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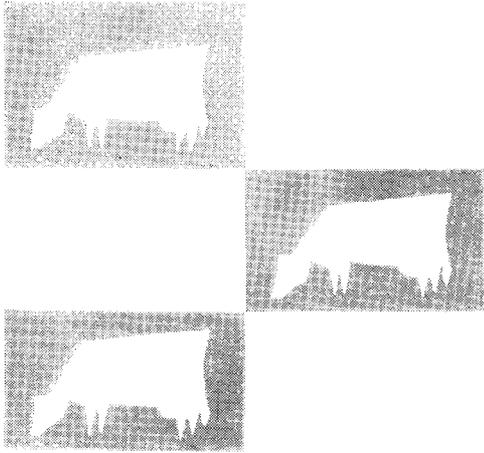
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Cow Pools, A Step Toward Integration?

What's the basis for interest in and, on the other hand, concern about the use of cow pools in Iowa? This article answers this question and points up some of the implications of which producers should be aware.

by J. R. Strain

VERTICAL INTEGRATION among dairy farmers is relatively common today. They've long affiliated themselves together in cooperative butter and cheese producing associations. Large cooperative bargaining associations with surplus grade A handling facilities—and, lately, bottling and distributing facilities—have permitted groups of producers to extend their control over their milk beyond the limits of the barnlot driveway. Acting jointly through a cooperative association has enabled these producers to vertically integrate on their own.

Why Worry? If vertical integration is nothing new to farmers, why the recent flurry of interest in the subject? Probably because of questions in two areas:

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The first involves who will do the integrating. Farmers are realizing that others—such as feed companies and retail grocers—also are investigating the possible savings of vertical integration.

The second concerns the speed at which integration can take place. In the past, the methods of integration more familiar to farmers depended upon the relatively slow process of accumulating money to build or buy additional firms—or of developing cooperative associations of farm firms for joint ownership of facilities to perform the next step in the marketing process.

But today, companies national in scope could conceivably, through contract, obtain rather complete integration between two or more phases of production, processing or marketing without the usual time lag and fund accumulation needed for acquiring ownership of the facilities.

Horizontal Combination or integration occurs when two or more firms at the same level of production, processing or marketing combine into one unit. In the dairy industry, for example, horizontal combination occurs when two or more creameries merge or consolidate into one business unit.

Combinations of this type have been quite common at the farm level also. Between 1940 and 1954, for instance, 213,000 Iowa farms combined into 193,000. Growth in the average size of farms has also been accompanied by increased specialization. In 1940, 90 percent of the 213,000 Iowa farms produced milk. In 1954, only 68 percent of 193,000 farms produced milk. Similarly only 2.2 percent of all farms milking cows received at least half of their income from the sale of dairy products in 1945. But 9 years later, in 1954, 4.4 percent did so.

Increased production per cow has accompanied specialization in milk production. The total number of dairy cows in the state dropped from near 1½ million in 1943 to less than a million in 1958, though total milk production has remained fairly constant. The 1947-56 state average was 6,073 million pounds of milk annually. In 1958 production was estimated at 6,163 million pounds.

What About Pools? Cow pools, as such, aren't a part of vertical integration. They're merely another step in specializing milk production. In a cow pool or contract milking arrangement, the milking and feeding of cows has simply been separated and set aside from the other activities performed by the farm family. A specialized firm, the cow pool, has combined the milking operations of many farm firms through contractual arrangements. Thus, cow pools are examples of *horizontal* combination rather than *vertical* integration.

The cow pool differs from other specialized large milking units. Both types represent an extension of the trend in horizontal combination of milk production. But the cow pool collects cows through contracts with many farm firms, while nonpool milking units col-

lect cows by acquiring ownership or buying them.

Either means of horizontal combination conceivably could replace the 125,000 farmers milking cows in Iowa in 1954 with less than a thousand milking units of around 1,000 cows each. And, if increase in output per cow accompanies this increased specialization as it has in the past, even fewer units would be needed to maintain Iowa's present milk output.

Aid Vertical Integration?

Large specialized operations such as a cow pool may attract potential integrators. Feed companies may wish to form or affiliate themselves with existing pools to make the outlet for their feed more certain. Some cow pool operators may choose to own their own hauling equipment—integrating themselves with one more step toward the consumer.

Some potential cow pool operators are indicating a desire to integrate—either through ownership or contractual arrangement—their milk-producing unit with a milk-processing and distribution firm. So the cow pool, while basically a horizontal combination, seems to lend itself to possible vertical integration.

Pools More Efficient? There are still some questions as to how widespread a cow-pool type of arrangement can become. Present interest in cow pools in Iowa is based almost entirely on a marketing phenomenon rather than a production efficiency phenomenon. The cow pool has offered a number of farmers the opportunity to move from a manufactured milk market to a superior grade A market without investing in buildings, equipment and bulk tank coolers and without learning the skills necessary to produce grade A milk.

If cow pools become more prevalent, opportunities to shift manufacturing milk into grade A outlets will diminish or disappear completely. If that happens, the only basis on which new cow pools could be started would be on a production efficiency rather than a market basis.

The relative production effi-

ciency of a cow pool as compared with a large farm herd hasn't yet been satisfactorily determined. It appears at this time, however, that a cow-pool arrangement can produce milk with considerably less physical facilities and physical costs per cow than can the average *small* Iowa dairyman. But physical efficiencies are only slightly greater than those of *large* efficient dairymen. Thus the prices paid for labor and other expense items in a cow pool could possibly be enough higher to offset the physical efficiencies. Put another way: Many producers don't value their labor or managerial skills as highly as they must pay for them in a commercial milking operation.

Future Form? If cow pools can provide a lower-cost method of producing milk than even our largest one-man dairy herds, cow pools will be likely to develop as follows: Privately owned and operated cow pools probably will be replaced by large milking units in which both the cows and facilities are owned by the operator or a corporation using investment capital. If large milking units are a profitable way for farmers to invest money, they probably will be profitable also for nonfarm investors.

If this is true, then the present cow-pool arrangement must be considered as a convenient or necessary stepping stone or transition from farmer-owned cows to pool operator or corporate-owned cows. The milking facilities operator, for example, will find one board of investors less complicated than 60-80 farmers with interests in specific cows. In addition, record keeping and payments to investors would be greatly simplified and less costly if all of the cows can be considered in one herd rather than in separate or several herds.

Cooperative Cow Pools?

In the past, farmers have invested money off the farm in cooperative creameries, cheese factories and bargaining facilities. The cow pool may offer an additional opportunity for cooperative investment. Investment in cows in a cow pool, for example, might per-

mit a farm operator to tie up or integrate his marketing of grain and roughage without hiring extra farm help to care for a herd of cows.

Investment in a cooperative cow pool could be coupled with existing investment in cooperative milk-processing plants. This kind of arrangement, through a cooperative association of farm firms, could permit almost complete vertical integration between an individual farm firm and the retail sale of milk and milk products.

Producers, on the other hand, may not wish to integrate in this type of operation cooperatively. If not, other forms of investor capital soon may be willing to integrate the production and marketing of milk and milk products for them.

Another Possibility: Another and more far-reaching implication of the cow-pool idea is that it possibly can produce milk at a lower cost than our present farm herds. If so, we must anticipate more milk at present prices, a general lowering of milk prices, or both—similar to what has happened in the poultry industry. This, of course, would mean increasing difficulty for the small producer with but a few cows.

In these circumstances, cow pools would hold another implication for our manufacturing creameries and cheese plants. As milk switched from our present creameries to a cow pool seeking a grade A outlet, the volume of ungraded milk available to our existing plants would decline. The day when all milk sold is grade A milk would be hastened. Similarly, the trend toward manufacturing milk products being made in central surplus disposal plants from excess grade A rather than from ungraded milk would be hastened.

And finally, a widespread and wholesale integration of milk production units with processing and distribution systems could do more than merely lower the general price for dairy products. It could close the grade A markets now available to the relatively small and less efficient dairyman. This could also be true for the independent grade A processor.