Business Capability Modeling: Theory & Practice

Leonard Greski
Topics

● Theory
  ● Business capabilities defined
  ● Why business capabilities are useful
  ● Characteristics of business capabilities
  ● Role of business capabilities in strategy to results process

● Practice
  ● Modeling capabilities in four easy steps
  ● Using the model to make decisions
  ● Common questions

● Q&A
What is a “business capability?”

An ability or capacity a business has to deliver value to customers and / or shareholders.

A set of related business processes, people, and physical assets that deliver value directly to customers, or are needed to run the business.
Two Types of Capabilities

Customer-Facing
Capabilities that deliver value directly to external customers

Operational
Capabilities that deliver value to shareholders, or are needed to operate the business
Characteristics of Business Capabilities

- More detailed than strategy elements; less detailed than business processes
- Hierarchical: capabilities can be represented at multiple levels of abstraction
- Illustrate relationships between people, processes, and physical assets
- Managed as assets

**Bottom Line:** Capabilities allow companies to create sustainable competitive advantage through unique combinations of people, processes, and physical assets
Uses for Business Capabilities

- Visualize consequences of strategy
  - Impact to existing capabilities
  - Missing capabilities
  - Capabilities no longer needed
- Manage ongoing operation of a capability
  - Evaluate impact of changes in planning assumptions on costs & benefits
  - Forecast investments in increased capacity
- Support merger & acquisition activity
  - Evaluate capabilities of acquisition target(s)
  - Identify integration synergies
  - Identify capabilities to be lost through divestiture
- Manage investments across the portfolio of capabilities
Capabilities in Context: Strategy to Results

- **Environment**: Influences Strategy
- **Business Capabilities**: Creates needs for Business Capabilities
- **Results**: Measured by Business Capabilities
  - Affects Results
  - Generate Results
Strategy to Future Business Model

Business Strategy → Operating Model → Required Business Capabilities

Planning Scenarios (3 – 5 year horizon) → Physical Assets

Future Business Model
- Results
- People
- Processes
Topics

- **Theory**
  - Business capabilities defined
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- **Practice**
  - Modeling capabilities in four easy steps
  - Using the model to make decisions
  - Common questions

- **Q&A**
## Four “Easy” Steps

<table>
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<tr>
<th>Step</th>
<th>Deliverable(s)</th>
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| 1. Develop the capability hierarchy | ● Scope statement  
● Capability hierarchy |
| 2. Identify key relationships | ● Association matrices |
| 3. Develop utilization models | ● List of demand sources: what generates utilization?  
● Utilization model over time |
| 4. Develop financial models | ● Sources of benefits  
● Sources of cost  
● Cash flow statement |
Develop the Hierarchy

- Internet Retailer
  - Online Store
    - Direct Sales
    - Third Party / Reseller Sales
  - Electronic Media Reader
  - Fulfillment
  - Web Services
    - Payment Services
    - Merchant Services
    - Workforce Services
Hierarchy: tips

- Engage your business partner(s) to identify starting scope
- Focus on breadth, not depth
  - 3 – 5 levels of hierarchy is sufficient
  - A capability should have more than one supporting process
- Start with customer-facing capabilities
- Make sure the team can explain how the capability generates value / benefits
- Use business partners’ language to describe elements in the hierarchy
Identify Relationships

- Document relationships between capabilities and
  - Strategy elements
  - Organization units
  - Business processes
  - Physical assets
  - People (roles)
Relationships: tips

- Use association matrices to find inconsistencies in the capability model
  - Capabilities not connected to strategy elements
  - Strategy elements with no capabilities
- Use numbers to measure strength of relationship where appropriate
Create Utilization Model

- Identify sources of demand
- Map demand to business process utilization
- Map demand to physical asset utilization
- Develop forecasting assumptions
- Forecast utilization into the future
Utilization Model: tips

- Use assumptions to discover stakeholder expectations about operation of capabilities
- The utilization model can alert the team to parts of a capability that won’t scale with growth
  - Business processes
  - Physical assets
Create Financial Model

- Identify quantifiable sources of benefits
- Identify sources of cost
- Create statement of cash flows
Financial Model: tips

- The financial model helps your stakeholders explain how a capability converts benefits into cash.

- Organizations frequently fail to account for process/labor costs to operate a capability, artificially inflating the returns on projects.
Defining Success

- Models help stakeholders see non-obvious patterns, assess impact of change
- Models allow stakeholders to perform “what if” analysis for different business scenarios
- Utilization and financial models focus stakeholders attention on:
  - Quantifiable benefits
  - Ongoing operation of capabilities
Capabilities & Process Management

- Capabilities are the “missing link” in the strategy to results abstraction chain.
- A single process may map to multiple capabilities, each having unique or conflicting requirements.
- Demand and financial models provide top-down ways to evaluate effectiveness & efficiency of processes.
Questions & Answers

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References

Architecture & Governance Magazine Articles

*Business Capability Modeling: Theory & Practice*

*Business Capability Modeling: Building the Hierarchy*

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