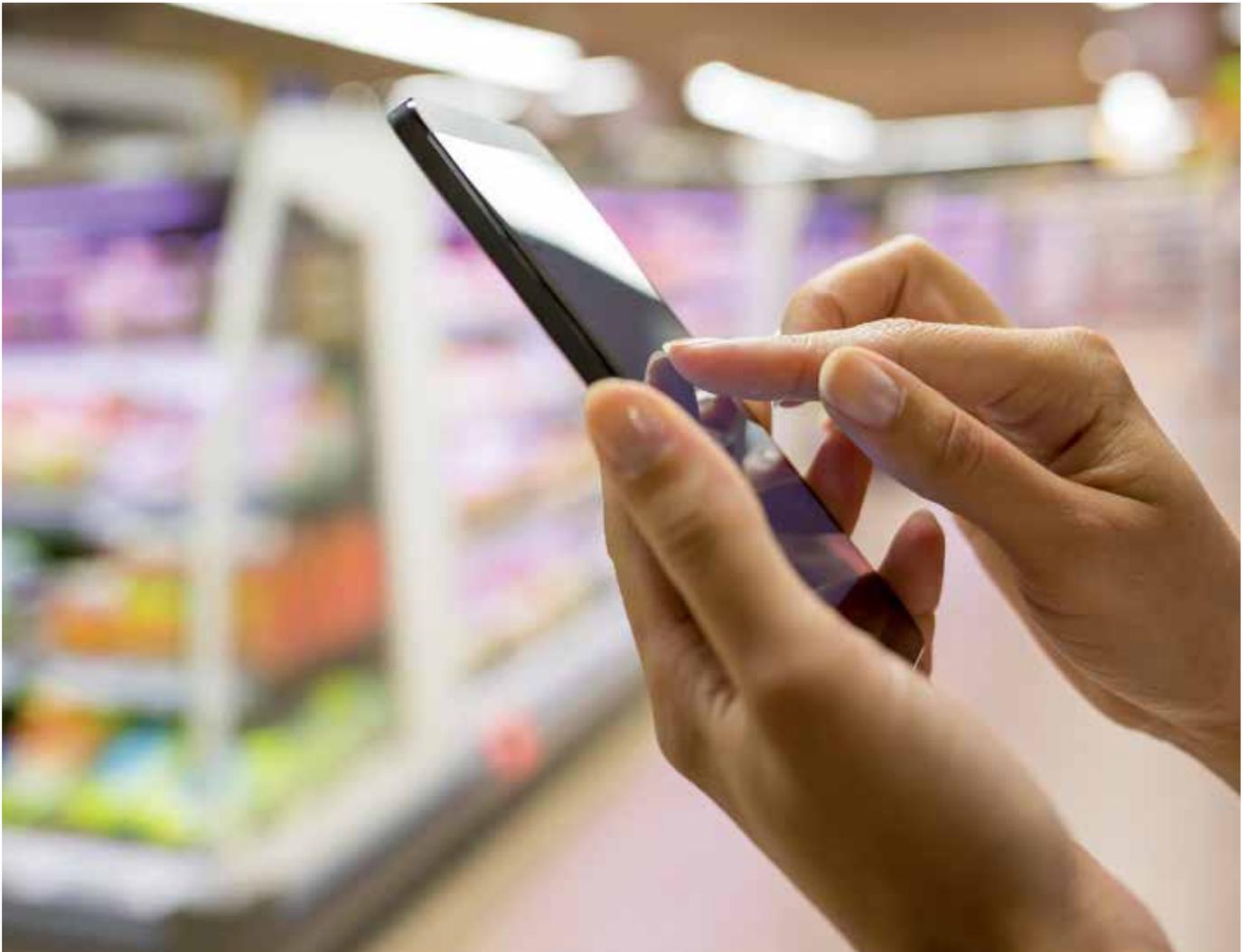


Ecommerce, iLottery, and Their Impact on Lottery Retail Sales



Selling products online complements, not cannibalizes, brick-and-mortar sales

Over the past decade, the Internet and ecommerce have contributed to a substantial transformation of many industries, often disrupting consolidated business sectors in a way that was unimaginable only 20 years ago. A few examples include:

- › Music, which experienced dramatic shifts in selling channels (and profitability) from physical recordings and record stores to digital distribution.
- › Travel, where most reservations, ticketing, and payment systems are now digital.
- › Health care, where the growing use of digital diagnostic equipment and record management will further accelerate with the spreading of wearable devices.
- › 3D printing, which will have dramatic impact on the value chain,

logistics and distribution, and cost of goods sold in several industries, including for example construction.

The trend toward digital is unstoppable and will only intensify. The speed of transformation, however, will vary greatly by industry, based on specific factors such as level of globalization, geographical differences, and regulation, radically shifting the relative relevance of different industries to consumers. This is especially the case in the entertainment sector, to which lottery belongs, where different industries satisfying similar consumers' needs compete for customer share of wallet – and customer share of mind.

While some have believed that digital distribution might completely overcome physical distribution, this is unlikely; both are an indispensable part of life and of business. Humans are social beings that need to

International Benchmark on Internet Sales Penetration over Total Lottery Sales (percent)

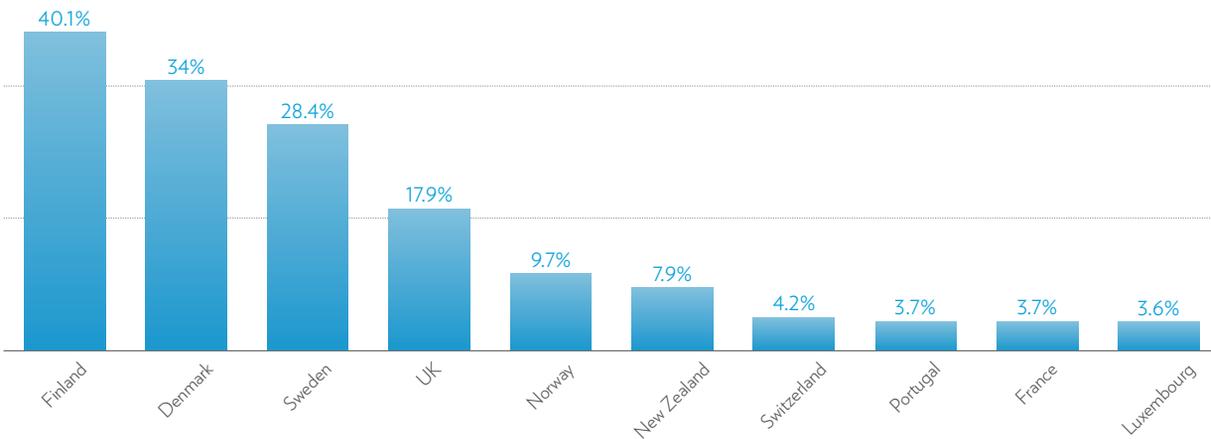


Figure 1 – Top European Lotteries for Interactive Sales

interact with other people and to make and touch things. Therefore, retailers are responding to the new challenge through innovation, and the most prominent ones are investing heavily in developing digital marketing and ecommerce capabilities: 9 of the top 12 ecommerce retailers are companies with established brick-and-mortar operations (source: Global ecommerce Research, Internet Top 500 Retailers in 2013) who are reacting to the evolving context.

As a result, the line between brick-and-mortar and online operations is blurring; more and more corporations are focusing on the omnichannel experience they can provide to create new sources of value. A few examples:

- ▶ Established retailers are pushing hard to develop their digital capabilities; Walmart now operates ecommerce websites in 10 countries; its largest, Walmart.com, sees 45 million visits a month, a number that is growing every year.
- ▶ More and more retailers are offering their physical stores as point of delivery for goods purchased online; on the other end it is rumored that Amazon is considering building physical stores.
- ▶ Apple appointed Angela Ahrendts, the former CEO of luxury brand Burberry, SVP for online and retail stores, clearly recognizing the opportunity to managing the two channels as a single integrated means to reach out to customers.

Mobile is part of this trend, and it is increasing its market shares among online sales:

- ▶ According to Criteo, in Q1 2015, 34% of all global ecommerce transactions, and 29% in the U.S., were via mobile.
- ▶ A senior executive at Walmart declared that over the 2014 Holiday season, mobile represented “70% of the orders ... taken through [their] digital business.”

Lotteries are taking part in this transformation; since the 1990s, the interactive channel has been a key international growth driver. Today several European lotteries see more than 25% of their sales being generated through digital channels (see Figure 1).

iLottery is also a key driver to modernize the lottery brand and to enable lotteries to be more relevant for consumers. The interactive channel:

- ▶ Attracts the young adult demographic that traditionally has been more difficult to serve effectively (see Figure 2 for an example from a European jurisdiction of the demographics of different games/channels).
- ▶ Enables innovative content and innovative ways to promote, for example through social spaces, traditional games.

These are all opportunities that need to be embraced by lotteries and their most loyal evangelists, the retailers.

In lottery and the general retail industry, interactive does not necessarily cannibalize retail sales, and can in fact be leveraged not only to improve player convenience but also to make the retailers a more attractive destination for consumers. The increased use of personal devices and smartphones can accelerate in-store innovations and improve the retail experience. New devices such as digital mirrors, which take a 360-degree video, allowing clients to see

Age Distribution of Customer Base (percent)

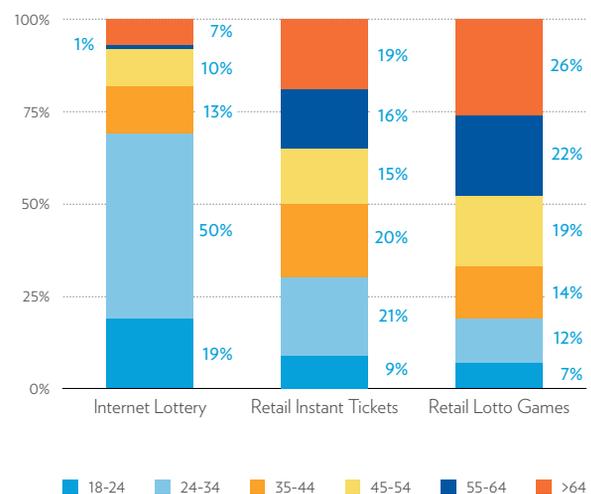


Figure 2 – Player Demographics of Interactive Lottery vs. Retail Lottery (example of a European lottery jurisdiction)

clothing on themselves from all angles, also enhance the consumer retailer experience; similarly, innovative concepts such as Bring Your Own Device, larger digital screens, paperless playslips, iBeacons, on-premise tethered wagering, and virtual betting can all enable further in-store playing opportunities and enhance the social aspect of the games. At the same time, leveraging these features will help lotteries to compete with other entertainment industries and to stay relevant to consumers as they increase the adoption of digital services and in-store experiences. This is already happening in other fields; 10% of Walmart’s online sales, for example, are for purchases made through mobile devices by consumers in-store.

Retail sales are increasing even while ecommerce is growing; in February, NRF (the National Retail Federation, the world’s largest retail trade association) forecasted a 4.1% increase for 2015 U.S. retail industry sales vs 2014, with non-store retail sales growing between 7% and 10%. Due to the interaction between the online and retail channels, the combination of the two is creating value, rather than developing one channel at the expense of the other.

“Not only are lottery retailers not negatively impacted by interactive sales, in some cases they can actually benefit from the development of interactive channels.”

International experience derived from lotteries with a longer history in the interactive channel shows a similar story. Figure 3 illustrates statistics from a number of best practice interactive lotteries where, since the launch of the online channels, both interactive and retail lottery sales have grown. It is important to note that not only are lottery retailers not negatively impacted by interactive sales, in some cases they can actually benefit from the development of interactive

channels, as this provides them for additional opportunities to earn a commission. Several examples exist, some of which are also emerging in the U.S.:

- » Often lotteries, to further promote integration between the interactive and the retailer channel, offer consumers the ability to top-up their ewallet in the stores, often recognizing a commission for the retailers:
 - » In the U.S. and Europe, some jurisdictions allow players to top up their ewallets at retail and reward retailers for that activity; in Italy about 35% of electronic top-ups occur at the retailers.
 - » Offering the option to pay cash in store for products ordered online is another possibility, and one that has been embraced by the general retail community: Walmart, for example, has offered this option since 2012.
- » IGT OnPremise mobile sports betting and casino gaming is made available at a dozen MGM Resorts in Nevada as a way to allow players to enjoy convenient and exciting new ways to wager seamlessly across multiple gaming channels through mobile, whether they’re at a sports book, slot floor, restaurant, or poolside.
- » In Norway a player card is mandatory for draw based game wagering at retail. This offers additional convenience to players, as all winnings they earn are automatically deposited to their player card. A similar optional feature is available to retail players in Sweden, where it is leveraged for 65% of wagers.
- » On-premise and tethered wagering being developed for keno retailers will provide retailers the possibility to earn a commission without having to input the transactions at the terminal, as they will be autonomously wagered by players through their device.

The facts are clear. Adding Internet sales to land-based retail can augment both channels while improving player convenience and increasing product relevance.

Contribution of Retail Sales to Lottery Sales Increase after Launch of Internet Wagering (percent)

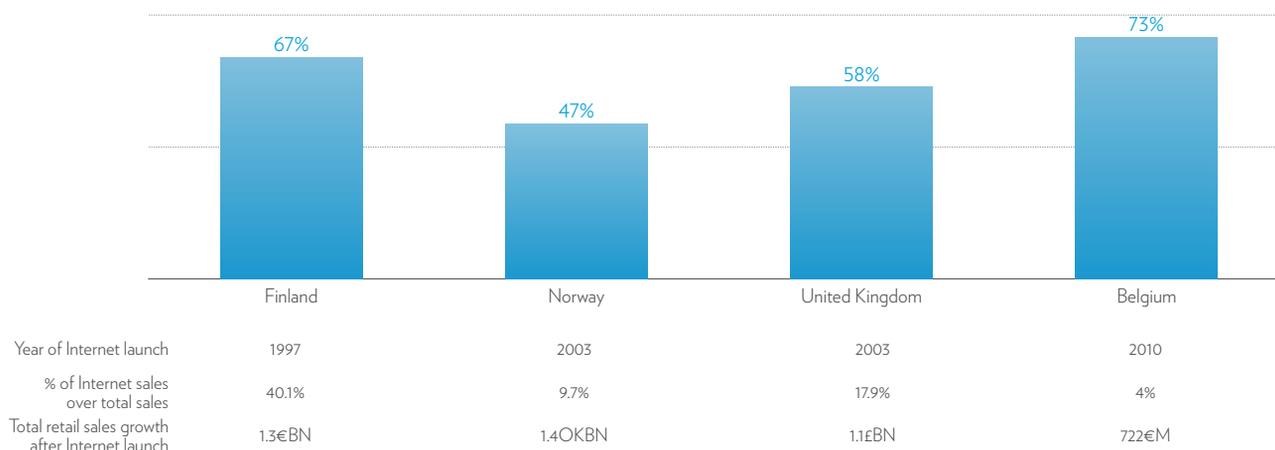


Figure 3 – Impact of Internet Wagering on Retailer Lottery Sales

