlike the government that has the power of taxation and deficit financing, private entities have to access capital markets for their financing. However, the long-term trend suggests P3 model infrastructure projects will gain in importance. Examples of P3 projects in Canada include:

### Exhibit 13. P3 Projects in Canada

Project Name	P3 Partner	Sector	Project Size
Niagara Health System Project	Plenary Health	Healthcare	N/A
Canada Line	SNC-Lavalin & Partners	Transportation	\$1.9 billion
Golden Ears Bridge	Bilfinger Berger	Transportation	\$1.1 billion
Lac Mirabel Complex	Gordon Group Holdings	Social Infrastructure	\$400 mm
Run of River Hydro Project - BC	GE Energy Financial & Plutonic Power	Power Infrastructure	\$660 mm

Source: Company reports, Newswires

## WHAT ARE SOME POTENTIAL PITFALLS?

Although infrastructure spending is touted as a panacea for the ongoing economic ills, there are some potential pitfalls that could limit the positive impact of infrastructure spending. They include:

**Federal vs. Provincial/State.** In both Canada and the U.S., the provincial/state and municipal governments own a larger share of infrastructure stock than the federal government. However, several provincial/state and municipal governments are facing fiscal challenges given the economic slowdown, with funds for infrastructure spending having to be channeled from federal sources. Any delay or red tape in getting funds allocated to the appropriate levels of government could mitigate the positive impact anticipated from infrastructure spending.

**Prudent Allocation.** The manner in which funds for projects are allocated will have a bearing on the effectiveness of infrastructure spending to stimulate the economy and create jobs. There is the potential for powerful local level politicians and lobby groups to influence the way funds are directed and there could be some scope for non-optimal expenditures.

**Adequate Human Resources.** The under spending in infrastructure over the last two decades in the U.S. and Canada has led to a shortage of experienced trades people (fitters, welders, ironworkers, etc), coupled with the retirement of the

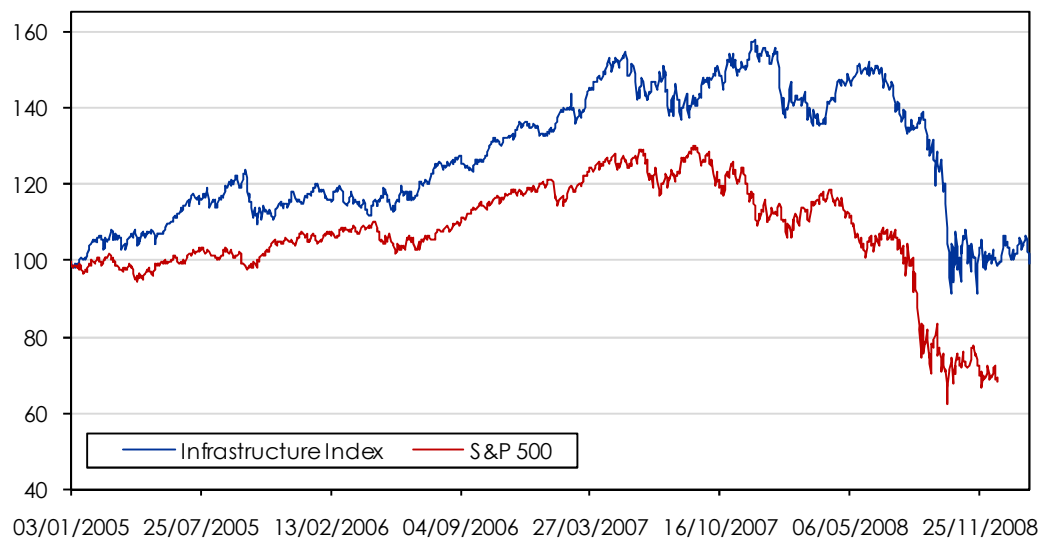
baby boom generation, creating shortages of experienced civil engineers and trades people. This could impact the ability to accelerate the deployment of more complex infrastructure works that involve intricate design, fabrication and project management.

**Political Constraints.** With rising unemployment in the U.S., some members of the U.S. Congress have demanded “Buy American” provisions into the stimulus package. Although it is uncertain to what extent these provisions will be implemented, it could impact the ability to get infrastructure projects completed on time and potentially on budget.

## SOME THOUGHTS ON VALUATION

**Diversification.** Our research suggests infrastructure assets have the potential to provide diversification and offer growth potential to a portfolio given their low correlation to major indices and their relative history of outperforming the broader index. Exhibit 14 highlights the relative performance of the Macquarie U.S. Infrastructure Index to the S&P 500. The Infrastructure Index consistently outperformed the S&P 500 over the most recent four year period.

**Exhibit 14. Infrastructure Index vs. S&P 500 Relative Performance**



Source: Bloomberg, Union Securities

Infrastructure stocks have also exhibited a relatively low correlation to broader indices. Exhibit 15 on the following page highlights the correlation of the S&P Global Infrastructure Index to several other indices. We note the Infrastructure index includes companies both in the “Infrastructure Operators” category and “Infrastructure Suppliers”. Infrastructure operators (power generation, pipelines,

etc.) typically have regulated rates of return, long life assets and high barriers to entry which ensure stable returns in the long run.

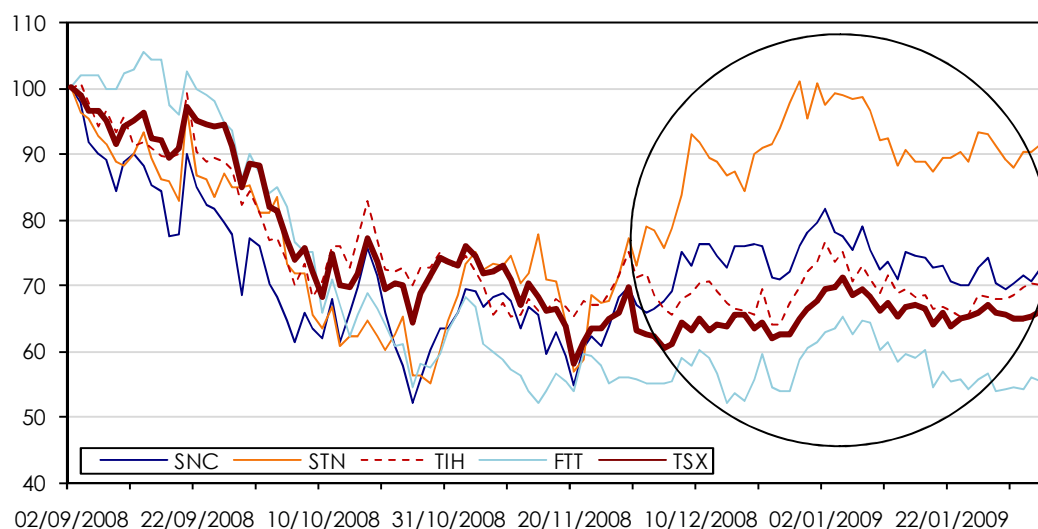
### Exhibit 15. Infrastructure Index Correlation

	S&P Global 1200 Index	S&P Infrastructure Index	S&P 500 Index	NAREIT Equity REIT Index	Lehman Brothers US Aggregate Bond Index	MSCI Index	Merrill Lynch Global Market Index
S&P Global 1200 Index	1.00						
S&P Global Infrastructure Index	0.78	1.00					
S&P 500 Index	0.95	0.67	1.00				
NAREIT Equity REIT Index	0.49	0.42	0.53	1.00			
Lehman US Aggregate Bond Index	-0.12	0.21	-0.14	0.16	1.00		
MSCI World Index	1.00	0.78	0.95	0.48	-0.12	1.00	
Merrill Lynch Global Broad Market Index	0.10	0.04	0.02	0.22	0.76	0.12	1.00

Source: Zephyr StyleADVISOR, Union Securities

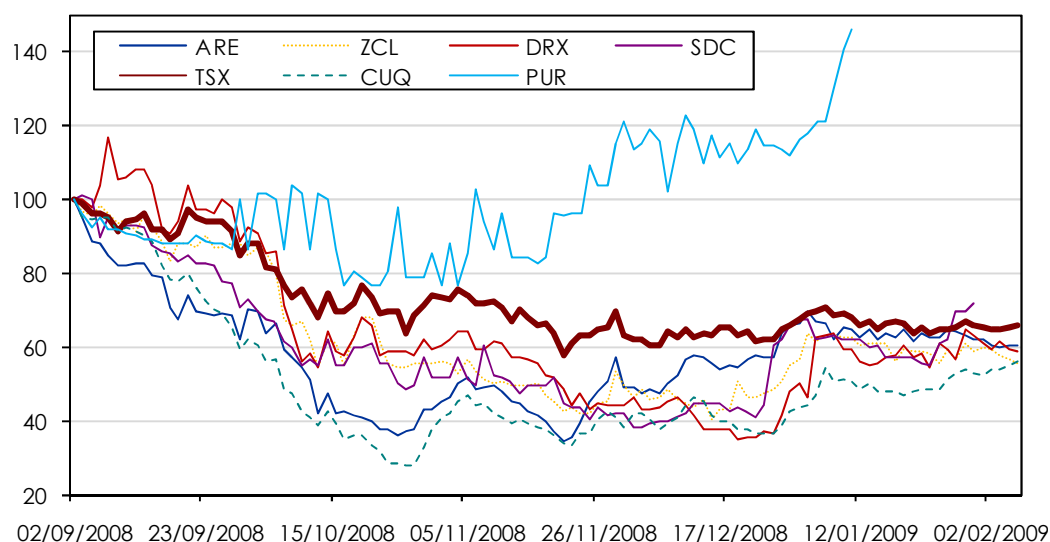
**Small Cap vs. Large Cap Relative Performance.** We looked at the performance of key large cap and small cap infrastructure stocks in Canada since early fall of last year, when it became obvious infrastructure spending would feature in the stimulus plans in both Canada and the U.S. Since early September in Canada, several large cap Infrastructure stocks have outperformed the TSX but several of their smaller cap peers have underperformed. We believe the weak market sentiment for small cap stocks in general could explain the underperformance of small cap infrastructure stocks. When market sentiment for this asset class improves, it is likely small cap Infrastructure stocks could rebound.

### Exhibit 16. Large Cap Infrastructure Stocks vs. TSX – Relative Performance



Source: Bloomberg, Union Securities

**Exhibit 17. Small Cap Infrastructure Stocks vs. TSX – Relative Performance**



Source: Bloomberg, Union Securities

**Trading Multiples.** From a trading perspective, we looked at trading multiples of large and small cap stocks in the Engineering & Construction (E&C) space as well as other stocks leveraged to the infrastructure theme. Large cap E&C names are trading at a forward PE of 11x – 12x and small cap E&C stocks in the 6x – 7x range.

**Exhibit 18. Large Cap E&C - Canada**

Company	Ticker	Share Price 18-Feb-09	Shares (MM)	Net Cash (MM)	Market Cap. \$MM	Net Cash / Share	EPS			Price/Earnings			EV/EBITDA			EV/Sales		
							FTM	FY1	FY2	FTM	FY1	FY2	FTM	FY1	FY2	FTM	FY1	FY2
Stantec, Inc	STN	\$26.30	45.5	-\$210	\$1,197	-\$4.62	\$2.17	\$2.19	\$2.49	12.1x	12.0x	10.6x	N.A	7.2x	6.5x	1.1x	1.0x	1.0x
SNC-Lavalin	SNC	\$32.55	152.1	-\$1,138	\$4,951	-\$7.48	\$2.25	\$2.19	\$2.27	14.5x	14.9x	14.3x	N.A	9.1x	9.1x	0.9x	0.9x	0.8x
Finning Intl	FTT	\$12.67	173.5	-\$1,581	\$2,198	-\$9.11	\$1.45	\$1.48	\$1.55	8.7x	8.6x	8.2x	5.2x	5.1x	5.2x	0.7x	0.7x	0.7x
Toromont Industries	TIH	\$20.51	65.6	-\$60	\$1,345	-\$0.91	\$1.81	\$1.87	\$1.93	11.3x	11.0x	10.6x	N.A	5.6x	5.7x	N.A	0.7x	0.7x
<b>Average</b>										<b>11.7x</b>	<b>11.6x</b>	<b>10.9x</b>	<b>5.2x</b>	<b>6.8x</b>	<b>6.6x</b>	<b>0.9x</b>	<b>0.8x</b>	<b>0.8x</b>

Source: Thomson, Bloomberg, Union Securities

**Exhibit 19. Small Cap E&C – Canada**

Company	Ticker	Share Price 18-Feb-09	Shares (MM)	Net Cash (MM)	Market Cap. \$MM	Net Cash / Share	EPS			Price/Earnings			EV/EBITDA			EV/Sales		
							FTM	FY1	FY2	FTM	FY1	FY2	FTM	FY1	FY2	FTM	FY1	FY2
Aecon Group	ARE	\$9.54	51.1	\$86	\$487	\$1.69	\$1.09	\$1.20	\$0.95	8.8x	8.0x	10.0x	3.6x	3.1x	3.4x	N.A	0.2x	0.2x
Seacliff Construction	SDC	\$6.90	21.8	\$99	\$150	\$4.53	\$1.27	\$1.17	\$1.01	5.4x	5.9x	6.8x	1.2x	1.4x	1.8x	N.A	0.1x	0.1x
Churchill Corp.	CUQ	\$8.35	18.2	\$69	\$152	\$3.79	\$1.98	\$1.79	\$1.20	4.2x	4.7x	7.0x	1.5x	1.7x	2.5x	N.A	0.1x	0.1x
Canam Group	CAM	\$6.34	49.4	-\$79	\$313	-\$1.61	\$0.85	\$0.77	\$0.76	7.5x	8.2x	8.3x	4.4x	5.3x	5.3x	0.5x	0.5x	0.6x
ADF Group	DRX	\$1.72	37.10	\$2	\$64	\$0.05	\$0.35	\$0.47	\$0.39	4.9x	3.7x	4.4x	2.8x	2.3x	2.6x	0.7x	0.6x	0.7x
<b>Average</b>										<b>6.2x</b>	<b>6.1x</b>	<b>7.3x</b>	<b>2.7x</b>	<b>2.8x</b>	<b>3.1x</b>	<b>0.6x</b>	<b>0.3x</b>	<b>0.3x</b>

Source: Thomson, Bloomberg, Union Securities

Historically, the large cap E&C names have traded between 17x – 19x and the small cap E&C stocks in the 14x – 17x range. With overall market multiples having compressed, we do not believe there will a rapid reversion to historical levels, but the steeper discount at which the small cap E&C companies are trading (53% vs. 33% for large cap E&C) suggests small cap E&C stocks could outperform large cap E&C names when market sentiment improves. We also looked at Industrial Products companies in the small cap segment that we believe are leveraged to infrastructure. They are trading between 13x and 16x excluding one outlier (PUR) at 20x – 29x. Historically, these companies have traded between 19x – 24x. The higher multiple for Industrial Products companies is likely on account of higher margins, less lumpy revenues and higher longer-term growth outlook.

#### Exhibit 20. Small Cap Industrial Products – Canada

Company	Ticker	Share	Shares	Net	Market	Net	EPS			Price/Earnings			EV/EBITDA			EV/Sales		
		Price					Cash /	FTM	FY1	FY2	FTM	FY1	FY2	FTM	FY1	FY2	FTM	FY1
		18-Feb-09	(MM)	Cash (MM)	\$MM	Share												
ZCL Composites	ZCL	\$4.60	26.1	-\$9	\$120	-\$0.33	N.A	\$0.48	\$0.53	N.A	9.6x	8.7x	N.A	5.7x	5.2x	N.A	0.9x	0.9x
Pure Technologies	PUR	\$3.55	32.6	\$18	\$116	\$0.54	N.A	\$0.12	\$0.18	N.A	29.6x	19.7x	N.A	20.1x	12.3x	N.A	3.4x	2.6x
Waterfurnace Renewable Energy	WFI	\$28.54	12.1	\$8	\$345	\$0.65	\$1.28	\$1.29	\$1.55	22.3x	22.1x	18.4x	13.4x	13.7x	11.4x	2.4x	2.4x	2.1x
Hammond Power Solutions	HPS/A	\$6.89	11.9	-\$10	\$82	-\$0.82	N.A	N.A	N.A	N.A	N.A	N.A	N.A	N.A	N.A	N.A	N.A	N.A
Rocky Mountain Dealership	RME	\$5.00	69.50	\$18	\$348	\$0.26	\$0.96	\$0.96	\$1.13	5.2x	5.2x	4.4x	11.3x	10.7x	10.4x	0.7x	0.7x	0.7x
<b>Average</b>											<b>13.8x</b>	<b>16.6x</b>	<b>12.8x</b>	<b>12.4x</b>	<b>12.6x</b>	<b>9.8x</b>	<b>1.6x</b>	<b>1.8x</b>

Source: Thomson, Bloomberg, Union Securities

In conclusion, we believe that Infrastructure has the potential to be a multi-year investment theme and is an asset class within the broader stock market that offers diversification and potential for growth. Although large cap infrastructure stocks in Canada appear to be pricing in the positive impact from the impending stimulus spending, they are still well off their historical trading ranges with small cap infrastructure stocks trading at a steep discount to historical levels. We believe, for investors with a medium-term horizon (> 1 year), and the capacity to withstand volatility, small cap infrastructure stocks could provide solid returns in the medium-term.



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