Is producing a Private Label Counterproductive for a Branded Manufacturer?

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Outline of the paper

- Issue:
  - Decision of a retailer to entrust the production of his private label product to the producer of the national brand or to a competitive fringe.
  - Impact of capacity constraint of the NB producer on the decision

Framework

- Monopolist retailer may sell PL, NB or both
- Monopolist NB producer
- Cost advantage for NB manufacturer
  - Cost quadratic w.r.t. quality
- Endogenous choice of PL quality
- Bargaining between NB producer and retailer
- Possible capacity constraint of the producer
  - Either for both products or only for PL

Results

- Without capacity constraint
  - PL produced by NB supplier iff quality of the NB is intermediary
    - (1) q_L low: PL only, produced by NB supplier if the cost advantage is large enough
    - (2) q_L intermediate: both products sold, PL produced by NB prod if cost advantage +bargaining power of the retailer high enough;
    - (3) q_L high: PL only as NB not profitable, same as (1)
- With capacity constraint:
  - Applies to both PL and NB: NB producer does not produce PL when capacity constraint is binding
  - Applies to PL only: NB producer may produce PL when cost advantage is sufficient

Discussion

- Timing of the game:
  - R commits to the choice of supplier of PL before negotiating conditions with NB producer: outside option is zero
  - Allowing for threat of buying from independent supplier would increase buyer power: consequences?
- Discuss shape of cost function
    - Separate effects of quality and cost
- Endogenize choice of NB quality
- Welfare?
- Capacity constraint at the retail level?