

# Chapter 3: Construction Businesses

This major group includes special trade contractors who undertake activities of a type that are specialized either to building construction, including work on mobile homes, or to both building and nonbuilding projects.

## General Indicators

1.25 to 2.5 times EBITDA

**Common Industry Multipliers** 

- Seasonality of revenues and employees
- Worker’s compensation claims and premiums increasing
- Industry typically follows a 6 year cycle and should be reflected in projections, so as to show upswings and downswings in revenue

**Trends**

- Key employee departing with the contractor’s license
- Key employees departing and leaving no labor in place
- Rising costs of materials

**Red Flags** 

## Plumbing and Heating/Air Conditioning Contractors

**SIC: 1711 NAICS: 238220**

This group includes contractors whose operations are primarily plumbing, heating/air conditioning, and related electrical work. Light sheet metal work associated with the installation of the equipment is included in this category.

**Description of Business**

This industry is the largest among specialized contractors, with 198,199 establishments on record during 2002. A typical business has fewer than 10 employees, yet there are leaders in the industry that employ high numbers and control a

**General Industry Information**

significant share of the business. Anjou International and American Residential Service Inc. are the largest Plumbing, HVAC (Heating, Ventilation/Air-conditioning) business.

Heating and plumbing trades provide installation work for new construction projects, including the construction of detached single family homes. Repair work to existing heating and plumbing systems is less cyclical than new installation business, which is generally a function of construction activity. Factors such as severe climates (freezing/breaking of pipes), aging buildings, and general maintenance ensure steady demand for these contractors.

Operation of a plumbing and heat/air conditioner contracting business is sensitive to increases in equipment and labor cost. The largest expenses are typically materials and tools, followed by labor and then subcontractings. Light electrical and sheet metal work typically accompanies HVAC installation.

**Financial Performance Ratios**

**Table 3-1: Plumbing and Heating/AC Contractors**

Margins	
Cost of Goods (% of revenue)	+/- 55%
Manager/Owner Salary (% of revenue)	15-20%
Operating Expenses (% of revenue)	40-45%
EBITDA/Operating Margin (% of revenue)	1-5%
Ratios	
Working Capital (% of revenue)*	2-10%
Current Ratio	+/- 1.25
Quick Ratio	+/- 0.55
Accounts Receivable Turnover (per year)	> 30 times
<i>*working capital ratios are typically higher for larger companies</i>	



**Business Valuation Formulas**

*Heating and Air Conditioning*  
 20-35% of annual revenues, plus tools and inventory  
 1.5 to 2 times ODCF, plus tools and inventory  
*Plumbing*  
 20-25% of annual revenues, plus inventory and tools  
 1 to 2 times ODCF, plus inventory and tools



**Equipment Valuation and Real Estate Rental Formulas**

*Equipment:*  
 OLV is typically 15-20% of retail value, depending upon condition.  
*Real Estate:*  
 Rent as a % of Sales: typically 2-3% in rural locations and can be higher in urban locations. The typical square footage leased is generally between 5,700 sq ft and 17,500 sq ft, with a median of 10,000 sq ft. The typical lease is a gross expense lease.