

# Abstract

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## Hidden Action Problems: The Case of Insurers and Business Policyholders in The Egyptian Car Insurance Market

**Purpose:** The paper seeks to investigate the effect of asymmetric information in an exchange relationship involving pre-screening by insurers, trust between insurer and policyholder, self-protection provided by different kinds of contracts on hidden action in the Egyptian car insurance market. **Design, methodology and approach:** The total population of all registered non-life insurance companies (32) in Egypt as approved by the Egyptian Financial Services Association (EFSA), the regulatory body in the insurance industry in Egypt, constitute the sampling frame for this study. In this study, respondents answered questions about their most recent cases of compensation by insurers based on a questionnaire. A total of 63 questionnaires were distributed and regression analysis was used to test and validate the hypotheses of this study. **Findings:** Information asymmetry is one of the main antecedents of hidden action problems by policyholders. The level of pre-screening done by insurer also goes a long way in attenuating hidden action. Furthermore, the level of trust in an exchange relationship attenuates the hidden action problems faced by policyholders. Moreover, the study found that self-protection attenuates hidden action problems at different types of contracts. It was further observed that self-protection is more efficient in genuinely attenuating hidden action with co-payment car insurance contract than with deductible car insurance contract. **Research limitation/implications:** As a result of numerous constraint in the field during the data collection phase, this study had a reasonable sample size which the authors would have easily increased 63 responses have been obtained for this study and as such is not exhaustive to generalize the findings. In addition, a cross sectional design was used at a particular time and as such this study does not inform changes in the market over time. Thus such is a provision for future research of longitudinal study to cater for market dynamics. **Theoretical implication:** The level of information asymmetry in a buyer seller relationship is an antecedent for hidden action problems as one party (policyholder) possess private information which the other party (insurer) desires and might lack due to self-seeking attitude of potential policyholders and they use this idiosyncratic information in purchasing their insurance policy. xi However, when insurer execute high level of pre-screening it serves as a basis to attract appropriate and high quality policyholder by revealing adequate information that help insurer in making selling decision this can serve as proactive strategy in attenuating hidden action. An exchange relationship characterized by trust tend to significantly weakens and attenuate hidden action problems by policyholders. **Managerial implication:** Hidden action is very harmful for the smooth and sustainable operation of business especially in the insurance market. This study has highlighted the antecedent of hidden action which business leaders and managers should take seriously in conducting business as it can ruin the performance of their client in honouring their contract. Also, it adversely affects exchange relationship, reduce market share and supply chain efficiency, increase the loss reserve of insurer, reduces profitability and affect the health of insurer's balance sheet. Thus, it is prudent to engage and coordinate effectively in an exchange relationship, developing trust which improves coordination and cooperation between trading partners and business performance. **Keywords:** hidden action problems, trust, self-protection, information asymmetry, pre-screening, kind of contract, size of damages, policyholders, insurers, insurance industry, Egypt, principal agent theory, relational contracting theory.