Game theory 1

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Can rational choice explain suicide terrorism?

Many criticisms against Rational choice

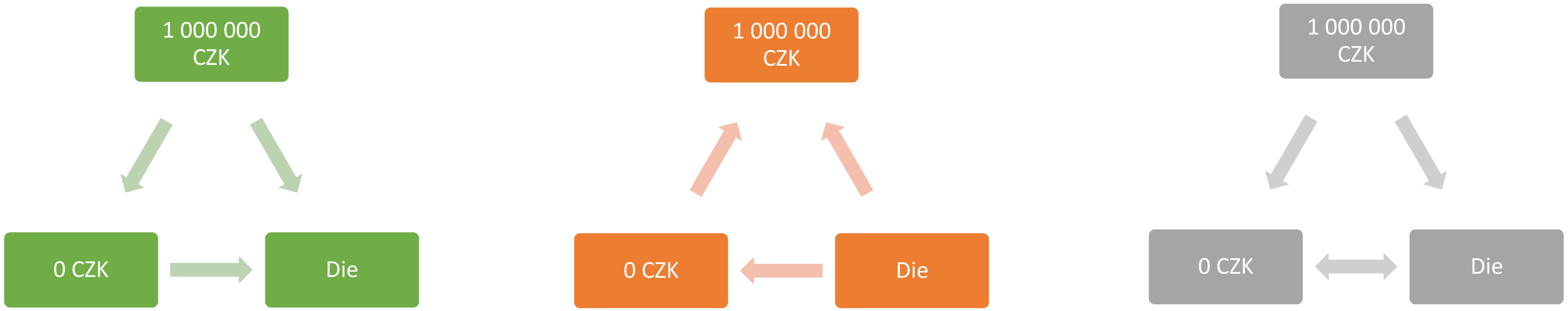
- Common criticism of rational choice – people behave irrationally
- Many times incorrect
- Rationality ≠ Sensibility
- Ordering preferences
- I can mostly prefer taking over the world and least painful death, but equally prefer most painful death and least taking over the world

Rationality

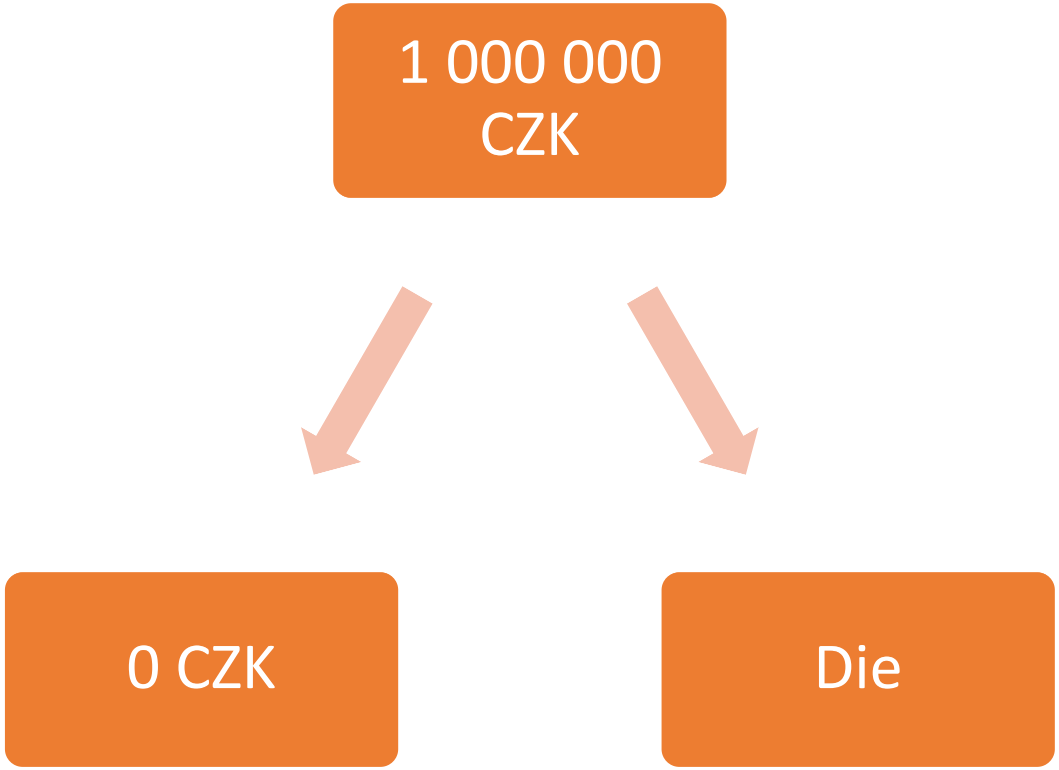
- Defined by two key premises
  - Completeness
  - Transitivity
- Indifferent to normative assessment of preferences and choices

Completeness

- Preference ordering complete if and only if for any two outcomes X and Y individual:
  - A) Prefers X to Y – strong preference relation
  - B) Prefers Y to X – strong preference relation
  - C) Is indifferent – weak preference relation

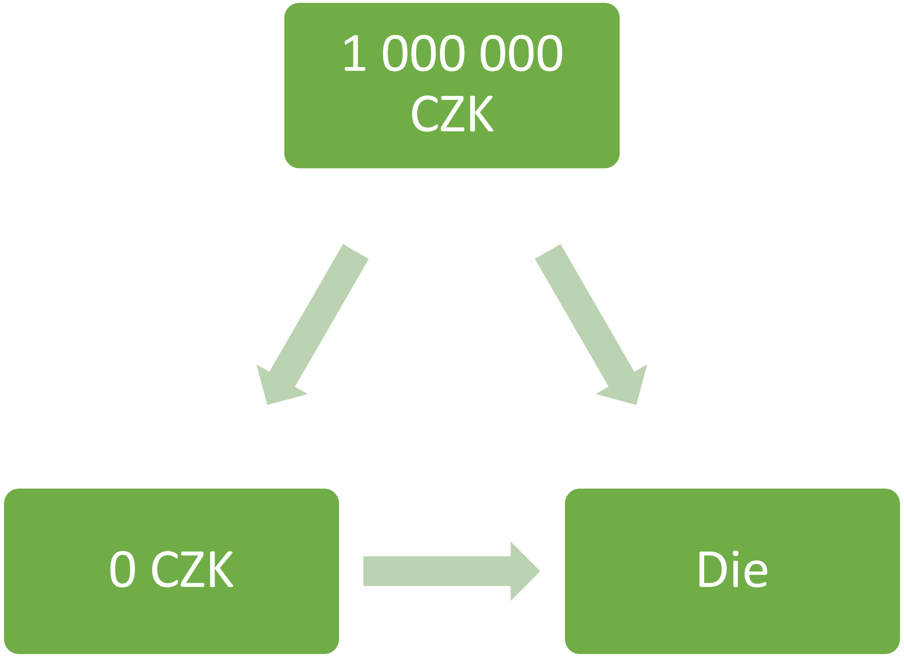


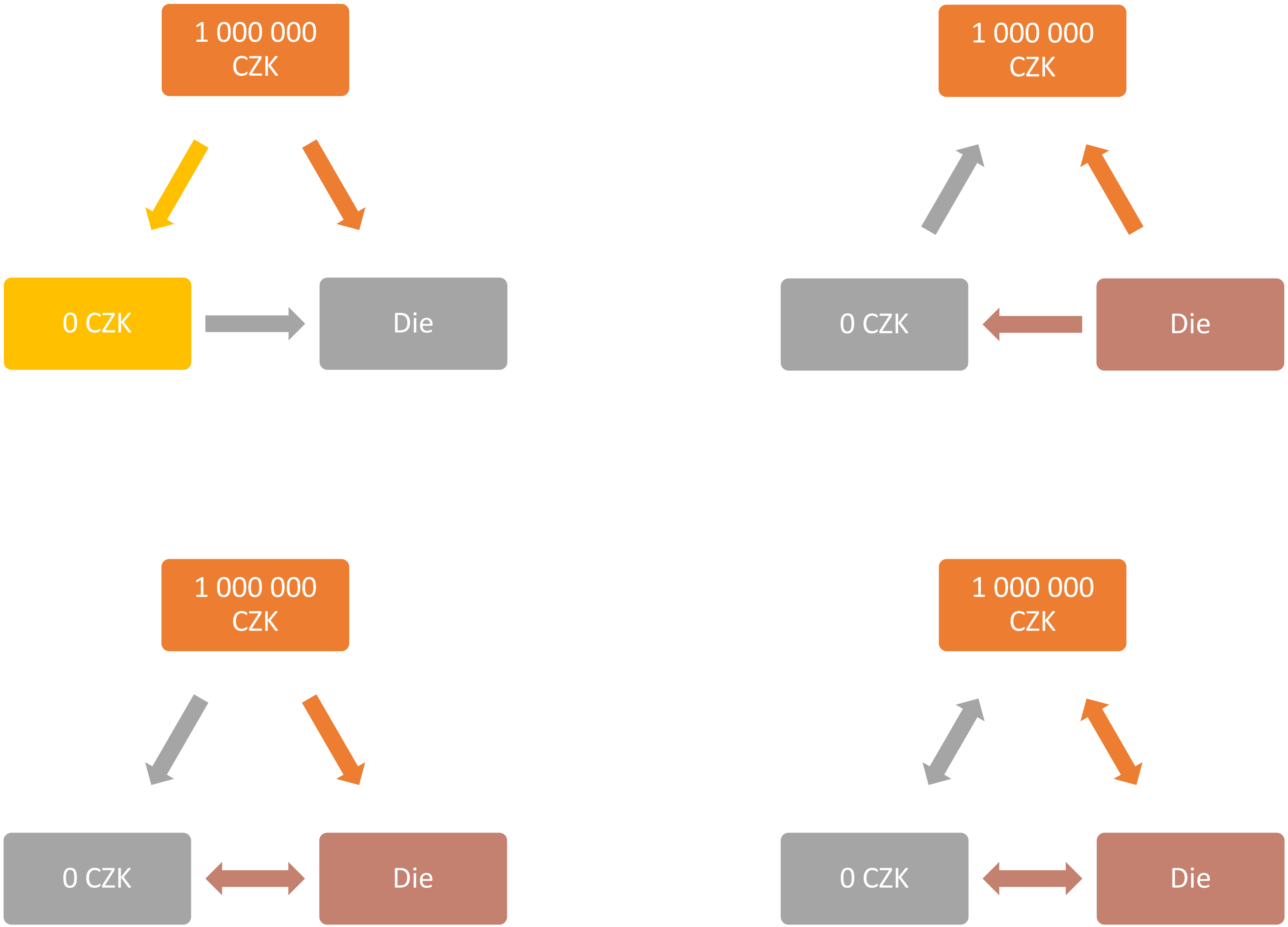
Incomplete preferences



Transitivity

- For any three outcomes X, Y and Z, if X is preferred to Y and Y is preferred to Z, X must be preferred to Z




1 000 000 CZK
0 CZK
Die
1 000 000 CZK
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Die
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Die
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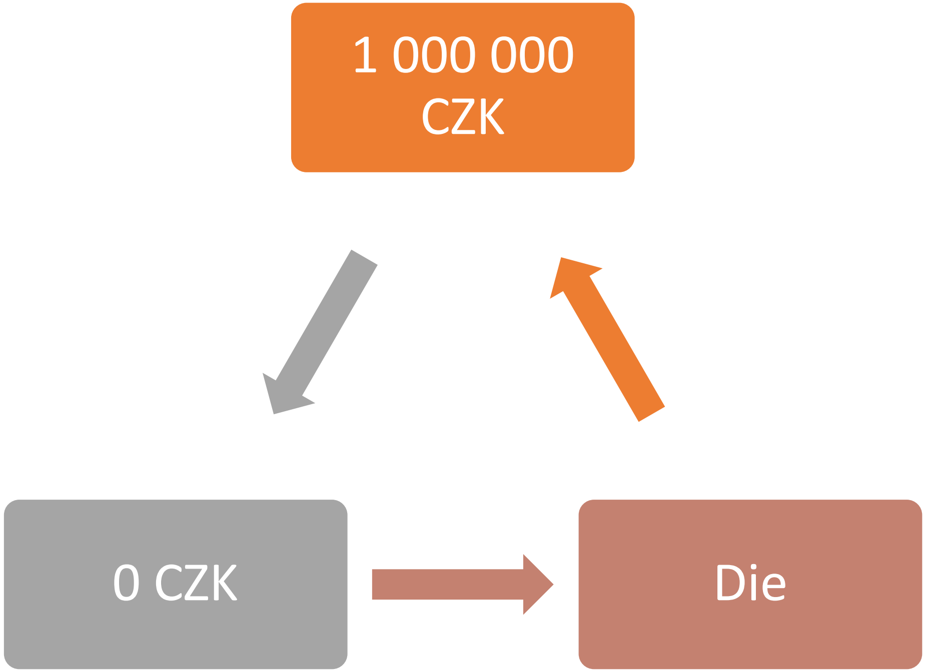
Die

Intransitive preferences

- Prefer X to Y, Y to Z and Z to X
- Doesn’t make sense



Other notions about preferences

- Preferences over outcomes are stable and do not change in the time of making decision – are fixed

- Preferences are **ordinal** – they order actions but the difference between the two values has no meaning unless they state utility

- Compare two situations
  - $u(C_1) = 1$, $u(C_2) = 2$, $u(C_3) = 0$
  - $u(C_1) = 1$, $u(C_2) = 200$, $u(C_3) = -50$

- Both situations have same preference ordering
  - C_2 p C_1 p C_3

Other notions about rationality

- Rational choice theory is not attempting to explain cognitive processes happening in individuals

- Rationality tells nothing about preferences over outcomes

- Rational actors may differ in choices in same situation

- Rational actors can err

Types of games

Types of games

- Games of perfect information
- Games of imperfect information

- Cooperative games
- Non-cooperative games

- Constant-sum game
- Positive-sum game

Games of perfect/imperfect information

Perfect information games

- All players know other players' strategies available to them
- All players know payoffs over actions
- All players know other players know

Imperfect information games

- Some information about other players' actions is not know to the player

Cooperative/non-cooperative games

Cooperative games

- Actors are allowed to make enforceable contracts
- Players do not need to cooperate, but cooperation is enfoceable by an outside party

Non-cooperative games

- Actors unable to make enforceable contracts outside of those specifically modeled in the game
- Players might cooperate, but any cooperation must be self-enforcing

Constant-sum/Positive-sum games

Constant sum games

- Sum of all players' payoffs is the same for any outcome
- Gain for one participant is always at the expense of another
- Special case of zero-sum game where all outcomes involve a sum of all player's payoffs of 0

Positive-sum games

- Combined payoffs of all players are not the same in every outcome of the game
- Positive-sum game implies that players may have interests in common, to achieve an outcome that maximizes total payoffs.

Introducing a game

What makes a game the game

- Players
- Actions
- Strategies
- Outcomes
- Payoffs of player

Game of grades

- Each pair can choose 2 actions: α or β
- If both choose α, both will receive C
- If both choose β, both will receive B
- If one chooses α and other β, one will receive A and other D

Game of grades – my grades

My opponent

Me

	α	β
α	C	**A**
β	**D**	B

Game of grades – my opponent's grades

		My opponent	
		α	β
Me	α	C	**D**
	β	**A**	B

Game of grades – normal form

My opponent

Me

	α	β
α	C , C	A , D
β	D , A	B , B

Games in normal form

Normal form representation of a game

- Called also “strategic form” or “matrix form”

- Visualized as a matrix

- Represents a game as if agents were acting simultaneously

Utilities (Payoffs)

- Grades are not utilites

- Utilities for game:
  - EU(A) = 3
  - EU(B) = 2
  - EU(C) = 1
  - EU(D) = 0

- Preference over outcomes: A > B > C > D -> APBPCPD

Game of grades with payoffs

		My opponent	
		α	β
Me	α	1 , 1	3 , 0
	β	0 , 3	2 , 2

Solution concepts

- Nash Equilibrium
  - Dominant Strategy Equilibrium
  - Pure Strategy Equilibrium
  - Mixed Strategy Equilibrium
- Subgame Perfect Equilibrium
- Bayesian Equilibrium
- Weak Perfect Bayesian Equilibrium

My opponent

Me		α	β
	α	1 , 1	3 , 0
	β	0 , 3	2 , 2

My opponent

Me	α	β
α	1 , 1	3 , 0
β	0 , 3	2 , 2

My opponent

Me	α	β
α	1 , 1	3 , 0
β	0 , 3	2 , 2

My opponent

Me		α	β
	α	C , C	A , D
	β	D , A	B , B

Prisoner’s dilemma

- Both players are tempted to defect, since cooperate is strictly dominated by defect
- The outcome of the game is that both players betray the other one and end up choosing α
- Both will end up with outcome that is less preferred than the optimal outcome β, β by seeking maximal gain from own action
- β, β is Pareto Efficient outcome – brings best outcomes for all players – no one could be better-off without making someone worse-off

Dominance

Dominant Strategy Equilibrium

- Strategy might be dominant

Two types of dominance

- Strict (strong) dominance
- Weak dominance

Strict dominance

- Player i
- Payoff u_i
- Dominant strategy s_i
- Dominated strategy s_i'
- Strategy of all other players s_{-i}

- Player i‘s strategy si’ is strictly dominated by player i‘s strategy si if and only if
- $u_i(s_i , s_{-i}) > u_i(s_i' , s_{-i})$ for **all** s_{-i}

- utility of playing s_i against others’ strategies s_{-i} is **greater** than utility of playing s_i' against others’s strategies s_{-i} for all others’ strategies s_{-i}

Game of grades – strict dominance

My pair

Me		α	β
	α	1 , 1	3 , 0
	β	0 , 3	2 , 2

Weak dominance

- Player i
- Payoff u_i
- Dominant strategy s_i
- Dominated strategy s_i'
- Strategy of all other players s_{-i}

- Player i‘s strategy si’ is weakly dominated by player i‘s strategy si if
- $u_i(s_i , s_{-i}) \geq u_i(s_i' , s_{-i})$ for **all** s_{-i} and
- $u_i(s_i , s_{-i}) > u_i(s_i' , s_{-i})$ for **some** s_{-i}

- utility of playing s_i against others’ strategies s_{-i} is **greater or equal to** utility of playing s_i' against others’s strategies s_{-i} for all others’ strategies s_{-i} and **greater for some** others’ strategies s_{-i}

Game of grades – weak dominance

My pair

Me	α	β
α	1 , 1	3 , 0
β	0 , 3	3 , 2

Never play dominated strategies

- Dominated strategy **brings lesser payoffs** than dominant strategy
- Dominated strategy brings lesser payoffs **no matter what strategy is selected by other player**
- Can’t control minds of others to force them not to play dominant strategy
- Event if **could** control minds of others and be sure they’ll play dominated strategy, than **rational to play dominant strategy anyway**

Choosing numbers

- Choose integer between 1 – 100 incl.
- All numbers will be averaged
- Winner is the one who will be closest to the 2/3 of the group's average

Choosing numbers

- Average = 100
- 2/3 of average = ~ 66.66
- X > 67 is strictly dominated strategy
  - Even if everyone else selected 100
  - One selected 67
  - I selected 68
  - Outcome – 68 is dominated by 67

- What is the rational choice for this game?

If all players were strictly rational, result is 1

I know you know

- I know
  - Numbers above 67 are never rational
- You know that I know
  - You'll never select number above 67, therefore numbers above 46 are never rational either
- I know You know that I know
  - I know that You'll never select above 46, hence I should never select number higher than 30
- You know that I know that You know that I know
  - You know that I won't select above 30, therefore I should never select number above 20

Get into opponent’s shoes

Real life results

- 2012 Game theory online course

- 10 000 + players

- Mean 34
- Mode 50
- Median 33
- Winner 23

- Spikes: 50, 33, 20, 1

Iterated deletion of dominated strategies

Iterated deletion of dominated strategies

- Can delete dominated strategies as if they were not present in the game
- Game becomes simpler than the original one
- Can find equilibriums quickly – games are dominance-solvable

Game of grades

My pair

Me		α	β
	α	1 , 1	~~3 , 0~~
	β	0 , 3	~~2 , 2~~

		My pair
		α
Me	α	1 , 1
	β	~~0 , 3~~

My pair

		α
Me	α	1 , 1

This game is dominance-solvable

Opponent

Me		s_1	s_2	s_3
	S_1	0 , 1	-2 , 3	4 , -1
Me	S_2	0 , 3	3 , 1	6 , 4
	S_3	1 , 5	4 , 2	5 , 2

S_1 vs S_2

Opponent

Me		s_1	s_2	s_3
	S_1	0 , 1	-2 , 3	4 , -1
	S_2	0 , 3	3 , 1	6 , 4
	S_3	1 , 5	4 , 2	5 , 2

S_1 vs S_3

		Opponent		
		s_1	s_2	s_3
	S_1	0 , 1	-2 , 3	4 , -1
Me	S_2	0 , 3	3 , 1	6 , 4
	S_3	1 , 5	4 , 2	5 , 2

S_2 vs S_3

Opponent

Me	s_1	s_2	s_3
S_1	0 , 1	-2 , 3	4 , -1
S_2	0 , 3	3 , 1	6 , 4
S_3	1 , 5	4 , 2	5 , 2

S_1 VS S_3

Opponent

		s_1	s_2	s_3
	S_1	0 , 1	-2 , 3	4 , -1
Me	S_2	0 , 3	3 , 1	6 , 4
	S_3	1 , 5	4 , 2	5 , 2

S_1 VS S_2

Opponent

		s_1	s_2	s_3
	S_1	0 , 1	-2 , 3	4 , -1
Me	S_2	0 , 3	3 , 1	6 , 4
	S_3	1 , 5	4 , 2	5 , 2

S_2 VS S_3

Opponent

		s_1	s_2	s_3
	S_1	0 , 1	-2 , 3	4 , -1
Me	S_2	0 , 3	3 , 1	6 , 4
	S_3	1 , 5	4 , 2	5 , 2

Opponent

Me		s_1	s_2	s_3
	S_1	~~0 , 1~~	~~-2 , 3~~	~~4 , -1~~
Me	S_2	0 , 3	3 , 1	6 , 4
	S_3	1 , 5	4 , 2	5 , 2

Opponent

Me		s_1	s_2	s_3
	S_2	0 , 3	3 , 1	6, 4
	S_3	1, 5	4 , 2	5 , 2

s_1 vs s_3 after deletion

Opponent

Me	s_1	s_2	s_3
S_2	0 , 3	3 , 1	6 , 4
S_3	1 , 5	4 , 2	5 , 2

s_1 vs s_2 after deletion

Opponent

Me		s_1	s_2	s_3
	S_2	0 , 3	3 , 1	6 , 4
	S_3	1 , 5	4 , 2	5 , 2

s_2 vs s_3 after deletion

		Opponent s_1	Opponent s_2	Opponent s_3
Me	S_2	0 , 3	3 , 1	6 , 4
Me	S_3	1 , 5	4 , 2	5 , 2

Opponent

Me	s_1	s_2	s_3
S_2	0 , 3	~~3 , 1~~	6 , 4
S_3	1 , 5	~~4 , 2~~	5 , 2

Opponent

Me		s_1	s_3
	S_2	0 , 3	6 , 4
	S_3	1 , 5	5 , 2

Opponent

Me

	s_1	s_3
S_2	0 , 3	**6** , 4
S_3	**1** , 5	5 , 2

Opponent

Me		s_1	s_3
	S_2	0 , 3	6 , **4**
	S_3	1 , **5**	5 , 2

Sometimes not solvable, but simplified

Limits of iterated deletion of dominated strategies

- Strictly dominated strategies may be deleted in a random order
- Deleting weakly dominated strategies in some order might delete equilibriums
- This solution concept is not always applicable – sometimes game simply don’t have dominance

How to solve the game without dominance?

Opponent

Me

	s_1	s_3
S_2	0 , 3	6 , 4
S_3	1 , 5	5 , 2

How to solve the game without dominance?

Opponent

Me		s_1	s_3
	S_2	0 , 3	6 , 4
	S_3	1 , 5	5 , 2

Nash Equilibrium

Nash Blonde Game

- 2 or more lusty males
- Several interested females
- At least one more female than male
- Just one female blonde
- Every male prefers blonde to brunette and brunette to no companion

Nash Blonde Game – normal form

M2

M1		Bl	Br
	Bl	0 , 0	2 , 1
	Br	1 , 2	1 , 1

Nash Equilibrium

- Set of strategies, one for each player, such that **no player has incentive to unilaterally change** her action
- Players are in equilibrium if a change in strategies by any one of them would lead player to earn less (considering strategies of others') than if she remained with her current strategy
- **Mutual best response** to others' choices

		A		
		L	C	R
	T	1 , 1	0 , 0	0 , 0
B	M	0 , 2	1 , 1	2 , -1
	B	0 , 0	1 , 2	2 , 1

A

B		L	C	R
	T	1 , 1	0 , 0	0 , 0
	M	0 , 2	1 , 1	2 , -1
	B	0 , 0	1 , 2	2 , 1

		A		
		L	C	R
B	T	1 , 1	0 , 0	0 , 0
	M	0 , 2	1 , 1	2 , -1
	B	0 , 0	1 , 2	2 , 1

		A		
		L	C	R
B	T	1 , 1	0 , 0	0 , 0
	M	0 , 2	1 , 1	2 , -1
	B	0 , 0	1 , 2	2 , 1

Games might have more NE

Pure strategy equilibrium

- Two equilibriums in this game
- (T , L)
  - u(A) = 1
  - u(B) = 1
- (C , B)
  - u(A) = 1
  - u(B) = 2
- These are **pure strategy equilibriums**