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Johnson Beverage, Inc. Case

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Strategic Business Dilemma Related to Customer Profitability:

Johnson Beverage's profitability chart underscores a strategic conundrum: the distribution of profitability is highly uneven among its top 20 customers. The dilemma centers on whether to continue servicing low to negative margin customers, who may offer volume but erode profitability, or to recalibrate the company's focus towards nurturing relationships with those yielding higher margins. The opportunity cost of servicing less profitable customers must be evaluated against potential gains from reallocating resources towards more lucrative accounts. It necessitates a strategic pivot towards a customer-centric profitability model, potentially revamping the customer portfolio to shed unprofitable accounts or renegotiate terms to elevate their profit contributions.

Impact of Costing Customer Costs by Activities:

Transitioning to an activity-based costing model presents a paradigm shift in customer negotiations. The granular view of profitability indicates that the cost-to-serve varies significantly across customers. For Johnson's 20 customers, negotiations can now be informed by the actual cost of servicing each account. High-maintenance, low-profit customers could be approached with data-driven justifications for price adjustments or service level modifications. Conversely, high-profit customers provide leverage to explore value-added services, reinforcing customer loyalty and potentially unlocking additional revenue streams.

Allocation Death Spiral and Its Effect:

The allocation death spiral poses a substantial risk to the sustainability of Johnson Beverage's customer portfolio. As depicted in the chart, the negative profitability of certain customers, if not addressed, could lead to a scenario where increasing costs are transferred to profitable customers, potentially prompting their attrition. This necessitates a strategic review of the cost allocation model, ensuring that profitable customers are not subsidizing the less profitable ones. It's imperative that Johnson Beverage avoids a reactionary cost allocation approach in response to customer negotiations and instead adopts a proactive stance that safeguards against the erosion of its customer base.