Construction Trade Convergence

New Trends require re-thinking Business Models

The trend towards energy efficiency, “green building” solutions, renovation or value-added services, induces that previously distinct construction trades and value chain structures are beginning to converge. Established construction companies, material suppliers or technical building equipment providers: Who will win the race to gain most of future market share? Is it time now for forward looking entrepreneurs to start innovating their business to outcompete their peers?

Trade & value chain convergence

Arthur D. Little distinguishes several key drivers stimulating trade convergence in the construction industry, thereby forcing construction industry majors to rethink their business models.

Increasing interrelation of construction technologies and materials: Achieving energy efficiency and green building standards requires integrated solutions to optimize the interplay between structures, facades, interior finishing and technical building. Rising demand for smart home systems and building automation will also lead to an increased need to reduce complexity and to integrate traditionally separated trades. New, intelligent materials and modular construction systems influence construction methods and necessitate the need to upgrade technological and construction expertise.

Mastering (renovation) complexity: More than sixty percent of the money spent in the construction industry, i.e. approx. 180 bn EURO in Germany, is within the renovation sector. However, very few players strategically address this segment with a distinct skillset and solution portfolio. The opportunity to meet specific market and customer requirements such as improving sustainability, fulfilling legal regulations or increasing rental value and flexibility of usage, offers the chance for established as well as new players to capitalize (Figure 1).

Eighty percent of the cost of a renovation project is determined in the early phases. Only players who master alternative management techniques will have a high process orientation along the value chain. Forward thinking cost control and a structured approach to quality and risk management will deliver both high customer value and profitable renovation projects.

Required success factors and competencies

Forward thinking entrepreneurs are aware that minor changes will not be enough to make a real impact to address these trends. An innovative revision of the whole formula is required to meet future market demand. Only those companies which establish new
Achieving the transition

Only a few companies have successfully capitalized on the potential of evolving market segments and managed to build up a clear competitive advantage. Addressing new market needs, or entering new adjacent market segments, can present a number of obstacles.

Over the last decade, companies have understood that constant renewal is a critical success factor to stay ahead of competition. They have improved their activities mainly in the areas of product, technologies or channel innovation. However, most companies do not go beyond this stage thereby leaving value proposition, business model or value chain positioning untouched.

Tapping into new business fields requires adjustments to structures and processes. This is in contrast to the widely observed phenomenon that business leaders are hesitant towards changing formal and informal structures or establishing new businesses around valued individuals. These boundaries prevent companies from setting up an optimum greenfield business approach.

Moreover, entering new market segments is characterized by an evolving and often not tightly managed process. A structured and agile approach addressing all relevant issues will save time and costs and guarantee a successful market launch. Once a decision has been made, rigorous execution with room for necessary adjustments needs to follow.

Taking an integrated approach

A compelling explanation as to why one company succeeds in establishing a thriving new business, can be put in a simple formula: The ability to accomplish the interplay between a sound value proposition, the right positioning on the value chain and the optimal design of a supporting business model to best serve the targeted customer group (Figure 2).

(1) Sound value proposition

Align your value proposition with your mission, goals and strategy. Understand what constitutes value in the mind of your target customers and communicate the benefits of your value proposition effectively.

Providing a superior technological solution, solving customer problems in a unique, innovative way or uncovering and addressing unmet customer needs are examples of substantial reasons why a customer should buy your service or product.

(2) Positioning on the value chain

Moving up or downstream or complementing value chain steps determines your positioning, offering, portfolio and required competencies. Appropriate positioning on the value chain can enable you to deliver the best value to your target customer group.

(3) Business model

Design your business model in line with your chosen value proposition. Arthur D. Little’s business model approach focuses on three key areas: how to create, deliver and capture value and their interrelation.

- Value Creation: Decisions need to be made about which competencies/resources are key to create value, whether they are of strategic or operational importance and whether they need to be owned or sourced. Furthermore, define how you want to design, manage and operationalize your value network. For example, by complementing your own expertise with specialized technology partners or additional external functional expertise.

- Value Delivery: The most effective go-to-market strategy, channel selection and desired customer relations mechanisms need to be determined. There should be particular focus on evolving channel conflicts for example when complementing an indirect with a direct customer approach. Design your customer interaction according to their requirements, for instance, transactional versus solution-driven.
Case study: Successful transformation into the renovation segment

A leading construction company leveraged its position by successfully expanding into the renovation market. Key success factors were capturing additional value chain steps, integrating partners for energy efficient renovation and retrofitting and structuring the new business in a separate organization (see Figure 3).

Successful transformation

Arthur D. Little recommends a four step approach to transform and capture the new opportunities of the dynamic construction market (Figure 4 overleaf).

Step 1 – Set the basis: Gain insight into future developments, trends and drivers. Analyze customer and market requirements and unmet needs along the value chain as a basis to define the future value proposition and positioning, in order to stay ahead of competition.

Step 2 – Understand competitive environment: Uncover dynamics within the competitive environment by analyzing established players and potential entrants. Gain understanding of your own strengths and limitations. Develop first ideas addressing white spots and closing gaps.
Step 3 – Design the business: Define your own future ambition and positioning for the new target market segment. Derive a winning strategy by formulating a compelling value proposition addressing the needs of the target customer groups, determining the required positioning on the value chain and shaping your business model.

Step 4 – Operationalize the business model: Finally, an evaluation of the feasibility and impact of the selected business model under consideration of risk and transformation need is recommended. Special focus should be given to identifying gaps between required and already existing competencies, structures and resources. Make strategic decisions to solve potential conflicts, for example the chosen model approach and concerns about existing and new businesses.

Conclusion

The trend towards energy efficiency, “green building” solutions, renovation or value-added services, offers growth potential for construction industry players. However, new entrants such as material suppliers and technical building equipment players have also shown interest in this new market segment. As a result, the previously distinct construction trades and value chain structures are beginning to converge and only those companies which effectively address the market needs with cost effective and all-embracing solutions will win the race to capture future market share.

Our analysis and experience shows that numerous companies are looking to address these issues but are currently showing a half-hearted approach. Arthur D. Little provides answers for your business and can help you design a winning strategy.

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