

Black Market Economics

Enforcement, Adaptation, and the
Paradox of Prohibition

Dr James Martin



A decorative graphic in the top-left corner consisting of a teal circle and a pink triangle.

Presentation outline

- Drug settings and longitudinal trends
- Insights from economics and game theory
- Case study: Australia's emerging War on Nicotine

National Drug Strategy 2017-2026

A Balanced Approach Across the Three Pillars of Harm Minimisation



Demand Reduction

Preventing the uptake and/or delaying the onset of use of alcohol, tobacco and other drugs; reducing the misuse of alcohol, tobacco and other drugs in the community; and supporting people to recover from dependence through evidence-informed treatment.



Supply Reduction

Preventing, stopping, disrupting or otherwise reducing the production and supply of illegal drugs; and controlling, managing and/or regulating the availability of legal drugs.



Harm Reduction

Reducing the adverse health, social and economic consequences of the use of drugs, for the user, their families and the wider community.

Risks and prices

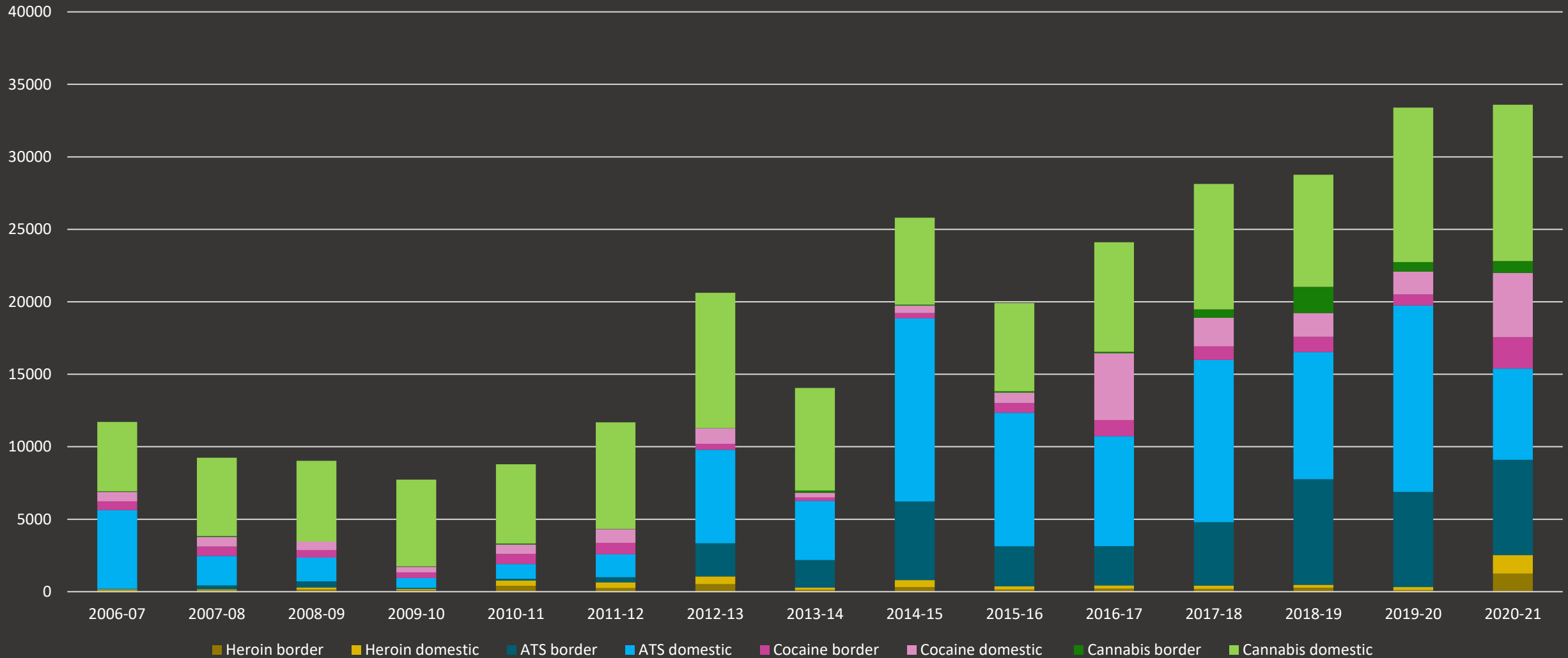


According to the Risks and Prices Framework, supply interventions should:

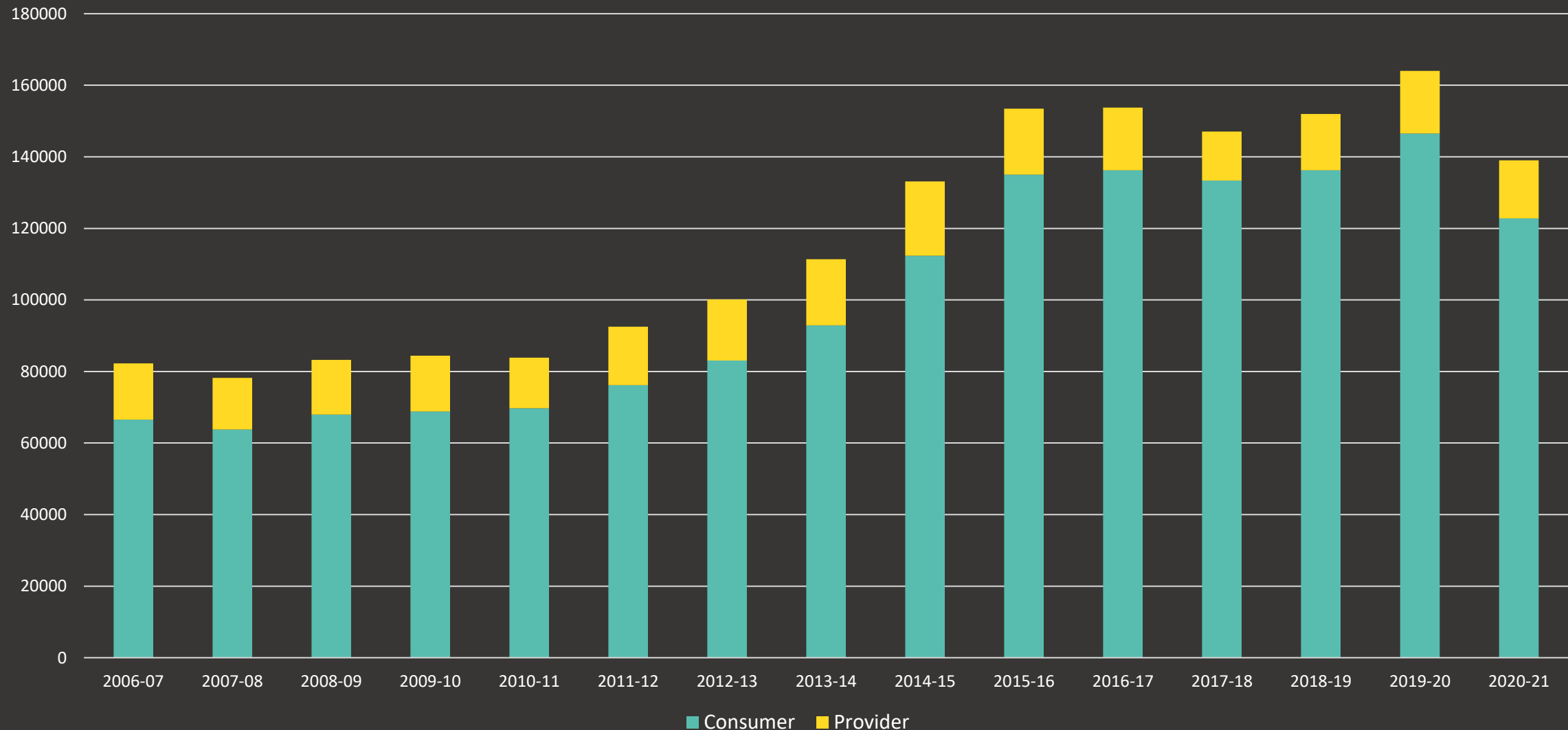
- Decrease availability of drugs
- Deter people from supplying drugs
 - Reducing profits
 - Adding risk (e.g., imprisonment)

In theory, this should **increase the price** of drugs which should then lead to **decreased consumption**

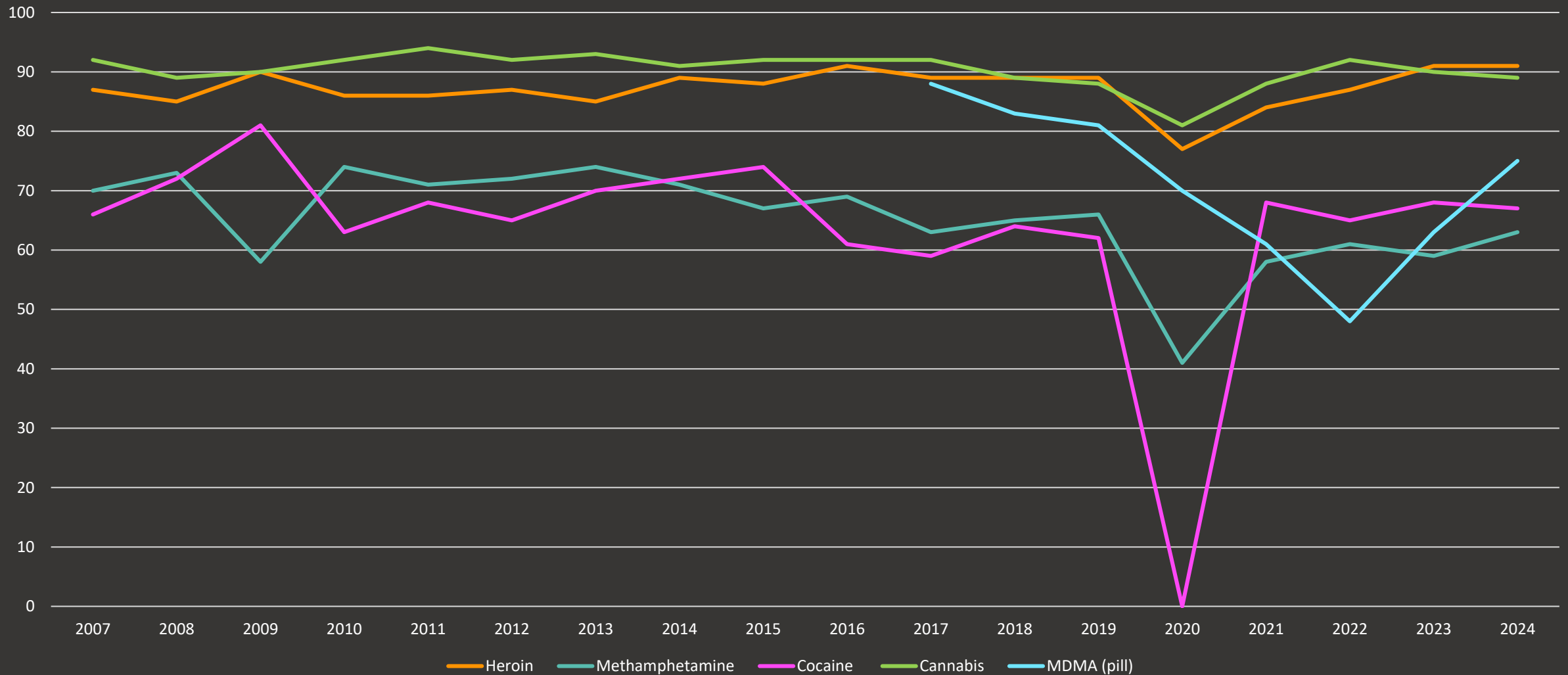
Border and domestic drug seizures (kilos)



Drug arrests – consumers and providers

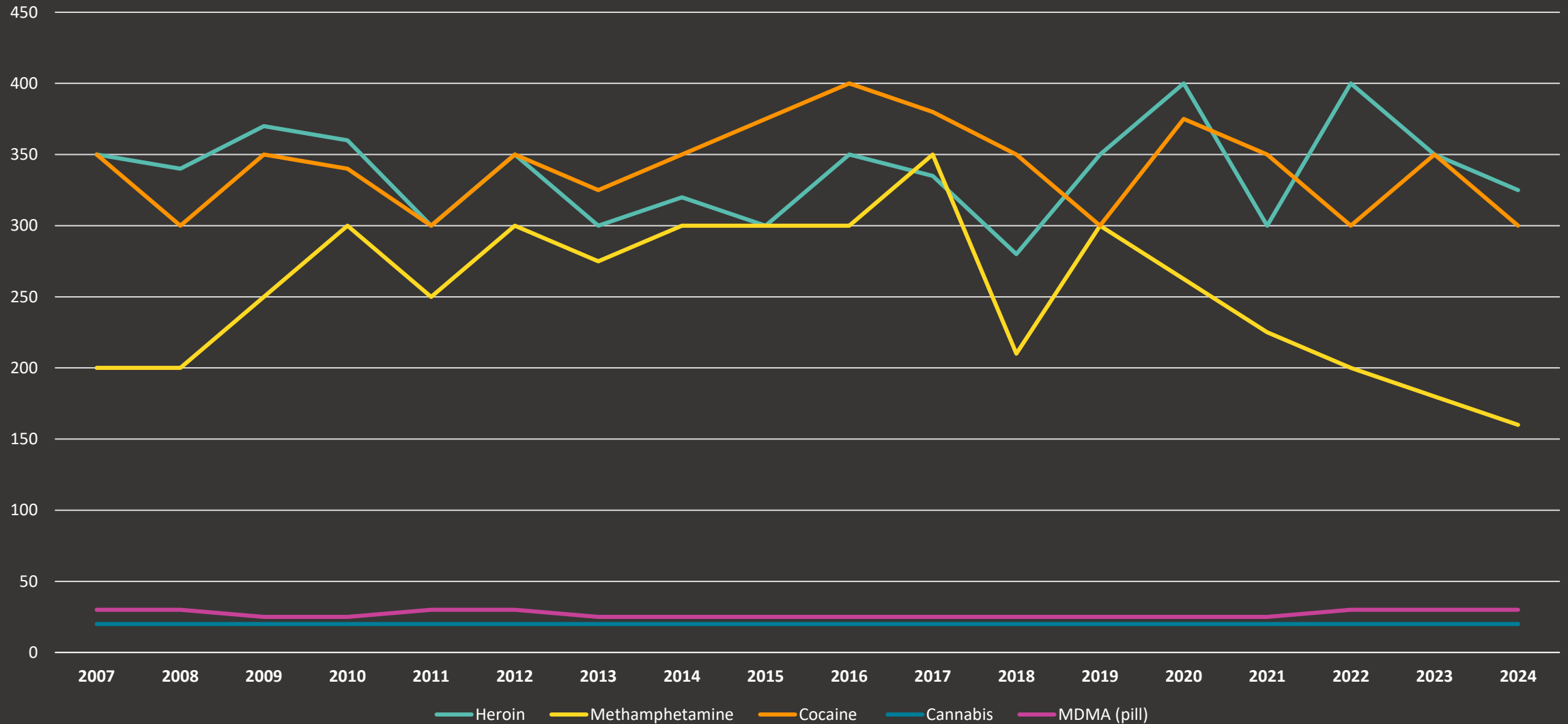


Perceived availability - easy or very easy to obtain



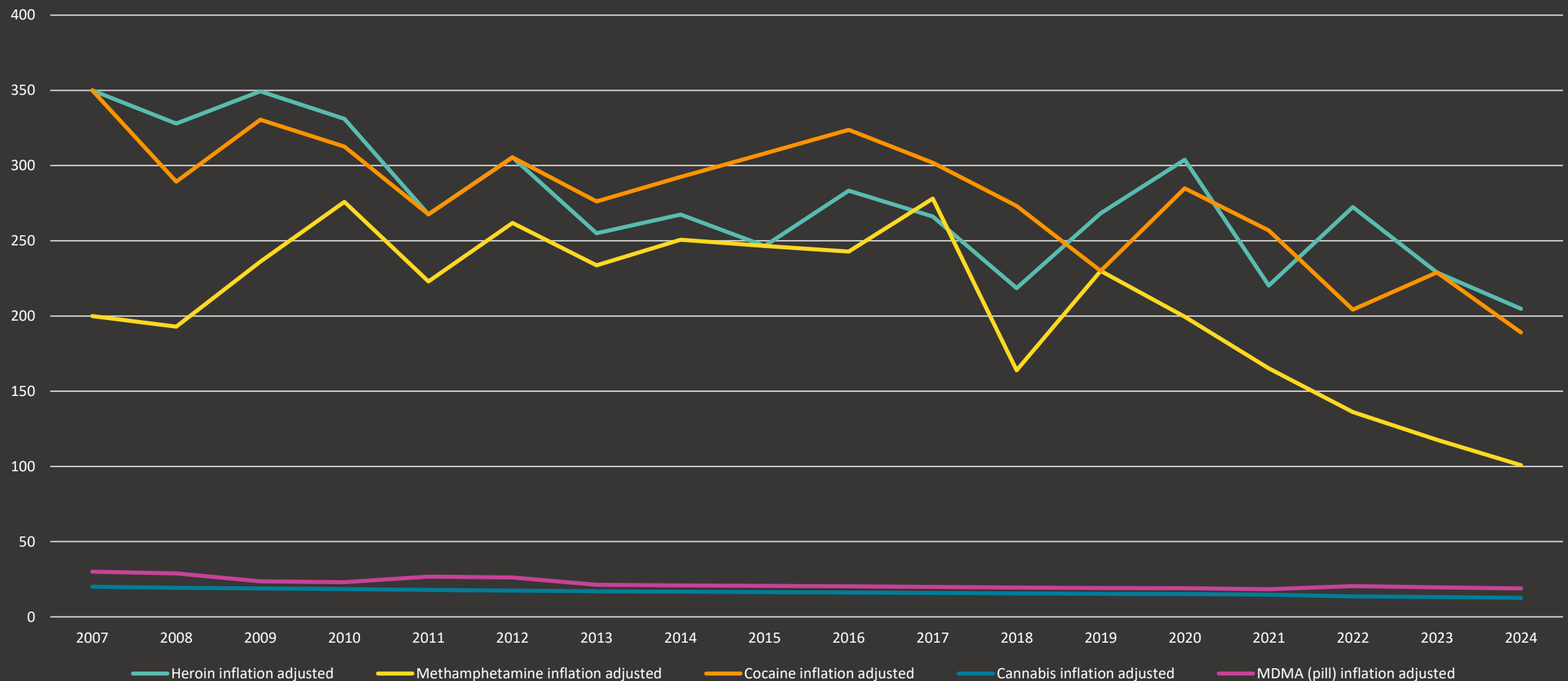
(Sutherland et al. 2024)

Drug prices \$ per gram



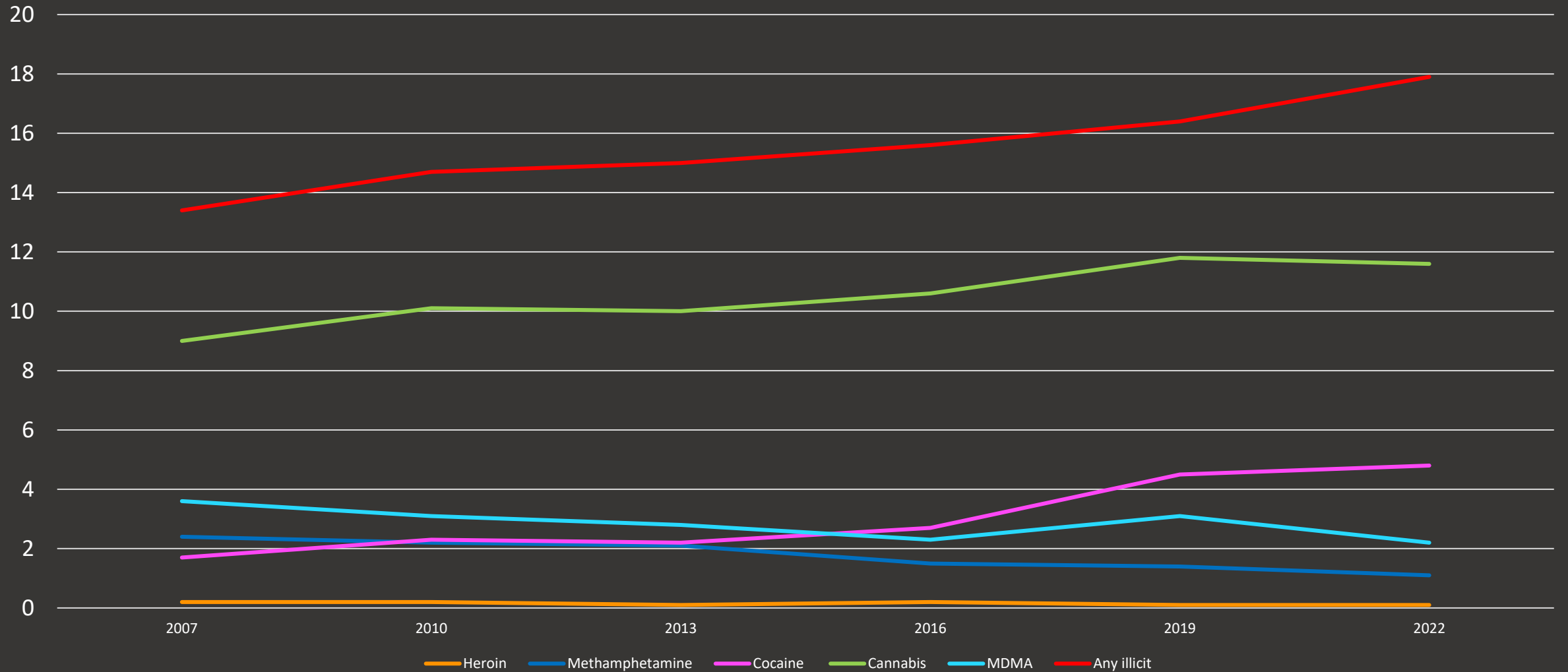
(Sutherland et al. 2024)

Drug prices \$ per gram inflation adjusted (2007 dollars)



(Sutherland et al. 2024)

Recent use people aged 14+



The paradox of prohibition

- Drug enforcement funded at record high level
- Record seizures and ongoing high rates of arrest

BUT




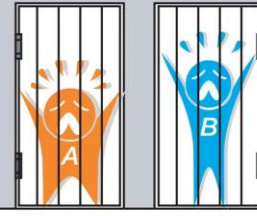


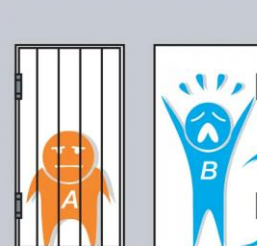
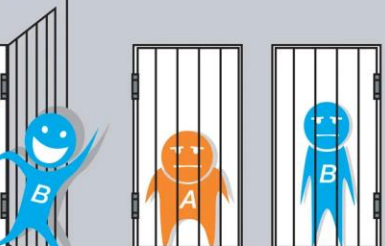
- Availability stable
- Drug prices generally declining – major declines when accounting for inflation
- Purity increasing for some drugs, stable for others
- Prevalence trending up generally but massive variation between drugs

Something weird and unaccounted by RPF for is afoot...

Introducing game theory

- Study of strategic decision-making, where individuals make choices that consider the responses of others to maximise self-interest
- Famous examples include the **Prisoner's Dilemma** which shows that under conditions of uncertainty people acting in self interest can produce counter-intuitive outcomes

Prisoners' dilemma

		prisoner B	
		confess 	remain silent 
prisoner A	confess 	 5 years 5 years	 0 year 20 years
	remain silent 	 20 years 0 year	 1 year 1 year

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Drug trafficking game

Price per gram	Quantity demanded
\$382	64kg
\$357	72kg
\$330	80kg
\$300	90kg
\$280	96kg
\$240	108kg

If there is there is 90kg of cocaine in the market, then the price will be \$300 per gram

If the trafficker sells that cocaine – 90kg X \$300 per gram

Profit = \$27,000,000

Drug trafficking game

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	Trafficker choices		
	Import 80kg	Import 100kg	Import 120kg
Seize 10%	8 (72) \$25,704,000	10 (90) \$27,000,000	12 (108) \$25,920,000

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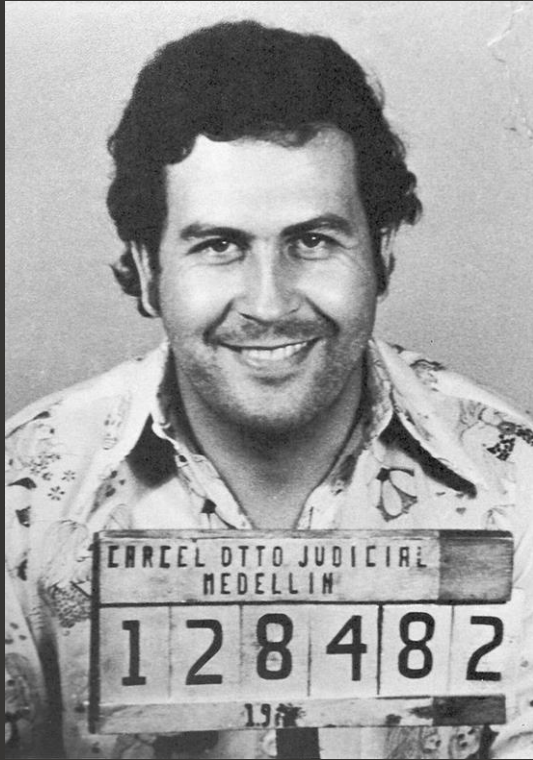
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Share of US cocaine market – 80%



Share of Australian grocery market – 65%

Kingpin strategy

- Where possible law enforcement target the biggest drug distribution syndicates
- Bad news for the targeted syndicate but good news for rival syndicates
- Opens up market share and stimulates competition (and violence)
- Practical effect on market is the same as an anti-trust exercise
- **Net effect = lower drug prices**



The smuggler's mindset



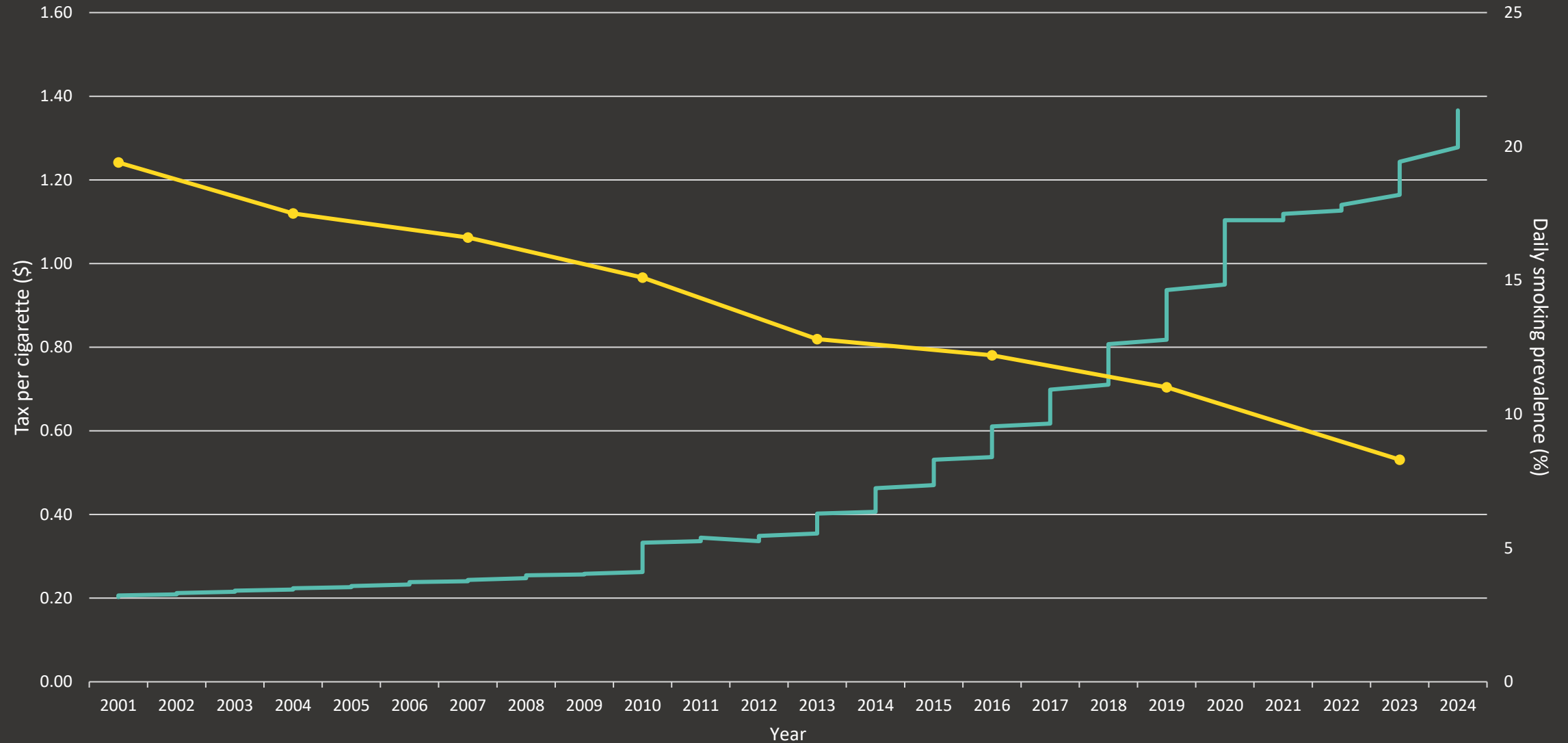
- Assumptions inherent to risks and prices not reflected in real world data
- Drug enforcement, associated laws and penalties, and borders have not proven to be effective deterrents (for some)
- Vast profits to be made ensure a sufficient stream of new participants, regardless of risks
- Obstacles and risks represent **opportunities for profit, arbitrage, and market share**

Case study: Australia's emerging War on Nicotine

- Disproportionate funding and emphasis on supply restrictions over demand and harm reduction
- Extraordinarily high taxation of tobacco and massive decline in legal sales
- Ban on consumer vapes and other less harmful nicotine products
- Concerns regarding extent and impact of 'youth' vaping (e.g., gateway effect)

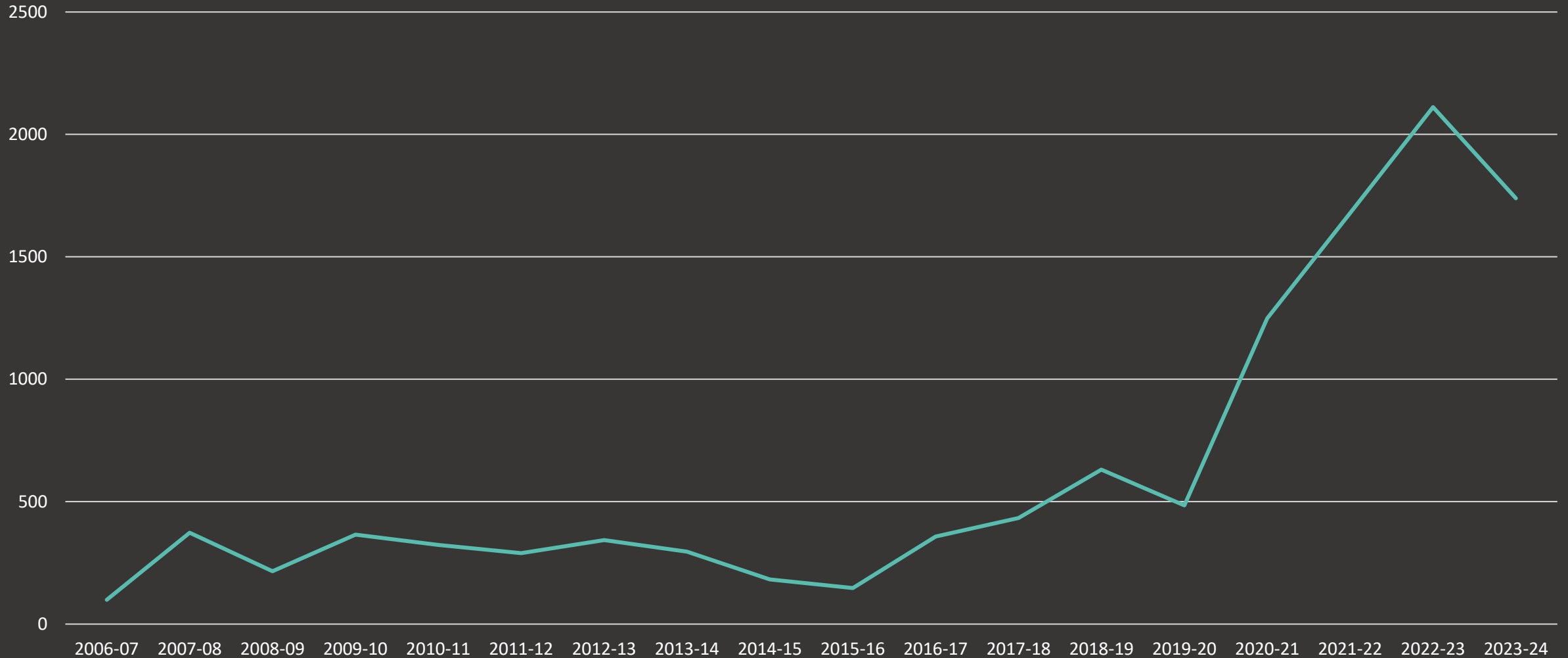


Tax and smoking prevalence



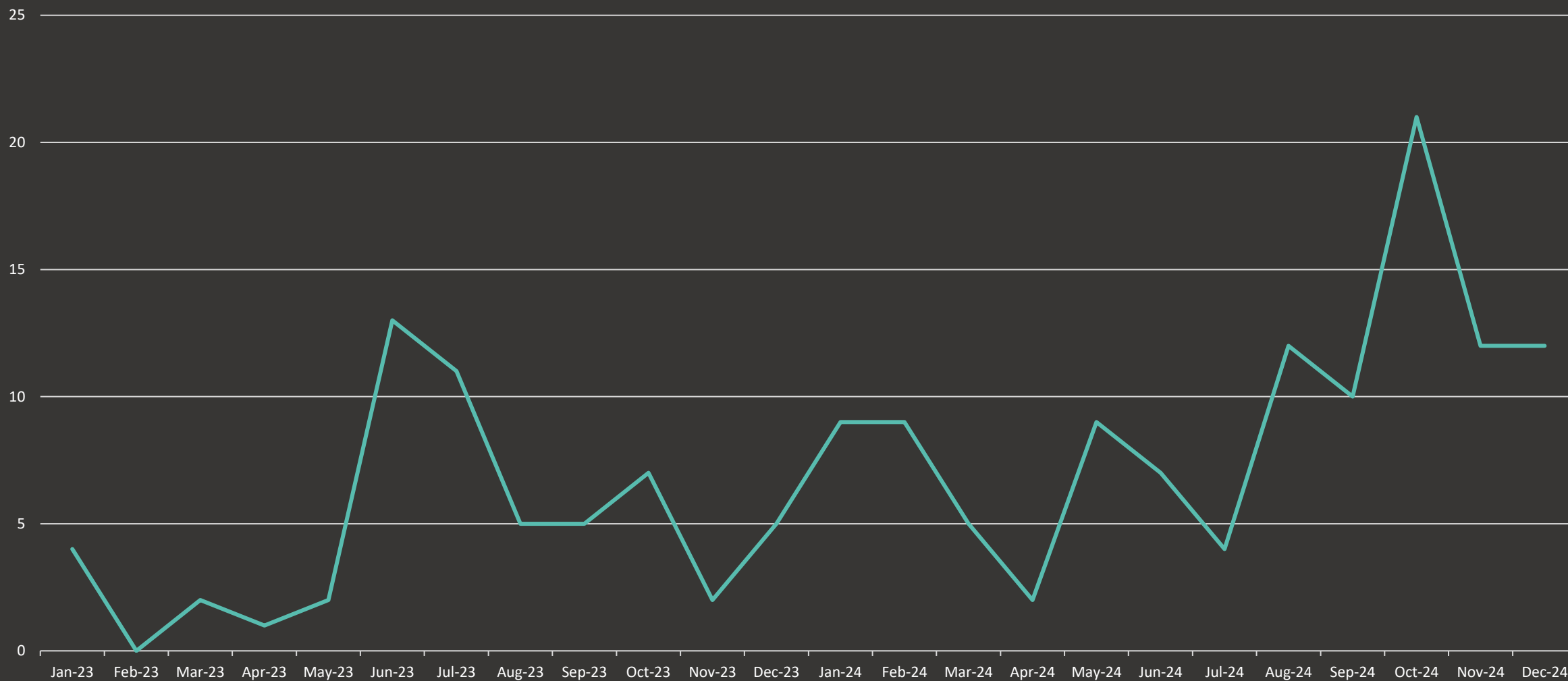
(Jegasothy & Markham 2024; NDSHS 2024; Greenhalgh et al. 2024; Wilkinson et al., 2019)

Tobacco border seizures (tonnes)



(Department of Home Affairs 2024)

Arson attacks - nationwide



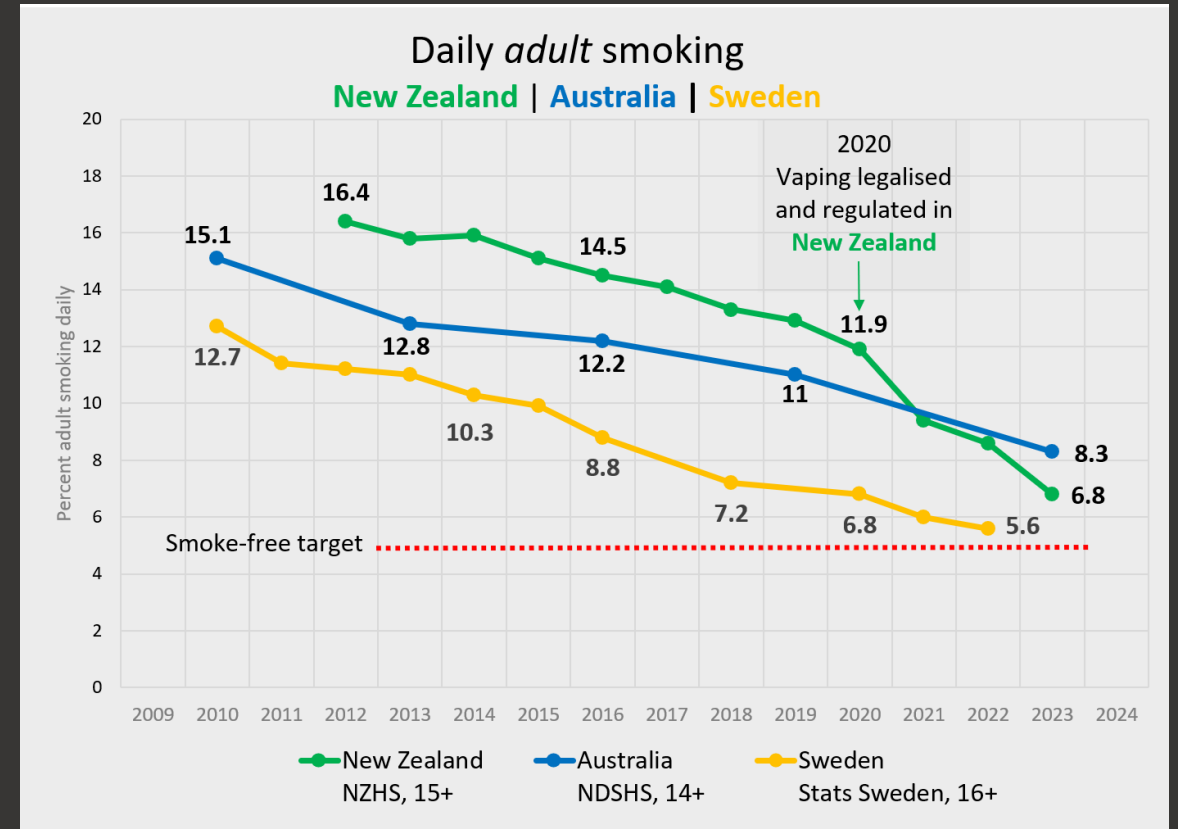
Counting the costs



- Creation of **2nd largest illicit drug market in the country**
- Collapse in tobacco excise revenue
- Massive expansion of organised crime and associated violence
- Increased burden on law enforcement and regulatory agencies
- Proliferation of more dangerous illicit substitutes

Lessons from abroad

- Comparable countries have embraced tobacco harm reduction
- Improved access to less harmful tobacco substitutes
- Greater effectiveness in reducing smoking prevalence
- No gateway effect – opposite is occurring (i.e., substitution)
- Negligible black markets and associated organised crime



(Glover et al. 2024)

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Concluding thoughts

- Risks and prices and government policy have it wrong – **intensified enforcement is costly and has not reduced drug availability or supply** over the long term
- **Price is not consistently correlated with prevalence** over the long term – demand for illicit drugs driven by a complex range of factors
- We are repeating the same mistakes with nicotine as other illicit drugs – restrictive policies are driving the expansion of a large, dangerous black market
- There may be a role for minimal enforcement, however, long-term evidence points to the necessity for rebalancing towards **demand and harm reduction**

Thank you!

Any questions?

