CS 5522: Artificial Intelligence II
Uncertainty and Utilities

Instructor: Alan Ritter
Ohio State University

[These slides were adapted from CS188 Intro to AI at UC Berkeley. All materials available at http://ai.berkeley.edu.]
Uncertain Outcomes
Worst-Case vs. Average Case

Idea: Uncertain outcomes controlled by chance, not an adversary!
Worst-Case vs. Average Case

Idea: Uncertain outcomes controlled by chance, not an adversary!
Idea: Uncertain outcomes controlled by chance, not an adversary!
Worst-Case vs. Average Case

Idea: Uncertain outcomes controlled by chance, not an adversary!
Worst-Case vs. Average Case

Idea: Uncertain outcomes controlled by chance, not an adversary!
Expectimax Search

- Why wouldn’t we know what the result of an action will be?
  - Explicit randomness: rolling dice
  - Unpredictable opponents: the ghosts respond randomly
  - Actions can fail: when moving a robot, wheels might slip

- Values should now reflect average-case (expectimax) outcomes, not worst-case (minimax) outcomes

[Demo: min vs exp (L7D1,2)]
Expectimax Search

- Why wouldn’t we know what the result of an action will be?
  - Explicit randomness: rolling dice
  - Unpredictable opponents: the ghosts respond randomly
  - Actions can fail: when moving a robot, wheels might slip

- Values should now reflect average-case (expectimax) outcomes, not worst-case (minimax) outcomes

- Expectimax search: compute the average score under optimal play
  - Max nodes as in minimax search
  - Chance nodes are like min nodes but the outcome is uncertain
  - Calculate their expected utilities
  - I.e. take weighted average (expectation) of children

- Later, we’ll learn how to formalize the underlying uncertain-result problems as Markov Decision Processes

[Demo: min vs exp (L7D1,2)]
Video of Demo Minimax vs Expectimax (Min)
Video of Demo Minimax vs Expectimax (Min)
Video of Demo Minimax vs Expectimax (Min)
Video of Demo Minimax vs Expectimax (Exp)
Video of Demo Minimax vs Expectimax (Exp)
Video of Demo Minimax vs Expectimax (Exp)
def value(state):
    if the state is a terminal state: return the state’s utility
    if the next agent is MAX: return max-value(state)
    if the next agent is EXP: return exp-value(state)
def value(state):
    if the state is a terminal state: return the state’s utility
    if the next agent is \texttt{MAX}: return max-value(state)
    if the next agent is \texttt{EXP}: return exp-value(state)

def max-value(state):
    initialize \( v = -\infty \)
    for each successor of state:
        \( v = \max(v, \text{value(successor)}) \)
    return \( v \)

def exp-value(state):
    initialize \( v = 0 \)
    for each successor of state:
        \( p = \text{probability(successor)} \)
        \( v += p \times \text{value(successor)} \)
    return \( v \)
Expectimax Pseudocode
def exp-value(state):
    initialize v = 0
    for each successor of state:
        p = probability(successor)
        v += p * value(successor)
    return v
def exp-value(state):
    initialize v = 0
    for each successor of state:
        p = probability(successor)
        v += p * value(successor)
    return v
def exp-value(state):
    initialize v = 0
    for each successor of state:
        p = probability(successor)
        v += p * value(successor)
    return v

v = (1/2) (8) + (1/3) (24) + (1/6) (-12) = 10
Expectimax Example
Expectimax Pruning?
Expectimax Pruning?
Depth-Limited Expectimax
Depth-Limited Expectimax
Depth-Limited Expectimax

Estimate of true expectimax value (which would require a lot of work to compute)
Probabilities
Reminder: Probabilities

- **A random variable** represents an event whose outcome is unknown
- **A probability distribution** is an assignment of weights to outcomes

**Example: Traffic on freeway**
- Random variable: $T =$ whether there’s traffic
- Outcomes: $T$ in {none, light, heavy}
- Distribution: $P(T=\text{none}) = 0.25$, $P(T=\text{light}) = 0.50$, $P(T=\text{heavy}) = 0.25$

**Some laws of probability (more later):**
- Probabilities are always non-negative
- Probabilities over all possible outcomes sum to one

**As we get more evidence, probabilities may change:**
- $P(T=\text{heavy}) = 0.25$, $P(T=\text{heavy} \mid \text{Hour=8am}) = 0.60$
- We’ll talk about methods for reasoning and updating probabilities later
Reminder: Expectations
The expected value of a function of a random variable is the average, weighted by the probability distribution over outcomes.

Example: How long to get to the airport?
The expected value of a function of a random variable is the average, weighted by the probability distribution over outcomes.

Example: How long to get to the airport?

<table>
<thead>
<tr>
<th>Probability</th>
<th>0.25</th>
<th>0.50</th>
<th>0.25</th>
</tr>
</thead>
</table>

[Images of road conditions including clear, mildly congested, and heavily congested traffic.]
The expected value of a function of a random variable is the average, weighted by the probability distribution over outcomes.

Example: How long to get to the airport?

<table>
<thead>
<tr>
<th>Time</th>
<th>Probability</th>
</tr>
</thead>
<tbody>
<tr>
<td>20 min</td>
<td>0.25</td>
</tr>
<tr>
<td>30 min</td>
<td>0.50</td>
</tr>
<tr>
<td>60 min</td>
<td>0.25</td>
</tr>
</tbody>
</table>
Reminder: Expectations

- The expected value of a function of a random variable is the average, weighted by the probability distribution over outcomes.

- Example: How long to get to the airport?

<table>
<thead>
<tr>
<th>Time</th>
<th>20 min</th>
<th>30 min</th>
<th>60 min</th>
</tr>
</thead>
<tbody>
<tr>
<td>x</td>
<td>x</td>
<td>x</td>
<td></td>
</tr>
<tr>
<td>Probability:</td>
<td>0.25</td>
<td>0.50</td>
<td>0.25</td>
</tr>
</tbody>
</table>
The expected value of a function of a random variable is the average, weighted by the probability distribution over outcomes.

Example: How long to get to the airport?

Time: 20 min 30 min 60 min
Probability: 0.25 0.50 0.25
Reminder: Expectations

- The expected value of a function of a random variable is the average, weighted by the probability distribution over outcomes.

- Example: How long to get to the airport?

<table>
<thead>
<tr>
<th>Time</th>
<th>Probability</th>
<th>Calculation</th>
</tr>
</thead>
<tbody>
<tr>
<td>20 min</td>
<td>0.25</td>
<td>20 min x 0.25</td>
</tr>
<tr>
<td>30 min</td>
<td>0.50</td>
<td>30 min x 0.50</td>
</tr>
<tr>
<td>60 min</td>
<td>0.25</td>
<td>60 min x 0.25</td>
</tr>
</tbody>
</table>

  \[\text{Expected Time} = (20 \text{ min} \times 0.25) + (30 \text{ min} \times 0.50) + (60 \text{ min} \times 0.25) = 35 \text{ min}\]
In expectimax search, we have a probabilistic model of how the opponent (or environment) will behave in any state.

- Model could be a simple uniform distribution (roll a die)
- Model could be sophisticated and require a great deal of computation
- We have a chance node for any outcome out of our control: opponent or environment
- The model might say that adversarial actions are likely!

For now, assume each chance node magically comes along with probabilities that specify the distribution over its outcomes.

Having a probabilistic belief about another agent’s action does not mean that the agent is flipping any coins!
In expectimax search, we have a probabilistic model of how the opponent (or environment) will behave in any state:

- Model could be a simple uniform distribution (roll a die)
- Model could be sophisticated and require a great deal of computation
- We have a chance node for any outcome out of our control: opponent or environment
- The model might say that adversarial actions are likely!

For now, assume each chance node magically comes along with probabilities that specify the distribution over its outcomes.

Having a probabilistic belief about another agent’s action does not mean that the agent is flipping any coins!
In expectimax search, we have a probabilistic model of how the opponent (or environment) will behave in any state
- Model could be a simple uniform distribution (roll a die)
- Model could be sophisticated and require a great deal of computation
- We have a chance node for any outcome out of our control: opponent or environment
- The model might say that adversarial actions are likely!

For now, assume each chance node magically comes along with probabilities that specify the distribution over its outcomes

Having a probabilistic belief about another agent’s action does not mean that the agent is flipping any coins!
Quiz: Informed Probabilities

- Let’s say you know that your opponent is actually running a depth 2 minimax, using the result 80% of the time, and moving randomly otherwise.
- Question: What tree search should you use?
Let’s say you know that your opponent is actually running a depth 2 minimax, using the result 80% of the time, and moving randomly otherwise.

Question: What tree search should you use?

Answer: Expectimax!
Let’s say you know that your opponent is actually running a depth 2 minimax, using the result 80% of the time, and moving randomly otherwise.

Question: What tree search should you use?

Answer: Expectimax!
Let’s say you know that your opponent is actually running a depth 2 minimax, using the result 80% of the time, and moving randomly otherwise.

Question: What tree search should you use?

Answer: Expectimax!

To figure out EACH chance node’s probabilities, you have to run a simulation of your opponent.
Quiz: Informed Probabilities

- Let’s say you know that your opponent is actually running a depth 2 minimax, using the result 80% of the time, and moving randomly otherwise.
- Question: What tree search should you use?

- Answer: Expectimax!
  - To figure out EACH chance node’s probabilities, you have to run a simulation of your opponent.
Quiz: Informed Probabilities

- Let’s say you know that your opponent is actually running a depth 2 minimax, using the result 80% of the time, and moving randomly otherwise.
- Question: What tree search should you use?

- Answer: Expectimax!
  - To figure out EACH chance node’s probabilities, you have to run a simulation of your opponent.
Let’s say you know that your opponent is actually running a depth 2 minimax, using the result 80% of the time, and moving randomly otherwise.

Question: What tree search should you use?

Answer: Expectimax!

To figure out EACH chance node’s probabilities, you have to run a simulation of your opponent.
Quiz: Informed Probabilities

- Let’s say you know that your opponent is actually running a depth 2 minimax, using the result 80% of the time, and moving randomly otherwise.
- Question: What tree search should you use?

  ![Diagram of a probability tree with 80% chance of one path and 20% chance of another path]

- Answer: Expectimax!
  - To figure out EACH chance node’s probabilities, you have to run a simulation of your opponent.
  - This kind of thing gets very slow very quickly.
  - Even worse if you have to simulate your opponent simulating you…
  - …except for minimax, which has the nice property that it all collapses into one game tree.
Modeling Assumptions
The Dangers of Optimism and Pessimism
The Dangers of Optimism and Pessimism

Dangerous Optimism
Assuming chance when the world is adversarial
The Dangers of Optimism and Pessimism

Dangerous Optimism
Assuming chance when the world is adversarial
The Dangers of Optimism and Pessimism

Dangerous Optimism
Assuming chance when the world is adversarial

Dangerous Pessimism
Assuming the worst case when it’s not likely
The Dangers of Optimism and Pessimism

Dangerous Optimism
Assuming chance when the world is adversarial

Dangerous Pessimism
Assuming the worst case when it’s not likely
### Assumptions vs. Reality

<table>
<thead>
<tr>
<th></th>
<th>Adversarial Ghost</th>
<th>Random Ghost</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Minimax</strong></td>
<td>Won 5/5</td>
<td>Won 5/5</td>
</tr>
<tr>
<td>Pacman</td>
<td>Avg. Score: 483</td>
<td>Avg. Score: 493</td>
</tr>
<tr>
<td><strong>Expectimax</strong></td>
<td>Won 1/5</td>
<td>Won 5/5</td>
</tr>
</tbody>
</table>

Results from playing 5 games

Pacman used depth 4 search with an eval function that avoids trouble
Ghost used depth 2 search with an eval function that seeks Pacman
Video of Demo World Assumptions
Random Ghost - Expectimax Pacman
Video of Demo World Assumptions
Random Ghost - Expectimax Pacman
Video of Demo World Assumptions
Random Ghost - Expectimax Pacman
Video of Demo World Assumptions
Adversarial Ghost - Minimax Pacman
Video of Demo World Assumptions
Adversarial Ghost - Minimax Pacman
Video of Demo World Assumptions
Adversarial Ghost - Minimax Pacman
Video of Demo World Assumptions
Adversarial Ghost - Expectimax Pacman

Assumptions vs. Reality

<table>
<thead>
<tr>
<th></th>
<th>Adversarial Ghost</th>
<th>Random Ghost</th>
</tr>
</thead>
<tbody>
<tr>
<td>Minimax Pacman</td>
<td>Won 5/5</td>
<td>Won 5/5</td>
</tr>
<tr>
<td></td>
<td>Avg. Score: 483</td>
<td>Avg. Score: 493</td>
</tr>
<tr>
<td>Expectimax Pacman</td>
<td><strong>Won 1/5</strong></td>
<td>Won 5/5</td>
</tr>
<tr>
<td></td>
<td><strong>Avg. Score: -303</strong></td>
<td>Avg. Score: 503</td>
</tr>
</tbody>
</table>

Results from playing 5 games

Pacman used depth 4 search with an eval function that avoids trouble
Ghost used depth 2 search with an eval function that seeks Pacman
Video of Demo World Assumptions
Adversarial Ghost - Expectimax Pacman

Assumptions vs. Reality

<table>
<thead>
<tr>
<th></th>
<th>Adversarial Ghost</th>
<th>Random Ghost</th>
</tr>
</thead>
<tbody>
<tr>
<td>Minimax Pacman</td>
<td>Won 5/5</td>
<td>Won 5/5</td>
</tr>
<tr>
<td></td>
<td>Avg. Score: 483</td>
<td>Avg. Score: 493</td>
</tr>
<tr>
<td>Expectimax Pacman</td>
<td>Won 1/5</td>
<td>Won 5/5</td>
</tr>
<tr>
<td></td>
<td>Avg. Score: -303</td>
<td>Avg. Score: 503</td>
</tr>
</tbody>
</table>

Results from playing 5 games

Pacman used depth 4 search with an eval function that avoids trouble
Ghost used depth 2 search with an eval function that seeks Pacman
Video of Demo World Assumptions
Adversarial Ghost - Expectimax Pacman

Assumptions vs. Reality

Pacman used depth 4 search with an eval function that avoids trouble
Ghost used depth 2 search with an eval function that seeks Pacman
Video of Demo World Assumptions
Random Ghost – Minimax Pacman
Video of Demo World Assumptions
Random Ghost - Minimax Pacman
Video of Demo World Assumptions
Random Ghost - Minimax Pacman
Other Game Types
Mixed Layer Types

- E.g. Backgammon
- Expectiminimax
  - Environment is an extra “random agent” player that moves after each min/max agent
  - Each node computes the appropriate combination of its children
Example: Backgammon

- Dice rolls increase $b$: 21 possible rolls with 2 dice
  - Backgammon $\approx$ 20 legal moves
  - Depth 2 = $20 \times (21 \times 20)^3 = 1.2 \times 10^9$

- As depth increases, probability of reaching a given search node shrinks
  - So usefulness of search is diminished
  - So limiting depth is less damaging
  - But pruning is trickier...

- Historic AI: TDGammon uses depth-2 search + very good evaluation function + reinforcement learning: world-champion level play

- 1st AI world champion in any game!
What if the game is not zero-sum, or has multiple players?

Generalization of minimax:
- Terminals have utility tuples
- Node values are also utility tuples
- Each player maximizes its own component
- Can give rise to cooperation and competition dynamically...
Multi-Agent Utilities

- What if the game is not zero-sum, or has multiple players?

- Generalization of minimax:
  - Terminals have utility tuples
  - Node values are also utility tuples
  - Each player maximizes its own component
  - Can give rise to cooperation and competition dynamically...

1, 6, 6  7, 1, 2  6, 1, 2  7, 2, 1  5, 1, 7  1, 5, 2  7, 7, 1  5, 2, 5
Multi-Agent Utilities

- What if the game is not zero-sum, or has multiple players?

- Generalization of minimax:
  - Terminals have utility tuples
  - Node values are also utility tuples
  - Each player maximizes its own component
  - Can give rise to cooperation and competition dynamically...
Utilities
Maximum Expected Utility

- Why should we average utilities? Why not minimax?
Maximum Expected Utility

- Why should we average utilities? Why not minimax?
Why should we average utilities? Why not minimax?
Maximum Expected Utility

- Why should we average utilities? Why not minimax?

- Principle of maximum expected utility:
  - A rational agent should chose the action that maximizes its expected utility, given its knowledge
Maximum Expected Utility

- Why should we average utilities? Why not minimax?

- Principle of maximum expected utility:
  - A rational agent should choose the action that maximizes its expected utility, given its knowledge

- Questions:
  - Where do utilities come from?
  - How do we know such utilities even exist?
  - How do we know that averaging even makes sense?
  - What if our behavior (preferences) can’t be described by utilities?
What Utilities to Use?
What Utilities to Use?

- For worst-case minimax reasoning, terminal function scale doesn’t matter
  - We just want better states to have higher evaluations (get the ordering right)
  - We call this insensitivity to monotonic transformations

- For average-case expectimax reasoning, we need magnitudes to be meaningful
What Utilities to Use?

- For worst-case minimax reasoning, terminal function scale doesn’t matter
  - We just want better states to have higher evaluations (get the ordering right)
  - We call this insensitivity to monotonic transformations

- For average-case expectimax reasoning, we need magnitudes to be meaningful
Utilities are functions from outcomes (states of the world) to real numbers that describe an agent’s preferences.

Where do utilities come from?
- In a game, may be simple (+1/-1)
- Utilities summarize the agent’s goals
- Theorem: any “rational” preferences can be summarized as a utility function

We hard-wire utilities and let behaviors emerge
- Why don’t we let agents pick utilities?
- Why don’t we prescribe behaviors?
Utilities: Uncertain Outcomes

Getting ice cream

Get Single

Get Double
Utilities: Uncertain Outcomes

Getting ice cream

Get Single

Get Double
Utilities: Uncertain Outcomes

Getting ice cream

- Get Single
- Get Double

Oops
Utilities: Uncertain Outcomes

Getting ice cream

Get Single

Get Double

Oops

Whew!
Preferences

- An agent must have preferences among:
  - Prizes: $A$, $B$, etc.
  - Lotteries: situations with uncertain prizes
    \[ L = [p, A; (1 - p), B] \]

- Notation:
  - Preference: $A \succ B$
  - Indifference: $A \sim B$
Preferences

- An agent must have preferences among:
  - Prizes: \( A, B, \) etc.
  - Lotteries: situations with uncertain prizes
    \[ L = [p, A; (1-p), B] \]

- Notation:
  - Preference: \( A \succ B \)
  - Indifference: \( A \sim B \)
Preferences

- An agent must have preferences among:
  - Prizes: \( A, B, \) etc.
  - Lotteries: situations with uncertain prizes
    \[ L = [p, A; (1 - p), B] \]

- Notation:
  - Preference: \( A \succ B \)
  - Indifference: \( A \sim B \)
Rationality
Rational Preferences

The Axioms of Rationality

**Orderability**

\[(A \succ B) \lor (B \succ A) \lor (A \sim B)\]

**Transitivity**

\[(A \succ B) \land (B \succ C) \Rightarrow (A \succ C)\]

**Continuity**

\[A \succ B \succ C \Rightarrow \exists p \ [p, A; \ 1 - p, C] \sim B\]

**Substitutability**

\[A \sim B \Rightarrow [p, A; \ 1 - p, C] \sim [p, B; \ 1 - p, C]\]

**Monotonicity**

\[A \succ B \Rightarrow (p \geq q \Leftrightarrow [p, A; \ 1 - p, B] \succeq [q, A; \ 1 - q, B])\]
Rational Preferences

The Axioms of Rationality

- **Orderability**
  \[(A \succ B) \lor (B \succ A) \lor (A \sim B)\]

- **Transitivity**
  \[(A \succ B) \land (B \succ C) \Rightarrow (A \succ C)\]

- **Continuity**
  \[A \succ B \succ C \Rightarrow \exists p \ [p, A; 1 - p, C] \sim B\]

- **Substitutability**
  \[A \sim B \Rightarrow [p, A; 1 - p, C] \sim [p, B; 1 - p, C]\]

- **Monotonicity**
  \[A \succ B \Rightarrow (p \geq q \iff [p, A; 1 - p, B] \succeq [q, A; 1 - q, B])\]

Theorem: Rational preferences imply behavior describable as maximization of expected utility.
Rational Preferences

The Axioms of Rationality

- **Orderability**
  \[(A \succ B) \lor (B \succ A) \lor (A \sim B)\]

- **Transitivity**
  \[(A \succ B) \land (B \succ C) \Rightarrow (A \succ C)\]

- **Continuity**
  \[A \succ B \succ C \Rightarrow \exists p \ [p, A; 1 - p, C] \sim B\]

- **Substitutability**
  \[A \sim B \Rightarrow [p, A; 1 - p, C] \sim [p, B; 1 - p, C]\]

- **Monotonicity**
  \[A \succ B \Rightarrow (p \geq q \Leftrightarrow [p, A; 1 - p, B] \succeq [q, A; 1 - q, B])\]

---

Theorem: Rational preferences imply behavior describable as maximization of expected utility.
Theorem [Ramsey, 1931; von Neumann & Morgenstern, 1944]
- Given any preferences satisfying these constraints, there exists a real-valued function $U$ such that:

\[
U(A) \geq U(B) \iff A \succeq B
\]

\[
U([p_1, S_1; \ldots; p_n, S_n]) = \sum_i p_i U(S_i)
\]

- I.e. values assigned by $U$ preserve preferences of both prizes and lotteries!
Theorem [Ramsey, 1931; von Neumann & Morgenstern, 1944]
- Given any preferences satisfying these constraints, there exists a real-valued function $U$ such that:

$$U(A) \geq U(B) \iff A \succeq B$$

$$U([p_1, S_1; \ldots ; p_n, S_n]) = \sum_i p_i U(S_i)$$

- I.e. values assigned by $U$ preserve preferences of both prizes and lotteries!

Maximum expected utility (MEU) principle:
- Choose the action that maximizes expected utility
- Note: an agent can be entirely rational (consistent with MEU) without ever representing or manipulating utilities and probabilities
- E.g., a lookup table for perfect tic-tac-toe, a reflex vacuum cleaner
Utility Scales

- Normalized utilities: $u_+ = 1.0$, $u_- = 0.0$
Utility Scales

- Normalized utilities: $u_+ = 1.0, u_- = 0.0$

- Micromorts: one-millionth chance of death, useful for paying to reduce product risks, etc.
Utility Scales

- **Normalized utilities**: $u_+ = 1.0$, $u_- = 0.0$

- **Micromorts**: one-millionth chance of death, useful for paying to reduce product risks, etc.

- **QALYs**: quality-adjusted life years, useful for medical decisions involving substantial risk
Utility Scales

- Normalized utilities: $u_+ = 1.0$, $u_- = 0.0$

- Micromorts: one-millionth chance of death, useful for paying to reduce product risks, etc.

- QALYs: quality-adjusted life years, useful for medical decisions involving substantial risk

- Note: behavior is invariant under positive linear transformation

$$U'(x) = k_1 U(x) + k_2 \quad \text{where } k_1 > 0$$
Utility Scales

- **Normalized utilities**: $u_+ = 1.0, u_- = 0.0$
- **Micromorts**: one-millionth chance of death, useful for paying to reduce product risks, etc.
- **QALYs**: quality-adjusted life years, useful for medical decisions involving substantial risk
- **Note**: behavior is invariant under positive linear transformation

\[ U'(x) = k_1 U(x) + k_2 \quad \text{where } k_1 > 0 \]

- With deterministic prizes only (no lottery choices), only ordinal utility can be determined, i.e., total order on prizes
Utilities map states to real numbers. Which numbers?
Utilities map states to real numbers. Which numbers?
Standard approach to assessment (elicitation) of human utilities:
Utilities map states to real numbers. Which numbers?

Standard approach to assessment (elicitation) of human utilities:
Human Utilities

- Utilities map states to real numbers. Which numbers?
- Standard approach to assessment (elicitation) of human utilities:
  - Compare a prize $A$ to a standard lottery $L_p$ between
    - “best possible prize” $u_+$ with probability $p$
    - “worst possible catastrophe” $u_-$ with probability $1-p$
Utilities map states to real numbers. Which numbers?

Standard approach to assessment (elicitation) of human utilities:
- Compare a prize A to a standard lottery $L_p$ between
  - “best possible prize” $u_+$ with probability $p$
  - “worst possible catastrophe” $u_-$ with probability $1 - p$

Pay $30
Utilities map states to real numbers. Which numbers?

Standard approach to assessment (elicitation) of human utilities:
- Compare a prize A to a standard lottery $L_p$ between
  - “best possible prize” $u_+$ with probability $p$
  - “worst possible catastrophe” $u_-$ with probability $1-p$

Pay $30
Human Utilities

- Utilities map states to real numbers. Which numbers?
- Standard approach to assessment (elicitation) of human utilities:
  - Compare a prize A to a standard lottery $L_p$ between
    - “best possible prize” $u_+$ with probability $p$
    - “worst possible catastrophe” $u_-$ with probability $1-p$
Utilities map states to real numbers. Which numbers?

Standard approach to assessment (elicitation) of human utilities:
- Compare a prize A to a standard lottery $L_p$ between
  - “best possible prize” $u_+$ with probability $p$
  - “worst possible catastrophe” $u_-$ with probability $1-p$

Pay $30 \sim \begin{cases} \text{No change} \\ \text{Instant death} \end{cases}$
Utilities map states to real numbers. Which numbers?

Standard approach to assessment (elicitation) of human utilities:
- Compare a prize A to a standard lottery $L_p$ between
  - “best possible prize” $u_+$ with probability $p$
  - “worst possible catastrophe” $u_-$ with probability $1-p$
- Adjust lottery probability $p$ until indifference: $A \sim L_p$
- Resulting $p$ is a utility in $[0,1]$

Pay $30

No change

Instant death
Utilities map states to real numbers. Which numbers?

Standard approach to assessment (elicitation) of human utilities:

- Compare a prize $A$ to a standard lottery $L_p$ between
  - “best possible prize” $u_+$ with probability $p$
  - “worst possible catastrophe” $u_-$ with probability $1-p$
- Adjust lottery probability $p$ until indifference: $A \sim L_p$
- Resulting $p$ is a utility in $[0,1]$

Human Utilities

<table>
<thead>
<tr>
<th>Pay $30</th>
<th>0.999999</th>
<th>0.000001</th>
</tr>
</thead>
<tbody>
<tr>
<td>No change</td>
<td>Instant death</td>
<td></td>
</tr>
</tbody>
</table>
Money does not behave as a utility function, but we can talk about the utility of having money (or being in debt)

Given a lottery $L = [p, X; (1-p), Y]$
Money

- Money does not behave as a utility function, but we can talk about the utility of having money (or being in debt).
- Given a lottery $L = [p, $X; (1-p), $Y]$
  - The expected monetary value $EMV(L)$ is $pX + (1-p)Y$
  - $U(L) = pU(X) + (1-p)U(Y)$
  - Typically, $U(L) < U(EMV(L))$
Money

- Money does not behave as a utility function, but we can talk about the utility of having money (or being in debt).
- Given a lottery $L = \{p, \$X; (1-p), \$Y\}$
  - The expected monetary value $EMV(L)$ is $pX + (1-p)Y$
  - $U(L) = pU(\$X) + (1-p)U(\$Y)$
  - Typically, $U(L) < U(EMV(L))$
  - In this sense, people are risk-averse
  - When deep in debt, people are risk-prone
Money does not behave as a utility function, but we can talk about the utility of having money (or being in debt).

Given a lottery \( L = [p, X; (1-p), Y] \)

- The expected monetary value \( EMV(L) \) is \( pX + (1-p)Y \)
- \( U(L) = pU(X) + (1-p)U(Y) \)
- Typically, \( U(L) < U(EMV(L)) \)
- In this sense, people are risk-averse
- When deep in debt, people are risk-prone
Example: Insurance

- Consider the lottery [0.5, $1000; 0.5, $0]
Example: Insurance

- Consider the lottery \([0.5, \$1000; 0.5, \$0]\)
  - What is its expected monetary value? ($500)
Example: Insurance

- Consider the lottery [0.5, $1000; 0.5, $0]
  - What is its expected monetary value? ($500)
  - What is its certainty equivalent?
Example: Insurance

- Consider the lottery [0.5, $1000; 0.5, $0]
  - What is its expected monetary value? ($500)
  - What is its certainty equivalent?
    - Monetary value acceptable in lieu of lottery
Example: Insurance

- Consider the lottery [0.5, $1000; 0.5, $0]
  - What is its expected monetary value? ($500)
  - What is its certainty equivalent?
    - Monetary value acceptable in lieu of lottery
    - $400 for most people
Example: Insurance

- Consider the lottery [0.5, $1000; 0.5, $0]
  - What is its expected monetary value? ($500)
  - What is its certainty equivalent?
    - Monetary value acceptable in lieu of lottery
    - $400 for most people
  - Difference of $100 is the insurance premium
    - There’s an insurance industry because people will pay to reduce their risk
    - If everyone were risk-neutral, no insurance needed!
Example: Insurance

- Consider the lottery \([0.5, \$1000; 0.5, \$0]\)
  - What is its expected monetary value? \(\$500\)
  - What is its certainty equivalent?
    - Monetary value acceptable in lieu of lottery
    - \$400 for most people
  - Difference of \$100 is the insurance premium
    - There’s an insurance industry because people will pay to reduce their risk
    - If everyone were risk-neutral, no insurance needed!
  - It’s win-win: you’d rather have the \$400 and the insurance company would rather have the lottery (their utility curve is flat and they have many lotteries)
Example: Human Rationality?

- Famous example of Allais (1953)
Example: Human Rationality?

- Famous example of Allais (1953)
  - A: [0.8, $4k; 0.2, $0]
  - B: [1.0, $3k; 0.0, $0]
Example: Human Rationality?

- Famous example of Allais (1953)
  - A: [0.8, $4k; 0.2, $0]
  - B: [1.0, $3k; 0.0, $0]
  - C: [0.2, $4k; 0.8, $0]
  - D: [0.25, $3k; 0.75, $0]
Example: Human Rationality?

- Famous example of Allais (1953)
  - A: [0.8, $4k; 0.2, $0]
  - B: [1.0, $3k; 0.0, $0]
  - C: [0.2, $4k; 0.8, $0]
  - D: [0.25, $3k; 0.75, $0]

- Most people prefer B > A, C > D
Example: Human Rationality?

- Famous example of Allais (1953)
  - A: [0.8, $4k; 0.2, $0]
  - B: [1.0, $3k; 0.0, $0]
  - C: [0.2, $4k; 0.8, $0]
  - D: [0.25, $3k; 0.75, $0]

- Most people prefer B > A, C > D

- But if U($0) = 0, then
  - B > A ⇒ U($3k) > 0.8 U($4k)
Example: Human Rationality?

- **Famous example of Allais (1953)**
  - A: [0.8, $4k; 0.2, $0]
  - B: [1.0, $3k; 0.0, $0]
  - C: [0.2, $4k; 0.8, $0]
  - D: [0.25, $3k; 0.75, $0]

- **Most people prefer B > A, C > D**

- **But if** $U(0) = 0$, then
  - $B > A \Rightarrow U($3k$) > 0.8 U($4k$)
  - $C > D \Rightarrow 0.8 U($4k$) > U($3k$)
Example: Human Rationality?

- Famous example of Allais (1953)
  - A: [0.8, $4k; 0.2, $0]
  - B: [1.0, $3k; 0.0, $0]
  - C: [0.2, $4k; 0.8, $0]
  - D: [0.25, $3k; 0.75, $0]

- Most people prefer B > A, C > D

- But if $U(0) = 0$, then
  - B > A $\Rightarrow U($3k$) > 0.8 U($4k$)
  - C > D $\Rightarrow 0.8 U($4k$) > U($3k$)
Example: Human Rationality?

- Famous example of Allais (1953)
  - A: [0.8, $4k; 0.2, $0]
  - B: [1.0, $3k; 0.0, $0]
  - C: [0.2, $4k; 0.8, $0]
  - D: [0.25, $3k; 0.75, $0]

- Most people prefer B > A, C > D

- But if $U(0) = 0$, then
  - B > A \implies U($3k) > 0.8 U($4k)
  - C > D \implies 0.8 U($4k) > U($3k)$
Next Time: MDPs!