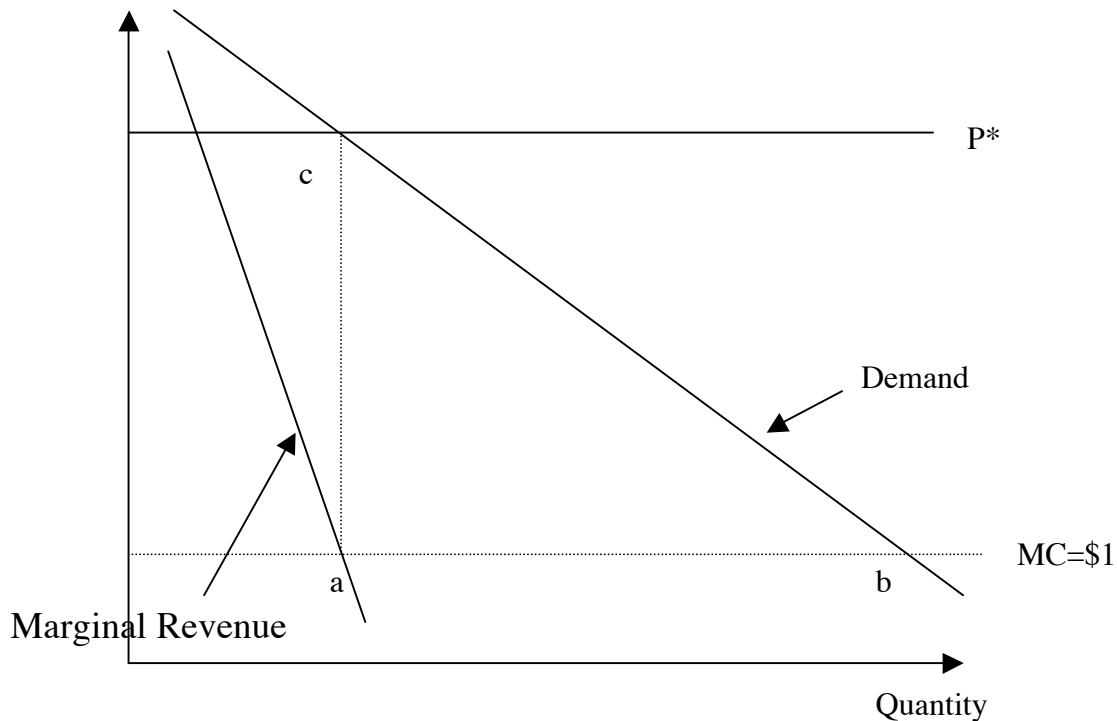


Competition, Monopoly, and Market Failure in the Market for Drugs



This figure shows the equilibrium price for a medication over which the manufacturer has monopoly power. The profit-maximizing price P^* is the price where marginal revenue equals marginal cost.

Pareto efficiency requires that the price be equal to the marginal cost. Since price is much higher, there is an economic inefficiency: consumers between points a and b would be willing to pay more than \$1 for the drug, but because the maximum they are willing to pay is $< P^*$ they will not obtain the medication.