In this talk, I apply contract theory to analyze the dynamics of the ongoing trade negotiation between the United States and China. The United States complained that previous bilateral engagements with China had yielded empty promises from China without substantial progress in the legal protection for the intellectual property owned by US businesses. Thus, in this round of trade negotiations, the United States insisted upon a rigid trade agreement, hoping that China would more credibly commit to its promises. China, on the other hand, preferred a flexible agreement that would allow it substantial leeway in determining how to write and enforce its own laws. The row regarding contract specificity directly resulted in an impasse. I argue that the US trade negotiators have overlooked the incomplete nature of the trade agreement. As such, the US negotiators have overestimated the benefit of writing a rigid contract while underestimating the price of dignity to the Chinese government in acceding to the US demand. Instead of continuing with the legalistic approach of attempting to draft a more complete contract, I urge the US trade negotiators to take an economic approach in dealing with China — sometimes, less is more.

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