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**PHASE FIVE [NEW00142.GIF](INTRODUCTION.docx)**

**EXERCISE TWELVE-B** House Information

**This exercise should be answered using the Phase 5 Variables Worksheet**

**[](variables5.xlsx)**

**Evaluating the Impact of a Layaway Service**

*The House* carries a number of high priced items such as men’s tuxedos and prom dresses. These items have a very high gross margin and Anne and Fred would like to increase the volume of their sales. Anne asked her sales clerks where the college and high school students get their formalwear for the homecoming dances and spring formals. Anne was told that when the dances occur most students cannot afford to buy their formalwear because of the other costs of the dances. They indicated that most students rent their formalwear from a rental store in Troy which they say is inconvenient and of questionable quality. Over dinner that evening Anne and Fred discussed what they might do to increase the sales of formalwear and meet the needs of the students. Anne thought that much of the problem was that all of the costs of the dances arose at the same time. She suggested that *The House* might reduce this constraint and convince the students to buy their formalwear instead of renting if *The House* implemented a layaway service. She also believed that other customers might utilize the service to spread payments of quality merchandise over time. Anne believed that such a service would increase the average item price by 1% due to the increase in sales of high price items. She also believed the overall product costs would decline by 0.50% for the same reason.

Fred was skeptical of the viability of a layaway service. He pointed out that such a service would require an additional half-time clerk at a cost of $10,000 to keep track of the open layaway accounts. In addition, he pointed out that an increase in focus on formalwear would require an additional shopping trip to purchase the formalwear at a cost of $4,500 and a further investment in inventory of $25,000. Anne pointed out that this additional inventory could be financed out of cash and accounts payable and should not increase total assets.

The Variables Worksheet you will need to run this simulation can be reached by clicking the red “5” above. You will need to enter the changes on the Input Form one at a time. The financial statements and ratios will automatically be updated and shown on the bottom of the input form. You must then copy the revised income statement and ratios to the scenario columns on the Answer Sheet. This process will have to be repeated if there is more than one scenario described in the exercise. Instructions for use of the Variables Worksheet can be reached by

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clicking on the “Help” button at the top right of the worksheet. Be sure to save your work and print a copy once you are satisfied with its correctness. After you complete your simulation there are questions you need to answer. These can be answered by typing your responses below the questions, saving your work, printing a copy, and handing it in to the instructor if required.

**EXERCISE TWELVE-B**

**QUESTIONS**

1. Should Fred and Anne follow through with the layaway service? Why?

1. How might a layaway service impact the other variables in the simulation model*?*
2. How would the use of a layaway service differentiate *The House* from other retailers of clothing? What benefits would *The House* accrue from such service?
3. What risks does *The House* incur if it decides to offer a layaway service?

*uH*