

ENERGY MARKETS AND POLICY

BEPP/OIDD 7630

Spring Semester 2023, Tu/Th 3:30-5:00 p.m., SHDH 211

Note: This syllabus will be continuously updated. Please check Canvas for the latest version. Readings will be added/updated throughout the semester and as policy developments occur.

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Course overview. Over the last several decades, energy markets have become some of the most dynamic markets of the world economy. Traditional fossil fuel and electricity markets have seen a partial shift from heavy regulation to market-driven incentives, while rising environmental concerns have led to a wide array of new regulations and “environmental markets”. The growth of renewable energy is another source of rapid change, but brings with it a whole new set of technological and policy challenges. This changing energy landscape requires quick adaptation from energy companies, but also offers opportunities to turn regulations into new business. The objective of this course is to provide the economist’s perspective on a broad range of topics that professionals in the energy industry will encounter. Topics include the effect of competition, market power and scarcity on energy prices, extraction and pricing of oil and gas, geopolitical uncertainty and risk in hydrocarbon investments, the environmental policies related to the energy sector and their effectiveness, and cap-and-trade markets. There is special emphasis on the economics and finance of renewable energy, including an introduction to energy storage.

Readings. A mix of newspaper articles, academic papers, reports, plus the following textbook: Nathaniel Keohane and Sheila Olmstead (KO), *Markets and the Environment*, Washington, D.C.: Island Press, second edition, 2016. Starred (*) readings are required. Many starred readings are short. Non-starred readings are optional but I will discuss them in class, and you are highly encouraged to read them if you want further background on a specific topic. The best way to use the readings is as a supplement to the lectures, which overlap partially (but certainly not perfectly!) with the readings. You will be responsible for required readings not covered in class.

Prerequisites. Managerial Economics (MGEC 6110/6120) or an equivalent intermediate microeconomics course approved by the instructor.

Attendance. Attendance is mandatory. Please email me in advance if you have a good reason not to attend a particular session.

Format. For most lectures, I will post prep questions on Canvas. Some lectures have pre-recorded videos. I will build on the video content in the lecture, so it is really important that you watch the assigned video beforehand. Occasionally, when a video is on the longer side, I will start the class later, so you have the option to watch it within the allocated 90-minute lecture slot. Feel free to email me (cc: Prakash) any questions that arise as you watch the videos.

Strategy games. Students will participate in two strategy games. The OPEC game is a series of simulations of the world oil market. Student teams represent countries and try to maximize profits by making output decisions that determine the world oil price. The Electricity Strategy Game is a simulation of an electricity market. Student teams manage a portfolio of generation units (coal, natural gas, nuclear and renewables) and bid into an electricity market.

Guest lectures. The course has three guest lectures by various energy experts. This year's emphasis will be on renewable energy finance, renewable energy policy, and energy storage. Attendance is mandatory and the content is fair game for questions on assignments and exams.

Assignments and grading. Three equally weighted assignments (30%), an exam (35%), the OPEC Game (12.5%), the Electricity Strategy Game (12.5%) and class participation (10%). The assignments are take-home. You may discuss assignments with other students but you need to formulate and submit answers on your own or joint with at most two other classmates. You earn participation points for submitting brief answers to pre-lecture questions on Canvas; only timely submission with good-faith effort counts, not accuracy/score. The exam will be on April 20 (in class). You should plan to attend the exam. Contact the MBA Program Office if you have a scheduling conflict with another class, a medical issue, or an emergency. No other exceptions. Please do not email me about alternative exam dates for other reasons as I have no flexibility to accommodate such requests in all fairness to other students.

Practice questions. An extensive set of practice questions and solutions will be posted early in the semester. You can discuss them with the TA or with me during office hours if needed.

Cheating policy. It should not be necessary to say this – but for completeness: all students are expected to comply with the University of Pennsylvania's Code of Academic Integrity. It is the policy of the department, and this course, to immediately fail any student for the course who is in violation of the University's Code of Academic Integrity. Additional sanctions may be imposed of the Office of Student Conduct. The Code of Academic Integrity can be reviewed [here](#).

Electronics. Taking notes on tablets is permitted. Phones are permitted for responding to polls, but should otherwise not be a distraction to you or your classmates. No laptops as the sound of typing has proven to bother other students.

Other details. The course is included in the MBA major in Business, Energy, Environment and Sustainability and in the BEPP-Law School certificate. Non-Wharton students are welcome and encouraged to contact the professor in advance to discuss prerequisites.

ELECTRICITY MARKETS

Lecture 1 (Jan 17): **Course Introduction & Energy Overview**

International Energy Agency, 2022. *World Energy Outlook*, Executive Summary ([link](#)).

Lecture 2 (Jan 19): **Market Efficiency and Scarcity Pricing**

Topics: market efficiency; scarcity pricing; electricity markets; refined products markets.

(*) Pre-recorded video: Market Efficiency.

(*) Pre-recorded video: Scarcity Pricing.

(*) KO Chapter 4: “The Efficiency of Markets”.

(*) J. Mouawad, “A Fast-Growing Independent Strikes Gold in Oil Refining”, *New York Times*, 5/18/05 ([link](#)).

(*) J. Mouawad, “Oil Refiners See Profits Sink as Consumption Falls”, *New York Times*, 5/14/08 ([link](#)).

(*) C. Krauss, “Oil Refining’s Fortunes Rise”, *New York Times*, 10/24/12 ([link](#)).

(*) L. Cook and B. Olson, “Hurricanes Stir up Profits for Refiners”, *Wall Street Journal*, 9/17/17 ([link](#)).

D. Winning and R. Elliott, “Pandemic Pushes Fuel Makers in Richer Countries to the Brink”, *Wall Street Journal*, 12/6/20 ([link](#)).

J. Lee, “America’s Refiners Are Running on Premium”, *Wall Street Journal*, 11/1/22 ([link](#)).

Lecture 3 (Jan 24): **Market Power in Electricity Markets (Start Lecture: 4:10 p.m.)**

Topics: market power; deregulation.

(*) Pre-recorded video: Market Power.

(*) S. Borenstein, 2000. “Understanding Competitive Pricing and Market Power in Wholesale Electricity Markets”, *The Electricity Journal* 13(6): pp. 49-57 ([link](#)).

(*) M. Slezak, “Energy Companies Withholding Supply to Blame for July Price Spike, Report Finds”, *The Guardian*, 8/17/16 ([link](#)).

Lecture 4 (Jan 26): **Electricity Market Design**

Topics: California electricity crisis; Texas electricity crisis; electricity retail pricing.

Pre-recorded video: Electricity Retail Pricing.

(*) S. Borenstein, 2018. “The Electricity Price Isn’t Right.” Energy Institute Blog, UC Berkeley ([link](#)).

(*) J. Bushnell, 2023. “(More) Breaking News! California Electricity Prices are Still High!” Energy Institute Blog, UC Berkeley ([link](#)).

(*) C. Krauss, M. Fernandez, I. Penn and R. Rojas, “How Texas’ Drive for Energy Independence Set It Up for Disaster”, *New York Times*, 2/21/21 ([link](#)).

G. McDonnell Nieto del Rio, N. Bogel-Burroughs and I. Penn, “His Lights Stayed on During Texas’ Storm. Now He Owes \$16,752”, *New York Times*, 2/20/21 ([link](#)).

S. Borenstein, 2002. “The Trouble with Electricity Markets: Understanding California's Restructuring Disaster”, *Journal of Economic Perspectives* 16(1): pp. 191-211 ([link](#)).

OIL AND GAS MARKETS

Lecture 5 (Jan 31): **Oil and Natural Gas Extraction and Pricing (1) & Introduction to the OPEC Game (End Lecture: 4:30 p.m.)**

Topics: trends in oil and gas reserves; optimal extraction; Hotelling model.

(*) Pre-recorded video: Hotelling Model.

(*) Pre-recorded video: Hotelling Model Extensions.

(*) KO Chapter 6: “Managing Stocks: Natural Resources as Capital Assets”.

(*) Lecture notes on the Hotelling model for optimal resource extraction (on Canvas).

B. Faucon and S. Said, "Russia’s Oil Ban Accelerates Shift in Global Energy Flows", *Wall Street Journal*, 12/30/22 ([link](#)).

Lecture 6 (Feb 2): Oil and Natural Gas Extraction and Pricing (2)

Topics: oil and gas price volatility; forecasting; futures.

(*) Video: Khan Academy, Forward and Futures Contracts, Lessons 1-5 ([link](#)). Lessons 6-12 are optional, but please watch if you need further explanation after the lecture.

(*) M. Mandavia, “Liquefied Natural Gas Will Have a Less Frenzied 2023”, *Wall Street Journal*, 1/19/23 ([link](#)).

(*) J. Jacobs, 2023. “US Stockpiles Natural Gas as Warm Winter Temperatures Cut Demand”, *Financial Times*, 1/15/23 ([link](#)).

(*) R. Dezember, “U.S. Oil Costs Less Than Zero After a Sharp Monday Selloff”, *Wall Street Journal*, 4/21/20 ([link](#)).

R. Dezember, “U.S. Glut in Natural-Gas Supply Goes Global”, *Wall Street Journal*, 8/27/19 ([link](#)).

J. Hamilton, 2009. “Understanding Crude Oil Prices.” *The Energy Journal* 30(2): pp. 179-188 (see Readings folder on Canvas). (*Note: this reading is old but still relevant!*)

Lecture 7 (Feb 7): Upstream Investment under Uncertainty

Topics: NOCs vs. IOCs; upstream contracts; drilling investment under uncertainty; geopolitical risk; expropriations.

(*) A. Ulmer and C. Pons, “Venezuela Ordered to Pay Exxon \$1.6 Billion for Nationalization”, *Reuters*, 10/9/14 ([link](#)).

(*) A. Scurria, “Venezuela Creditor Cleared to Resume Citgo Seizure Efforts”, *Wall Street Journal*, 9/30/19 ([link](#)).

(*) M. Parraga and G. McWilliams, “U.S. Judge Approves Sales Process for Shares in Citgo Petroleum's Parent”, *Reuters*, 10/11/22 ([link](#)).

S. Valle, “Exxon Exits Russia Empty-Handed with Oil Project 'Unilaterally Terminated'”, *Reuters*, 10/17/22 ([link](#)).

ENERGY AND ENVIRONMENTAL POLICY

Lecture 8 (Feb 9): **Global Climate Change**

Topics: climate change impacts; the climate change debate; discounting; risk and uncertainty; social cost of carbon.

(*) Pre-recorded video: Climate Change Discounting.

(*) Lecture notes on climate change mitigation and discount rates (on Canvas).

(*) N. Farah and L. Clark, “EPA Floats Sharply Increased Social Cost of Carbon”, *E&E News*, 11/21/22 ([link](#)).

K. Rennert and B. Prest, “The US Environmental Protection Agency Introduces a New Social Cost of Carbon for Public Comment”, *Resources*, 11/15/22 ([link](#)).

B. Litterman, 2013. “What Is the Right Price for Carbon Emissions?”, *Regulation* 36(2): pp. 38-43 ([link](#)).

United Nations Environment Programme, 2022. *Emissions Gap Report*, Executive Summary ([link](#)).

Lecture 9 (Feb 14): **Externalities and Policy Instruments & OPEC Group Meetings**

Topics: environmental externalities; tragedy of the commons; Coase Theorem; property rights; taxes vs. subsidies vs. standards; effect of regulations on business; double dividend.

(*) Pre-recorded video: Externalities and Policy Instruments.

(*) KO Chapter 5: “Market Failures in the Environmental Realm”.

(*) KO Chapter 8: “Principles of Market-Based Environmental Policy”, pp. 139-162.

(*) G. Ip, “Carbon Tax Sidelined in Biden’s Push on Climate, Taxes”, *Wall Street Journal*, 3/24/21 ([link](#)).

Lecture 10 (Feb 16): **Cap-and-Trade (End Lecture: 4:30 p.m.)**

Topics: basics of cap-and-trade; cost-effectiveness; introduction to market design issues.

(*) Pre-recorded video: Cap-and-Trade.

(*) Lecture notes on the economics of cap-and-trade (on Canvas).

(*) KO Chapter 9: “The Case for Market-Based Instruments in the Real World”, pp. 168-184.

Lecture 11 (Feb 21): **Designing Real-World Environmental Markets**

Topics: market design issues in cap-and-trade markets; EU Emissions Trading Scheme; RECLAIM; acid rain trading program.

(*) KO Chapter 9: “The Case for Market-Based Instruments in the Real World”, pp. 190-198.

(*) KO Chapter 10: “Market-Based Instruments in Practice”, pp. 199-207, 208-210 and 217-220.

Lecture 12 (Feb 23): **OPEC Game Debriefing**

--- **MBA CORE EXAMS AND SPRING BREAK/OPPORTUNITY WEEK** ---

Lecture 13 (Mar 14): **U.S. and Global Policy Developments**

Topics: global carbon trading developments; U.S. climate change policy.

(*) J. Wolman, “Carbon Markets Are Heating Up”, *Politico*, 3/9/23 ([link](#)).

(*) S. Twidale, K. Abnett and N. Chestney, “EU Carbon Hits 100 Euros Taking Cost of Polluting to Record High”, *Reuters*, 2/21/23 ([link](#)).

(*) McKinsey & Company, “The Inflation Reduction Act: Here’s What’s In It”, 10/24/22 ([link](#)).

(*) “Q&A: What is China’s Carbon Trading Scheme?”, *Phys.org*, 2/7/21 ([link](#)).

“China Will Crack Down on Data Fraud to Bolster Its Ailing Carbon Trading Market”, *Bloomberg*, 3/4/23 ([link](#)).

THE ECONOMICS AND FINANCE OF RENEWABLE ENERGY

Lecture 14 (Mar 16): **The Economics of Renewable Energy & Introduction to the Electricity Strategy Game**

Topics: electricity strategy game; key trends in renewable energy; levelized cost of electricity.

(*) Pre-recorded video: Electricity Strategy Game.

(*) Lecture notes on renewable energy finance and policy, pp. 1-4 (on Canvas).

Lazard, “Levelized Cost of Energy and Levelized Cost of Storage – 2021”, 10/28/21 ([link](#)).

Lecture 15 (Mar 21): **Renewable Energy Finance (1)**

Topics: intermittency; the variable value of renewable energy; intro to renewable energy finance; tax credits; accelerated depreciation; solar leases and PPAs.

(*) Lecture notes on renewable energy finance and policy, pp. 4-7 (on Canvas).

(*) K. Treece, “How Does a Solar Lease Work?”, *Consumer Affairs*, 3/2/23 ([link](#)).

(*) B. Church, “Solar Lease vs. Solar PPA”, *Consumer Affairs*, 3/10/23 ([link](#)).

Department of Energy, 2023. “Federal Solar Tax Credits for Businesses” ([link](#)).

Lecture 16 (Mar 23): **Renewable Energy Finance (1) Cont’d & Electricity Strategy Game Auction**

Topics: energy storage basics; tax equity; securitization.

(*) Pre-recorded video: Energy Storage Basics.

(*) Lecture notes on renewable energy finance and policy, pp. 11-13 and 19 (on Canvas).

Video: Tax Equity Structure in US Renewable Energy Sector ([link](#)).

Lecture 17 (Mar 28): **Energy Storage**

Guest speaker: Marco Ferrara, Co-Founder and Senior Vice President, Form Energy

Topics: the economics of storage; the various technologies; the connection between storage and large-scale renewables deployment.

Note: this lecture will be held in JMHH F85.

(*) I. Ragazzi and S. Burger, “Solving the Clean Energy and Climate Justice Puzzle”, *Form Energy White Paper*, 7/20 ([link](#)).

(*) S. Burger, M. Ferrara, R. Go and A. Olson, “To Build a Zero-Carbon Grid, We First Need to Model It Accurately”, *Utility Dive*, 12/23/20 ([link](#)).

Optional: Form Energy's *Insights* page has several other interesting articles ([link](#)).

Lecture 18 (Mar 30): **Renewable Energy Finance (2) (Video Only)**

Topics: renewable portfolio standards; (S)RECs.

Note: There will be no lecture during the regular hours from 3:30-5:00 p.m., but I will hold extra virtual office hours about the content of this lecture on Monday April 3, 3:00-4:00 p.m. You can join on Canvas via the Zoom tab.

(*) Pre-recorded video: Renewable Energy Finance

(*) Lecture notes on renewable energy finance and policy, pp. 8-11, 13-18 (on Canvas).

Lecture 19 (Apr 4): **Renewable Energy Policy**

Topics: net metering; PACE; feed-in tariffs; tenders; import tariffs; green subsidy vs. carbon tax; waterbed effect.

(*) S. Borenstein, "Can Net Metering Reform Fix the Rooftop Solar Cost Shift?", *UC Berkeley Energy Institute Blog*, 1/25/21 ([link](#)).

(*) S. Evans, "Record-Low Price for UK Offshore Wind Is Nine Times Cheaper Than Gas", *CarbonBrief*, 7/8/22 ([link](#)).

J. Deign, "When Will European Offshore Wind See Negative Bids?", *Greentech Media*, 11/18/19 ([link](#)).

Lecture 20 (Apr 6): **Renewable Energy Project Finance**

Guest speaker: Gianluca Signorelli, VP, Head of Project Finance and M&A Execution, U.S. SB Energy (SoftBank)

Topics: renewable energy project finance, tax equity, capital structure, PPAs, hedging.

Note: this lecture will be held in JMHH F85.

(*) Norton Rose Fulbright, "Project Finance NewsWire", 3/23 ([link](#)). Please read pages 1-13, 14-18, and 23-20.

Lecture 21 (Apr 11): **Financing Offshore Wind Investments**

Guest speaker: Udit Goyal, Head of Project Finance, Offshore North America, Ørsted

Topics: investing in wind energy, wind energy finance, wind energy contracts.

Note: *this lecture will be held in JMHH F85.*

(*) Center for American Progress, “The Road to 30 Gigawatts: Key Actions to Scale an Offshore Wind Industry in the United States”, 3/14/22 ([link](#)).

(*) U.S. Department of the Interior, “Biden-Harris Administration Sets Offshore Energy Records with \$4.37 Billion in Winning Bids for Wind Sale”, 2/15/23 ([link](#)).

K. Martin, “Cost of Capital: 2023 Outlook”, Norton Rose Fulbright, 3/6/23 ([link](#)).

E. Pogue et al., “US Offshore Wind Challenges”, *Project Finance International*, 4/20/22 ([link](#)).

Lecture 22 (Apr 13): **Electricity Strategy Game Debriefing**

Lecture 23 (Apr 18): **Unintended policy consequences & Course Wrap Up**

Topics: congestion policies; enforcement; cheating; emissions leakage; course summary.

Lecture 24 (Apr 20): **Exam**

Note: *the exam will be held during the regular class time but spread over two different rooms (location info below).*

DUE DATES

Assignment dates

Assignment 1: posted on February 2, due by February 16

Assignment 2: posted on March 9, due by March 27

Assignment 3: posted on March 28, due by April 18

OPEC Game

January 31 Introduction to the OPEC game in class
February 3 Production quantities due by 10 p.m. for phase 1, period 1
February 6 Production quantities due by 10 p.m. for phase 1, period 2
February 8 Production quantities due by 10 p.m. for phase 2, period 1
February 9 Production quantities due by 10 p.m. for phase 2, period 2
February 10 Production quantities due by 10 p.m. for phase 2, period 3
February 13 Production quantities due by 10 p.m. for phase 2, period 4
February 14 OPEC group meetings in class
February 15 Production quantities due by 10 p.m. for phase 3, period 1
February 16 Production quantities due by 10 p.m. for phase 3, period 2
February 17 Production quantities due by 10 p.m. for phase 3, period 3
February 20 Production quantities due by 10 p.m. for phase 3, period 4
February 23 OPEC strategy memo due before class
February 23 OPEC game debriefing in class

Electricity Strategy Game

March 16 Introduction to the Electricity Strategy Game in class
March 20 Bids due for the ESG test run
March 23 First ESG divestiture auction, in class
March 27 ESG strategies due by 10 p.m. for year 1, day 1
March 29 ESG strategies due by 10 p.m. for year 1, day 2
March 30 ESG strategies due by 10 p.m. for year 1, day 3
April 3 Sealed portfolio bids for year 2 due by 10 p.m.
April 5 ESG strategies due by 10 p.m. for year 2, day 1
April 6 ESG strategies due by 10 p.m. for year 2, day 2
April 7 ESG strategies due by 10 p.m. for year 2, day 3
April 13 ESG strategy memo due before class
April 13 ESG debriefing in class

Exam

Date/time: Thursday April 20, 3:30-5:00 p.m.

Locations: last names A through H – SHDH 211; last names I through Z – SHDH 1206