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MEASURING AND MANAGEMENT CUSTOMER PROFITABILITY IN WIND INDUSTRY

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Abstract: *The only value that an organization will ever create for its stakeholders is the value associated with customers or comes from its customers, both the existing clients as well as the ones acquired in the near future. To remain competitive, the organizations must determine ways to keep their clients for longer, grow them into more significant customers while making them more profitable. This research paper will focus on ways such organizations can gain more focus on their customers. Indeed, some high demanding clients might not be profitable, but the challenge is that many organizations have no means of reporting the customer profitability analysis to support this rationale. The organizations' lack the proper and consistent managerial accounting structures can make available more reports on the 65 customer's profitability, and this becomes more challenging because the organizations have no way of making verification of the profitable and unprofitable customers. The research explains how an organization can use activity-based accounting to trace the source of the consumption of the company expenses. ABC enhances accuracy since it employs several phrases to track as well as segment all the resources expenditures as calculated costs through a system assignment of the costs into the value of the closing objects.*

Keywords: *customers, profitability, organisation, activity-based accounting, chief finance officer, profits, wind industry.*

COMPANY COMPETITIVENESS

Companies are obliged to create value for their owners and shareholders in the form of value offered to current customers and to prospective ones. Therefore, the determination of the best way to maintain customers, development of the customers into more profitability, serving them more competitively and acquisition of more profitable customers will secure a company's competitiveness (Hegner-Kakar et al., 2018). However, a challenge is posed by customers who are increasingly modifying their perception of the suppliers' goods and services.

Customers' standard lines of service and products are from the customers' perception considered as merchandises. This signifies that customers must focus and distinguish deals, price discounts, offers, and services presented to current clientele to realize success in growing and retaining them. This differentiation will assist in the acquisition of new customers based on the similarities with their relatively more profitable customers and thereby replace the traditional mentality that all customers are valuable. Therefore, organizations need to change their focus from product-based to customer-based (Hegner-Kakar, Richter, & Ringle, 2018). However, the majority of companies lack reliable managerial accounting systems that can provide reports on client profitability which poses challenges in the verification of profitable from unprofitable customers. Increasingly, it is becoming more challenging in identifying which customers to win back, grow, retain or criteria for acquisition of valuable customers.

With the change in focus from product-based to customer-based, business managers are seeking more information on customers and intangibles like customer loyalty. Even though marketing and sales units have suspicions over the existence of profitable and unprofitable customers, they lack the necessary evidence to support their intuition (Hegner-Kakar et al., 2018). It is the management accountants who have access to such evidence and avail it to marketing and sales. Still, the former is reluctant in reforming their measurement systems and practices, hence, unable to assist the latter. Furthermore, the sales force is motivated based on the revenues generated rather than from profitable sales. This should not be the case as it leads a company into valuing growth in sales and increased market share. Therefore, the adoption of a compensation model that combines profits and customer sales volume is highly recommendable.

There is a general challenge in differentiating the troublesome customers and the number of profit margins they drain from a company. The traditional accounting methodologies are partially responsible as they report on the product gross profit margin. The conventional reporting prevents managers from having a visual of the most significant and critical "bottom half" of the entire income statement (Hegner-Kakar et al., 2018). The

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methodologies mask profit margin layers that are not visible in the reports on customer-based costs like marketing costs, credit, customer service, selling, and the distribution channel. Moreover, esteemed customers cannot be identified by the traditional accounting methodologies, which fail to differentiate a profitable customer from an esteemed one (Hegner-Kakar et al., 2018). Nevertheless, the most significant aspect is the establishment of measures that can assess these customer-related attributes to enable the managers to set corrective actions that might increase a company's profitability from individual customers.

2. PROFITABLE VS UNPROFITABLE CUSTOMERS

When there is the addition of non-product related costs to serve customers who buy products of low-profit margin without considering the associated standard service lines and costs of product mix they buy, a company can find these customers as non-profit generating. On the contrary, customers who insist on additional services after purchasing product mix of high-profit margin are possibly non-profit generating. The presence of profitable and non-profitable customers in every organization is undeniable (Plowman, 2017). For instance, low-maintenance "profitable" customers simply make purchases without commotion, whereas high-maintenance "non-profitable" customers typically insist on outstanding services and price discounts as well as special delivery arrangements. The high-maintenance customers regularly contact the company's customer service or return goods while the low-maintenance customer contacts the seller on genuine cases of product fault which rarely occur.

There is an accumulation of the additional costs for the maintenance of non-profitable customers. Nevertheless, after the evaluation of the profitability levels for all categories of customers, "profit margin management" methodologies can be applied to shift them all towards increased profitability. From a study on the application of administrative and selling costs to a product, producers had higher chances to undergo losses as a result of failure to manage administrative and marketing costs even after addition of all the factory finances in their entirety (Ballings, McCullough, & Bharadwaj, 2018). Ideally, the principles applied in costing should be replicate in managing the administrative and selling cost of production; a company may fail to capture benefits of competent low-cost production.

3. ADDRESSING PROFITABILITY AND COMPETITIVENESS

In learning about customer profitability levels, an organization can address more direct aspects that are critical in the realization of increased profit margins from individual customers or groups of customers sharing the same attributes (Ballings et al., 2018). Therefore, the company must be in a position to tackle questions like:

- Is there a possibility of shifting work from or to customers based on who has reduced process costs?
- Should the company push for margin or volume when handling particular customers?
- Can the organization induce their customers to modify their habits to interact more profitably with the organization?
- Does the customers' sales volume warrant the offers, promotion, or rebates framework offered to them?
- Is there a possibility of improving profitability through modification of the packages, delivery, sale, or customer service?

A good comprehension of a company's source of turnover, cost structure, and cost is mandatory to establish its competitiveness. Such information can guide the actions relevant to enhance profitability. An example is the exploration of passive options of charging for the additional services rendered or raising the charges progressively to send the high-maintenance customers to the competitor (Ballings et al., 2018). Otherwise, the company might contemplate on the reduction of additional activities for its workforce when attending to low-maintenance customers through modifying customers' habits with incentives that will enable the customers to initiate less demand on the company. Besides, the company can restructure its process of delivery and subsequently reduce its employee's workload in attending to profitable customers.

4. ACTIVITY-BASED COSTING (ABC)

The ABC is a management accounting method that allows a company to track the utilization of its resource expenses precisely using an economic model. Through ABC, the company can trace its resource expenses to products and service lines and to the variety of channels and customer categories that add varying amounts of workload demand on the workforce. With ABC, companies should do away with the tendency of failing to assign non-traceable cost to their sources (Kumar & Reinartz, 2016). The system enables increased precision when reporting as it complies with the causality principle for cost utilization correlations. The enhanced accuracy is due to the ABC system employing several phases to track and segment all the resource expenses as computed costs through a network of assignment of the costs into the final objects cost. In companies with complex and intensive support, complicated customer can precede a chain of direct activities into the costs of the final objects (Ballings et al., 2018). The sequences cause activity-to-activity expense assignments that depend upon intermediate activities expense drivers tracked to consuming activities similar to the final cost objects that depend upon activities cost drivers to reallocate the activity costs into final expense objects according to their differences and range.

With the ABC software, the challenge of converting indirect costs into direct costs is resolved as the integrated software permits intermediate direct costing to a native procedure. Moreover, the software permits the tracking of the cost amidst the final objects' costs. Eventually, the integrated software reallocates 100 per cent of the resource expenses into the ultimate accrued cost of customers, products, channels, service lines, as well as supporting business work (Ballings et al., 2018).

Within the cost assignment network, there is a ubiquitous prominence of cost, inclusive of the manner that expenses are propelled by cost activity drivers that comply with the correlation of cause and effect. The distinction of expenditures assists in the identification of focal areas for improvement.

Figure 1 illustrates the cost assignment network that comprises of modules linked by paths of cost assignment. The paths indicate the amount of costs passing through. With the ABC software, the paths to cost assignment track the costs from their source to their destination. From the illustration, resources offer the existing capabilities to conduct work. Hence, resource costs may originate from the company's coffers as employee payroll and procurement purchases (Ballings et al., 2018). At this phase, where money exits the accounting in the form of electrical power, operating salaries, or remuneration. The drivers of resource costs are ascertained and evaluated as a measure of changing resource costs into activity costs. Tracking or assignment of resource costs equates to the time that equipment or people devote to performing work activities.

From the illustration in Fig. 1, customers can be ascertained as the source of the costs by reversing the path arrowheads from bottom up. The revelation from the switch of the polar opposite is that all expenses arise from the customer's demand-pull and the computed cost assess the impact in the reverse direction (Ballings et al., 2018). Notably, the resources placed up in the network of cost assignments offer the available capabilities to perform activities. The company's chequebook is the source of resource costs in the form of employee salaries and procurement purchases.

Employees are considered as assets as they perform work, converting resource into output in the module of work activities. The activity cost drivers are the measures taken to achieve the desired outcome from this project (Ballings et al., 2018). For instance, the number of pregnancy tests conducted in a hospital, or the quantity of inventory collected in a warehouse, or even the number of bank accounts opened. An additional benefit of the ABC software is the unit-level expense utilization rates, which are critical benchmarking studies comparatively and for the forecasting of costs and

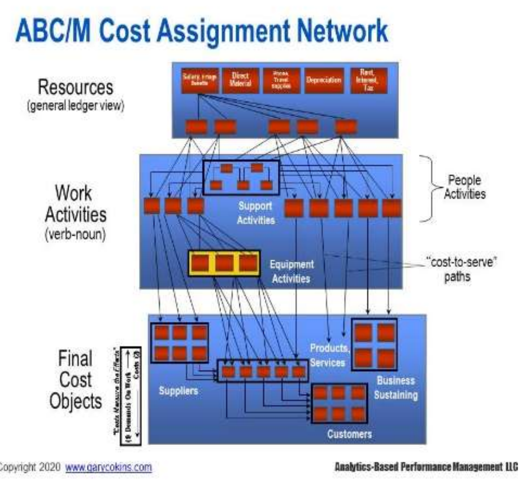

Fig. 1. ABC Cost Assignment Network.

expenses in the future. Examples of the costs and expenses comprise outsourcing decisions, what-if scenario analysis, and rolling financial projections (Ballings et al., 2018).

For projecting future costs and expenses, predictive accounting could include a different element to management accounting comprising the categorization of resource capacity costs. The resource capacity costs are categorized as variable, step-fixed, fixed, or sunk relative to modifications, dependent on the type of decision and the length of time taken in the planning horizon.

At the bottom of the cost, network assignment is the final objects cost that is representative of the full diversity of services and outputs where cost ultimately accrue. Customers initiate the necessity for the supply of resource costs as they are the final cost objects. The total final cost is represented by the "for whom or the what" that do work activities (Kumar & Reinartz, 2016). Cost of capital drivers comprises a customer's days' sales outstanding, or a normal inventory level of a product. The cost of capital drivers can track balance sheet items like customer receivables or inventories when advanced costing models are employed.

Nevertheless, there are activities within companies that do not add to the quality, responsiveness, and customer value directly (Plowman, 2017). The implication of such activities is magnanimous as they cannot be decreased or eliminated without causing damage to the company. A case scenario is the preparation of regulatory reports that contribute nothing to customer satisfaction or the addition of product value. However, the development of such a statement is invaluable to a company as it offers a legal mandate to conduct commerce. Such activities costs are referred to as business sustaining costs as they are the sustaining cost object. These costs should not be allocated to products, service lines or customers because they do not cause them to be incurred. Example of a business sustaining cost objects are senior management who require reports or government regulatory agencies who establish requirements to comply with.

There is no association between business sustaining costs with the provision of customer services or product delivery, yet the costs are inclusive with the profits for the entire organization. They still must be recovered with prices and revenues for the company to be profitable.

The architecture and design of a cost network assignment are the foundation of a proficient ABC system. The destinations and sources in the network are the "nodes" through which computed costs reallocate all the cost. The nodes within the network deliver the value and utility of the data necessary for making decisions.

5. THE PROFIT CLIFF AND UNREALIZED PROFITS

The profit cliff represented in Fig. 2 is the accumulation of individual customer's profit. In the graph, also known as the "humpback whale" curve based on its shape, there is the categorization of customers starting with the low-maintenance to the high-maintenance. The sorting includes customers whose costs surpass their income and are thereby a financial obligation to the company as they are unprofitable (Kumar & Reinartz, 2016). Within the "humpback whale" curve, the organization's total profit and loss statement reconcile with the last data point.

The representation depicts how a reasonable portion of the company's profits is not is masked as unrealized profits hidden due to inadequate costing under the gross profit margin line of the product. Besides, the majority of managers believe that the curve would be considerably horizontal. The flat-curve belief originates from crushing the cost accuracy by the broad averaging of ancient cost allocation of non-causal overheads (Kumar & Reinartz, 2016). The ABC software is efficient n the detection of distinct differences of the final objects cost utilization of the work activities and their associated resource costs for the provision of capacity. The information from the ABC system has a stunning effect on managers and executives because of the general assumption that majority of their customers are profitable contrary to the actual presence of massive profit-takers as well as profit makers.

The unrealized profits can as well be hidden due to allocation techniques of incomplete current costs. The ABC provides a profit and loss statement for each customer together with categories of similar customers. Several organizations depict the same trend displayed by the profit cliff (Plowman, 2017). The pattern exhibited by the graph illustrates that, from right to left, the organization makes a remarkable profit from a small section of the customers, a few lead to a breakeven point, and the remainder consumes the profits gained.

6. CUSTOMER LIFETIME VALUE (CLV)

Most business-to-customer organizations have customers that undergo a life cycle path. Examples of such organizations are telecommunication and banking industries where there is a significant distinction between customers who are potentially profitable in the future and those that are profitable presently. This variation swings the focus from the present profit margins to future expected profit margins (Plowman, 2017). Accountants from these business-to-customer organizations can efficiently compute individual customer's customer lifetime value prior and after different marketing efforts and targeted deals and offers. Therefore, the marketing and sales units can evaluate which customers have the potential to attain increased profitability from activities.

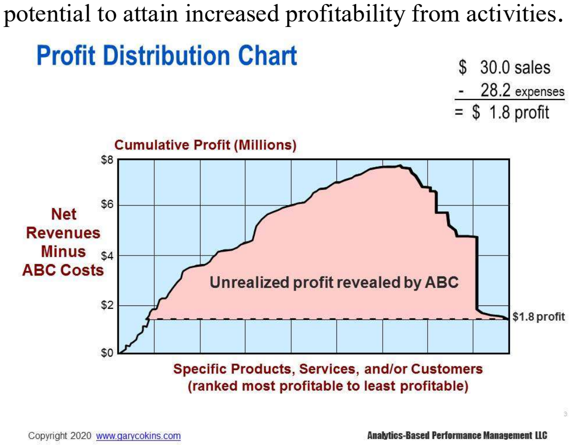

Fig. 2. Profit cliff.

7. SHIFTING CUSTOMERS TO HIGHER PROFITABILITY

Employment of the ABC software in the computation of valid customer profitability information obtained the data on transactions between the company, and the customer is not the main challenge but the integration and wise application of the information (Kumar & Reinartz, 2016). The advantage is realized from the identification of profit-lift possibilities from customers and then identifying the potential with smart actions and decisions.

Figure 3 demonstrates two tiers of a "costed" utilization chain of cost in the bottom final objects cost component. The picture disintegrates the final objects cost represented in ABC cost network assignment (Fig. 1). Ultimately, the final objects cost indicate the customer utilizing the entire final objects cost leaving behind the costs of sustaining the business only (Kumar & Reinartz, 2016). From the illustration, each of the final objects cost classes such as customer, service line, and supplier has an independent cost of sustenance. These sustaining costs can be assigned to the end-user or end product employing an object cost driver to mirror the various utilization correlations.

The left to right chain of cost drivers' activities generates layers of profit margin, which creates a provision for an authentic profit and loss statement for individual customers together with groupings of customers or logical divisions. The personal customer statement of profitability as represented in Fig. 4. The ABC profit and loss statement provide managers with the ability to evaluate separate service lines and products bought in profound detail. The details encompass the mixture of low and high-profit margin product procurements, as per their prices and unit costs. Moreover, the managers can as well mine data concerning the profit margins of the product mix for more clarity. The user can also assess the cost of the work activities, content, and materials for individual service line and products (Kumar & Reinartz, 2016). The revelation that all customers are not profitable is evident with their profit margins minus the sales volume. Thus, the profit and loss quantify the suspicions of the employees.

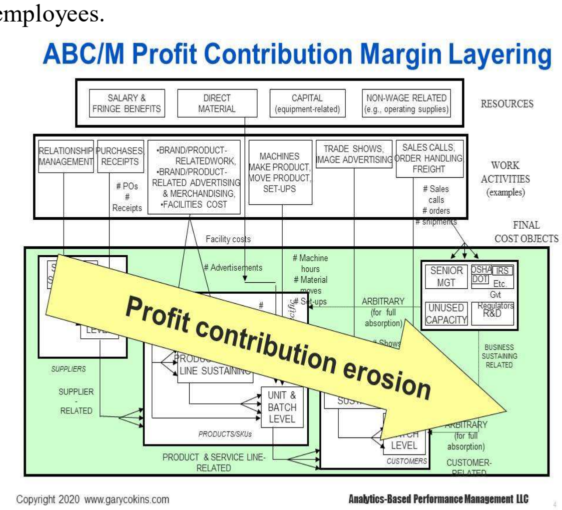

Fig. 3. Profit Contributing Margin Layering.

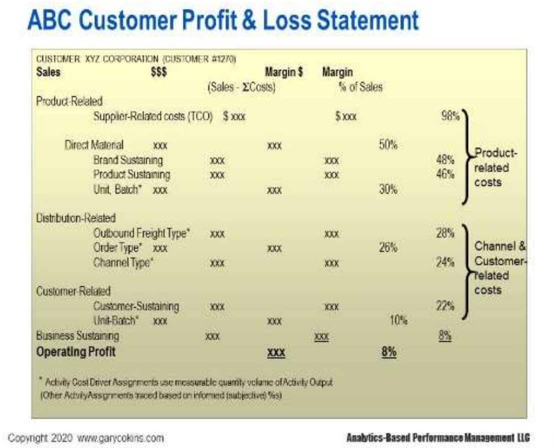

Fig. 4. Customer Profit and Loss Statement.

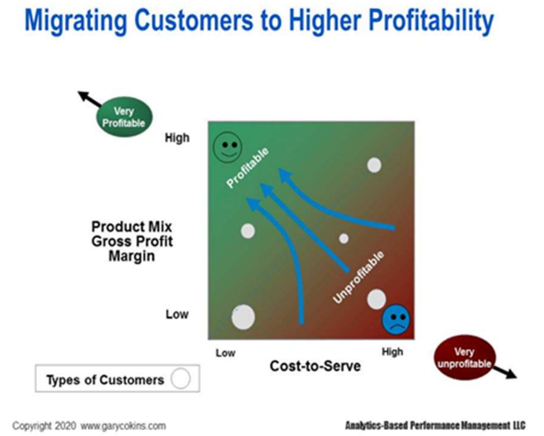

Fig. 5. Shifting Customers to Advanced Profitability.

As much as the loyalty and satisfaction of the customers are significant to the organization, the increase in corporate profitability is a long-term goal. The long-term goal aims at increasing the turnover for the shareholders through increments in customer profits. There is an increase in customer profits as if individual customers are an asset in a stock portfolio (Kumar & Reinartz, 2016). The perception aims at the purpose of actions taken to intensify the return on customer finance. It is critical that a balance between managing the spending and the level of customer service necessary to gain customer loyalty and the effect of the actions on the shareholders' wealth. The profit and loss statements of any organization consist of two primary "coatings" of the profit margin:

- The service lines and product mix bought
- The costs associated with serving the customer different from the rare combination of service lines and products. The costs to serve are visible in the lower part of the illustration.

The "coatings" of the profit margins combine in Fig. 5 where the first axis grid depicts the composite profit margin of a product that individual customers buy with a reflection of the net prices to the customers. The second axis grid reflects the costs required to serve the customers. For each group of customers with resembling attributes or individual customers, there is an intersection that reflects the customers' revenues. The figure discredits the belief that customers generating high-profit margins are those with the highest sales volume. A company aims to produce additional turnover from all customers (Kumar & Reinartz, 2016). From the illustration, the company will achieve its aim by shifting customers to the upper-left corner. Achievement of this shift is possible can be attained through cross-selling, upselling, and surcharging.

Generally, the application of the ABC software can assist the marketing and finance units in collaborating and establishing "next-best-offer recommendations" founded on a market analysis of service or product dealings. The examination employs rules of association that detect products that repeatedly trail other products in data-based transactions (Kumar & Reinartz, 2016). For instance, when a customer purchases product C and D, they are likely to purchase product E. With such insight, organizations can suggest offers to customers who have acquired product C and D.

Shifting customers to the upper-left corner of the grid is in real sense transferring specific data points from right to left within the profit cliff. Nevertheless, it is the ABC data that provides knowledge of the customers' location on the graph. All in all, an essential motive for the determination of individual customers' position on the profit cliff is to secure the low-maintenance customers from the competitors (Kumar & Reinartz, 2016). Since fewer customers account for a remarkable percentage of the turnover, then the possibility of losing them is considerable. From Fig. 2, the lengthier the distance to the left side of the "humpback whale" profile distribution curve that the peak is situated, the more vulnerable the bottom line organizational turnover is. The vulnerability is in respect to attacks from competitors winning an organization's primary customers.

8. POSSIBILITIES OF RAISING THE HUMPBACK WHALE CURVE

Evaluation of an organization's customer profit information is relevant as it assists the organization in assessing the actions necessary to increase the profitability of its customers (Kumar & Reinartz, 2016). Hence, profitability can be increased by:

- Reduction of individual customers' costs to serve to minimal levels.
- Establishment of surplus charges or re-pricing expensive costs to service activities.
- Management of services with minimal impact on customers.
- Introduction of standard service lines new products.
- Raising prices that might not be realistic to competitors.
- Abandonment of customers, services, or unprofitable products.
- Improvement of high productivity business processes.
- Provision of discounts to customers with low costs to serve to gain more sales volume.
- Increment of the costs on activities that indicate a bias towards customer preference.

- Cross-selling and up-selling the customer's mix of purchases towards higher-margin service lines and products.
- Provision of customer positive-profit service level choices.

It is critical that during the interpretations of the profit distribution illustrations, the following significant aspects be in simple steps before taking rash actions. The steps can be the cause for poor decisions:

- There are situations where a company decides to deliberately sell at a loss of some products to generate more sales from those valuable goods.
- The overview of the time's expense does not indicate the service lines, product's life cycle costs, or customers that have utilized the resource and costs of activities for that specific time frame. For instance, a launched product may have pending cost reductions as well as decreased sales volumes that will develop during the shake-out phase. Hence, in the oncoming time frame, there will be movement of the product towards the left of the "humpback whale" curve.

9. EXPANSION OF THE OPERATION

There has been increasing alteration of the responsibilities of the chief financial officers (CFO) as strategic consultants to involve participation in operational roles. The function has expanded beyond cost control, governance roles, reporting, and financial accounting for the CFO’s accounting (Kumar & Reinartz, 2016). They can augment the function of the marketing and sales unit by assisting them in targeting the more profitable customers to win back, grow, and retain. With assistance from the CFO's, the marketing and sales units can quickly gain more valuable and beneficial customers.

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