# Index

#### A

Agent's disutility, 108 Agent's expected utility rate moderately risk-seeking agent, 90–91 risk-averse agent, 21 risk-neutral agent, 9, 10 risk-seeking agent, 66 SRA agent, 44, 47, 49, 53, 55 strongly risk-seeking agent, 103 WRA agent, 23–25, 34–36 WRS agent, 68 Agent's risk premium, 20, 66, 108, 109

# С

Compensation rate moderately risk-seeking agent, 97, 98 risk-averse agent, 23 risk-seeking agent, 67 WRA agent, 23, 34 WRS agent, 81–83

#### Е

Equipment's failure rate, 107 Equipment units, 1, 2, 5, 19, 104, 108, 109

#### F

Failure rate, 5, 6, 34, 45, 55, 62, 63, 81, 82, 98, 107, 109

## M

Marginal cost, 6, 107 Markov process, 2, 6, 9 Moderately risk-seeking agent, 109 agent's expected utility rate, 90–91 agent's optimization problem, 89 compensation rate, 97, 98 lemmas subcases, 91–96 principal's expected profit rate, 99–102 principal's optimal strategy, 99–102 proof for Proposition, 89–93 sensitivity analysis, 97–99

## 0

Optimal compensation rate, 62, 108 Optimal contract, 7, 15, 67, 107-108, 111 Optimal principal-agent contract formulas, 109-110 Optimal strategies agent's optimal response, 13 conditions, 12-13 forms of  $u(\mu)$ , 11–12 game structure, 17-18 moderately risk-seeking agent (see Moderately risk-seeking agent) proof for Proposition, 11-12 second-best solution, 16-17 sensitivity analysis, 15-16 SRA agent (see Strongly risk-averse (SRA) agent) strongly risk-seeking agent, 102-104

© Springer International Publishing Switzerland 2016 S. Zeng, M. Dror, *Formulating Principal-Agent Service Contracts for a Revenue Generating Unit*, SpringerBriefs in Operations Management, DOI 10.1007/978-3-319-18672-6 Optimal strategies (*cont.*) technical lemma, 11 Theorem, 12, 14–15 WRA agent (*see* Weakly risk-averse agent) WRS agent (*see* Weakly risk-seeking agent)

## P

Penalty rate moderately risk-seeking agent, 97-98 risk-averse agent, 19 risk-neutral agent, 9-10 risk-seeking agent, 65 SRA agent, 54, 55, 57 WRA agent, 34-35 WRS agent, 81-83 Principal-agent cooperation, 108 Principal-agent setting average downtime, 5 contract structure, 3 cumulative downtime, 5 equipment unit, 3 first-order approach, 4 individual rationality principal, 6-7 literature on. 5-6 marginal cost, 6 Markov process, 6 performance measures, 4 profit function. 4 revenue rate. 6 second-best solution, 4 set of admissible solutions, 7 strategy set, 7 variables, 5 weakly dominates, 7 Principal's expected profit rate moderately risk-seeking agent, 99-102 risk-neutral agent, 10 SRA agent, 56-60 strongly risk-seeking agent, 104 WRA agent, 23, 40-44 WRS agent, 68, 83-88 Principal's optimal strategy expected profit rate, 36 lemma subcases, 41-42 moderately risk-seeking agent, 99-102 non-negative expected utility rate, 38 optimization problem, 56 optimizing values, 56 principal offers, 36-37 principal's expected profit rate, 40, 56 principal's optimization problem, 40

proof for Proposition, 39–40 restrictions, 38 SRA agent, 56–60 strongly risk-seeking agent, 102 technical lemmas, 37–38, 57 Theorem, 42–45, 57–60 WRS agent, 83–89

#### R

Repair capacity marginal cost, 107 Repair rate, 5, 107 Revenue rate, 6, 107, 111 Risk-averse agent, 2 agent's expected utility rate, 21 agent's risk coefficient, 60-61 compensation rate, 23 expected profit rate, 21 expected utility rate, 21 monotonicity and concavity/convexity, 21 - 22optimal strategies (see Optimal strategies) penalty rate, 19 random variable, risk of, 19 revenue rate, 60-61 risk premium, 20 second-best solution, 63-64 sensitivity analysis, 61-63 standard deviation, 19 utility function, 21 Risk-neutral agent, 2 agent's expected utility rate, 10 compensation rate, 9-10 expected penalty rate, 9-10 expected profit rate, 9-10 Markov process, 9 optimal strategies (see Optimal strategies) performance based contract, 10 principal's expected profit rate, 10 Risk premium risk-averse agent, 20, 108 risk-seeking agent, 66, 109 Risk-seeking agent, 2 agent's penalty rate, 65 Bernoulli random variable, 65 compensation rate, 67 contract offers, 104-105 expected utility rate, 66 moderately risk-seeking, 66, 99-102 optimal strategies (see Optimal strategies) principal's expected revenue rate, 67 Prospect Theory, 65, 66

#### Index

risk measure, 65–66 risk premium, 66 set of admissible solutions, 67–68 strongly risk-seeking, 67, 102 weakly risk-seeking, 66, 83–89

## S

Sensitivity analysis moderately risk-seeking agent, 97-99 SRA agent, 54-56 weakly risk-seeking agent, 81-83 WRA agent, 33-36 Standard deviation, 19, 20, 108 Strongly risk-averse (SRA) agent, 108 accepts contract, 54 agent's expected utility rate, 44, 47, 49, 53, 55 lemma subcases, 49-53 penalty rate, 54, 55, 57 principal's expected profit rate, 56-60 principal's optimal strategy, 56-60 proof for Proposition, 46-49 sensitivity analysis, 54-56 technical lemmas, 46-47  $w_4$  and  $p_4$  functions, 46 Strongly risk-seeking agent, 102-104, 109

## W

Weakly risk-averse (WRA) agent, 108 agent's expected utility rate, 23-25, 34-36 agent's optimal service capacity, 23 compensation rate, 23, 34 optimal response, 24-25 optimization of  $u(\mu)$ , 25–27 penalty rate, 34-35 principal's expected profit rate, 23, 40-44 principal's optimal strategy (see Principal's optimal strategy) sensitivity analysis, 33-36 service capacity, 27-33 technical lemmas, 23-24 Weakly risk-seeking (WRS) agent, 109 agent's expected utility rate, 68 agent's optimal service capacity, 68 compensation rate, 81-83 lemma subcases, 74-75, 79-80 monotonicity and concavity/convexity function, 69, 72 penalty rate, 81-83 principal's expected profit rate, 68, 83-88 principal's optimal strategy, 83-89 proof for Proposition, 71-74, 76-77, 79 sensitivity analysis, 81-83 technical lemmas, 70-71