

Does Japanese Liquor Taste Different?: Empirical Analysis on the National Treatment under the WTO

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Abstract

The national treatment obligation, along with most favored nation obligation, is an ant principle of non-discrimination adopted by the WTO. It requires that foreign products be treated no less favorably than national products. This paper empirically examines the 1996 WTO recommendation that a Japanese distilled alcohol beverage, *shochu*, is a ‘directly competitive or substitute product’ to the other distilled drinks, and thus not taxing similarly is in violation of its national treatment obligation. Demand estimates obtained from a random coefficient discrete choice model reveal, contrary to the WTO conclusion, that it is not the case that a common production process (i.e. distillation) necessarily leads to strong substitution relationship. Upon the recommendation by the WTO Appellate Body, Japan made all distilled liquors at issue be taxed at the same rate in 2000. Our simulation analysis suggests that, while the tax revision contributed consumer welfare, a more desirable situation would have been actualized if the constraints by the NT obligation had been imposed based on the correct substitution relationship.

Keywords: National treatment obligation; WTO; Random coefficient discrete choice model; Alcohol demand

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