BARGAINING POWER AND FEDERAL MILK ORDERS
FOR FLUID MILK PRODUCERS

by J. R. Strain

In Iowa there is probably no agricultural commodity group that is more completely organized or that has realized more financial gains through bargaining than producers of grade A milk. A few groups of grade A producers are either incompletely organized or not organized at all. However, a single organization represents all of the producers in most of the larger market areas.

There also are many organizations of ungraded producers, but most of these are on a much smaller scale than grade A producers. Members join solely to process their milk on a joint basis, not to gain bargaining strength. In general, they do no bargaining. They take the price offered for their product by their marketing agency.

However, there is one exception to this general situation. State Brand Creameries market the output of their affiliated plants with all of the sales techniques at their command, including some promotion, advertising, and bargaining.

Grade A producers have made many apparent economic gains through their bargaining strength and through federal milk marketing orders. The intent of this paper is to examine the history of grade A bargaining associations and the peculiarities of the grade A product market in order to evaluate the possibilities for similar gains to other agricultural commodities.

The Beginning

At one time milk was milk as far as its use and price were concerned. However, as the economy began to grow and distribution systems became more complex, keeping quality became a concern, and milk-borne disease problems appeared. Taste preferences expressed by consumers and sanitary standards set by health authorities resulted in the establishment of a special "fluid" grade of milk. This milk was produced and handled with specified equipment and under specified conditions to qualify for use in the fluid form. This grade evolved into our present grade A milk program.

Special equipment and handling procedures made grade A milk production more costly than under conventional methods. The consumer demand schedule permitted charging a higher retail price and paying a substantially higher farm price for fluid milk. However, the amount of milk that could be marketed at higher prices in fluid form was fairly consistent throughout the year; the

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production of milk that qualified for fluid use varied widely between summer and winter. During short seasons there often was not enough qualified milk to fill demands at the going price. At other times a large surplus had to be marketed at lower prices for use in manufactured products such as butter and cheese. Thus the farm price a distributor could pay for qualified milk depended not only on amount of additional returns realized from the sale of milk in the bottle, but also on the proportion of qualified milk he received that could be sold in fluid form.

**Setting for Cooperative Action**

In the beginning many individual farmers separately offered their qualified milk for whatever premium price they could obtain. Separately they had little effect on that price. They sold to relatively large buying units, which varied considerably in the type of use they made of the milk and hence the returns they could realize from its sale.

Distributors who sold most of their input as bottle milk realized a higher average return than those who had to process a considerable amount of it into cheese or butter. Yet all tended to pay about the same price at the farm for this qualified milk. The price was usually established by the plants with the largest surplus.

Also in these early days, the product offered by farmers varied considerably in quality and other characteristics even though it was approved for fluid use. This variation often prompted plants with more milk than they could bottle to quit buying from certain producers, sometimes permanently and sometimes just for the summer, to keep their average returns as high as possible. This practice left farmers who had no market often willing to undercut their neighbors to obtain a market above the cheese milk price. When a dealer found he could buy one farmer's milk for a lower price, he tended to use this as a lever for buying everyone's milk at a lower price. This jockeying often led to disorderly marketing.

**Development of Cooperative Bargaining Associations**

In this setting the cooperative bargaining association movement developed in an attempt to improve producers' income. The associations sought to raise the bargaining power of the individuals by amassing a comparatively large volume of the supply for a market area and putting its administration in the hands of a skilled sales executive.

They developed a classified pricing system in which dealers were charged for the milk they received according to the use they made of it. Thus a dealer who sold a large part of his purchases in bottle form no longer had the advantage of a greater average return over the dealer with a large surplus. In theory, this policy reduced the incentive of a plant with more milk than it needed for bottling purposes to quit buying from producers at will.
The "pooling" practice was developed along with classified pricing. In effect all sales were lumped together, whether for class I (fluid use) or for surplus, and a uniform blend price was determined. Thus with all producers sharing in class I sales, individual producers no longer had incentive to undercut their neighbor to obtain a higher return for their milk.

Full acceptance of these cooperative programs was retarded considerably by variation in the products mentioned above. Thus cooperatives in general embarked on an extensive program for improving product quality, standardizing grading, and bettering assembly methods. In some cases, surplus milk was processed in cooperatively-owned plants to lower handling costs and increase returns to members.

**Local Markets**

Primarily, the activities mentioned thus far relied upon differing demand schedules for the various uses of the same product. Equally important to the pattern of development of producer groups is the fact that fluid milk markets are relatively local in scope. Qualified milk in the fluid form has been relatively perishable and bulky (thus costly to transport from market to market) when compared with products such as butter, pork, corn, beef, or wheat. When the sociological and psychological problems or organizing relatively small groups of milk producers were overcome, these groups could then bargain, invest in facilities, and obtain a considerable economic advantage before their gains became large enough to attract a supply from producers in another market. This situation made possible market-by-market organization of producers a much easier accomplishment than simultaneous organization of all producers of a region or a nation.

**Federal Order Program**

The cooperatives often had considerable difficulty in initiating the classified pricing system, in bargaining for gains, and in realizing that a bargain, once reached, would be honored. Firms marketing as processed dairy products a high proportion of the milk they bought from farmers wanted a pricing program which would permit them to pay producers a price equivalent to that paid by firms selling most of their milk in the bottle. Those who sold a relatively high proportion of their milk in bottle form preferred to buy at a classified use price in order to maintain a stable and high quality supply. Many stories have been told of dealers who refused to purchase the milk of the officers of a co-op (for "quality" reasons) or offered the co-op officers a special price to discourage their concern for the general interest of the entire co-op membership. Dealers who did bargain with a local association often would refuse any form of audit so that the co-op never knew for sure if milk purchased at a lower price for use in manufactured dairy products didn't end up in the bottle.
These difficulties reached their peak in the early 1930's with groups of farmers occasionally dumping milk, shooting holes through tankers, and so forth. At this point the Federal Order Program began with the objective of promoting orderly marketing and establishing a price for fluid milk that would assure an adequate and dependable supply the year around. The Federal program adopted the practice of classifying prices and pooling of receipts (initiated by the cooperatives) and instituted a federal audit as a means of verifying the usage of the milk in each price category.

**Basis of Bargaining Gains to Fluid Milk Producers**

The gains achieved by grade A producers have not been solely through organization, bargaining strength, or the Federal Order Program. Two contributing phenomena, both unique to fluid milk, have provided the setting within which the other activities have operated. One is the substantially smaller elasticity of demand that exists for milk in the fluid form compared with milk in the many alternative manufactured product uses. The other is a relatively local market situation for fluid milk, permitting relatively small groups of producers to organize, bargain, and retain the gains obtained by these activities for their members. The organization of producers, bargaining strength, and government regulation, working within this unique economic situation, have brought substantial gains to producers of grade A milk.

**Possibilities for Other Groups**

The above discussion indicates that success in transferring the organization, methods, and government regulation used successfully in marketing fluid milk to other commodities such as manufactured milk will hinge on the elasticity of demand of the various uses of the commodity. For instance, manufactured milk does have many uses, but the demand schedules for these various uses appear so similar and interrelated that minor gains may be the best that can be hoped for. Furthermore, markets for these products are so universal that a producer organization which gains a price advantage of only a cent or two in given areas, such as the Chicago metropolitan market, may be confronted by a flood of easily substitutable products from New York, Florida, California, or Oregon. Perishability, quality, and transportation cost restrictions are so small for most of these manufactured products that a program of market-by-market development, as occurred with fluid milk, could not retain in the local area the gains of such development. The gains would be dissipated quickly to other producers and other areas. If such gains are possible and if the producers who bear the cost of development are to retain the benefits, they will have to be obtained on a national or at least a regional basis.

Currently, a similar situation seems to exist for every other major agricultural product marketed from Iowa farms. Thus the possibility of producers gaining from organizing and proceeding in a way similar to that followed by the grade A associations appears extremely limited both from the
point of view of the scale of the organization required and the similarities that exist in the elasticity of the demand for the various uses of these commodities.

**Role of Government**

If producer groups can isolate similar phenomena for other agricultural products, they may require government assistance in organizing on a production-wide basis and in developing a discriminatory pricing arrangement to take advantage of their findings. Past experience in the milk industry indicates that if the same buyer makes two or more products from the same but discriminatively priced raw material, market order and federal audit may be required. On the other hand, if each use of a product requires a separate sale to a separate buyer, a government market order may offer no advantage.