CS 2740 Knowledge representation
Lecture 23

Decision making in the presence of uncertainty II

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Information-gathering actions

- **Many actions and their outcomes irreversibly change the world**
- **Information-gathering (exploratory) actions:**
  - **make an inquiry about the world**
  - **Key benefit:** reduction in the uncertainty
- **Example: medicine**
  - Assume a patient is admitted to the hospital with some set of initial complaints
  - We are uncertain about the underlying problem and consider a surgery, or a medication to treat them
  - But there are often lab tests or observations that can help us to determine more closely the disease the patient suffers from
  - **Goal of lab tests:** Reduce the uncertainty of outcomes of treatments so that better treatment option can be chosen

Decision-making with exploratory actions

In decision trees:

- **Exploratory actions can be represented and reasoned about the same way as other actions.**

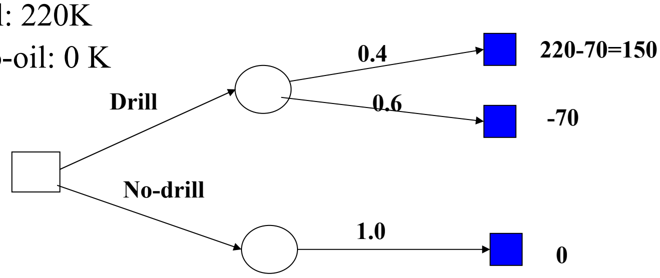
How do we capture the effect of exploratory actions in the decision tree model?

- Information obtained through exploratory actions may affect the probabilities of later outcomes
  - Recall that the probabilities on later outcomes can be conditioned on past observed outcomes and past actions
  - Sequence of past actions and outcomes is "remembered" within the decision tree branch

Oil wildcatter problem.

An oil wildcatter has to make a decision of whether to drill or not to drill on a specific site

- **Chance of hitting an oil deposit:**
  - Oil: 40% $P(Oil = T) = 0.4$
  - No-oil: 60% $P(Oil = F) = 0.6$
- **Cost of drilling:** 70K
- **Payoffs:**
  - Oil: 220K
  - No-oil: 0 K



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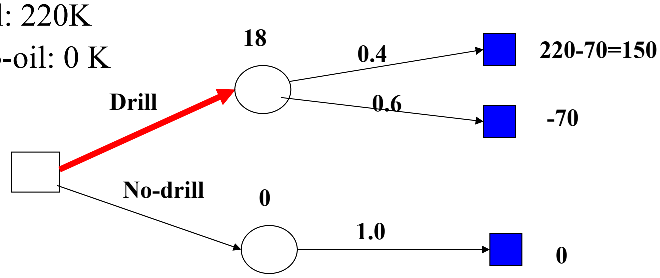


Oil wildcatter problem

- Assume that in addition to the drill/no-drill choices we have an option to run the **seismic resonance test**
- **Seismic resonance test results:**
  - **Closed pattern** (more likely when the hole holds the oil)
  - **Diffuse pattern** (more likely when empty)

  $\mathbf{P}(Oil \mid Seismic\ resonance\ test)$

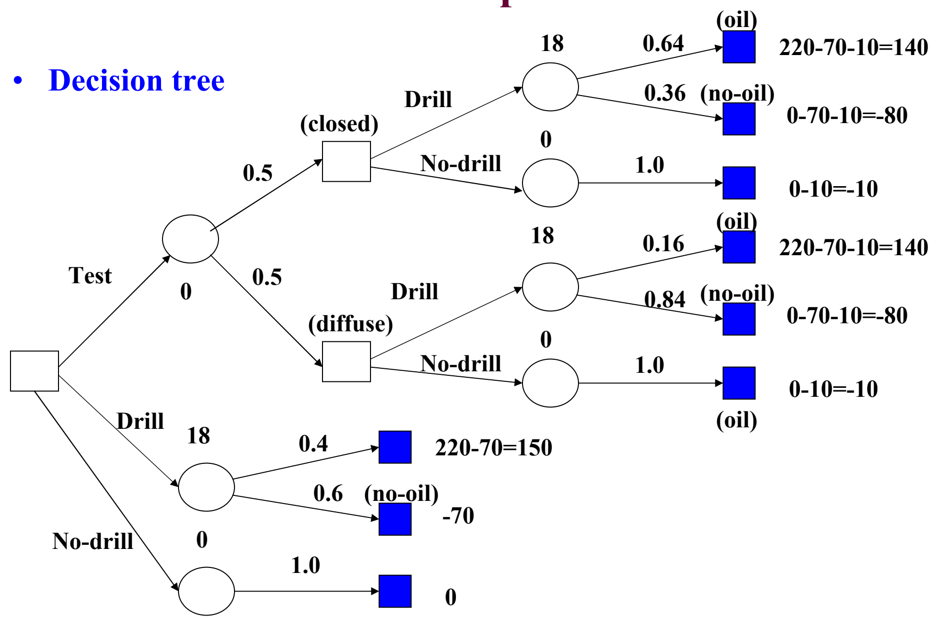
Seismic resonance test pattern

Oil		*closed*	*diffuse*
	True	0.8	0.2
	False	0.3	0.7

- **Test cost:** 10K

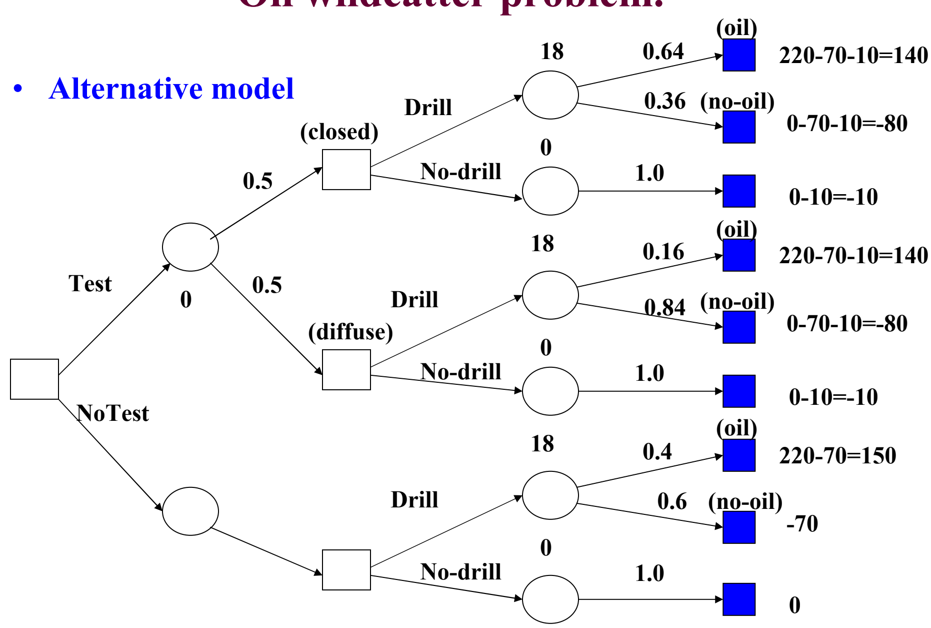
Oil wildcatter problem.

- **Decision tree**



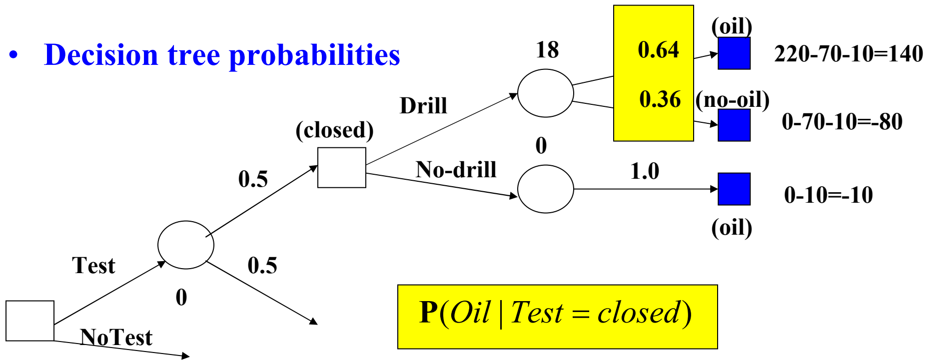
Oil wildcatter problem.

- **Alternative model**



Oil wildcatter problem.

- **Decision tree probabilities**



$$\mathbf{P}(Oil \mid Test = closed)$$

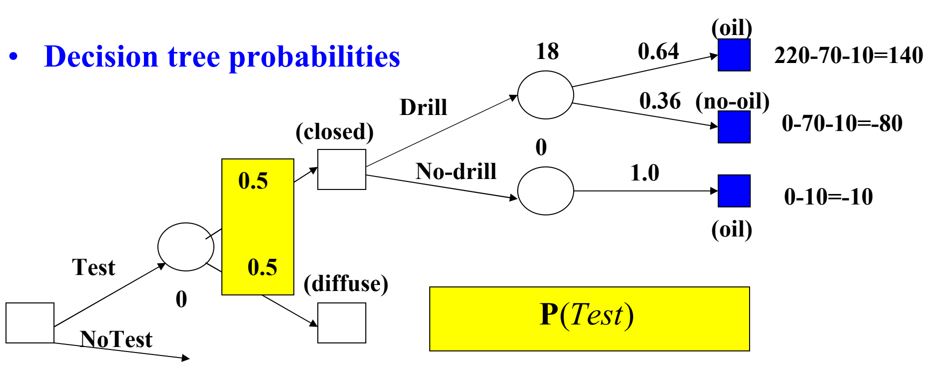
$$P(Oil = T \mid Test = closed) = \frac{P(Test = closed \mid Oil = T)P(Oil = T)}{P(Test = closed)}$$

$$P(Oil = F \mid Test = closed) = \frac{P(Test = closed \mid Oil = F)P(Oil = F)}{P(T = closed)}$$

$$P(Test = closed) = P(Test = closed \mid Oil = F)P(Oil = F) + P(Test = closed \mid Oil = T)P(Oil = T)$$

Oil wildcatter problem.

- **Decision tree probabilities**



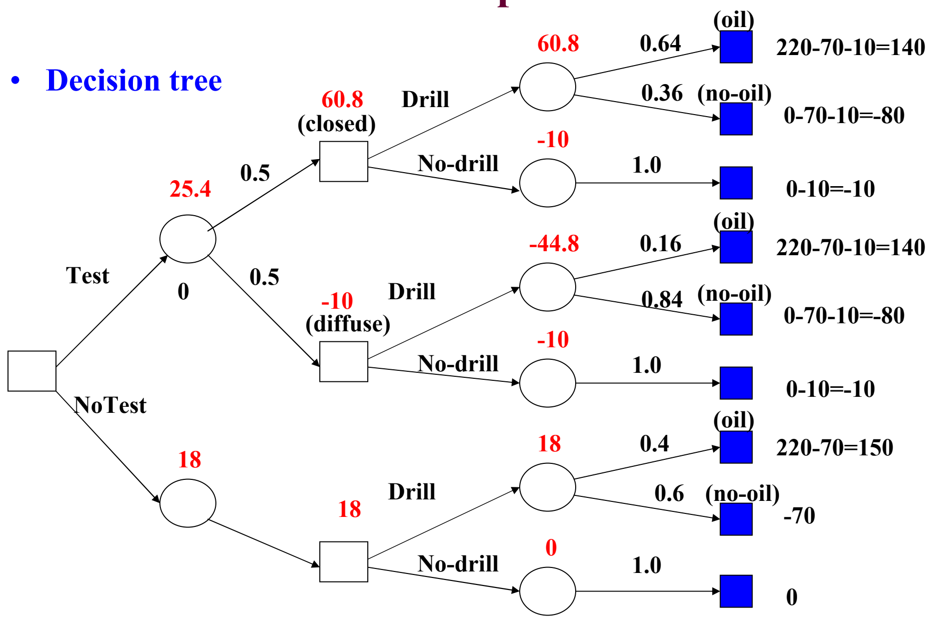
$$\mathbf{P}(Test)$$

$$P(Test = closed) = P(Test = closed \mid Oil = F)P(Oil = F) + P(Test = closed \mid Oil = T)P(Oil = T)$$

$$P(Test = diff) = P(Test = diff \mid Oil = F)P(Oil = F) + P(Test = diff \mid Oil = T)P(Oil = T)$$

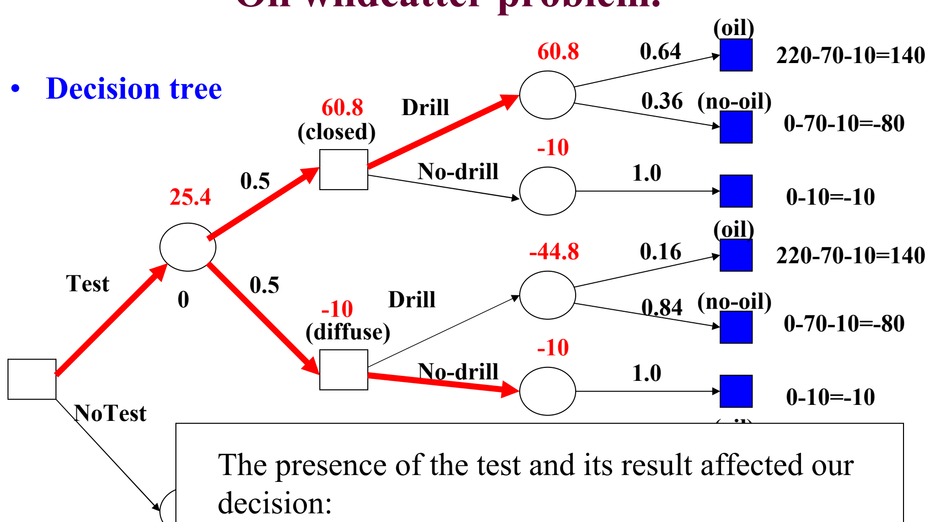
Oil wildcatter problem.

- **Decision tree**



Oil wildcatter problem.

- **Decision tree**



The presence of the test and its result affected our decision:

if test =closed then <u>drill</u>

if test=diffuse then <u>do not drill</u>

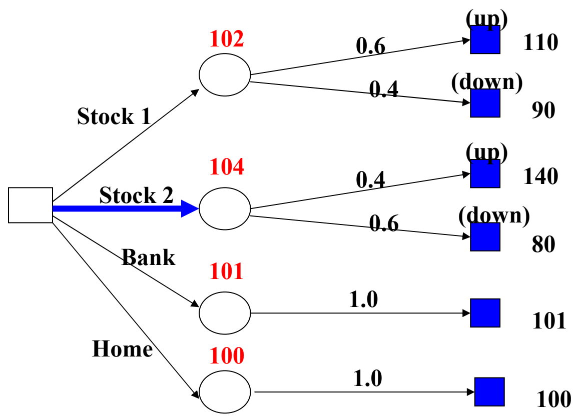
Value of information

- **When the test makes sense?**
- Only when its result makes the decision maker to change his mind, that is he decides not to drill.
- **Value of information:**
  - Measure of the goodness of the information from the test
  - Difference between the expected value with and without the test information
- **Oil wildcatter example:**
  - Expected value without the test = 18
  - Expected value with the test =25.4
  - Value of information for the seismic test = 7.4

Utilities

Selection based on expected values

- **Until now:** The optimal action choice was the option that maximized the expected monetary value.
- **But is the expected monetary value always the quantity we want to optimize?**



Selection based on expected values

- **Is the expected monetary value always the quantity we want to optimize?**
- **Answer:** Yes, but only if we are risk-neutral.

- But what if **we do not like the risk (we are risk-averse)?**
- In that case we may want to get the premium for undertaking the risk (of loosing the money)
- **Example:**
  – we may prefer to get \$101 for sure against \$102 in expectation but with the risk of loosing the money
- **Problem:** How to model decisions and account for the risk?
- **Solution:** use **utility function, and utility theory**

Utility function

- **Utility function (denoted U)**
  - Quantifies how we “value” outcomes, i.e., it reflects our preferences
  - Can be also applied to “value” outcomes other than money and gains (e.g. utility of a patient being healthy, or ill)
- **Decision making:**
  - uses expected utilities (denoted EU)

$$EU(X) = \sum_{x \in \Omega_X} P(X = x) U(X = x)$$

$U(X = x)$ the utility of outcome x

Important !!!

- Under some conditions on preferences **we can always design the utility function that fits our preferences**

Utility theory

- Defines axioms on preferences that involve uncertainty and ways to manipulate them.
- Uncertainty is modeled through **lotteries**
  - **Lottery:**

$$[p : A; (1-p) : C]$$

    - Outcome A with probability p
    - Outcome C with probability (1-p)
- The following six constraints are known as the axioms of utility theory. The axioms are the most obvious semantic constraints on preferences with lotteries.
- **Notation:**

  $\succ$ - preferable

  $\sim$ - indifferent (equally preferable)

Axioms of the utility theory

- **Orderability:** Given any two states, the a rational agent prefers one of them, else the two as equally preferable.

$$(A \succ B) \vee (B \succ A) \vee (A \sim B)$$

- **Transitivity:** Given any three states, if an agent prefers A to B and prefers B to C, agent must prefer A to C.

$$(A \succ B) \wedge (B \succ C) \Rightarrow (A \succ C)$$

- **Continuity:** If some state B is between A and C in preference, then there is a p for which the rational agent will be indifferent between state B and the lottery in which A comes with probability p, C with probability (1-p).

$$(A \succ B \succ C) \Rightarrow \exists p\, [p : A; (1-p) : C] \sim B$$

Axioms of the utility theory

- **Substitutability:** If an agent is indifferent between two lotteries, A and B, then there is a more complex lottery in which A can be substituted with B.

$$(A \sim B) \Rightarrow [p : A; (1-p) : C] \sim [p : B; (1-p) : C]$$

- **Monotonicity:** If an agent prefers A to B, then the agent must prefer the lottery in which A occurs with a higher probability

$$(A \succ B) \Rightarrow (p > q \Leftrightarrow [p : A; (1-p) : B] \succ [q : A; (1-q) : B])$$

- **Decomposability:** Compound lotteries can be reduced to simpler lotteries using the laws of probability.

$$[p : A; (1-p) : [q : B; (1-q) : C]] \Rightarrow$$
$$[p : A; (1-p)q : B; (1-p)(1-q) : C]$$

Utility theory

If the agent obeys the axioms of the utility theory, then

1. there exists a real valued function U such that:

$$U(A) > U(B) \Leftrightarrow A \succ B$$

$$U(A) = U(B) \Leftrightarrow A \sim B$$

2. The utility of the lottery is the expected utility, that is the sum of utilities of outcomes weighted by their probability

$$U[p : A; (1-p) : B] = pU(A) + (1-p)U(B)$$

3. Rational agent makes the decisions in the presence of uncertainty by maximizing its expected utility

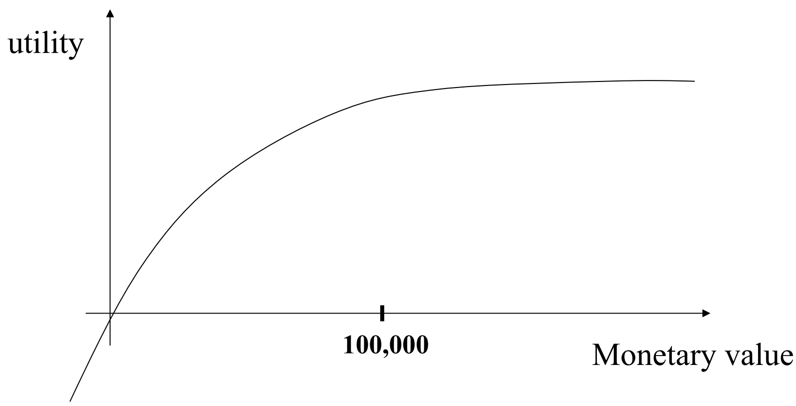
Utility functions

We can design a utility function that fits our preferences if they satisfy the axioms of utility theory.

- **But how to design the utility function for monetary values so that they incorporate the risk?**
- **What is the relation between utility function and monetary values?**
- Assume we loose or gain \$1000.
  - Typically this difference is more significant for lower values (around \$100 -1000) than for higher values (~ \$1,000,000)
- What is the relation between utilities and monetary value for a typical person?

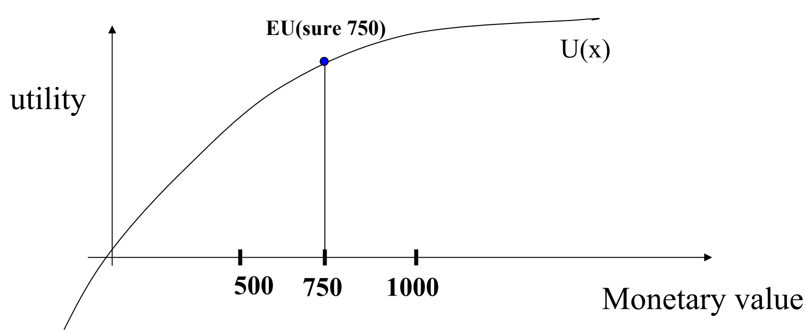
Utility functions

- What is the relation between utilities and monetary value for a typical person?
- Concave function that flattens at higher monetary values



Utility functions

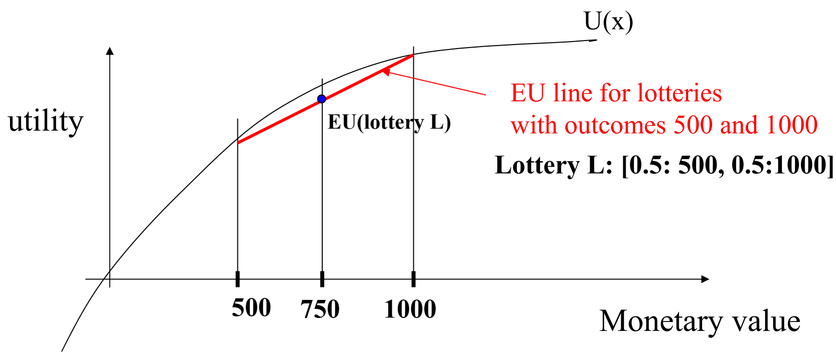
- Expected utility of a sure outcome of 750 is 750



Utility functions

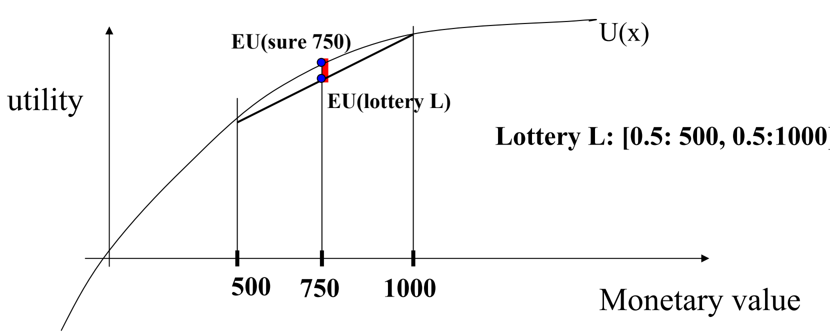
Assume a lottery L [0.5: 500, 0.5:1000]

- Expected value of the lottery = 750
- Expected utility of the lottery EU(L) is different:
  - EU(L) = 0.5U(500) + 0.5*U(1000)



Utility functions

- Expected utility of the lottery EU(lottery L) < EU(sure 750)



- Risk aversion – a bonus is required for undertaking the risk