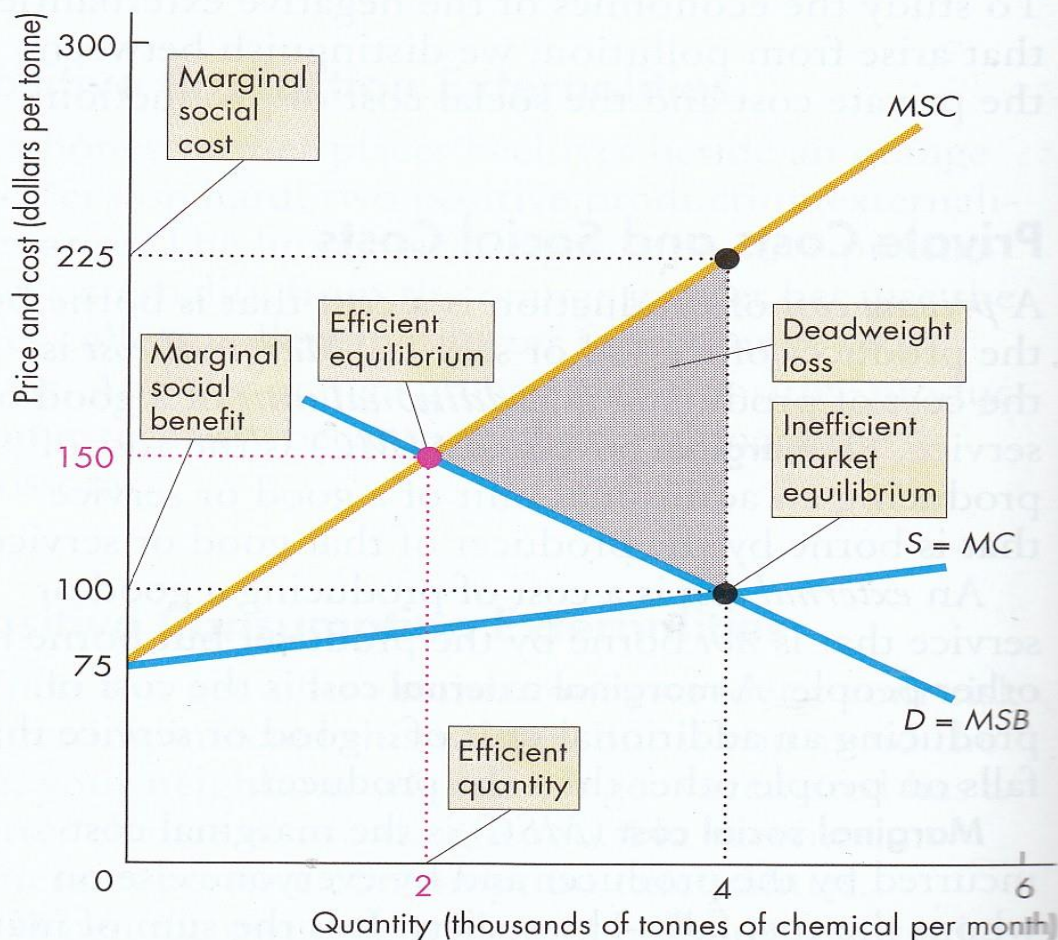FIGURE 16.2 Inefficiency with an External Cost

The supply curve is the marginal private cost curve, S = MC. The demand curve is the marginal social benefit curve, D = MSB. Market equilibrium at a price of $100 a tonne and 4,000 tonnes a month is inefficient because marginal social cost exceeds marginal social benefit. The efficient quantity is 2,000 tonnes a month. The grey triangle shows the deadweight loss created by the pollution externality.