ORIGINAL ARTICLE

BeneÞts of sourcing alternative inputs of manufacturers for suppliers

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low-quality inputs to partially replace the inputs from its supplier to produce nished products with lower quality. The above situations of sourcing alternative inputs in product

the lower retail price of nal products, interestingly, the manufacturer can make greater pro ts from sourcing alternative inputs because of the resulting lower marginal cost of the manufacturer. The reason for this nding is that in our model, the manufacturer s production cost is endogenously determined by its product design choice, namely, the proportion of each input used in nal products. In this way, the supplier can exert a signi cant in uence on the manufacturer s sourcing decisions by strategically setting the wholesale price. Although the wholesale price of the supplier s superior inputs can be higher, surprisingly, the manufacturer s production cost can remain lower by using more of alternative cheaper inputs, thereby resulting in a higher pro t for the manufacturer. In a nutshell, we show that despite the induced higher wholesale price, sourcing alternative inputs by the manufacturer can bene t the entire supply chain s members. Consumers also bene t from the resulting lower retail prices.

Moreover, we nd that the wholesale price of the supplier s inputs can be higher than the retail price of the manufacturer s products. Although this implies that the ut

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