CONTRACTION OPTIONS AND OPTIMAL MULTIPLE-STOPPING IN SPECTRALLY NEGATIVE LÉVY MODELS

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ABSTRACT. This paper studies the Lévy model of the optimal multiple-stopping problem arising in the context of the timing option to withdraw from a project in stages. The profits are driven by a general spectrally negative Lévy process. This allows the model to incorporate sudden declines of the project values, generalizing greatly the classical geometric Brownian motion model. We solve the one-stage case as well as the extension to the multiple-stage case. The optimal stopping times are of threshold-type and the value function admits an expression in terms of the scale function. A series of numerical experiments are conducted to verify the optimality and to evaluate the efficiency of the algorithm.

Key words: Optimal multiple-stopping; Spectrally negative Lévy processes; Real options
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1. INTRODUCTION

Consider a firm facing a decision of when to abandon or contract a project so as to maximize the total expected future cash flows. This problem is often referred to as the abandonment option or the contraction option. A typical formulation reduces to a standard optimal stopping problem, where the uncertainty of the future cash flow is driven by a stochastic process and the objective is to find a stopping time that maximizes the total expected cash flows realized until then. A more realistic extension is its multiple-stage version where the firm can withdraw from a project in stages.

In a standard formulation, given a discount rate $r > 0$ and $X_t = x + (\mu - \frac{1}{2}\sigma^2)t + \sigma W_t$ for a standard Brownian motion $W$, $\mu \in \mathbb{R}$ and $\sigma > 0$, one wants to obtain a stopping time $\tau$ of $X$ that maximizes the expectation

$$
\mathbb{E} \left[ \int_0^\tau e^{-rt}(e^{X_t} - \delta)dt + e^{-r\tau}K \mathbb{1}_{\{\tau<\infty\}} \right].
$$

The profit collected continuously is modeled as the geometric Brownian motion $e^{X_t}$ less the constant operating expense $\delta \geq 0$. The value $K \in \mathbb{R}$ corresponds to the lump-sum benefits attained (or the costs incurred) at the time of abandonment. Here a technical assumption $r > \mu$ is commonly imposed so that the expectation is finite and the problem is non-trivial. The problem is rather simple mathematically; it reduces to the well-known perpetual
American option (or the McKean optimal stopping problem). An explicit solution can be attained even when $X$ is generalized to a Lévy process (see, e.g., Mordecki [28]).

In this paper, we generalize the classical model by extending from Brownian motion to a general Lévy process with negative jumps (spectrally negative Lévy process), and consider the optimal stopping problem of the form:

$$\sup_{\tau} \mathbb{E} \left[ \int_{0}^{\tau} e^{-rt} f(X_t) \, dt + e^{-r\tau} g(X_{\tau}) 1_{\{\tau < \infty\}} \right].$$

We obtain the optimal stopping time as well as the value function for the case $f$ is increasing and $g$ admits the form $g(x) = K - bx - \sum_{i=1}^{N} c_i e^{a_i x}$ for some positive constants $a_i$, $b$, and $c$. We also show the optimality among all stopping times of threshold type (see (2.4) below) when $g$ is relaxed to be a general decreasing and concave function. The decreasing property of $g$ reflects the fact that the cost of abandoning a project is higher when the project is large.

We further extend to the multiple-stage case where one wants to obtain a set of stopping times $\{\tau^{(m)}; 1 \leq m \leq M\}$ such that $0 = \tau^{(0)} \leq \tau^{(1)} \leq \cdots \leq \tau^{(M)}$ a.s. and achieve

$$\sup_{\tau^{(1)} \leq \cdots \leq \tau^{(M)}} \sum_{m=1}^{M} \mathbb{E} \left[ \int_{\tau^{(m-1)}}^{\tau^{(m)}} e^{-rt} F_m(X_t) \, dt + e^{-r\tau^{(m)}} g_m(X_{\tau^{(m)}}) 1_{\{\tau^{(m)} < \infty\}} \right]$$

when $g_m$ and $f_m := F_m - F_{m+1}$ (with $F_{M+1} = 0$), for each $1 \leq m \leq M$, satisfy the same assumptions as in the one-stage case. The multiple-stopping problem arises frequently in real options (see e.g. [15]) and is well-studied particularly for the case $X$ is driven by Brownian motion. In mathematical finance, similar problems are dealt in the valuation of swing options [11, 12] with refraction times between any consecutive stoppings.

Although the use of Brownian motion is fairly common in real options, empirical evidence suggests that the real world is not Gaussian, but with significant skewness and kurtosis (see, e.g., [9, 14, 32]). Dixit and Pindyck [15] considered the case with jumps of a fixed size with Poisson arrivals. Boyarchenko and Levendorski˘ı [10] considered the EPV approach for a general Lévy process satisfying the (ACP)-condition (with a focus on exponential-type jumps for illustration); they solved a related multiple-stage problem with $g$ being constant. The Lévy model is in general less intractable than the continuous diffusion counterpart, especially when the lump-sum reward function $g$ is not a constant. When jumps are involved, the process can potentially jump over a threshold level, requiring one to compute the overshoot/undershoot distributions that depend significantly on the form of the Lévy measure. Technical details are further required when it has jumps of infinite activity or infinite variation.

In this paper, we take advantage of the recent advances in the theory of the spectrally negative Lévy process (see, e.g., [8, 23]). In particular, we use the results by Egami and Yamazaki [19], where we obtained and showed the equivalence of the continuous/smooth fit condition and the first-order condition in a general optimal stopping problem. Unlike the two-sided jump case, the identification of the candidate optimal stopping time can be conducted efficiently without intricate computation. The resulting value function can be written in terms of the scale function, which also can be computed efficiently by using, e.g., [17, 31]. The extension to the multiple-stage can be carried out without losing generality. The resulting optimal stopping times are of threshold type with possibly simultaneous stoppings, and the value function again admits the form in terms of the scale function. We also conduct a series of numerical experiments using the spectrally negative Lévy process with phase-type jumps so as to verify the optimality of the proposed strategies and also the efficiency of the proposed algorithm. We refer the
reader to, among others, [1, 4, 18, 24, 27] for optimal stopping problems and [6, 7, 16, 21] for optimal stopping
games of spectrally negative Lévy processes.

The rest of the paper is organized as follows. In Section 2, we review the spectrally negative Lévy process and
the scale function and then solve the one-stage problem. In Section 3, we extend it to the multiple-stage problem.
In Section 4, we verify the optimality and efficiency of the algorithm through a series of numerical experiments.
Section 5 concludes the paper.

2. ONE-STAGE PROBLEM

Let \((\Omega, \mathcal{F}, \mathbb{P})\) be a probability space hosting a spectrally negative Lévy process \(X = \{X_t : t \geq 0\}\) characterized
uniquely by the Laplace exponent
\[
\psi(\beta) := \log \mathbb{E}^0 \left[ e^{\beta X_1} \right] = c \beta + \frac{1}{2} \sigma^2 \beta^2 + \int_{(0, \infty)} (e^{-\beta z} - 1 + \beta z 1_{0 < z < 1}) \Pi(dz), \quad \beta \geq 0, \tag{2.1}
\]
where \(c \in \mathbb{R}, \sigma \geq 0\) and \(\Pi\) is a Lévy measure concentrated on \((0, \infty)\) such that
\[
\int_{(0, \infty)} (1 \wedge z^2) \Pi(dz) < \infty. \tag{2.2}
\]
Here and throughout the paper \(\mathbb{P}^x\) is the conditional probability where \(X_0 = x \in \mathbb{R}\) and \(\mathbb{E}^x\) is its expectation. We exclude the case \(X\) is a negative subordinator (decreasing a.s.) and we shall further assume that the Lévy measure
is atomless:

**Assumption 2.1.** We assume that \(\Pi\) does not have atoms.

This section considers the one-stage optimal stopping problem of the form (1.2) where the supremum is taken
over the set (or a subset) of stopping times with respect to the natural filtration \(\mathcal{F} = (\mathcal{F}_t)_{t \geq 0}\) generated by \(X\). We assume the running payoff function \(f\) to be locally bounded and increasing. The stochastic process \(X\) models the state/scale of the project and the monotonicity of \(f\) means that it yields higher benefits when \(X\) is high. Typically one assumes \(f(x) = e^x - \delta\) as in (1.1) and this is clearly a special case of this model. Regarding the terminal reward function \(g\), we consider two cases: (i) when \(g\) is a sum of linear and exponential functions (Assumption 2.2 below) and (ii) when \(g\) is a general decreasing and concave function (Assumption 2.3 below).

The results discussed in this section are applications of Egami and Yamazaki [19] and will be extended to the multiple-stage problem in the next section. Fix \(r > 0\). Let \(\mathcal{S}\) be the set of all \([0, \infty]\)-valued \(\mathcal{F}\)-stopping times and define for any \(\tau \in \mathcal{S},
\[
\mathcal{u}(x, \tau) \equiv \mathcal{u}(x, \tau; f, g) := \mathbb{E}^x \left[ \int_0^\tau e^{-r t} f(X_t) \, dt + e^{-r \tau} g(X_\tau) 1_{\{\tau < \infty\}} \right], \quad x \in \mathbb{R}. \tag{2.3}
\]
After a brief review on the scale function and the results of [19], we shall solve, under Assumption 2.2 below, the problem:
\[
\mathcal{u}(x) := \sup_{\tau \in \mathcal{S}} \mathcal{u}(x, \tau).
\]
We then obtain under Assumption 2.3 below a weaker version of optimality:
\[
\tilde{\mathcal{u}}(x) := \sup_{\tau \in \mathcal{S}} \mathcal{u}(x, \tau),
\]
over the set of all first down-crossing times,

\[ \tilde{S} := \{ \tau_A : A \in \mathbb{R} \}, \]

where

\[ \tau_A := \inf \{ t > 0 : X_t \leq A \}, \quad A \in \mathbb{R}, \] (2.4)

with \( \inf \emptyset = \infty \) by convention. This form of optimality is often used in real options and also in the field of corporate finance and credit risk as exemplified by Leland’s endogenous default model [25, 26]. In practice, a strategy must be simple enough to implement and it is in many cases a reasonable assumption to focus on the set of stopping times of threshold type as in (2.4). Because \( \tilde{S} \subset S \), it is clear that \( u \geq \tilde{u} \). For the rest of the paper, let \( h_{\pm}(x) := \pm h(x) \lor 0 \), \( x \in \mathbb{R} \), for any measurable function \( h : \mathbb{R} \to \mathbb{R} \).

2.1. Review of scale functions and Egami and Yamazaki [19]. For any spectrally negative Lévy process, there exists a function called the \((r-)\)scale function

\[ W^{(r)} : \mathbb{R} \to \mathbb{R}, \]

which is zero on \((-\infty, 0)\), continuous and strictly increasing on \([0, \infty)\), and is characterized by the Laplace transform:

\[ \int_{0}^{\infty} e^{-sx} W^{(r)}(x)dx = \frac{1}{\psi(s) - r}, \quad s > 1, \]

where

\[ \Phi_r := \sup \{ \lambda \geq 0 : \psi(\lambda) = r \}, \quad r \geq 0. \]

Here, the Laplace exponent \( \psi \) in (2.1) is known to be zero at the origin, convex on \([0, \infty)\); \( \Phi_r \) is well-defined and is strictly positive whenever \( r > 0 \). We also define

\[ Z^{(r)}(x) := 1 + r \int_{0}^{x} W^{(r)}(y)dy, \quad x \in \mathbb{R}, \]

which is also called the scale function. As we shall see below, the pair of scale functions \( W^{(r)} \) and \( Z^{(r)} \) play significant roles in our problems.

Recall (2.4) and define the first up-crossing times of \( X \) by \( \tau_b^+ := \inf \{ t \geq 0 : X_t \geq b \} \). Then, for any \( b > 0 \) and \( x \leq b \),

\[ \mathbb{E}^x \left[ e^{-r\tau_b^+} 1_{\{ \tau_b^+ < \tau_0 \}} \right] = \frac{W^{(r)}(x)}{W^{(r)}(b)}, \]

\[ \mathbb{E}^x \left[ e^{-r\tau_b^+} 1_{\{ \tau_b^+ > \tau_0 \}} \right] = Z^{(r)}(x) - Z^{(r)}(b) \frac{W^{(r)}(x)}{W^{(r)}(b)}, \]

(2.5)

\[ \mathbb{E}^x \left[ e^{-r\tau_0} \right] = Z^{(r)}(x) - \frac{r}{\Phi(r)} W^{(r)}(x). \]

As in Lemmas 8.3 and 8.5 of Kyprianou [23], for each \( x > 0 \), the functions \( r \mapsto W^{(r)}(x) \) and \( r \mapsto Z^{(r)}(x) \) can be analytically extended to \( r \in \mathbb{C} \). Fix \( a \geq 0 \) and define \( \psi_a(\cdot) \), as the Laplace exponent of \( X \) under \( \mathbb{P}_a \) with the
change of measure \( \frac{d\mathbb{P}^0}{d\mathbb{P}^0}\big|_{\mathcal{F}_t} = \exp(aX_t - \psi(a)t), \ t \geq 0; \) as in page 213 of [23], for all \( \beta > -a, \)

\[
\psi_a(\beta) := \left( a\sigma^2 + c - \int_0^1 u(e^{-au} - 1)\Pi(du) \right)\beta + \frac{1}{2}\sigma^2 \beta^2 + \int_0^\infty (e^{-\beta u} - 1 + \beta u 1_{0< u < 1})e^{-au}\Pi(du). \tag{2.6}
\]

If \( W_a \) and \( Z_a \) are the scale functions associated with \( X \) under \( \mathbb{P}^a \) (or equivalently with \( \psi_a(\cdot) \)). Then, by Lemma 8.4 of [23],

\[
W_a^{(r - \psi(a))}(x) = e^{-ax}W(r)(x), \quad x \geq 0. \tag{2.7}
\]

In particular, by setting \( a = \Phi_r \) (or equivalently \( r = \psi(a) \)), we can define

\[
W_{\Phi_r}(x) := W_{\Phi_r}^{(0)}(x) = e^{-\Phi_r x}W(r)(x), \quad x \in \mathbb{R}, \tag{2.8}
\]

which satisfies

\[
\int_0^\infty e^{-\beta x}W_{\Phi_r}(x)dx = \frac{1}{\psi(\beta + \Phi_r) - r}, \quad \beta > 0.
\]

The smoothness and asymptotic behaviors around zero of the scale function are particularly important in our analysis. We summarize these in the remark given immediately below.

**Remark 2.1.**

1. Assumption 2.1 guarantees that \( W(r) \) is \( C^1 \) on \((0, \infty)\). In particular, when \( \sigma > 0 \), then \( W(r) \) is \( C^2 \) on \((0, \infty)\). For more details on the smoothness of the scale function, see Chan et al. [13].
2. As in Lemmas 4.3 and 4.4 of [24],

\[
W^{(r)}(0) = \begin{cases} 0, & \text{unbounded variation} \\
\frac{1}{\mu}, & \text{bounded variation} \end{cases},
\]

\[
W^{(r)}(0+) := \lim_{x \downarrow 0} W^{(r)}(x) = \begin{cases} \frac{2}{\sigma^2}, & \sigma > 0 \\
\infty, & \sigma = 0 \text{ and } \Pi(0, \infty) = \infty \\
\frac{r + \Pi(0, \infty)}{\mu^2}, & \text{compound Poisson} \end{cases},
\]

where \( \mu := c + \int_{(0,1]} z \Pi(\mathbb{R}) \), which is finite when \( X \) is of bounded variation.

In [19], we have shown that a candidate optimal stopping time can be efficiently identified using the scale function. Define the expected payoff corresponding to the down-crossing time (2.4) by

\[
u_A(x) := u(x, \tau_A), \quad x, A \in \mathbb{R}, \tag{2.9}
\]

which equals \( g(x) \) for \( x \leq A \). By combining the compensation formula for Lévy processes and the resolvent measure written in terms of the scale function, this can be written in a semi-explicit form. Let

\[
\Psi_f(A) := \int_0^\infty e^{-\Phi_r y}f(y + A)dy, \quad A \in \mathbb{R}, \tag{2.10}
\]

\[
\Theta_f(x; A) := \begin{cases} \int_x^A W^{(r)}(x - y)f(y)dy, & x > A, \\
0, & x \leq A \end{cases}, \tag{2.11}
\]
and

\[ \rho_{g,A}^{(r)} := \int_{(0,\infty)} \Pi(du) \int_{0}^{u} e^{-\Phi_r^*(g(z + A - u) - g(A))} dz, \]
\[ \equiv \int_{(0,\infty)} \Pi(du) \int_{A}^{u + A} e^{-\Phi_r(y - A)}(g(y - u) - g(A)) dy, \quad A \in \mathbb{R}, \] (2.12)

\[ \varphi_{g,A}^{(r)}(x) := \int_{(0,\infty)} \Pi(du) \int_{0}^{u \wedge (x - A)} W^{(r)}(x - z - A)(g(z + A - u) - g(A)) dz, \quad x > A. \]

These integrals are well-defined if

\[ \int_{0}^{\infty} e^{-\Phi_r y} |f(y)| dy < \infty, \] (2.13)

\[ g \in C^2, \quad \text{and} \quad \int_{1}^{\infty} \Pi(du) \max_{A - u \leq \zeta \leq A} |g(\zeta) - g(A)| < \infty, \quad A \in \mathbb{R}. \] (2.14)

If these are satisfied, we can write \( u_A(x) \) as in (2.9) for \( x > A \) as the sum of the following three terms:

\[ \Gamma_1(x; A) := g(A) \left[ Z^{(r)}(x - A) - \frac{r}{\Phi_r} W^{(r)}(x - A) \right], \]
\[ \Gamma_2(x; A) := W^{(r)}(x - A) \rho_{g,A}^{(r)} - \varphi_{g,A}^{(r)}(x), \] (2.15)
\[ \Gamma_3(x; A) := W^{(r)}(x - A) \Psi_f(A) - \Theta_f(x; A). \]

Egami and Yamazaki [19] obtained the first-order condition that makes \( \partial u_A(x) / \partial A \) vanish and showed that it is equivalent to the continuous fit condition \( u_A(A^+) := \lim_{x \downarrow A} u_A(x) = g(A) \) when \( X \) is of bounded variation and to the smooth fit condition \( u'_A(A^+) := \lim_{x \downarrow A} u'_A(x) = g'(A) \) when \( \sigma > 0 \). Recall that \( X \) is of bounded variation if and only if \( \sigma = 0 \) and

\[ \int_{(0,\infty)} (1 \wedge z) \Pi(dz) < \infty. \] (2.16)

It has been shown that

\[ u_A(A^+) = g(A) + W^{(r)}(0) \Lambda(A), \quad A \in \mathbb{R}, \] (2.17)

where

\[ \Lambda(A) \equiv \Lambda(A; f, g) := -\frac{r}{\Phi_r} g(A) - \frac{\sigma^2}{2} g'(A) + \rho_{g,A}^{(r)} + \Psi_f(A), \quad A \in \mathbb{R}. \] (2.18)

In view of Remark 2.1 (2), for the unbounded variation case, continuous fit holds whatever the choice of \( A \) is, while, for the bounded variation case, it holds if and only if \( \Lambda(A) = 0 \).

Furthermore, it has been shown, on condition that there exists some \( \delta > 0 \) satisfying

\[ \int_{1}^{\infty} \Pi(du) \sup_{0 \leq \xi \leq \delta} |g(A + \xi) - g(A + \xi - u)| < \infty, \] (2.19)

we have

\[ \frac{\partial}{\partial A} u_A(x) = -e^{\Phi_r(x-A)} W_{\Phi_r}(x - A) \Lambda(A), \quad x > A, \] (2.20)
where $W_{\Phi_r}$ is defined in (2.8). It is known that $W_{\Phi_r}$ is increasing and hence, if $\Lambda(A)$ is monotonically increasing, the down-crossing time $\tau_A$ for such $A$ with $\Lambda(A) = 0$ becomes a natural candidate for the optimal stopping time.

2.2. Exponential and Linear Case. We first consider the case where $g$ admits the form:

$$g(x) = K - bx - \sum_{i=1}^{N} c_i e^{a_i x}, \quad x \in \mathbb{R},$$

(2.21)

for some constants $K \in \mathbb{R}, c_i, a_i > 0, 1 \leq i \leq N, N \geq 0$, and $b \geq 0$. We assume without loss of generality that $a_i \neq a_j$ for $i \neq j$. The conditions (2.14) and (2.19) are satisfied on condition when $b > 0$ that $\int_{1}^{\infty} u \Pi(du) < \infty$ or equivalently $\mathbb{E}^0 X_1 = \psi'(0+) \in (-\infty, \infty)$. For $f$, we need a technical condition so that (2.13) is guaranteed. We summarize the condition in the Assumption given below.

Assumption 2.2. We assume that

1. $f(\cdot)$ is continuous, increasing, $f(-\infty) := \lim_{x \downarrow -\infty} f(x) > -\infty$ and $\int_{0}^{\infty} e^{-\Phi_r y} f_+(y)dy < \infty$;
2. $g(\cdot)$ admits the form (2.21) for some $K \in \mathbb{R}, b \geq 0$, and strictly positive constants $a_i$ and $c_i$, $1 \leq i \leq N$, $N \geq 0$ such that $a_i \neq a_j$ for any $i \neq j$,
3. for the case $b > 0$, $\mathbb{E}^0 X_1 = \psi'(0+) \in (-\infty, \infty)$.

With Assumption 2.2, we simplify (2.18) using

$$\varpi_r(a) := \left\{ \begin{array}{ll}
\frac{r - \psi(a)}{\Phi_r - a}, & a \neq \Phi_r \\
\psi'(\Phi_r) = \lim_{a \rightarrow \Phi_r} \frac{r - \psi(a)}{\Phi_r - a}, & a = \Phi_r
\end{array} \right\}, \quad a > 0. \quad (2.22)$$

By the monotonicity of $\psi$, $\varpi_r(a) > 0$ for any $a > 0$. The proof of the following lemma is given in Appendix A.1.

Lemma 2.1. For every $A \in \mathbb{R}$, we have

$$\Lambda(A) = -\frac{r}{\Phi_r} K + b \left( \frac{r}{\Phi_r} + \frac{r A - \psi'(0+)}{\Phi_r} \right) + \sum_{i=1}^{N} c_i e^{a_i A} \varpi_r(a_i) + \Psi_f(A). \quad (2.23)$$

In view of (2.23) above, the function $\Lambda(A)$ is clearly continuous and increasing. Therefore, if $\lim_{A \downarrow -\infty} \Lambda(A) < 0 < \lim_{A \uparrow \infty} \Lambda(A)$, there exists a unique root $A^* \in \mathbb{R}$ such that $\Lambda(A^*) = 0$. Otherwise, let $A^* = -\infty$ if $\lim_{A \downarrow -\infty} \Lambda(A) \geq 0$ and let $A^* = \infty$ if $\lim_{A \uparrow \infty} \Lambda(A) \leq 0$.

Remark 2.2. Except for the case $g$ is a constant, because $\Lambda(A)$ increases to $\infty$, we have $A^* < \infty$.

With our assumption on the form of $g$, the value function can be written succinctly. Fix $-\infty < A^* < \infty$. By Proposition 2 of Avram et al. [5], if $\psi'(0+) \in (-\infty, \infty)$,

$$\mathbb{E}^x[e^{-r\tau_A} X_{\tau_A}] = \mathbb{Z}^{(r)}(x) - \psi'(0+) \mathbb{W}^{(r)}(x) - \frac{r - \psi'(0+)}{\Phi_r} \mathbb{W}^{(r)}(x), \quad x \in \mathbb{R},$$

where

$$\mathbb{Z}^{(r)}(x) := \int_{0}^{x} Z^{(r)}(y)dy, \quad x \in \mathbb{R}.$$

This together with (2.5) gives, for any $x, A \in \mathbb{R}$,

$$\mathbb{E}^x[e^{-r\tau_A} X_{\tau_A}] = \mathbb{Z}^{(r)}(x - A) + \left( A - \frac{\psi'(0+)}{r} \right) Z^{(r)}(x - A) + \frac{\psi'(0+)}{r} - \frac{r - \psi'(0+)}{\Phi_r} \frac{r A \Phi_r}{\Phi_r^2} \mathbb{W}^{(r)}(x - A).$$
With the help of Exercise 8.7 (ii) of [23], (2.9) or the sum of the terms of (2.15) becomes
\[
\begin{aligned}
    u_A(x) = K \left( Z(r)(x - A) - \frac{r}{\Phi_r} W(r)(x - A) \right) - \sum_{i=1}^{N} c_i e^{a_i x} \left( Z_{a_i}^{(r-\psi(a_i))}(x - A) - \varpi_r(a_i) W_{a_i}^{(r-\psi(a_i))}(x - A) \right) \\
    - b \left[ Z(r)(x - A) + \left( A - \frac{\psi'(0+)}{r} \right) Z(r)(x - A) + \frac{\psi'(0+)}{r} - r - \frac{\psi'(0+)}{\Phi_r + r A \Phi_r} W(r)(x - A) \right] \\
    + W(r)(x - A) \Psi_f(A) - \Theta_f(x; A).
\end{aligned}
\]

Moreover, if \( A^* \in (-\infty, \infty) \), by how \( A^* \) is chosen as in (2.23) and by (2.7), it can be simplified to
\[
\begin{aligned}
    u_{A^*}(x) = K Z(r)(x - A^*) - b \left[ Z(r)(x - A^*) + \left( A^* - \frac{\psi'(0+)}{r} \right) Z(r)(x - A^*) + \frac{\psi'(0+)}{r} \right] \\
    - \sum_{i=1}^{N} c_i e^{a_i x} Z_{a_i}^{(r-\psi(a_i))}(x - A^*) - \Theta_f(x; A^*).
\end{aligned}
\]

(2.25)

The verification of optimality requires the following smoothness properties, whose proofs are given in Appendix A.2.

**Lemma 2.2.** Suppose \(-\infty < A^* \leq \infty\).

1. \( u_{A^*}(x) \) is \( C^1 \) on \( \mathbb{R} \setminus \{A^*\} \).

2. In particular, when \( X \) is of unbounded variation, \( u_{A^*}(x) \) is \( C^2 \) on \( \mathbb{R} \setminus \{A^*\} \).

Herein, we add a remark concerning continuous/smooth fit. The following remark confirms the results in [19] and further verifies that smooth fit holds whenever \( X \) is of unbounded variation even when \( \sigma = 0 \). This observation only requires the asymptotic behavior of the scale function near zero as in Remark 2.1 (2).

**Remark 2.3 (continuous/smooth fit).** Suppose \(-\infty < A^* < \infty\).

1. Continuous fit holds (i.e. \( u_{A^*}(A^*) = g(A^*) \)) because, by (2.25), \( Z(r)(0) = Z_{a_i}^{(r-\psi(a_i))}(0) = 1 \) and \( \lim_{x \downarrow A^*} \Theta_f(x; A^*) = 0 \).

2. In particular, when \( X \) is of unbounded variation, smooth fit holds (i.e. \( u'_{A^*}(A^*) = g'(A^*) \)) because
\[
\begin{aligned}
    u'_{A^*}(x) &= K r W(r)(x - A^*) - b \left[ Z(r)(x - A^*) + r (A^* - \frac{\psi'(0+)}{r}) W(r)(x - A^*) \right] \\
    &\quad - \sum_{i=1}^{N} c_i e^{a_i x} (r - \psi(a_i)) W_{a_i}^{(r-\psi(a_i))}(x - A^*) - \sum_{i=1}^{N} a_i c_i e^{a_i x} Z_{a_i}^{(r-\psi(a_i))}(x - A^*) - \Theta_f'(x; A^*) \\
    &\xrightarrow{x \downarrow A^*} - b - \sum_{i=1}^{N} a_i c_i e^{a_i A^*} = g'(A^*),
\end{aligned}
\]
\]

thanks to \( W(r)(0) = W_{a_i}^{(r-\psi(a_i))}(0) = 0 \), \( Z(r)(0) = Z_{a_i}^{(r-\psi(a_i))}(0) = 1 \) and \( \lim_{x \downarrow A} \Theta_f'(x; A) = 0 \); see also the proof of Lemma 2.2.

We now state the main results of this subsection. The proof is given in Appendix A.3.

**Proposition 2.1.** (1) If \(-\infty < A^* < \infty\), the stopping time \( \tau_{A^*} := \inf \{ t \geq 0 : X_t \leq A^* \} \) is optimal over \( S \) and the value function is \( u(x) = u_{A^*}(x) \) as in (2.25) for all \( x \in \mathbb{R} \).
(2) If \( A^* = \infty \), immediate stopping is always optimal and \( u(x) = g(x) \) for any \( x \in \mathbb{R} \).

(3) If \( A^* = -\infty \), it is never optimal to stop (i.e. \( \tau^* = \infty \) is optimal), and the value function is given by

\[
u(x) = \int_{-\infty}^{\infty} \left( \Phi'_v e^{-\Phi_v(x-y)} - W^{(r)}(y-x) \right) f(y) dy,
\]

(2.26)

where \( \Phi'_v \) is the derivative of \( \Phi_v \) with respect to \( r \).

2.3. For a general concave and decreasing \( g \). We now relax the assumption on \( g \) and consider a general concave and decreasing function \( g \). We also drop the continuity assumption on \( f \).

**Assumption 2.3.** Suppose

(1) \( f(\cdot) \) is increasing such that \( f(-\infty) := \lim_{x \to -\infty} f(x) > -\infty \) and \( \int_0^\infty e^{-\Phi_v y} f_+(y) dy < \infty \);

(2) \( g(\cdot) \) is twice-differentiable, concave and monotonically decreasing such that (2.14) and (2.19) hold.

Under this assumption, we see that \( \Lambda(A) \) is increasing. Indeed, we have by assumption

\[
\frac{\partial}{\partial A} \left[ -\frac{r}{\Phi_v} g(A) - \frac{\sigma^2}{2} g'(A) \right] = -\frac{r}{\Phi_v} g'(A) - \frac{\sigma^2}{2} g''(A) \geq 0.
\]

Moreover, \( \rho_{g,A}^{(r)} \) is increasing by the concavity of \( g \). On the other hand, \( \Psi_f(A) \) is increasing because \( f \) is. Therefore, we again define \( A^* \) in the same way as the unique root of \( \Lambda(A) = 0 \) (if it exists). The proof of the following result is given in Appendix A.4.

**Proposition 2.2.** Suppose Assumption 2.3.

(1) When \(-\infty < A^* < \infty\), then \( \tau_A^* \) is optimal over \( \tilde{S} \) and the value function is given by

\[
\bar{u}(x) = u_{A^*}(x) = g(A^*) Z^{(r)}(x - A^*) + W^{(r)}(x - A^*) \frac{\sigma^2}{2} g'(A^*) - \varphi_{g,A^*}^{(r)}(x) - \Theta_f(x; A^*), \quad x > A^*.
\]

For \( x \leq A^* \), we have \( \bar{u}(x) = g(x) \).

(2) If \( A^* = \infty \), immediate stopping is always optimal and \( \bar{u}(x) = g(x) \) for any \( x \in \mathbb{R} \).

(3) If \( A^* = -\infty \), then \( \tau^* = \infty \) is optimal over \( \tilde{S} \) and (2.26) holds.

3. MULTIPLE-STAGE PROBLEM

In this section, we extend to the scenario the firm can decrease its involvement in the project in multiple stages as defined in (1.3). As in the one-stage case, we consider two modes of optimality:

\[
U^{(M)}(x) := \sup_{(\tau(1), \ldots, \tau(M)) \in \mathcal{S}_M} \sum_{m=1}^M \mathbb{E}^x \left[ \int_{\tau(m-1)}^{\tau(m)} e^{-rt} F_m(X_t) dt + e^{-r\tau(m)} g_m(X_{\tau(m)}) 1_{\{\tau(m) < \infty\}} \right],
\]

(3.1)

\[
\bar{U}^{(M)}(x) := \sup_{(\tau(1), \ldots, \tau(M)) \in \tilde{\mathcal{S}}_M} \sum_{m=1}^M \mathbb{E}^x \left[ \int_{\tau(m-1)}^{\tau(m)} e^{-rt} F_m(X_t) dt + e^{-r\tau(m)} g_m(X_{\tau(m)}) 1_{\{\tau(m) < \infty\}} \right],
\]

(3.2)

for all \( x \in \mathbb{R} \) where we define \( \tau^{(0)} := 0 \) for notational brevity and the supremum is, respectively, over the set of increasing sequences of \( M \) stopping times,

\[
\mathcal{S}_M := \{ \tau(m) \in \mathcal{S}, 1 \leq m \leq M : \tau^{(1)} \leq \cdots \leq \tau^{(M)} \},
\]
and over the set of increasing sequences of $M$ down-crossing times,
\[ \tilde{S}_M := \{ \tau^{(m)} = \tau_{Am} \in \tilde{S}, 1 \leq m \leq M : A_1 \geq A_2 \cdots \geq A_M \}. \]

Clearly, \( \tilde{S}_M \subset S_M \) and hence \( \tilde{U}^{(M)} \leq U^{(M)} \).

We first consider the case \( g_m \) admits the form
\[ g_m(x) := K_m - b_mx - \sum_{i=1}^{N_m} c_{mi}e^{\alpha_{mi}x}, \quad 1 \leq m \leq M, \quad (3.3) \]
for some constants \( K_m \in \mathbb{R}, b_m \geq 0, c_{mi}, \alpha_{mi} > 0, 1 \leq i \leq N_m \), and show the optimality in the sense of (3.1) as an extension of Proposition 2.1. We then consider a more general case where \( g_m \) is twice-differentiable, concave and monotonically decreasing and show the optimality over \( \tilde{S}_M \) as an extension of Proposition 2.2. Regarding the running reward function \( F \), define the differences:
\[ f_m := F_m - F_{m+1}, \quad 1 \leq m \leq M, \]
with \( F_{M+1} \equiv 0 \). As is also assumed in [10], we consider the case \( f_m \) is increasing. Using the notation as in (2.3), we can then write for all \( x \in \mathbb{R} \)
\begin{align*}
U^{(M)}(x) &= \sup_{(\tau^{(1)}, \ldots, \tau^{(M)}) \in \tilde{S}_M} \sum_{m=1}^{M} u(x, \tau^{(m)}; f_m, g_m), \\
\tilde{U}^{(M)}(x) &= \sup_{(\tau^{(1)}, \ldots, \tau^{(M)}) \in \tilde{S}_M} \sum_{m=1}^{M} u(x, \tau^{(m)}; f_m, g_m).
\end{align*}

(3.4) (3.5)

In summary, we assume Assumptions 3.1 and 3.2 below for (3.1) and (3.2), respectively.

**Assumption 3.1.** For each \( 1 \leq m \leq M \), we assume that \( f_m \) and \( g_m \) satisfy Assumption 2.2.

**Assumption 3.2.** For each \( 1 \leq m \leq M \), we assume that \( f_m \) and \( g_m \) satisfy Assumption 2.3.

As is clear from the problem structure, simultaneous stoppings (i.e. \( \tau_k = \cdots = \tau_{k+l} \) a.s. for some \( k \) and \( l \)) may be optimal in case it is not advantageous to stay in some intermediate stages (i.e. stages \( k+1, \ldots, k+l \)). For this reason, define, for any subinterval \( I = \{\min I, \min I + 1, \ldots, \max I\} \subset \{1, \ldots, M\} \),
\[ g_I := \sum_{i \in I} g_i \quad \text{and} \quad f_I := F_{\min I} - F_{\max I+1}, \quad (3.6) \]
and consider an auxiliary one-stage problem (1.2) with \( g = g_I \) and \( f = f_I \). Notice that Assumption 3.1 (resp. Assumption 3.2) guarantees that \( f_I \) and \( g_I \) also satisfy Assumption 2.2 (resp. Assumption 2.3) for any \( I \). Hence Propositions 2.1 and 2.2 apply.

Let
\[ \Lambda_m(A) := \Lambda(A; f_m, g_m), \quad A \in \mathbb{R}, 1 \leq m \leq M, \quad (3.7) \]
as the function (2.18) for \( (f_m, g_m) \). Because \( \rho_{h_1+h_2,A}^{(r)} \equiv \rho_{h_1,A}^{(r)} + \rho_{h_2,A}^{(r)} \) and \( \Psi_{h_1+h_2}(A) \equiv \Psi_{h_1}(A) + \Psi_{h_2}(A) \) for any measurable functions \( h_1 \) and \( h_2 \) in view of (2.10) and (2.12), we see that
\[ \Lambda_I(A) := \Lambda(A; f_I, g_I) = \Lambda \left( A; \sum_{m \in I} f_m, \sum_{m \in I} g_m \right) = \sum_{m \in I} \Lambda_m(A) \quad (3.8) \]
We shall consider the cases (i) $U$-Two-stage problem. optimal. For (ii), we shall show that simultaneous stoppings are optimal. We first consider the former.

Suppose Assumption 3.2. We set $A$ and the stopping time $I = \Lambda_{A}^{-\infty} = \Lambda_{A}^{-\infty}, x > A$ and obtain $u_I(x) = \inf \{t > 0 : X_t \leq A_x^* \}$ is optimal.

If $A_x^* = \infty$, $u_I(x) = g_I(x)$ for any $x \in \mathbb{R}$ with optimal stopping time $\tau^* = 0$.

If $A_x^* = -\infty$, it is never optimal to stop, and the value function is given by

$$u_I(x) = \int_{-\infty}^{\infty} \left( \Phi^r_x e^{-\Phi^r_x(y-x)} - W^r(y-x) \right) f_I(y) dy. \tag{3.9}$$

Suppose Assumption 3.2.

If $-\infty < A_x^* < \infty$, then

$$\bar{u}_I(x) = u_A^* x \sum_{m \in I} \left( K_m Z^r(x - A_x^*) - b_m \left[ Z^r(x - A_x^*) + A_x^* - \frac{\psi'(0+)}{r} \right] Z^r(x - A_x^*) + \frac{\psi'(0+)}{r} \right)$$

$$- \sum_{i=1}^{N_m} c_{mi} e^{a_{mi} x} Z^r_{a_{mi}} (x - A_x^*)^{-\psi(a_{mi})}) (x - A_x^*) - \Theta_{f_I}(x; A_x^*),$$

and the stopping time $\tau_{A_x^*} := \inf \{t > 0 : X_t \leq A_x^* \}$ is optimal.

(2) If $A_x^* = \infty$, $\bar{u}_I(x) = g_I(x)$ for any $x \in \mathbb{R}$ with optimal stopping time $\tau^* = 0$.

(3) If $A_x^* = -\infty$, then $\tau^* = \infty$ is optimal over $\mathcal{S}$ and (3.9) holds.

3.1. **Two-stage problem.** In order to gain intuition, we first consider the case with $M = 2$ and obtain $U^{(2)}(x)$ and $\bar{U}^{(2)}(x)$ under Assumptions 3.1 and 3.2, respectively. Following the procedures discussed above, $A_x^* \in [-\infty, \infty]$, or the root of $\Lambda_m(A) = 0$, is well-defined for $m = 1, 2$. As a special case of (3.6),

$$f_2 \equiv F_2, \quad f_1 \equiv F_1 - F_2 \equiv F_1 - f_2, \quad \text{and} \quad f_{(1,2)} \equiv F_1 \equiv f_1 + f_2. \tag{3.10}$$

We shall consider the cases (i) $A_x^+ > A_x^*$ and (ii) $A_x^+ \leq A_x^*$, separately. For (i), we shall show that $(\tau_{A_x^+}, \tau_{A_x^*})$ is optimal. For (ii), we shall show that simultaneous stoppings are optimal. We first consider the former.
Proposition 3.1. If \( \infty \geq A_1^* > A_2^* \geq -\infty \), then \((\tau_{A_1^*}, \tau_{A_2^*})\) is optimal; the value function is given by \( U^{(2)}(x) = \sum_{m=1,2} u^{(m)}_{A_m}(x) \) and \( \bar{U}^{(2)}(x) = \sum_{m=1,2} u^{(m)}_{A_m}(x) \) under Assumptions 3.1 and 3.2, respectively. In particular, under Assumption 3.1 and if \( \infty > A_1^* > A_2^* > -\infty \),

\[
U^{(2)}(x) = \sum_{m=1,2} \left( K_m Z^{(r)}(x - A_m^*) - b_m \left[ Z^{(r)}(x - A_m^*) + \left( A_m^* - \frac{\psi'(0+)}{r} \right) Z^{(r)}(x - A_m^*) + \frac{\psi'(0+)}{r} \right] \right.
\]

\[
- \sum_{i=1}^{N_m} c_{mi} e^{a_{mi} x} Z^{(r - \psi(a_{mi})} (x - A_m^*) \left] - \int_{A_1^*}^{x} W^{(r)}(x - y) F_1(y) dy - \int_{A_2^*}^{x} W^{(r)}(x - y) F_2(y) dy. \right.
\]

(3.11)

Proof. Suppose Assumption 3.1 holds. By relaxing the constraint that \( \tau^{(1)} \leq \tau^{(2)} \), we can obtain an upper bound:

\[
U^{(2)}(x) \leq \bar{U}^{(2)}(x) := \sum_{m=1,2} \sup_{\tau^{(m)} \in S} \chi(x, \tau^{(m)}; f_m, g_m) = \sum_{m=1,2} u^{(m)}_{A_m^*}(x),
\]

where the last equality holds by Corollary 3.1. On the other hand, because \( \tau_{A_1^*} \leq \tau_{A_2^*} \) a.s. (hence \( (\tau_{A_1^*}, \tau_{A_2^*}) \in S_2 \)) thanks to \( A_1^* > A_2^* \), we have \( U^{(2)}(x) \geq \bar{U}^{(2)}(x) \), as desired. The same result holds under Assumption 3.2 by relaxing the constraint that \( A_1 \geq A_2 \) and noticing that \( (\tau_{A_1^*}, \tau_{A_2^*}) \in \bar{S}_2 \).

For the second claim, because \( A_1^* > A_2^* \) and by (3.10),

\[
\sum_{m=1,2} \Theta_{f_m}(x, A_m^*) = \sum_{m=1,2} \int_{A_m^*}^{x} W^{(r)}(x - y) f_m(y) dy = \int_{A_1^*}^{x} W^{(r)}(x - y) F_1(y) dy + \int_{A_2^*}^{x} W^{(r)}(x - y) F_2(y) dy,
\]

and hence (3.11) holds in view of Corollary 3.1.

\[\square\]

Now consider the case \(-\infty \leq A_1^* \leq A_2^* \leq \infty \).

Lemma 3.1. Suppose \(-\infty \leq A_1^* \leq A_2^* \leq \infty \). Under Assumption 3.1 (resp. Assumption 3.2), the first optimal stopping cannot occur on \((A_2^*, \infty)\); namely if \( t^{*} \) is the optimal first stopping time in the sense of (3.1) (resp. (3.2)), then \( X_{t^{*}}(1) \in (-\infty, A_2^*] \) a.s. on \( \{ t^{*} < \infty \} \).

Proof. The result is immediate when \( A_2^* = \infty \) and hence we assume \( A_2^* < \infty \).

Suppose Assumption 3.1 holds, and in order to derive a contradiction, we suppose there exists some \( \hat{x} > A_2^* \) at which it is optimal to stop. Under this assumption, the value function must satisfy

\[
U^{(2)}(\hat{x}) = g_1(\hat{x}) + \sup_{\tau \in S} u(\hat{x}, \tau; f_2, g_2) = g_1(\hat{x}) + u^{(2)}_{A_2^*}(\hat{x}).
\]

(3.12)

We shall show that this is in fact smaller than \( u^{(1)}_{A_2^*}(\hat{x}) + u^{(2)}_{A_2^*}(\hat{x}) \), which is the value obtained by \( (\tau^{(1)}, \tau^{(2)}) = (\tau_{A_2^*}, \tau_{A_2^*}) \in \bar{S}_2 \subset S_2 \). By (2.17) and (2.20),

\[
\Lambda_1(A) \leq (\geq) 0 \Rightarrow \frac{\partial}{\partial A} u^{(1)}_{A}(\hat{x}) \geq (\leq) 0, \quad \forall A < \hat{x},
\]

(3.13)

\[
u^{(1)}(A+) = g_1(A) + W^{(r)}(0) \Lambda_1(A).
\]

(3.14)
By (3.13)-(3.14) and because $A_1^* < A_2^* < \hat{x}$ and $\Lambda_1$ is increasing,
\[
    u_{A_2^*}^{(1)}(\hat{x}) > \lim_{\Lambda_{A_2^*} \uparrow} u_{A_1^*}^{(1)}(\hat{x}) = g_1(\hat{x}) + W^{(r)}(0)\Lambda_1(\hat{x}) \geq g_1(\hat{x}).
\]

Regarding the last inequality, for the unbounded variation case, it holds because $W^{(r)}(0) = 0$ by Remark 2.1 (2).

For the bounded variation case, it also holds because (3.13) and $\hat{x} > A_1^*$ imply $\Lambda_1(\hat{x}) > 0$. Therefore, we get, by (3.12), $U^{(2)}(\hat{x}) < u_{A_2^*}^{(1)}(\hat{x}) + u_{A_2^*}^{(2)}(\hat{x})$ leading to a contradiction. Because $\hat{x}$ is arbitrary on $(A_1^*, \infty)$, we have the claim. The same contradiction can be derived under Assumption 3.2 because $(\tau_{A_2^*}, \tau_{A_2^*}) \in \tilde{S}_2$.

The following lemma suggests under $-\infty \leq A_1^* \leq A_2^* \leq \infty$ that the optimal strategy is the simultaneous stopping corresponding to the threshold level $A_1^*$, which is the value that makes $\Lambda_{\{1,2\}} \equiv \Lambda_1 + \Lambda_2$ as in (3.8) vanish.

**Proposition 3.2.** Suppose $-\infty \leq A_1^* \leq A_2^* \leq \infty$.

1. We have $A_1^* \leq A_{\{1,2\}} \leq A_2^*$.

2. It is optimal to stop simultaneously and the value function is given by $U^{(2)}(x) = u_{A_{\{1,2\}}^*}^{(1,2)}(x)$ under Assumption 3.1 and $\tilde{U}^{(2)}(x) = u_{A_{\{1,2\}}^*}^{(1,2)}(x)$ under Assumption 3.2.

**Proof.**

(1) Because both $\Lambda_1$ and $\Lambda_2$ are increasing, $\Lambda_{\{1,2\}}$ is increasing as well. Because $A_1^* \leq A_2^*$, $\Lambda_1(A_2^*) \geq 0$ and hence $\Lambda_{\{1,2\}}(A_2^*) \geq 0$. Similarly, $\Lambda_{\{1,2\}}(A_1^*) \leq 0$. The increasing property of $\Lambda_{\{1,2\}}$ now shows the claim.

(2) Under Assumption 3.1, for any pair of stopping times $(\tau^{(1)}, \tau^{(2)}) \in S_2$, because $F_2 = f_2$ as in (3.10) and by the strong Markov property of the Lévy process $X$,

\[
    \mathbb{E}^x \left[ \sum_{m=1,2} e^{-r\tau^{(m)}} g_m(X_{\tau^{(m)}}) 1_{\{\tau^{(m)} < \infty\}} + \int_{\tau^{(1)}}^{\tau^{(2)}} e^{-rt} F_1(X_t) dt + \int_{\tau^{(2)}} e^{-rt} F_2(X_t) dt \right]
    = \mathbb{E}^x \left[ e^{-r\tau^{(1)}} g_1(X_{\tau^{(1)}}) 1_{\{\tau^{(1)} < \infty\}} + \int_{\tau^{(1)}}^{\tau^{(2)}} e^{-rt} F_1(X_t) dt 
        + 1_{\{\tau^{(1)} < \infty\}} e^{-r(\tau^{(2)} - \tau^{(1)})} \mathbb{E} \left[ e^{-r(\tau^{(2)} - \tau^{(1)})} g_2(X_{\tau^{(2)}}) 1_{\{\tau^{(2)} < \infty\}} + \int_{\tau^{(2)}}^{\tau^{(1)}} e^{-rt} F_2(X_t) dt \big| F_1(\tau^{(1)}) \right] \right]
    \leq \mathbb{E}^x \left[ e^{-r\tau^{(1)}} g_1(X_{\tau^{(1)}}) 1_{\{\tau^{(1)} < \infty\}} + \int_{\tau^{(1)}}^{\tau^{(2)}} e^{-rt} F_1(X_t) dt + 1_{\{\tau^{(1)} < \infty\}} e^{-r\tau^{(1)}} \sup_{\tau \in S} u(X_{\tau^{(1)}}, \tau; f_2, g_2) \right]
    = u(x, \tau^{(1)}; F_1, g_1 + u_{A_2^*}^{(2)}).
\]

Similarly, under Assumption 3.2, (3.15) also holds for any $(\tau^{(1)}, \tau^{(2)}) \in \tilde{S}_2$ by replacing $S$ with $\tilde{S}$ in the expectation of the third term. This together with Lemma 3.1, shows $U^{(2)}(x)$ (resp. $\tilde{U}^{(2)}(x)$) is less than or equal to

\[
    \sup_{\tau \in S(A_2^*)} u(x, \tau; F_1, g_1 + u_{A_2^*}^{(2)})
\]

under Assumption 3.1 (resp. Assumption 3.2) where $S(A_2^*)$ is the set of $\tau \in S$ (resp. $\tau \in \tilde{S}$) such that $X_{\tau} \in (-\infty, A_2^*)$ a.s. on $\{\tau < \infty\}$. Because, for any $\tau \in S(A_2^*)$, $u_{A_2^*}^{(2)}(X_{\tau}) = g_2(X_{\tau})$ a.s. on $\{\tau < \infty\}$ and because
$F_1 = f_{\{1,2\}}$ as in (3.10), (3.16) equals
\[
\sup_{\tau \in \mathcal{S}(A^*_2)} u(x, \tau; f_{\{1,2\}}, g_{\{1,2\}}) \leq \sup_{\tau \in \mathcal{S}} u(x, \tau; f_{\{1,2\}}, g_{\{1,2\}}) = u^{\{1,2\}}_{A^*_1}(x),
\]
by Corollary 3.1 and because $\mathcal{S}(A^*_2) \subset \mathcal{S}$. Namely, $U^{(2)}(x) \leq u^{\{1,2\}}_{A^*_1}(x)$ under Assumption 3.1 and $\bar{U}^{(2)}(x) \leq u^{\{1,2\}}_{A^*_1}(x)$ under Assumption 3.2. These in fact hold with equality because $u^{\{1,2\}}_{A^*_1}(x)$ is attained by $(\tau_{A^*_1}, \tau_{A^*_1}) \in \tilde{S}_2 \subset S_2$.

\[\square\]

3.2. Multiple-stage problem. We now generalize to the multiple-stage problem and solve (3.1)-(3.2) or equivalently (3.4)-(3.5) with $M \geq 3$. For $1 \leq m \leq M$, let
\[
U^{(M)}_m(x) := \sup_{(\tau^{(m)}, \ldots, \tau^{(M)}) \in \mathcal{S}_{M-m+1}} \sum_{k=m}^{M} u(x, \tau^{(k)}; f_k, g_k), \tag{3.17}
\]
\[
\bar{U}^{(M)}_m(x) := \sup_{(\tau^{(m)}, \ldots, \tau^{(M)}) \in \tilde{S}_{M-m+1}} \sum_{k=m}^{M} u(x, \tau^{(k)}; f_k, g_k). \tag{3.18}
\]
In particular, $U^{(M)}_1 \equiv U^{(M)}_1$ and $\bar{U}^{(M)}_1 \equiv \bar{U}^{(M)}_1$, and by Corollary 3.1
\[
U^{(M)}_M(x) = \sup_{\tau \in \mathcal{S}} u(x, \tau; f_M, g_M) = u^{(M)}_{A^*_M}(x) \quad \text{and} \quad \bar{U}^{(M)}_M(x) = \sup_{\tau \in \tilde{S}} u(x, \tau; f_M, g_M) = u^{(M)}_{A^*_M}(x), \tag{3.19}
\]
under Assumptions 3.1 and 3.2, respectively. The expressions for $U^{(M)}_{M-1}$ and $\bar{U}^{(M)}_{M-1}$ can also be obtained as in the two-stage case.

Given $1 \leq m \leq M$, let us partition $\{m, m+1, \ldots, M\}$ to an $L(m)$ number of (non-empty) disjoint sets $\mathcal{I}_m := \{\mathcal{I}(k; m), 1 \leq k \leq L(m)\}$ such that
\[
\{m, m+1, \ldots, M\} = \mathcal{I}(1; m) \cup \cdots \cup \mathcal{I}(L(m); m)
\]
where, if $L(m) = 1, \mathcal{I}(1; m) = \{m, \ldots, M\}$ and, if $L(m) \geq 2$,
\[
\mathcal{I}(1; m) := \{m, \ldots, n_{1,m} - 1\}, \\
\mathcal{I}(l; m) := \{n_{l-1,m}, \ldots, n_{l,m} - 1\}, \quad 2 \leq l \leq L(m) - 1, \\
\mathcal{I}(L(m); m) := \{n_{L(m)-1,m}, \ldots, M\},
\]
for some integers $m < n_{1,m} < \cdots < n_{L(m)-1,m} < M$. We consider the strategy such that, if $k$ and $l$ are in the same set, then the $k$-th and $l$-th stops occur simultaneously a.s.

We shall show that (3.17) and (3.18), for any $1 \leq m \leq M$, can be solved by a strategy with some partition $\mathcal{I}^*_m := \{\mathcal{I}^*(k; m), 1 \leq k \leq L^*(m)\}$ satisfying
\[
A^*_{\mathcal{I}^*(1; m)} > \cdots > A^*_{\mathcal{I}^*(L^*(m); m)},
\]
where $A^*_2$ is defined as in (3.8) for any set $\mathcal{I}$. The corresponding expected value becomes
\[
U^{(M)}_{m, \mathcal{I}_m}(x) := \sum_{k=1}^{L^*(m)} u(x, \tau_{A^*_2(k; m)}; f_{\mathcal{I}^*(k; m)}, g_{\mathcal{I}^*(k; m)}) = \sum_{k=1}^{L^*(m)} u^{\mathcal{I}^*(k; m)}_{A^*_2(k; m)}(x), \tag{3.20}
\]
whose strategy is given by for any \( m \leq n \leq M \),

\[
\tau^*(n) = \tau A^*_I(k,m) \quad \text{for the unique } 1 \leq k \leq L^*(m) \text{ such that } n \in I^*(k;m).
\]

We shall show that (3.20) is optimal, i.e. \( U_m^{(M)} = U_{m,I_m}^{(M)} \) under Assumption 3.1 and \( \bar{U}_m^{(M)} = U_{m,I_m}^{(M)} \) under Assumption 3.2 for any \( 1 \leq m \leq M \). Moreover, \( I^*_m \) can be obtained inductively moving backwards starting from \( I^*_M \) with \( L^*(M) = 1 \) and \( I^*(1;M) = \{M\} \). For the inductive step, the following algorithm outputs \( I^*_{m-1} \) from \( I^*_m \) for any \( 2 \leq m \leq M \). By repeating this, we can obtain the partition \( I^*_1 \); the resulting \( U_{1,I^*_1}^{(M)} \) as in (3.20) becomes the value function \( U^{(M)} = U_1^{(M)} \).

---

**Algorithm** \( I^*_{m-1} = \text{Update}(I^*_m, m) \)

**Step 1:** Set \( i = 1 \).

**Step 2:** Set

\[
\hat{I} := \begin{cases} 
(m - 1), & i = 1, \\
\{m - 1\} \cup I^*(1;m) \cup \cdots \cup I^*(i - 1;m), & i \geq 2.
\end{cases}
\]

**Step 3:** Compute \( A^*_I \) and

1. if \( i = L^*(m) + 1 \), then **stop and return** \( I^*_{m-1} = \{I^*(1;m - 1)\} \) with \( L^*(m - 1) = 1 \) and \( I^*(1;m - 1) = \{m - 1, \ldots, M\} \);
2. if \( A^*_I > A^*_I(i;m) \), then **stop and return** \( I^*_{m-1} = \{I^*(k;m - 1), 1 \leq k \leq L^*(m - 1)\} \) with \( L^*(m - 1) = L^*(m) - i + 2 \) and

\[
I^*(1;m - 1) = \hat{I} \quad \text{and} \quad I^*(l;m - 1) = I^*(l + i - 2;m), \quad 2 \leq l \leq L^*(m - 1);
\]

3. if \( A^*_I \leq A^*_I(i;m) \), set \( i = i + 1 \) and go back to **Step 2**.

---

The role of the algorithm is in words to extend from \( n(= M - m + 1) \)-stage problem to \( n + 1(= M - m + 2) \)-stage problem. The idea is similar to what we discussed in the previous section on how to extend from a one-stage problem to a two-stage problem. When a new initial stage is added, the corresponding threshold value \( A^*_I \) is first calculated. Depending on whether its value is higher than that of the subsequent stages or not, simultaneous stopplings may become optimal. For \( n \) larger than two, we must solve it recursively by keeping updating the set \( \hat{I} \), or the set of the first (simultaneous) stopplings, as given in this algorithm. If \( A^*_I \) is low, the strategy of the new initial stage may naturally depend on the strategies of all the subsequent stages. Unlike the extension to the two-stage problem which only needs to take into account the strategy of the stage immediately next, it needs to reflect the strategies of all subsequent stages.

We prove the following under Assumption 3.1 for the optimality (3.1). As is already clear after the detailed discussion on the two-stage case, only a slight modification is needed for (3.2) under Assumption 3.2.
Lemma 3.2. In view of the algorithm above, suppose Assumption 3.1 and fix $2 \leq m \leq M$. Given that $\mathcal{I}_m^*$ satisfies, for every $1 \leq l \leq L^*(m)$,

$$U_{\min \mathcal{I}^* (l;m)}^{(M)}(x) = \sum_{k=l}^{L^*(m)} u_{A_{\mathcal{I}^* (k;m)}}(x),$$ \hspace{1cm} (3.22)

and is used as an input in the algorithm. Then, we have the following.

(1) At the end of Step 2, if $1 \leq i \leq L^*(m)$,

$$U_{m-1}^{(M)}(x) \leq \sup_{\tau \in \mathcal{S}} \left[ u(x, \tau; f_{\hat{I}}, g_{\hat{I}}) + \sum_{k=i}^{L^*(m)} u(x, \vartheta_{I}(A_{\hat{I}^* (k;m)}); f_{\hat{I}^* (k;m)}, g_{\hat{I}^* (k;m)}) \right],$$ \hspace{1cm} (3.23)

where $\vartheta_{I}(A) := \nu_{A} \circ \theta_{I}$ for any $\nu \in \mathcal{S}$ and $A \in \mathbb{R}$ with the time-shift operator $\theta_{I}$, and if $i = L^*(m) + 1$

$$U_{m-1}^{(M)}(x) = \sup_{\tau \in \mathcal{S}} u(x, \tau; f_{\hat{I}}, g_{\hat{I}}) = u_{\{m-1, \ldots, M\}^*}(x).$$

(2) Let $\mathcal{I}_{m-1}^*$ be produced by the algorithm. For any $1 \leq l \leq L^*(m-1)$,

$$U_{\min \mathcal{I}^* (l;m-1)}^{(M)}(x) = \sum_{k=l}^{L^*(m-1)} u_{A_{\mathcal{I}^* (k;m-1)}}(x).$$ \hspace{1cm} (3.24)

Proof. (1) We shall show by mathematical induction.

(Base-step) Suppose $i = 1$. By our assumption (3.22) and by an argument similar to (3.15),

$$U_{m-1}^{(M)}(x) \leq \sup_{\tau \in \mathcal{S}} \mathbb{E}^x \left[ e^{-\rho \tau} g_{m-1}(X_{\tau}) 1_{\{\tau < \infty\}}^\tau + \int_0^\tau e^{-\rho s} F_{m-1}(X_s) ds + e^{-\rho \tau} U_{\min \mathcal{I}^* (1;m)}^{(M)}(X_{\tau}) 1_{\{\tau < \infty\}} \right]$$

$$= \sup_{\tau \in \mathcal{S}} \left[ u(x, \tau; f_{m-1}, g_{m-1}) + \sum_{k=1}^{L^*(m)} u(x, \vartheta_{I}(A_{\hat{I}^* (k;m)}); f_{\hat{I}^* (k;m)}, g_{\hat{I}^* (k;m)}) \right].$$

Now (3.23) holds because $\hat{I} = \{m - 1\}$ for $i = 1$.

(Inductive-step) Now we assume (3.23) for $i = j \leq L^*(m) - 1$, i.e., $\hat{I} = \{m-1\} \cup \mathcal{I}^* (1; m) \cup \cdots \cup \mathcal{I}^* (j-1; m)$ and

$$U_{m-1}^{(M)}(x) \leq \sup_{\tau \in \mathcal{S}} \left[ u(x, \tau; f_{\hat{I}}, g_{\hat{I}}) + \sum_{k=j}^{L^*(m)} u(x, \vartheta_{I}(A_{\hat{I}^* (k;m)}); f_{\hat{I}^* (k;m)}, g_{\hat{I}^* (k;m)}) \right],$$ \hspace{1cm} (3.25)

and show that it will hold for $i = j + 1$.

Because when $A_{\hat{I}} > A_{\hat{I}^* (j;m)}$, the algorithm stops at $j$ and never returns to Step 2, we suppose here that $A_{\hat{I}} \leq A_{\hat{I}^* (j;m)}$. In view of the right-hand side of (3.25), if there exists some $\hat{x} > A_{\hat{I}^* (j;m)}$ at which it is optimal to stop, then the value function becomes $g_{\hat{x}}(\hat{x}) + U_{\min \mathcal{I}^* (j;m)}^{(M)}(\hat{x})$ by our assumption (3.22). Using the same reasoning as in Lemma 3.1, this is in fact smaller than $u_{A_{\hat{I}^* (j;m)}}(\hat{x}) + U_{\min \mathcal{I}^* (j;m)}^{(M)}(\hat{x})$. Hence is is never optimal to stop on $(A_{\hat{I}^* (j;m)}, \infty)$ for the optimization problem on the right-hand side of (3.25) (see also the proof of Proposition 3.2).

Now let $\mathcal{S}(A_{\hat{I}^* (j;m)})$ be the set of all stopping times at which $X \in (-\infty, A_{\hat{I}^* (j;m)})$ a.s. For all $\tau \in \mathcal{S}(A_{\hat{I}^* (j;m)})$, we have $\tau = \vartheta_{I}(A_{\hat{I}^* (j;m)})$ a.s. and hence $u(x, \vartheta_{I}(A_{\hat{I}^* (j;m)}); f_{\hat{I}^* (j;m)}, g_{\hat{I}^* (j;m)}) = u(x, \tau; f_{\hat{I}^* (j;m)}, g_{\hat{I}^* (j;m)})$. 

Therefore (3.25) implies
\[
U^{(M)}_{m-1}(x) \leq \sup_{\tau \in S(A^{*}_{(i,m)})} \left[ u(x, \tau; f_{\mathcal{I}^{*}(j,m)}, g_{\mathcal{I}^{*}(j,m)}) + \sum_{k=j+1}^{L^{*}(m)} u(x, \vartheta_{\tau}(A^{*}_{(k,m)}); f_{\mathcal{I}^{*}(k,m)}; g_{\mathcal{I}^{*}(k,m)}) \right]
\]

\[
\leq \sup_{\tau \in S} \left[ u(x, \tau; f_{\mathcal{I}^{*}(j,m)}, g_{\mathcal{I}^{*}(j,m)}) + \sum_{k=j+1}^{L^{*}(m)} u(x, \vartheta_{\tau}(A^{*}_{(k,m)}); f_{\mathcal{I}^{*}(k,m)}; g_{\mathcal{I}^{*}(k,m)}) \right].
\]

Hence, (3.23) holds for \( i = j + 1 \), as desired. This proves (1) by mathematical induction.

(2) When the algorithm stops, it is either (i) \( i = L^{*}(m) + 1 \) at Step 3 (1) or (ii) \( A^{*}_{l} > A^{*}_{(i,m)} \) at Step 3 (2).

(i) Suppose \( i = L^{*}(m) + 1 \). In this case, \( \mathcal{I} = \{m - 1, \ldots, M\} \) and, by (3.23),
\[
U^{(M)}_{\min \mathcal{I}^{*}(i;m)}(x) = U^{(M)}_{m-1}(x) \leq \sup_{\tau \in S} u(x, \tau; f_{\mathcal{I}^{*}(m-1,m)}, g_{\mathcal{I}^{*}(m-1,m)}) = u_{A^{*}_{(m-1,m)}}(x),
\]
which in fact holds by equality because the right-hand side is attained by \( (\tau A^{*}_{(m-1,m)}, \ldots, \tau A^{*}_{(m-1,m)}) \in \mathcal{S}_{M-m+2} \subset \mathcal{S}_{M-m+2} \).

(ii) Suppose the algorithm exits at \( i \) with \( A^{*}_{l} > A^{*}_{(i,m)} \). By (3.23), we have
\[
U^{(M)}_{m-1}(x) \leq \sup_{\tau \in S} u(x, \tau; f_{\mathcal{I}^{*}(m-1,m)}, g_{\mathcal{I}^{*}(m-1,m)}) + \sup_{\tau \in S} \sum_{k=1}^{L^{*}(m)} u(x, \vartheta_{\tau}(A^{*}_{(k,m)}); f_{\mathcal{I}^{*}(k,m)}; g_{\mathcal{I}^{*}(k,m)}).
\]

Regarding the second supremum of the right-hand side, the strategy \( \{\tau^{(l)}; \min \mathcal{I}^{*}(i,m) \leq l \leq M\} \), defined by \( \tau^{(l)} = \vartheta_{\tau}(A^{*}_{(k,m)}) \) for the unique \( i \leq k \leq L^{*}(m) \) such that \( l \in \mathcal{I}^{*}(k,m) \), is feasible (or in \( \mathcal{S}_{M+1-\min \mathcal{I}^{*}(i,m)} \)) for any stopping time \( \tau \in S \) and therefore
\[
\sup_{\tau \in S} \sum_{k=1}^{L^{*}(m)} u(x, \vartheta_{\tau}(A^{*}_{(k,m)}); f_{\mathcal{I}^{*}(k,m)}; g_{\mathcal{I}^{*}(k,m)})
\]
\[
\leq \sup_{(\tau^{(\min \mathcal{I}^{*}(i,m)}, \ldots, \tau^{(M)}) \in \mathcal{S}_{M+1-\min \mathcal{I}^{*}(i,m)}} \sum_{k=\min \mathcal{I}^{*}(i,m)}^{M} u(x, \tau(k); f_{k}, g_{k}) = U^{(M)}_{\min \mathcal{I}^{*}(i;m)}(x).
\]

Hence, we obtain a bound \( U^{(M)}_{m-1}(x) \leq u^{*}_{A^{*}_{l}}(x) + U^{(M)}_{\min \mathcal{I}^{*}(i;m)}(x) \). This together with (3.21) and (3.22) shows
\[
U^{(M)}_{m-1}(x) \leq u^{*}_{A^{*}_{l}}(x) + \sum_{k=1}^{L^{*}(m)} u_{A^{*}_{(k,m)}}(x) = \sum_{k=1}^{L^{*}(m-1)} u_{A^{*}_{(k,m-1)}}(x).
\]
This holds by equality because the left-hand side is attained by a feasible strategy defined by \( \mathcal{I}^{*}_{m-1} \). This shows (3.24) for case \( l = 1 \).

On the other hand, for any \( 2 \leq l \leq L^{*}(m-1) \), by (3.21) and (3.22),
\[
U^{(M)}_{\min \mathcal{I}^{*}(i;m-1)}(x) = U^{(M)}_{\min \mathcal{I}^{*}(l+i-2,m)}(x) = \sum_{k=l+1}^{L^{*}(m)} u_{A^{*}_{(k,m)}}(x) = \sum_{k=l}^{L^{*}(m-1)} u_{A^{*}_{(k,m-1)}}(x),
\]
which guarantees (3.24), as desired.

\[\square\]
Using Lemma 3.2 as an inductive step, the main theorem is immediate. Indeed, (3.22) holds trivially for $M$ by Corollary 3.1. By applying the algorithm $M - 1$ times, we can obtain (3.1) for $M - 1, M - 2, \ldots, 1$.

**Theorem 3.1.** Let $\{I_m; 1 \leq m \leq M\}$ be produced by the algorithm.

1. Under Assumption 3.1, for every $1 \leq m \leq M$ and $1 \leq i \leq L^*(m)$,
   \[
   U^{(M)}_{\min I^*(i;m)}(x) = \sum_{k=1}^{L^*(m)} u_{A^*_2(k;m)}^*(x).
   \]
   In particular,
   \[
   U^{(M)}(x) = U^{(M)}_{\min I^*(1;1)}(x) = \sum_{k=1}^{L^*(1)} u_{A^*_2(k;1)}^*(x). \tag{3.26}
   \]

2. Under Assumption 3.2, for every $1 \leq m \leq M$ and $1 \leq i \leq L^*(m)$,
   \[
   \widetilde{U}^{(M)}_{\min I^*(i;m)}(x) = \sum_{k=1}^{L^*(m)} u_{A^*_2(k;m)}^*(x).
   \]
   In particular,
   \[
   \widetilde{U}^{(M)}(x) = \widetilde{U}^{(M)}_{\min I^*(1;1)}(x) = \sum_{k=1}^{L^*(1)} u_{A^*_2(k;1)}^*(x). \tag{3.27}
   \]

4. PHASE-TYPE CASE AND NUMERICAL EXAMPLES

In this section, we consider spectrally negative Lévy processes with i.i.d. phase-type jumps and provide numerical examples. Any Lévy process can be approximated by that of a compound Poisson process with phase-type jumps (phase-type Lévy process); see, e.g., [20]. In a related work, Egami and Yamazaki [17] approximate the scale function of the spectrally negative Lévy process by those of phase-type Lévy processes.

4.1. Spectrally negative Lévy processes with phase-type jumps. Let $X$ be a spectrally negative Lévy process of the form
   \[
   X_t - X_0 = \mu t + \sigma B_t - \sum_{n=1}^{N_t} Z_n, \quad 0 \leq t < \infty. \tag{4.1}
   \]
Here $B = \{B_t; t \geq 0\}$ is a standard Brownian motion, $N = \{N_t; t \geq 0\}$ is a Poisson process with arrival rate $\lambda$, and $Z = \{Z_n; n = 1, 2, \ldots\}$ is an i.i.d. sequence of phase-type-distributed random variables with representation $(m, \alpha, T)$; see [2]. These processes are assumed mutually independent. The Laplace exponent (2.1) of $X$ is then
   \[
   \psi(s) = \mu s + \frac{1}{2} \sigma^2 s^2 + \kappa (\alpha(sI - T)^{-1}t - 1), \quad \text{with } t = -T[1, \ldots, 1]',
   \]
which is analytic for every $s \in \mathbb{C}$ except at the eigenvalues of $T$. Suppose $\{-\xi_{i;r}; i \in \mathcal{I}_r\}$ is the set of the roots of the equality $\psi(s) = r$ with negative real parts, and if these are assumed distinct and $\sigma > 0$, then the scale function can be written
   \[
   W^{(r)}(x) = \sum_{i \in \mathcal{I}_r} C_i (e^{\Phi_{i;r}} - e^{-\xi_{i;r}x}),
   \]
where
\[ C_i := \frac{s + \xi_{i,r}}{r - \psi'(s)} \bigg|_{s=-\xi_{i,r}} = -\frac{1}{\psi'(-\xi_{i,r})}; \]
see [17]. Here \( \{\xi_{i,r}; i \in \mathcal{I}_r\} \) and \( \{C_i; i \in \mathcal{I}_r\} \) are possibly complex-valued.

With \( \Phi_r^{(c)} := \Phi_r - c \) and \( \xi_{i,r}^{(c)} := \xi_{i,r} + c \), for any \( i \in \mathcal{I}_r \) and \( c \geq 0 \), we have by (2.7) for any \( x \geq 0 \)
\begin{align*}
W_c^{(r - \psi(c))}(x) &= \sum_{i \in \mathcal{I}_r} C_i \left[ e^{\Phi_r^{(c)} x} - e^{-\xi_{i,r}^{(c)} x} \right], \\
Z_c^{(r - \psi(c))}(x) &= 1 + (r - \psi(c)) \sum_{i \in \mathcal{I}_r} C_i \left[ \frac{1}{\Phi_r^{(c)}}(e^{\Phi_r^{(c)} x} - 1) + \frac{1}{\xi_{i,r}^{(c)}}(e^{-\xi_{i,r}^{(c)} x} - 1) \right].
\end{align*}
(4.2)

Thanks to their forms as sums of exponential functions, the value function we obtain below admits closed forms.

For our examples, we assume \( \sigma = 0.2 \) and \( \mu = \lambda = 1 \). For the phase-type distribution for \( Z \), we assume \( m = 6 \) and
\[
T = \begin{bmatrix}
-5.5209 & 0.0000 & 0.0000 & 0.0000 & 0.0000 & 0.0000 \\
0.0073 & -5.4523 & 5.4443 & 0.0000 & 0.0000 & 0.0000 \\
5.4959 & 0.0000 & -5.4959 & 0.0000 & 0.0000 & 0.0000 \\
0.2193 & 0.0030 & 0.2920 & -5.6885 & 5.1589 & 0.0154 \\
0.2703 & 0.8484 & 0.0027 & 0.0000 & -5.6502 & 4.5262 \\
0.0020 & 4.8467 & 0.0157 & 0.0000 & 0.0000 & -5.9780
\end{bmatrix},
\alpha = \begin{bmatrix} 0.0000 \\
0.0048 \\
0.0044 \\
0.9906 \\
0.0002 \\
0.0000 \end{bmatrix},
\]
which give an approximation of the Weibull distribution with density function \( f(x) = 2x \exp \{-x^2\}, x \geq 0 \), obtained using the EM-algorithm; see [17] regarding the approximation performance of the corresponding scale function.

4.2. Numerical results on the one-stage problem. We first consider the one-stage problem as studied in Section 2. In our numerical examples, we consider two examples for \( g \) satisfying (2.21):

(a) mixture of exponential functions: \( g^{(exp)} = K - \sum_{i=1}^{N} c_i e^{a_i x} \) for some constants \( K \in \mathbb{R}, c_i, a_i > 0, 1 \leq i \leq N, N \geq 0; \)

(b) linear function: \( g^{(lin)}(x) := -\alpha x, x \in \mathbb{R} \), for some \( \alpha > 0 \).

Regarding \( f \), we consider the following three examples:

(i) simple function: \( f^{(sim)}(y) := \sum_{-\infty < n < \infty} f^{(n)} l_n(y) \) for some constants \( f^{(0)} < f^{(-1)} < f^{(-2)} < \cdots < f^{(-n)} < f^{(-n+1)} \); such that \( \lim_{n \to \infty} f^{(n)}(y) = \lim_{n \to \infty} f^{(n)}(y) = 0 \) for \( y \in \mathbb{R} \);

(ii) linear function with a lower bound: \( f^{(lin)}(y) := b_1 [(y + b_2) \vee b_3] \) for some \( b_1 > 0 \) and \( b_2, b_3 \in \mathbb{R} \);

(iii) exponential function with an upper bound: \( f^{(exp)}(y) := e^{(L_2 y)^\wedge B} \) for some \( L > 0 \) and \( B \in \mathbb{R} \).

These satisfy Assumption 2.3 (1) and in particular (ii) and (iii) satisfy Assumption 2.2 (1). Hence Proposition 2.2 holds (or \( \bar{u} = u_{A^+} \)) for any choice and in particular Proposition 2.1 holds (or \( u = \bar{u} = u_{A^+} \)) for (ii) or (iii).

In order to implement the optimal strategy, we first obtain \( A^+ \) using (2.23) and then compute the value function via (2.25). Toward this end, we need to compute \( \Theta_f(x; A) \) for (i)-(iii). The proof of the following lemma is tedious but straightforward and is hence omitted.
Define, for any \( s < t \) and \( k \geq 0 \),
\[
    w_{x,A}^{(k)}(s,t) := \sum_{i \in \mathbb{Z}_r} C_i \left[ \frac{1}{\Phi_r} \left( e^{\Phi_r(s-A)+} - e^{\Phi_r(t-A)+} \right) + \frac{1}{\xi_{i,r}} \left( e^{-\xi_{i,r}(s-A)+} - e^{-\xi_{i,r}(t-A)+} \right) \right].
\]

This vanishes whenever \([s,t] \cap [A,x] = \emptyset\). Also let for any \( s < t \) and \( a \in \mathbb{R} \), \( \gamma(a,s,t) := \int_{s}^{t} ye^{ay} \, dy = \left( \frac{1}{a} - \frac{1}{a^2} \right) e^{at} - \left( \frac{a}{a} - \frac{1}{a^2} \right) e^{as} \).

**Lemma 4.1.** (1) For every \( A \in \mathbb{R} \),
\[
    \Psi_{f(sim)}(A) = \frac{1}{\Phi_r} \sum_{-\infty \leq l < +\infty} f^{(n)} \left( e^{-\Phi_r(l-A)+} - e^{-\Phi_r(l+1-A)+} \right),
\]
\[
    \Psi_{f(lin)}(A) = b_1 \left[ \frac{b_3}{\Phi_r} (1 - e^{-\Phi_r(b_3-(b_2+A))}) + \frac{b_2 + A}{\Phi_r} e^{-\Phi_r(b_3-(b_2+A))} + e^{-\Phi_r(b_3-(b_2+A))} \left( \frac{b_3 - (b_2 + A)}{\Phi_r} + \frac{1}{\Phi_r^2} \right) \right],
\]
\[
    \Psi_{f(exp)}(A) = \frac{e \Phi}{\Phi_r} e^{-\Phi_r(b_2/A+)} + \frac{e \Phi R}{\Phi_r} \left( 1 - e^{-\Phi_r(L)(b_2/A+)} \right).
\]

In particular, for any sufficiently small \( b_3 \), \( \Psi_{f(lin)}(A) = b_1 \left[ \frac{b_2 + A}{\Phi_r} + \frac{1}{\Phi_r^2} \right] \).

(2) For every \( x, A \in \mathbb{R} \),
\[
    \Theta_{f(sim)}(x,A) = \sum_{-\infty \leq l < +\infty} f^{(n)} w_{x,A}^{(0)}(l_n,l_{n+1}),
\]
\[
    \Theta_{f(lin)}(x,A) = b_1 \left[ b_3 w_{x,A}^{(0)}(A, (b_3-b_2) \lor A \land x) + b_2 w_{x,A}^{(0)}((b_3-b_2) \lor A \land x, x) \right]
\]
\[
    + b_1 \sum_{i=1}^{J+1} C_i \left[ e^{\Phi_i x \gamma(-\Phi_i)} ((b_3-b_2) \lor A \land x, x) - e^{-\xi_{i,r} x \gamma(\xi_{i,r})} ((b_3-b_2) \lor A \land x, x) \right],
\]
\[
    \Theta_{f(exp)}(x,A) = e^{(B/L) x} w_{x,A}^{(0)}(A \lor (B/L) \land x, x) + w_{x,A}^{(L)}(A \lor (B/L) \land x).
\]

We are now ready to show our numerical results for the one-stage problem. For \( g \) and \( f \), we consider any combination of the following:

(a) \( g = g^{(exp)} \) with \( a = [0.1, 0.2, 0.3, 0.4] \) and \( c = [4, 3, 2, 1] \) and \( K = 10 \);

(b) \( f = g^{(lin)} \) with \( \alpha = 1 \);

and

(i) \( f = \gamma f^{(sim)} \) with \( I_1 = (-\infty, 0) \), \( I_2 = [0, \infty) \), \( f^{(1)} = -10 \) and \( f^{(2)} = 10 \);

(ii) \( f = \gamma f^{(lin)} \) with \( b_1 = 1 \) and \( b_2 = 0 \) with sufficiently small \( b_3 \);

(iii) \( f = \gamma f^{(exp)} \) with \( L = B = 1 \);

for the weight parameter \( \gamma = 0, 0.05, 0.1 \).

The results for (a) \( g = g^{(exp)} \) and (b) \( g = g^{(lin)} \) are graphically shown in Figures 1 and 2, respectively. In each figure, we plot the function \( \Lambda(T) \) as in (2.18) and the value function \( u_{A*} \) for each choice of \( f \). As can be confirmed, the function \( \Lambda(T) \) is indeed monotonically increasing and hence the unique root \( A^* \) of \( \Lambda(A) = 0 \) can be obtained easily by the bisection method. Using these optimal threshold levels, the value functions are computed via (2.25) and Lemma 4.1.
We see that the value functions are differentiable even at the optimal threshold levels $A^*$ and this confirms the smooth fit as in Remark 2.3 because $X$ is of unbounded variation with $\sigma > 0$. For $f^{(\text{sim})}$ with a discontinuity at zero, the value function turns out to have a kink at zero.

In order to verify that these are indeed optimal, we focus on the case $\gamma = 0.05$ and plot in Figure 3 the value function $u_A$ in comparison to the expected values of “perturbed” strategies $u_A(\cdot)$ for $A = A^* - 2, A^* - 1, A^* + 1, A^* + 2$. Notice that these can be computed by the formula (2.24). For any choice of $A$, it is easy to see that $u_A$ is continuous as in Remark 2.3 but fails to be differentiable at $A \neq A^*$. We can confirm in all six cases that $u_A$ indeed dominates $u_A$ for $A \neq A^*$ uniformly in $x \in \mathbb{R}$. This numerically verifies Propositions 2.1 and 2.2.

4.3. Numerical results on the multiple-stage problem. We now move onto the multiple-stage problem. We assume $M = 3$ for brevity and use for $f$ and $g$ the functions (a)-(b) and (i)-(iii) defined for the one-stage problem.

For $m = 1, 3$, we assume $g_m = g^{(\exp)}$ for some $a_m = (a_{mi})_{1 \leq i \leq N_m}$ and $c_m = (c_{mi})_{1 \leq i \leq N_m}$ with $N_m = 4$ and a fixed value $K = 10$, whereas for $m = 2$, $g_2 = g^{(\text{linc})}$ for some $\alpha_2$. Also, let (i) $f_1 = \gamma_1 f^{(\text{sim})}$ with $I_1 = (-\infty, 0)$, $I_2 = [0, +\infty)$, $f^{(1)} = -10$ and $f^{(2)} = 10$, (ii) $f_2 = \gamma_2 f^{(\text{linc})}$ for $b_1 = 1$ and $b_2 = 0$ with sufficiently small $b_3$ and (iii) $f_3 = \gamma_3 f^{(\exp)}$ for $L = B = 1$.

We conduct a number of experiments for various values of coefficients. By using the algorithm given in Subsection 3.2, the optimal threshold levels $A^* = (A^*(1), A^*(2), A^*(3))$ take values among \{1, 2, 3, 4, 5\} and satisfy one of the following four cases:

- Case 1: $A^*(1) = A^*(2) = A^*(3)$;
- Case 2: $A^*(1) > A^*(2) > A^*(3)$;
- Case 3: $A^*(1) = A^*(2) > A^*(3)$;
- Case 4: $A^*(1) > A^*(2) > A^*(3)$.

Here we use a random random number generator to sample $a_m, c_m$ for $m = 1, 3, \alpha_2$, and $\gamma_m$ for each $1 \leq m \leq 3$ until we attain each of Cases 1 to 4. The generated parameters and the corresponding threshold levels are summarized in Table 1. In order to validate the optimality of the strategy $(\tau_{A^*}^{(1)}, \tau_{A^*}^{(2)}, \tau_{A^*}^{(3)})$, we compare in Figure 4 the value function with those of perturbed strategies $(\tilde{\tau}_{A_k}^{(1)}, \tilde{\tau}_{A_k}^{(2)}, \tilde{\tau}_{A_k}^{(3)})$, $1 \leq k \leq 6$, where

$$\tilde{\tau}_{A_k} := (A_k^{(1)}, A_k^{(2)}, A_k^{(3)}) + \delta_k$$

with $\delta_1 := (1, 0, 0)$, $\delta_2 := (1, 1, 0)$, $\delta_3 := (1, 1, 1)$, $\delta_4 := (0, 0, -1)$, $\delta_5 := (0, -1, -1)$ and $\delta_6 := (-1, -1, -1)$. It is clear that $(\tau_{A_k}^{(1)}, \tau_{A_k}^{(2)}, \tau_{A_k}^{(3)}) \in \mathcal{S}_3 \subset \mathcal{S}_3$ because $A_k^{(1)} \geq A_k^{(2)} \geq A_k^{(3)}$ by construction. Figure 4 suggests in all cases that the value obtained by $(\tau_{A^*}^{(1)}, \tau_{A^*}^{(2)}, \tau_{A^*}^{(3)})$ dominates uniformly over $x$ those obtained by the perturbed strategies. These results are indeed consistent with our main theoretical results. In view of Figure 4, we also observe that there are up to three kinks (at $A^*$) in the value function although these still appear to be differentiable. This is again due to smooth fit as in Remark 2.3. The perturbed strategies on the other hand fail to be differentiable while they are still continuous.

5. Concluding Remarks

In this paper, we studied a wide class of optimal stopping problems for a general spectrally negative Lévy process and extended them to multiple-stopping. Our framework is applicable to a wide range of settings particularly in real option problems where the firm withdraws from a project in stages. Our analytical results suggest that the
$\Lambda(\cdot)$ for $f^{(\text{sim})}$

value function for $f^{(\text{sim})}$

$\Lambda(\cdot)$ for $f^{(\text{lin})}$

value function for $f^{(\text{lin})}$

$\Lambda(\cdot)$ for $f^{(\text{exp})}$

value function for $f^{(\text{exp})}$

**FIGURE 1.** Plots of $\Lambda$ and the value function $u_{A^*}$ when $g = g^{(\text{exp})}$. 
Figure 2. Plots of $\Lambda$ and the value function $u_{A^*}$ when $g = g^{(lin)}$. 
Figure 3. Verification of optimality: the value function $u_{A^*}$ (solid black) and the stopping value $g$ (solid blue) in comparison with $u_{A^*}(\cdot)$ for $A = A^* - 2, A^* - 1, A^* + 1, A^* + 2$ (dotted).
optimal solutions can be characterized by the threshold levels that are zeros of certain monotone functions and the corresponding value functions can be expressed in terms of the scale function. Our numerical experiments suggest, for the phase-type jump case, that these can be solved instantaneously with high precision. These tools we developed in this paper are highly valuable and can be used flexibly for analysis in real options and other fields of finance and industrial applications.

There are several directions for future research. First, our results can be pursued for a general Lévy process with both positive and negative jumps. While it makes the problem less tractable, it is expected that these can be done at least for the cases with analytical forms of Wiener-Hopf factors such as meromorphic Lévy processes [22] and phase-type Lévy processes [2]. Second, by using phase-type fitting, one can approximate any Lévy process by those with phase-type jumps as in Section 4. By calibrating with real financial and industrial data as in [3], one can conduct detailed empirical analyses on optimal stopping strategies and the value functions. Finally, it is an interesting extension to “swing option type” multiple-stopping with refracting time as in [11, 12] where there have to be some intervals between any two consecutive stoppings.

### Appendix A. Proofs

| $a_1$ | $a_3$ |
|-------|-------|
| Case 1 | 0.49, 0.19, 0.17, 0.03 | 0.05, 0.24, 0.46, 0.13 |
| Case 2 | 0.47, 0.17, 0.06, 0.12 | 0.24, 0.18, 0.19, 0.05 |
| Case 3 | 0.04, 0.06, 0.01, 0.12 | 0.01, 0.11, 0.26, 0.05 |
| Case 4 | 0.39, 0.28, 0.17, 0.16 | 0.06, 0.01, 0.40, 0.08 |

| $c_1$ | $c_3$ |
|-------|-------|
| Case 1 | 2.11, 2.09, 3.51, 3.49 | 4.71, 1.51, 2.70, 0.89 |
| Case 2 | 0.66, 2.88, 1.77, 0.22 | 4.78, 1.17, 0.08, 3.24 |
| Case 3 | 1.84, 2.39, 4.20, 2.23 | 3.01, 3.72, 2.57, 4.20 |
| Case 4 | 3.01, 3.45, 0.42, 0.76 | 3.27, 2.25, 4.57, 2.69 |

| $\alpha_2$ | $\gamma_1$ (simple) | $\gamma_2$ (linear) | $\gamma_3$ (exponential) |
|------------|---------------------|---------------------|---------------------|
| Case 1 | 0.9991 | 0.2920 | 0.4317 | 0.0155 |
| Case 2 | 0.6477 | 0.4173 | 0.0497 | 0.9027 |
| Case 3 | 0.6265 | 0.3070 | 0.0611 | 0.2195 |
| Case 4 | 0.0782 | 0.0759 | 0.0540 | 0.5308 |

| $A^*_1$ | $A^*_2$ | $A^*_3$ | $A^*_{\{1,2\}}$ | $A^*_{\{1,2,3\}}$ | $A^*_{\{1\}}$ | $A^*_{\{2\}}$ | $A^*_{\{3\}}$ |
|--------|--------|--------|-----------------|------------------|----------------|----------------|----------------|
| Case 1 | -2.44  | -2.83  | -1.39 | -2.59 | -2.03 | -2.21 | -2.21 | -2.21 |
| Case 2 | -0.48  | -2.31  | -2.18 | -0.85 | -2.22 | -1.34 | -0.48 | -2.22 | -2.22 |
| Case 3 | -3.15  | -2.35  | -5.67 | -2.85 | -4.14 | -3.75 | -2.85 | -2.85 | -5.67 |
| Case 4 | -0.76  | -3.07  | -3.64 | -0.85 | -3.59 | -1.89 | -0.76 | -3.07 | -3.64 |

**Table 1.** Parameters and threshold levels.
$\rho_{g_1, A}^{(c)} = -b \int_{(0, \infty)} \Pi(du) \int_0^u e^{-\Phi_r z} (z - u)dz = \frac{b}{\Phi_r^2} \int_{(0, \infty)} \Pi(du)(1 - e^{-\Phi_r u} - u\Phi_r),$

Figure 4. Illustration of optimality for the multiple-stage case: the value function (solid) in comparison with the perturbed strategies.

A.1. Proof of Lemma 2.1. Let $g_1(x) := -bx$. We have
and hence
\[
\Lambda(A; 0, g_1) := -\frac{r}{\Phi_r} g_1(A) - \frac{\sigma^2}{2} g_1'(A) + \rho^{(r)}_{g_1, A} = b \left[ \frac{r}{\Phi_r} A + \frac{\sigma^2}{2} - \frac{1}{\Phi_r^2} \int_{(0, \infty)} \Pi(du)(1 - e^{-\Phi_r u} - u\Phi_r) \right] \\
= \frac{b}{\Phi_r} \left[ c\Phi_r + \frac{\sigma^2}{2} \Phi_r^2 + \int_{(0, \infty)} (e^{-\Phi_r u} - 1 + \Phi_r u 1_{(0 < u < 1)}) \Pi(du) \right] \\
- \frac{b}{\Phi_r} \left[ c - \int_{[1, \infty)} u 1_{(0 < u < 1)} \Pi(du) - rA \right] \\
= b \left[ \frac{r}{\Phi_r^2} - \frac{\psi'(0+) - rA}{\Phi_r} \right].
\]

Let \( g_2(x) = -\sum_{i=1}^N c_i e^{a_i x} \). Then,
\[
\rho^{(r)}_{g_2, A} = -\sum_{i=1}^N c_i e^{a_i A} \int_{(0, \infty)} \Pi(du) \int_0^u e^{-\Phi_r z} (e^{a_i (z-u)} - 1) dz. \tag{A.1}
\]

(Case 1) First suppose \( a_i \neq \Phi_r \) for all \( 1 \leq i \leq N \). Simple algebra gives
\[
\Lambda(A) = -\frac{r}{\Phi_r} K + b \left[ \frac{r}{\Phi_r} A + \frac{rA - \psi'(0+)}{\Phi_r} \right] + \sum_{i=1}^N c_i e^{a_i A} M_r(a_i) + \Psi_f(A) \tag{A.2}
\]
where
\[
M_r(a) := r + \frac{a\sigma^2}{2} \Phi_r + \int_0^\infty \Pi(du) \left[ (1 - e^{-\Phi_r u} - e^{-au} (1 - e^{-(\Phi_r-a)u}) \frac{\Phi_r}{\Phi_r - a}, a \in \mathbb{R} \setminus \{\Phi_r\}.
\]

By the definition of \( \psi \) and \( \Phi_r \), we rewrite \( M_r(a) \) as
\[
r + \frac{a\sigma^2}{2} \Phi_r + \int_{(0, \infty)} \Pi(du) \left[ (1 - e^{-\Phi_r u} - \Phi_r 1_{(u \in (0, 1))}) - e^{-au} (1 - e^{-(\Phi_r-a)u}) \frac{\Phi_r}{\Phi_r - a}, \Phi_r + 1_{(u \in (0, 1))} \right] \\
= (c - \int_{(0, 1)} u (e^{-au} - 1) \Pi(du)) \Phi_r + \frac{\sigma^2}{2} \Phi_r (\Phi_r + a) \\
- \frac{\Phi_r}{\Phi_r - a} \int_{(0, \infty)} \Pi(du) e^{-au} \left( 1 - e^{-(\Phi_r-a)u} + (\Phi_r - a) 1_{(u \in (0, 1))} \right) \\
= \frac{\Phi_r - \psi_a(\Phi_r - a)}{\Phi_r - a},
\]
where the last equality holds by (2.6). On the other hand, \( \psi_a(\Phi_r - a) = \psi(\Phi_r) - \psi(a) = r - \psi(a) \); see page 213 of [23]. Hence
\[
\Phi_r \varpi_r(a) = \frac{\Phi_r}{\Phi_r - a} (r - \psi(a)) = \frac{\Phi_r}{\Phi_r - a} \psi_a(\Phi_r - a),
\]
which shows for the case \( a_i \neq \Phi_r \) for all \( 1 \leq i \leq N \).

(Case 2) Suppose \( a_j = \Phi_r \) for some \( 1 \leq j \leq N \) (with \( a_i \neq a_j \) for \( i \neq j \) by assumption). Take a sequence of (strictly) increasing sequence \( a_j^{(m)} \uparrow a_j = \Phi_r \). Then a modification of (2.18) with \( a_j \) replaced with \( a_j^{(m)} \) is by Case 1
\[
\Lambda^{(m)}(A) = -\frac{r}{\Phi_r} K + b \left[ \frac{r}{\Phi_r^2} A + \frac{rA - \psi'(0+)}{\Phi_r} \right] + \sum_{1 \leq i \leq N, i \neq j} c_i e^{a_i A} \varpi_r(a_i) + c_j e^{a_j^{(m)} A} \varpi_r(a_j^{(m)}) + \Psi_f(A).
\]
By the definition of \( \varpi_r \) as in (2.22), we have

\[
\lim_{m \to \infty} \Lambda^{(m)}(A) = -\frac{r}{\Phi_r} K + b \left[ \frac{r}{\Phi_r^2} + \frac{rA - \psi'(0+)}{\Phi_r} \right] + \sum_{i=1}^{N} c_i e^{A_i x} \varpi_r(a_i) + \Psi_f(A).
\]

On the other hand, in view of (A.1), its integrand is monotone in \( a \). Hence by the monotone convergence theorem and because \( g \) and \( g' \) are continuous in \( a \), \( \lim_{m \to \infty} \Lambda^{(m)}(A) = \Lambda(A) \), and the proof is complete for Case 2.

A.2. Proof of Lemma 2.2. Because \( g(x) \) is infinitely differentiable, the results are clear for \( x \in (-\infty, A^*) \). Hence we show for \( x \in (A^*, \infty) \). Because \( W^{(r)}(y) \) is differentiable on \( y > 0 \) as in Remark 2.1 (1),

\[
K Z^{(r)}(x - A^*) - b \left[ Z^{(r)}(x - A^*) + (A^* - \psi'(0+)) Z^{(r)}(x - A^*) + \psi'(0+) \right] - \sum_{i=1}^{N} c_i e^{A_i x} Z^{(r)}(x - A^*) \]

is twice differentiable.

Regarding \( \Theta_f(x; A^*) \), as in the proof of Lemma 4.5 of [18], integration by parts, thanks to the continuity of \( f \), gives

\[
r \int_{A^*}^{x} W^{(r)}(x - y) f(y) dy \]

equals

\[
\left[ f(y) (Z^{(r)}(x) - Z^{(r)}(x - y)) \right]_{y=A^*}^{y=x} - \int_{A^*}^{x} f'(y) (Z^{(r)}(x) - Z^{(r)}(x - y)) dy \]

equals

\[
f(x)(Z^{(r)}(x) - 1) - f(A^*)(Z^{(r)}(x) - Z^{(r)}(x - A^*)) - (f(x) - f(A^*))Z^{(r)}(x) + \int_{A^*}^{x} f'(y) Z^{(r)}(x - y) dy \]

equals

\[
- \left[ -f(x) + f(A^*) Z^{(r)}(x - A^*) + \int_{A^*}^{x} f'(y) Z^{(r)}(x - y) dy \right].
\]

Hence

\[
\Theta_f(x; A^*) = \frac{1}{r} \left[ -f(x) + f(A^*) Z^{(r)}(x - A^*) + \int_{A^*}^{x} f'(y) Z^{(r)}(x - y) dy \right].
\]

Because \( Z^{(r)}(0) = 1 \), \( \Theta_f(x; A^*) \) is differentiable with

\[
\Theta_f'(x; A^*) = f(A^*) W^{(r)}(x - A^*) + \int_{A^*}^{x} f'(y) W^{(r)}(x - y) dy.
\]

When \( X \) is of unbounded variation, because \( W^{(r)}(0) = 0 \) as in Remark 2.1 (2), \( \Theta_f(x; A^*) \) is twice-differentiable with

\[
\Theta_f''(x; A^*) = f(A^*) W^{(r)'}(x - A^*) + \int_{A^*}^{x} f'(y) W^{(r)'}(x - y) dy.
\]

A.3. Proof of Proposition 2.1. Suppose \(-\infty < A^* < \infty \). By directly using the results of [19] (Lemma 3.7 and Proposition 3.4), we obtain

\[
(\mathcal{L} - r) u_{A^*}(x) + f(x) = 0, \quad x \in (A^*, \infty),
\]

\[
u_{A^*}(x) \geq g(x), \quad x \in \mathbb{R},
\]

where \( \mathcal{L} \) is the infinitesimal generator of \( X \) applied to a sufficiently smooth function \( h \), i.e.,

\[
\mathcal{L} h(x) = ch'(x) + \frac{1}{2} \sigma^2 h''(x) + \int_{0}^{\infty} \left[ h(x - z) - h(x) + h'(x) z 1_{\{0 < z < 1\}} \right] \Pi(dz).
\]

We shall show \( (\mathcal{L} - r) u_{A^*}(x) + f(x) \leq 0 \) on \( x \in (-\infty, A^*) \) and verify the optimality. First

\[
(\mathcal{L} - r)x = \mathbb{E}_0 [X_1] - rx = \psi'(0+) - rx.
\]
By the definition of $\psi$,

$$L e^{ax} = e^{ax} \left[ ca + \frac{1}{2} \sigma^2 a^2 + \int_0^\infty \left[ e^{-az} - 1 + a z 1_{(0 < z < 1)} \right] \Pi(dz) \right] = e^{ax} \psi(a)$$

for any $a > 0$ and hence we have

$$(L - r)g(x) + f(x) = -rK + b(\psi'(0^+) - rx) + \sum_{i=1}^{N} c_i e^{ai}x(r - \psi(a_i)) + f(x). \quad \text{(A.4)}$$

By how $A^*$ is chosen,

$$0 = -rK + b\left( \frac{r}{\Phi_r} - (\psi'(0^+) - rA^*) \right) + \sum_{i=1}^{N} c_i e^{ai}A^* \Phi_r \varpi_r(a_i) + \Phi_r \Psi_f(A^*). \quad \text{(A.5)}$$

Because $f$ is increasing and $x < A^*$

$$\Phi_r \Psi_f(A^*) \geq \Phi_r \int_0^\infty e^{-\Phi_r y} f(x) dy = f(x). \quad \text{(A.6)}$$

By $A^* \geq x$ and $\Phi_r > 0$,

$$b\left( \frac{r}{\Phi_r} - (\psi'(0^+) - rA^*) \right) \geq -b(\psi'(0^+) - rx).$$

It is also easy to see that

$$e^{ai}A^* \Phi_r \varpi_r(a_i) \geq e^{ai}x(r - \psi(a_i)), \quad 1 \leq i \leq N. \quad \text{(A.7)}$$

Indeed, for the case $r - \psi(a_i) > 0$, we must have $\Phi_r - a_i > 0$ and hence (A.7) holds by $A^* > x$; for the case $r - \psi(a_i) < 0$, the left-hand side is positive while the right-hand side is negative in (A.7); for the case $r - \psi(a_i) = 0$, the left-hand side is positive because $\psi'(\Phi_r)$ is, while the right-hand side is zero. Hence, by (A.5)-(A.7), $(L - r)u_{A^*}(x) + f(x) \leq 0$ holds.

This result also holds for the case $A^* = \infty$. In this case, $0 > -rK + \sum_{i=1}^{N} c_i e^{ai}A^* \Phi_r \varpi_r(a_i) + b\left( \frac{r}{\Phi_r} - (\psi'(0^+) - rA) \right) + \Phi_r \Psi_f(A^)$, for any $A \in \mathbb{R}$. Therefore $(L - r)g(x) + f(x) < 0$ holds by the same reasoning as in (1) by simply replacing $A^*$ with $A$.

Finally, we verify the optimality of $u_{A^*}(x)$ for the case $A^* \in (-\infty, \infty]$. Thanks to Lemma 2.2 and the continuous/smooth fit condition as in Remark 2.3, a version of Meyer-Ito’s formula as in Theorem IV.71 of [30] (see also Theorem 2.1 of [29]) implies

$$e^{-r^t}u_{A^*}(X_t) - u_{A^*}(X_0) = \int_0^t e^{-rs}(L - r)u_{A^*}(X_{s-}) ds + M_t,$$

with

$$M_t := \int_0^t \sigma e^{-r^u}u_{A^*}'(X_{s-}) dB_s - \lim_{\varepsilon \downarrow 0} \int_{[0,\varepsilon]} \int_{(\varepsilon,1)} e^{-rs} u_{A^*}'(X_{s-}) y(N(ds \times dy) - \Pi(dy)ds)$$

$$+ \int_{[0,\varepsilon]} \int_{(0,\infty)} e^{-rs}(u_{A^*}(X_{s-} - y) - u_{A^*}(X_{s-}) + u_{A^*}'(X_{s-}) y 1_{y \in (-1,0)})(N(ds \times dy) - \Pi(dy)ds),$$

where $N(ds \times dx)$ is the Poisson random measure associated with the dual process $-X$. 
Fix any stopping time $\tau$ and define for each $m \in \mathbb{N}$, the stopping time $\tau_m$ as
$$
\tau_m := \inf\{t > 0 : |X_t| > m\} \wedge \tau,
$$
and the martingale process $M = \{M_{t \wedge \tau_m} : t \geq 0\}$, with $M_0 = 0$.

By optional sampling and because $(L - r)u_{A^*} + f \leq 0$,

$$
\mathbb{E}^x\left[e^{-(r(t \wedge \tau_m))}u_{A^*}(X_{t \wedge \tau_m}) + \int_0^{t \wedge \tau_m} e^{-rs}f(X_s)ds\right] \leq u_{A^*}(x).
$$

When $A^* \in (-\infty, \infty)$, $u_{A^*}(x) = g(x) \geq g(A^*) > -\infty$ for $x \leq A^*$ and $u_{A^*}(x) \geq \lim_{A_1 \to -\infty} u_A(x) \geq \int_0^\infty e^{-rt} f(-\infty) dt > -\infty$ for $x > A^*$ by (2.20). When $A^* = \infty$, by Remark 2.2, $u_{A^*}(x) = K > -\infty$ for $x \in \mathbb{R}$.

Hence, Fatou’s lemma gives upon $t \uparrow \infty$ and $m \uparrow \infty$

$$
\mathbb{E}^x\left[e^{-r\tau}u_{A^*}(X_\tau) + \int_0^{\tau} e^{-rs}f(X_s)ds\right] \leq u_{A^*}(x).
$$

Finally, (A.3) shows the result for $A^* \in (-\infty, \infty)$.

It is now left to show for the case $A^* = -\infty$. Because $\partial u_A(x)/\partial A < 0$ for any $A \in \mathbb{R}$ as in (2.20), there exists

$$
u_{-\infty}(x) := \lim_{A_1 \to -\infty} u_A(x) = \lim_{A_1 \to -\infty} \mathbb{E}^x\left[\int_0^{\tau_A} e^{-rt} f(X_t)dt\right].
$$

By Assumption 2.2 (1) and by the monotone convergence theorem, we can write

$$
u_{-\infty}(x) = \lim_{A_1 \to -\infty} \left(\mathbb{E}^x\left[\int_0^{\tau_A} e^{-rt} f_+(X_t)dt\right] - \mathbb{E}^x\left[\int_0^{\tau_A} e^{-rt} f_-(X_t)dt\right]\right)
$$

$$
= \mathbb{E}^x\left[\int_0^\infty e^{-rt} f_+(X_t)dt\right] - \mathbb{E}^x\left[\int_0^\infty e^{-rt} f_-(X_t)dt\right] = \mathbb{E}^x\left[\int_0^\infty e^{-rt} f(X_t)dt\right].
$$

Now by Corollary 8.9 of [23], $\nu_{-\infty}$ attains the proposed form. Because $\partial u_A(x)/\partial A < 0$ for any $A \in \mathbb{R}$, clearly $\nu_{-\infty}(x) > g(x)$ for any $x \in \mathbb{R}$. Moreover, because $\nu_{-\infty}$ is attained by $\tau^* = \infty$, we have the claim.

A.4. Proof of Proposition 2.2. (1,2) We first suppose $x < A^*$. Then by definition $u_{A^*}(x) = g(x)$. Because $u_A(x) = g(x)$ for any $A \geq x$, it is sufficient to show $u_A(x) \leq g(x)$ for $A < x$. This is indeed so because by (2.17), (2.20) and $\Lambda(x) < 0$ due to $x < A^*$,

$$
u_A(x) \leq \nu_{A}(x+) = g(x) + W^{(x)}(0)\Lambda(x) \leq g(x) = u_{A^*}(x), \quad A < x < A^*.
$$

This proves (2). For (1), suppose $x \geq A^*$. Then by (2.20) $u_{A^*}(x) \geq u_A(x)$ for any $A \leq x$. For $A \geq x$, $u_A(x) = g(x)$ and by (2.17), (2.20) and $\Lambda(x) > 0$ due to $x > A^*$,

$$
u_{A^*}(x) \geq \nu_{A(x)}(x) = g(x) + W^{(x)}(0)\Lambda(x) \geq g(x) = u_{A^*}(x), \quad A \geq x > A^*.
$$

Therefore $u_{A^*}(x) \geq u_A(x)$ uniformly in $x \in \mathbb{R}$, as desired.

The corresponding value function (for (1)) can be expressed as the sum of (2.15):

$$
\tilde{u}(x) = g(A^*)Z^{(r)}(x - A^*) + W^{(r)}(x - A^*) \left(-\frac{r}{\Phi_{r}}g(A^*) + \rho_{g,A^*}^{(r)} + \Psi_f(A^*)\right) - \psi^{(r)}_{g,A^*}(x) - \Theta f(x; A^*).
$$

From the definition of $A^*$ that makes (2.18) vanish,

$$
\tilde{u}(x) = g(A^*)Z^{(r)}(x - A^*) + W^{(r)}(x - A^*) \frac{\sigma^2}{2} g'(A^*) - \psi^{(r)}_{g,A^*}(x) - \Theta f(x; A^*),
$$
as desired.

(3) the proof is the same as that of Proposition 2.1 (3).

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