Health Care Expenditures and Gross Domestic Product: The Turkish Case

Seher Nur Sülkü and Asena Caner

Department of Economics
TOBB University of Economics and Technology

Working Paper No: 09-03
TOBB University of Economics and Technology
Department of Economics

July 2009

HEALTH CARE EXPENDITURES AND GROSS DOMESTIC PRODUCT: THE TURKISH CASE

Seher Nur Sülkü[*]
and
Asena Caner[**]

July 2009

Abstract

Our study examines the long-run relationship among per capita gross domestic product (GDP), per capita health expenditures and population growth rate in Turkey during the 1984-2006 period employing the Johansen multivariate cointegration technique. Related previous studies on OECD countries have mostly excluded Turkey, an OECD country itself. The only study on Turkey examines the 1984-1998 period. However, after 1998, major events and policy changes that had a substantial impact on income and health expenditures took place in Turkey, including a series of reforms to restructure the health and social security system. In contrast to the earlier findings in the literature, we find that the income elasticity of total health expenditures is less than one, which indicates that health care is a necessity in Turkey in the period of analysis. According to our results, a 10% increase in per capita GDP is associated with an 8.7% increase in total per capita health expenditures, controlling for population growth. We find that the income elasticity of public health expenditures is less than one. But, in the case of private health care expenditures, the elasticity is greater than one, meaning that private health care is a luxury good in Turkey.

Keywords: health care expenditures, income elasticity, cointegration, health care reform, Turkey
JEL Classification: I11, H51, C22

[*] Ministry of Health of Turkey, Mithatpaşa Cad. No. 3, Sıhhiye, Ankara, Turkey, 06434 and Karadeniz Technical University, Econometrics Department, Trabzon, Turkey, 61080. E-mail: sehernur.sulku@saglik.gov.tr, Phone: 01190 312 585 2317, Fax: 011 90 312 585 2349.

[**] TOBB-Economics and Technology University, Economics Department, Söğütözü Cad. No. 43, Söğütözü, Ankara, Turkey, 06560. E-mail: acaner@etu.edu.tr, Phone: 011 90 312 292 4111, Fax: 011 90 312 287 1946.

Acknowledgements: We are grateful to our colleagues Taylan Bali and Rezzan Kaynak for their contribution to and comments on an earlier unpublished version of this study. The usual disclaimer applies.

1. Introduction

For policymakers, it is crucial to know the long-term relationship between national income and health expenditures. Knowing this relationship enables them to make a judgement on how much aggregate health expenditures will change in the coming years, based on a forecast of the trend in national income. It helps policymakers to plan health reforms and to allocate resources efficiently. Although there are many studies on the link between health expenditures and GDP in OECD countries, we do not know much about the case in Turkey, an OECD member itself. Studies that used OECD data have excluded Turkey due to data availability or data comparability issues.

In this contribution, we examine the long-run relationship among per capita gross domestic product (GDP), per capita health expenditures and population growth rate in Turkey during the 1984-2006 period, using the Johansen multivariate cointegration technique. To the best of our knowledge, Kiymaz et.al. [15] is the only study in the literature that examines this link in Turkey. These authors use data for the 1984-1998 period from the OECD Health Data 2002 to find that the GDP elasticity of health expenditures is greater than one, thereby reaching the conclusion that health care is a luxury good in Turkey. However, after 1998, some major events and policy changes that had a substantial impact on income and health expenditures took place in Turkey. These events and policy changes are so important that they have surely affected the relationship between income and health expenditure, therefore, a new analysis is needed.

There was a devastating earthquake in 1999. In the years 1998-1999 a financial crisis occurred due to excessive risks taken by the Turkish banking sector, and partly due to the contagion effect of a worldwide financial crisis. Turkey faced its deepest financial crisis in 2001. Such financial crises deteriorate macroeconomic balances substantially. In 2001 real per capita GDP shrank 8,77% [1]. Nevertheless, during the 2002-2006 period, the Turkish economy recovered very quickly. Real per capita GDP growth rate reached 10% in 2006 [2]. Moreover, significant gains were reported in reducing the rate of inflation. Indeed, during the 1984-2006 period, the country experienced single-digit inflation for the first time in year 2004.

During the recovery from the 2001 crisis, the government adopted a reform program that included a major revision of the health and social security system in Turkey. The "Health Transformation Program" (HTP) was launched in 2003. The main aims of the HTP were to improve access, equity and efficiency, and to provide modern high quality health services, adequate financial protection against high health expenses while establishing a financially sustainable health system. After 2003, a series of reforms were made such as integrating different

[1] , [2] Own calculations based on OECD Health Data 2007.

social security schemes under the newly established Social Security Institution, initiating the Universal Health Insurance system, and introducing a performance based supplementary payment system in the Ministry of Health (MoH) facilities.

Our study contributes to the literature in an important way. We update the Kiymaz et.al. [15] study by extending the analysis period to 1984-2006, thereby incorporating the effects of the events that took place after 1998. As this time period includes important events and sudden changes, it is likely that taking it into account will have an effect on the long-run relationship between health expenditures and GDP. Moreover, as we employ a longer time series, we do a better job in terms of estimating the long-run relationship. In contrast to the cited study, we find that the income elasticity of total health expenditures is less than one, suggesting that health care is a necessity good in Turkey. According to our findings, a 10% increase in per capita GDP is associated with an 8.7% increase in total per capita health expenditures.

We proceed in section 2 to review the literature on the long-run relationship between income and health expenditures. In section 3, we report on the major events that happened after 1998 and that we expect to influence the long-run relationship between our two variables of interest. We also briefly describe the provision and financing of the health system prior to the HTP reforms. In section 4, we describe the data and the methods used in the econometric analysis. We explain our findings in section 5. Finally, section 6 summarizes and concludes our study. In the Appendix, we provide the chronology of the HTP reforms.

2. Related Literature

It is well known that there is a significant relationship between national expenditures on health care and gross domestic product (GDP). Many studies find that there is a strong and positive correlation between these two variables. However, there is no consensus on the magnitude of the income elasticity of health expenditures. Estimates vary depending on the country sample, the time period and the analysis technique used. Reported income elasticity estimates in the literature are often greater than one [5, 8, 13 (public health expenditures), 15, 20, 21 (for some OECD countries), 23], but estimates that are less than one [1, 7, 4, 13 (private health expenditures)] or at or around one have also been reported [12, 13 (total health expenditures), 19]. Some other studies find no long-run relationship between the two variables of interest [3, 11, 16, 21 (for some OECD countries)].

The earlier studies in this literature usually performed cross-sectional regression analyses with a small number of observations and a few variables. For example, Newhouse [20] used data from 13 developed countries in (or closest to) year 1970 to estimate income elasticity that is greater than one. Using a larger dataset and purchasing power parity prices to compare expenditures in

different countries instead of exchange rates, Parkin et.al. [23] found that health care is closer to being a necessity than being a luxury good. Gerdtham et.al. [8] estimated the income elasticity of health expenditures as 1.33 (and significantly greater than one) based on data from 19 OECD countries in year 1987.

Another group of studies took advantage of the panel structure of the OECD data to analyse the statistical relationship between per capita real health care expenditure and aggregate income. Based on pooled cross-sectional, time-series data for 22 OECD countries from 1972 to 1987, Gerdtham [7] found that health care expenditure does not appear to be income elastic, contrary to results of earlier studies. This group of studies confirmed the finding that aggregate income is the most important determinant of health care expenditure. Again, based on pooled OECD data, Hitiris and Posnett [12] estimated income elasticity to be at or around unity, but also suggested that OECD countries should not be regarded as a single, homogeneous group.

The third and the most recent group of studies, some of which are cited below, include analyses of the existence of cointegrating relationship between per capita income and health expenditures. Realizing that the variables used in econometric analyses are not stationary, researchers started using techniques designed for handling such variables, such as unit root tests, cointegration and vector error correction models. The findings of these studies have varied depending on the data and the technique used. Moreover, despite the large amount of literature produced, the issues of the existence of cointegration and the magnitude of income elasticity are still controversial.

Murthy and Ukpolo [19] found evidence for cointegration and estimated that the income elasticity of per capita health expenditure was not significantly different from one, using U.S. data in the 1960-1987 period. Another study that followed the same methodology examined the data from 20 OECD countries in the 1960-1987 period and conducted a separate analysis for each country [11]. Interestingly, these authors found no cointegration relationship between income and health expenditures for most of these countries. They speculated that this finding was due to the shortness of the time series and probably due to the misspecification of the model.

Increasing availability of data from a higher number of countries and for longer periods, enabled researchers to conduct panel data analyses. Blomqvist and Carter [1] examined the long-run relationship between income and health spending in 19 OECD countries in a 32-year time period from 1960 to 1991. Based on the results from a cointegration model that included country dummies and a linear time trend, the authors argued that previous studies overestimated the income elasticity, whose true value should be closer to one. The authors argued that overestimation is due to ignoring the time series properties of the variables and also due to not including a time trend in the analysis. Gerdtham and Löthgren [9] also found a cointegration

relationship between health expenditures and income (both per capita real) by using time series and panel data analyses. Their study used data from 21 OECD countries in the 1960-97 period.

Due to structural differences between developed and developing countries, the results obtained for the former group may not be relevant for the latter group. In developing countries, economic stagnation, debt, structural adjustment programs and health sector reform are more common. Jaunky and Khadaroo [13] conducted cointegration analysis based on data from 28 African countries in the period 1991-2000 to find that the income elasticity of public health expenditure is greater than one, whereas the income elasticity of private health expenditure is less than one. The authors do not find this result surprising, since in Africa the rich minority already purchases high-tech private health care services, while the public sector struggles to provide basic services to the poor majority, making health a luxury good for the poor. Although not a time-series study, the paper by Jowett [14] is relevant here as it discusses health expenditures in low-income countries. This paper examined the period from 1990 to 1995 in 44 low-income countries and found that private health expenditures were substituted for public health expenditures due to the structural adjustment and privatization policies in these countries. Despite the substitution, total health expenditures declined. The observation that the changes in health expenditures and income are in opposite directions is surprising and runs counter to the experience in developed countries.

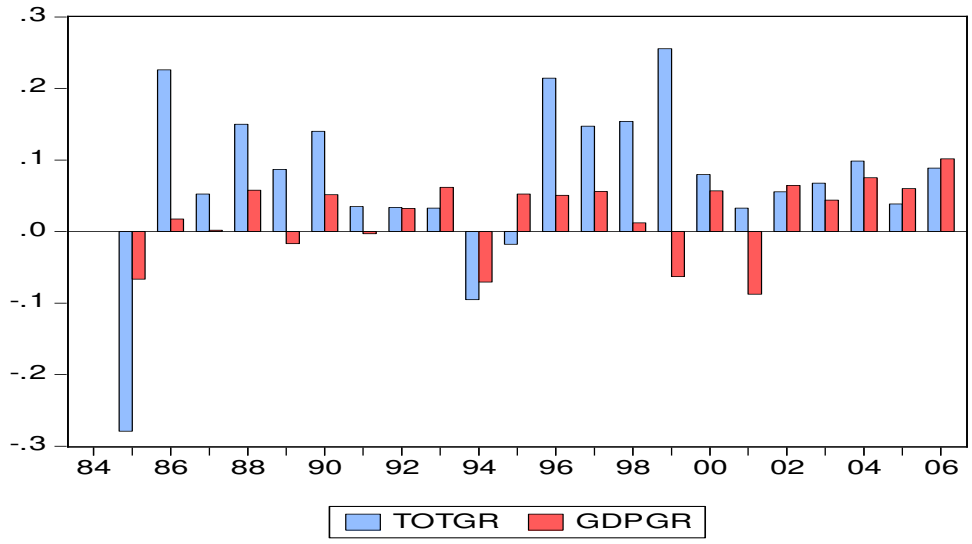
A very recent study uses a panel threshold regression model to derive country-specific and time-specific income elasticities for 17 OECD countries in the period 1975-2003 [4]. This cited study finds that health care is a necessity rather than a luxury, similarly to the finding of our analysis, but using a different technique.

Kiymaz et.al. [15], which is so far the only empirical study in the literature on the relationship between health expenditures and GDP in Turkey, is based on an analysis of the 1984-1998 period data using Johansen cointegration method. The study uses total, public and private per capita health expenditures, per capita national income and population growth rate data from the OECD 2002 database, and estimates that the GDP elasticity of health expenditures is greater than one. In particular, the authors find that a 10% increase in the GDP leads to a 21.9% increase in total health expenditures. Rather than reflecting long-term trends, the findings of this study explain the dynamics in the 1984-98 period. Due to reasons explained in the next section, the income-health expenditure relationship has probably changed in the period after 1998. Therefore, a new analysis that covers the after-1998 period is required.

3. Major Events in the Post-1998 Period in Turkey

In this study we examine the 1984-2006 period, whereas Kiymaz et.al. [15] study is based on the 1984-1998 period. After 1998, some major events and policy changes that affected the income-health expenditure relationship took place in Turkey. Figure 1 shows the annual percentage changes in per capital real GDP (GDPGR) and in per capita total health expenditures (TOTGR). As can be seen in the figure, TOTGR and GDPGR mostly had the same sign before 1998. Furthermore, the magnitudes of these variables were quite different. However, this pattern seems to have changes in the after-1998 period. In 1999 and 2001, the earthquake and the crisis years respectively, these variables not only took different signs but their magnitudes were also very different. In other years, both of the two variables had positive sign and they were very close to each other in magnitude. In other words, health expenditures and GDP increased at almost the same rate every year after 1998, with the exceptions being years 1999 and 2001.

Figure 1: Per Capita Real Total Health Care Expenditures and Per Capita Real GDP Annual Percentage Changes: 1984-2006 Period



Note: TOTGR = Annual percentage change in per real capita total health expenditure, GDPGR = Annual percentage change in real per capita GDP.
Source: Authors' calculations based on the OECD Health Data 2007 for the period 1984-2005 and the Ministry of Health (2007) Data for 2006.

In August 1999, an earthquake of 7.4 magnitude struck the northwest part of Turkey. More than 17,000 people were killed, more than 43,000 were injured and more than 500,000 people lost their homes [2]. The disaster area is the industrial centre of the country, therefore the economic loss caused by the disaster was substantial. Based on the OECD Health Data 2007, in 1999 GDP per capita declined by 6% while total health expenditures per capita increased by 25% relative to the previous year.

In year 2001, the country suffered an economic crisis. GDP per capita declined by 8.77%, while per capita total health expenditures increased by 3.28% with respect to year 2000, according to OECD Health Data 2007. Therefore, 2001 was a year during which changes in per capita GDP and per capita health expenditures were in opposite directions. Health expenditures were rising fast and uncontrollably, along with concerns about accessibility and equity issues regarding health care services.

During the 2002-2006 period Turkish economy recovered very quickly. Real per capita GDP growth rate was as high as 10% in 2006 [3]. Significant gains were reported in keeping inflation under control. Indeed, during the 1984-2006 period, the country experienced single-digit inflation for the first time in year 2004. During the recovery from the 2001 crisis, the government adopted an "Urgent Action Plan" which included a proposal for reform in the health and social security system called the "Health Transformation Program" (HTP).

Before the HTP reforms, Turkey had complexity and fragmentation in the health financing and delivery systems. Health care delivery system in Turkey was composed of public and private providers. There were three main public providers: the Ministry of Health (MoH), the Social Insurance Organization (SSK), and universities. There were three different social security schemes: SSK covering private sector employees and blue-collar public sector employees, Government Employees Retirement Fund (GERF) covering retired civil servants and the Social Insurance Agency of Merchants, Artisans and the Self-employed (Bag-Kur) covering self-employed people. These security funds provided both pension and health insurance. Health spending of active civil servants was financed from the general government budget through the budget of public institution they work for. The Green Card scheme, directly funded by the government budget, was providing free health services for people earning less than a minimum level of income. Separate public health insurance schemes had varying benefit packages and regulations; GERF had the deepest health benefit package while Green Card scheme had the shallowest (OECD [22] and Savas et. al [25]).

The "Health Transformation Program" (HTP) was launched in 2003. In the implementation of this reform proposal major changes that affect health expenditures have taken place.[4] Performance based supplementary payment system has been initiated in the MoH health facilities. The introduction of a performance based wage scheme in public hospitals has led to an increase in the volume of services provided along with an increase in the earnings of health care personnel. The SSK health facilities were transferred to the MoH; SSK members gained access to all MoH hospitals. The range of services provided for the Green Card holders, which included only inpatient healthcare services prior to HTP, has been expanded over time to include

[3] Own calculations based on OECD Health Data 2007.
[4] Please see the Appendix for a chronology of reforms.

outpatient health expenses. Both Green Card holders and SSK members gained access to private pharmacies. Patients have been given more freedom in their hospital and physician choice. Contractual agreements have been made with private health care facilities to increase service availability. There have also been major changes in the payment policies regarding medications, medical supplies and medical services with the aim of restraining costs. Furthermore, the three public social security institutions (GERF, SSK and Bag-Kur) have been united to form one national institution (called the "Social Security Institution"). Moreover, in 2008 Universal Health Insurances (UHI) has been initiated. With this program, benefits packages across various health insurance schemes will be eventually unified. (OECD [22]).[5]

We should mention that although the policy changes described above are expected to have effects on health expenditures, in the long run they can bring unit costs down by increasing the efficiency of the healthcare system, by improving health indicators of the general public and by triggering labour productivity increases. Therefore, if the reforms can be successfully implemented, they can have substantial positive effects on Turkish economy. Indeed, during 2002-2006 the growth rates of health expenditures and real GDP were comparable, which suggests that health expenses were sustainable in this period (see Figure 1).

4. Data and Methodology

Our data are composed of annual time series of total, private and public health expenditures, GDP and population growth rate in the 1984-2006 period. For the 1984-2005 period, health care expenditures data and the GDP series are taken from the OECD Health Data 2007.[6] Both health care and GDP series are in per capita terms at constant 2000 prices. Data for 2006 are acquired from the Ministry of Health (2007) in nominal terms. To convert them into real per capita terms, the GDP deflator and population size are employed, acquired from the IMF World Economic Outlook and the OECD Health Data 2008, respectively. Finally, during the 1984-2006 period annual population growth rates are calculated using the population series obtained from the OECD Health Data 2008. All of the series, total (LNTOT), public (LNPUB) and private (LNPRI) health care expenditure series and GDP series (LNGDP), except for the population growth rate (POPGR) are transformed into natural logarithms.

[5] UHI aims to cover the whole population. However, the reform process takes time; GERF members and green card holders are planned to be covered by UHI in three years. In this study we cannot examine the effect of the introduction of the UHI since we have data up to year 2006.

[6] Both OECD Health Data 2007 and 2008 provide the same health expenditures series up to year 2005. However, regarding the GDP data, the 2008 version has the new GDP series recently adjusted by the Turkish Statistics Institute, whereas the 2007 version has the old series. The new GDP series has been adjusted starting from 1998. Therefore the 1984-2006 series has a break in year 1998. To stay away from this problem, we have chosen to use the old GDP series in the 2007 version of the OECD Health Data.

The Johansen cointegration methodology is employed to explore the long run relationship between health care expenditures, GDP and population growth rate in Turkey during the 1984-2006 period. According to cointegration theory, first, the integration order of variables should be checked. If a series y_t must be differenced d times to be stationary, it is said to be "*integrated of order d*", denoted by $y_t \sim I(d)$. In our study, the integration orders of variables are determined by using the well known Augmented Dickey-Fuller (ADF) (1981) and Phillips and Perron (PP) (1988) unit root tests[7], which test the null hypothesis of nonstationarity against the alternative hypothesis of stationarity.

In the application of the Johansen procedure, a vector autoregressive (VAR) model is constructed to obtain a long-run relationship among the stochastic variables. The VAR model can be expressed as:

$$\Delta x_t = \Gamma_1 \Delta x_{t-1} + \Gamma_2 \Delta x_{t-2} + ... + \Gamma_{k-1} \Delta x_{t-k+1} + \pi x_{t-k} + \mu c_t + \varepsilon_t , \qquad (1)$$

where Δ is the first difference operator, x_t is an nx1 vector of variables, π is an n x n matrix of rank 'r', c_t is the intercept and ε_t is an n x 1 vector of residuals with zero mean and variance matrix Ω.We define the vector x_t as (LNHealth, LNGDP, POPGR)', where LNHealth stands for either LNTOT, LNPUB or LNPRI depending on the case, since we examine total health expenditures as well as public and private health expenditures.

The rank of the π matrix determines the dimensionality of the cointegrating space, where

$$\pi = \alpha\beta` \qquad (2)$$

is the matrix of long-run responses, where α and β are n x r matrices for n variables and r cointegrating vectors. If $0 < r < n$, there are r cointegrating vectors; but if $r = 0$, there is no cointegration between health care expenditure, GDP and POPGR series. The case of $r = n$ implies the stationarity of the GDP, population growth and health care expenditure series in their levels; therefore cointegrating relation cannot exist among them. α matrix is called the loading matrix and gives the weight attached to each cointegrating vector in every equation. β is the matrix of cointegrating vectors which can be estimated as the eigenvectors associated with the r largest, statistically significant eigenvalues found by calculating

$$| \lambda S_{kk} - S_{k0} S_{00}^{-1} S_{0k} | = 0. \qquad (3)$$

In the above equality, S_{00} is the residual moment matrix from the least squares regression of Δx_t on Δx_{t-1}, ..., Δx_{t-k+1} and S_{kk} is the residual moment matrix from the least squares regression of x_{t-k} on Δx_{t-k+1}. S_{0k} is the cross product moment matrix. Using these eigenvalues one can test the

[7] Since these tests are very commonly used in the literature, we do not provide detailed information on them. Please see Dickey and Fuller (1981) and Phillips and Perron [25] for details.

hypothesis that there are at most r cointegrating vectors by using the eigenvalues and calculating the likelihood test statistics

$(-2)\ln(Q) = -T \Sigma_{i=r+1} 1n (1-\lambda_i)$, (4)

where $\lambda_{r+1} .... \lambda_n$ are the (n-r) smallest eigenvalues, and this is called the trace test. There is also a likelihood ratio test, called the maximal eigenvalue test (λ Max), in which the null hypothesis of r cointegrating vectors is tested versus the alternative of r + 1 cointegrating vectors. In this study, we use the trace test.

5. Empirical Findings

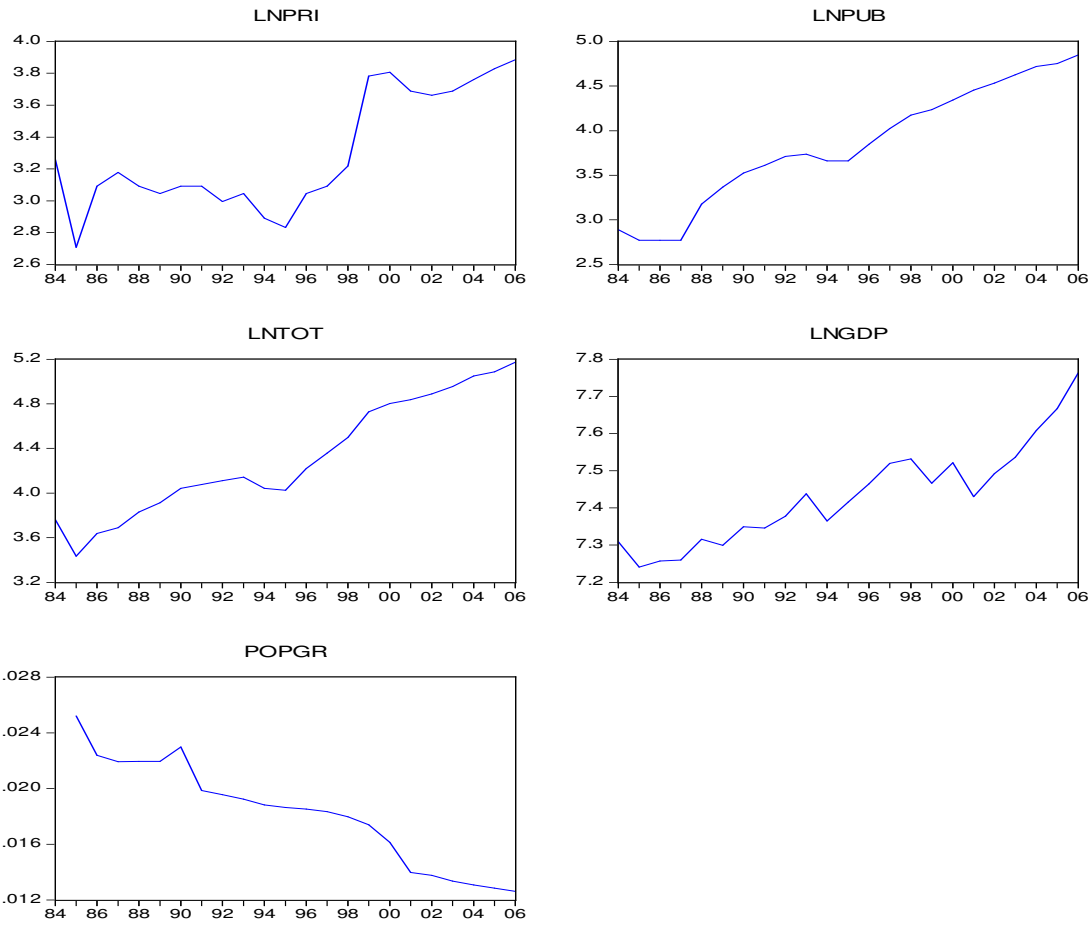
We present the descriptive statistics of our variables in Table 1. Among the health expenditure series public health expenditure series has the highest variation followed by total and private health expenditures. The variation of LNGDP series is lower than any of the health expenditure series. Except for the LNPUB and POPGR series, all of the series have positive skewness (i.e. the mean of the series is greater than the median). All of the series are leptokurtic (i.e. the distribution has a sharper peak and a fatter tail than the normal distribution). The average population growth rate is 2%. The time series graphs of the variables are shown in Figure 2. In the LNGDP graph, the negative effects of the 1999 earthquake and the 2001 crisis are visible. After year 2001, LNTOT has been increasing steadily but at a slower rate than LNGDP.

Table 1: Distributional Characteristics of the Variables Used in the Analysis

Variables	N	Mean	Standard Deviation	Skewness	Kurtosis
LNPRI	23	3.29	0.37	0.36	1.66
LNPUB	23	3.84	0.67	-0.17	1.92
LNTOT	23	4.32	0.52	0.18	1.76
LNGDP	23	7.43	0.14	0.59	2.85
POPGR	23	0.02	0.004	-0.06	1.99

Note: All variables, except for the population growth rate, are in natural logarithms and per capita terms at 2000 prices. **Source:** Authors' calculations based on the OECD Health Data 2007.

Figure 2: Time Series Graphs of the Variables Used in the Analysis



Note: LNPRI = Reel per capita private health expenditure in natural logarithms, LNPUB = Reel per capita public health expenditure in natural logarithms, LNTOT = Reel per capita total health expenditure in natural logarithms, LNGDP = Reel per capita GDP in natural logarithms, POPGR = Population growth rate. **Source:** Authors' calculations based on the OECD Health Data 2007.

As explained in section 4, the first step in cointegration analysis is to determine the integration order of the variables. Therefore, the ADF and PP unit root tests are conducted on both levels and first differences of series by using the E*Views* 6 package. The results are reported in Table 2. For the ADF regression lagged differences are introduced into the model so that the residuals are white noise processes. The numbers in parentheses in the ADF test represent the highest order of lag for which the t-statistic in the regression is significant. The lag lengths are determined according to the Schwartz information criterion. For the PP test, Parzen kernel spectral estimation method is chosen and the Newey–West procedure is used in order to adjust the standard errors. The numbers in parentheses in the PP test represent the bandwidth of the Newey-

West procedure.[8] Except for the LNPUB and LNTOT variables, there is a consensus between the ADF and PP tests results.[9] According to the ADF test all of the series, all time series but LNPUB are I(1) processes which means that they are nonstationary, and become stationary when they are first-differenced. For LNPUB series, it is possible to reject the hypothesis that the series is nonstationary at 1 percent significance level. But, when we apply PP test all of the series including LNPUB are found as I(1) processes at 1 percent significance level except for LNTOT. According to the PP test, the LNTOT series is stationary at its level. With these exceptions in mind, it is reasonable to conclude that all of the series are integrated of order one, I(1).

Table 2: ADF and PP Unit Root Tests

	ADF Level	**ADF First Difference**	**PP Level**	**PP First Difference**
Variable	with constant and trend	with constant	with constant and trend	with constant
LNPRI	-2.77 (0)	-6.41** (0)	-2.83 (3)	-6.12** (3)
LNPUB	-4.78** (4)	-3.72* (0)	-2.26 (9)	-4.41** (12)
LNTOT	-1.70 (1)	-7.15** (0)	-3.36* (1)	-7.15** (0)
LNGDP	-2.26 (0)	-5.59** (0)	-2.45 (5)	-5.54** (4)
POPGR	-3.25 (0)	-5.60** (0)	-3.25 (7)	-10.07** (13)

Note: **, * denote significance at 1% and 5% levels respectively.
Source: Authors' calculations based on the OECD Health Data 2007 using EViews 6.

Since the cointegration results are sensitive to the lag length of VAR, the optimum lag length of the cointegration is found according to the Schwarz criterion. We consider the VAR(1) and VAR(2) models. Since, our data are annual, the maximum length is chosen as 2. The models are estimated without a constant. The minimum of Schwarz criterion for each gives the optimum lag length for the VAR model. The Schwarz test values for all models are shown in Table 3. It is found that VAR(1) models are optimal in all cases.

Table 3: Selection of the VAR Model

	VAR (1)	VAR (2)
LNPRI	-14.3	-13.8
LNPUB	-15.6	-15.2
LNTOT	-16.1	-15.7

Note: The Schwarz criterion is used to find the optimum lag length of the VAR models.
Source: Authors' calculations.

[8] E-views employs the MacKinnon critical values in the ADF and PP tests.
[9] Even though the ADF and PP tests are asymptotically equivalent, they may differ in finite samples because of the different ways in which they correct for the serial correlation of the test regression. Please see Perron and Ng [24] and Schwert [27] for a detailed comparison of these techniques.

The long run relationship among the health expenditure, per capita GDP and population growth rate series are explored by using the Johansen procedure without an intercept term in the equation. The cointegration analysis is computed by E-views version 6 which derives the critical values for the trace test using MacKinnon-Haug-Michelis [16] p-values. The results of multivariate cointegrating analyses are reported in Table 4. Regarding LNPUB, the trace test indicates two cointegrating vectors at the 1% level. Similarly, the trace test results of LNTOT suggest two cointegrating equations at the 5% level. However, the results of LNPRI model show that the null hypothesis of no-cointegrating relationship can be weakly rejected at 5% significance level, which indicates only one cointegrating relationship among LNPRI, LNGDP and POPGR.

Table 4: Johansen Multivariate Cointegration Tests

H_0	H_A	Trace Test	%5 Critical Value	Prob.$^{++}$
LNPUB				
R=0	r=1	35.2**	24.2	0.00**
r ≤ 1	r=2	18.6**	12.3	0.00**
r ≤ 2	r=3	3.8	4.1	0.06
LNPRI				
R=0	r=1	24.0*	24.2	0.05*
r ≤ 1	r=2	7.0	12.3	0.32
r ≤ 2	r=3	0.2	4.1	0.65
LNTOT				
R=0	r=1	28.6**	24.2	0.01**
r ≤ 1	r=2	13.4*	12.3	0.03*
r ≤ 2	r=3	0.8	4.1	0.39

Notes: $^{++}$MacKinnon-Haug-Michelis [16] p-values. If the p-value is less than 0.01 (or 0.05) then the null hypothesis is rejected at %1 (or %5) level. **, * denote significance at 1% and 5% levels respectively.
Source: Authors' calculations.

Finding evidence for the existence of a cointegration relationship tells us that there is a long-run relationship among the health care expenditure, GDP and population growth series. In order to understand how the GDP and population growth rate series affect the health care expenditure series, we normalize the cointegrating vectors with respect to the coefficient of health care expenditures. The signs and the magnitudes of the normalized coefficients are given in Table 5.

Table 5: Cointegration Coefficients Normalized with respect to the Coefficient of the Health Expenditures Variable

		LNGDP	POPGR
LNPUB:	**Vector 1**	0.89 (0.03)**	-145.49 (10.51)**
	Vector 2	0.75(0.10)**	-131.73(38.9)**
LNPRI:	**Vector 1**	1.81 (0.46)**	- 351.33 (179.3)*
LNTOT:	**Vector 1**	0.30 (0.24)	-11.08 (97.78)
	Vector 2	0.87 (0.02)**	-118.02(7.11)**

Notes: The estimated standard errors of the coefficient estimates are presented in parentheses. **, * denote significance at 1% and 5% levels respectively. **Source:** Authors' calculations.

The results shown in Table 5 indicate that there is a positive relationship between per capita reel GDP (LNGDP) and each of the per capita real health care expenditure series. However, there is a negative cointegrating relationship between population growth and each of the per capita reel health care expenditure series. These results are as expected, since during the 1984-2006 period POPGR has a negative time trend whereas all of the healthcare expenditure series have positive trends (see Figure 1).

In our model, the coefficient of the LNGDP variable can be interpreted as an estimate of the income elasticity of health care expenditures. We know that if the income elasiticity of a good is between zero and 1 (or greater than 1) that good is defined as a necessity (or a luxury). When the cointegration model exploring the long run relationship between LNPUB and LNGDP is considered, it is seen that the estimated coefficients of both of the cointegrated vectors are statistically significant. The estimated coefficients are 0.89 and 0.75 according to vector 1 and vector 2 respectively. As a result a 10% increase in GDP will cause either a 8.9% or 7.5% increase in public health expenditure. Since the income elasticity is less than 1 in both cases, we conclude that public health care services are a necessity during the 1984-2006 period.

When the model presenting the cointegrating relationship between LNPRI and LNGDP is examined, the estimated LNGDP coefficient is found to be 1.81 which is statistically significant. Therefore, a 10% increase in GDP will lead a 18.1% increase in private health care expenditure. Since the income elasticity of LNPRI is greater than 1 in this case, we can say that private health care services is as a luxury during the 1984-2006 period.

Finally, the cointegrating vectors establishing the long-run relationship between LNTOT and LNGDP are examined. It is observed that only the second vector (vector 2) has statistically

significant cofficients. The estimated LNGDP coefficient of vector 2 is 0.87, which means that a 10% increase in GDP will create a 8.7% increase in total health care expenditure. As a result, total health care expenditure has an income elasticity less than 1, thus during the 1984-2006 period LNTOT represents a necessity.

6. Summary and Conclusions

In this study, we examine the long-run relationship between health care expenditures and national income in Turkey. We applied the Johansen multivariate cointegration technique to investigate the cointegrating relationship among per capita health expenditures, per capita GDP, and population growth rate in Turkey during the 1984-2006 period. Firstly, employing the ADF and PP unit root tests, all of the series are found as integrated of order one, I(1). Following the tests of nonstationarity, we perform the cointegration analyses. As a result, we find evidence for multivariate cointegrating relationship among the health care expenditures (public, private, total), GDP and population growth series. Finding evidence for the existence of a cointegration relationship tells us that there is a long-run relationship among the considered series.

Since we would like to estimate the income elasticity of health expenditures, the cointegrating vectors are normalized with respect to the coefficient of health care expenditures. When the cointegration model of public health care expenditure and GDP is considered, two significant cointegrating vectors are observed. The normalized coefficients of the LNGDP variable are 0.89 and 0.75 with respect to vector 1 and vector 2. Thus, a 10% increase in per capita GDP will cause a 7.5 - 8.9% increase in public health expenditure while controlling for population growth. In the case of private health expenditures, we found only one cointegrating vector. We observe that, a 10% increase in GDP will lead to an 18.1% increase in private health expenditures. Furthermore, we find that the income elasticity of total health expenditures is less than one, which indicates that health care is a necessity in Turkey during the 1984-2006 period. According to our results, a 10% increase in per capita GDP is associated with an 8.7% increase in total per capita health expenditures while controlling for population growth.

Although there are numerous studies of the relationship between health expenditures and GDP in OECD countries, Kiymaz et.al. [15] is the only study that examines this link on Turkey, as far as we know. These authors study the 1984-1998 period. However, after 1998, some major events and policy changes took place in Turkey, including a series of reforms to restructure the health and social security system. Evidently, these events and changes have had a non-negligible influence on the long-run relationship between our two variables of interest. In contrast to findings of Kiymaz et. al. [15], we find that health care is a necessity in Turkey. We believe that our findings will help policymakers to make a better judgement on how much aggregate health expenditures will change in the coming years, given a forecast of the trend in national income.

References

1. Blomqvist, A. G. and R. A. L. Carter (1997), "Is health care really a luxury?", *Journal of Health Economics*, 16, 207-229.
2. Bolt, Bruce A. (2004), *Earthquakes*, W.H. Freeman and Company.
3. Carrion-i-Silvestre, J.L. (2005) "Health care expenditure and GDP: are they broken stationary?", *Journal of Health Economics*, 24 (5), 839–854.
4. Chakroun, M. (2009), "Health care expenditure and GDP: An international panel smooth transition approach", Munich Personal RePEc Archive Paper No. 14322, May, online at http://mpra.ub.uni-muenchen.de/14322/
5. Clemente, J. J., C. Marcuello, A. Montañés and F.Pueyo (2004), "On the international stability of health care expenditure functions: are government and private functions similar?", *Journal of Health Economics*, 23, 589–613.
6. Dickey, D. A. and W. A. Fuller (1981) "Likelihood Ratio Test Statistics for Autoregressive Time Series with A Unit Root," *Econometrica*, 49, ss. 1057-1072.
7. Gerdtham, U.G. (1992), "Pooling international health care expenditure data", *Health Economics*, 1(4), 217-231.
8. Gerdtham, U. G., J. Sogaard, F. Andersson and B. Jönsson (1992), "An econometric analysis of health care expenditure: A cross-section study of the OECD countries", *Journal of Health Economics*, 11, 63-84.
9. Gerdtham, U. G. and M. Löthgren (2000), "On stationarity and cointegration of international health expenditure and GDP", *Journal of Health Economics*, 19, 461–475.
10. Hagist C. and L. J. Kotlikoff (2005), "Who's Going Broke? Comparing Growth in Healthcare Costs in Ten OECD Countries", NBER Working Paper No. 11833.
11. Hansen P. and A. King (1996), "The determinants of health care expenditure: A cointegration approach", *Journal of Health Economics*, 15, 127-137.
12. Hitiris, T. and J. Posnett (1992), "The determinants and effects of health care expenditure in developed countries", *Journal of Health Economics,* 11(2), 173-181, August.
13. Jaunky, V. C. and A. J. Khadaroo (2008), "Health Care Expenditure and GDP: An African Perspective", *Applied Econometrics and International Development*, 8(1), 131-146.
14. Jowett, M. (1999), "Bucking the Trend? Health Care Expenditures in Low-Income Countries 1990-1995", *International Journal of Health Planning and Management*, 14, 269-285.
15. Kiymaz, H., Y. Akbulut and A. Demir (2006), "Tests of stationarity and cointegration of health care expenditure and gross domestic product", *European Journal of Health Economics*, 7(4), 285-289.
16. MacKinnon, J., A. A. Haug, and L. Michelis (1999), "Numerical Distribution Functions of Likelihood Ratio Tests for Cointegration", *Journal of Applied Econometrics*, 14(5), 563-577.
17. McCoskey, S. and T. M. Selden (1998), "Health care expenditures and GDP: panel data unit root test results", *Journal of Health Economics*, 17, 369–376.
18. Ministry of Health (2007), *Türkiye'de Sağlığa Bakış 2007 (A Look at Health in Turkey 2007)*, Hıfzıssıhha Mektebi Müdürlüğü, T.C. Sağlık Bakanlığı, Ankara, Türkiye.
19. Murthy, N.R.V. and V. Ukpolo (1994), "Aggregate health care expenditure in the United States: evidence from cointegration tests", *Applied Economics*, 26, 797-802.

20. Newhouse, J. P. (1977), "Medical-Care Expenditure: A Cross-National Survey", *Journal of Human Resources*, 12(1), 115-125.
21. Okunade, A. and M. Karakus (2001), "Unit root and cointegration tests: time series versus panel estimates for international health expenditure models", *Applied Economics*, 2001, 33, 1131-1137.
22. OECD (2009), *Reviews of Health Systems Turkey*, OECD and the International Bank for Reconstruction and Development/The World Bank.
23. Parkin, D., A. McGuire and B. Yule (1987), "Aggregate health expenditures and national income: Is health care a luxury good?", *Journal of Health Economics*, 6, 109-127.
24. Perron P. and S. Ng (1996), "Useful Modifications to Some Unit Root Tests with Dependent Errors and their Local Asymptotic Properties," *Review of Economic Studies*, 63(3), 435-463, July.
25. Phillips, P. and P. Perron (1988), "Testing for a unit root in time series regression", *Biometrika*, 75(2), 335-346.
26. Savas, S.B., Ö. Karahan, Ö. Saka (2002), *Health care systems in transition: Turkey*. In: Thomson S, and Mossialos E, editors. Copenhagen, European Observatory on Health Care Systems; 4(4).
27. Schwert, G.W. (1989), "Test for Unit Roots: A Monte Carlo Investigation," *Journal of Business and Economic Statistics*, 7(2), 147-159.
28. TEPAV (2008), *Turkey Health Report*, Project No: 106G133, Economic Policy Research Foundation of Turkey (TEPAV), Ankara, Turkey.

Appendix: Recent Developments in The Turkish Health Care System: The Chronology of HTP Reforms (Sources: OECD [22], TEPAV [28] and our research.)

2004

January – Performance based supplementary payment system has been initiated in MoH health facilities.

January – MoH and SSK signed protocol for common use of their health facilities.

March – Value added of prescription drugs dropped to 8% from 18%.

April – Reference price system has been established.[10]

May - Green Card holders has been covered for outpatient health expenses.

2005

January - Green Card holders allowed to access private pharmacies.

January - Value added of health services and non-prescription drugs dropped to 8% from 18%.

[10] According to this system 5 (or at most 10) European Union countries' drug prices were followed and the cheapest ones were taken as reference for the drug prices in Turkey.

February – SSK health facilities has been transferred to MoH.

February – SSK pharmacies closed and members permitted to access private pharmacies.

May – Green Card holders has been required to pay 20% contribution for outpatient prescription drug expenses.

June –"Licensing Regulation" for pharmaceuticals passed and expiration time of the licenses have been established as 5 years.

July – Generic drug application has been expanded to 333 active groups instead of 77 groups.

September - Family Medicine has been initiated first in Duzce.

2006

January – All of the reimbursement institutions started to use one common positive list.

May - Law 5502 implemented. Social Security Institution (SSI) has been established; SSK, Bag-Kur and GERF have been integrated under one institution.

2007

June – SSI has established health implementation notice (SUT).

July – Primary care became free for all citizens (even if not covered under social security)

2008

April – Law 5754 “Social Security and UHI Law and its amendments” has been accepted.

July - All private hospitals under contract with SSI were allowed to charge patients at most 30% higher than SUT prices; contracted private hospitals were required to provide cancer therapy, emergency and intensive care to patients (insured by SSI).

October – UHI system has been initiated.