We develop a theoretical framework to study illicit drugs markets, and we estimate it using data on drug purchases. Buyers are searching for high-quality drugs, but they can determine drugs’ quality (i.e., their purity) only after consuming them. Hence, sellers can rip-off first-time buyers, or can offer higher-quality drugs to induce buyers to purchase again from them. In equilibrium, a distribution of qualities persists. The estimated model implies that sellers’ moral hazard reduces the average and increases the dispersion of drug purity, thereby affecting drug consumption. Moreover, the estimated model implies that increasing penalties may increase the purity and the affordability of drugs traded, because it increases sellers’ relative profitability of targeting loyal buyers versus first-time buyers.