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Optimal replenishment and sales team initiatives for pharmaceutical products – A mathematical model

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ABSTRACT

The paper addresses an inventory model of pharmaceutical products where the demand rate of the customers increases with the volume of the initiatives of the sales team. In this model, the deterioration of the product varies depending on on-hand inventory. The volume of sales team initiatives is a control variable. It is dependent on on-hand inventory and vice versa. The profit function of the farm is formulated by the trading of inventory costs, purchasing costs, losses due to deterioration and sales team initiative costs, considering inflation and the time value of the monetary cost and profit parameters. Finally, the profit function is maximized by a variation of the calculus method. A numerical example is given to justify our model.

1. Introduction

Pharmaceutical products are essential commodities in health care management. Many substitutable pharmaceutical products are present in the market. Consequently, the managers of pharmaceutical farms/companies have to think about new strategies to capture market demand. Generally, it is observed that medical representatives act as salesmen of pharmaceutical products. As a result, the sales team should be composed of qualified and knowledgeable pharmacists, doctors and marketing researchers. For this purpose, investment in the sales team and in sample medicines of a particular drug is necessary and constitutes important cost factors for the firms. On the other hand, pharmaceutical products undergo deterioration/decay over time and should not be neglected in the inventory system.

In the present article, we develop a mathematical model that considers sales revenue, inventory holding cost, purchasing/procurement cost, loss due to deterioration and investment in sales team initiatives. Here, the demand for the products in the market has two parts: one part is fixed, which is the demand of fixed customers who have a good relationship with the firm, and other part is an increasing function of the sales team initiatives in which the customers are motivated by the awareness activities that the salesmen use to promote the product. The initiative function of the salesmen is a control variable. The profit function is maximized by a variation of the calculus method by trading off sales revenue, inventory holding cost, loss due to deterioration and cost of sales team initiatives. Finally, optimal values of replenishment and sales team initiatives are calculated to maximize the profit function.

2. Brief review of the literature

In practice, it is observed that perishable pharmaceutical products undergo deterioration over time. Deterioration generally includes spoilage, obsolescence, evaporation and pilferage of the products and increases with time. Many researchers have focused on this topic. Wu et al. (2009) solved an inventory system with non-instantaneous deteriorating items and price-sensitive demands to determine the optimal sales price and length of the replenishment cycle such that the total profit per unit of time of the retailer was maximized. Chang et al. (2010) characterized the optimal solution and obtained theoretical results to determine the optimal order quantity and the optimal replenishment time under a discounted cash-flow (DCF) approach. Jaggi et al. (2011) studied a two-

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warehouse inventory model with a linear trend in demand under inflationary conditions with different rates of deterioration, in which partial backlogging at the owned warehouse was allowed. Widyadana et al. (2011) optimized an inventory model for perishable items with a simplified approach, considering the issue with and without backordering. Ghosh et al. (2011) developed a production- inventory model with backlogging for perishable items with a linear price dependent demand. Sarkar (2012) developed an e*conomic order quantity* model for time with a varying demand and deterioration rate of the items, including trade credit financing and different discount rates on the purchasing costs. Sarkar and Sarkar (2013) extended an inventory model for time varying deteriorating items with stock-dependent demand, allowing time varying backlogging. Sarkar (2013) considered three types of continuous probabilistic deterioration functions in a two-echelon supply chain to analyse a production-inventory model by a simple algebraic approach. Goyal et al. (2013) developed an economic production quantity (EPQ) model for ameliorating/deteriorating items with a ramp type demand, and they minimized the total relevant cost of the system by using a genetic algorithm (GA). Taleizadeh et al. (2015) analysed a Vendor Managed Inventory (VMI) model for a two-level supply chain to obtain the optimal retail price, the replenishment frequency of raw material, the replenishment cycle of the product and the production rate, when both the raw material and the finished product have different deterioration rates.

Research in supply chain management of pharmaceutical products has been extensively applied in the field of health care management. In a pharmaceutical supply chain system, the integration of all performances involved with the flow of products from raw materials to the end customers improves the relationship with the channel members to achieve sustainable competitive opportunities. According to Aptel and Pourjalali (2001), the management of pharmaceutical products is a vital managerial issue in health care industries. Veral and Rosen (2001) showed that one of the long-term benefits of outsourcing could be a reduction in the number of suppliers, which results in lower procurement costs for downstream members of the chain. Nicholson et al. (2004) compared the costs of inventory and service levels for inventory items of an in-house three-echelon distribution network and outsourced a two-echelon distribution network. Kim (2005) studied an integrated supply chain management system, addressing issues related to drugs in health care sectors. Vernon et al. (2005) suggested both analytic and simulation methods for firms to determine the feasible range of prices of products considering licensing risk and developmental Go/No-Go decisions for the payers' use of the cost-effectiveness method. Almarsdóttir and Traulsen (2005) described four types of strategies to curb rising pharmaceutical costs and a taxonomy of strategies for price and profit controls, reimbursement system charges, other fiscal measures, and quality measures. Zhao et al. (2006) discussed the development of software infrastructure for scientists in pharmaceutical industries to help manage information, capture knowledge and provide intelligent decision support for pharmaceutical product formulations. They provided a balanced approach to policymaking in an environment with rising pharmaceutical costs. Lapierre and Ruiz (2007) emphasized scheduling decisions for supply chains of the products instead of multi-echelon inventory systems. Meijboom and Obel (2007) analysed supply chain coordination in the pharmaceutical industry with multi-location and multi-stage operation systems. Chen and Whittemore (2008) suggested that the use of an offsite warehouse to pool resources saved costs on holding inventory by reducing on-hand inventory. Woosley (2009) indicated that hospital administrators and pharmacy managers suffered due to complicated distribution networks for inventory management problems because most hospital administrators and pharmacy managers were doctors without sufficient knowledge of supply chain management. Khan and Shefeeq (2009) showed that mathematical modelling for controlled drug delivery is invaluable in the ongoing struggle to develop new and more effective therapies for the treatment of cancer. Kelle et al. (2012) developed a periodic review inventory model of pharmaceutical products, applying operational and tactical strategies. Uthayakumar and Priyan (2013) investigated a two-echelon pharmaceutical supply chain inventory model for multiple products, considering permissible delays in payment and the inventory lead time under some limitations. Priyan and Uthayakumar (2014) extended the above model for situations in unclear environments. Cárdenas-Barrón et al. (2014) investigated an economic order quantity model in honour of Ford Whitman Harris. Cárdenas-Barrón and Sana (2014, 2015) studied a production inventory model for single and multi-item products in a two-echelon supply chain when end customers' demand varied according to sales team initiatives.

The rest of the paper is organized as follows: Section 3 includes notations that are used to develop the proposed model. The formulation of the model is given in Section 4. Section 5 illustrates the model with numerical examples. Section 6 analyses the sensitivity analysis of the key parameters and provides some managerial insights for the proposed model. Concluding remarks are given in Section 7.

3. Notation

The following notations are used to discuss the model.

$q(t)$ − On-hand inventory at time 't'.
$E(t)$ − The sales team initiatives at time 't', a control variable.
$D(E)$ − Demand rate of the item.
T − The finite time horizon.
R − Replenishment lot size.
θ − Perishable factor ($0<\theta<1$), a fraction of the on-hand inventory.
$\delta=(r-i)-r$ is rate of interest per unit currency ($) per unit time, and i is inflation rate per unit currency ($) per unit time.
c_h − Inventory holding cost per unit per unit time.
c_0 − Purchasing cost per unit item.
c_1 − Cost per unit effort of the sales team.
p − Selling price per unit item.
E_0 − Initial level of sales team initiatives.
J − Profit of the objective function.
R^*− Optimum value of replenishment lot size.
E_0^* − Optimum initial value of the initiatives of the sales team.
J^* − Maximum profit of the objective function.

4. Formulation of the model

In this model, the demand rate is

$$D(E)=a_0+a_1\sqrt{E(t)} \tag{1}$$

where a_0 is fixed demand, which is independent of sales team initiatives, and a_1 is a scale parameter of the demand rate, which is sensitive to sales team initiatives. The demand rate is an increasing function of $E(t)$ that is obvious in practice. Generally speaking, medical representatives are employed to capture the market demand. On the other hand, some pharmaceutical stores employ a medical practitioner to attract customers and boost sales. Under this philosophy, customers/patients benefit from the medical practitioners, and the store owners earn more from selling more