

An Opium Market Mystery

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Wednesday, April 25, 2007; Page A17

Something strange is going on in the global opium market, and it could spell trouble.

Opium is a commodity -- an illegal commodity, but it should still be subject to the normal rules of supply and demand.

Annual demand for opium is approximately 4,500 tons. Last year a record 6,100 tons were produced in Afghanistan alone. That country's production is 30 percent more than total world demand. Heroin prices should, in theory, be plummeting. But they are not. So what is going on?

Does opium defy the laws of economics? Historically, no. In 2001, prices surged tenfold from 2000, to a record high, after the Taliban all but eliminated opium poppy cultivation across the Afghan territory under its control. So why, with last year's bumper crop, is the opposite not occurring? Early estimates suggest that opium cultivation is likely to increase again this year. That should be an added incentive to sell.

Yet prices seem to be resilient. The (unweighted) national average price of dry opium at the farm gate in Afghanistan is dropping, but not significantly -- it was \$125 per kilo in December 2006 compared with \$150 per kilo a year earlier. Prices differ across the country, not surprisingly, since Afghanistan is not a unified territory or market, even for opium. But overall, the drop in prices is modest when compared with the massive increase in opium production, 50 percent, in 2006.

Heroin prices on the streets of Western Europe are also relatively steady, although the drug's purity is going up -- a telltale sign of greater availability.

Are farmers stockpiling the drug? Unlikely. Opium, unlike cocaine, has a long shelf life and can be stored as a form of saving, a source of liquidity and as collateral for credit. But why would poor farmers sit on more than \$1 billion worth of stock when they are struggling to make ends meet and common sense suggests that prices could easily fall?

An alternative hypothesis is that new heroin markets may be emerging somewhere we do not yet know about, perhaps in Asia. But if new markets were absorbing a 1,500-ton surplus, we would expect an increase in seizures of the drug and overdoses in these countries. That hasn't been happening.

So where is it? I fear there may be a more sinister explanation for why the bottom has not fallen out of the opium market: Major traffickers are withholding significant amounts.

Drug traffickers have a symbiotic relationship with insurgents and terrorist groups such as the Taliban and al-Qaeda. Instability makes opium cultivation possible; opium buys protection and pays for weapons and foot soldiers, and these in turn create an environment in which drug lords, insurgents and terrorists can operate with impunity.

Opium is the glue that holds this murky relationship together. If profits fall, these sinister forces have the most to lose. I suspect that the big traffickers are hoarding surplus opium as a hedge

against future price shocks and as a source of funding for future terrorist attacks, in Afghanistan or elsewhere.

What can be done? Since NATO forces are wary of making enemies out of opium farmers by being associated with eradication, and since the Afghan government is opposed to spraying poppy fields, rounding up the major traffickers may be the best available option for disrupting Afghanistan's lucrative opium market.

Another step in the right direction would be to draw up a list of most-wanted traffickers involved in the Afghan drug trade. These criminals would be subject to international arrest warrants, asset freezes, travel bans and, where appropriate, extradition to face justice.

More could also be done to find and destroy opium storage facilities and heroin labs. This is by no means easy, but interdiction at the source is always more effective than trying to catch drug shipments dispersed into smaller units and smuggled across mountain passes and deserts.

Afghanistan's neighbors are either accomplices or victims in the opium trade, so they need to be part of the solution. They could, for example, improve intelligence-sharing and border security to ensure that more opium is seized. At the moment, less than a quarter of the world's opium is intercepted, compared with around half of global cocaine output.

But even if the surplus is tracked down and destroyed, and even if law enforcement efforts improve, interdiction alone will not solve Afghanistan's opium problem. More needs to be done to wean farmers off illicit crops, especially by giving them sustainable alternative sources of income.

Most important, the consuming countries need to get serious about curbing drug addiction. If there was less demand for heroin, the bottom really would fall out of the opium market.

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