

Management in the Post-Crisis Era: Diverse World and Diversified Management

后危机时代的管理:

多元化的世界, 多元化的管理

Proceedings of 2010 International Conference on Management

2010管理国际大会论文集

Editor-in-chief: Department of Management Sciences,
National Natural Science Foundation of China

国家自然科学基金委员会管理科学部 编



National Natural Science
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国家自然科学基金委员会



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国家自然科学基金委员会管理科学部 编

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序 言

改革开放三十多年来，中国经济与社会持续地高速发展。尤其在金融危机之后，中国经济为世界经济的复苏做出了无可比拟的贡献。与此同时，中国的宏观管理、工商管理实践，以及管理学研究，也正悄然地影响着世界管理学理论与实践。

国家自然科学基金委员会管理科学部定期举办管理国际大会，其宗旨就是为了促进中国管理学研究走向世界，在提高自身研究水平的同时，为世界管理理论与实践做出贡献。

次贷危机爆发后，许多西方主流的管理学理论和观点受到挑战与质疑，人们开始认识到，管理理论只有多极化地发展，才能使管理学研究的生态更加健康。正因如此，此次在上海召开的第七届管理国际大会将大会主题定为：“后危机时代的管理——多元化的世界、多元化的管理”。

这次会议是一次高水平的会议。为保证会议的质量，大会组委会采取了严格的论文评审制度，通过专业委员会的层层筛选，从收到的 250 余篇论文中，最终确定了 104 篇论文入选本次会议论文集。本论文集涵盖了管理学领域的诸多方面，包括“运作管理与物流”、“最优化方法与模型”、“决策理论与应用”、“信息管理与电子商务”、“金融工程与风险管理”、“营销学与服务管理”、“组织与行为学”、“经营战略与全球化”、“技术创新与创业”、“中国特色的管理”、“经济与政策模型”、“环境、能源与自然资源管理”、“财务管理”、“人力资源管理”，及“管理科学的其他问题”等 15 个专题，可以说，这是对我国管理学研究水平的一次全面检验。我们高兴地看到，我国管理学研究水平已经有了长

足的进步，尤其是许多年青的学者，他们的研究成果让人感到后生可畏，他们代表了中国管理学界的未来与希望。

更让人欣喜的是，中国管理学界已经完成了从追求数量到追求质量的嬗变。可以相信，中国的管理学研究开始走向良性发展的道路，如果真的是这样，则中国幸甚，世界幸甚。

是为序。

国家自然科学基金委员会管理科学部主任

郭重庆

中国工程院院士、工程管理学部副主任

2010年11月12日于上海

CONTENTS

◎ Operation Management And Logistics

A Study On Outsourcing Decision-making Strategy For OEM And CM <i>HAN Jin, et al.</i>	3
CLRIP Based On JITD In Two-echelon Distribution Network Of Service Parts <i>MA Hanwu, et al.</i>	9
Multi-items Inventory Replenishment Under The Constraints Of Total Service Level <i>SUN Can, et al.</i>	15
Pareto-efficient Pricing And Capacity Choices For A Service Facility <i>LIU Tianliang, et al.</i>	21
Performance Analysis Of Inventory System In A Closed-loop Supply Chain With Stochastic Returns <i>ZHAO Xiaomin, et al.</i>	27
Study On Partial Transshipment Mode In A Two-echelon Emergency Supply System With Multi-items <i>XU Changyan, et al.</i>	37
Study On The Investment Decision-making Model Of Logistics RFID Technology <i>CHEN Jun</i>	43
The Optimal Strategy Of Periodical Adjustment Processes <i>YANG Jianfeng</i>	47
The Research On The Construction Of Grain Logistics Market Operation Network System Of China <i>SUN Hongling, et al.</i>	53
The Study On A Reverse Channel With Competing Retailers <i>XIAO Xuexun, et al.</i>	59
Three-level Analysis Of Safety Operation System In Manufacturing <i>ZHANG Zhongqiang, et al.</i>	67

◎ Optimized Mythology And Model

A Comparative Study Of Different Index Portfolio VaR Model Based On Normal Distribution And T Distribution <i>ZHANG Ying</i>	75
Analysis Of Parameters For Multi-swarm Cooperative Particle Swarm Optimizer <i>NIU Ben, et al.</i>	81
Improved Genetic Algorithm For Capacitated Vehicle Routing Problem <i>DAI Shouyu, et al.</i>	89
Portfolio Optimization Using Non-linear Inertia Weight PSO <i>LI Li, et al.</i>	95
Study On Optimal Group Decision Model For IT R & D Based On Improved Simulated Annealing Algorithm Combined With Fuzzy AHP <i>ZHANG Shouhe, et al.</i>	103

◎ Decision Theory And Application

Analysis Of Product Warranties With Screening And Signaling <i>WANG Haiyan, et al.</i>	109
---	-----

A New Decision Making Method For Vendor Selection With FAHP And FAD	
SHI Guohong, <i>et al.</i>	113
Intellectual Property Right Protection And Strategic R & D Subsidy: From A Developing Country's View	
LI Keke, <i>et al.</i>	119
Nash Equilibriums For Co-operative Strategy When Advertising Threshold Effects Exists	
LIU Yanze, <i>et al.</i>	127
Research For Conflict Coordination Mechanism And Model Of Large Group Decision Based On "HeXie"	
Management Theory	
XU Xuanhua, <i>et al.</i>	135
Study On Symmetry Breaking And Its Applications To Strategic Alliances	
GAO Gao, <i>et al.</i>	145

© Information Management And E-Business

A Talent Recommendation Model Towards Knowledge Product Online Customization	
LV Yingjie, <i>et al.</i>	155
Mobile Innovation Service—From B2C To B2B2C	
QI Ming, <i>et al.</i>	161
Research On The Constructs Of Small And Medium-sized Enterprises Dynamic Alliance Information	
Platform Based On The ASP And Information Sharing	
WANG Youfa, <i>et al.</i>	167
The Design And Application Of A Distributed And Collaborative Anti-SMS-spam System	
QI Ming, <i>et al.</i>	175
The Success Factors Of Small Online Vendors In China: A Content Analysis	
WANG Shan, <i>et al.</i>	183

© Financial Engineering And Risk Management

A New Approach For Modelling And Estimating Expected Shortfall	
QIN Xiao, <i>et al.</i>	195
An Research On Stock Market Evolutionary	
LIU Yumin, <i>et al.</i>	203
A Value-at-Risk Analysis With Long Memory Of Volatility: Evidence From The Chinese Stock Market	
CHUN Weide	211
Does A Positive Perpetual Growth Rate Exist? —A Fundamental Rethinking Of Finance	
ZHANG Zhiqiang	221
Extreme Value Theory And Financial Market Risk Measurement: Empirical Evidence Of SSEC And	
S & P 500	
LIN Yu	229
Foreign Entry And Multiple-stage Credit Competition In Bank Industry: A Steady-state Model	
LI Qiang, <i>et al.</i>	239
Valuation Under The Criterion Of Required Payback Period	
ZHANG Zhiqiang	251

© Marketing And Service Management

An Empirical Study On Impacts Of Customer Equity Drivers	
TIAN Jinmei, <i>et al.</i>	263

A Review Of The Studies On Brand Crisis Based On The Perspective Of Consumer	
WANG Xinyu, <i>et al.</i>	273
Consumer Attitude And Intention To Low-carbon Appliances In China	
WANG Xiucun, <i>et al.</i>	281
Credit Rating Of Software Services Industry Based On Factor Analysis	
LI Li, <i>et al.</i>	289
Effects Of Tourist Experience On Buying Intention: A SEM Analysis Based On PLS	
LI Qigeng, <i>et al.</i>	297
Exploration And Verification On Emotional Intelligence Of Consumers	
ZHANG Yong, <i>et al.</i>	305
Identification Of Key Points Of Service Improvement And The Prophase Mechanism Research In Banking Industry—Based On Empirical Study Of Different Influencing Factors Of The Trust In Two-dimension	
XING Bo, <i>et al.</i>	313
Information Of Luxury Advertisement On Attitudes Of Consumers With Different Competition-contingency Of Self-esteem	
CHEN Jie, <i>et al.</i>	321
Listed Companies Performance Evaluation In Jiangxi Province Using Factor Analysis And Cluster Analysis	
LI Li, <i>et al.</i>	331
Research On Brand Pulling Force: An Example Of College Students' Brand Selection	
SUN Feichao	339
The Consumer Perception Online Of The Context For eWOM: The Third-person Effect	
LI Naihe, <i>et al.</i>	347
The Impact Of Market Orientation And Corporate Social Responsibility On Firm Performance: Evidence From China	
QU Riliang	369
The Key Status Of Relationship Marketing In The Corporation—The Insight Of Relationship Marketing In ArcelorMittal	
CHEN Zhixin, <i>et al.</i>	379
The Study On Utility Of Perceived Risk Reduction Strategies In Internet Shopping	
LI Baoling, <i>et al.</i>	387
Third-party Effects on Consumption Decisions of Electronic Digital Products	
YU Yinglei, <i>et al.</i>	393
Trust And Commitment: A Tracking Study On Generation Difference And Intergenerational Influence Of Time-honoured Brand Relationship Quality In China	
HE Jiaxun	399

◎ Organization And Behavior

Absorptive Capacity And Firm Innovation Performance	
WANG Changfeng	409
An Empirical Study Of Relation Between Intra-team Social Networks And Knowledge Transfer Among Team-members	
ZHOU Mi	417
A Study On Measurement Tool Of Managers' Work-life Integration Attitude: Development And Test	
LI Guiqing, <i>et al.</i>	427
Effects Of Supervisory Support On Employees' Outcomes: The Mediating Roles Of Citizenship Role Definition And Trust In Supervisor	
LIANG Jian, <i>et al.</i>	439

Exploration Of Organizational Culture Competency: Implication Determinants To Be Exposed	
YUE Guolin	453
Job Satisfaction And Creative Behavior: The Role Of The Five-factor Traits	
GU Qinxuan, et al.	461
The Analysis Of Tourist Attractions Destination Pattern With Behavior Proliferation Based Services Resource	
DAI Zhimin, et al.	469
The Influence Of Corporate Governance Structure On The Effectiveness Of Internal Control	
XIAO Xiang, et al.	477
The Mechanism Of Paternalistic Leadership In Cross-functional Teams Under Crisis Situations	
LUO Yulin, et al.	483
The Review And Prospect Of Knowledge Sharing Based On The Theory Of Social Capital	
JIN Hui, et al.	493
Validation And Modification Of Holistic Thinking Scale In China	
WEI Sean, et al.	505

◎ Business Strategy And Globalization

Analysis For Information Spreading Based On Gilpin-Ayala Competition Model In Emergency Management	
HUO Liang'an, et al.	517
Enterprise External Network And Its Performance: Based On The Intermediate Role Of Absorptive Capacity	
LIU Lu	523
From Cost Leadership To Vertical Integration: A Perspective From The Economizing Theory Of Strategy	
YANG Zhi	531
The Competitive Advantage Of Intellectual Property On The Base Of Resource And Capability	
ZHU Weimin, et al.	543
The Effect And Factors Of The Localization Of Top Management: Evidence From The Foreign Subsidiaries In China	
ZHU Jinwei	551
The Effects Of Capabilities And Distance On Chinese Firms' OFDI Motivations: A Conceptual Model	
WU Xiaobo, et al.	561
The Interpretation On Vertical Decision Of Pharmaceutical Companies: A Positive Study Of Chinese Public Companies	
HUANG Dan, et al.	569

◎ Technology Innovation And Entrepreneurship

Managing Creative Coalitions: Reflections On The Social Side Of Services Innovation	
XIAO Cailin	587
Organizational Effects On New Service Development: A Case Study On Commercial Banking	
LI Jinghua, et al.	593
Organizational Learning And Innovativeness Of Products In Transitional Economy	
WANG Dong, et al.	603
Technological Innovation And Sustainable Development Of Small And Medium Enterprises In Post-crisis Period	
GONG Yi, et al.	607
The Effect Of R & D Teams' Strategic Behavior Of Cooperation And Competition On Performance: The Relative Absorptive Capacity As Moderator	
LIU Huafang, et al.	613

The Study Of Green Technological Innovation Diffusion Model And Patterns In The Post-crisis Era <i>GUO Li, et al.</i>	623
The Study On The Characteristics And Countermeasures Of Tri-type Metallurgical Construction Industry <i>ZHU Shan, et al.</i>	629

◎ Management With Chinese Features

Chinese Company's Ownership Structure Under Financial Crisis <i>CHEN Ling, et al.</i>	639
Corporate Social Responsibility And Corporate Performance In The Perspective Of Marketization <i>HUANG Yan, et al.</i>	649
Industry Cluster, Technological Innovation And Economic Effects—Based On The Data Of Anhui Province <i>LIU Yinguo, et al.</i>	657
Management Intuition And Logic—Potential Science With Management Decision-making And Time Innovation <i>LI Dechang, et al.</i>	665
Perceptions Of Face among Undergraduate Business Students And Business Managers: A Decline In Moral Values? (A Preliminary Report) <i>ZHANG Wei, et al.</i>	675
Research On Symbiotic Relationship Between Property Management And Community Management From The Perspective Of Co-governance <i>CHEN Xiqiang, et al.</i>	683

◎ Economy And Policy Model

Application Of Two-Base-Point Entropy Method In Online-advertising Effectiveness <i>ZHU Jing, et al.</i>	691
Latecomer Advantage, Disruptive Innovation, And Industry Growth In Developing Countries <i>WANG Mingming, et al.</i>	695
Transmission Mechanism Of Monetary Policy That Reaction In Financial Crisis—A Simple Dynamic Model <i>HE Huaping, et al.</i>	705

◎ Environment, Energy And Natural Resource Management

A Study Of The Pollution Charge Standard Based On Circular Economy <i>LI Renfang, et al.</i>	713
From Varied Networks To A Unified Regime: Creating A Quality National Park System In China Towards A Healthy Environment Management <i>WANG Lianyong, et al.</i>	721
Global Garden City Construction In Dualistic Societies: A Case Study Of Chengdu City, China <i>BAO Wen</i>	731
The Research On How To Upgrade The Energy Efficiency Of Shandong Province <i>WANG Lei, et al.</i>	739

◎ Finance Management

A BOT Concession Model <i>WU Min</i>	751
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Optimal Instants Of Capital Account Liberalization, Perspective From The Outbound Portfolio Investment And Loan Flowing	
<i>LI Wei, et al.</i>	759

◎ Human Resource Management

A Study Of The Relationship Between Corporate Social Performance And Employees' Contextual Performance—Under The Framework Of Internal Stakeholder	
<i>CHEN Shengjun, et al.</i>	775
Empirical Study Of The Salary Institutions Based On The Consensual Payment Models	
<i>LI Zhihong, et al.</i>	783
Research On The Method Of Employee Performance Measurement	
<i>DU Guoliang, et al.</i>	787
Study On Psychological Contract Characteristics Of The Talent In High-tech Enterprise	
<i>ZHU Xiaomei, et al.</i>	793
The Impact Of Workload On Intragroup Conflicts—The Exploration Of Main Effects And Boundary Conditions	
<i>WANG Min, et al.</i>	801

◎ Other Issues About Management

An Empirical Study On Perceived Effect Of Chinese Cultural Soft Power	
<i>GUO Yingzhi, et al.</i>	813
A Study Of Knowledge City And The Management Of Urban Knowledge Capital	
<i>WANG Zhizhang, et al.</i>	821
Empirical Study On Engineering Project Governance Of Chinese Constructional Industry Under Current Supervision	
<i>WANG Liang, et al.</i>	835
On Application Of The BP Artificial Neural Network Analysis In The Oilfield Exploitation—A Case Study of Chang 2 Reservoir Of Sai-A Wellblock Of Changqing Oilfield Company	
<i>JIA Yuqing</i>	845
The Evaluation And Measurement Research Of the Agricultural Catastrophe Losses In China	
<i>GU Hongbo, et al.</i>	851
The Study On Evolution Mechanisms Of The Enterprise Network In Xi'an Software Industry Cluster Based On Affiliation Network	
<i>HU Ping, et al.</i>	859
The Study On Evolving Simulations Of The Enterprises' Technical Cooperation Networks For The Information Industry Cluster In Xi'an	
<i>HU Ping, et al.</i>	869
To Accelerate The Construction Of China's Sustainable Urbanization—The Necessity And Suggestions	
<i>YAO Fengyun, et al.</i>	877
Triangle Dynamics Of Institutional Innovation; Inspirations From Wind Energy Industry In Denmark, Germany And The U. S.	
<i>CAO Xuanwei, et al.</i>	883

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A Study On Outsourcing Decision-making Strategy For OEM And CM

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Abstract

Recently the contract manufacturing industry has grown rapidly, as original equipment manufacturers (OEM) in a wide range of industries have increasingly preferred buying finished products from contract manufacturers (CM). And new technologies are being constantly introduced to CMs for upgrading the products. This paper focuses on the outsourcing strategy on technology introduction in a supply chain with one OEM and one CM. This study investigates the impact of inducing new technology to the CM for increasing the products' value. Through the development of analytical models that maximize the profits, the optimal outsourcing decisions for OEM and CM are explored under both competition and cooperation scenarios.

Key words

outsourcing, OEM, CM, Game theory

1 Introduction

Outsourcing has received considerable attention in the popular and business press over the last two decades. Within economics there exist numerous studies that have used alternative theoretical frameworks to study outsourcing issues. These studies have relied on contract theory, transaction cost theory, industrial general equilibrium and so on. Quelin, B. and F. Duhamel (2003) analyzed the outsourcing motives and risks, then pointed out that bringing together strategic outsourcing and corporate strategy is preferable. Sang, Chung and Joseph (2010) studied outsourcing with quality competition by developing a three-stage game theoretic model. There are several researches on the effect of contract manufacturing, concerning the effect of OEM totally home-made, partly outsourcing or totally outsourcing. Plambeck and Taylor (2005) explored the impact of contract manufacturing on innovation, capacity, and profitability. They found that outsourcing could be detrimental to innovation and profit, especially if the OEMs are weak relatively to the CM. Gilbert (2006) investigated strategic outsourcing for competing OEMs that faced cost reduction opportunities. John, Brian and Aleda (2009) studied outsourcing to a powerful contract manufacturer with the consideration of the effect of learning-by-doing.

Along with the emergence of contract manufacturers in many industries such as automotive, electronics and pharmaceuticals, many original equipment manufacturers prefer to outsource the entire manufacturing of products for reducing costs of labor or raw materials. Traditional brand owners, now named OEMs, focus on the things that most enhance products' value, such as R & D, design and marketing (Benito, 2006).

In this paper, we assume there is an OEM and a CM. Initially, OEM outsources all products to the CM. Later, OEM needs to upgrade its products to gain more profit or market shares. When OEM and CM make the centralized decision for maximizing profits of both sides, this situation is called cooperation. On the other hand, if OEM and CM make the decentralized decision to maximize their individual profit, this situation is called competition. And in the case of competition, CM might use the technology to produce and sell its own brand products.

2 Problem Description and Assumptions

Suppose, firstly, that the quantity of current products ordered by OEM from CM is q_n , and the variable cost is C_n . Assuming the market model is a perfect competitive market, so the demand function becomes $P_n(q_n) = x$, which means, with given price x , q_n current products could be sold.

Consider, later on, OEM will develop a new product with the quality level denoted by v , the investment in

product innovation is denoted by $I_n(v)$, the new demand function is assumed to be $P_n(q_n) = a + bv - zqn(a, b, z > 0)$. The price of a new product purchased by OEM from CM is denoted as w . Besides producing q_{OEM} for OEM, CM might use the technology to produce and sell its own brand products to the market, the quantity is q_{CM} . We suppose these two kinds of productions are not substitutable. The demand function of CM own brand production is $P_n(q_n) = a' + b'v - z'q_n(a', b', z' > 0)$.

We introduce the parameter δ to adjust the ratio of $I_n(v)$ between OEM and CM ($0 \leq \delta \leq 1$). Suppose that the OEM and CM share the investment with the ratio of δ and $1 - \delta$ respectively.

3 The Model

3.1 Case of current products

Firstly, we discuss the case of OEM outsourcing the current products with quantity of q_o to CM, the unit price is w_o . The variable cost is

$$C_o(q_o) = \frac{1}{2}m_o q_o^2, m_o > 0 \quad (1)$$

The profit of the entire supply chain (both OEM and CM) can be given as

$$\pi_o = xq_o - \frac{1}{2}j_o q_o^2 \quad (2)$$

The profits of OEM and CM can be obtained as

$$\pi_{OEM} = (x - w_o)q_o \quad (3)$$

$$\pi_{CM} = w_o q_o - \frac{1}{2}m_o q_o^2 \quad (4)$$

The profit maximization problem can be solved by taking the first derivative of Eq. (2) with respect to q_o and let the first derivative equal 0, we then have

$$\frac{\partial \pi_o}{\partial q_o} = x - m_o q_o = 0 \quad (5)$$

The equilibrium quantity (q_o^*) and profit (π^*) can be derived as

$$q_o^* = \frac{x}{m_o} \quad (6)$$

$$\pi^* = \frac{x^2}{2m_o} \quad (7)$$

In a game with perfect information, the OEM and CM will share the net profit, and then we have

$$\pi_{OEM}^* = \pi_{CM}^* = \frac{x^2}{4m_o} \quad (8)$$

$$w_o^* = \frac{3}{4}x \quad (9)$$

3.2 Case of new products

In the situation that the OEM plans to invest in new technology for developing new products, the CM is required for cooperation.

The demand function now is

$$P_n(q_n) = a + bv - zq_n \quad (10)$$

The variable cost is

$$C_n(q_n) = \frac{1}{2}m_n q_n^2 \quad (11)$$

The investment in new product development is

$$I_n(v) = \beta v^2 \quad (12)$$

So the objective profit of the supply chain can be expressed as

$$\pi_n(q_n, v) = (a + bv - zq_n)q_n - \frac{1}{2}m_n q_n^2 - \beta v^2 \quad (13)$$

3.2.1 Cooperation scenario

In this scenario, the OEM and CM will cooperate for maximizing the sum of both individual profits. Taking partial derivatives of Eq. (13) with respect to q_n and v , respectively, we have

$$\frac{\partial \pi_n}{\partial q_n} = a + bv - (2z + m_n)q_n \quad (14)$$

$$\frac{\partial \pi_n}{\partial v} = bq_n - 2\beta v \quad (15)$$

The equilibrium quantity (q_n^*), quality level (v^*) and profit (π_n^*) can be derived as

$$q_n^* = \frac{a + bv}{2z + m_n} \quad (16)$$

$$v^* = \frac{bq_n}{2\beta} \quad (17)$$

$$\pi_n^* = \frac{(a + bv)^2}{2(2z + m_n)} - \beta v^2 = aq_n + \frac{b^2 - 4\beta z - 2\beta m_n}{4\beta} q_n^2 \quad (18)$$

Since both OEM and CM will share the net profit, then we have

$$\pi_{OEM}^* = \pi_{CM}^* = \frac{1}{2} \pi_n^* = \frac{(a + bv)^2}{4(2z + m_n)} - \frac{1}{2} \beta v^2 = \frac{1}{2} aq_n + \frac{b^2 - 4\beta z - 2\beta m_n}{8\beta} q_n^2 \quad (19)$$

From Eq. (19), it can be seen that if $\beta \leq \frac{b^2}{4z + 2m_n}$, the profits of both OEM and CM are the convex function of quality level v and quantity q_n . This means if the investment on new product development is lower than a specific level $\beta_- = \frac{b^2}{4z + 2m_n}$, then both OEM and CM will prefer a higher quality level v .

3.2.2 Competition scenario

Under the competition scenario, the outsourcing policy for both OEM and CM can be found through a two-stage game model as follows:

Stage 1: OEM chooses the purchasing quantity q_{OEM} and technology level v .

Stage 2: CM chooses the quantity q_{CM} of the products to produce with its own brand.

Assuming the unit price that the OEM pays to CM is

$$w(v) = w_o + \alpha v, \quad (\alpha > 0) \quad (20)$$

The profit function of OEM consists of three terms; sales revenue, outsourcing cost, and new product development investment share. Then the objective function can be expressed as

$$\pi_{OEM}(q_{OEM}, v) = (a + bv - zq_{OEM})q_{OEM} - (w_o + \alpha v)q_{OEM} - \delta\beta v^2 \quad (21)$$

Let the partial derivation of Equation (21) with respect to q_{OEM} and v respectively equal 0, we have

$$\frac{\partial \pi_{OEM}}{\partial q_{OEM}} = a - w_o + (b - \alpha)v - 2zq_{OEM} = 0 \quad (22)$$

$$\frac{\partial \pi_{OEM}}{\partial v} = (b - \alpha)q_{OEM} - 2\delta\beta v = 0 \quad (23)$$

Then the equilibrium quantity (q_{OEM}^*) and quality level (v^*) can be derived as

$$q_{OEM}^* = \frac{a - w_o + (b - \alpha)v}{2z} = \frac{2\delta\beta(a - w_o)}{4z\delta\beta - (b - \alpha)^2} \quad (24)$$

$$v^* = \frac{(b - \alpha)q_{OEM}}{2\delta\beta} = \frac{(a - w_o)(b - \alpha)}{4z\delta\beta - (b - \alpha)^2} \quad (25)$$

$$\pi_{OEM}^* = \frac{\delta\beta(a - w_o)^2}{4z\delta\beta - (b - \alpha)^2} + \frac{2\delta\beta(b - \alpha)^2(a - w_o)^2}{[4z\delta\beta - (b - \alpha)^2]^2} \quad (26)$$

As the demand function of CM own brand production is supposed to be $P_n(q_n) = a' + b'v - z'q_n$, the profit function of the CM consists of four terms; outsourcing revenue, own brand production revenue, manufacturing cost and new product development investment share. Then the objective function $\pi_{CM}(q_{CM})$ becomes

$$\pi_{CM}(q_{CM}) = (w_o + \alpha v)q_{OEM} + (a' + b'v - z'q_{CM}) - \frac{1}{2}m_n(q_{CM} + q_{OEM})^2 - (1 - \delta)\beta v^2 \quad (27)$$

Let the partial derivation of Eq. (27) with respect to q_{CM} equal 0, we have

$$\frac{\partial \pi_{CM}}{\partial q_{CM}} = a' + b'v - 2z'q_{CM} - m_n q_{OEM} - m_n q_{CM} = 0 \quad (28)$$

Then the equilibrium quantity (q_{CM}^*) can be obtained as

$$q_{CM}^* = \frac{a' + b'v - m_n q_{OEM}}{m_n q_{OEM} + 2z'} \quad (29)$$

Inserting the Equations (24) and (25), we can get the q_{CM}^* as

$$q_{CM}^* = \frac{a'[4z\delta\beta - (b-a)^2] + b'(a-w_o)(b-a) - 2m_o\delta\beta(a-w_o)}{2m_o\delta\beta(a-w_o) + 2z'[4z\delta\beta - (b-a)^2]} \quad (30)$$

Taking Eq. (31) into Eq. (27), we can get the π_{CM}^* as

$$\begin{aligned} \pi_{CM}^* = & \left[w_o + \frac{a(a-w_o)(b-a)}{4z\delta\beta - (b-a)^2} \right] \cdot \frac{2\delta\beta(a-w_o)}{4z\delta\beta - (b-a)^2} + \left[a' + \frac{b'(a-w_o)(b-a)}{4z\delta\beta - (b-a)^2} \right] \cdot \\ & \frac{a'[4z\delta\beta - (b-a)^2] + b'(a-w_o)(b-a) - 2m_o\delta\beta(a-w_o)}{2m_o\delta\beta(a-w_o) + 2z'[4z\delta\beta - (b-a)^2]} - \\ & z' \left\{ \frac{a'[4z\delta\beta - (b-a)^2] + b'(a-w_o)(b-a) - 2m_o\delta\beta(a-w_o)}{2m_o\delta\beta(a-w_o) + 2z'[4z\delta\beta - (b-a)^2]} \right\}^2 - \\ & \frac{1}{2} m_o \left\{ \frac{a'[4z\delta\beta - (b-a)^2] + b'(a-w_o)(b-a) - 2m_o\delta\beta(a-w_o)}{2m_o\delta\beta(a-w_o) + 2z'\delta\beta - (b-a)^2} + \right. \\ & \left. \frac{2\delta\beta(a-w_o)}{4z\delta\beta - (b-a)^2} \right\}^2 - (1-\delta)\beta \left[\frac{(a-w_o)(b-a)}{4z\delta\beta - (b-a)^2} \right]^2 \end{aligned} \quad (31)$$

In competition scenario, the total profit π_i could be obtained by adding up Eqs. (26) and (31),

$$\pi_i^* = \pi_{CM}^* + \pi_{OEM}^*$$

According to Eqs. (19), (26) and (31), the OEM and CM could make the outsourcing decision in either cooperation or competition scenario to maximize their profits.

3.3 Numerical experiments

In the following, numerical examples are presented for sensitivity study. Considering a system with the following parameters:

$$a = 100, b = 5, z = 1, \alpha = 3, a' = 60, b' = 4, z' = 2, w_o = 50, m_o = 1 \text{ and } \beta = 9.$$

Now in cooperation scenario, the total profit π_o^* is a concave function of quality level v and outsourcing quantity q_o (see Figures 1 and 2). In practice, OEM can choose the proper quality level v^* and then invest in the new product development to maximize the profit.

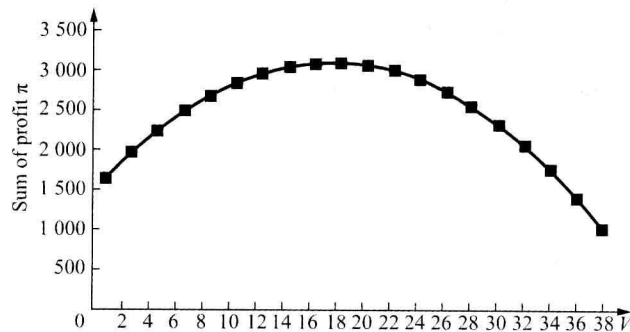


Figure 1 Sum of profit when v varies

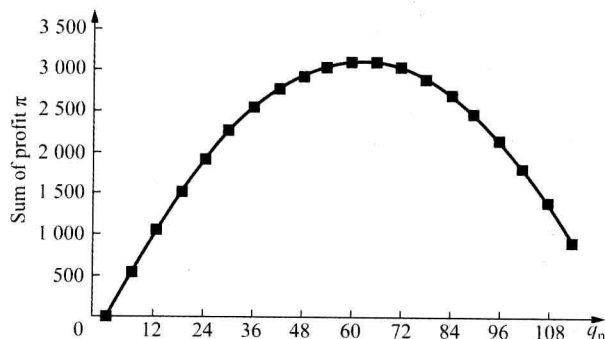


Figure 2 Sum of profit when q_o varies