

***Filling Institutional Voids: Market Self Organisation,  
Informal Sector or Organised Crime***

A CRCE Colloquium

Wednesday 25 September – Saturday 28 September 2013

***Informal and Shadow Economy***

Chairman: Bernard Brscic

Discussion leaders:

Norma Rossi – *Conceptualizing Illicit Sovereigns*.

Rok Spruk – *Macroeconomic Effects of Mexico's Drug War*

**Bernard Brscic:** On my right-hand side is Norma Rossi, to start us off with her presentation conceptualizing illicit sovereigns. Norma is a PhD student at the University of Reading, and is conducting her research on the mafia. On my left hand-side is Rok Spruk, who is a graduate student at the University of Utrecht, and he will be talking about the macroeconomic effects of Mexico's drug war, exploring a new data set.

**Norma Rossi:** Thank you very much, and thank you again for this invitation and I am really glad to be here.

I would like to introduce our discussion by looking at how organised crime infiltrates and influences the process of state building. The topic of discussion builds upon my PhD research on violent non-state actors and it is part of a wider post-doctoral research agenda, which I am developing at the moment. In order to illustrate my preliminary findings, I will draw upon two exploratory case studies, Iraq and Afghanistan.

In the context of fragile statehood – particularly in contexts where there are insurgent movements, the literature focuses on the link between insurgent/terrorist activities and organised crime. Organised crime and insurgent/terrorist activities are understood to be often mutually enabling and this is studied very widely nowadays under the concept of “terror-crime nexus”. The concept of the “nexus” is used to indicate the increasing overlap between terrorist/insurgent activities with organized crime, both locally and globally.

At the same time, when we reason in terms of external state-building forces intervening in such situations – by external state-building forces I mean UN forces and NATO missions – these are implicitly conceptualised as being in opposition to organised crime. So indeed organised crime is understood as filling the voids left empty by a fragile state or a failed state, and the state-building forces are understood as fighting back against organized crime and preventing it from filling these voids. The argument that I want to put forward today is that contrary to what I have just said on the basis of my preliminary observations, external state-building forces also contribute to fuelling organized crime instead of fighting it. Examining the role of external forces intervening in this area is extremely relevant nowadays, because since the 1990s there have been increasing efforts by the international community to conduct

state-building and governance building. Specifically, I will focus on the counter-insurgency forces in Afghanistan and in Iraq. Nowadays the role of external armies is increasingly important, because they have a central function in initiating the processes of state-building for the simple reason that as, David Kilcullen has written, in several modern campaigns – Iraq, Afghanistan, Pakistan –, “the government, or indeed the coalition forces, started the campaign.” So often the armed forces hold the first step in the state-building process. I will argue that there are three issues which make counter-insurgency activities potentially beneficial to rather than fighting organized crime. First is the use of capital as a strategy of legitimisation for acquiring authority and legitimacy in the eyes of the local population. The second element is that the short-term perspective of counter-insurgency forces, which are under pressure for ending their mission, clashes with the long-term processes that state-building and governance building require. The third point is that in spite of the fact that the new counter-insurgency strategy supposedly puts the protection of the local population first, in practice the security of the counter-insurgency forces is prioritised.

In the following part of this presentation I will show how these three elements that I have raised are fuelling, rather than fighting, organized crime. The analysis that I have conducted so far is based upon the analysis of counter-insurgency documents, international crisis groups’ reports and elite interviews, which I conducted with members of the Italian and the British armed forces.

With regard to the first point regarding monetary means as a strategy of legitimisation, the problem of acquiring authority and legitimacy is very central for counter-insurgency forces, which come from outside the country. This is a very pressing issue, as General Petraeus has argued: “Act quickly, because every army of liberation has a half-life.” Indeed, the lack of legitimacy is experienced by external military forces’ officers on a daily basis. For example a military officer in the Italian army serving in Afghanistan has told me that, “the local police officers, with whom we work usually, call us ‘bastard infidels’.” The strategy then to solve this problem – of lack of legitimacy – follows a rationalist and individualist approach. It is based on a strategy of legitimisation through money. Indeed, again following the words of the two central figures in shaping the COIN strategy in Afghanistan and Iraq, General Petraeus and General McChrystal, the latter argued that “this is not a philosophical issue but a practical one. People decide according to whatever they get.” Therefore money becomes ammunition. Yet money as a strategy of legitimisation contributes to introducing a strictly market logic in the political dispute and to favour the emergence of certain types of actors rather than others. So the ICG report on Afghanistan has said, and I quote:

“The inflow of billions of dollars in international assistance has failed to significantly strengthen the state’s capacity to provide security or basic services, and has instead, by progressively choosing the interests of political gatekeepers and insurgency commanders, provided new opportunities for criminals and insurgents to expand their influence inside the government. The economy as a result is increasingly dominated by a criminal oligarchy of politically-connected businessmen.”

Obviously, using money as “ammunition” is not only an approach adopted by external armed forces, but reflects a much more holistic strategy, however, it could be argued that the way in which this issue is handled right from the beginning of the mission becomes of crucial importance in shaping the future possibilities. Indeed, the result of this strategy of legitimisation has an ambiguous nature. A British army officer who served in Iraq told me in our interview that the relationship between counter-insurgency forces and the Iraqi people is characterised by the fact that: “It is more about Americans buying people to support them,

than actually rejecting the insurgency.” Therefore, by favouring certain actors rather than others, and by fuelling a logic which is based on an economic negotiation on the reconstitution of state institutions and structure of governance, this strategy of legitimisation shapes the state and the governance-building process in a specific way. Arguably, this logic of legitimisation through a big inflow of money contributes to the affirmation of profit driven actors- i.e. organised crime.

The second element is that, as I mentioned before, there is potentially a very strong contradiction between the need for short-term stabilisation that external armed coalitions have, because the pressure to end the mission is always very strong, and the long-term solution that state-building processes instead requires. So the short-term need can lead to a strategy of legitimisation which neglects to accept and prepare for the risks that come from targeting powerful political and business elites with legal prosecution and sanctions. This risks leaving the power in the hands of the already-formed local elites, then sacrifices the goal to enforce a democratic system of governance. In this sense, it constitutes a system of governance that does not challenge powerful local groups, which have seem to be both local forms of power but also involved in more or less legal transnational trafficking (the example of the KLA in Kosovo is exemplary in this matter). In other words, the exigency of a short term stabilisation might lead external forces to turn a “blind eye” to the illegal activities as a price to achieve stability.

The third point is that there can be a contrast between the protection of the counter-insurgency army and the security personnel which have been sent there, and the population of the country where the counter-insurgency operation is taking place. So in spite of the fact that the so-called doctrine of ‘hearts and minds’ claims to focus on the security of the local population, this understanding does not seem to be the prevailing one according to one of my interviewees:

“So, the priority is always on protecting the force that is in the country, and the security of the population is very much behind that as a priority. So the protection will always be of the armed force, the occupying force, and the security forces. So it is very much about making sure for example, in the case of Iraq for example, that the British forces would be secured first, and the local population was very much a secondary priority.”

In this sense the security of the local population is more a means than an end in itself, and the safety of the counter-insurgency forces might take priority to protecting the population. Again this highlights the relevance of local power groups, which can help fuel forms of “protection rackets” other than the State, to use Charles Tilly’s expression. The extreme case has been the Italian forces in Afghanistan, which as certain classified documents made public have revealed, have paid protection money to local non-state forces in order not to be attacked. As the documents show, the American Ambassador Ronald Spogli pressured the Italian government on this topic on two occasions in 2008. The first time in April 2008 the Ambassador said “We lay down a strong marker objecting to past practices of paying protection money and negotiating deals for the release of hostages.” Again a few months later the Ambassador also told Berlusconi, the then-Prime Minister that “we continue to receive disturbing reports of Italians paying off local warlords and other combatants.”

To provide a short conclusion, the use of “private racketeers”, can actually be understood as an unwritten strategic choice which is often implied in counter-insurgency. This emerges from its contradictory ways of constituting both legitimacy and good governance, which

instead are fundamental for conducting efficient state-building processes. This can lead to a paradoxical situation in which state governance is strengthened and functions because of organised crime, but at the same time works as an empty shell. For all these reasons I want to stress the importance of focusing great attention on transnational organised crime not only in terms of law enforcement, but also in terms of the wider political issue of state building and governance building. These issues are particularly relevant nowadays since the transnational and local dimensions are particularly interlinked, and the lack of security governance in many parts of the world makes it difficult to contain and prevent the spread of transnational security problems.

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**Bernard Brscic:** Now I will ask Rok to speak.

**Rok Spruk:** Despite the on-going effort of Mexico's federal government to combat drug-related violence, Mexico's most powerful drug cartels have become the major wholesale illicit drug producer and account for 90% of the cocaine entering the U.S. market. In a detailed report to the U.S Congress, Coleen Cook estimated the wholesale earnings from the illicit drug trade to be in the range from \$13.6 billion to 49.6 billion annually.<sup>1</sup> The response of Mexican authorities to the growing influence and market power of major drug cartels has spurred waves of violence across the country. Drug-war related murders increased by six-fold between 2001 and 2011. By the end of Felipe Calderon's six-year presidency, the official death toll was at least 60,000 although unofficial accounts estimate the homicide rate well above 100,000 given the large number of people who have disappeared.

The literature on the origins and causes of the Mexican drug war typically suggest the failure of an inefficient education system unable to provide a good education to the large population which has resulted in a massive pool of unskilled labour and encouraged school drop-outs to pursue lucrative careers making easy-money in drug cartels. Major sources suggest that Sinaloa Cartel, the country's most powerful drug cartel, repeatedly provided funds to schools, hospitals and the senate, fuelling rampant corruption among the Mexican political elite which significantly increased the cartels' market power and influence.

Few accounts of the cost of Mexico's drug war have taken into account the macroeconomic effects of Mexico's drug war and related violence. Recent estimates by the OECD suggest that PPP-adjusted per capita income in Tijuana and Juarez, most heavily affected by drug-related violence and cross-border smuggling, either declined or remained stagnant in recent years whereas per capita income rose in other metropolitan areas.<sup>2</sup> The attempts to gauge the effects of drug trade and related violence, cross-border smuggling and trafficking clearly precipitate a theoretical framework based on microeconomic foundations as a starting point to estimate large-scale macroeconomic effects of drug trade and its externalities. Furthermore, the attempts to assess the effects of the Mexican drug war have been constrained by the absence of official macroeconomic accounts which disallowed the assessment of key effects resulting from drug trafficking and related activities.

To this end, in a new dataset, regional per capita GDP is reconstructed for 32 Mexican states for the period 1940-2011. Recent estimates of regional GDP per capita from the *OECD Regional Database* for the period 1992-2009 are adjusted for PPP and linked to the historically reconstructed real per capita GDP series for the period 1940-1992 by Germán-Soto (2005). The reconstructed long-term regional per capita GDP series is adjusted for inflation at 2005 constant prices. The new dataset covers the entire Mexican territory. Its major contribution to the literature is multifold. First, the dataset presents an attempt to provide empirical foundations to study the aggregate and disaggregate effects of illicit drug trade, trafficking and smuggling. Second, the dataset allows exploiting the policy changes using difference-in-difference approach to investigate the policy effectiveness in combating drug cartels. Third, the dataset also presents an attempt to estimate both direct and indirect contribution of illicit drug trade and production to the GDP from a regional perspective.

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<sup>1</sup> Cf. Colleen Cook, *Mexico's Drug Cartels*. CRS Report to the Congress, Congressional Research Center, 2007.

<sup>2</sup> Cf. OECD Statistics, *Metropolitan Areas, Cities: Population and Economic Data*, 2013. The Metropolitan database contains data for 268 metro areas with a population of 500,000 or more over 29 OECD countries. These metro areas follow a harmonized functional definition developed by the OECD

Fourth, the dataset is framed into a broader field of growth and development economics since it nonetheless provides an empirical support to study the patterns of convergence and divergence across Mexican states in the long-run. This is nevertheless essential in identifying true binding constraints on long-term growth performance. Moreover, the dataset can contribute towards a better understanding and assessment of the effectiveness of combating drug-related crime and violence with respect to the disruption of economic activity and regional economic performance of Mexican states.<sup>3</sup>

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**Bernard Brscic:** Does anyone have any questions? Yes Richard, please.

**Richard Connolly:** Thank you, that was very interesting, and certainly looking at some very interesting cases there. I had one query from the beginning of your presentation. I gather, as I understood it and perhaps I missed it for some reason, that insurgency drives organised crime. Are they not, in these two countries at least, often the same thing? What I mean by that is that Afghanistan has been in the state of civic disturbance for quite a few years; Iraq similarly. And I always got the impression, and I do not have any real idea of what is going on out there; I always got the impression that organised crime was carried out by insurgents to pay for weapons, to pay for looking after the population, to do whatever insurgents need to do to guard their legitimacy and so on. And whether or not that also leads to the fact that there are two highly securitized countries; Iraq in particular had a large security force, many of whom stood down with the American declassification. This left a lot of people with a specialism in violence who then went on to become insurgents. Are these the same people or are there different criminals? I did not catch the answer to this.

**Norma Rossi:** Thank you; no I did not specify at all on this point so thank you for asking. I think there is a very messy situation there and I do not claim to have a particular knowledge. But from what is my understanding, it is definitely the case that insurgents inevitably carry out criminal activities in order to fuel their everyday activities, because obviously they are denied legitimacy, so they have to get arms and food and everything they require from somewhere else. So their activities are intrinsically criminal. But, some literature makes the distinction between some groups that have a political aim and those that are just focused on making money and they are not really interested in who wins the political fight. And there are groups which have contrasting factions; so this distinction has a lot of overlap and a lot of mess. Then on top of this you have the transnational dimension, so how groups from other regions interact with the local situation and procure arms and so on.

**Bernard Brscic:** Let me ask you a question regarding the whole idea of state building. Somehow you assume the state-building process is good. But would you not say that given the historical experience from Iraq and Afghanistan, possibly from Syria, that actually it is a

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<sup>3</sup> The dataset is available from the author on request

bad thing that actually the West interferes in endogenous processes; that actually the arguments put forward for the intrusions into the domestic mess is possible spillover effect.

**Tomasz Mickiewicz:** So Rok, would you say that basically the mafia redistribute income, and they redistribute income so the poor people get more income, is that the case, or is it the other way round?

**Silvana Malle:** Just a question for clarification, maybe I missed something because I could not read very well – did you show the figures on how much this drug trade represents as a percentage of GDP? The second thing is that these lines showing that the states bordering the United States are doing better; of course but this could also be because of the prisons. Drugs... You do not necessarily need to send drugs to borders; there are people travelling by plane but also other means and transporting drugs, so I do not really see the connection between bordering states they are with and the drug. So if you could explain that better. There is of course a policy issue in that but that is not the point of your paper. As we know, if drugs were made legitimate, not illicit, then the whole thing would collapse. So is there any movement that you know of in Mexico for legalizing drugs? I would vote for that immediately. And there are very few people actually now in the world, who are addressing this from an economic point of view. In the 1930s it was whisky and so on, and I really do not see from an economic point of view but even from a health point of view why they should not be made legal.

On Norma's paper, that is really interesting, I did not think of this issue in terms of the wars you analyse. But yes, it reminded me of the stories that during the Second World War the United States is said to have courted a number of 'cosa nostra' people in Sicily in order to get them to fight the local war. I do not know whether this is true or not, but it is more or less in line with what you say.