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THE POLITICAL ECONOMY OF DRUG TRAFFICKING:

CASE OF PERU

by

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ABSTRACT

An important phenomenon of the past two decades has been the rapid rise in the production and trade in illegal drugs at the international level. According to official sources, between 1985 and 1994, production of opium and marihuana has increased by more than 150% and coca leaf production has more than doubled. However, since 1995, major changes occurred in the illicit drug trade, many of which were brought about by aggressive drug law enforcement. No nation has been immune to the devastating problems caused by drug abuse. At the same time, a broad spectrum of the world community has demonstrated intense concern over the problem: the insidious long-term effects of drug use and its impact on the user, the family, the community, and on society. Drug abuse is not a new phenomenon in Latin America, although it has recently acquired new characteristics. The proportion of the population that uses illicit drugs has grown in size. Illegal production and distribution of drugs affect the economies of many nations. Associated crime, violence, and political disruption have no historical precedents. The illicit production, distribution and consumption of drugs have intimidated and corrupted public servants, and have even destabilized governments. This drug-sponsored violence and confrontation with the state were associated principally with the Cali and Medellin cartels based in Colombia, as well as other gangs such as the cartels of Juarez and Tijuana in Mexico and smaller groups in Peru and Bolivia. In order to understand the impact of drugs throughout the Andean countries of Colombia, Bolivia and Peru that have developed as centers of production and distribution of drugs and, in particular Peru, which is considered the world's leading producer of coca leaf and cocaine base, I will focus this thesis on the Peruvian case in which social, economic, cultural, and political consequences of the production and trafficking of illicit drugs will be described. Hence, the purpose of this study is to analyze first the dimensions of the problem and then, assessing policy alternatives of making a living for impoverished populations that currently support the cocaine market as a means of supporting themselves.

This thesis will be structured in the following way. The first section will examine the political and economic dimensions of the narcotics economy in Peru. It will analyze the significance of the coca leaf and coca paste in the main economic aspects, as well as the socio-economic impact of narcotics in Peru. It will also analyze the dynamics of the coca industry, making reference to the process of coca leaf, cocaine, its use, zones of production, its distribution in the market, the structure and division of labour, and what it offers. Furthermore, it will describe the effect of narco-dollars, their concomitant social and ecological impacts, and the drug-insurgency nexus. The efforts to control production of coca and drug traffic have brought into the scene the direct participation of the United States. The politics of control and eradication evaluate the role of foreign aid and political pressure vis-a-vis the internal resistance and group interests in the national society. Therefore, the second section will examine the problems, strategies and solutions to tackle the underlying issues, analyzing the role of governments and the military, and the responsibility of supply and demand countries. It will outline Peru's position facing the drug trafficking problem, the U.S. intervention, the evaluation and measure of effectiveness, and options regarding drug control and alternative development policies. Finally, this thesis will conclude with some opinions that must be considered in order to develop an effective economic and counter-narcotics program with the goal of giving Peru economic alternatives for its urgently needed national development and modernization.

Contents

List of Tables		**iv**
List of Charts		**v**
Acknowledgements		**vi**
I.	***The Political Economy of Drugs in Peru***	**1**
	1.1 Economic Trends	11
II.	***Part One***	
	Defining the Problem	**32**
	2.1 Significance of the Coca Leaf and Coca Paste in the Main Economic Aspects	32
	2.1.1 Production of Coca and Coca Paste	32
	2.1.2 Distribution in the Market	50
	2.1.3 Structure and Division of Labour	53
	2.1.4 What Does Coca Offer?	56
	2.2 The Socio-Economic Impact of Narcotics in Peru	60
	2.2.1 Money Laundering	60
	2.2.2 Socio-Demographic Impact	66
	2.2.3 Violence and Insurgency	72
	2.2.4 Externalities of the Coca Industry	79
III.	***Part Two***	
	Assessing Policy Alternatives	**84**
	3.1 Problems. Strategies and Solutions to Attack Drug Trafficking	84
	3.1.1 Role of Governments	85
	3.1.2 Role of the Military	86
	3.1.3 Responsibility of Supply Countries	89
	3.1.4 Responsibility of Demand Countries	91
	3.1.5 Peruvian Position Facing the Drug Trafficking Problem	92
	3.1.6 United States Intervention	100
	3.1.7 United States Policy and Strategy Goals	103
	3.1.8 Evaluation and Measures of Effectiveness	107
	3.1.9 Options	109
IV.	***Conclusion***	**116**
V.	***Bibliography***	**127**
Annex: Maps		**133**

Tables

Table 1.1.a:	GDP Growth by Sector	23
Table 1.1.b:	Coca by-product Export related to Macroeconomic Variables	26
Table 2.1.1.a:	Worldwide Potential Net Production 1994-1991 (metric tones). Worldwide Cultivation Totals (Hectares)	34
Table 2.1.1.b:	Basic Indicators on Coca and Drug Trafficking in Bolivia. Colombia and Peru.1975-95	39
Table 2.1.1.c:	Production of Coca Leaves. Coca Paste and Cocaine. Plus Prices and Income Generated. For Bolivia. Colombia and Peru. 1985-95	40
Table 2.1.1.d:	Distribution of the Profit From Drug Trafficking in the Andean Countries.1985-95	41
Table 2.1.1.e:	Economic Impact of Illegal Drugs. Andean Countries. 1994	46
Table 2.1.1.f:	Peru-Increasingly Efficient Farmers	47
Table 2.1.1.g:	Prices in US$/Kg	49
Table 2.1.4.a:	Peru-Estimate Net Annual Income. 1994. Coca and Legal Crops	58
Table 2.2.2.a:	Population and Population Growth Rates in the Upper Huallaga Valley and Two Clusters Within It	69
Table 2.2.4.a:	Cocaine Processing	81

Charts

Chart 1.1.a:	Measures of Poverty. 1994	18
Chart 1.1.b:	Distribution of Poverty	19
Chart 1.1.c:	Macroeconomic Variables	22
Chart 1.1.d:	Social Expenditure in real terms: 1990-1995 (US$ MM)	24
Chart 1.1.e:	Peru: Export of Coca Leaf. 1985-1994 (Kgs.)	25
Chart 2.1.1.a:	Cultivation and Production of Coca Leaf	43
Chart 2.1.1.b:	Cultivation and Production of Coca Leaf	44
Chart 2.1.1.c:	Cultivation and Production of Coca Leaf	45
Chart 3.1.6.a:	Coca Leaf. Coca Paste and Cocaine Seizures and Drug Arrests	103

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I. The Political Economy of Drugs in Peru

The debate about drug control and drug trafficking worldwide is intense. Tensions abound, policies clash, human tragedy and suffering continue on a massive scale. The origins of some of these tensions are clear: rapid changes in political alignment, reduced family and community cohesiveness, increased unemployment and underemployment, economic and social marginalization and increased crime. At a time dramatic improvements are taking place in some sectors such as communications and technology, improvement of the quality of life for many people has fallen far short of the potential that exists and the rising expectations of people who know life can be better.

At a time of rising social and political tensions in the developing countries, the macroeconomic environment has fundamentally changed. In the beginning of the 1990s, the directors of the International Monetary Fund and the World Bank observed that the strong performance of many developing countries, reflected in markedly higher savings rates, greater investment in physical as well as human capital, higher efficiency of investment and stronger overall growth in productivity, was due to fundamental economic development that had led to more stable and sustainable economic conditions. This major influence of thinking about development was the phenomenon of globalization. More than ever, development includes the question of how to compete in global markets. The trend towards globalization is continuing, helping to accelerate development for many countries. Hence, more widespread and sustainable progress will now depend on building strong capacities to achieve good governance, reduce poverty, and protect the environment. Civil conflict, terrorism, population and migration pressures, epidemic disease, environmental degradation, and international crime and corruption hinder the efforts of developing countries and concern us all.

A new, more open international trade regime has been established with the entry into force of the Uruguay Round and the inauguration of the World Trade Organization. World trade and investment have expanded and brought to some areas of the developed and developing world substantial economic benefits. Capital and goods move much more frequently and freely across nation borders than was the case previously. In many industries, multinational enterprises operate on a world scale by allocating production according to the comparative advantage of individual countries or regions, by selling in diverse geographical markets and by undertaking financial operations where it is most advantageous. Developing countries have been among the most active in shaping these new norms for expanding trade. Their participation in global negotiations and the market opening reforms that many of them are adopting have given developing countries new international influence, and a new stake in a functioning world economic system.

Growth in world trade is continuing to outpace overall economic growth, and developing countries are becoming increasingly active participants in global markets. The World Bank projects that world merchandise trade will expand by more than 6 percent a year over the next ten years and that trade in services will expand even faster. Both economic growth and trade growth by the developing countries are expected to exceed the corresponding growth rates in the industrialized countries[1]

The global changes which have allowed goods and money to move from one country to another cheaply and easily have also had other consequences. Globalization clearly presents risks as well as opportunities for developing countries, including the risk that not only individuals. but entire countries and regions. may be left behind. A number of developing countries. especially those in Africa and selected countries in Latin America and Asia. have largely missed out on the benefits of increases in world trade and investment and consequent economic growth. In some cases. this has been the result of political instability. ethnic conflict. massive impoverishment or mismanagement of the economy. which are compounded by the links of terrorist activities. Whatever the reason in a given country. the lack of economic progress has put such countries in a financial bind and frequently placed severe restrictions on government services available to the most vulnerable segments of the population. For example. with the freer and larger movement of goods and the increased volume of trade. it has become easier for drug dealers and weapon smugglers to move their wares across countries.

Another potential cost of globalization is that it has also provided the opportunity for drug producers and traffickers to organize themselves on a global scale. to produce in developing countries. to distribute and sell in all parts of the world. to move drug cartel members easily from country to country and to place and invest their drug profits in financial centres offering secrecy and attractive investment returns. The same deregulation that has allowed legitimate businesses to move money around the world electronically with few national controls has also permitted drug traffickers to launder illicit drug profits so that these funds appear to be legitimate. Therefore. to analyze the impact of these problems becomes especially relevant.

From its origin in the Andean region of Peru. Bolivia and Colombia coca fields to its final destination. primarily North America and European urban centres. the coca and cocaine enterprises form a long chain involving a wide diversity of links: persons.

occupations, equipment, transactions, resources and consequences. While in industrial societies cocaine is a social evil, in the Andes of Peru, coca production is part of the traditional ecological exchange but cocaine preparation and traffic has become an important source of cash integrating farmers into the nexus of global trade.

The cultivation of the coca plant in Andean countries is an Indian tradition of uncertain origin. The chewing of coca leaves can release an extremely small amount of cocaine hydrochloride, and traditionally coca leaf chewing has been popular in Indian communities to combat hunger and altitude sickness. In addition, coca leaves are used as part of traditional herbal cures, to make tea, to predict the future, and other activities. In fact, traditional uses of coca leaves for chewing and other purposes remains a legal activity in Bolivia and Peru. However, according to the Instituto Nacional de Estadística e Informática (INEI), 95% of coca leaf output in recent years has served as a base for the production of refined cocaine for export[2].

Thus, the infiltration of an underground economy into the indigenous people's lifestyle has brought about a new type of economic dependence which is known as the narco-economy.

It was only in the last twenty years, as cocaine became the drug of choice among the young and comfortable of Western Europe and the United States, that coca farming went from a cultural artifact to the best-paying industry in Peru. Distribution systems vary according to the drug. Largely because production has been concentrated within the Andean region, the processing and distribution of cocaine has fallen under the control of centralized organizations, especially the Colombian cartels based in Cali and Medellin. This international organized crime came to the jungle, adopting the traditional culture of coca to its own purposes, collapsing the agricultural industry, and creating an underground economy of unemployed migrants, peasants, officials that now reaches from the jungle throughout the rest of the country, contributing to a culture of shakedowns, payoffs and crime.

Crime and drugs may be related in several ways, none of them simple. Illicit production, manufacture, distribution or possession of drugs may constitute a crime. Drugs may increase the likelihood of other, non-drug crimes occurring. They may be used to make money, with subsequent money-laundering, and may be closely linked to other major problems, such as the illegal use of guns, various forms of violence and terrorism. A number of terrorists and organized criminal gangs are involved in or have close ties to the illicit drug trade. The link between the two is often money and power. One example is Colombia, which has emerged as a centre of trafficking in cocaine, blending highly organized social and economic interests with an underground specializing in drug crime.

Political changes may affect smuggling patterns, organized crime and drug abuse. Nowadays, the effect of opening the borders within Latin America has raised the issue of drug trafficking and terrorism. In the past, close links existed between terrorist groups in several Latin countries. Fewer control points between these countries may make it more difficult to maintain adequate security. Moreover, several points deserved mention at the outset.

First, moving against the cocaine traffic entails serious and political costs. This industry has represented a relatively important source of foreign exchange for Andean countries, it is an important source of jobs and income in regions characterized by desperate poverty and widespread unemployment. People are employed directly in the upstream and downstream phases of the industry-cultivation, initial processing, refining, and smuggling. All along the cocaine production chain, people receive substantially higher wages than they would in the licit economy.

Second, the success of international drug traffickers can be seen in the sophisticated networks of distribution which have often adopted the techniques of large, legitimate, multinational corporations. Traffickers keep abreast of peak demand areas and the drug of choice in a specific geographic location, while maintaining the flow of narcotics around the world. The cocaine industry as a whole has accumulated significant political clout. Cocaine traffickers play the role of power brokers and are a major source of funding for political campaigns and terrorist groups. Traffickers such as Pablo Escobar and Carlos Lehder of Colombia, Luis Arce Gómez of Bolivia, Carlos Demetrio Chávez Peñaherrera "El Vaticano", the Cachique Rivera brothers, and Reynaldo Rodríguez Lopez "El Padrino" of Peru have also penetrated and corrupted nearly every important national institution[3]. The corrupting influence of vast sums of drug money is patently clear at every level, from the local community upward, both in political and administrative terms. It begins with a payoff to a local authority or police officers to overlook an illegal crop or laboratory. The bribery is carried out at various levels, stops at no border and recognizes the authority of no country. Since the major drug traffickers have almost unlimited funds at their disposal, the thousands spent in bribing officials may be viewed as a good investment to ward off the threat of being shut down or arrested. Traffickers can and do use millions of narco-dollars to influence how strictly an international treaty is complied with, and to exercise power throughout entire regions of the world.

Third, the war on cocaine is not especially popular in South America: it is perceived as a program imposed on South America by the United States. In the 1970s. the Drug Enforcement Administration (DEA) initiated new efforts to address the illicit profits of drug trafficking. As an example in the past ten years. they have carried out programs such as Operation Bahamas and Turks and Caicos (OPBAT). Operation SNOWCAP. the Northern Border Response Force (NBRF) and Operation CADENCE which have provided the backbone of the U.S. Andean Strategy for cocaine suppression. Asset removal has been a difficult objective. but today the DEA alone is seizing about US$ 1 billion in trafficker assets each year. These U.S. initiated measures include extradition. the spraying of illicit crops. U.S. military intervention against cocaine laboratories. and economic sanctions against cocaine-exporting countries. Altogether. the Latin American drug trade has complicated relations between the United States and many of its southern neighbours over a variety of issues. ranging from offshore banking privacy rights related to the laundering of dirty money. narcotics enforcement. corruption. and the search for alternative crops[4].

Estimating and analyzing the economic impact of the narcotics industry on producer countries are important tasks. Thus. this thesis will focus on estimates of the economic impact on the narcotics economy in Peru. It will examine available estimates and pertinent methodological issues. indicating why resulting estimates are uncertain. and why it is not possible to determine in a clear manner why whether the narcotics industry has been good or bad for Peru.

For these reasons. the impact of the narco-industry on producer countries has frequently been obscured. One thus should focus on the most important dimensions of the problem and try to quantify relevant variables. With regard to Peru. it would be desirable to know: (i) how much money do Peruvians make a year in the narco-industry?. (ii) how much of that income do the narco-traffickers bring back and spend in Peru. and how much do they keep abroad?. (iii) what is the net worth of the narco-traffickers. and how much of it is inside and outside of Peru?. (iv) what has been the impact of narco-capital flows on the Peruvian economy and on the government's policies?. (v) how does policies impact on the narco-economy?. (vi) what is the impact on the balance of payment and payment of debt services?. and (vii) what are the long-term implications for Peruvian economic policy of the large amount of capital accumulated by narco-traffickers?

Unfortunately. the information available is not official and provides only imperfect. incomplete. and indirect responses to these questions. All calculations about size of the narco-industry begin with estimates by the U.S. National Narcotics Intelligence Consumers Committee (an inter-agency committee that collects data on drug production and trafficking) whose satellite pictures are used to estimate the area cultivated with coca. marijuana. and other illicit crops. However. these appraisals are likely to be quite inaccurate because of technical difficulties in determining the nature of an agricultural enterprise and because marijuana and coca plants are frequently grown alongside other crops that hide them from view[5].

The environment. socio-economic. cultural. and political impact of illicit cultivation. manufacture. and traffic of narcotics has reached critical levels. The impact of these activities has altered economic activity. deteriorated the long-term real exchange rate. distorted the job market. and spawned violence and social instability in those areas directly and indirectly affected.

These economic effects of the drug trade have been widely debated by economists in Latin America, the United States and elsewhere. Some sharp differences in opinion can be noted. For instance, Francisco Thoumi argues that the drug industry depressed the growth of the formal sector of the economy and that the Andean economies would do better without drugs, than with them[6].

Another related problem is that the cocaine industry itself produces few backward or forward linkages to the legal economy: that is, the industry generates relatively little demand for local products and cocaine cannot be used to feed into other industries. According to scholars Mario de Franco and Ricardo Godoy, each dollar of cocaine exported requires the purchase of only US$ 0.03 of goods and services from the non-cocaine economy: in contrast, commercial agriculture, mining, energy manufacturing, construction and services require the purchase, on average, of US$ 0.27 from the rest of the economy. At the same time, the influx of hard currency associated with narcotics exports made possible more imports and less external debt. Coca and cocaine substituted for the failure of past formal economy in Peru and Bolivia, providing alternate employment, maintaining income levels and stabilizing the national currency[7].

Historically, coca growing has been an important, if not a predominant, economic activity in Peru. Regardless of the legal status or social effects of coca growing, it is a way of surviving to which hundreds of thousands of poor, landless, and unemployed people have turned to. For them, it is simply the industry with the most opportunities. Participating in the cocaine economy is the goal of the great majority of people in the Andes.

The case study of Peru shed light on these important economic issues while providing interesting lessons about the prospects for alternative development as a strategy for weaning peasants farmers away from producing the coca leaf. It can comprise a range of activities designed to limit or reduce cultivation of illicit drug crops: crop replacement programs, improvements in physical infrastructure, and introduction of facilities or services designed to improve the quality of life of local residents and improve governance. This means to induce farmers to grow crops other than coca by providing knowledge, materials and facilities than make other crops more attractive. It can also mean providing coca growing areas with roads, schools and other amenities as a means of integration with the rest of the economy, so as to encourage non-agricultural substitute activities. It can also include activities that build local government management capacity and other nation-building activities that increase the government's access and control over zones dominated by guerrilla groups and drug producers. In a more broader sense, it means improving the attractiveness of other areas of the country, so as to induce migration of people out of areas which have comparative advantage in few crops other than coca or opium. In this context, the concept requires an alternative macroeconomic framework that promote diversified economic growth and job creation throughout the national territory, including employment opportunities in rural areas.

It is therefore important to consider solutions which address the immediate problem presented by cultivation while employing a longer term strategy to address the causative factors. The response must therefore include elements of sustainable economic reform. This second component is more complex and long-term in nature both in term of the effort required and the time for results to be realized. It will deal with the broader social and economic issues which contribute to the reasons to participate in illicit cultivation and explore alternatives in crops or other means to generate income.

1.1 Economic Trends

It is clear that coca has always been present in the Peruvian economy. However, today its presence in the economy has been magnified to the extent that the country found itself in a situation of grave socio-economical and political crisis. Therefore, an assessment of the evolution of the coca economy can be described in the following way: from the 1970s to the early 1980s, coca growing concentrated basically in three valleys: Marañon, Huallaga and La Convencion. According to the official registry, there were around 16.000 ha. planted with coca in the mid-1970s. In 1978, around 18.000 ha. were registered, coca cultivation had spread to about fourteen departments. The military government of Morales Bermudez issued in February of 1978 the Ley de Drogas (Decree Law 22095). It became obvious then that illicit coca cultivation had spread to many remote areas in the country. Controlling operatives such as "Green Sea" were started then[8]. In these years, given that the activity was relatively unknown in the country, systems of production and marketing were oriented toward what one might consider mid-size enterprises. This was possible because an export oriented activity had developed in remote areas of the country without risks of any type of law enforcement. It was the beginning of the large migration to the jungle, especially from the Andean areas. Coca growers produced coca leaf; wholesalers processed the leaf into coca paste and cocaine base. It was an economy where a few wholesalers marketed the production of many agricultural producers. In this stage, coca growers used to be very close to the cities who where able to conduct their business very successfully without governmental interference. Firms exported coca paste to Colombia. Cocaine was also produced for local consumption for cities. such as Tarapoto and Tingo María (in the Amazon region).

Within this new structure. the upper jungle became a key gathering point in whose surrounding coca was gathered and coca base was produced. The illicit by-product were transported by roads or rivers to get to the exporting points to finalize the transactions.

From early 1980s to 1989 was characterized by the multiplicity of small coca farming growing units. The law enforcement applied to the coca growing areas triggered dispersion of the activity to many different areas. Andean migrants from Huanuco. San Martin. La Libertad and jungle producers participated in this process. The key city during this phase was Tingo María. but the producing areas were around Uchiza and Tocache. At this stage. there were still many coca growers but they were already learning how to make coca paste. it was the beginning of their agroindustrial integration. It was still profitable to sell coca leaf[9].

This second stage was fostered by the "Green Sea" and "Condor" operatives. Government control forced producers to shrink the size of their operations. Migrants workers came from the upper jungle to the lower jungle. Production sites multiplied. Exports to Colombia and Brazil were consolidated using different routes. Marketing systems with the wholesalers and firms became consolidated. This is the coca boom period when subversion increased and drug-smugglers penetrated the valley[10].

During these two stages. from 1970s to 1989. Peru was in the throes of economic turmoil and near collapse. The inadequate policies applied during those years not only prevented the efficient development of the plentiful natural and human resources of Peru. but led the country into a process of stagnation and downright decadence.

During this period. and especially as a result of the measured adopted by president Velasco between 1968 and 1975 of an economic development model of import substitution. Peru became a protected economy. with inward-oriented growth. and a regime of heavy state intervention. The state controlled many of the basic services. mainly through state ownership and management of the productive sectors through state monopolies in several key areas of the economy. Some examples are large mining concerns. chemical. fertilizers. oil and the petrochemical industries. energy and water supply. fisheries. cement. paper. cellulose manufacturing. iron and steel production. and the export of raw materials. This nationalized and co-operativitised regime restricted foreign investment. and took many other measures that hindered the economic and social development of Peru.

During the 1980s. under the governments of president Fernando Belaunde and Alan Garcia. the Peruvian economy confronted hyperinflation. serious distortions in the structure of relative prices. recession. unemployment and the reduction of worker's real incomes. decreased tax revenues and a persistent fiscal imbalance. increasing financial disintermediation. and the increased flow of drug trafficking. In addition. the decay of the state's institutional apparatus. the deterioration of living standards. and increase in political violence were social correlates of the economic crisis. The state apparatus displayed growing inefficiency. and the government as a whole was progressively weakened in its capacity to respond to the economic decay.

From the analysis of the management and performance of the Peruvian economy during the last two decades specific conclusions can be derived. First. in the early 1980s.

the Peruvian economy was adversely affected by several external shocks, including a sharp decline in the terms of trade and rising international interest rates, which significantly increased the nation's foreign debt burden. Peru's problems were compounded by the ineffective policies of the government of Fernando Belaunde (who was elected president in 1980 after 12 years of military rule) and by a series of natural disasters, including floods, droughts, and changes in the sea currents which affected several hectares of crops nationwide (Phenomenon of El Niño). A 1982 Standby agreement with the IMF failed to stem the tide of economic decline. Nor did a last-ditch orthodox economic program by the Belaunde government succeed in restoring stability. The political result of this was a sweeping victory by the APRISTA social democrat Alan Garcia in the 1985 election.

Second, Alan Garcia's decision to restrict its foreign debt payments to 10% of the country's exports was not cost free. Relations with its creditors, especially with the multilateral organizations, deteriorated and isolated it from the international financial community. Therefore, as part of a drastic change in the economic policy, Peru had to negotiate with its foreign creditors a sustainable way of rejoining the international financial community.

By 1988, the government was bankrupt, and it began to pay its expenses by printing more money. For a while, Peru was virtually blacklisted by public and private international lenders. Exports and national reserves declined, while average income plummeted. In sum, the Garcia administration adopted a policy it thought would encourage rapid economic growth and more equitable distribution of income. But by avoiding fiscal stabilization, it threw the country into deeper crisis and made it more difficult for the poor to live better lives.

Finally. Peru's successive stabilization attempts failed because they did not consistently confront the causes of the macroeconomic imbalances. These failures in the Belaunde and Garcia's administrations increased the inflationary effect and prevented nominal devaluations and nominal adjustments in controlled prices from eliminating the misalignment in relative prices. In fact. the stabilization attempts at the end of the 1980s had an unnecessarily high inflationary and recessionary cost.

In fact. according to the INEI. estimates of unemployment and underemployment went from a 50% level in 1980 to almost 80% in 1990. On the other hand. Peru's gross domestic product declined by over 30 percent during that time. Unprecendented triple-digit inflation early in the decade was followed by staggering four-digit levels. which rose to a peak of 7.650% in 1990[11]. During this period. the acceleration of inflation abruptly reduced the total liquidity of the banking system and the real levels of credit available to the public and the private sectors. The formal banking system began to lack funds to loan. forcing businesses also to resort to curbside credit markets for working capital. This reduction in real credit and increase in its cost had a strong recessionary impact. At the same time. the fluctuations in the parallel exchange rate impeded a complete dollarization of the financial system[12]. Under these circumstances. firms could not make financial plans and the investment and financing options were limited. The banking system's reduced intermediation and the rise of informal financial institutions limited the Central Bank's control on aggregate money supply. The loss of control was accompanied by the deterioration in the ability of the Superintendence of Banks to supervise the behaviour of financial institutions and by an increased risk of bank insolvency.

It was evident that when the government of president Alberto Fujimori was inaugurated on July 28. 1990. Peru was suffering the worst crisis in its modern history.

Hence. Peru urgently needed a consistent economic stabilization program that addresses all causes of its economic crisis. In addition. the extreme deterioration of social welfare and the explosive increase of terrorist violence that killed more than 25.000 people and was responsible for well over US$ 20 billion in property damage has demanded that the restoration of macroeconomic order be accompanied by a social assistance program to ensure an equitable distribution of the stabilization effort. The design of the program must implement policies requiring complex systems of controlling and monitoring economic and social conditions in order to undertake the structural reforms required to pull the country out of its lethargy.

When Fujimori assumed the presidency. he inherited an economy in its third year of four-digit hyperinflation. along with a prolonged recession that had plunged Peruvians' per capita income back to the levels of the late 1950s. In response. he imposed a package of neoliberal reforms with three principal components. The first step was a stabilization program adopted in August 1990 to control inflation and capture revenues needed to renew payments of the debt service. Price subsidies. social spending. and public sector employment were slashed. interest rates and taxes on government services were increased. and exchange rates were unified. producing a de facto devaluation of the currency. A second set of institutional reforms. began in February 1991. was designed to move beyond stabilization toward a market-based restructuring of the Peruvian economy. These reforms included the deregulation of financial and labor markets. a reduction and unification of tariffs. the privatization of public enterprises. and efforts to broaden the tax base and reduce tax evasion. Finally, these market reforms, improving fiscal health, and the resumption of debt-service payments allowed Peru's reintegration into international financial circuits[13].

Under president Alberto Fujimori, Peru has begun to address these major structural problems. A package of reform measures, known collectively as the "Fujishock" program, has attempted to ease the heavily regulated economic environment as well as open the economy to more foreign trade and investment. Fujimori also expanded the property registration program begun by his former advisor Hernando de Soto to legitimize peasant landholders in the rural areas, seeking to confer incentives for growing alternative crops. This initiative represented a significant breakthrough in attempting to integrate the informal sector into the formal economy. Progress has been achieved, but major problems remain.

This structural adjustment was harsh medicine for an economy that had already suffered through a prolonged crisis, with devastating effects upon popular living standards. After losing 800.000 jobs in the 1988-89 economic crisis, employment declined by another 13.9 percent in industry, 13.7 percent in services, and 21.8 percent in commerce in the first eighteen months under Fujimori[14]. Inflation, which had been running at about 40 percent per month, shot up to 398 percent in August 1990, before declining sharply to 3-5 percent per month in late 1992 and 1-2 percent per month in 1994. The number of Peruvians living in poverty rose to 55 percent of the population in the aftermath of the "Fujishock" (see Charts 1.1.a and 1.1.b: poverty is falling since 1994): the percentage of the workforce considered underemployed or unemployed rose from 81.4 percent in 1990 to 87.3 percent in 1993; the informal sector grew from 45.7 percent of the workforce in 1990 to 57 percent in 1992; and real wages fell by 40 percent between 1990 and 1992, to 33 percent of the 1980 level in the private sector and 9 percent in the public sector. A decade-long trend toward increasing inequality also continued: the share of the national income represented by wages declined from 46.7 percent in 1980 to 19.9 percent in 1990 and 13 percent in 1992, whereas the share represented by profits rose from 25.9 percent in 1980 to 49.3 percent in 1990 and 54.5 percent in 1992[15]

Chart 1.1.a: Measures of Poverty, 1994

	1985	1991	1994
Not Poor	62%	45%	52%
Poor	38%	55%	48%
Extreme	15%	24%	18%
Non-Extreme	23%	31%	30%

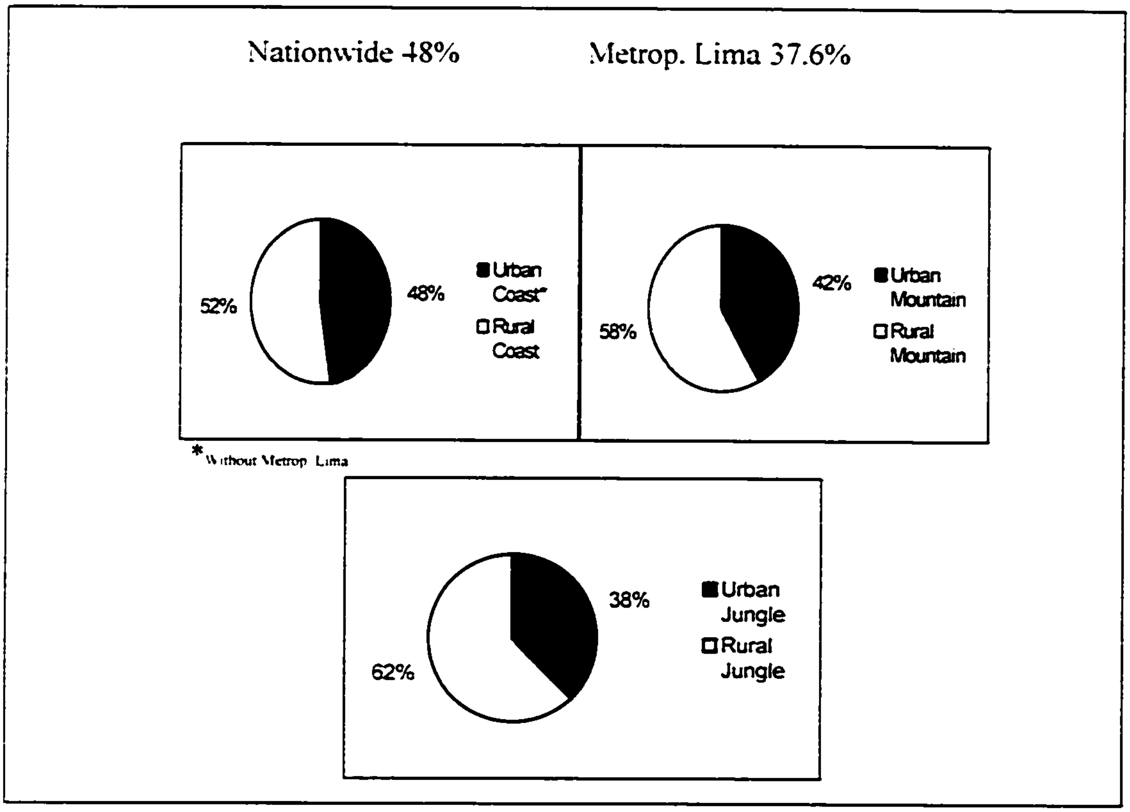
Source: Instituto Nacional de Estadística e Informática, Perú, Reporte Anual, 1996.

As such, the only significant economic gain for popular sectors in the early years of structural adjustment was the sharp decline in the inflation rate, which fell from 7,650 percent in 1990 to under 20 percent in 1994. This gain was significant, as popular sectors were especially vulnerable to hyperinflation, given the inefficacy of wage indexation and the inability of the poor to protect income levels by holding foreign currency or sending capital abroad. But if stabilization reduced economic uncertainty, it was achieved at the cost of significant economic contraction and reduced consumption.

Despite an enhanced government socio-economic commitment in 1990, the government's political will into action in narcotics producing areas was slow and uneven. Its ability to control coca cultivation, processing, and export was limited by terrorism, lack of resources, economic depression, the government's implementation of the drastic economic reform and stabilization program, the debilitation of official institutions, especially, the judiciary, and widespread corruption that impedes his reform program and narcotics law enforcement in order to disrupt Peru's illegal drug industry and the escalating threat of the terrorist movement.

Therefore, on April 5, 1992, president Fujimori, with the support from the military, pulled off a self-coup. The coup was a direct response to the institutional paralysis of Peruvian democracy and reflected the absence of institution building in the previous democratic governments.

Chart 1.1.b: Distribution of Poverty: 1994



Source: Instituto Nacional de Estadística e Informática. Perú. Reporte Anual. 1996.

He at once announced the dissolution of the national parliament and regional governments and a reorganization of the judiciary system, threw several opposition leaders and senators in jail or put them under house arrest, and suspended the Constitution. As head of an Emergency and National Reconstruction Government, he ruled by decree until the election of a Constituent Democratic Congress (CCD). which would frame a new constitution. Eventually. he said. the country would return to democracy. but that in a context of a worsening economic situation and growing terrorist violence. this was a necessary evil required to put the country back on track.[16] Democracy. according to Fujimori. as well as to over 65 percent of the population that supported the coup. had proven inadequate in handling the problems of corruption. drugs. terrorism. the economy. and ineffective government. Furthermore. his neoliberal program was supported by a coalition of interests. including the military. civilian technocrats. international financial agencies. and domestic business groups. The underlying consensus among these interests was that neoliberal policies had to be adopted and that such an action required a strengthened state apparatus to be effective[17].

Strong support continued in Peru. especially in September 1992 when the founder and leader of the Shining Path. Abimael Guzmán. was captured along with other Sendero leaders. Fujimori also shored up additional support by advocating a more hard-line approach to terrorist and drug trafficking criminals. Fujimori's solution of imposing the death penalty and life sentences to criminals after trials that can be as short as three hours is hailed as a direct reason for the decline in terrorist violence by many Peruvians.

As promised. Fujimori called a Constituent Democratic Congress in 1993 to draft a new Constitution. which was approved on October 31. 1993. The new constitution strengthened Fujimori's authority and allows him to run for re-election in 1995. The vote was seen by many to be a referendum on Mr. Fujimori's three-year rule as well as a vote of confidence for his actions of April 1992[18].

Was the coup a necessary step as Fujimori has insisted? Francisco Sagasti. a respected commentator. argues that Fujimori's self coup was unjustified because the laws needed to fight terrorism and inflation were already in place. Another observer commented that the Congress. in order to demonstrate its confidence in the Fujimori's new government in 1990. had already granted him extraordinary legislative powers which enabled him to launch his Fujishock. or stabilization program[19].

Fujimori had found democratic institutions. such as the Congress. a hindrance. and showed obvious disdain for democratic procedures: yet. due to international pressure. divisions within his own coalition. and the failure to solve pressing social and economic problems. he has also discovered that developing formal authoritarian structures are limited. Pressured into creating a new constitution. Fujimori nonetheless oriented the new constitution to further solidify his power. The new constitution strengthened the powers of the executive. created a unicameral legislature that can be dismissed by the president. increased executive control over the judiciary. included a clause allowing presidential reelection. and also. implemented all of Fujimori's decrees that had not been passed by the former Congress. In other words. Fujimori created an institutional void by destroying democratic institutions yet built nothing in its place. leaving the underlying causes for poverty. unequal distribution of income. and other social problems unaddressed. In fact. some scholars argue that even evaluated in strictly economic terms. Fujimori's program has largely failed to achieve its stated goals: poverty and inequality had worsened. Meanwhile political institutions were rendered incapable of helping the situation[20].

In general terms. growth in GDP. which had been negative by the end of the 1980s in the order of –8.4%. -11.8% and –4.1%. was positive in 1991 and registered and increase of 2.6% and then fell to –1.8% in 1992. By 1993. however. Fujimori's strategies began to change slowly. as a resumption of economic growth and tax reform. which has encouraged an increased in the activity levels through higher corporate and consumer confidence. the attraction of more foreign investment and the start of the privatization program. as well as a restoration of ties to international lending institutions. alleviated fiscal constraints. As a result. Peru's economy grew 13.0% in 1994. 6.9% in 1995 and 2.8% in 1996[21]. The sectoral breakdown of the economy shows the areas in which the turnaround from recession has been most notable (see Table 1.1.a).

Taking a three years view. Peru has had the highest GDP growth in the region. Although this represents a significant recovery from current levels of growth. the government is confident about the future because of the high level of investment (over 23% of GDP) and the likelihood of a recuperation of some sectors that did relatively poorly in his first three years in power[22].

Chart 1.1.c: Macroeconomic Variables

	1990	1991	1992	1993	1994	1995	1996
Real GDP Growth (%)	-2.3	2.4	-1.8	6.5	13.0	6.9	2.8
Inflation (%)	7,650	139.2	56.7	39.5	15.4	10.3	11.8
Exports (US$ m)	3,323	3,391	3,534	3,515	4,555	5,580	5,785
Imports (US$ m)	2,930	3,530	4,090	4,085	5,575	7,690	7,890
Trade Balance (US$ m)	393	-139	-556	-570	-1,020	-2,110	-2,105
Current Acc. Deficit (% of GDP)	3.8	3.6	5.0	5.6	5.3	7.3	5.9
Balance of Payment (US$ b)	-1.52	33m	-310m	647m	1.9	528m	-41m
Net Foreign Reserves (US$ b)	-143m	1.93	2.4	2.9	6.0	6.7	8.8
External Debt (US$ b)	22.85	25.44	26.61	27.48	30.22	33.51	33.51
Foreign Investment (US$ b)	1.3	1.4	1.5	2.4	6.1	7.6	9.9
Devaluation (%)	3,748.50	86.7	62.3	32.6	-0.7	8.5	10.8
Unemployment (%)	8.3	8.7	9.4	9.9	8.8	7.4	9.2
Real Minimum Wages(US$)	48.1	31.80	97.25	45.12	59.5	56.4	53.9
Social Expenditure (% of GDP)	3.2	4.5	4.5	5.0	6.0	7.5	7.8

Source: Instituto Nacional de Estadística e Informática. Perú. Reporte Anual. 1996.

Just as in 1994. construction was the leading sector of the economy in 1995. with an expansion of 17.6%. There has. however. been a significant slowing down and growth in 1996 was negative. Services have also had a good year. again with a notable deceleration at the beginning of this year. A similar scenario has occurred in manufacturing and agriculture. but they have been accentuated by the poor performance of fisheries and cheap food policies. respectively. With the fishing sector contracting by 14.6%. the main Peruvian exporting product. fishmeal has seen a 7% drop in GDP. Moreover. mining has had a disappointing years in 1995 and 1996 because the decline of oil production. but metal output has risen slightly. Definitively as it can be seen in Table 1.1.a. the rate of expansion of GDP has slowed both because of the deliberate efforts to restrain demand. but also because of specific sectoral trends that are unrelated to the overall level of demand[23].

Table 1.1.a: GDP Growth by Sector

	1988	1989	1990	1991	1992	1993	1994	1995	1996	Jan-March 97
Agriculture	4.90	-3.60	-9.00	2.20	-7.40	6.20	13.20	7.40	8.30	20.60
Fishing	17.20	5.20	-4.40	-11.60	12.70	13.30	31.40	-14.60	6.10	-11.30
Mining	-18.60	1.70	-4.20	-1.70	-3.30	8.90	4.30	2.30	2.80	2.50
Manufacturing	14.20	-17.60	-5.80	7.70	-2.40	3.60	17.10	4.50	2.70	2.70
Construction	-5.40	-15.90	3.30	-1.10	4.00	14.00	34.70	17.60	-4.60	9.80
Government	-10.10	-13.70	-3.90	2.80	3.10	-0.10	0.10	0.20	0.40	-0.70
Other	-6.80	-11.80	-4.50	1.30	-1.20	4.80	10.80	6.10	3.90	4.30
GDP	-8.40	-11.80	-4.10	2.60	-1.80	5.60	13.00	6.90	2.80	4.80

Source: Instituto Nacional de Estadística e Informática. Perú. Reporte Mensual. April. 1997.

The favourable economic trend will be reinforced by a drop in inflation from 11.9% in 1996 to an approximately 10.0% in 1997. Projections for this year's growth is approximately 5%. lead by higher mining output and increase construction and agriculture activity.

Due to this growth trend. the government began to spend on social emergency programs (see Chart 1.1.d). The government had initiated ten thousand small-scale projects in agriculture. health care. education. sanitation. nutrition. transportation. and microenterprise promotion in an effort both to provide public services and to generate new employment. A new residential infrastructure program was also expanded to begin housing construction. and Fujimori sharply increased the pace of his visits to poor communities to inaugurate public works projects[24].

The question here is also to determine how the impact of the stabilization program and the structural reforms have affected the narco-economy in Peru.

Chart 1.1.d: Social Expenditure in real terms:1990-1995 (US$ MM)

	Social Expenditure*	GDP	% of GDP	% of Total Expenditure*
1990	980	30319	3.2	20.9
1991	1877	41995	4.5	23.4
1992	1902	42240	4.5	27.3
1993	2036	40954	5.0	32.0
1994	2899	50083	6.0	35.3
1995	4264	56532	7.5	40.9

* It includes IPSS

Source: Ministry of Finance. Budget Office. 1996.

According to Humberto Campodonico. member of the Centro de Estudios y Promoción del Desarrollo (DESCO). the liberalization process accompanied by the suppression of credit to the agriculture sector. a lack of land reform. budget austerity. and unconsolidated financial reform process occurred since the early 1990s have had direct effects on the coca-by product export (see Chart 1.1.e). when the dollars obtained from the higher illicit exports are now easily cashed without any control and used by drug-traffickers to buy goods and services. such as trucks and automobiles. electronic and electrical appliances. real estate and companies. or else the illicit coca proceeds can be monetized into other financial assets or securities (see money laundering)[25].

Chart 1.1.e: Peru: Export of Coca Leaf. 1985-1994 (kgs.)

Year	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
Coca Leaf	23.700	45.400	46.400	2.000	-	-	46.000	46.000	63.000	69.000

Source: ENACO S.A.. Memoria 1993 (Lima 1993). and Budget and Operative Plan 1994.

When the exports of the coca by-product are cashed into dollars. increase the money supply. and these dollars are channeled into the real productive and financial sectors of the economy. it becomes more difficult to measure the full impact of exports of illicit drugs in the capital accounts. This is so because it is not easy to determine the percentage of the money supply that comes from cashing dollars related to coca exports. The measurement of the impact is made more difficult because those dollars that come into the productive sector of the economy are multiplied into other demands for other goods and services that are supplied in different markets. Furthermore. the rest of the drug-dollars that are cashed into the financial sector are also multiplied through the money multiplier process into larger money supplies that when monetized feed again the multiplier process through new demands of goods and services.

How far has the impact of the macroeconomic changes affect the illicit production and trafficking of coca by-product industry? This is an important question which is not easy to answer. However. it stresses an aspect of the illicit sector that needs to be fully analyzed. There is not much information conveyed in the approach based on the ratio coca by-product value added and GDP. Information is poor because of measurement errors. and because it only gives a very rough indication of direct effects. Consider the following scenario in Table 1.1.b.

Table 1.1.b: Coca by-product exports related to macroeconomic variables

	EX	C/Y	A	B	C	D	E	F	G
1987	1,366.0	52.0	52.0	3.7	48.3	173.0	121.0	-	29.0
1988	1,196.0	628.0	628.0	4.1	623.9	621.0	-7.0	-	46.0
1989	918.0	2,510.0	2,510.0	4.8	2,505.2	1,300.0	-1,210.0	-	29.0
1990	532.0	6,761.0	7,650.0	5.4	7,644.6	3,748.0	-3,902.0	-	43.0
1991	1,005.0	410.0	139.0	4.2	134.8	86.0	-53.0	3.0	40.0
1992	960.0	73.0	56.0	3.0	53.0	62.0	6.0	209.0	162.0
1993	686.0	49.0	39.0	3.0	36.1	32.0	-7.0	317.0	152.0
1994	682.0	24.0	15.0	2.6	12.4	-0.7	-15.7	2,619.0	3,084.0
1995	540.0	11.0	10.0	2.6	7.4	8.0	-2.0	1,059.0	2,083.0

Source: Data provided by Central Bank of Peru and U.S. Agency for International Development/Peru. Drug Enforcement Administration. UNDCP Office in Peru.

EX : Exports of coca by-product in million of dollars.
C/Y : Ratio (%) of coca by-product exports over GDP.
A : Inflation rate in Peru
B : Inflation rate in the U.S.
C : Difference between rates of inflation in Peru and U.S.
D : Percentage change of the nominal exchange rate=rate of devaluation
E : Difference between the rate of devaluation and the rate of inflation in Peru.
F : Selling proceeds from privatization of enterprises (million of US dollars)
G : Direct foreign investment (million of US dollars)

Table 1.1.b shows that coca exports and its share (C/Y) to GDP fell significantly from 1987 to 1990 while there was substantial inflation (A) and a large difference (C) with regards to U.S. inflation that fueled devaluation (D) in the Peruvian economy. The increasing difference of inflation was partly due to monetization of coca exports proceeds (EX).

On the other hand, the rate of devaluation lagged well behind that of the Peruvian inflation during the years 1988-1992 of higher coca exports inducing the so-called appreciation of the real exchange rate as shown by the negative value of the variable (E). This happened again in 1994-1995 notwithstanding the relatively large capital inflow from privatization (F) and direct foreign investment (G)[26].

Foreign direct investment never reached a value higher than that of foreign exchange coming from coca exports, except for the years 1994-1995. However, the impact of foreign investment was not strong enough to dominate the alleged real appreciation of the Peruvian unit currency that appears associated to coca exports proceeds.

The importance of the illicit sector can neither be determined nor assessed by simply looking at a declining coca by-product sector ratio (C/Y). There are indirect effects of coca exports trafficking realized through the derived demands of traffickers. Traffickers demand other goods and services with cleaned dollars. These indirect effects unfold and multiply over time but are not openly revealed in the market nor duly registered as demands of good and services induced by coca export impact.

There is a debate in Peru that the capital inflows from direct foreign investment and privatization are the main factors causing the real appreciation of the exchange rate in the last two years. There is however not enough data to prove such claim. Real appreciation seems to be decreasing as shown in Table 1.1.b compared to the levels obtained in 1989-1990. There is an estimate of US$ 3.670 million of proceeds from privatization versus US$ 1.320 million of cocaine exports for 1994. However, that does not mean that privatization proceeds are a main determinant of the exchange rate since these flows are channeled to public work, poverty programs and the construction sector. In contrast, and although a smaller amount as compared to previous years, cocaine exports are transformed through the process described above into clean liquid monetary expansion and securitized assets that are eventually also monetized and injected to the system.

Apart from capital inflows due to privatization that reached US$ 2.619 million in 1994, there were other important capital inflows in the same year. Direct foreign investment accounted for US$ 3.084 million; portfolio investment reached US$ 465 million and long-term capital via balance of payments, US$ 3.652 million. These flows give a total of US$ 9.820 million. Obviously. such flows had an impact on the accumulation of foreign exchange and thus on the exchange rate. However. total international reserves in 1994 only reached US$ 6.025 million. Where did the remaining US$ 3.795 million go? Obviously. there was important capital flight which offset the inflow of foreign investment which supports the argument that the impact of the coca export is not negligible in Peru.

According to an official source[27]. the current account deficit- a measure of its trade in goods. services and investments - was nearly 6.0% of gross domestic product last year. and the country is one of the most indebted in Latin America. The projected current account deficit of 5.6% of GDP in 1997 may not be sustainable and will require heavy reliance on external capital. especially as the proceeds from the highly successful privatization program shrink. The government has recently implemented the so-called Foreign Investment Status. which. among other things. secure equal treatment for Peruvian and non-Peruvian investors and allow foreign investment in any form as well as the repatriation of profits. The government also announced an acceleration of its privatization efforts. principally in the mining sector. Thus. Peru should continue to experience abundant inflows of foreign capital expected to reach between US$ 1 and US$ 1.5 billion throughout 1997 and 1998[28].

In this context. since April the fifth to the present. with the new anti-narcotics and anti-terrorist legislation. different laws. decrees and other legislative instruments have been approved aimed at controlling money laundering. diversion of chemical substances. small-scale drug pushing. poppy cultivation. and other related activities[29]. The Fujimori government approved several decrees and resolutions recognizing alternative development as the appropriate mechanism for the control of coca cultivation and export. specifying that coca farmers are the valid interlocutors in the rural rehabilitation process. In this sense. the National Plan for Drug Prevention and Control. 1994-2000. was officially approved in October 1994. and envisages. inter alia. a new institutional framework and a central governmental counterpart for the coordination of drug control. The setting up of the new institutional framework is the first step the government is currently taking to implement the National Plan. A working commission conformed by the Ministries of the Presidency. Defence. Economy and Finance. Interior. Justice. Health. Agriculture and Education. was installed through a Supreme Resolution in July 1995 for that purpose. The country's strategy as reflected in the Plan focuses on the following five key priorities areas: (i) effective legal and institutional framework. (ii) prioritization of alternative development to reduce coca production. (iii) law enforcement activities in coca producing areas. (iv) community mobilization for drug demand reduction. and (v) provide a proper national institutional setting for drug control[30].

This section has focused on economic development and its relationship with drug trafficking issues in Peru. Its strategic economic roles in the illegal industry have made the nation a principal focus for anti-drug policies in the Western Hemisphere. Discussion of the subject should not be limited to an ethnographic account of the processes. thus. this research will critically explore in the next two sections the significance of the coca leaf and coca paste in the main economic aspects and the problems. strategies and solutions to attack drug trafficking in Peru.

Notes

[1] "*Global Economic Prospects and the Developing Countries*". The World Bank (1995). See also *International Trade-Trends and Statistics*. World Trade Organization (1995).
[2] INEI. "*Peru: Statistics of Production, Trafficking and Consumption of Drugs. 1994-96.*" Lima. February 1997.
[3] Carlos E. Percovich. "*Money Laundering*". Lima. 1996.
[4] Office of National Drug Control Policy. "*National Drug Control Strategy. 1990*". U.S. Department of State. Washington D.C.
[5] See Ethan A. Nadelmann. "*Latinoamérica: Economia Política del Comercio de Cocaina*". September-December 1986. p. 27-49.
[6] Francisco Thoumi. "*Economia. Política y Narcotráfico.*" Bogota: TM Editores. 1994.
[7] Mario de Franco and Ricardo Godoy. "*The Economic Consequences of Cocaine Production: Historical, Local and Macroeconomic Perspective.*" Harvard University. 1991.
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[12] Carlos E. Paredes and Jeffrey D. Sachs. "*Peru's Path to Recovery. A Plan for Economic Stabilization and Growth*" (Washington. D.C.: The Brooklings Institution. 1991). p. 83.
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[14] *Peru Country Profile. 1992-93* (London: Economist Intelligence Unit. 1992).
[15] Data are taken from the Compendio Estadistico del Banco Central de Reserva. 1993.
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[19] E. Gonzales. "*Economic Stabilization and Structural Adjustment Under Fujimori.*" Journal of Interamerican Studies and World Affairs. Vol. 35. No.2 (Summer 1993).
[20] Ibid. p. 75.
[21] Instituto Nacional de Estadística e Informática. "*Perú. Reporte Mensual*". Abril. 1997.
[22] Banco Central de Reserva. "*Memoria 1996*". Lima-Perú.
[23] Modest growth was seen in all sectors. in the first quarter of 1997. except fishing and government which fell 11.03% and 0.7% respectively. The volatile fishing sector posted this decline due to the yearly indefinite fishing ban. Economic activity in this period was led by growth in agriculture (20.6%). construction (9.8%) and commerce (4.3%). Although growth will accelerate relative to the recent trough registered last year. the expansion will fall well short of the double digit pace recorded earlier in the 1990s with the consolidation of the stabilization and privatization program.
[24] Ministerio de la Presidencia. "*Igualdad de Oportunidades para un Desarrollo Sostenido. Estrategia Focalizada de Lucha contra la Pobreza*". Lima. 1996.
[25] Humberto Campodónico. "*Importancia Económica del Narcotráfico y su relación con las Reformas Neo-liberales del gobierno de Fujimori*". Lima. 1994.
[26] "*Memoria 1996*". Lima-Peru.
[27] Instituto Nacional de Estadística e Informática. "*Perú. Reporte Anual*". 1996.
[28] "*The Peruvian Enterprise Project.*" CONFIEP. January 1996.
[29] Compared to the Ley General de Drogas law No. 22095 of 21 February 1978 which is the main legal instrument for drug control in Peru aimed at the repression of illicit drug trafficking. rehabilitation of drug-addicts. and reduction of coca cultivation. Since its approval. modifications have been affected. especially

due to the approval of a new penal code in 1991 that stipulates harsher penal measures for coca cultivation and trafficking.

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II. Part One
Defining the Problem

2.1 Significance of the Coca Leaf and Coca Paste in the Main Economic Aspects

The purpose of this section is to examine the main features of the production-chain for cocaine. from the cultivation of coca leaves to the export of the finished drug (cocaine hydrochloride) from the Andean region. It will also deal with its distribution and marketing. including statistics and comparative data and. finally. what it offers for many farmers in the Andean region.

2.1.1 Production of Coca and Coca Paste

Long before the world economy felt the impact of globalization of money. markets and products. illicit drugs moved internationally from producer countries in less developed areas of the world to consumer countries that were usually more developed. Production in rural areas was transported to and sold in other continents after large price increases along the way. providing high profit and risk incentive to traffickers (See Map 1).

Many experts think that the first stage. when plants are grown in the fields or consumable drugs are produced in the laboratory. is the most vulnerable point in the chain of illicit production. distribution and consumption. The second major stage. the distribution phase. is also considered by some as an equally good intervention point for drug control purposes. However. the potential for easy movement. disguise and diversion of drug shipments and the vast numbers of shipments of small quantities of drugs decrease the yield of enforcement for each unit of intervention effort. The third stage of possible intervention and often target of law enforcement is at the time of consumption. Here, a particularly vulnerable point is when drugs pass from dealers to consumers.

Estimates of illicit drug production come from several sources. Systematic attempts to provide information about the amount of drug produced may employ high technology satellite mapping, ground survey, agronomic characteristics or consumption figures.

New regions have enter into the production of opium, coca and marijuana, as a result of the displacement of other agricultural crops. Table 2.1.1.a provides gross estimates of the major supplier of these illicit drugs since the 1990s.

Since some drugs are more available and used more often than others, the questions that arise are the following: what properties of specific drugs, what personal characteristics of the users and what social or cultural factors in a given country influence the attractiveness of a drug?. Or, in another way, why do users want certain drugs as opposed to others and how does this influence their willingness to pay for them? Studies suggest that production and distribution of illicit drugs follow supply-demand principles with some allowance for the illegal nature of the product. In terms of its impact on global drug problems and its large scale financial implications, coca-cocaine is the primary drug of current interest.

Erythroxylon coca is a variety of shrub native to the tropical slopes of South America, but is now found in other parts of the world with climates similar to the Amazon tropics[31].

Table 2.1.1.a: Worldwide Potential Net Production 1994-1991 (metric tones) and Worldwide Cultivation Totals (Hectares)

Country	1994		1993		1992		1991	
	Cultivated	Production	Cultivated	Production	Cultivated	Production	Cultivated	Production
Opium								
Afghanistan	27,860	600	27,420	570	23,515	415	17,190	585
Iran	21,530	300	19,310	300	17,428	385	12,740	300
Pakistan	165	125	12,540	180	11,660	165	8,645	130
Total	49,555	1,025	59,270	1,050	52,603	965	38,575	1,015
Burma	2,587	2,250	18,501	2,350	172,910	2,250	161,102	2,430
Laos	285	250	33,624	265	31,550	275	29,625	375
Thailand	40	32	7,589	35	7,093	40	4,200	50
Total	2,912	2,532	59,714	2,650	211,553	2,565	194,927	2,855
Colombia	18	15	2,576	27	2,454	22	2,316	19
Lebanon	64	51	3,812	46	3,631	40	3,400	34
Guatemala	15	10	1,875	17	1,820	13	1,721	12
Mexico	85	55	11,329	41	10,980	62	10,310	66
Total	182	131	19,592	131	18,885	137	17,747	131
Total Opium	52,649	3,688	138,576	3,831	283,041	3,667	251,249	4,001
Coca Leaf								
Bolivia	41,000	44,100	40,000	43,800	43,884	52,800	54,386	60,600
Colombia	51,620	40,800	50,000	40,600	48,038	39,100	43,472	35,900
Peru	108,600	163,300	108,800	155,500	129,200	223,900	132,500	121,500
Ecuador	120	100	112	40	130	170	120	270
Total Coca	201,340	248,300	198,912	239,900	221,252	315,970	230,478	218,270
Marijuana								
Mexico	28,690	7,000	26,854	7,775	25,650	19,715	28,710	30,200
Colombia	2,457	1,500	2,156	1,500	1,870	1,500	2,000	2,800
Jamaica	650	600	1,875	641	1,650	825	1,783	190
Belize	110	50	86	49	275	60	320	65
Others	3,890	3,840	3,680	3,658	3,550	3,320	3,700	3,500
Total Marijuana	35,797	12,990	34,651	13,623	32,995	25,420	36,513	36,755

Source: INCB. Report of the International Drug Control Board. 1975-95; INCSR. International Narcotics Control Strategy Report. 1988-96. DEA. Illegal Drug Price/Purity Report 1994.
Several of these figures are rough estimates which may be disputed.

There are 250 species and four major varieties grown on the eastern slopes of the Andes in Peru and Bolivia in conditions ranging from poor to fertile soils, tropical or dry climates, flat lands or steep slopes and at altitudes ranging from 200 meters to 2000 meters above sea level.

Peru has often been cited as a classic example of an export-led economy. The celebrated guano age in the mid-nineteenth century made Peru a monoproduct export economy that failed to achieved self-sustaining growth. The rubber boom in the 1890s and 1900s had its impact in the jungle region. with little effect on the remainder of the country[32]. Rather. coca has always conditioned the culture and economy. Many local economies that generated revenues for the national government functioned around coca trade. Before the advent of modern communications. it was the Andean montañero's role to bring coca up to the highlands. Although this ecological movement of coca still continues. new types and methods of trade have evolved with the rush of cocaine production to satisfy international demand.

Prior to the cocaine boom. there were two kinds of montañeros in the highlands: the commercial voyagers who went to the forest to bring coca. coffee grains. and fruits to sell to local merchants in small towns and cities: and peasants who went occasionally to the closest coca fields to buy one or two arrobas (1 arroba=11.5 kgs) of coca. mostly for their own use. The former took food from the highlands to the jungles in order to trade for coca. Because of government control. the number of commercial travelers has diminished tremendously. However. peasants from remote rural areas have increased the frequency of their trading trips to the foothills of the Andes so much that they are becoming dependent on the new coca economy[33].

Change first came to this ancient social system in the 1950s. when the Peruvian government initiated a program to encourage migration from the overcrowded coastal cities to the scarcely peopled forests along the eastern slopes of the Andes. Most of this colonization took place in the province of Leoncio Prado. of which Tingo María. located in the heart of the coca belt. is the capital. The government sponsored plantations of tea. coffee. and tobacco did not yield anything close to the returns that the new colonist expected. so they turned their lands to the traditional and easy crop. the coca. It was a good time to cultivate the plant. The boom in cocaine use had begun in industrialized countries. so growing numbers of cocaine processing hideouts in the forest stood ready to absorb the increased production of coca[34].

Until the sixties. coca was mostly produced for traditional chewing. The Peruvian government established an official bureau to control coca agriculture and to collect tax revenues from coca trade. This agency. Estanco de la Coca. was a subdivision of the Department of Treasury. Tax collectors were posted in towns and strategic locations where the movement of montañeros could be controlled more effectively. Several old-time travelers asserted that. in addition to paying their taxes. the peasants were forced to work for the tax collectors. Many government employees themselves were coca planters and legal cocaine manufacturers. Up in the highlands. the collectors made the travelers labor in the fields or do private construction work. Once the travelers sold their coca to the stores. retailers paid another excise tax. By 1972. the Estanco de la Coca disappeared and the National Bank took over coca-tax collection. Later. the National Coca Enterprise (ENACO) was organized. and it was announced that distribution and sale of coca was free of taxes. As local farmers turned their land to coca cultivation. production of the coca leaf increased rapidly since then[35].

It is essential to understand the reasons for illegal coca expansion because many of these factors still persist and could lead to the resurgence of this activity. Aside from strong external demand and Peru's comparative advantage for coca production. there are internal reasons for the expansion of coca. One concerns a pattern of agricultural development that has yield very low levels of income in the Andean region. where the majority of the farms are of less than 5 hectares. As a result. Peru has levels of poverty comparable to those in the least developed areas of Asia and even Africa. Studies estimate per-capita income for Andean peasants at around US$ 50/month[36]. In addition. food consumption patterns in Peru have undergone drastic change. The traditional emphasis on Andean goods (sweet. potato. barley. soft maize. soft wheat) has gradually been replaced by a more westernized diet in the urban areas (rice. white potato. chicken. dairy products. bread. noodles. and other processed foods). Thus. in the last decades Andean farmers have faced a declining market for the type of foodstuffs they can produce within the ecological zones they inhabit as well as the import of food staples initiated in the military government of president Velasco. increasing dramatically in the early 1980s and continued under president Fujimori. As a result. profitability for most of the agricultural sector sharply declined and coca production earnings rose[37].

Castro Pozo argues that. during the last two decades. transformation of the Andean society and culture at large is more evident. and its western direction is inevitable. These changes may be the result of conscious and unconscious policies of land distribution and population control in the country at large. However. the land reform that was designed to create equal distribution of land further impoverished the peasantry due to topographic variations. low temperature. drought. especially on the western Andes. lack of capital investment and technical support. and marketing obstacles[38]. The highland agriculture frontier did not work. causing Indian and peasant populations to search for other sources of subsistence as it was mentioned above.

Peru. Bolivia and Colombia account for 95 percent or more of the world's production of coca[39]. One of the most widely quoted estimates has come from Rensselaer Lee III:

"In the mid-1980s. SouthAmerican cocaine traffickers probably earned between USS 5 and USS 6 billion dollars annually from international sales in the U.S. market. Perhaps USS 1.5 to USS 2 billion flowed to the cocaine-producing countries. Viewed in terms of repatriated dollars. cocaine exports are equivalent to an estimated 10 to 20% for Colombia's legal exports. 25 to 30% of Peru's. and 50 to 100% of Bolivia's. Cocaine is almost certainly the most important export in Peru and Bolivia. although in Colombia it probably earns less than coffee and petroleum"[40].

As it can be seen in Table 2.1.1.b diverse information is shown for the years 1975. 1980. 1985. 1990 and 1993. for Peru. Bolivia and Colombia.

The information covers the area under cultivation: production of coca leaf. coca paste. and cocaine: the price paid to the producers for the leaf: the number of people directly and indirectly employee: and the number of drugs users. The main conclusions are: (a) cultivation rose constantly. (b) the tendency is for the price to the producer to fall. and (c) there is an increase in traditional consumption. but also by drugs users.

Tables 2.1.1.c and 2.1.1.d show that only 3.8 per cent of the value produced by the coca-cocaine complex in Colombia. Peru and Bolivia stayed in those countries. The rest remained in the countries of the North. essentially the United States. but also in Europe. It goes without saying that the proportion remaining in the producer countries. between 5 and 8 percent between 1985-88. is very similar to that for legal primary products such as coffee. cacao. cotton. or bananas.

Table 2.1.1.b: Basic Indicators on Coca and Drugs Trafficking in Bolivia. Colombia and Peru. 1975-95.

Country and Year	Ha. under coca (000s)	Prod. of Leaf Tons (000s)	Prod. of Coca Paste Tons	Prod.of Cocaine Tons	Price of coca leaf ($/kg)	Direct Involvement (000s)	Indirect Involvement (000s)	Consumer of leaf (000s)	Consumer of drugs (000s)
Bolivia									
1975	11.3	9.6	11	6	2.00	15.0	50.0	2000.0	50.0
1980	22.8	19.3	22	12	2.00	35.0	100.0	2300.0	80.0
1985	44.3	37.5	42	23	2.00	65.0	200.0	2600.0	100.0
1990	58.4	64.0	119	64	0.55	90.0	260.0	3200.0	130.0
1993	40.0	43.8	81	44	1.00	60.0	180.0	3500.0	150.0
1995	41.6	45.3	84	42	1.05	68.0	195.0	3700.0	165.0
Colombia									
1975	1.0	0.7	18	20	1.50	1.0	5.0	50.0	200.0
1980	3.5	2.4	63	67	1 .50	4.0	15.0	45.0	250.0
1985	15.5	10.8	283	303	2.00	15.0	90.0	40.0	280.0
1990	41.0	33.4	402	487	0.55	40.0	200.0	35.0	300.0
1993	50.0	40.6	489	569	1.00	50.0	250.0	30.0	330.0
1995	52.0	42.7	509	592	1.05	54.0	275.0	27.0	354.0
Peru									
1975	19.0	20.9	62	6	3.00	40.0	100.0	3000.0	100.0
1980	40.5	44.5	132	13	3.00	80.0	240.0	3250.0	110.0
1985	95.2	90.5	269	27	2.00	190.0	570.0	3500.0	130.0
1990	132.5	121.5	315	32	0.70	270.0	750.0	3750.0	140.0
1993	108.8	155.5	256	43	1.00	370.0	1000.0	4000.0	150.0
1995	115.3	207.5	273	67	1.19	470.0	1500.0	4250.0	165.0
Total									
1975	31.3	31.2	91	32	2.17	56.0	155.0	5050.0	440.0
1980	66.8	88.2	216	92	2.17	119.0	355.0	5595.0	440.0
1985	155.0	138.8	593	353	2.00	270.0	850.0	5140.0	510.0
1990	231.9	218.9	836	563	0.60	400.0	1210.0	6985.0	570.0
1993	198.6	239.9	826	656	1.00	480.0	1430.0	7530.0	630.0
1995	208.9	295.5	866	701	1.09	592	1970	7977	684

Source: INCB. Report of the International Drug Control Board. 1975-95: INCSR. International Narcotics Control Strategy Report. 1988-96. DEA. Illegal Drug Price/Purity Report 1994.
Several of these figures are rough estimates which may be disputed. The heading of consumer drugs does not include social drugs like tobacco and alcohol.

Table 2.1.1.c: Production of Coca Leaves. Coca Paste and Cocaine. Plus Prices and Income Generated. For Bolivia. Colombia and Peru. 1985-95.

Country and Year	Income to Internal market ($m)				Income to Intermed.			Price per Kg ($ million)			Production (tonnes)		
	Leaf	Coca Paste	Cocaine	Total	Port	Street	Total	Leaf	Coca Paste (000s)	Cocaine (000s)	Leaf (000s)	Coca Paste	Cocaine
Bolivia													
1985	75	113	219	407	0.70	2.40	3.10	2.00	2.70	105	37.60	42	23
1986	73	123	182	378	0.60	2.60	3.20	2.00	2.50	100	36.40	49	26
1987	79	118	116	313	0.40	2.90	3.30	2.00	2.00	100	39.50	59	29
1988	102	96	137	335	0.60	3.90	4.50	2.00	1.20	108	51.10	80	39
1989	59	153	228	440	1.70	9.80	11.50	0.90	0.90	127	66.00	170	91
1990	35	52	129	216	1.50	8.10	9.60	0.55	0.40	130	64.00	119	64
1993	54	71	96	221	1.20	7.50	8.70	1.00	0.60	129	43.80	81	44
1994	59	81	98	238	1.50	7.80	9.30	0.90	0.72	139	44.00	87	46
1995	62	86	103	251	1.60	8.10	9.70	1.05	0.76	142	45.30	84	42
Colombia													
1985	22	764	2879	3665	9.10	31.80	40.90	2.00	2.70	105	10.80	283	303
1986	40	808	2506	3354	7.90	35.80	43.70	2.00	2.50	100	20.00	323	358
1987	40	686	1512	2238	5.70	37.80	43.50	2.00	2.00	100	20.00	343	378
1988	43	442	1414	1899	6.10	40.40	46.50	2.00	1.20	108	21.60	389	404
1989	30	446	1383	1859	10.50	59.70	70.20	0.90	0.90	127	33.50	495	553
1990	29	175	934	1138	10.70	59.30	70.00	0.55	0.40	130	33.40	402	487
1993	31	258	791	1080	10.30	60.30	70.60	1.00	0.60	134	40.60	489	569
1994	35	264	796	1095	10.90	62.50	73.40	0.90	0.72	139	40.80	485	425
1995	38	270	801	1109	11.20	64.20	75.40	1.05	0.76	142	42.70	509	592
Peru													
1985	181	724	257	1162	0.80	2.80	3.60	2.00	2.70	105	90.40	268	27
1986	210	760	210	1180	0.70	3.00	3.70	2.00	2.50	100	105.00	304	30
1987	218	632	128	978	0.50	3.20	3.70	2.00	2.00	100	109.20	316	32
1988	231	384	112	727	0.50	3.20	3.70	2.00	1.20	108	115.50	320	32
1989	110	325	90	525	0.70	3.90	4.60	0.90	0.90	127	121.70	361	36
1990	85	137	64	286	0.70	4.10	4.80	0.70	0.40	130	121.30	315	32
1993	235	205	68	508	10.20	4.60	14.80	0.87	0.60	134	155.50	256	43
1994	254	220	75	549	10.90	4.90	15.80	1.00	0.72	139	202.00	270	54
1995	260	228	86	574	11.30	5.60	16.90	1.19	0.76	142	207.50	273	57
Total													
1985	278	1601	3355	5234	10.60	37.00	47.60	2.00	2.70	105	138.80	593	353
1986	323	1691	2898	4912	9.20	41.40	50.60	2.00	2.50	100	161.40	676	414
1987	337	1436	1756	3529	6.60	43.90	50.50	2.00	2.00	100	168.70	718	439
1988	376	922	1663	2961	7.20	47.50	54.70	2.00	1.20	108	188.20	789	475
1989	199	924	1701	2824	12.90	73.40	86.30	0.90	0.90	127	221.20	1026	680
1990	149	364	1127	1640	12.90	71.50	84.40	0.55	0.40	130	218.70	836	583
1993	320	534	955	1809	21.70	72.40	94.10	0.87	0.60	134	239.90	826	756
1994	348	565	969	1882	23.30	75.20	98.50	1.00	0.72	139	286.00	842	535
1995	360	584	990	1934	24.10	77.90	102.00	1.09	0.76	142	296.6	866	701

Source: INCB. Report of the International Drug Control Board. 1975-95: INCSR. International Narcotics Control Strategy Report. 1988-96. DEA. Illegal Drug Price/Purity Report 1994.

Table 2.1.1.d: Distribution of the Profit From Drug Trafficking in the Andean Countries. 1985-95

Year	Internal Market (Smillion)				External Market (Smillion)			Total Profit
	Leaf	Coca Paste	Cocaine	Total	Port	Street	Total	
1985	278	1.601	3.354	5.233	10.590	37.065	47.655	52.888
1986	323	1.690	2.898	4.911	9.108	41.400	50.508	55.419
1987	337	1.436	1.756	3.529	6.585	43.900	50.485	54.014
1988	376	922	1.663	2.961	7.125	47.500	54.625	57.586
1989	199	923	1.700	2.822	12.920	73.440	86.360	89.182
1990	138	364	1.126	1.628	12.949	71.501	84.450	86.078
1993	331	568	946	1.845	12.063	71.320	83.383	85.228
1994	340	578	925	1.843	12.023	71.452	83.475	85.318
1995	368	640	910	1.918	12.005	71.650	83.655	85.573
Total	2.690	8.722	15.278	26.690	95.368	529.228	624.596	651.286
Year	Percentage Value				Percentage Value			
1985	0.5	3.0	6.4	9.9	20.0	70.1	90.1	100.0
1986	0.6	3.0	5.3	8.9	16.4	74.7	91.1	100.0
1987	0.6	2.7	3.2	6.5	12.2	81.3	93.5	100.0
1988	0.7	1.6	2.8	5.1	12.4	82.5	94.9	100.0
1989	0.3	1.0	1.9	3.2	14.5	82.3	96.8	100.0
1990	0.2	0.4	1.3	1.9	15.0	83.1	98.1	100.0
1993	0.4	0.7	1.1	2.2	14.1	83.7	97.8	100.0
1994	0.4	0.7	1.1	2.2	14.1	83.7	97.8	100.0
1995	0.4	0.8	1.0	2.2	14.0	83.8	97.8	100.0
Total	0.4	1.3	2.2	3.8	12.1	65.9	78.0	81.8

Source: INCB. Report of the International Drug Control Board. 1975-95; INCSR. International Narcotics Control Strategy Report. 1988-96. DEA. Illegal Drug Price/Purity Report 1994. Figures are derived from Table 2.1.1.c

However. the situation is even worse in the case of the coca leaf since. of the gross value of the production of the coca-cocaine complex. only 0.4 per cent stayed in the hands of the peasant producers.

In Peru. coca is grown principally in five departments (regional divisions of Peru): Cuzco. Ayacucho. San Martin. Huanuco and La Libertad. The most important growing area are the Upper Huallaga Valley and the Upper Urubamba Valley (See Map 2).

The town of Tingo Maria soon became a mecca of unrefined cocaine traffic. and nearby towns emerged a strategic location for cocaine production. An ancient social system for the exchange of labour and food. based on the trade of coca. has been infiltrated and altered by the international underworld, who now use the peasants' traditions of coca raising as agents of production and trafficking. An unskilled labourer in the capital earns about three times less than a peasant carting a bale of dried coca leaves, the lowest paid worker in the underground industry. It is hardly surprising that migrants began making the trek to the jungle from the highlands of the Andes and from the coastal cities. The prosperity of the region creates expectations that cannot be met by any other more modest source of income. Like cocaine itself, the money of the jungle is addictive. The Peruvian government has attempted in vain to limit the cocaine production by controlling the huge chemical industry linked with it[41].

The importance of production of illicit drugs to an economy will vary significantly from country to country. Speaking of Peru and according to the non-governmental research organization Macroconsult Ltd.[42], it has estimated that in 1995, 115.300 hectares of coca have been planted, of which 33.700 hectares are in the Upper Huallaga region alone. In the Amazon region 30 percent of the land is cultivable and one-fifth of this land is used for coca plantations.

Chart 2.1.1.a Cultivation and Production of Coca Leaf

	1992		1993		1994		1995	
Valleys	Cultivated (Has)	Prod. (MT)	Cultivated (Has)	Prod. (MT)	Cultivated (Has)	Prod. (MT)	Cultivated (Has)	Prod. (MT)
Total	129.200	223.900	108.800	155.500	108.600	163.300	115.300	207.540
Upper Huallaga	61.100	138.200	33.600	73.400	28.900	64.400	33.700	67.550
Central Huallaga	8.500	13.800	9.400	13.800	8.500	15.500	7.500	12.720
Lower Huallaga	2.000	2.300	8.600	2.300	7.500	2.300	6.500	11.200
Aguaytia	16.600	23.200	17.800	23.200	21.400	38.200	19.600	23.975
Ucayali	2.600	3.000	2.300	2.600	2.000	2.300	7.100	13.780
Apurimac	12.800	14.200	14.300	14.200	17.000	14.600	21.000	37.800
Cusco	11.600	13.200	9.400	10.700	9.900	10.700	10.000	18.000
Other	14.000	16.000	13.400	15.300	13.400	15.300	9.900	22.515

Source: Macroconsult, 1995.
* For illustrative description see Map 3.

The volume of dry coca leaves harvested from 115.300 hectares amounts to about 207.540 tons (1.8 tons per hectare) and was estimated to be worth 540 million U.S. dollars in 1995 (2.600 U.S dollars per ton). A total of 1.885 tons of cocaine base is estimated to have been produced from this harvest with an approximate market value of 700 U.S dollars per kilo or a gross inflow of 1.320 million U.S. dollars into Peru's narco-traffic industry. Between 1988 and 1995, coca leaf accounted for 5 percent of Peruvian agricultural production. The value of cocaine trafficking was the equivalent of 25 percent of the country's legal exports.[43] According to other research organization, Cuanto S.A., in the 1970s, coca leaf cultivation was 16.400 ha. and grew up to 57.000 ha. between 1980 and 1986. The same source mention that between 1987 and 1995, the area cultivated increased to 133.000 ha[44]. In other sources, such as the National Development Institute (INADE) has estimated for 1995 an extension of 125.000 ha. Similarly, according to the Agriculture Information Office of the Ministry of Agriculture, coca leaf cultivation was 39.861 ha. in 1980, however, in 1995 this amount grew to 120.000 ha., which meant an increase of

201% (see Chart 2.1.1.b)[45]. Further below are the figures endorsed by US government agencies. Thus, masses of peasant farmers in drug producing regions have moved upstream into the value-added processing of coca paste to further integrate themselves into the international cocaine economy.

The total number of cultivated hectares and potentially harvestable coca leaf only include coca plantations in full production which can be fully detected via satellite and other methods. Accordingly, absolute figures of the above tables and charts are subject of debate, and coca leaf production in Peru may be higher.

Illicit drugs are a commodity, and a particularly lucrative one relative to others exported by developing countries. Coca is an attractive crop to Andean farmers because it produces a secure profit. In most cases the rate of return on coca is two to five times higher than most traditional crops, or higher. In many remote coca zones, transport problems and soil constraints and other factors add up to an inhospitable environment for legal cash crop.

Chart 2.1.1.b: Cultivation and Production of Coca Leaf

	1,992		1,993		1,994		1,995	
Valleys	Cultivated (Has)	Prod. (MT)	Cultivated (Has)	Prod. (MT)	Cultivated (Has)	Prod. (MT)	Cultivated (Has)	Prod. (MT)
Total	129,200	223,900	108,800	155,500	108,600	163,300	115,300	207,540
Upper Huallaga	61,100	138,200	33,600	73,400	28,900	64,400	33,700	67,550
Central Huallaga	8,500	13,800	9,400	13,800	8,500	15,500	7,500	12,720
Lower Huallaga	2,000	2,300	8,600	2,300	7,500	2,300	6,500	11,200
Aguaytia	16,600	23,200	17,800	23,200	21,400	38,200	19,600	23,975
Ucayali	2,600	3,000	2,300	2,600	2,000	2,300	7,100	13,780
Apurimac	12,800	14,200	14,300	14,200	17,000	14,600	21,000	37,800
Cusco	11,600	13,200	9,400	10,700	9,900	10,700	10,000	18,000
Other	14,000	16,000	13,400	15,300	13,400	15,300	9,900	22,515

Source: Ministry of Agriculture-Agriculture Information Office. Annual Statistics, 1995.

* Pachitea was formed in 1995 by combining areas in Aguaytia with areas in the other category.

Chart 2.1.1.c: Coca Cultivation Estimates. 1991-1994

	1991		1992		1993		1994
Valleys	Cultivated (Has)	% Change	Cultivated (Has)	% Change	Cultivated (Has)	% Change	Cultivated (Has)
Total	120,800	+11.0	134,087	-23.46	108,600	+6.16	115,300
Upper Huallaga	60,100	+6.46	63,987	-121.40	28,900	+16.60	33,700
Central Huallaga	7,000	+21.42	8,500	0	8,500	-30.76	6,500
Lower Huallaga	1,500	+100.0	3,000	+150	7,500	-15.38	6,500
Aguaytia	10,100	+64.35	16,600	+28.9	21,400	-9.18	19,600
Ucayali	2,600	0	2,600	-30.0	2,000	+255.0	7,100
Apurimac	12,400	+11.3	13,800	+23.2	17,000	+23.52	21,000
Cusco	13,100	-12.93	11,600	-17.17	9,900	+1.01	10,000
Other	14,000	0	14,000	-4.4	13,400	-35.35	9,900

Source: United States Department. International Narcotics Control Strategy Report. 1995.

Table 2.1.1.e attempts to make a reasonable estimate of its gross revenue. value added. exports and employment for the drug industry in the three Andean countries. These estimates indicate gross revenues from illegal drugs of about US$ 8-11 billion. or about 70% of legal commodity exports. However. this estimate includes funds which may be retained by drug trades abroad. In terms of value added. the drug industry is roughly equivalent to about 5-6 percent of GDP of these three countries[46]. There are marked differences between countries. however. with drugs having a significantly larger economic impact in Colombia than in Peru and Bolivia. For Colombia. value added from cocaine represents about 7-8% of legal GDP. compared to only about 3-5% for Bolivia and 2-3% for Peru. In terms of exports. estimated gross earnings from drugs equal 94% of Colombia's official exports but 28% in the case of Bolivia and 25% for Peru. This disparity reflects Colombia's overall dominance of refining and exporting. Colombia supplies an estimated 70 to 80 percent of the cocaine sold in world markets. and about 15%

to the U.S. heroin market, and earns huge value-added in smuggling drugs to the United States and Europe.

The employment impact of the drug trade is relatively small: only about 2-3% of the total labor force are employed by this industry, but many of these are concentrated in rural areas, where they constitute a more significant part of the rural labor force. The employment impact of cocaine in Colombia is smaller than in the other source countries, and is also qualitatively different. A maximum of 160,000 people or 1.3 percent of the labor force works in the cocaine industry. Employment in the industry above the farm level comprises perhaps 20,000 to 25,000 people. Of these a critical level of 6,000 to 7,000 leader entrepreneurs and specialized operators coordinate principal trafficking functions. In Peru and Bolivia, cocaine provides proportionally about twice as many jobs as in Colombia, yet only a small percentage of the cocaine work force, less than 5 percent in Bolivia and less than 3 percent in Peru, engages in cocaine refining and export operations whereas in Colombia the proportion reaches 15 percent[47].

Table 2.1.1.e: Economic Impact of Illegal Drugs, Andean Countries, 1994

	Colombia	Bolivia	Peru	Total
Gross Revenues (US$)	7 to 9 billion	200 to 300 m	1 to 1.5 billion	8-10 billion
Value Added/GDP (%)	7 to 8	3 to 5	2 to 3	5 to 6
Gross Revenues to Legal Exports(%)	94	28	25	71
Drug area/total cropped area (%)	1.9-2.3	2.5	2.9-5.5	2.4-3.7
Cocaine work force (inc. Farm labor)	160,000	74,000	230,000	464,000
Percent of National Work Force	1.3	2.8	2.9	2

Source: U.S. Department of State, International Narcotics Control Strategy Report (March 1995) and United Nations, Economics and Social Consequences of drug Abuse and Illicit Trafficking, Nov. 1994.
Bolivia and Peru are based on cocaine exports only. Colombia's estimates assume US$ 1 billion for exports of heroin and marijuana.

Coca farming is not a static activity. Farmers can exploit various opportunities to increase yields and income by applying more sophisticated techniques. There is evidence that coca farmers are implementing agronomic improvements that make their fields more productive (see Table 2.1.1.f). In addition, coca farmers seem to be adding to their income by diversifying downstream of paste or base. In so doing they have realized higher profits, especially from base production. In the case of Peru, according to USAID data, a farmer could realize profits of US$ 3,300 per hectare by converting coca leaves to base, about 40 percent more than what he could earn by selling leaf alone.

Table 2.1.1.f: Peru – Increasingly Efficient Farmers

	1989	1990	1991	1992	1993	1994
Coca Yield Per Hectare (MT)	1.48	1.53	1.63	1.47	1.35	1.50

Source: Department of State, Bureau of International Narcotics Matters, Strategy Report 1995, p. 24.

With respect to their revenues, these estimates depend on the amount of coca leaves that are used for domestic consumption, the amount wasted at each stage of production, the amount of cocaine and by products consumed in the producing countries, and the amount seized by authorities.

Despite declining coca cultivation in the Upper Huallaga in 1993 and 1994, the country's main coca producing area, production is still expanding in other areas, particularly in the Apurimac and Aguaytia valley. However, according to the Ministry of Agriculture yields per hectare and profit margins have decreased considerably as a consequence of the fungus Fusarium Oxysporum, a newly detected disease, in the Apurimac valley, increased production costs (fertilizers, etc.) and lower coca prices.

Prices of most primary commodities have not only remained low since the 1990s, many have actually declined in nominal terms, owing to abundant supply or overstock. However, in 1993, the prices of cocoa and coffee have begun to recover, but whether this upward trend is sustainable remains in doubt. The comparison shown in Table 2.1.1.g between the prices of cocoa. coffee and coca leaf reflect a strong economic incentive to cultivate the latter. however. coca leaf prices have begun to experience a drastic decline in 1995. This fall in the price of coca leaf is basically a consequence of increased interdiction efforts in Colombia and Peru in 1994 and the dismantlement of the leading Colombian cartels of Medellin in the late 1980s and later on the cartel of Cali (1995) as well as the capture of important heads of provider firms in Peru. Eventhough prices have fallen to 1989 levels (US$ 0.4 to US$ 0.8) production costs are now on average 5 times higher than the price obtained by the coca growers. The situation is economically worrying with respect to the subsistence alternatives of thousands of coca growers. At the same time. of course. the price for cocaine base has also suffered a substantial decline in 1995.

The recent drastic price fall has caused despair among thousands of farmer families who depend economically on coca cultivation and has strengthened their will to return to legal crops.

The fact that the country until now has not had an extended history of a broad-based agricultural development strategy benefiting its peasant producers partly explains the massive migrations to coca producing areas and suggests the entrenched interests and political influence of upper income social groups. Highland migration in search of employment and income becomes a rational response within a context of severe economic crises on top of decades of discrimination by state policies. In short. whereas the migration to the coca growing areas. the Upper Huallaga region. for coca leaf cultivation has been stimulated by the relative high prices for coca from the 1970s until 1995. the push factor of extreme poverty in highland communities is also part of the problem.

Table 2.1.1.g: Prices in US$/kg

Year	Coca Leaf	Cocoa	Coffee
1990	0.66	0.83	0.51
1991	1.45	0.91	1.76
1992	2.46	0.72	0.59
1993	1.25	0.81	0.61
1994	2.48	1.04	1.85
1995	1.20	1.20	1.91
1996	0.71	1.14	1.50

Source: UNDCP-Country Programme Framework. Peru. 1997

Andean public policies have led to decades of exploitation and marginality creating the necessary pre-conditions for expanded coca growing. The national interest in fighting drugs becomes a highly ambiguous concept when the current government faces massive unemployment. and increasing poverty among its citizens.

The current conjunction favors the implementation of a widespread alternative development programme. The only option left for the peasants is to rehabilitate abandoned areas traditionally cultivated with cacao. coffee. etc. and to commence the implementation of other agricultural or livestock activities promoted by national projects and other entities being encouraged to initiate and support alternative development activities in different areas. This is reflected in increased levels of collection and marketing of coffee and cacao through the cooperatives and producers' associations which are target groups of ongoing national projects.

National experts' opinions claim that the current price tendency might only be temporary until narcotraffickers reorganize themselves to find alternative routes to transport cocaine base. It has already been speculated that the border with Brazil might be considered a practical alternative to transport semi-processed cocaine instead of using traditional direct flights between Peru and Colombia.

Finally, since cocaine and various other illicit drugs are agricultural-based products, policy makers must analyze the impact of national agricultural policies on the peasants producer sector. Policy makers must take into account what is happening to peasants economies locally, the growing areas and plantations, the labour market in the Huallaga valley and migrant workers, in response to broader regional and national socio-economic changes.

2.1.2 Distribution in the Market

Results from the relationship between the national economic needs and the international underworld economy are manifested in social and economic behaviour of the groups that participate in production, distribution, and marketing of coca paste and other good related to the industry.

Border controls are a major focus of interception efforts. However, with the increased flow of commercial traffic between countries and the free movement of goods in large regional trade blocks, the success rate of interdiction at national borders, low to begin with, may decrease further. Vigorous action by authorities in one area often leads to shifts in the pattern of illicit activity or to movement of the illegal activity to another area. While interception efforts may result in lengthening or altering the chain of illicit movement and increase the exposure of the illicit operation to seizure in a given area, unless the interdiction and seizure success rates are high, illicit shipments of drugs will likely continue. Those who get caught smuggling drugs are often low level persons who can easily be replaced with new recruits.

Before leaving the production zone for the national or international markets. the white coca paste circulates in communities and towns. Then they take diverse routes. Coca paste producers try to sell it few hours after manufacturing. for if it is kept for many days. the substance's weight is reduced. In each territory dominated by one boss there are two kinds of buyers: independent and contracted. Independent buyers operate their own business: contracted collectors work for commissions. averaging about 100 dollars per week. Coca paste manufacturers resist doing business with independent buyers. because they demand more money. Furthermore. if independent buyers pay better prices than official buyers. contracted collectors complain to their bosses. Their bosses get rid of the unfair competition. Independent buyers can continue their operations only by paying the same prices stipulated by the local organized group.

Fluctuations in prices are functions of international demand. presence of organized crime. police control. and distances to shipping points (airports). Primarily. Peru supplies semiprocessed cocaine to the Colombians for refining and subsequent export to the United States and Europe. When the bosses in Colombia send the more cash requesting greater amounts of coca paste. the local boss authorizes raising prices. Arguments for stipulating new prices can be attributed to the saturation of international market or heavy competition. Organized crime stipulates prices based on seniority in the territory. Like other legal consumer commodities. coca paste market values add expenses such as human labour required for transportation. the use of secret routes to mislead police. and other unexpected expenditures. Besides being heavily concentrated in drug terminal towns and using regular transit roads. coca paste also moves through villages and communities in the highlands as it proceeds on its way to national and international markets.

Two kinds of people are involved in the local trafficking of cocaine. The small trader either buys coca paste at the first stage or goes to the jungle to bring paste to towns for resale to wholesale dealers. The second type of drug dealer is the local middle-class public employee. Town wholesalers always have the small traders in their power. in that they lend money at high interest or pay lower prices arguing an overstock. Small traders are the best consumers of the services available in the coca paste terminal settings. In the second stage. commercial movement of coca paste is almost completely open. Everyone knows who is who in the business. and it is not rare to observe local and non-local small dealers walking around with their saddlebags hung over their shoulders.

Coca paste from the second stage goes to the national market via surface transportation. Buses. trucks. and private cars carry the drug. declaring it as food being transported from coca production zones in Cuzco. Ayacucho. San Martin. Huanuco and La Libertad to Lima and other cities on the coast such as Piura. Tumbes. Trujillo. and Arequipa among others. when is checked by the traffic police stations. In theory. these stations are responsible for searching for cocaine in the vehicles travelling the route. However. it is an impossible task for few policemen to do more than simply check personal identifications. detain suspects. or accidentally discover smuggled coca paste. Smugglers and dealers have their own ways of finding their way out when passing these controls.

In these urban cities. some sell their product to customers or people to whom they were recommended. and some are caught by police.

Important reasons for bringing coca paste to the market in the cities are to satisfy individual consumption and to supply it to refining laboratories. Slums and shantytowns are ideal settings for cutting, packaging, distributing, and establishing smoking areas. It takes unsuspected roads and routes to international markets. The most outstanding feature of distribution and marketing of coca paste is its return to the jungle.

2.1.3 Structure and Division of Labour

The underground network is a rigid hierarchy. The people who participate in the national and international underground economy are organized and labeled according to production, distribution, and marketing of both the coca paste and the cocaine hydrochloride. At the top of the pyramid is the boss of the operation who is its link to international organizations. He is always known as a "colocho", a nickname used in the jungle to denote a Colombian but which, in the cocaine industry, simply means someone associated with the processing and trafficking that is centered in Colombia. However, this does not mean that the traffic in cocaine is totally controlled by Colombians. Many nationals from other Latin American countries are connected directly to the United States[48].

Another social level that is widely used in Peru and that carries recognition, respect, and prestige based on economic power on the local and, to some extent, national level is the word "narco". A narco always has an investment in one of the sectors of the economy. His legal activity is to incorporate narco-dollars into the legal economy and thereby to participate in every aspect of national life, a phenomenon known as bleaching cocaine money. Moreover, a narco may be a jungle crime boss who is stipulating prices and controlling local population, and to those who live in the jungle, the boss is a shadowy figure known only by his code name. Other groups structured around the participation in the illicit economy are the pick-up men; local bosses, or patrones; runners, or collectors of coca paste: and transportation and security support staff members.

The pick-up man, or "bag man", comes in an airplane to transport the merchandise to Colombia. The plane is loaded with contraband such as watches, appliances, liquor, arms, etc. The pick-up man and the pilot are the only occupants of the small plane. Fuel supplies and the size of air fields and planes are decisive factors in landing. Because some small planes do not have the fuel capacity to cross the borders they often refuel or leave their loads at points where several loads are collected for transport in large planes. Commercial, private, and air force airstrips are sometimes used with the cooperation of corrupt officials. Although the communication with Colombia is critical, because of tight control, new methods and routes of transportation and communication are developed constantly. After landing, neither the pilot nor the pick-up man leave the plane. The operation is so well organized that from landing to departure takes less than ten minutes. The delivery men carry a full load of coca paste to the plane where also bodyguards and two or three gunmen position themselves on the ground with their fingers on the trigger, and there they stay until the plane leaves with the merchandise.

Another important member in the organization is the patron, who may be a colocho or a narco. A person with an enviable lifestyle. His residence is full of luxuries. Color television sets, home video equipment, and imported liquor are very common place there. In towns and villages, the patron can eat, drink, and entertain his friends without any cash in his pockets. Although his involvement in the drug business makes him seem like a dangerous man to many local town people, he acts like a gentleman and a humanitarian. He helps the poor and makes sure that his bodyguards throw out crooks that are either disturbing the community or suspected of being against him.

Continuing down the structure, the organization presents a group of people known as runners or collectors of coca paste. Depending on the number of runners and pick-up flights, the patron gives the runners cash to buy coca paste. The range of maximum amounts collected by the runners is between 50 and 100 kilos. Into cash, the range is from \$50,000 to \$100,000. The coca paste collector gets a commission of about \$50 to \$100 per assignment, which takes from three to five days.[49]

The lowest people who handle the coca paste are the delivery men. They are mostly unemployed migrants and highland peasants who transport the drugs for extra income. In their regular activities they may be coca leaf pickers, high school students, teachers, or any person who wants to make more money, depending on distances walked or skills. They deliver the illegal good to consumer markets and refining laboratories. They are intermediaries between sellers and buyers of coca paste or cocaine hydrochloride. The seller may be a producer or a drug dealer; the buyer may be a coca paste or cocaine retailer or both, or a national or international wholesaler. In addition, given the kinds of goods transported and the risks faced, their wages are very low. The average pay for a delivery job that takes from three to five days is \$40 to \$60, or the equivalent of two month's worth of minimum salary.[50]

As we can see, the illegal trade generates a variety of occupations and activities that support both legal and illegal economies. Moreover, the underground economy helps maintain legal industries that produce materials for the preparation of coca paste and the manufacture of cocaine.[51]

Estimation of the cocaine industry's size and profitability confronts the problem of continuous innovation within the industry itself. Narcotics enterprises in the 1990s are more dynamic. evolving. and increasingly efficient. As law enforcement pressure has increased. production techniques. storage technologies. and smuggling strategies have improved commensurably. For instance. some cocaine laboratories now are equipped with chemical recycling and recovery plants as well as with vacuum-packing facilities and microwave drying ovens. Smuggling methods continue to advance and to proliferate. Drug-traffickers have extended their smuggling reach by buying or leasing cargo planes. including jets and turboprop aircraft: smuggling aircraft today may carry one to six tons of cocaine compared to 400 to 500 kilograms in the 1980s. The sheer variety of vehicles that modern smuggling use to move bulk cocaine shipments such as cargo jets. maritime containerized cargo. tractor trailers. camouflaged small boats. and even semi-submersible vessels. represents a new considerable challenge to law enforcement officials[52].

The mafia organizations and the coca lobby constitute what might be called the cocaine constituency in South America countries. These organizations integrate a range of activities. are multinational in scope. and command substantial technical. financial. and human resources. This industry is relatively concentrated. and the actors cooperate on both strategic and operational matters. In general. the mafia's structure. capabilities. and methods of operation convey the impression of strength and resiliency.

2.1.4 What does Coca Offer?

For many farmers in Peru. Bolivia and Colombia. coca is the sole cash crop. because it offers what is in many respects the complete package for farmers. Although market conditions vary. coca is typically much more profitable than licit cash crop in Peru. Bolivia and Colombia. The high profits associated with cultivating the plants mean that a farmer who wants to start a coca farm can obtain financing, fertilizer, seed and even technical assistance from drug traffickers or their intermediaries. The plant is easily cultivated and seems to flourish in agronomic and climate conditions that are unsuitable for most other crops.

Statistically, according to Peru's Andean Report[53], a coca farmer in the Upper Huallaga Valley could earn a maximum gross income of $12,350 per hectare per year 1990; of this sum, 60 percent was profit. A coca farmer's net per hectare earnings were ten times those of a cacao farmer and ninety-one times those of a rice farmer. As it was shown in Table 2.1.1.g, prices of South American coca leaf have dropped significantly from their peak levels, primarily because of the overproduction of leaf and intensified enforcement against cocaine laboratories. However, coca yields relatively quick returns. Coca can be harvested 18 months after planting. Many alternative cash crop, for example, oranges, rubber, tea or coffee require 4 years or more from planting to the first harvest. In sum, coca cultivation presents a very superior cash flow option for Peruvian, Bolivian and Colombian farmers.

Within the area of coca cultivation, some lands are more marginal than others. The flat, alluvial lands along the river, which are suited to growing traditional crops contrast with the humid jungle hillsides, which are not. Farmers in some cases may have shifted land out of food production, like rice, bananas, oranges, and the like, into coca cultivation. Data from the USAID project in Peru indicates that the net income per hectare for coca was significantly higher than most alternatives (see Table 2.1.4.a). The net annual income per hectare for coca is estimated to be US$ 1178, compared to US$ 156 for traditional crops[54].

Table 2.1.4.a: Peru – Estimate Net Annual Income. 1994. Coca and Legal Crops

Crop	Initial Investment	Net Annual Income
	(US$/ha)	(US$/ha)
Coca	1.118	1.178
Pineapple	1.645	330
Maracuya	2.936	920
Citrus Fruits	2.565	308
Bananas	643	89
Palm Hearts	1.898	462
Traditional Crops	617	156

Source: USAID. Alternative Development Project. Lima 1994. p. 2.
Net Annual Income excludes initial investment cost.

While citrus and pineapple can match these returns using advanced technologies and optimum conditions. the cultivation methods for these crops are much more sophisticated. and the initial investment costs are much higher. In the case of pineapple. the initial investment is 4 times that needed for coca. Crops such as maracuya and palm hearts are crops which are now being grown only on a limited scale. but because they have relatively thin markets. substantial increased production is likely to lower prices and economic returns.

Compared to exotic products with uncertain markets. coca produces quick yields. generating enough cash to repay the initial investment. In addition. coca has a high value to weight ratio and presents few handling problems for farmers. Coca can harvested at any time. and the leaves dried and stored until collected. Crops such as bananas. citrus and pineapple must be picked when ripe and shipped on time. Remote areas are not naturally the best areas for growing these bulky commercial crops which are aimed at urban and export markets.

A constraint on developing profitable alternatives to coca arises from the relative distance of the regions that produce the plant. Such regions are hundreds of miles from urban centres and are not connected to them by roads or commercial air transport. Peru's Upper Huallaga Valley lies 400 to 750 miles from the capital. a ten hour drive from Lima to the closest city (the town of Tingo Maria) at the southern end of the Valley.

Distance can increase the required cost to ship commodities to market. and in the coca growing region of Peru. Bolivia and Colombia these costs are likely to be very high. Consequently. peasants find themselves at a competitive disadvantage. If cocaine industry does not operate as an efficient engine of economic progress. it still provides an escape from poverty and misery for many inhabitants of the Andean world. Moreover. for rural dwellers especially. the cocaine industry offers a kind of instant introduction to modern lifestyle. For these reasons. it is difficult to imagine that coercive measures against peasants could ever have positive results. Peasants producing coca have nothing to lose. As long as coca provides a family livelihood. they will protect their coca crop at all costs. In this way. coca cultivation and cocaine trafficking have created radically new expectations and aspirations within Andean societies.

2.2 *The Socio-Economic Impact of Narcotics in Peru*

The following section will analyze the effect of the underground dollar economy in the Financial System. It also describes how cocaine production constitutes a significant source of employment: the implication of coca chewing as a natural, social practice in the Andean society, and their concomitant ecological and cost impacts.

2.2.1 Money Laundering

Narcotics money laundering has evolved over the last three years into an important foreign policy as well as a financial management priority in many key financial center countries. These priorities are reflected in virtually wholesale changes to laws and regulations, as well as improved cooperation. These changes result from a growing international conviction that drug trafficking can not be halted unless we deprive trafficking organizations of their proceeds, as well as from a shared sense of responsibility for halting the production, trafficking and consumption of drugs[55].

The purchase of state-own enterprises, the acquisition of businesses by private investors, and the shift to full currency convertibility all provide ample scope for financial manipulation by criminal organizations associated with the illicit drug industry. This threat if often generalized under the umbrella term of money-laundering. The internationalization of money laundering has been brought about by two factors. First, the integration of financial markets through the liberalization trade given by macroeconomic reforms into a complex, global entity: and second, the effort by trafficking to avoid detection by concentrating operations in countries where enforcement is weak and legislation is absent.

Unfortunately. many countries fall into this latter category. in particular those classified as emerging markets. In becoming more internationalized. money laundering is in fact simply following the global macro-economic trend of legitimate goods and financial services. It works to the benefit of the launderer in as much as it creates more scope to move from one place to another. taking advantages of gaps in legislation and discrepancies in regulatory control.

The Financial Action Task Force. established in 1989 by the heads of State of the Group of Seven major industrialized countries. estimates that approximately $ 85 billion is laundered each year in Europe and the United States. The new shift in focus towards emerging markets in Asia and Latin America raises concern about the risks facing emerging financial systems[56]. Such risks go well beyond the mere recycling of illicit revenues into legitimate enterprise. an act which amounts to little relative to the total value of private sector capital flowing into developing countries. With the trend towards privatization. the real danger comes from the ability of drug trafficking not only to launder funds. but also to acquire portions of what constitutes a second-hand sale of global proportions.

Most of the billion of dollars earned by cocaine traffickers stay abroad in offshore heavens such as the Cayman Islands. Barbados. Aruba or Panama or in investments in foreign real estate. securities. and business. In Peru. according to the Anti-Narcotics National Bureau-DINANDRO[57]. Reynaldo Rodriguez Lopez. a trafficker who was a trusted adviser to Peru's top police officials. owned a travel agency that served as a cover for his cocaine smuggling operations. Similarly. other Peruvian traffickers who were captured in the 1993-95 period such as Demetrio Chávez Peñaherrera. Umberto Ammaturo

Rochino. Cachique Rivera and Tijero Guzmán. controlled nationwide and through intermediaries real estates: cattle ranching: commercial stores (whole sale and retail): luxury residences and condominiums (mostly in Lima and Tingo María): services and recreation (gymnasiums. hotels. restaurants. and discotheques): small light aircrafts and luxury cars.

Once established in the legitimate domestic economy. drug traffickers generally have considerable freedom: (a) to transport illicit goods under the guise of legal merchandise: (b) to create new markets for wholesale or retail distribution: (c) to establish or arrange for new sources of precursor chemicals: and (d) to launder even more illicit revenues.

Whether traffickers invest their money at home or abroad depends on several conditions in the source country: investment opportunities. interest rates. political stability. and perhaps the most important. government policy towards the drug trade. Profits that return or remain at home may add to the country's official reserves or may circulate in the underground dollar economy. Due to the difficulties in deriving an accurate and precise figure for the amount of money laundering. different experts have provided some rough estimate of the amount of money laundering occurring in the country.

Unfortunately. the vast majority of institutions lack sufficient data to support any credible estimate. The most comprehensive figures remain the results of the study produced by Macroconsult Ltd.[58]. which says that of the approximately 1.400 million dollars that the drug industry generated for Peru. 870 million never entered the country's financial system due to capital flight. Half of the remaining 700 million dollars are believed to have been invested in the Peruvian goods and services industry. while the remaining 350 million dollars found their way into the legal banking system. Other sources. such the Central Bank. provides figures ranged from US$ 1.500 million to US$ 2.000 million for the amount of money laundering during 1995. Moreover. other experts offered data on sums seized pursuant to money laundering investigations or prosecutions. Thus. some of them were unable to establish the magnitude of money laundering taking place. but as an example could show that the Drug Enforcement Agency in 1995-96. had 1.233 cases of money laundering prosecuted with a total value of US$ 1.62 billion[59]. However this information does not support a valid estimate of the amount of tainted funds entering the legitimate financial stream. as it can only be a small percentage of the total amount of proceeds of crime because most of the money laundering takes place in different financial markets. involving criminal organizations worldwide. through wholesale and retail channels.

When viewed in terms of macroeconomic indicators. the impact of the illicit drug industry on a producer country's trade balance such as Peru tends to be positive for the simple reason that exports of illegal drugs generate inflows of foreign exchange. This is precisely the reason why some analysts have the assumption that any producer country benefits from illicit drug exports. Namely. the money is not allocated to investments which are considered productive from the aspects of economic development. but are placed in the balance of payments to be part of the payments for the servicing of Peru's external debt. However. there is no evidence of such operations because as trade in illicit drugs is not recorded. balance of payment variations can give only indirect clues as to the size of the trade and its impact.

Cocaine money also brings into the industry money brokers who spread coca-dollars throughout the country. Money exchanges travel back and forth through the cocaine towns. collecting coca-dollars and concentrating them in Lima and. to some extent. spreading them throughout the country. In addition to making U.S. dollars available to the general public. coca-dollar brokers send the American currency back to the United States. Therefore. because of its underground roots. it is extremely difficult to know or estimate the amount and proportion of coca-dollars that remain in Peru or leave the country[60].

Banks offer a wide range of financial products and hold the largest share of the financial market. and accordingly the services they provide are widely used for money laundering. However. non-bank financial institutions and non-financial businesses are becoming more attractive to these brokers for introducing ill-gotten gains into regular financial channels as the anti-money laundering regulations in the Peruvian banking sector become increasing effective. Some delegations continue to report a significant shift in laundering activity from the traditional banking sector to the non-bank financial sector and to non-financial businesses.

Among the most general example is that in the capital city. circulation of coca-dollars has become wide open. Since 1991. dozens of new money-exchange offices are opened in downtown and middle-class sections of Lima. In particular. Lima's financial district is flooded with U.S. dollars. Hundreds of dealers holding their calculators and bundles of dollars and soles deal with passers-by. Tourists. businessmen. and others who needed to buy or sell dollars would go to these streets of Lima.

This bureaux de change. exchange offices or casa de cambio pose an ever more significant money laundering threat. They offer a range of services which are attractive to criminals: (a) exchange services which can be used to buy or sell foreign currencies. as well as consolidating small denomination bank notes into larger ones. (b) exchanging financial instruments such as travelers cheque. money orders and personal cheque. and (c) telegraphic transfer facilities. The criminal element continues to be attracted to bureaux de change because they are not as heavily regulated as traditional financial institutions or not regulated at all. Even when regulated the bureaux often have inadequate education and internal control systems to guard against money laundering. This weakness is compounded by the fact that most of their customers are occasional. which makes it more difficult for them to know their customer. and thus makes them more vulnerable[61].

As anti-money laundering regulations is consolidating in the national financial sector. the criminals place increasing reliance on professional money laundering facilitators. The experts reported a significant number of cases involving lawyers. accountants. financial advisors. notaries. secretarial companies and other fiduciaries whose services are employed to assist in the disposal of criminal profits. Among the most common tactics observed have been the use of solicitors' or attorneys' client accounts for the placement and layering of funds. By this method the launderer hopes to obtain the advantage of anonymity. through the solicitor client privilege. The making available of bank accounts and the provision of professional advice and services as to how and where to launder criminal money is likely to increase as counter measures become more effective.

In addition to the use of shell companies. there was also widespread use of real businesses in Peru. to camouflage the illegitimate laundering of money. Techniques used in conjunction with these businesses included false invoicing. commingling of legal and illegal moneys. the use of loan back arrangements and layers of transactions through offshore shell companies. Often the laundered proceeds would then be invested through the real company into real estate or other businesses. though one country reported that there was a trend away from investing illegal proceeds in real estate. and into less visible investments such as financial businesses[62].

Drug trafficking remains the most frequently mentioned sources of illegal proceeds. Nowadays. in the 1990s. drug trafficking is still the largest single generator of illegal proceeds. Banks and bankers are compelled by due diligence conventions and other sanctions in numerous countries to accept responsibility for ensuring that their institutions take affirmative steps to prevent narcotics money laundering. We believe banking systems in many key countries are less vulnerable today. at least at the placement stage. thanks to the adoption of new laws and banking regulations.

2.2.2 Socio-Demographic Impact

Traditionally in Peru. the indigenous population of the Andean region were always associated with their habitual coca-chewing. This traditional social and cultural practice has changed to more sophisticated and addictive behaviours. Cigarette smoking and alcohol abuse are probably still the most serious health hazards and social problems affecting traditional and modern societies alike. But another. coca paste smoking. has appeared in Peru and some Latin American countries. While production coca paste and the retailing of "ketes" (in the 1980s. coca paste was retailed under this name). have created an economic dependence and caused inflationary prices. they have also brought about physical and psychological dependence[63].

Beside economically supporting the underworld. the highland peasants undergo the social consequences of using coca paste. Their trend of coca-chewing. especially among young male peasants, is now changing to the use of coca paste, that is to a more addictive and dangerous habit.

Besides the obvious availability of coca paste, there are two main reasons for the consumption of the substance in the jungle: economic and social. In the jungle, food is expensive. Since the cocaine entrepreneur has to provide the peasant with food during his employment, it is to the entrepreneur's advantage to keep production expenses low by letting his workers consume coca paste. Socially, the Andean peasant is used to working under the stimulation of coca and is aware of the social impact that has been attached to coca-chewing.

The most damaging effect of addiction to drugs is the self-destruction of hundreds and thousands of children who enter the drug subculture very early in their lives. Statistics from population surveys have shown that smoking coca paste began when children were nine or ten years old, and across the board, they have been smoking coca paste for one to five years. The younger addicts usually get their daily dosages by way of homosexual services or exchange of sexual gratification. Non-addicted homosexuals and heterosexuals also trade coca paste for the same purpose[64].

The illicit drug trade brings with it drug abuse and a host of other social problems. Available evidence, though, suggest that consumption of cocaine and other drugs is far less widespread in Latin America than in the United States. In Colombia, for instance, a 1992 study commissioned by the National Drug Directorate showed that 1.4 million people (4.1 percent of the population) had consumed at least one illegal drug at some time in their lives. In the United States, however, lifetime drug prevalence is 77 million or 31 percent of the U.S. population. Comparable figures for cocaine are 340,000 (1.0 percent of the population) in Colombia and 23.5 million (9.4 percent of the population) in the United States. In Peru, according to the INEI, lifetime prevalence as of 1995 is somewhat higher than Colombia (1.5 percent for cocaine and 2.9 percent for cocaine paste). Such numbers are still much lower than those in the U.S. In Bolivia a study by the National Directorate of Drug Prevention, Treatment Rehabilitation and Social Reintegration found that only 1.2 percent of the Bolivian population had used cocaine paste as base at some time in their lives. While current rates of use are low, it is likely that the continued presence of a well developed illegal export drug industry will eventually focus on developing domestic consumption, and usage rates are likely to rise in the future[65].

Therefore, the Upper Huallaga Valley, the region of great concern due to its important cocaine industry, has had a very significant increase since 1940. This increase, nevertheless, has not been homogenous all over the valley. Overall population growth there has been higher than the national average as can be seen in Table 2.2.2.a. But if we analyze the growth rate according to two clusters of places, the first localities around Tingo Maria and the second one around Uchiza, things change considerably. For the first cluster we find a descending although higher than average growth rate since the period 1940-1960. People got to those places especially between 1940 and 1970, as part of a migratory wave to a very promising region. When in the second part of the 1970s the coca boom began at the same time that a very severe economic crisis, the cluster became an important point in the development of the cocaine industry. Repressive policies that included forced eradication, simple substitution schemes and sheer force, pushed the whole production system in the direction of Tarapoto and created the second cluster. Indeed, it is very clear that population growth rates are ascending for that cluster and get to an all time high between 1982 and 1990. This corresponds with the period when the insurrection of Shining Path developed and probably the cocaine industry and the subversive movement combined in creating the big migratory wave that corresponds to the last years.

About 80% of the urban population is concentrated in Tingo Maria, Uchiza, Tocache and Nuevo Progreso. One of the most important features of the area's population is that almost 90% of it is made up of people who arrived there recently and followed a colonization pattern that run from south to north in the direction of the construction of the marginal highway, a project of former president Fernando Belaunde.

Table 2.2.2.a: Population and Population Growth Rates in the Upper Huallaga Valley and Two Clusters Within It

	1940		1961		1972		1982		1990
Total	71,832		124,454		185,094		241,011		313,090
Growth Rate		2.60%		3.70%		2.90%		3.00%	
Cluster I (Tingo Mana, Progreso)	2,619		24,475		55,631		31,241		112,988
Growth Rate		11.20%		7.80%		4.20%		3.70%	
Cluster II (Juanjui, Tocache, Bellavista, Sion, Uchiza, Pachiza)	8,882		20,712		36,605		54,231		109,179
Growth Rate		6.70%		6.80%		4.30%		9.70%	

Source: Instituto Nacional de Estadística e Informática, Perú. Oficina de Estudios Demográficos y Sociales. Reporte Anual, 1996, p. 17.

This colonization was, as noted, promoted by the state, but without any serious planning beyond noting the region's development potential. Most of the migrants came from Peru's northern highlands, in a disorganized and spontaneous way. The settlers' motivations included securing land, obtaining jobs and, less frequently, family ties with colonists who were already there. In some of the surveys undertaken in the region, marginal road construction and migration from the Andean region coincide with the failure of the military government's agrarian reform policies and the lack of opportunities in the cities[66]. Some of the newcomers were second time migrants who. disenchanted with city life. hit the road for the jungle.

Clearly. the governments in the past two decades acted twice: first promoting. via road construction and a certain initial organizing presence: then disappearing. leaving a sort of gate used by a disorderly migration flow in search of opportunities. one of which. if not the most important. is the coca industry.

Two additional factors have influenced the shift from legal to illegal crops. including the purely economic factor. On the one hand. cultivation was based on field rotation more than on crop rotation. This. of course. promotes displacement and instability in the relationship between the peasant and the soil. On the other hand. the legal system that regulated land tenancy was cumbersome and inefficient. so that obtaining a property title was nearly impossible. But a title is needed in order to receive a bank loan credit and technical assistance. so that illegal crops were a natural and almost understandable option for many of the settlers. most of whom were affected by the lack of legal stability. Of course. those that cultivate illegal crops are by definition excluded from any system of national or international cooperation. In other word. it is a vicious circle. The most recent initiative as was mentioned before. promoted by the current government. intends to change that situation by given legal titles to the farmers. From that point. a progressive substitution scheme with international support would follow (Drug-trafficking Strategy Enforcement. 1990)[67]. With this register. it becomes feasible to promote alternative crops and avoid a larger flow from rural regions into urban. which would only worsen the problems of low standards of living and unemployment. Also. it is possible to negotiate a crop substitution program and improve it over time. An evaluation of the progress of the program, thanks to the land registration and legalization process, can lead to the concentration of the repression and legal fight against the drug trade itself, and those that do not comply with the crop substitution agreements. It can also support the fight against the terrorists.

The drug trade has had a negative effect on the general quality of life in affected countries, and particularly in the Andean producer countries, have contributed to a high level of social violence. Drugs are associated with the degradation of the judicial sector and with the increasing ineffectiveness of the court systems in resolving civil disputes. The cocaine ethic also has diminished the moral basis of the society, spewing corruption at all levels, and increasing the incidence of kidnappings and street crime. These social costs can also have a direct economic cost, in terms of reduced labor productivity, increased costs for crime prevention and security[68].

In analyzing the socio-demographic phenomena generated by the coca boom in the high jungle, we find characteristics that are not unexpected in a country like Peru, or for that matter in a region where sudden economic structural reform is undertaken: lack of continuity and planning by state that at first generates expectations. This is followed by a lack of authority, institutionalization and support, which are compensated through unorganized but vigorous illegal forces that do not abide by the rules.

An important direct cost associated with the drug trade is the cost of enforcing the drug laws, prosecuting drug kingpins and implementing demand reduction via treatment and prevention programs. Peru's national drug budget is about US$ 2 billion this year or about 3.4 percent of Peru's GDP[69]. Of this amount, almost 90 percent is allocated to the

Ministry of Defense and the National Police, for crop eradication and counter-trafficking activities, while the remaining amount goes to the Ministries of Health and Education which share responsibility for fighting domestic drug addiction. Drug control efforts are very costly. Thus, the Andean countries bear a relatively high cost for sustaining efforts against drug production and drug abuse, and these efforts divert resources from the development of other parts of the economy.

The most important part of the program is that it should adopt the point of view of the poor, creating institutions which support their efforts to attain the right to their property, therefore integrating them into the legal market framework. It also becomes possible to establish the presence of the state in the coca production areas as a legitimate authority and source of alternatives for the millions of peasant land holders.

2.2.3 Violence and Insurgency

The impact of the drug trade on the Peruvian political and socio-economical system has been considerable as it is founded upon an alliance between leftist guerrilla groups and coca farmers. Therefore, it is necessary to explore this important complex relationship and collaboration with the cocaine industry.

The violence and insurgency plays a significant role in the Latin American drug trade. The drug-insurgency relationship is the formation of political-military enclaves controlled by traffickers in alliance with leftist, revolutionary groups. This means that the funding and equipping of terrorist activities are accomplished by involvement in drug-related activities that may include the production and export of narcotics.

It is in this scenario that the Shining Path, a left-wing guerrilla movement, emerged in May of 1980. The initial focus of the Shining Path's terrorist acts was the city of Ayacucho. where sociologists. anthropologists. philosophers and students at the University of Huamanga incited both young mestizos and peasants to attempt armed struggles against the government. The moving forced behind the Shining Path's creation was Abimael Guzmán. a philosophy professor at the University of Huamanga. Noting the striking class differences in the society. Guzmán concluded that as Peru approached the twenty-first century. it was still a semi-feudal and semi-colonial society. Moreover. the government embodied a fascist structure masquerading as democracy and engaging in the construction of a corporate state and the development of bureaucratic capitalism. Guzman's political ideology was predominantly Maoist. As such. Guzmán held that the social reform could be had only by making revolutionaries out of Peruvian peasants for the purpose of overthrowing the established government.

The Shining Path first came to widespread public attention after a full decade of dogmatic self-examination and rigorously selective recruitment. The violence against the government began in July 1980. and by the end of the year some 240 incidents had been recorded. including the destruction of local tax records. bombing of government offices. and sabotage of electrical pylons. By 1981 the rate of incidents had increased. expanding to such activities as the raiding of banks. mines. and the police posts. Kidnapping and attacks to offices and personnel associated with the eradication of the coca plant and control of the production and trafficking of cocaine was added the following year[70].

In the jungle. unlike the rest of the country. no banks. schools or power plants have been destroyed. Such terrorist acts would have affected local drug economies more than the national economy. Cities that provide consumer goods to drug-producing areas have not been targets of any kind of serious terrorist attacks so far. whereas other highland cities and towns whose economies are not based on cocaine have attracted the Shining Path. Moreover. if the Shining Path were politically important in towns and villages producing drugs. and if the movement were supported by organized crime. there would have been only sporadic attacks. Both the highland guerrillas and the cocaine underworld have been more organized and better equipped than the national army in the area[71].

Most of the victims of the drug traffickers' attacks are police informers. policemen. and members of the armed forces. They set fire to encampments and offices. torture their victims and chop their bodies into pieces. put them in plastic bags. and dump them in the woods or throw them in the river. When they get their hands on people they want very badly. they beat them up and hang them with wires. putting signs on their bodies which read. "This is the way informers die."[72] The drug traffickers communicate and organize so quickly against police raids. that many law enforcement officers are more concerned with their own survival and livelihoods than with law enforcement functions.

The ideological politics of the Shining Path became most evident in the focus of its terrorist activities during 1986. In southern Peru. the Shining Path guerrillas captured plantations and haciendas. sometimes killing their owners and employees. and distributing cattle. sheep. alpacas. and other goods to local peasants. A state of emergency. with constitutional guarantees in abeyance. existed in almost two thirds of Peru. affecting half the population. Moreover. the Shining Path was believed to have fielded some 5.000 guerrillas and 500.000 followers nationwide[73].

The Shining Path has acted with a combination of what could be called tactical simplicity and strategic sophistication. Since the war began in 1980. it has had long-range goals and mid-range goals. and has taken immediate. specific action. all carefully and centrally planned by Guzmán.

Shining Path has imposed itself in some regions of the Andes through sheer terror with little social support. The Upper Huallaga Valley is. in that sense. an ideal setting. State control is almost absent. and when it is present it brings conflict. repression and corruption. The drug traffickers represents violence and economic exploitation. As we have already seen. the peasants. poorly organized and lacking social support systems. are mistreated by everyone. The Shining Path protects the coca cultivators. regulates their dealings with the traffickers. harasses the few people who represents the state and defends coca cultivation against international and national eradication programs. In other words. the Shining Path. has established a legitimacy in the region that it has not been able to achieve elsewhere. The latest antidrug strategies (militarization of the antidrug efforts. via the army). suit Shining Path's ideology perfectly as the conflict takes on an international scope. The coca growers would be at the center of the war of national resistance against the American efforts to take the Peruvian peasants livelihood away from them.

Drug traffickers and Shining Path guerrillas represent two totally different social movements. Drug traffickers are members of an underground social organization with purely economic interests[74]. They are usually conservative and status quo-oriented. They do not have any ideological and emotional identification with national problems. The Shining Path and other political groups. on the other hand. are usually seeking to radically transform their respective societies by overthrowing their governments and implementing a revolutionary new order usually based on an offshoot of Marxist-Leninist ideology. Hundreds of people in both the highlands and urban areas did join the guerrillas. For them.

there was no other way to express the frustration. poverty. misery and abuse experienced in the country. For this reason. the highland Indians and peasants directly or indirectly have supported the rural guerrillas.

The narco-terrorism link. however. apparently deteriorates in the downstream phase of the cocaine industry. Cocaine dealers and guerrillas compete bitterly for territory and resources and for control over the coca growing peasantry.

Given this pattern of conflict. it is not surprising that the Peruvian sociologist Gustavo Gorriti suggests that drug dealers can develop certain forms of cooperation and a tacit alliance with the state. From the state's perspective. after all. guerrillas pose a greater strategic threat than the cocaine industry.

Nonetheless. powerful groups related to drug trafficking have evolved in the past few years. They have tried to infiltrate and control society and influence political parties. Two examples come to the mind: between 1975-1980. drug trafficker Carlos Lanberg built up an influence network during the last years of the military government. He influenced leaders of the left-of-center APRA party which everyone thought was slated to win the elections after the return of the military to their barracks. Lanberg contributed generously to the APRA political campaign in 1980. After the electoral defeat. APRA underwent a renewal that saw Alan Garcia. a young and largely unknown politician. rise to power. From the Garcia focused on the presidency. which he achieved in 1985. Another example is Reynaldo Rodriguez Lopez. an obscure accountant who. between 1980-1985. built up a network of illicit activities tied to drug trafficking protected by the highest ranking police officers during Fernando Belaunde's second government. between 1980-1985. Contrary to Colombia. however. once drug traffickers are exposed. they and their organizations tend to crumble. The two central figures and many others are still in jail and attempts to liberate them have met with strong and effective opposition from the political establishment and from the press[75].

These two aspects entertain with civil society diverse and ambiguous relationships. As for production, there are more and more doubts about the intelligence of treating the coca farmers as criminals, which only makes the Shining Path, the most real and important danger to the country's integrity, stronger. The state should accept the legitimacy of the coca farmers' organizations and design with them alternative development plan. As for drug traffickers, less powerful in Peru and Bolivia than in Colombia, for example, the problem is one of corruption. They are capitalist entrepreneurs that do not want to be bothered by the state and should be vigorously searched for and enprisoned.

Drug trafficking is, indeed, synonymous with corruption. To cite an example: in the Upper Huallaga Valley, in the July-August period of 1988, as well as in other years, traffickers reportedly paid $12,000 in bribes per shipment of cocaine base flown out of the Valley. In one recorded case, $5,000 went to the local military command, $5,000 to the local contingent of the national police, and $2,000 to community organizations affiliated directly with the Shining Path.[76]

On the rare occasions when leading traffickers are arrested, they can bribe their way out of custody on the spot. When traffickers do, in spite of everything, land in jail, corrupt judges or prison wardens may release them from custody. For example, one of Latin America's most notorious drug traffickers, Juan Ramón Matta Ballestores, escaped from prison in Bogota, Colombia, by paying $2 million to each of his guards.[77]

There is a limit to the mafia's ability to penetrate and corrupt enforcement agencies: it cannot buy immunity for all its activities. Hence, the mafia needs an intelligence network to supplement the protection network and provide advance warning of planned anti-drug operations such as raids on laboratories, custom searches, and police sweeps. The network, consists of strategically placed informants in the bureaucracy. Sometimes cocaine traffickers themselves occupy position of trust and responsibility. In Peru, for example, the trafficker Reynaldo Rodriguez Lopez was an advisor to the Director of the Peruvian Investigation Police while maintaining an office at the headquarters.

This intelligence capability functions within a broader system of social relationships is created by the narco-mafia. Cocaine traffickers earn friends and supporters within society by spending money within the society.

Cocaine trafficking, as already noted, buy protection from police, prosecutors, judges, and, where necessary, the military. Time magazine reported in February 1985 that at least 100 Colombian air force personnel and 200 national policemen had been discharged because of drug connections. Also, 400 judges reportedly were under investigation by the Colombian Attorney General's office for alleged complicity in the trade[78].

Cocaine traffickers sometimes try to sway official policy by capitalizing on governments' financial problems. For example, the Bolivian trafficker Roberto Suárez, in a meeting with president Siles' narcotics adviser in 1983, offered to give the Bolivian government $2 billion in four $500 million instalment to help pay off Bolivia's foreign debt. Suárez, according to accounts of the meeting, wanted the Siles government to acknowledge the independence of his cocaine trafficking enclave. In early 1984, a Peruvian trafficker by the name of Guillermo Cárdenas reportedly offered to pay off Peru's national debt in return for his freedom from jail. In the same year, Colombian cocaine traffickers, in meetings with that country's attorney general, offered to repatriate an estimated $2 billion to Colombia in return for official amnesty. Roughly 2 years later, they offered informally to pay Colombia's $13 billion national debt[79].

The state has played an incoherent role that has oscillated between a certain resignation towards an activity that has permitted it to mitigate certain aspects of the national crisis, especially the lack of hard currency and increase in domestic production, and intense, although inconstant, actions targeted more at the coca farmers than at the cocaine industry as a whole. The truth is that the Upper Huallaga Valley is not quite under Peruvian government control and it cannot offer the people who make coca their livelihood crop substitution schemes. The effects of this issues are already transforming the Huallaga population's perception of elected and future governments.

2.2.4 Externalities of the Coca Industry

From a global perspective, it must be recognized that the environmental damage caused by illicit drug production is minimal compared with that produced by other causes, such as the production of clorofluorocarbons. It is, however, at the country level where the impact of illicit drug production is inarguably devastating[80].

Environmental problems associated with the narcotics industries can be included in the category of indirect economic costs. Such costs are associated with the pollution of Peru's waterways. Chemicals required for the refining of coca, such as kerosene, sulfuric acid, quicklime, carbide and acetone, are dumped into the major rivers. Further deforestation is caused by the slash and burn techniques used by the coca farmers to clear plots of land (see Table 2.2.4.a). Present consumption is estimated at 10 million liters of sulfuric acid. 16 million liters of ethyl ether. 8 million liters of acetone. and up to 770 million liters of kerosene. annually. although some of this can be recycled. To the extent that processors spill or dump used chemicals onto the ground. they quickly end up in the region's rivers. The result is widespread deforestation along the riverbanks. land erosion and the poisoning of rivers which are so vital for the livelihood of industries and the population at large[81].

In this light. it is all the more tragic that the Huallaga region has evolved into the world's primary source of illicit coca. Peru's coca growing areas spanned thousand of hectares since the 1980s. The local economy of the Huallaga region was once based on cocoa and coffee produced by small-scale landholders.

The system deteriorated owing to the following: (a) the lack of appropriate land ownership legislation: (b) inadequate agricultural extension services: (c) the absence of viable marketing options and distribution channels: and (d) isolation due to civil strife.

The environmental impact of drug production is an issue that must be seen within the context of sustainable development. The link between population pressure and drug production. for example. is not at first sight obvious. but is crucial nonetheless. Population growth often results in greater agricultural expansion aimed at maintaining minimum subsistence levels. This often results in a decrease in follow periods. Ultimately soil fertility is reduced. This lowers the potential for marginal yields. In view of their income potential and relative ability to withstand harsh terrains. illicit crops are seen as an attractive alternatives. But their harvesting leads to further soil degradation. thereby eliminating the possibility of a return to other crops.

Table 2.2.4.a: Cocaine Processing

Leaf to Paste	Step 1: The coca leaves are put in an above-ground container or in a plastic lined pit. An alkaline material (usually sodium bicarbonate) and water are added to the leaves. Step 2: A water immersible solvent (usually kerosene) is added to water, solution, and leaves. Step 3: Cocaine alkaloids and kerosene separate from water and leaves. The water and leaves are then drained off. Step 4: Cocaine alkaloids are extracted from the kerosene into a dilute acid solution. Alkaline material (sodium bicarbonate) is added to the remaining solution which causes a precipitate to form. The acid and the water are drained off and the precipitate is filtered and dried to produce coca paste, a chunky, off-white to light brown, putty-like substance.
Paste to Base	Step 5: The coca paste is added to sulfuric acid or hydrochloric acid and water. The paste is dissolved into the acid solution. Step 6: Potassium permanganate is combined with water. The mixture is added to the coca paste and acid solution. Potassium permanganate is used in this step to extract other alkaloids and material that is undesired in the final product. Step 7: The solution is filtered and the precipitate is discarded. Ammonia water is added to the filtered solution and another precipitate is formed. Step 8: The liquid is drained from the solution and the remaining precipitate is usually dried with heating lamps. The resulting powder is cocaine base.
Base to HCL	Step 9: Acetone or ether is added to dissolve the cocaine base and the solution is filtered to remove undesired material. Step 10: Hydrochloric acid diluted in acetone or ether is added to the cocaine solution. The addition of the hydrochloric acid causes the cocaine to precipitate out of the solution as cocaine hydrochloride. Step 11: Cocaine HCL is dried under heat lamps, laid out to dry with aid of fans, or dried in microwave ovens.
Cocaine HCL to crack	Step 12: Cocaine HCL powder is mixed with water and baking soda to form a thick paste. Paste is heated in a microwave oven or on a stove. Resulting product, crack, is broken into small chunks or rocks and placed in clear plastic vials for sale to customers.

Source: Andestudio. Market Study: the coca leaf international possibilities. Final Report. ENACO. 1992, p. 8.

In this light, illicit drug production fits into the oft-cited nexus of population growth, agricultural stagnation and environmental degradation.

Coca leaf was cultivated for centuries in the Andes with techniques that were efficient and respectful of the environment. This was carried out in response to social and culture pressures of the ancient Andean word. This, in turn, controlled the extension of cultivated areas. But in the high jungle regions where new areas of cultivation have expanded wildly in the last 15 years, things are different. Colonists settled here attracted by prospects of easy money. They indiscriminately exploit an ecosystem that has enormous potential for the future development of Peru.

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III. Part Two
Assessing Policy Alternatives

3.1. Problems. Strategies and Solutions to Attack Drug Trafficking

The problems of narcotics control in the Andean countries stem largely from the power of entrenched narcotics interests. However. such problems are also attributable to other factors: weak control of government. the absence of strong public support. and tension between civilian and military authorities. The drug issue has also been a source of conflict and mutual recrimination between North and South America. Producing countries and consuming countries blame each other for the accelerating drug traffic and advocate. respectively. demand-side and supply-side solutions. The existence of widespread narcotics cultivation and trafficking in the Andean region. inevitably accompanied by corruption of government and armed forces officials. weakens the reliability of the Latin American countries. Thus. the United States considers the illegal flow of cocaine from Latin America a serious threat to U.S. national security.

Has there been any clear progress in campaigns against drug abuse and trafficking? What has failed? What has worked? What have been the outcomes. intended and unintended. of governmental intervention in this area? Therefore. it is the objective of Part Two to analyze the efforts to reduce or eliminate both the production and supply of illicit drugs and its consumption. It begins with an overview of the role of governments and military: and the responsibility of supply and demand countries. The section concludes with a description of the United States policy. an evaluation and measure of effectiveness and some options aimed at combating narcotics production and trafficking in the region.

3.1.1 Role of Governments

Andean governments find themselves in an uncomfortable position in the war against drugs. On the one hand, the cocaine trade injects needed dollars into Andean economies and employs hundreds of thousands of people. Drug enforcement measures generally have little popular appeal because it is perceived as a program imposed on the Andean region by the United States. Certain U.S. measures such as extradition, the spraying of illicit crops, U.S. military intervention against cocaine laboratories, and economic sanctions against cocaine-exporting countries have caused considerable anti-American popularity: indeed, they arouse substantial opposition. Governments themselves are apt to feel that the war against drugs conflicts with other priorities: for example, coping with inflation and unemployment, promoting economic growth, and combating crime and subversion.

At the same time, Latin American governments are under some domestic and international pressure to control drug trafficking. Moreover, Latin American governments face the threat of reprisals by the United States for not taking strong action. American Congressional attitudes have hardened in recent years, and legislation has endorsed progressively stiffer and more wide ranging sanctions against governments that are uncooperative on drug control.

These contradictory tendencies condition the ways that governments approach narcotics control. So, it is possible to mention several distinct approaches. First, governments set up elaborate bureaucratic structures for fighting the drug traffic. Second, they sought to maximize the inflow of international aid for this purpose and to minimize their own outlays. Third, in Peru and Bolivia, they tried to refocus drug control strategy, stressing interdiction over eradication. Governments find it politically easier to raid cocaine laboratories than to destroy peasants' coca fields. Finally, continuing controversy over narcotics policy within the bureaucracy and within the society at large, has immobilized governments in important ways. They cannot implement enforcement measures that could materially advance the cause of drug control. Significant measures apparently on hold include the use of herbicides to eradicate coca and the extradition of leading cocaine traffickers to the United States.

Latin American governments see the war on drugs as a drain on scarce resources and as underfunded by the international community. They cite the awesome economic and military power of international cocaine mafias and the relatively low levels of international support as reasons for their failure to control the drug traffic. In addition, governments in varying measure perceive narcotics control as imposing economic and social side effects, principally in the form of lost income and jobs. The rich drug-consuming countries, in their view, should compensate for their losses with major new infusions of money and development assistance.

3.1.2 Role of the Military

Andean military establishments do not have a major anti-narcotics mission. Rather, they provide occasional logistical support, such as helicopters and pilots, for operations planned, executed and controlled by anti-drug units of the national police. In Peru and Bolivia, the military has contributed almost no resources or manpower to fight the drug traffic[82]. Furthermore, there have, in fact, been episodes of collaboration between military factions and cocaine traffickers throughout the Andean world. The linkages may derive, as it was discussed above, from corruption, from strategy considerations, or even from shared political and ideological values. Also, the inherent nationalism of the armed forces has been a barrier to increased international cooperation against narcotics. Finally, there is rivalry and historical animosity between the military and the national police in the Andean region. Military establishments seek effective control over the legitimate use of force in the zone: for this reason, they have resisted efforts by the national police to develop an independent drug-fighting capability.

The events of the last decades suggest that the U.S. sponsored narcotics control effort in South America is to some extent a hostage of the military. The police must depend on the military for mobility and firepower. It is evident that Peru provided a much better argument for the use of military, for it is both the principal source of coca and a place where guerrillas are involved in the drug enterprise.

The crop and lab destroyers in Peru faced two serious problems. Farmers planted fields and traffickers built labs in new and more isolated locations. More serious, however, was the inability or unwillingness of Peruvian security forces to protect antidrug workers against the violent resistance which inevitably occurred, especially that of the Shining Path. If the crop eradication and the lab destruction program was to succeed, the Upper Huallaga Valley had to be made secure[83].

Many residents of the Huallaga Valley welcomed the arrival of the Shining Path. When coca growing and trafficking boomed in the lawless of the Valley and tensions were subsequently raised by the antidrug campaign, the guerrillas moved into the Valley and imposed order, something the Peruvian government had not done. Colombian traffickers, who had been abusing the growers, were disciplined and taxed: the Shining Path thus gained support from the growers and income with which to pursue its political ends.

The Peruvian military failed largely because it was ordered to follow a contradictory policy. It could fight the guerrilla or engage in antidrug efforts but not both. Antidrug efforts drove people into the protective arms of the Shining Path while attacks on the guerrillas gave the drug producers a free hand to pursue their business. Peruvian military leaders, by and large, preferred to concentrate on the guerrilla, believing that the Shining Path was the serious threat to national security and one that the military was trained to fight. The United States, however, more interested in destroying drugs and protecting antidrug workers, pressured Peru to focus on drugs.

Peruvians are unlikely to sustain their fear and anger about illicit drug production. They will become bored with drug news and divert their attention to other issues, especially as they slowly adjust to the reality that a certain percentage of the population, even though higher than they might wish, will always produce illicit drugs. The drug problem pales in comparison to other national problems even though it received an inordinate amount of attention through past years. The drug issue has been part of a much larger issue in Peruvian society, that of social control. The Peruvian governments represented, among other things, an effort to restore social control. Peruvian wanted their national government to fight those things which they believed threatened the normal way of life such as terrorism, its educational system, the persistence of poverty, deterioration of its economic infrastructure, reduced clout in the international economy, urban decay, environmental pollution, budget deficit, and what role it will play in international affairs.

3.1.3 Responsibility of Supply Countries

Several Latin American countries account for the bulk of illegal marijuana, cocaine and heroin smuggled into the United States each year from the Western Hemisphere. Some 90% of all imported marijuana that enters the U.S. market originates in one of the following countries: Mexico, Colombia, Jamaica or Belize[84].

Colombia emerged in the mid-1970s as the principal refining country and for more than a decade has controlled roughly 75% of all the refined cocaine exported from the Andean region to the United States[85]. In the last three years, several other countries: Venezuela, Brazil, Ecuador, Paraguay and Argentina have revealed not only transit points but also budding processing centres as well, although still on a relatively small scale. This has come about, in large part, because stepped-up U.S. and Latin American enforcement operations have driven some grower-dealers to search for cheaper and safer alternatives for cultivation and processing outside the traditional coca-growing regions[86].

Since a permanent though varying demand for illegal drugs is likely to persist, it will be necessary to reduce the supply of available drugs. Drug availability can be decreased by operating against every link in the drug chain from cultivation to production and trafficking. Drug crop cultivation must be addressed both domestically and abroad. Drugs must be interdicted while in transit. The diversion of precursor chemicals must be prevented. Illicit profits must be traced to their criminal sources and, where possible, seized and trafficking organizations must be broken. Because drug trafficking is fundamentally a profit oriented enterprise, attacking the economics of every aspect of the illegal drug industry offers a way to reduce drug availability. Interdiction must continue to be a vital component of a balanced supply-reduction effort. Bilateral, multilateral, regional, and international cooperation is critical to the success of any effective interdiction efforts which require flexible and intelligence driven operations. Moreover, it will be essential for the reduction of drug availability the continued development of law enforcement programs and organizations that can move effectively against sophisticated trafficking organizations. For this reason, and in compliance with international drug control treaties, cooperation between countries will need to include the exchange of information, expertise, and assistance to reduce production of illicit drugs in supply countries.

Supply reduction effort should focus on specific crops grown for illicit purposes in the major cultivation zones. This will be supplemented with alternative development projects in rural economic zones, which strive to generate and promote lawful, profitable, and environmentally sustainable production and help to make it possible to overcome the condition that gave rise to illicit crop cultivation. The need here is to promote the cultivation of other crops, such as banana, tobacco, pineapple, rice, coffee, cacao, and potato among others. The use of these crops provides the assurance of the existence of a market. However, it also means that the new producer will be competing with established producers for the same market niche, or will have to try to create a new niche.

Close coordination in agricultural development policy between the Andean countries is also needed, so as to diminish competition between producer countries. All South American coca producing regions are located in a similar climatic belt, and are therefore likely to be producing the same alternative crops. It should also be considered that the United States are likely to be the main export target for any coca replacement crops, and strong competition for a U.S. market niche may result.

The suitability of alternative food. fodder and potential cash crops to larger scale production. their yield potential. and their suitability for sustainable farming systems still needs to be evaluated. Basic production problems need to be solved such as disease and weed control. and unfamiliarity of the grower with the cultivation requirements of the crop.

In order to revive and develop the agricultural potential of the Andean region much has to be done to reverse the damage of land mismanagement and to cope with the increasing demands of an increasing population. The best approach appears to be the development of agroindustry systems integrated into a rural development package which should be aimed at small to medium sized farms in areas that are not too isolated to be integrated into regional and national markets. The objective must be to stop and reverse environmental degradation. rehabilitate terraces. increase the productivity of slopes. protect and regulate water sheds. to improve and develop crop varieties and their adaptation to the environment. Agricultural development must be accompanied by the building of local infrastructures (roads are to be upgraded. power plants and agricultural facilities constructed. and marketing facilities). by making credit available to local farmers. and by gaining the cooperation of local people through involving them in the decision-making processes. With active community participation in planning and execution. activities will be developed to create lawful opportunities to generate income. reduce poverty. raise the quality of life. and conserve the environment in order to reduce the supply of drugs.

3.1.4 Responsibility of Demand Countries

There are approximately 22 to 28 million marijuana smokers in the United States. 6.3 million regular users of cocaine and 0.7 million heroin addicts. At retailer street prices. the

United States public may spend as much as $150 billion on illicit drugs a year[87]. According to Donald Mabry, the profit potential is obviously immense at all levels of the industry, although some 90% of the value-added is realized in the distribution process once the drugs have been brought into the United States: only 8% to 10% of the profits accrue to the Latin American source and transit countries.[88] In the short-run, a general strategy to drastically reduce the American consumption of narcotics has to be defined. This strategy could include rehabilitation and prevention programs. Pursue a vigorous advertising and public communications program dealing with danger illicit drugs. Strengthen law enforcement, including federal, state, and local drug task force, to combat drug-related violence, disrupt criminal organizations, and arrest the leaders of illicit drug cartels. Break the cycle of drug abuse and crime. Promote international policies and laws that deter money laundering and facilitate anti-money laundering investigations as well as seizure of associated assets.

In order for supply and demand initiatives to work, they must be supported by appropriate organizational structures, including comprehensive, coordinated, community based strategies, and intergovernmental (federal, state, and local) coordination. Information on which drug policy decisions are based must be timely, accurate, and available to all drug control agencies. Initiatives should be supported by research and the application of emerging technologies. Specific operations must be supported by good intelligence that both anticipates drug trafficking efforts and allows for their criminal prosecution.

3.1.5 Peruvian Position Facing the Drug Trafficking Problem

The Peruvian government has never exercised full control over its national territory. In these remote jungle regions, traffickers establish coca plantations.

laboratories. airstrips. and storage facilities. Such areas are remote from metropolitan centres. relatively inaccessible. and patrolled by guerrillas or other hostile groups.

During the early eighties. a blind eye. which means that there was no effective program initiated against drug trade in the region. was cast by the Belaúnde administration on the drug trade even though it was rumored that the police and the army were involved. The United States began pressuring Peru to fight against the illicit industry. They supplied Peru with financing for law enforcement. crop eradication and crop substitution programs. Economic hard times. however. meant that a lot of the plans backfired and high unemployment and hyperinflation contributed to the growing number of dissatisfied peasants. The Shining Path took advantage of the growing unpopularity of the government in remote areas where the central authority's power was weak. The guerrillas intended to act as a union for the narco-peasants by attempting to cut out the Peruvian middlemen. In this way. they intended to negotiate a better price for the peasants who. in return. were taxed by the Shining Path to fund the purchase of ammunition and weapons. Further backlashes to the anti-narcotic policies were due to the fact that they were being identified with external pressure. particularly from the United States. The Garcia as well as the Fujimori administrations stepped up the anti-drug policies by destroying laboratories. bombing clandestine airstrips. seizing coca paste and arresting those involved.

As it was mentioned in the first section. president Fujimori announced in late 1990. his commitment to fight drugs through the implementation of a comprehensive strategy. The strategy would place narcotics-related military and law enforcement efforts. demand reduction and alternative development under one specialized governmental office. the Autonomous Authority for Alternative Development.

U.S. has been in engaged discussions with the Peruvian government on the basis of this proposal and are hopeful that the two governments will be able to work together to combat narcotics production and trafficking in the future. The ability of the Peruvian government to implement its comprehensive narcotics strategy will be an important indicator of its resolve in narcotics issues.

The government policy is to eliminate illegal coca production by providing viable economic alternatives. This effort is nationwide, recognizing that wide-spread poverty is a major impetus for continued drug trafficking. The government's program also includes efforts to improve the administration of justice and to promote public awareness of the harm done by the drug trade. The Armed Forces increasingly have recognized their responsibility to support narcotics enforcement, since it is evident that narcotics supported internal subversion, and incursions of Colombian trafficking aircraft into Peruvian air space, threaten national security. Police units charged with counter-insurgency and other functions began making narcotics arrests and seizures as well. Nevertheless, progress has been made in regaining control of narcotics cultivation and processing areas from the Shining Path, resulting in only modest narcotics seizures and lab destructions.

The government labors under many handicaps, but it has undertaken a variety of initiatives to exercise more effective control. Thus, according to the United Nations Drug Control Programme, Peru has signed comprehensive drug control and alternative development agreements followed by supplementary agreements on counter-narcotics law enforcement, economic, and military assistance with the following countries: Argentina, Bolivia, Brazil, Colombia, Chile, Ecuador, the United States, Italy, Mexico, Cuba and Paraguay[89].

To date. the following multilateral drug control agreements have been signed by Peru: establishment of the Inter-American Drug Abuse Control Commission (1986). Inter-American Programme of Action (1986). Declaration and Programme of Action-Ixtapa (1990). and Inter-American Programme of Quito (1990). Relevant subregional agreements signed by Peru include the following: Cartagena Agreement. signed by the president of Bolivia. Colombia. the United States and Peru (1990). San Antonio Declaration. signed by Bolivia. Colombia. Ecuador. Mexico. Venezuela. the United States and Peru (1992). and the Memorandum of Understanding (MOU) signed by Argentina. Chile. Bolivia. Peru and UNDCP (1994).

In the past years have seen United States drug agencies pay increased attention to international aspects of cocaine trafficking. Recognizing that police actions alone will not work. the Drug Enforcement Administration and the International Narcotics Matter Office of the U.S. State Department. proposed to the government of Peru that it reduce coca leaf cultivation through a program of crop eradication and economic incentives.

The U.S. government. in cooperation with the government of Peru. proposes financing a set of economic alternatives to coca leaf production in the high jungle. while a massive eradication and control program there is concurrently carried out.

The goal is to eliminate coca leaf totally in one area of Peruvian high jungle (the foothills of the Andes). where the U.S. government claims that enough leaf is grown to supply up to 35 percent of the cocaine consumed in the United States. The proposal calls for the development of an economic infrastructure in this region which. for over a decade. has seen very little development. and which remains poorly integrated with the rest of the nation. Therefore. strategies have been ongoing with the objective to reduce illicit coca production in Peru. In such, in May 1995, a project grant agreement was signed between the government of Peru and the United States acting through USAID related to the funding of alternative development activities in determined coca growing areas (See Map 4). The budgetary provisions include an estimated USAID funding of US$ 30 million over a five year period, supplemented by a counterpart contribution of the Peruvian government of US$ 14 million[90].

Regarding interdiction, a new strategy was announced for the fight against drugs, which comprehends the control of the rivers in the coca zones (a new transport route for drugs and production supplies). Likewise, the creation of 3 Anti-drug Tactical Operation Divisions (DIOTAD) which cover the east of the country have also been announced. Moreover, the creation of 2 anti-drug bases in these zones has been announced for 1997, as well as the creation of twenty mobile bases, which would travel the areas with the largest amount of drug trafficking activity in the jungle (their installation would count with North American support).

In January 1997, the Secretary of Health and the head of the Fight Against Drug Abuse Council (CONTRADROGAS), Dr. Marino Costa Bauer announced the institution's objective to reduce the cultivation area by 50% for the year 2000. They seek to reduce the area to approximately 60,000 ha and in the long term to an amount sufficient to fulfill medical and traditional uses.

The initiation of the National Alternative to the Cultivation of Coca Leaves Development Program was announced. According to official sources, it will require an investment of 1.5 to 2.0 billion dollars. The first stage will begin in early 1998. A group of projects for the development of the productive infrastructure and the fight against drugs (in prevention and rehabilitation areas) for 430 million dollars has been presented to the member countries of the Mesa de Donantes (Donors Board) to seek financing through the canceling of debt through investment. Likewise an agreement between the National Development Institute and the International Development Agency for 4 million dollars destined to credit for the peasants of the Apurimac River valley to substitute the cultivation of coca leaves has also been announced (See Maps 5-6).

Regarding the administration of justice for drug trafficking cases, the National Anti-drug Upper Court was created in 1996. According to the International Commission of Jurists, it specializes in illicit drug traffic crimes, which will permit the processing of the most serious cases. As of November, 5 decentralized offices had been installed, which in two and a half months received 601 cases rendering judgement in 38 of them. In March 1997, the Judicial Power Reorganization Committee deactivated the Court, establishing that the cases be handled by the Second Transitory Criminal Branch of the Supreme Court[91]. Said branch would be in charge of creating a new judicial administrative structure and handling the final appeals in the cases of drug trafficking and related crimes.

In this context, the anti-drug czar, Barry McCaffrey, praised the governments successes in the cultivation reduction policy. The full certification received by Peru is largely due to these achievements. The rupture of the air bridge between Colombia and Peru maintained the fall in the price of coca paste and forced the peasants to abandon coca for other crops which would not bring them losses[92].

These certifications are the annual evaluation made by the president of the United States on the anti-drug management of the 31 producing or transfer countries. Certification this year offered no surprises but simply confirmed the predictions of the analysts: Peru and Bolivia were fully certified whereas Colombia was once again decertified notwithstanding the efforts made by its government in the fight against drug trafficking. In contrast. Mexico received full certification despite accusations of corruption in official instances. and the scandal caused by the detention of the director of the National Institute for the fight against drugs. General Jesus Gutiérrez Rebollo. at having been bribed by the leader of the Juárez Cartel. I believe the difference in treatment. in comparison with Colombia. is basically due to political reasons and the desire of the United States to maintain good relations with a country with which it shares a large border and with which it maintains important commercial relations. However. there is pressure in the government and Congress to review the certification of Mexico.

Finally. the government's overall objective is to achieve a balanced cooperation programme. consolidating alternative development efforts and strengthening activities in the fields of supply and demand reduction and control measures. including precursors and essential chemicals control. According to the UNDCP in Lima. over the past ten years. several projects have been concentrated mainly on supply reduction through alternative development in the Huallaga and Quillabamba areas[93]. These alternative development projects are currently undergoing consolidation phases. and are scheduled to end in early 1998.

Future alternative development efforts in Peru must become fully integrated in national alternative-rural development programs that are effectively supported by the government. within the framework of the National Plan for Drug Prevention and Control 1994-2000. Also. new alternative development projects should count to the greatest extent possible on substantial national and international financial resources. Alternative development and drug control should be linked with the broader development dimensions of international technical cooperation. in particular considering the need to count with support for integrated rural development. Accordingly. linkages need to be established between alternative development in the context of the National Plan for Drug Prevention and Control. and the development plans in the selected regions. including the role of national development institutions such as the Ministry of Education. Ministry of Health. Ministry of Agriculture. Ministry of Justice and the National Development Institute. among others.

Such national institutions will need to promote the incorporation of the drug dimension into mainstream national rural development programs. with substantial emphasis on the monitoring of illicit cultivation. the propagation of community commitment towards the elimination of illicit cultivation. and the design of integrated area development schemes which address drug abuse problem.

To curb illicit traffic. emphasis will have to be placed on national and subregional law enforcement training programs. as well as on technical cooperation in the areas of education. treatment. rehabilitation. social integration. customs control. data gathering. money laundering and precursors control. Both in the demand reduction and control measures fields. Peru will also benefit increasingly from other subregional programs involving Argentina. Bolivia. Colombia. Mexico and Chile and possible other countries.

In the context of the National Plan for Drug Prevention and Control. the government will necessary have to provide policy guidance and selected direct support in the field of institutional capacity building. particularly at the legal. training and managerial levels. Special interest should be placed on assistance to develop mechanisms for measuring illicit crop areas, and monitoring the progress of drug control efforts.

3.1.6 United States Intervention

The primary U.S. policy response to its domestic drug abuse problem has been to attempt to reduce foreign drug supplies through interdiction, coca seedbed eradication, alternative development, law enforcement, public awareness, and international cooperation.

These areas of cooperation are set out in agreements between the two countries. Effective counter-narcotics law enforcement will raise the costs for trafficking in Peru and Colombia, while interdiction and seedbed eradication in Peru will block the delivery of illicit drugs, erode the profitability of coca cultivating and processing for coca growers, and create economic conditions in which alternative development programs become more attractive and effective. The government of Peru must provide adequate security for alternative development programs in the coca-producing areas to be successful.

The United States has traditionally viewed drug abuse as a foreign problem, crossing its borders from other countries. As a result, the focus of U.S. cooperative efforts has been on reducing the supply of drugs produced by its neighbours in the Western Hemisphere. Only recently has drug abuse become a critical problem in these countries, erasing the historical distinction between consumer and producer nations. Governments strategies must now reflect the complex interaction of supply and demand within individual countries as well as across national boundaries.

There is a multitude of sociological, economic, and individual reasons for the growth of drug abuse in Latin America. One theory is that excessive supplies of coca, a by-product of the explosion in U.S. demand in the past two decades. helped create a new domestic market in the producer countries. In contrast to the United States. where drug supplies rush in to meet demand. the root of the problem in Latin America appears to be the reverse: that increasingly cheap. easily available drugs led to new consumption.

The U.S. proposal to eradicate coca leaf and develop the Peruvian high jungle serves a number of North American government interests. It would also create economic incentives in the high jungle which would result in a transition away from farming based upon a simple and traditional agricultural technology to the cultivation of cash crop for the legitimate market. further integrating peasants into the commercial sector through the production of a marketable surplus.

Cultivating and processing these other crops and agroindustrial products depends more on farm machinery. chemicals and management services than does simple coca leaf farming. U.S. aid to eradicate coca leaf and promote alternative crops. therefore. implies Peruvian dependence on imported farm technology as well.

Hence the appeal of the U.S. proposal would increase Peru's agriculture and agroindustrial exports as well as its production of food crops. It might increase work opportunities for Peru's unemployed and a geographical area into which some of Peru's highly concentrated highland Indian population might be funnelled.

Another motive for the U.S. proposal to eradicate coca leaf in Peru is that it represents an attempt by drug control agencies in the U.S. to show that they can effectively stop cocaine trafficking. Therefore. the U.S. effort to eradicate coca leaf. even if only partially successful. can also be viewed as an effort by the United States government to deal with the corruption and disequilibrium of the circulation of vast amounts of illegal currency and its causes.

In this scenario. Peru presents a difficult situation because of the complexity of its programs. Therefore. the United States has helped to improve counter-narcotics cooperation with the Peruvian policies. assisting the Armed Forces to assume a more vigorous role. This cooperation has resulted in increased seizure of drugs and essential chemicals. laboratory busts and destruction of clandestine airstrips. Consequently. pressure on the trafficking organizations and destruction of their activities have increased.

Furthermore. the Fujimori administration has publicly committed itself to fight narcotics traffickers and insurgents. and to adhere to international human rights standards: but with a wide range of serious internal problems. it has moved slowly and sometimes uncertainly toward developing a comprehensive strategy. There is. however. significant support within the government and in the public for developing a workable counter-narcotics program in cooperation with the United States.

Despite the security threat posed by the Shining Path and without the entire cooperation of the Peruvian military. Peruvian law enforcement agencies have destroyed more laboratories and seized more cocaine than in previous years (see Chart 3.1.6.a). However. these efforts only had a marginal effect on the overall flow of cocaine base from Peru.

In cooperative efforts. the United States and Peru signed a Tax Information Exchange Agreement at the Cartagena Drug Summit in 1990.[94] This agreement will allow for the exchange of information between tax authorities of the two countries. and will also be helpful in money laundering investigations.

Chart 3.1.6.a: Coca Leaf. Coca Paste and Cocaine Seizures and Drug Arrests

	1993	1994	1995	1996
Seize of Coca Leaf (MT)	103.95	145.64	209.02	119.42
Seize of Coca Paste (Kgs)	8.431.39	10.540.85	15.002.21	11.360.74
Seize of Cocaine (Kgs)	440.9	93.68	7.658.84	692.06
Arrested by the National Police (000)	5	6.6	10.7	15.5

Source: Anti-Narcotics National Bureau-Dinandro. Lima. 1996.

Upon the request of the Director of the Anti-narcotics Division of the Peruvian National Police. DEA has been providing direction and input on how to improve the intelligence structure of the anti-narcotics division and the ability of the organization to provide counter-narcotics intelligence to fight drug-trafficking.

3.1.7 United States Policy and Strategy Goals

The drug problem has been assuming growing importance on the world scene. The overall problem of illegal drugs and related crimes represents a direct threat to the health and well-being of the people of the hemisphere. The problems of drug abuse and demand. and the production. trafficking and illegal distribution of drugs. including designer drugs. continue to be serious and intertwined. All countries in the hemisphere are being affected by this and recognize they have a shared responsibility to ensure that all aspects of the problem are addressed. This is a complex. world-wide and constantly changing problem for which there are no simple solutions. In this regard. drugs pose as great a risk to national security in the United States as well as in the Andean countries as terrorism. environmental degradation. among other factors.

Against this backdrop, narcotics control has emerged in recent years as an increasingly central issue in the formulation and implementation of American foreign policy. The U.S. goal is to reduce the flow of drugs to the United States by demonstrating to the international community that there is a common interest in stopping this menace and by working with the producer and transit countries to strengthen their political will and stability to fight it.

In this context, in 1988 several important breakthroughs occurred that have put the U.S. on a course reversing the dangerous and costly production, trafficking, and abuse trends of earlier decades. According to the U.S. Department of State, the passage of the Anti-Drug Abuse Act of 1988 established the Office of National Drug Control Policy (the Drug Czar) and mandated the development of a comprehensive, integrated, national drug control strategy. At the same time, the United Nations completed the UN Convention Against Illicit Traffic in Narcotics Drug and Psychotropic Substances, an agreement that set the stage for unprecedented international cooperation to pursue increasingly complex international counter-narcotics tactics[95].

The Office of National Drug Control Policy has the overall responsibility for formulating and coordinating the federal government's drug control policy. It moved immediately to assess the counter-narcotics threat and in 1989 published the first National Drug Control Strategy, which it has updated annually. The strategy is comprehensive, addressing supply, demand, and treatment, its top priority being to reduce the availability of cocaine to the United States. To translate the policy priorities into action the strategy seek to achieve progress across the following fronts.

First, it seeks to attack the major organizations by creating an international political and legal environment that is hostile to narcotics trafficking. In many countries this means working to pass conspiracy, asset forfeiture, and other laws and then develop the institutions needed to prosecute the leading traffickers who manage and finance the trade. Yet this leadership has generally been overlooked by past control tactics that have focused on interdiction and crop suppression. The leaders have been able to rebound from these operations usually by expanding and depending their corrupt ties to the political, legal, and security institutions. The way to break this chain is for governments to target, investigate, and convict the drug leaders.

Second, the strategy seeks to increase the cost of operations to international trafficking through interdiction and other enforcement actions to attack the drug infrastructure. These measures are most effective when they can erode traffickers' profits and weaken their organizations, raise drug prices and lower demand, and create financial barriers that prevent new organizations from entering the trade. In this regard, the strategy emphasize improved detection and monitoring to locate drug shipments, caches, and processing centers and enhanced capabilities of response forces to attack these targets.

Finally, the strategy aim at reducing and eventually eliminating the cultivation of illegal drugs. This goal involves not only efforts to curtail production in traditional areas that supply the U.S. market, but to prevent cultivation from spreading to new areas as well. Crop substitution or rural development schemes without the enforcement deterrent simply will not work, and this latter condition almost always requires governments to have political control over the growing areas. Consequently, crop control efforts are not the work of a few months: they take time to effect a substantial change.

Thus, a major component of the American international efforts continues to be supporting the principal cocaine source countries: Peru, Bolivia, and Colombia, in their fight against the multinational criminal organization that support the production. processing. transportation. and distribution of drugs to the United States and other countries. For an effective long term counter-narcotics strategy. the U.S. is working with these countries to enhance their institutional capability. This effort will require high priorities to bilateral programs with important drug-fighting missions. such as man-time and coastal patrols. customs services and crop control through training and material assistance. In providing this assistance. U.S. will insist that internationally accepted standards on human rights be respected.

Since Brazil. Ecuador and Venezuela also have the potential for large-scale profitable cultivation of coca leaf. and because of their proximity to large-scale trafficking centres. the U.S. will need to ensure that neither the cultivation nor the trafficking organizations spread to these countries.

A key question raised by policy makers is whether or not the strategy can work: that is. will the American government proposed increases in aid (military. economic. law enforcement) provide the Andean nations with sufficient assistance to combat drug production and traffic? And. if so. would this have a favourable impact in the sense of reducing production of illegal drugs and drug related crime?

The international drug control policy of the United States is aimed at curtailing the international trade in illicit drugs. In this effort. cooperation with and by other nations is essential. U.S. seeks to reduce the foreign supply of drugs by motivating other countries to engage their own resources and efforts to combat the worldwide drug trade. to dismantle their own illicit drug industries and to reduce the demand for drugs.

U.S. will assist these governments with appropriate but selective programs to strengthen their institutions. and to encourage them to undertake more effective actions against the drug trade. particularly in such high-value elements as money flows and precursor chemicals. Major emphasis on the cocaine transit areas is being placed on the three key source countries of Peru. Bolivia and Colombia. which are dealt with in the Andean strategy. The principal focus of this strategy is to block the flow of drugs destined for the U.S. at the international checkpoints between the three principal producer countries and U.S. borders[96].

Through these and other programs. the U.S. will seek to raise the level of national concern about the extent and nature of drug production. trafficking. and use. the acute threat to national security posed by the entrenchment of drug trafficking and their interests. and the danger posed by the drug trade to stable sustained economic growth.

3.1.8 Evaluation and Measure of Effectiveness

A key question facing policy makers is how to evaluate the success of the strategy. An important issue is that given demonstrated traffickers ability to adapt quickly to policy changes and change course accordingly. a need may exist to modify policy. goals. and implementation methods. For this reason. the strategy may be seen as a changing or evolving process. In this context. quantitative goals. such as the reduction in the amount of coca produced. are viewed as crucial aspects of progress. However. failure to achieve such goals in the short run does not necessarily mean that the strategy will fail over the long run. Experts generally agree that. due to the clandestine nature of the business. it is impossible to know with any precision the exact amount of coca leaf grown. cocaine produced. and cocaine shipped: in addition to which. important sectors of the trade are decentralized by the presence of many small suppliers.

Without access to such data and without truly reliable base figures. it is difficult to guess with any reliability whether. indeed. drug production and shipment to the United States is increasing or decreasing according to any specific percentage. Moreover. since the law enforcement can seize small percentage of the drugs on the market. any sustained increase in the amount seized may only indicate. on one level. that more drugs are entering the United States and other consumer countries and are available for seizure. A major weakness of the arguments that question the reliability of statistics. however. is that they are the only measure available. Consequently. given these limitations. most analysts use such figures with caution and complement their evaluation with other. less tangible indicators.

Some of the indicators used in evaluating the effectiveness of the strategy include such tangible figures as number of aircraft seized or intercepted. amount of cocaine seized. number of arrests of major traffickers. dollar value of assets seized. quantities of chemicals seized. and hectares of drugs eradicated. However. analysts suggest that less tangible indicators might include host government levels of cooperation and attitudes. host country public opinion on drug cooperation. host nation levels of corruption. changes in trafficking modes. increase in costs to traffickers. restructuring of traffickers organizations. and levels of coordination and cooperation among the U.S. government agencies that formulate. implement. fund. and oversee the strategy.

The eventual criteria for evaluating U.S. and host country law enforcement and military efforts will be closely linked to the goal of suppressing the international drug trade organization. Host countries will be judged as much by the result of their efforts as on the efforts themselves. The U.S. will judge as effective those efforts resulting in sustained, net reductions in trafficking activity, not merely those efforts involving a net increase in host country effort or manpower.

3.1.9 Options

What is to be done? One major U.S. tactical option might be to finance mobilization of Latin America's drug-fighting capabilities. The United States could provide source countries with the billions annually required to establish effective control over drug-producing areas, many of which are occupied by terrorist forces of mafia organizations. In practice, this option would require firepower, helicopters, communication equipment, and intelligence support. In addition, producing countries could be given more advanced technologies for combating the narcotics industries via beefed-up bilateral and multilateral aid programs: herbicides for spraying, radar systems to track the movement of drug smugglers' aircraft, modern anti-drug weapons, electronic devices to bug and jam traffickers' communications, and heat-seeking equipment to detect drug laboratories. In many Latin American countries, more sophisticated security systems for top government officials, judges, and witnesses would have to be part of this option. Such mobilization, of course, cannot take place unilaterally: politically difficult institutional reforms would have to be made in drug-producing and transiting countries to enable them to cooperate in a reciprocal fashion.

A second U.S. tactical option might be to Americanize its anti-drug operations in Latin America, which would entail the U.S. government assuming drug enforcement functions that source countries do not perform, if those countries consent. Models of Americanization are the extradition and trial of drug traffickers in U.S. courts and the U.S. Army operation against cocaine laboratories in the region. The effectiveness of the Americanization model, however, inherently limited and can produce rejections in some countries for the introduction of U.S. forces. Americanization, is therefore, a risky, potentially counter-productive approach that should be applied only under extraordinary circumstances.

A third U.S. option might be to support Latin American governments' efforts to come up with viable economic alternatives to the drug trade. The United States could make a major contribution by helping the economically depressed Latin American nations to provide crop and income-substitution programs for drug farmers. It could help open new economic opportunities by lowering imports barriers for legitimate exports (textiles, sugar, coffee, flowers, etc). It could also alleviate the crushing burden of Latin American debt by taking the lead in devising new formulas of debt relief. Indeed, it will be unrealistic to expect the Andean countries to commit economic suicide by destroying a major source of foreign currency without some assistance to overcome the destabilizing effects of such actions. In this context, economic aid is viewed as part of the price that must be paid to obtain the cooperation of host nations in implementing policies whose components may well provoke economically and politically disruptive fallout. Definitely, a renewal of economic development in the region is an essential component of any successful, long term effort to reduce drug trafficking.

A fourth, radically different tactical option would be to abandon the war against drugs and move instead to legalize, or at least decriminalize, drug consumption.

Proponents of legalization or decriminalization claim that a distinction should be made between the public health problems caused by drug abuse and the violence and criminality that surround the drug trade simply because it is illegal. They believe that the best way to curtail drug trafficking is to treat drugs as a public health problem rather than a criminal one. It would be possible to remove the clandestine profits from the drug trade. eliminating the motives of criminal gangs to get involved in the trade. corrupt police and judges and kill. Moreover. the government could tax the sale of drugs. thereby earning billions of dollars in revenue to finance programs in drug education. prevention and rehabilitation.

There are. of course. people that consider the idea of legalizing drug use out of the question. Drug abuse may increase if drugs are legalized: there would undoubtedly be many practical problems in setting up a distribution system for drugs.

The central point is that the public health and safety aspects of drug abuse can. and should. be separated from the violence and criminality arising from illegality. Logical or not. however. it is abundantly clear that political winds in the United States are not in favour of legalization: hence this option. at least for the time being. does not appear a viable or realistic method for Latin American drug trade.

In this section I bring together various options to deal with the problem of drug trafficking. the proliferation of coca destined for illegal consumption. and the abusive consumption of drugs considered illegal. especially in the Andean countries. cocaine.

I am a defender of the coca leaf. of its traditional consumption and cultivation. and I am in favour of its beneficial industrial production. I am also roundly opposed to drug trafficking and its consequences. as well as the illegal use of drugs in both North and South. However. I reject the war on drugs as a matter of principle because it compromises the sovereignty of the Andean countries and has been unable either to reduce drugs trafficking or the abuse of drugs.

This is the starting point of a U.S. intervention, because any solution based on military or police actions only makes the problem worse. The only result of more than 10 years of the imposition of the U.S. strategy is the proliferation of drugs trafficking, and the growth of illegal drugs use.

The International Narcotics Control Board, has recognised that the policies followed until now should be reviewed, and the UN Commission on Narcotics Drugs has indicated that the problem needs to be faced as a whole, respecting the social and cultural aspects of consumption. I would agree with this, although I would stress that the same issue should be extended to producers of the raw materials used in the production of drugs.

The peasants producers themselves should work to establish sustainable integrated rural development projects in the areas in which coca is produced, and in those areas where most of the peasants producers come from. Besides the neoliberal market model, I believed that a new proposal should be conceived from below, given impetus from within the producer countries, and designed for their benefit, structurally independent, decentralised, redistributive, and ecologically sustainable. This would involve the creation of internal markets, the development of agroindustry (always emphasising peasant production of foodstuffs- a need to change the national food policy which has often promoted food imports over the development of Andean crops), and would include the design of economic alternatives to drug trafficking and drug production.

That is to say, the proposal implies a model which differs from the traditional policies aimed at tackling poverty, one which involves the full participation of the population, and which respects the cultural aspects of agricultural production and consumption. The coca leaf is one of these traditional agricultural products, which is fundamental to Peruvian and

Bolivian society. The proposed new economy would not be based, as has up to now been the case, almost exclusively on the cultivation of coca and its illegal derivatives: it would be based on agricultural and agroindustrial diversification, beside which small but necessary cultivations of coca would be maintained. The model should be based on multicropping and should combine different ecological niches and produce primarily for the internal market, although also for export if this were considered advantageous, while always maintaining a balance with nature.

This kind of development necessarily implies that the economy in which drugs trafficking and rural poverty exist would have to be replaced by an economic structure that offered a real alternative. It would be important to preserve the positive aspects (above all technical, social, and infrastructural) of the current alternative development' programmes financed by international organizations (USAID, UNDCP, etc) and donors countries (Germany, Sweden, Italy, Japan, etc).

Stimulus should be given to macroeconomic policies that favour rural production, help to reconstruct the food production system, the rational exploitation of forest, and the export of competitive goods, while always prioritising the social agenda.

This necessarily implies revising existing economic policies which have palpable negative effects on society. Furthermore, such policies are being revised around the world, both in the North and the South. Several bodies are involved in the search for new policies, such as the World Bank, the IMF, the Economic Commission for Latin America and the Caribbean (ECLAC) and the Latin American Economic System (SELA). ECLAC and SELA identify the search as one for policies of growth with social progress.

There should be a wholesale reassessment of policies on privatization. agricultural credit. exchange rate. prices paid to producers. import duties. foreign technical assistance. investment. national and foreign trade. productive and social infrastructure. and so on. The current undecentralized. poverty-producing export model does not totally work for the majority of the population. For this to be considered. it is vital that the social organizations be involved in its revision.

Dealing with the problem should be a serious concern at regional. national and international level. It is an alarming situation. as important as the problem of urban and rural poverty. Indeed. it is perhaps more accurate to think of it as a consequence of this poverty. Anti-drug campaigns in the North and in the South should not fall into the error of following the official discourse of the war on drugs. a discourse which speaks only in terms of the guilty. that is. the countries of the South. and of the victims. the countries of the North. The problem is an overarching one. multilateral and interrelated. which encompasses medical. public health and cultural themes. as well as a stronger law enforcement and judicial systems. better government control over drug-producing zones. and a pattern of self-sustaining economic growth.

Notes

[82] Donald J. Mabry. *"Andean Drug Trafficking and the Military Option: The Military Review"*. Washington 1990. p. 39.

[83] For more detailed examination of the coca enterprise and U.S. drug policy in Peru see Edmundo Morales. Cocaine: White Gold Rush in Peru. 1989.

[84] Rensselaer W. Lee III. *"The Drug Trade and Developing Countries"*. (Policy Focus 4: 1987).

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[86] L. Tullis. *"Beneficiaries of the Illicit Drug Trade: Political Consequences and International Policy at the Intersection of Supply and Demand"*. Discussion Paper 19. UNRISD. March 1991.

[87] International Narcotics Control Strategy Report: INCSR. 1996.

[88] Mabry. p. 45.

[89] Report of the United Nations Drug Control Programme. *"Anti-Narcotics Activities in Peru 1984-1993"*.

[90] U.S. Congress. Senate Committee on Appropriations. Department of Defense-Support for Drug Interdiction. Washington D.C.. 1995.

[91] *"The Andes: emergent or emergency?"*. Andean Commission of Jurists. Lima. 1997.

[92] Interviews with Peruvian narcotics experts in Lima. September 1997.

[93] Ibid.

[93] Review of the 1991 International Narcotics Control Strategy Report.

[94] International Narcotics Control Strategy Report. U.S. Department of State. 1996.

[95] Review of the 1991 International Narcotics Control Strategy Report.

IV. Conclusion

The purpose of this thesis has been threefold: (a) to describe the political economy of the size of the illicit drug sector. (b) to have a better picture of the structure of the cocaine industry and finally (c) to provide assessments of policy alternatives to attack drug trafficking in Peru.

In the first section the purpose was to analyze the macroeconomic impact of the illicit drug sector on the economy and viceversa during the period 1970-1997.

The problem facing Peru were a daunting complex of economic. political and social ills. Structural adjustments did not always succeed in such years. But neither did some alternatives strategies. In the early 1980s Peru tried stabilization programs with little success. Its efforts could not overcome the effects of both world recession and the debt crisis. Economic conditions deteriorated. inflation soared. real output fell. and widening budget deficit appeared. Stabilization policies nonetheless began until the last quarter of 1988. when the government announced a severe readjustment of prices that increased consumer prices by 114%. The adjustments consisted primarily of price increases without real wages increases. characterized the last two years of the Garcia's administration. By the time the Fujimori's administration came to power in 1990. inflation was running close to 3.000% a year. Production and wages were falling. Adding to the problem of Peru was the Shining Path. a corp of fanatic guerrilla insurgents seeking to purify Peru by violence.

Fujimori's reforms in trade. fiscal policy and deregulation. coupled with renewed debt services payments that repaired relations with the international financial community. have restored the credibility of the Peruvian government.

Fujimori's commitment to real structural economic reform has been put to the test by a domestic political environment that remains troubled by labour unrest, sporadic guerrilla terrorism, and popular discontent. Structural adjustment demanded austerity: it called for deep cuts in government spending to cut budget deficits. It also meant removing price controls and freeing market forces to promote efficiency.

As Peru's economy has become more stable, the public and private sectors have let go hundreds of thousands of workers. But the government has not strongly focused yet on social programs like training for laid-off employees, education, health care and housing.

I recognize that in the context of global crisis triggered by neoliberal economic adjustment programs, peasants producers have been left with no alternative but to produce coca for the drugs traffickers in order to combat their poverty. In the current national and international circumstances it is the only profitable product available to them. As a result of this, the economic structure becomes dependent on a prime export product which degrades natural resources, enriches only a small section of society, retards medium-term production, and makes the pricing structure of the whole economy chaotic. Finally, it leads to the development of an economy which strikes at the peasant economy, distorting it by removing the incentive to produce foodstuffs.

Society as a whole becomes heavily influenced by the problem of drugs, which leads to ever greater damage to the social structure by imposing the rules of the game which the drugs mafias follow.

Politics is affected by the same process, closing the spaces which worker and peasant organizations had previously opened up, as well as destroying the formal democratic structures which the ruling classes had imposed on them.

The environment deteriorates. leading to levels of destruction in the Andean-Amazonian basin that are so great they cannot be measured. Whereas the traditional cultivation of coca leaves does not damage and erode the environment. cultivation destined for the coca by-product export does.

The analysis of the macroeconomic impact shows that coca by-product exports directly determine the real exchange rate. and indirectly determine the exchange rate through the influence on non-banking securities. Thus. despite the declining importance of the coca sector over Peru's GDP due to a drastic fall in the price of coca leaf and its overstock as a consequence of stronger prevention activities in the Andean region. the sector still has an important macroeconomic impact. It has also effects when the dollars obtained from the illicit exports are cashed and used to buy good and services. The indirect effects of coca exports induce a demand push on inflation that exacerbates the pressures on anticipated devaluation of the nominal exchange rate. These effects have to be considered to fully determine the coca export impact and interpret the implications of estimated impact coefficients.

In Part I an attempts has been made to improve estimates of and to calculate the size of the illicit drug sector in Peru. It is important to emphasize here that to the extent that we are dealing with an underground activity the resulting estimates can only be considered good efforts to record an illicit sector. The data developed here have been based on field work in coca growing areas. and microeconomic data on illicit coca production gathered by various organizations. It is also important to mention here that the quality of the estimates have been improved somewhat due to the availability of data for certain variables. such as prices at all levels. since they are recorded for several zones. Thus. given that coca prices at various stages (paste, base and cocaine) are known at each of the different stages, the revenues generated in the sector depend on the assumptions made regarding hectares and yields.

Peru did not really produce official data on illicit drugs. It is only recently with the INEI and the Ministry of Agriculture that data on illicit production are collected and published officially. This information on the coca industry until 1995 is consistent with the private consultant Macroconsult Ltd. and the U.S. Department of State's INCSR.

Their result for the year 1995 based on 115,300 hectares produced a coca sector value added of approximately US$ 1,400 million. The National Development Institute has estimated for 1995 an extension of 125,000 hectares. Similarly, the Ministry of Agriculture's data for the same year range between US$ 1,450 and US$ 1,600 million. Its estimates assume 120,000 hectares. Official sources announced the objective to reduce the cultivation area by 50% for the year 2000. They seek to reduce the area to approximately 60,000 ha. With respect to prices, the data were provided by U.S. resources, UNDCP in Peru and various Peruvian sources. Since Macroconsult Ltd. did not consider all other rural activities, such as cattle raising and the lack of recording by the Ministry of Agriculture's statistical office of some crops, the number of hectares calculated can be considered much higher.

Moreover, this section presented a historical evolution of the illicit drug sector and has also attempted to describe the structure of the illicit coca industry in Peru. Different stages of evolution as well as the agents who participate and the current marketing procedures of the industry were identified and described. Some of these issues are the type, or nature, of incorporation of the coca producer to the cocaine industry, the products that are marketed abroad and those sold domestically, the type of transportation utilized, the types of centers of production and international crime. The description of the structure of the coca economy shows the vertical integration which coca growers have gone through.

One fact that appears clearly in this section is the moving nature of the activity. Indeed. coca growing has spread widely and frequently in the Peruvian jungle. Another fact is the dynamic and quick responses given by the different agents as their economic environment changes.

Calculations made by several studies show that the value of the coca sector's purchases from other sectors ranged between 13 and 18 percent of the coca sector's intermediate demand. The major implication of this is. contrary to what was found in the early 1990s. that the coca sector has important backward linkages with the rest of the economy. especially with the chemicals. petroleum derivatives. as well as transportation and storage sectors.

An aspect that is also worth discussing here is the employment effects of the coca sector. The sector employed directly between 210.000 and 240.000 people in 1994. This is about seven percent of the economically active agricultural population of the economy. or two to three percent of the total economically active population of Peru. These shares of the active population would be higher if the indirect employment were considered.

In pre-empting the emergence of large-scale financial activities by organized international crime. control efforts must focus on both the supply and demand sides of the transactions in which criminal organizations have a role to play. International crime feeds on the revenues from the drug trade. And yet. despite encouraging progress. the perception lingers that drug control is exclusively a country-level concern. Drug-control efforts at the international level must become a more central means of tackling drug-trafficking organizations: until they do. the revenues accruing to crime will continue to grow. and with it. the threat of criminal finance will become an ever greater thorn in the side of economic reform.

Cost created by the illegal coca trade are multiple. complex. and extremely difficult to measure. These costs may offset the benefits derived from coca and create more poverty for the country in the long run. Principal among them are the ecological destruction of the Peruvian jungle and the alliance of convenience between the guerrilla and those in the illegal coca trade against the state.

Part of the problem can be solved. though. by giving narco-dependent economies. such as the Peruvian case. feasible. legal alternatives to alleviate a wide range of political. economical and social problems which cannot be done using only militaristic policies. It was therefore the purpose of Part II to discuss the solutions which address the immediate problem presented by cultivation while employing a longer term strategy to attack drug trafficking.

In the macroeconomic framework. the country needs to take steps to control money and credit growth and to stabilize domestic demand so as to limit or reduce the current account deficit by reducing import growth. It should also consolidate the exchange rate to be more flexible (to avoid further foreign-exchange reserve losses). reduce foreign debt and re-examine privatization. agricultural credits. price structures. tariffs. technical support. and investment programs.

While we cannot turn the clock back on financial liberalization. we can at least absorb the lessons of experience. However. this does not mean that the country should reverse the deregulation procedure. What is required is a liberalized. deregulated market framework so that competition is accompanied by risk-controlling. conservative practices on the part of the institutions themselves. such as adequate capital ratios. ample provisioning. transparent accounting and proper credit-risk analysis. A greater influx of foreign expertise. technology and capital to the economy would all help Peru to achieve these goals.

Economic liberalization -with a human face- must be the objective of the Fujimori's administration. Since taking office on July 28. 1995. he has renewed his electoral pledge to continue the market liberalization policies of his previous government. but also has served notice that his administration will take a more active role in solving longstanding social problems. If these efforts prove successful. the government will serve to reduce popular dissatisfaction and strengthen Peru's democratic institutions.

Financing these social expenditures will not be a problem. After recording an average real growth gain of 7% in the 1993-1996 period. the economy will probably expand at a 5.5-6% annual clip in 1997. buoyed by strong copper and fishmeal prices and ever larger export earnings from the country's vast new mining fields and agriculture development. In fact. in recent weeks the government has taken several precautionary monetary and credit measures to cool demand and price increases and to squeeze excess liquidity out of the economy.

The next phase of reforms will require profound institutional changes to maintain growth rates. and if possible increase them. The validity of this type of generalization will vary with the implicit assumptions regarding the distribution of the benefits of growth between income groups within the country. In the recent past. growth and investment have varied widely between regions and there has been a tendency toward more economic inequality and even. in some cases. for economic growth to be accompanied by increases in unemployment. So, in order to sustain high growth rates, Peru must appreciably increase its savings rates.

The sustainability of the reform process remains a key issue, in view of the enormous costs that have been imposed on people, and the inequity with which the benefits of reform have been shared. Governance is also developing into a crucial issue: institutional reforms targeted at increasing the efficiency, legitimacy and equity of state policies are vital to the country's stability and to the pursuit of democratic development. In addition, rampant corruption unrelated to drugs, in both the private and public sectors, remains a serious threat to socio-economic growth and good governance.

Thus, consolidating the political, economic and social reforms, making them a permanent feature of the Peruvian economic and social landscape, is an enormous challenge facing in the prompt future.

I think this is the moment to effectively implement a realistic program of integral development. Five years ago it was not, nor will it be five years from now, since during the next five years anything can happen. In the last two years, the price for Peruvian coca leaf and for coca paste for cocaine has plummeted, but not the price for refined cocaine. The street price for cocaine has risen in the U.S. Until December of last year, Peruvian coca growers, both in the areas where coca is grown for traditional consumption and even more in the areas growing coca for drug trafficking, were being paid US$ 40 per arroba, which is equivalent to 11.5 kg, about US$ 4 per kg. Right now, the price is US$ 0.40 per kg. This has caused a major economic crisis as well as a major social crisis in the countryside.

Another important element is the surplus of both coca leaf and cocaine in storage. While the overall consumption has remained about the same or has diminished somewhat, the amount of cocaine produced continues to increase. leaving a surplus each year. And this has been occurring for the past four or five years. creating a huge stockpile of cocaine. To sum up. I think this is a great opportunity for Peru because the price for coca leaf have fallen. and because the peasant who grow the coca leaf have been convinced for some time that it is necessary to combine their traditional crops with some cultivation of coca leaf for traditional use and for beneficial products. Therefore. it is extremely important that nationally and internationally there is support for projects for integral sustainable rural development that not only looks at the issue of crops. but also at marketing the products both domestically and internationally. and also deals with infrastructure such as roads and highways to facilitate access to new markets.

In addition. the strategy must also combine eradication/interdiction programs to lower farmgate returns on the one hand. and alternative development to raise the returns from alternative on the other. Moreover. efforts to bolster the capacity of the states in the region to penetrate remote. conflict-ridden rural areas beset by drug traffic. to rein in paramilitary and guerrilla violence. and to deliver essential government services must be strengthened along with drug law enforcement efforts. It has been seen that the U.S. government could and should provide support for comprehensive development programs as part of its overall antidrug strategy. The United States clearly will not be able to foot the entire bill for the Andean countries. much less for the entire hemisphere. but it could and should contribute significantly to such efforts and encourage other developed nations to do so as well.

By itself. drug law enforcement cannot be expected to solve the problem by itself. It must be complemented by strong diplomatic initiatives. viable economic alternatives for drug-growing peasants. effective criminal justice systems. and expanded use of relatively new approaches. such as removing the profit of drug trafficking and controlling precursor and essential chemicals.

The American administration must move beyond symbolism to serious and sustained cooperation with the Andean and other source and trafficking countries in Latin America. Excessive emphasis on military and police repression will not work and poses multiple risks to civilian leadership. human rights. and democracy in the Andes and elsewhere in the hemisphere. Institutional-building. multilateral coordination. and economic development must all be incorporated into a comprehensive response to the regional drug trade.

Hard and soft drugs pose serious challenges to societies. They should not be decriminalized or legalized. Both supply and demand approaches are required. ranging from crop eradication (on the supply side) to greater public awareness. What is required is a mass mobilization of consciousness about the effect of drug use and an involvement of every sector of the community. from family to school. from workplace to social clubs. in a sustained program to discourage experimentation with. tolerance. and consumption of narcotics. Moreover. there should be more frequent regional and interregional training seminars and workshops for drug law enforcement personnel: provision of rapid. secure and direct means of communication: and establishment of bilateral agreements between states with common problems arising from the illicit traffic.

Thoughtful Peruvians of varied political view. including members of the armed forces. argue that the spread of Sendero. the cultivation of coca. and the unhealthy expansion of military power within a democratic state are problems which cannot be resolved without a coherent strategy for development and national integration. Therefore. serious attention must be given to the medium and long term future of the drug phenomenon. U.S. and Latin

American leaders must anticipate and plan a viable strategy, and then implementing it consistently. This will necessitate significantly higher levels of U.S. funding both domestically and internationally and sustained efforts to cooperate with Latin Americans.

Policies must include policing to attack the industry in the short term. High costs and low results do not legitimize the existence of this strategy in the long term and, thus, development of Peru's economy and reduction of the world's cocaine demand must be initiated on a large scale immediately. The longer the wait for this change in policies, the more remote the possibility of reducing the coca industry.

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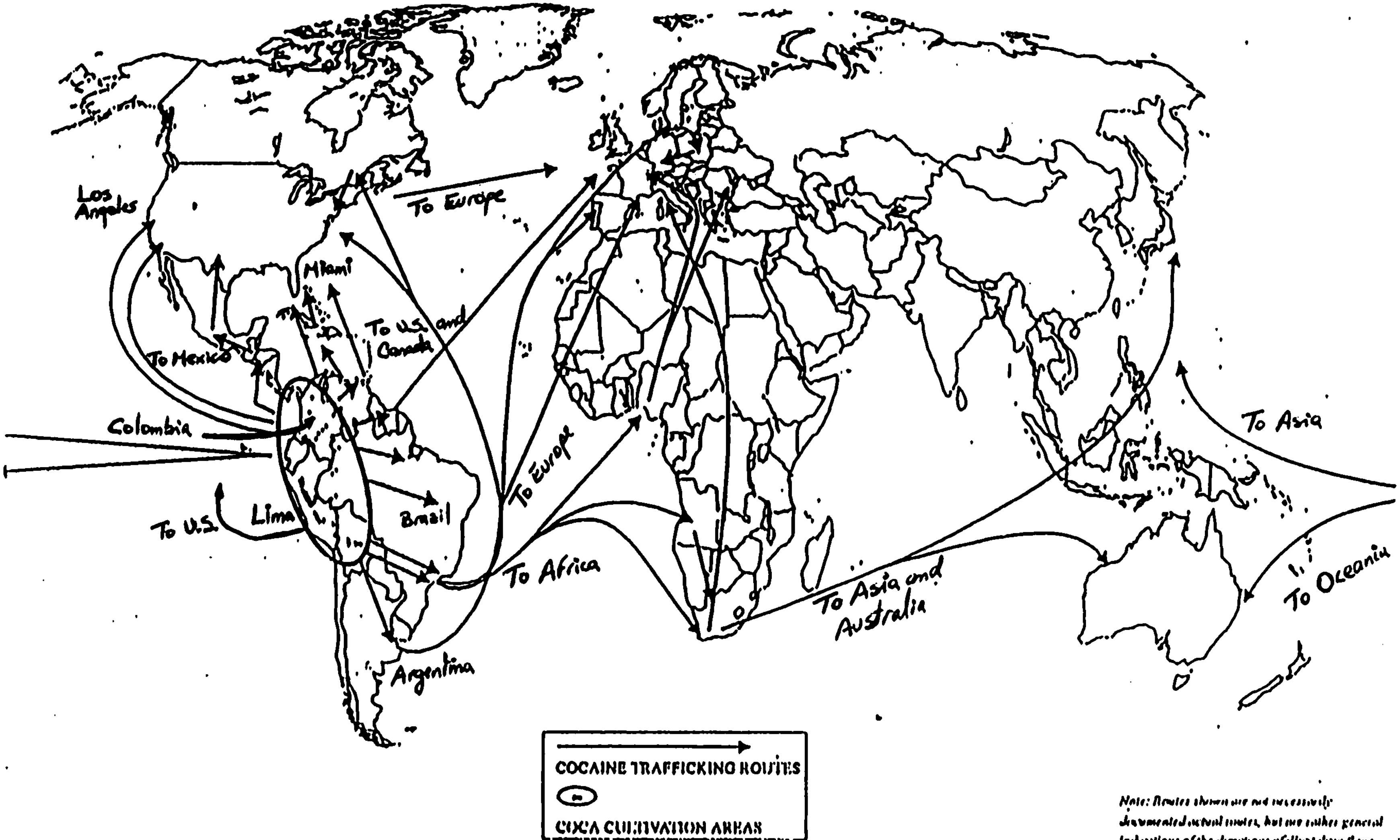
Annex-Maps

1. Coca and Cocaine: Major Cultivation and Trafficking Routes.
2. Principal Coca Growing Areas in Peru.
3. Valleys with Coca Cultivation.
4. INADE/USAID – Action Zone of the Alternative Development Program.
5. Alternative Development Project in the Valleys.
6. CONTRADROGAS – Target Zones of the Alternative Development National Program.

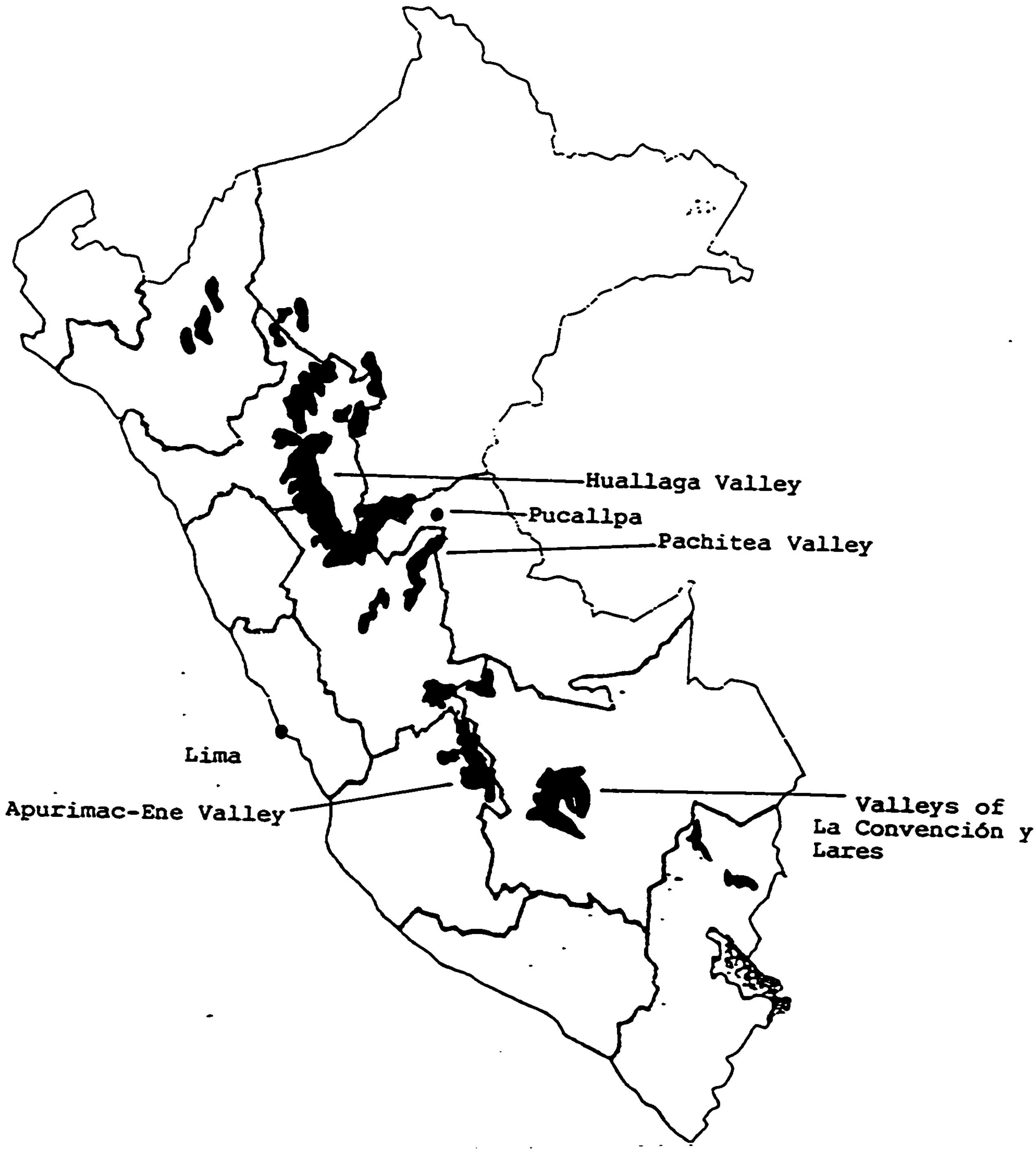
Coca and Cocaine: Major Cultivation and Trafficking Routes



Note: Routes shown are not necessarily documented actual routes, but are rather general indications of the directions of illicit drug flows.

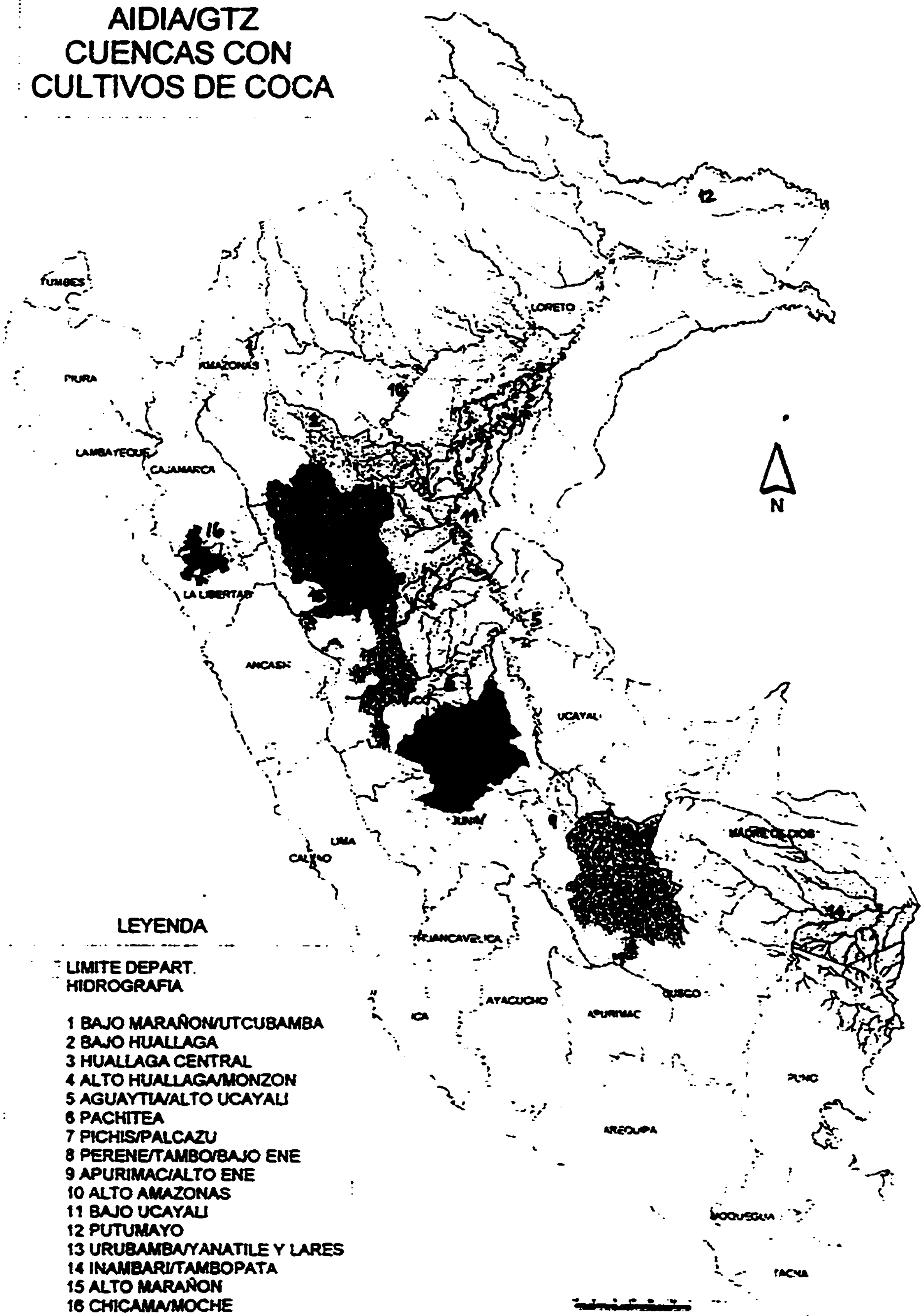
Source: United Nations International Drug Control Programme. World Drug Report. Oxford University Press Inc., New York, 1997.

PRINCIPAL COCA GROWING AREAS IN PERU



Source: Asesoria e Investigación para el Desarrollo
Integral Andino-Amazónico (AIDIA). GTZ, Oficina en Lima-Perú, 1997.

AIDIA/GTZ
CUENCAS CON CULTIVOS DE COCA



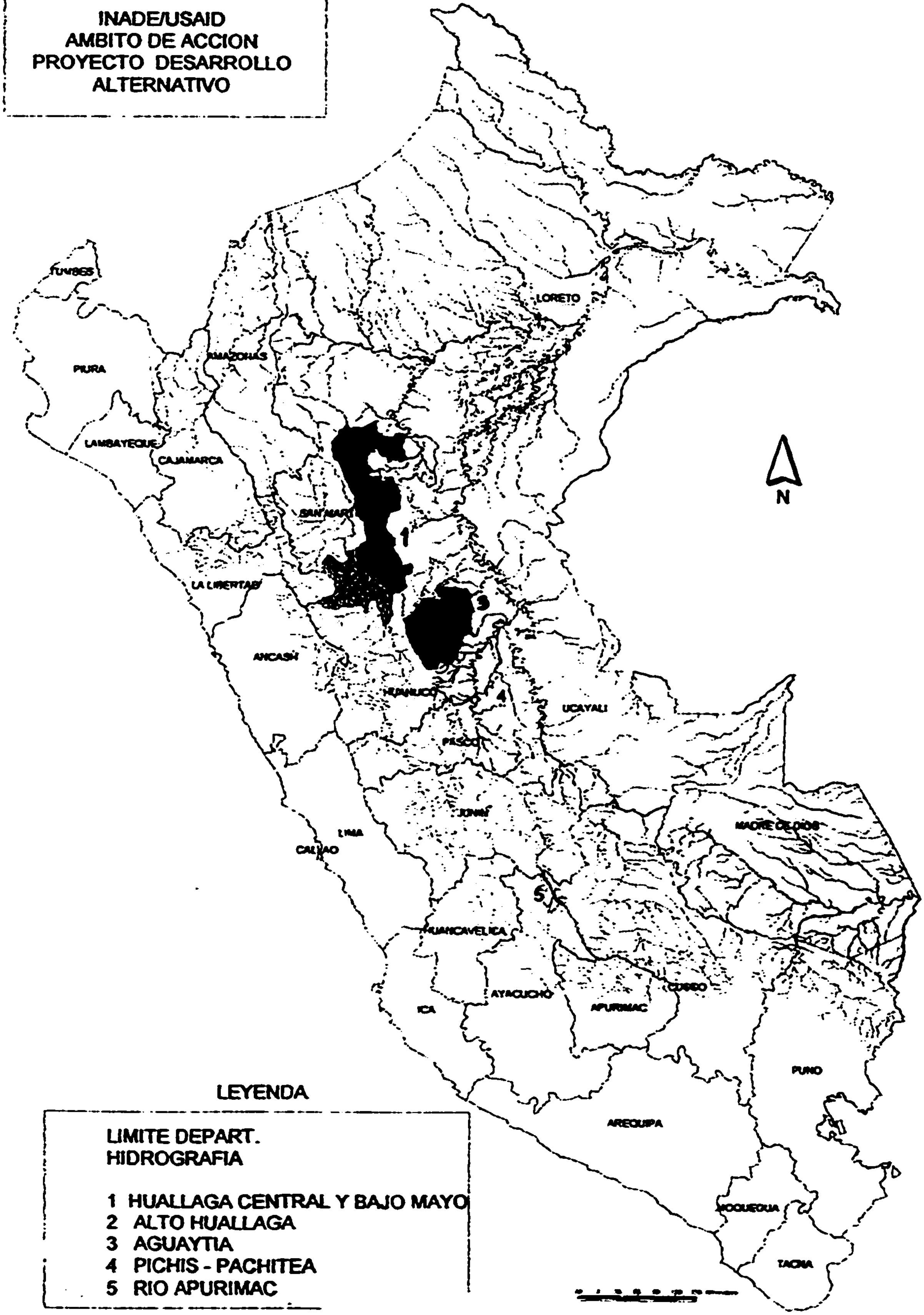
LEYENDA

LIMITE DEPART.
HIDROGRAFIA

1 BAJO MARAÑON/UTCUBAMBA
2 BAJO HUALLAGA
3 HUALLAGA CENTRAL
4 ALTO HUALLAGA/MONZON
5 AGUAYTIA/ALTO UCAYALI
6 PACHITEA
7 PICHIS/PALCAZU
8 PERENE/TAMBO/BAJO ENE
9 APURIMAC/ALTO ENE
10 ALTO AMAZONAS
11 BAJO UCAYALI
12 PUTUMAYO
13 URUBAMBA/YANATILE Y LARES
14 INAMBARI/TAMBOPATA
15 ALTO MARAÑON
16 CHICAMA/MOCHE

ELABORACION ______ en Lima-Perú, 1

INADE/USAID
AMBITO DE ACCION
PROYECTO DESARROLLO
ALTERNATIVO



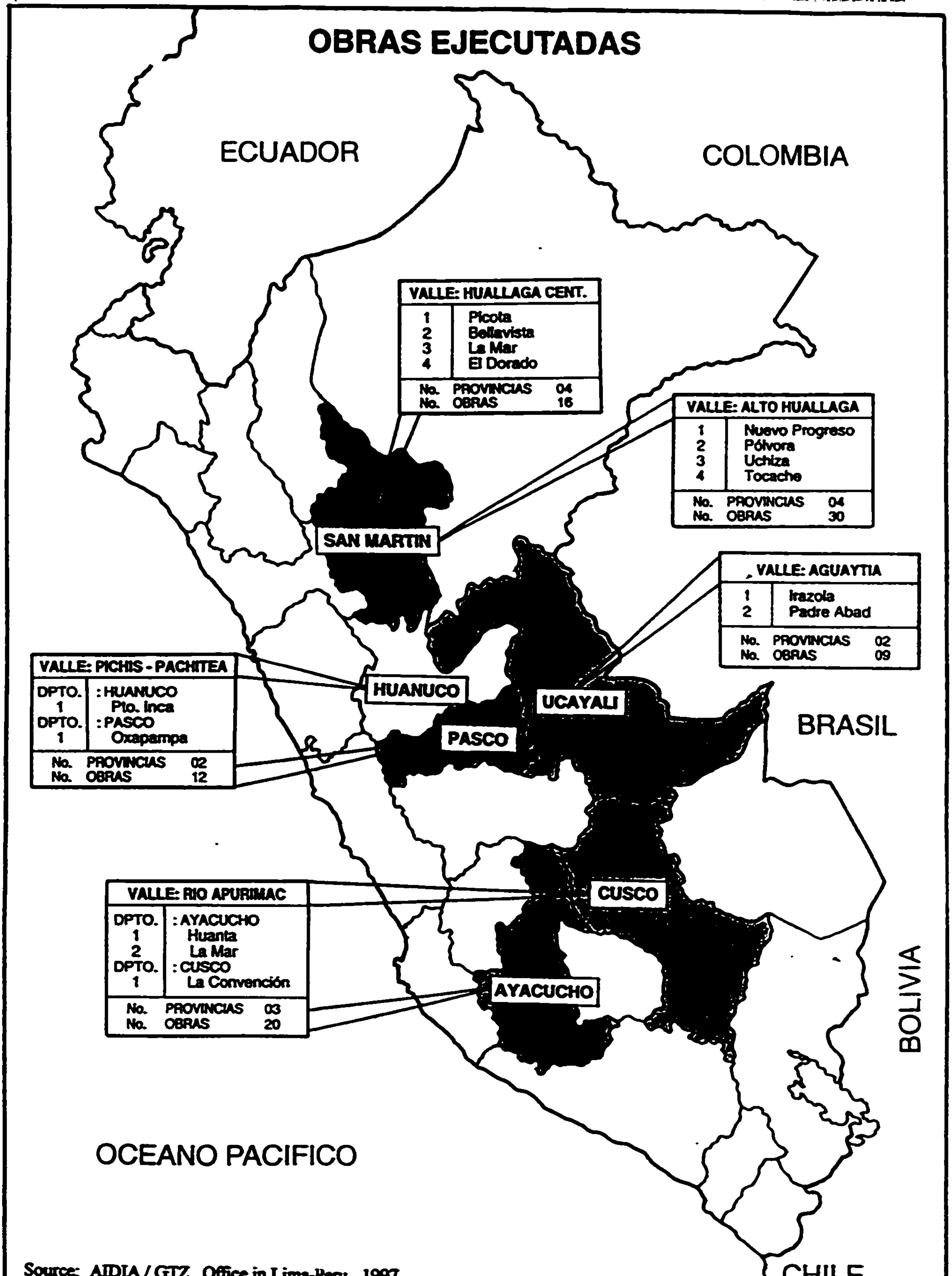
LEYENDA

LIMITE DEPART.
HIDROGRAFIA

1 HUALLAGA CENTRAL Y BAJO MAYO
2 ALTO HUALLAGA
3 AGUAYTIA
4 PICHIS - PACHITEA
5 RIO APURIMAC

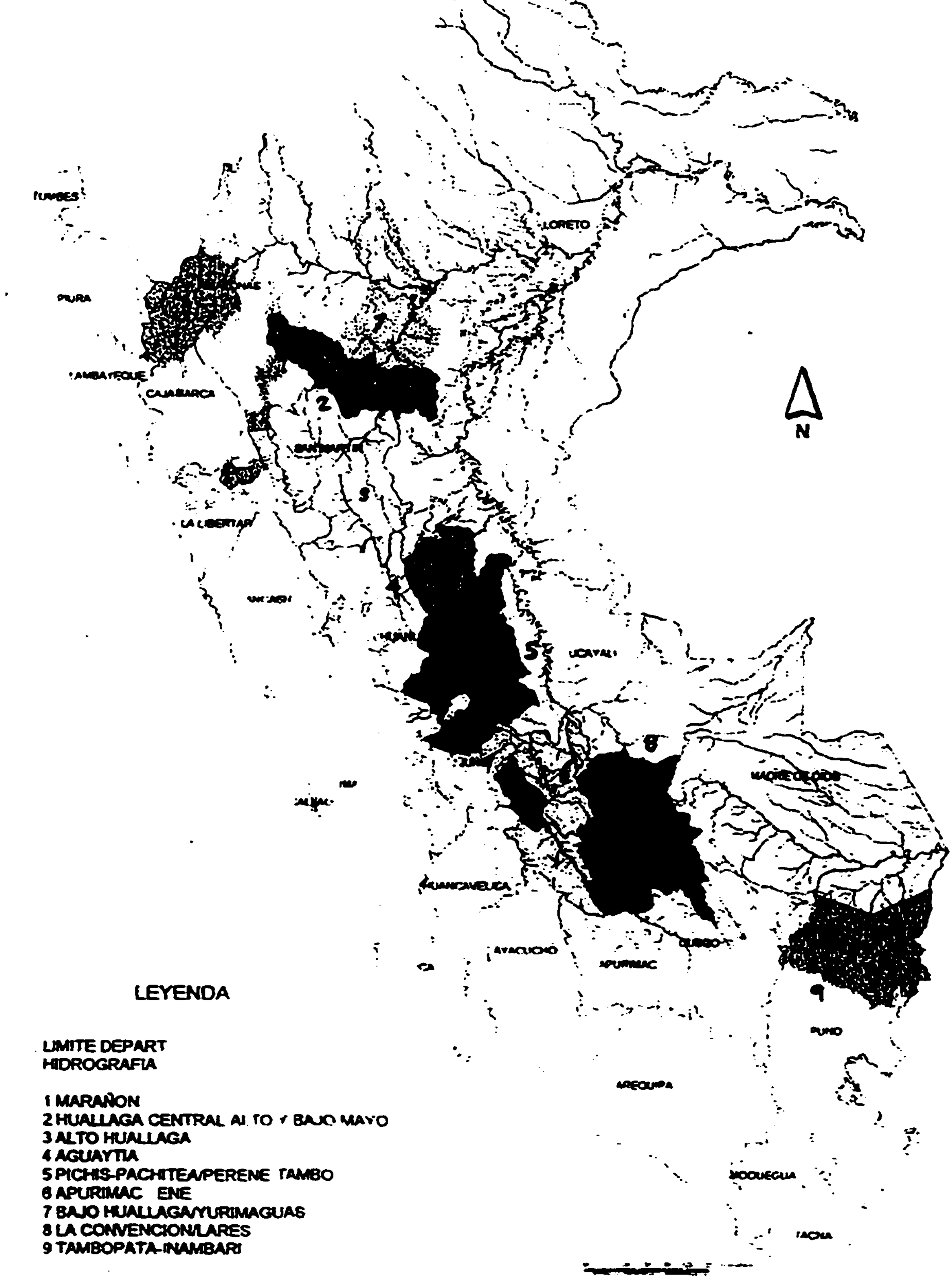
ELABORACION: AIDIA/GTZ. Office in Lima-Peru, 1997.

PROYECTO DESARROLLO ALTERNATIVO



Source: AIDIA / GTZ. Office in Lima-Peru, 1997.

CONTRADROGAS
ZONAS OBJETIVO
DEL PROGRAMA NACIONAL
DE DESARROLLO ALTERNATIVO



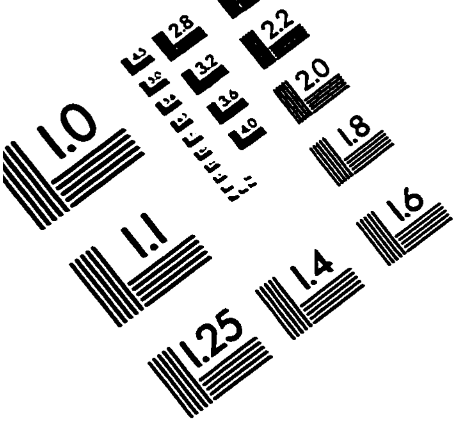
LEYENDA

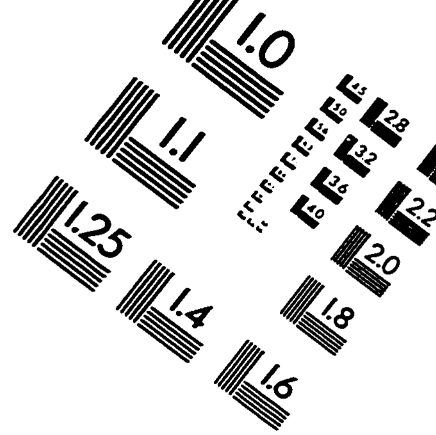
LIMITE DEPART
HIDROGRAFIA

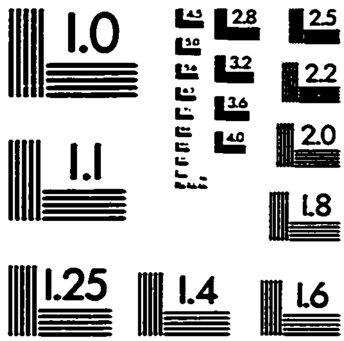
1 MARAÑON
2 HUALLAGA CENTRAL ALTO Y BAJO MAYO
3 ALTO HUALLAGA
4 AGUAYTIA
5 PICHIS-PACHITEA/PERENE TAMBO
6 APURIMAC ENE
7 BAJO HUALLAGA/YURIMAGUAS
8 LA CONVENCION/LARES
9 TAMBOPATA-INAMBARI

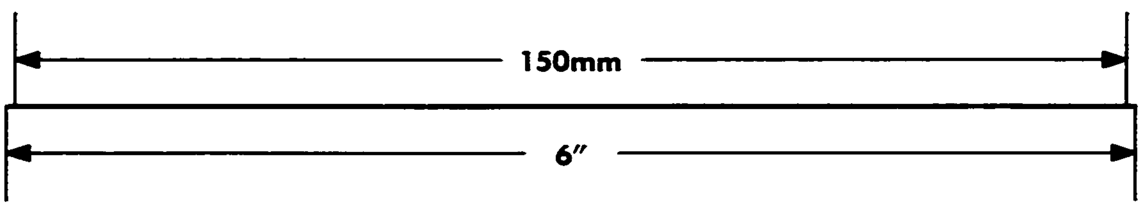
ELABORACION AIDIA/GTZ . Office in Lima-Peru, 1997.

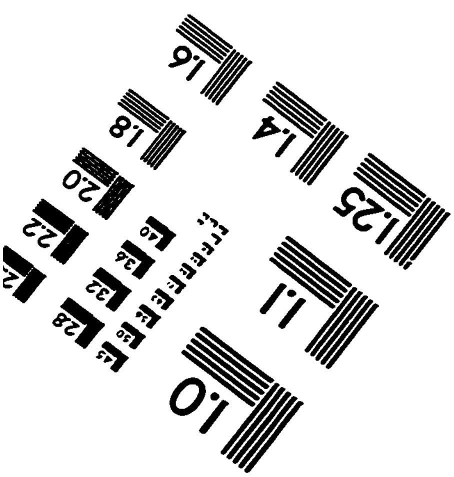
TEST TARGET (QA-3)

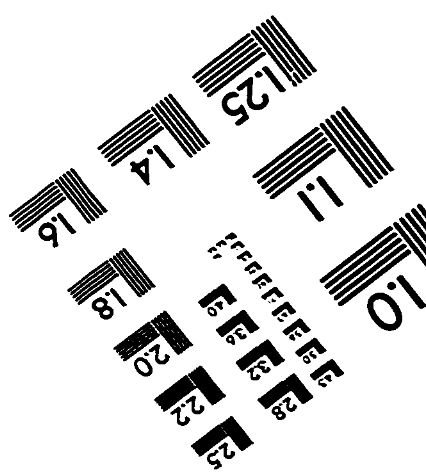












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