

# The Title of your Report

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**Abstract**—A short summary of your project. You should change also the title, but do *not* enter any author names or anything that unnecessarily identifies any of the authors. It is suggested you use a similar structure (sections, etc.) as demonstrated in this document, but you can make the section headings more descriptive if you wish. Of course you should delete all the text in this template and write your own! – this text simply provides detailed instructions/hints on how to proceed.

## I. INTRODUCTION

In the following paper we implement three different reinforcement learning agents and evaluate their performance within a supply chain environment. All the code used to create the results presented in this paper can be found here <sup>1</sup>.

The supply chain optimization environment represents a problem faced by companies whose supply chain consists of a factory and multiple warehouses (so called hub-and-spoke networks as described by [4]). The main decision that needs to be made in these settings is how many products should be produced in the factory and how much stock should be build up in the warehouses. Seasonal demand can further complicate the decision problem since it might require the companies to start building up stock early so that high demands in the future can be satisfied (e.g. think about christmas where the stock of eggnog needs to be build up during november and december to be able to satisfy the high demand levels during the holidays). This requirement for mid- to long-term planning indicates that the problem can be formulated as a multi-step decision problem and further exhibits a weak signal because the reward for an early build-up of stock will only be realized in the future when the actual demand reaches its maximum. Even for small supply chain networks we find that due to the curses of dimensionality, as described by [2], the state- and action-spaces of the respective decision problems become unfeasibly large. Therefore we turn to function-approximation and policy-search methods of reinforcement learning that are less affected by these problems. In our case we chose approximate SARSA and the REINFORCE algorithm as a basis for the agents.

## II. BACKGROUND AND RELATED WORK

The supply chain optimization problem presented in this paper will be modeled as a markov decision process (MDP). Furthermore we rely on the approximate SARSA and REINFORCE algorithms to design agents capable of finding a good strategy to navigate within the environment. MDPs are multi-step stochastic decision problems that rely on the markov property which implies that the transition probability  $P(s_{n+1} | s_n)$  between two states  $s_{n+1}$  and  $s_n$  only

relies on the current state  $s_n$ . We describe the MDP similar to [1] and [2] as an eight-tuple  $(S, D, A, \mathcal{X}, T, Q, r, \gamma)$  consisting of a state-space  $S$ , a random environment process  $D$ , an action space  $A$ , a set of feasible actions  $\mathcal{X}$ , a transition function  $T$ , transition probabilities  $Q$ , a one-step reward function  $r$  and some discount factor  $\gamma$ .

The designed agents are based on the blueprints for the approximate SARSA and REINFORCE algorithm from [3]. We compare the performance of these reinforcement learning algorithms with an agent that acts according to a fixed heuristic based on the  $(\varsigma, Q)$ -Policy <sup>2</sup> as described by [5].  $(\varsigma, Q)$ -Policies induce a simple replenishment strategy where the stock of a warehouse will be replenished by some amount  $Q$  as soon as it falls under a threshold  $\varsigma$ . A basic visualization of the  $(\varsigma, Q)$ -Policy is depicted in Figure 1.

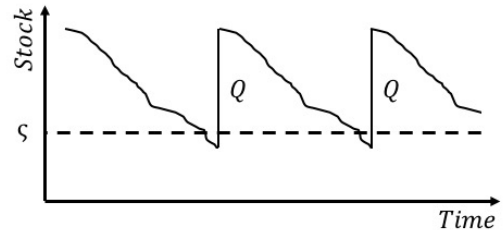


Fig. 1: Schematic visualization of a  $(\varsigma, Q)$ -Policy for a single warehouse.

Furthermore we use several different stepsize formulars from [2] that are used to update some of the agents parameters such as the learning rate  $\alpha$ . The idea of specific stepsize rules is to allow the agent to go through a longer learning phase in the beginning with higher learning rates and then converge in the long term to stepsizes close to 0. Among others we use a so called search-then-converge stepsize rule as presented in [2] where the learning rate in the  $n^{th}$  iteration is calculated by

$$\alpha_n = \alpha_0 \frac{\frac{b}{n} + a}{\frac{b}{n} + a + n^\beta} \quad (1)$$

with some parameters  $\alpha_0, b, a$  and  $\beta$  that can be set by the user based on the required behavior of the stepsize.

## III. THE ENVIRONMENT

We will model the environment as a MDP that we regard over an infinite number of periods  $t = 0, 1, \dots$ . The environment consists of one factory (indexed by 0) and up to  $k \in \mathbb{N}$  warehouses (indexed by  $j = 1, \dots, k$ ) where in each period it needs to be decided how many units of a product (e.g. butter) should be produced and how many should be

<sup>1</sup>Our code is available here: <http://anonymouslinktoyourcode.zip>

<sup>2</sup>In the literature this policy is usually called  $(\varsigma, Q)$ -Policy. We chose a slightly different name to avoid notation conflicts in our model description.

shipped to the individual warehouses. A representation of a network with 5 warehouses is depicted in Figure 2. The state



Fig. 2: Example of a supply chain network with  $k = 5$  warehouses ( $s_1, \dots, s_5$ ) and the factory ( $s_0$ ).

space consists of  $k + 1$  elements describing the current stock levels of the factory and the warehouses ( $s_j, j = 0, \dots, k$ ), where each stock level is limited by some capacity  $c_j \in \mathbb{N}$ . Note that this implies that the factory itself can also build up stock. Furthermore we assume an environment process with states  $d \in D \in \{0, \dots, d_{max}\}^k, d_{max} \in \mathbb{N}$  describing the (stochastic) demand  $d_j$  at each warehouse with transition probabilities  $q_d(d')$  that are unknown by the agent. We assume a discretized version of a sinus-function and some shocks  $\epsilon$  where the demand follows a model

$$d_{i,t} = \left\lceil \frac{d_{max}}{2} \sin\left(\frac{2\pi(t+2i)}{12}\right) + \frac{d_{max}}{2} + \epsilon_{i,t} \right\rceil \quad (2)$$

with  $\lceil \cdot \rceil$  the ceiling function and  $P(\epsilon_{i,t} = 0) = P(\epsilon_{i,t} = 1) = 0.5$ . We will include  $d_{last}, d_{hist} \in D$  in our state space where for some time  $t$  we have the tuple  $\tilde{s} = (s, d_{last}, d_{hist})$  with  $s = s_t, d_{last} = d_{t-1}$  and  $d_{hist} = d_{t-2}$ . Note that this implies that the demand  $d_t$  of period  $t$  is not observed by the agent. This means, that the demand in a period  $t$  will be realized after observing the stock levels  $s_t$  and can only be observed in the next period  $t + 1$ . The reason we add the old demands to the state space is to allow the agent to have a simple understanding of the demands movement. In each period the agent can now set the factories production level for the next period  $a_0 \in \{0, \dots, \rho_{max}\}$  (with a maximum production of  $\rho_{max} \in \mathbb{N}$ ) aswell as the number of products shipped to each location  $a_j \in \mathbb{N}^k$  that is naturally limited by the current storage level in the factory ( $\sum_{j=1}^k a_j \leq s_0$ ). Based on this information and the demand  $d$  we can now describe the state transitions ( $\tilde{s}, d, a \rightarrow T(\tilde{s}, d, a)$ ) by

$$T(\tilde{s}, d, a) := \left( \min\left\{s_0 + a_0 - \sum_{j=1}^k a_j, c_0\right\}, \right. \\ \min\{s_1 + a_1 - d_1, c_1\}, \\ \dots \\ \min\{s_k + a_k - d_k, c_k\}, \\ d, \\ d_{last} \Big). \quad (3)$$

The reward within each period consists of the revenue from sold products at a fix price  $p$  less production costs  $\kappa_{pr}a_0$ , storage costs  $\sum_{j=0}^k \kappa_{st,j} \max\{s_j, 0\}$ , penalty costs  $\kappa_{pe} \sum_{j=1}^k \min\{s_j, 0\}$  and transportation costs  $\sum_{j=1}^k \kappa_{tr,j} \lceil a_j / \zeta_j \rceil$ . We let  $p, \kappa_{pr}, \kappa_{pe}, \kappa_{st,j}, \kappa_{tr,j} \in \mathbb{R}_+$  and  $\zeta_j \in \mathbb{N}$ . We can now define the one-step reward function by

$$r(\tilde{s}, d, a) := p \sum_{j=1}^k d_j - \kappa_{pr}a_0 - \sum_{j=0}^k \kappa_{st,j} \max\{s_j, 0\} \\ + \kappa_{pe} \sum_{j=1}^k \min\{s_j, 0\} - \sum_{j=1}^k \kappa_{tr,j} \left\lceil \frac{a_j}{\zeta_j} \right\rceil. \quad (4)$$

Furthermore we chose a discounting factor  $\gamma \in (0, 1)$  that can be interpreted e.g. as a result of inflation.

Based on this model description we can now formulate the task as an infinite horizon markov decision process that is subject to a varying environment. Thereby we receive the tuple  $(S, I, A, \mathcal{X}, T, Q, r, \gamma)$  with

#### Definition 1.

1.  $S \times D^3 := \prod_{j=0}^k \{s_j \in \mathbb{Z} \mid s_j \leq c_j\} \times D^3, c_j \in \mathbb{N}$  the state space consisting of elements  $(\tilde{s}, d) = ((s, d_{last}, d_{hist}), d)$ ;
2.  $A := \{0, \dots, \rho_{max}\} \times \mathbb{N}_0^k$  the action space consisting of elements  $a = (a_0, \dots, a_k)$ ;
3.  $\mathcal{X}(\tilde{s}) := \{0, \dots, \rho_{max}\} \times \{a \in \mathbb{N}_0^k \mid \sum_{j=1}^k a_j \leq s_0\}$ , the set of all feasible actions in a state  $\tilde{s}$  and  $\mathcal{X} := \{(\tilde{s}, d, a) \in S \times D^3 \times A \mid a \in \mathcal{X}(\tilde{s})\}$ ;
4.  $T : S \times D^3 \times A \rightarrow S$  the transition function defined by Eq. (3);
5.  $Q : \mathcal{X} \times S \times D^3 \rightarrow [0, 1]$  the transition probabilities with  $Q(\tilde{s}', d' \mid \tilde{s}, d, a) := q_d(d')$  for  $\tilde{s}' = T(\tilde{s}, d, a)$  and 0 otherwise;
6.  $r : S \times D^3 \times A \rightarrow \mathbb{R}$  the one-step reward function as described in Eq. (4);
7.  $\gamma \in (0, 1)$  the discounting factor.

For the calculation of the expected discounted revenue for each tuple  $(\tilde{s}, d)$  we obtain the value function  $V$  with

$$V(\tilde{s}, d) = \max_{a \in \mathcal{X}(\tilde{s})} \{r(\tilde{s}, d, a) \\ + \gamma \sum_{d' \in D} q_d(d') V(T(\tilde{s}, d, a), d')\}, \quad (5) \\ \tilde{s} \in S \times D^2, d \in D.$$

#### IV. THE AGENT

In this paper we evaluated the performance of three agents based on different algorithms: a heuristic based on the  $(\varsigma, Q)$ -Policy that we use as the baseline for performance evaluation, an approximate SARSA algorithm and an implementation of the REINFORCE algorithm.

**The  $(\varsigma, Q)$ -Policy** based agent is not smart in the way that it does not learn over time. Due to the popularity of the  $(\varsigma, Q)$ -Policy in practice we use it as a baseline for performance evaluation of the other agents. In the heuristic we iterate over  $s_1, \dots, s_k$  and replenish the respective warehouses by some

amount  $a_i = Q_i$  if the current stock is below a level  $\varsigma_i$  and there is still stock left in the factory  $s_0$ . At the end we set the production level for the next period to  $Q_0$  if  $s_0 - \sum_{i=1}^k a_i < \varsigma_0$  and 0 otherwise. The thresholds  $\varsigma$  and replenishment levels  $Q$  need to be set by the user when initializing the agent.

**Approximate SARSA** uses a linear approximation  $Q_\theta(\tilde{s}, a) = \theta^T \phi(\tilde{s}, a)$  of the actual Q-function  $Q^\pi$ . We chose this method as it solves the problem of exponentially growing state- and action- spaces that is likely to occur in multidimensional environments. Furthermore it allows us to use our knowledge of the environment (especially the structure of the reward function  $r(\tilde{s}, d, a)$ ) to design  $\phi(\tilde{s}, a)$  such that it preserves some of the MDPs structure. The algorithm is implemented as depicted in (add ref.). The underlying intuition for the definition of  $\phi$  is to value states  $\tilde{s}$  based on an approximation of the individual storage levels, recent demands ( $d_{last}, d_{hist}$ ) and the sales price  $p$ . We assume that the stock in each warehouse  $s_1, \dots, s_k$  will be roughly equivalent to the current stock level minus the current demand (which is used as a proxy of the demand in the next step). For the factory  $s_0$  we solely regard the current storage level but deduct the production cost  $\kappa_{pr}$  from the sales price. Based on this intuition we can define  $\phi : S \times D \times A \rightarrow \mathbb{R}^{k+1}$  by

$$\begin{aligned} \phi(s, a) := & ((s_0 + a_0)(p - \kappa_{pr}), \\ & (s_1 + a_1 - d_1)p, \\ & \dots \\ & p(s_k + a_k - d_k)p). \end{aligned} \quad (6)$$

When testing the approximate SARSA algorithm we found that for some environments the parameters  $\theta$  would increase until computations became numerically unstable. To avoid this issue we restrict the temporal difference

$$\delta_n = r(\tilde{s}_n, d_n, a_n) + \gamma \theta_n^T \phi(\tilde{s}_{n+1}, a_{n+1}) - \theta_n^T \phi(\tilde{s}_n, a_n) \quad (7)$$

that is used to update  $\theta_n$  within the interval  $[-1e50, +1e50]$ .

## V. RESULTS AND DISCUSSION

This is one of the most important sections. You put your agent to the test in the environment, you show – and most importantly – you interpret the results.

### A. Performance of your Agent in your Environment

Show plots, graphs, tables (e.g., Table I), etc. You may wish to encourage readers to reproduce results for themselves, e.g., run `runDemo.py` in our source code. Show how your agent performs well, or, if it doesn't perform well, it is better to explain why (this is a result in itself!). In any case, you *must* highlight the weaknesses of your agent as well as its strengths.

TABLE I: This table is just an example.

Environment config.	Standard SARSA	Our Improved Agent
Simulation 1	10	15
Simulation 2	12	11

### B. Performance of your Agent in the ALife Environment

You deploy your agent in the ALife<sup>3</sup> environment (a random screenshot shown in Figure 3). Does it work well? Why? Why not? Justify the adaptation you think is best.



Fig. 3: An example figure

## VI. CONCLUSION AND FUTURE WORK

This section summarizes the paper: Your environment and agent, its strength and its weaknesses. Also remark about what would be the next steps you would take if you or someone else were to continue/extend this project. Note that for the initial submission you are limited strictly to 4 pages (double column), *not including references*. An extra page will be allowed for final submission (after the initial reviews).

## REFERENCES

- [1] L. N. Moritz, Target Value Criterion in Markov Decision Processes, *Karlsruhe, KIT, Diss.*, 2014.
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- [4] K. Furmans, D. Arnold, Materialfluss in Logistiksystemen, *Springer Berlin Heidelberg*, 2009.
- [5] H. Tempelmeier, Inventory management in supply networks: problems, models, solutions, *Books on Demand*, 2011.

<sup>3</sup><https://github.com/jmread/alife>