

Chapter 20—Setting the Right Price

TRUE/FALSE

1. The first step in setting the right price for a new product is to estimate demand, costs, and profits.

ANS: F

The first step in setting the right price is to establish pricing goals.

PTS: 1 REF: 319 OBJ: 20-1 TOP: AACSB Reflective Thinking
KEY: CB&E Model Pricing MSC: BLOOMS Knowledge

2. All pricing objectives have trade-offs that managers must weigh.

ANS: T PTS: 1 REF: 319 OBJ: 20-1
TOP: AACSB Reflective Thinking KEY: CB&E Model Pricing
MSC: BLOOMS Comprehension

3. Once he compiles information on pricing objectives, market demand, quantity supplied, and the price elasticity of demand, the owner/operator of a home cleaning service will be ready to determine the optimal price for a new service offering.

ANS: F

He must also collect information or estimates about costs and total revenue at a variety of prices. Only then can he make reasonable estimates about profits and market share.

PTS: 1 REF: 320 OBJ: 20-1 TOP: AACSB Reflective Thinking
KEY: CB&E Model Pricing MSC: BLOOMS Application

4. The manufacturer of Trek Natural sports drink would like to introduce a Trek Natural brand energy drink in the already crowded energy drink category. This company would have a great amount of freedom in choosing a price for its new energy drink.

ANS: F

If a firm brings out a new item similar to a number of others already on the market, its pricing freedom will be restricted.

PTS: 1 REF: 320 OBJ: 20-1 TOP: AACSB Reflective Thinking
KEY: CB&E Model Pricing MSC: BLOOMS Application

5. Penetration pricing is sometimes referred to as a “market-plus” approach to pricing.

ANS: F

Price skimming is sometimes referred to as a “market-plus” approach to pricing.

PTS: 1 REF: 320 OBJ: 20-1 TOP: AACSB Reflective Thinking
KEY: CB&E Model Pricing MSC: BLOOMS Comprehension

6. It makes the most sense to use price skimming as a pricing policy when supply is greater than demand.

ANS: F

It makes the most sense to use price skimming as a pricing policy when demand is greater than supply.

PTS: 1 REF: 321 OBJ: 20-1 TOP: AACSB Reflective Thinking
KEY: CB&E Model Pricing MSC: BLOOMS Comprehension

7. Procter & Gamble entered the electric toothbrush market with the Crest Spinbrush at a price considerably lower than lesser-known competitors. It used penetration to gain market share.

ANS: T PTS: 1 REF: 321 OBJ: 20-1
TOP: AACSB Reflective Thinking KEY: CB&E Model Pricing
MSC: BLOOMS Application

8. One disadvantage of using a penetration pricing policy is that the high unit profit margins will attract potential competitors into production of similar products.

ANS: F
Penetration pricing has low profit margins on each unit sold. This is seen as an advantage because it discourages potential customers from entering the market.

PTS: 1 REF: 321 OBJ: 20-1 TOP: AACSB Reflective Thinking
KEY: CB&E Model Pricing MSC: BLOOMS Comprehension

9. There are two limousine services that drive customers from communities in North Georgia to the Atlanta airport. Whenever one reduces its fare, its competitor reduces its fares by the same amount. This is an example of status quo pricing.

ANS: T PTS: 1 REF: 322 OBJ: 20-1
TOP: AACSB Reflective Thinking KEY: CB&E Model Pricing
MSC: BLOOMS Application

10. Price fixing is only illegal in some instances.

ANS: F
Price fixing is illegal under the Sherman Act and the Federal Trade Commission Act. Price fixing is one area where the law is quite clear, and the Justice Department's enforcement is vigorous.

PTS: 1 REF: 323 OBJ: 20-2 TOP: AACSB Reflective Thinking
KEY: CB&E Model Pricing MSC: BLOOMS Comprehension

11. Price discrimination can sometimes be justified.

ANS: T PTS: 1 REF: 323-324 OBJ: 20-2
TOP: AACSB Reflective Thinking KEY: CB&E Model Pricing
MSC: BLOOMS Comprehension

12. A winery that makes a huge profit on merlot wines may lower its price on pinot noir wines to cause damage to wineries that only produce pinot noir. This is an example of predatory pricing.

ANS: T PTS: 1 REF: 324 OBJ: 20-2
TOP: AACSB Reflective Thinking KEY: CB&E Model Pricing
MSC: BLOOMS Application

13. Manufacturers know the approximate price level they can expect when establishing a product price. This approximate price is called the base price.

ANS: T PTS: 1 REF: 324-325 OBJ: 20-3
TOP: AACSB Reflective Thinking KEY: CB&E Model Pricing
MSC: BLOOMS Knowledge

14. A retailer of furniture for babies that is allowed to deduct 3 percent from its total bill if it pays by a specific date is receiving a promotional discount.

ANS: F
This is describing a cash discount.

PTS: 1 REF: 325 OBJ: 20-3 TOP: AACSB Reflective Thinking
KEY: CB&E Model Pricing MSC: BLOOMS Application

15. Functional discounts are typically calculated as the wholesale price times the accumulated margin percentages.

ANS: F
Functional discounts are typically a percentage discount from the base price.

PTS: 1 REF: 325 OBJ: 20-3 TOP: AACSB Reflective Thinking
KEY: CB&E Model Pricing MSC: BLOOMS Comprehension

16. Sears and John Deere run major sales on their lines of riding lawn mowers every fall. This is an example of a seasonal discount.

ANS: T PTS: 1 REF: 325 OBJ: 20-3
TOP: AACSB Reflective Thinking KEY: CB&E Model Pricing
MSC: BLOOMS Application

17. Functional discounts, noncumulative quantity discounts, and promotional allowances are examples of rebates given to the trade customer.

ANS: F
Rebates involve a cash refund for the purchase of a product during a specific period.

PTS: 1 REF: 325 OBJ: 20-3 TOP: AACSB Reflective Thinking
KEY: CB&E Model Pricing MSC: BLOOMS Comprehension

18. A markdown allowance is a payment to a dealer for promoting the manufacturer's product.

ANS: F
This is the definition of a promotional (or trade) allowance.

PTS: 1 REF: 325 OBJ: 20-3 TOP: AACSB Reflective Thinking
KEY: CB&E Model Pricing MSC: BLOOMS Knowledge

19. The basic assumption with price skimming is that the firm is customer driven, seeking to understand the attributes customers want in goods and services they buy and the value of that bundle of attributes to customers.

ANS: F
This is the basic assumption for value pricing.

PTS: 1 REF: 325-326 OBJ: 20-3 TOP: AACSB Reflective Thinking