

# Product differentiation and outsourcing under spatial competition

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*We analyse product differentiation by final goods producers under spatial competition with strategic input price determination by firm-specific input suppliers when the final goods producers undertake complete outsourcing or bi-sourcing. Under complete outsourcing, product differentiation decreases as the distance between the input suppliers decreases, but it may increase or decrease with the transportation costs of the consumers and the firms depending on the distance between the input suppliers. The possibility of bi-sourcing reduces the benefit from saving the transportation costs of firms, and creates effects which are opposite to that of under complete outsourcing. Thus, our results differ significantly from the extant literature considering either no strategic input price determination or strategic input price determination under competition in the input market. We also discuss the implications on profits, consumer surplus and welfare, and the implications of the endogenous location choice of the input suppliers.*