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# **THE ECONOMICS OF DRUG SELLING: A REVIEW OF THE RESEARCH**

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# The Economics of Drug Selling: A Review of the Research

## Overview

The economics of the illicit drug market in the United States have been a source of much speculation and misinformation. A key reason for this lack of knowledge relates to the inherent nature of drug selling. Drug distribution is an illegal business venture, and is therefore cloaked in secrecy in order to protect the participants who are engaged in what is often a dangerous enterprise. Because of the concealed nature of drug markets, few researchers have been able to penetrate their boundaries and gain the trust of participants in order to observe and describe these networks.

This briefing paper surveys the relative handful of studies that have been able to evaluate the workings of drug markets. These include data analyses of drug gang finances, surveys of convicted drug offenders, and ethnographic studies involving interviews with drug sellers. The findings of these various studies generally indicate that drug selling, while clearly illegal, shares many characteristics of other business enterprises. Further, many of the commonly held perceptions regarding the lucrative nature of the drug trade turn out to be significantly exaggerated.

Overall, three sophisticated studies have addressed the economics of the drug trade. Levitt and Venkatesh (2000) used a unique set of data to provide significant insight into the drug selling economy.<sup>1</sup> They combined interview responses with financial data (costs, revenue, price, quantity) that were kept by a gang leader in order to manage a distribution network. This offered the researchers the opportunity to track, over time, how money flowed, and to whom, within a drug market.

A second study, sponsored by RAND, looked at persons engaged in the sale of drugs in Washington, DC.<sup>2</sup> The authors combined interviews of drug sellers with arrest data, offense history, personal demographics, education, and employment.

A third study, in Wisconsin, examined drug markets by placing them in the larger context of the conventional labor market, paying particular attention to the fluid movement between illicit and legal forms of employment.<sup>3</sup>

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<sup>1</sup> Levitt, S.D. & Venkatesh, S.A. (2000). "An Economic Analysis of a Drug-Selling Gang's Finances." *The Quarterly Journal of Economics*, Vol. XX, 755-789. Due to the sensitive nature of the data, there was no location given for the city in which this drug gang operated.

<sup>2</sup> Reuter, P., MacCoun, R., & Murphy, P. (1990). *Money from Crime: A Study of the Economics of Drug Dealing in Washington, D.C.* Santa Monica, CA: RAND-Drug Policy Research Center.

<sup>3</sup> Hagedorn, J.M. (1994). "Homeboys, Dope Fiends, Legits and New Jacks." *Criminology*, 32, (2), 197-219. & Hagedorn, J.M. (1998). "The Business of Drug Dealing in Milwaukee." *Wisconsin Policy Research Institute Report*, Vol. 11, (5).

## Earnings

Overall, all three studies conclude that the average earnings of a person working in the drug trade are far less than have been traditionally perceived. At the top of the drug hierarchy, earnings can be very substantial. The Levitt and Venkatesh study estimates that annual earnings for drug gang leaders are between \$50,000 and \$130,000.<sup>4</sup> This is clearly significantly higher than these individuals could earn locally in the legitimate labor market. However, very few persons in any given drug market make these wages. The Officers, the second level of the hierarchy, are estimated to earn \$12,000 per year, or slightly higher than minimum wage for a full-time job. The lowest level of the hierarchy, and the most prevalent, are the street level sellers. These are the individuals who are actively engaged in the daily sale of drugs, and who are generally paid based upon the amount of product they dispense. On average, street dealers make less than \$2500 per year. Even though they only work approximately 20 hours per week, their pay level is still far below the minimum wage. The fact that the job requires minimal skills, with a veritable army of reserves waiting to fill in any job opening, puts consistent downward pressure on wages for street level dealers.

The authors of this study conclude, despite the radical skewing of the wage distribution, that on average, the earnings of individuals involved in drug dealing are not appreciably higher than available market alternatives. But this average figure is raised significantly by the relative handful of high level dealers who are making substantial wages. Therefore, a question that arises is: if wages are so low for low-level drug dealers, why would they be willing to engage in such high-risk labor rather than working in the safer and higher paying legitimate economy? Researchers Levitt and Venkatesh conclude that the desire to move up through the hierarchy and make the earnings of gang leaders is sufficient motivation for sellers to “pay their dues” by laboring in the low end of the wage spectrum.

The two other studies under review have come to similar conclusions. In the analysis of Washington, DC markets, RAND researchers concluded that the median earnings for those engaged in drug selling were \$721 per month.<sup>5</sup> These figures varied significantly based on how much time the individual spent in this pursuit. The average respondent reported a net income of \$700 per month from drug sales, with a range from \$25 for the small earner to \$2500 for the typical large earner.<sup>6</sup> For the people who sold daily, a fraction of the sample, the median net earnings were \$2000 per month. Based upon their limited working hours, this translates into an hourly wage of \$30.

Research in Wisconsin by John Hagedorn also reported earnings that varied based upon the amount of time spent on drug dealing. Of the sample interviewed, a third made less than or equal to minimum wage, one-third made in the range of \$13 to \$25 per hour and a handful reported making in excess of \$10,000 per month.<sup>7</sup> Hagedorn concludes that the majority of drug

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<sup>4</sup> Levitt & Venkatesh.

<sup>5</sup> Reuter, MacCoun, & Murphy

<sup>6</sup> There are significant differences between the net and gross income. The gross income is a tally of all revenue from drug sales, while the net income deducts the cost of any materials necessary as well as any stock taken by the seller for personal use.

<sup>7</sup> Hagedorn, (1994).

dealers in his case study in Milwaukee earned (gross) between \$1000 and \$5000 per month, and worked long hours in order to achieve this wage. Oftentimes, this income was supplemented by wages from the legitimate sector.<sup>8</sup>

### **Time Spent on Drug Dealing**

Two of the three studies examined conclude that drug dealing is far less of an all encompassing economic pursuit than many have speculated. Very few dealers spend all of their working time selling drugs and most have some form of legitimate employment for which they use drug dealing as a means of supplementing income.

In the Washington, DC study group, most individuals were selling drugs on a part-time basis. Close to 25% of the sample sold drugs no more than once a week, and these people reported monthly net earnings from the drug trade of just \$50 a month. About three-eighths sold daily, with a median gross income of \$3600 per month, and a median net income of about \$2000. Typically, people in this sample spent about three hours a day selling drugs, averaging about 13 sales per day.

In Wisconsin, about 50% of those who had reported to have sold cocaine sold in no more than 12 months out of the previous 36 months. Only slightly over 1 in 10 sold more than 24 out of the past 36 months.

### **Other Employment**

All three studies conclude that the persons involved in drug sales were sporadically moving in and out of legal and illegal employment markets. In Milwaukee, Hagedorn observed that few individuals earned their income solely from sales of illegal drugs; rather, they used the income to supplement legal employment, which often paid a wage that was unable to meet their needs. In Washington, DC, three-quarters of the sample had some form of legitimate work during the period studied. The median monthly income from that job was approximately \$800. In analyzing arrest data in Washington DC, the authors found that of those charged with possession, 74% were employed and of those charged with a drug sale, 67% were otherwise employed. They concluded that drug selling was not a specialized industry, and was a complement to, rather than a substitute for, legitimate employment.

Levitt and Venkatesh report similar figures, estimating that 75-80% held low-paying jobs in the legitimate sector at some point throughout the year.

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<sup>8</sup> Hagedorn, (1998).

## **Characteristics of Drug Markets**

The handful of studies on the economics of illicit narcotics markets indicate several common characteristics:

**1-**Few drug sellers are making substantial earnings. Most use drug dealing as a supplement to wages made in the legitimate sector, raising questions about the availability of economic opportunity in low-income urban communities.

**2-**Most drug dealers spend a fraction of their time selling drugs, but are forced to work significant hours in order to attain these earnings.

**3-**The drug market is a perpetually fluid situation, and most individuals' careers are very short, with earnings often fleeting. Hagedorn reported that most drug dealers were on what he characterized as an economic merry-go-round in which they rotated in and out of the legitimate and illegitimate earnings sector. Levitt and Venkatesh also noted that most of the drug dealers they had interviewed for their study had since abandoned the trade.

**4-**Most of those in the drug trade are not generally engaged in violence. Authors of the Washington, DC study concluded that only about one-quarter of their sample had ever been arrested for a violent crime, and about one-sixth had been convicted of a violent crime. Hagedorn posits that violent activity is most likely to occur as new markets emerge, but as they reach a point of stasis, violence decreases. The longer markets remain in operation, the less likelihood that violence will occur. Those surveyed in Milwaukee reported no daily occurrences of violence, and most reported only occasional incidence of violence. This should come as little surprise, as violence and disruption are intimately linked, and business (licit or illicit) does not like disruption.

**5-** The profile of drug offenders in prison confirms that, to a large extent, lower-level drug users and sellers represent a substantial portion of persons convicted and sentenced to prison. Analysis of the most recent data available (1997) indicates that of those currently incarcerated on a drug charge, 58% have no history of violence or high-level drug activity and three-quarters have a criminal record of only drug charges or other non-violent offenses.<sup>9</sup>

**6-**Those who patronize drug markets, according to evidence from Milwaukee, are primarily from outside the neighborhood where drugs are being sold. Only a small minority of persons buying drugs resided in the proximate neighborhood, and a significant percentage of consumers in this urban market were white. Hagedorn also concludes, in his comparison of urban (minority) and suburban drug markets (white), that the suburban drug market is far larger, despite the fact that this is not represented in arrest data.

**7-**The values and ideals espoused by the respondents in these studies closely mirror those that are reported to be held by most Americans. Hagedorn concludes that conventional values can co-exist within the drug market, as selling is simply seen as work, and not crime. He contends that

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<sup>9</sup> King, R.S. & Mauer, M. (2002). "Distorted Priorities: Drug Offenders in State Prisons." Washington, DC: The Sentencing Project.

persons working in the drug market are seeking to attain the core values of “the American way of life.” Levitt and Venkatesh agree, concluding that the reason that many are willing to work in such a dangerous enterprise for such low pay is the belief that they are “paying their dues” and they will “move up the ladder” and fulfill “the American dream.”

The common thread that runs through these reports is that drug dealing is a transitory enterprise, undertaken periodically by individuals struggling to survive and viewing it as a means of supplementing income in order to help propel them towards attaining their personal goals. This raises the question of the role of incarceration in dealing with drug markets. An alternative approach would be to address the issue of economic development in urban neighborhoods. In this regard, drug dealing can be seen not as a cause of urban decline, but rather as a response to the evaporation of a sustainable employment market with the exodus of manufacturing and commerce from urban areas beginning in the 1960s.