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Paul Jason, Public Gaming: Is the 'controlled opening' the best regulatory model for France and La Française des Jeux?

Christophe Blanchard-Dignac: The fact is that the world is changing, the markets are changing with it, and the regulatory frameworks are changing along with everything else. So, the issue really is not about what is best for society as an abstract exercise or philosophical discussion. The issue is how to optimize the position of our stakeholders in the context of the way of the world as it really works. We need to ask ... What can lotteries do to position themselves for success, not in an ideal world that doesn't exist, but in the real world that does? Markets and regulatory changes are being forced upon all of us. We can choose to resist those changes and hope they don't happen too quickly, or we can choose to get out in front and position lotteries to stay preeminent gaming operators in the world. At la Française des Jeux, we are choosing to embrace the opportunity to change and adapt. We want to meet the needs of the 21st century consumer

Introduction: The regulatory framework in Europe especially for sports betting has been in quite a state of flux for the past number of years. The EU Commission has challenged the member states to change their regulatory frameworks to allow for more open competition. As a result, member state governments are reshaping those frameworks. This is affecting the basic lottery model which has always depended upon a stable, predictable, and exclusive marketplace. All lotteries are striving to defend the interests of their stakeholders, but the decisions about how the regulatory models change are being made not by lotteries as much as by political leaders. As shapers of public policy determine how the markets are to be regulated, lotteries are given the task of adapting to those changes, optimizing performance, and continuing to generate funding for Good Causes.

The EU Commission required France to make changes to its online regulatory model and France complied by implementing what is called a 'controlled opening'. The markets in many gambling categories (like sports-betting and Internet gaming) are opened up to multiple licensed operators. Other categories, like lottery, continue to be controlled by the state. The lottery and gaming community is watching to understand how this works because the French model meets the requirements of the EU Commission while also serving the needs of the state. Likewise, lotteries are watching to see how the French lottery, la Française des Jeux, adapts to a regulatory model that pitches the lottery operator into direct competition with an ambitious, sophisticated, and well-funded stable of commercial enterprises. La Française des Jeux is the world's third biggest lottery operator, with €10.55 billion of bets placed in 2010, a 5.5% increase over 2009. As Chairman and CEO for the past ten years, Christophe Blanchard-Dignac is charged with steering the lottery into this new age of more opportunity combined with more challenge.

on their terms, evolving our approach to be the kind of service provider that keeps pace with its customers. That means facing a dynamic marketplace that is more difficult and challenging than ever. But it is also richer with potential for the entrepreneurial operator to create better products, innovate the business model, build new and better distributional channels, and connect with the consumer in new, forward-leaning and always sustainable ways.

Lotteries have some distinct competitive advantages that should empower us to do well in this dynamic new world of gaming. The thing is, we need to face up to the reality that some of our competitive advantages are being obsoleted by changes in the marketplace and regulations. Frankly, lottery products and business practices have been very fortunate to enjoy a life-cycle that has lasted as long as it has. Most businesses have to reinvent themselves and their products every three to five years to just stay relevant and avoid being displaced by a competitor: life cycles are going to be shorter and shorter. The

time has long since come that lottery needs to reinvent itself. Of course, we want to do everything we can to protect the model that serves the interests of our beneficiaries and stakeholders. The regulatory model that provides protection for the traditional lottery games is being preserved for the benefit of the general interest. But there's two things happening that require us to evolve our entire approach to the business. First, the regulatory model that governs the broader gaming and gambling industry is changing, opening up more recreational gaming options for the consumer. Second, consumer preferences themselves are changing and we need to evolve our products and business practices to keep up with those changes. So, la Française des Jeux is committed to accelerating its own evolution to stay out in front of the changes, stay ahead of the competition, and meet the needs of the consumer.

Prior to the controlled opening, France had a flourishing underground market, didn't it?

C. Blanchard-Dignac: Of course. Just like all

jurisdictions that attempt to prohibit gambling. Complete prohibition of online gaming does not work. That just provides a fertile market for illegal operators to satisfy the consumer demand. That's why it is so much better for the state to regulate the market. Providing a regulated option for the players also gives the state the flexibility to prohibit the more dangerous kinds of games and ensures that licensed operators are held to high standards of integrity, security, and Responsible Gaming. Lotteries need to understand and embrace that fact and support the formation of a sensible regulatory policy, one that addresses the market realities, protects the consumer, and makes sense for everyone. Our transition is made easier by genuinely embracing the agendas of our political constituents.

Could we get a brief overview of the French regulatory framework?

C. Blanchard-Dignac: There's only one lottery in France, la Française des Jeux, and it has exclusive rights for all offline and online lottery gaming. The only gambling activity that is open to competition under a licensing process includes online sports betting, online horse betting, and online poker. Online poker was prohibited until last year. That does not mean there weren't hundreds of thousands of people playing online poker in France. There were in fact. They were just playing with illegal operators based outside of France, not paying taxes, and not complying with the highest standards of consumer protection and integrity. That is obviously the worst of all possible worlds – high social costs and no benefit to society. Another way to think of complete prohibition is that you are simply allowing the market to be regulated by offshore operators who don't pay their fair share to the community or comply with high standards of integrity and player protection.

Still, it must be a difficult decision to invite a regulatory framework that opens up the market.

C. Blanchard-Dignac: Of course, it's always difficult for a lottery director to suggest to the government, in effect, to open up the online market to competitors. The decision is easier, though, when you re-frame the question. Would I rather compete with competitors who are regulated, and held to the same standards and tax obligations as la Française des Jeux, or would I rather compete with unregulated offshore competitors whose cost structures are so much lower since they do not pay taxes or normal salaries? From a business standpoint, our stakeholders are much better served by a regulated market in which la Française des Jeux is not at a competitive disadvantage. So now we have competition in the online sports-betting space. Offline is still under exclusive rights to la Française des Jeux and that represents nearly 10% of our revenue. Online sports-betting is only 1% of our activity and now that is legally open to competition. But at least now it is regulated and properly licensed; and society is enjoying the benefit of tax receipts from online sports-betting, and players have better protection. After one year, we represent about 14 % of the online sports-betting market; not as much as we would like, but much more than we had before the market was opened (4%). And - this is the most important - our off-line sports-betting business and lottery revenue base has not been damaged. In fact, it appears that all the advertising done by the online sports-betting operators could have benefitted our off-line sports-

betting business where la Française des Jeux is the exclusive operator. Most consumers still prefer to go to the off-line outlets than to the online operators. This has worked out very well for us, since la Française des Jeux has 36,000 outlets in France, with 25,000 of them able to sell sports-betting products.

Weren't the retailers concerned that they would lose customers to the online channels.

C. Blanchard-Dignac: The retailers were very anxious. They did think the customers would easily switch to betting and buying the products over the Internet. It did not happen that way at all. The customers are used to their retailers. They like to go to a place where they know each other, they can talk with the other, they can interact and enjoy being with and around other people. Our land-based outlets do very well and are our main competitive advantage. The younger players are definitely online more and we do need to make the products available to them on a variety of media and channels.

The main thing is that no matter what the channel or method of distribution, the games need to be secure and marketed in a responsible way. Security and integrity are two of our key brand attributes what we want people to think of when they think of la Française des Jeux.

Everyone recognizes that Responsible Gaming is good public policy. But it seems to me that you are turning it into an effective competitive advantage as well.

C. Blanchard-Dignac: Exactly. For la Française des Jeux, Responsible Gaming is the definition of gaming. It's embedded into our products from the beginning of the product development cycle. Just as a product is tested to see whether it appeals to the consumer, we test to make sure the psychological and emotional response will not lead to problem or addictive gaming. We also train our retailers to help us make sure the games are good for the consumers and not producing any negative effects. We cannot eliminate Problem Gambling, but there are many things we can do to minimize it, and monitor player behavior to respond quickly whenever there is evidence of a problem. We think of Responsible Gaming as our economic mission; and our social mission is of course to give back money to the society.

You are now streaming live sports events on your website www.Parionsweb.fr. I would think this would attract a much larger player group.

C. Blanchard-Dignac: We hope so but it will take time. This would be a great example of how the need to compete with aggressive commercial operators is challenging us to develop new ways to connect with the consumer. We are developing a much better understanding of new media and how it can augment all of our business groups. Competing in new spaces puts us into a constant state of acquiring new capabilities that enhance every part of our business, including traditional lottery.

La Française des Jeux transfers about 2.6 billion Euros a year over to its beneficiaries, one of which is grassroots sports organizations. The commercial licensees seem to always be complaining about taxes they are required to pay to support grassroots sports organizations.

C. Blanchard-Dignac: We are pleased and proud to support grassroots sports. Along with protecting the players, serving our beneficiaries is our mission,

our whole reason for existence.

The online operators seem to have a competitive advantage because they just transferred the underground market which they had been serving illegally over to their newly legitimized websites.

C. Blanchard-Dignac: There are two conditions for lottery to be successful. The first thing is to have an enforceable regulatory framework that holds everyone to the same tax and regulatory standard. Lotteries that transfer a significant percentage of their revenues to beneficiaries, and adhere to a high standard of player protection and integrity cannot compete in an unregulated market dominated by off-shore operators who do not comply with those standards.

The second thing we need is time. Operators that have taken many years to build their market illegally have a big advantage when the markets are opened up. The huge customer base they have is easily migrated right over to their new licensed website. Games as online poker for instance require a sufficient volume of players. Operators which have been complying with the law have no base of players to start out with. That makes it almost impossible to gain any traction against the operators which acquired their base and experience illegally. So it is vital that the regulatory framework be implemented in a fashion that enables those which have been complying with the laws to have a chance against competitors that have been operating illegally for years. For other jurisdictions considering a similar regulatory framework, a simple way to remove that unfair competitive advantage would be to require the customer accounts that were acquired prior to having a legal license to do business, to simply close those customer accounts, giving back the money to the customers, so that we are all on an equal footing. Operators could then all open their virtual doors for business at the same time and compete for the customers. All that being said, we are making good progress in all product categories and distribution channels.

That's been the big obstacle for la Française des Jeux in the online poker space?

C. Blanchard-Dignac: Yes. We also needed time to build from scratch the IT and supplier infrastructure in these new spaces like online poker. We are very good in land-based outlets, but we did not have an online presence and that is a different channel with an entirely different player group. If we have a responsible regulatory framework that creates an even playing field for all competitors and laws and tax obligations that are enforceable, and we have time to prepare for launching a competitive product and business model, then we will be successful. France now has a consistent regulatory framework. It strikes a well thought out balance by allowing a competitive, dynamic marketplace to coexist within a framework that protects the consumer. Preservation of 'Public Order' and the highest standards of Responsible Gaming are key parts of the French regulatory framework.

The EU Commission appears to be objecting to Germany's system of multiple operators in sports-betting but keeping the lottery exclusive to the government. The basic idea being that lottery is less likely to cause problem gambling than sports-betting, so if you allow multiple operators in sports-betting, you should allow multiple operators in the lottery space as well.

C. Blanchard-Dignac: The French government

has taken a proactive role at evolving our regulatory framework to allow “controlled” competition among multiple vendors consistency of the national regulation. The online gaming market is an especially dynamic, diverse, and competitive marketplace. The regulatory model is designed to support an industry that will grow and evolve, provide economic opportunity for a diverse commercial community, and also to respect the consumer, preserve the integrity of sports, protect the interests of the state, and serve the interests of the general public. The end result is a model that balances this wide variety of objectives. Gaming and gambling is a complex, multi-faceted industry and we think our regulatory framework addresses the many considerations in a fashion that works well for everyone. Commercial operators would prefer lower taxes, we would prefer exclusivity, but all of us now have an equal opportunity to pursue our goals and meet the expectations of our stakeholders. As pertains to the lottery, the exclusive arrangement is for the purpose of protecting the players and the interests of the state. The French online experience provides the foundation for a responsible and dynamic marketplace that respects the specificity of gaming while being compatible with EU Treaty.

More About la Française des Jeux

La Française des Jeux is the world’s third biggest lottery operator, with €10.55 billion of bets placed in 2010, a 5.5% increase over 2009. Offering its 28 million customers a range of lottery games and betting services for major sporting events, it is committed to responsible, recreational betting in secure conditions. Together with its subsidiaries Lotsys and LVS, the group has over 1,200 employees, a network of 35,800 local points of sale and a multimedia gaming service with some 900,000 registered users. It operates in the online poker market through barrierepoker.fr, a jointly held subsidiary set up with Groupe Lucien Barrière.

La Française des Jeux has an active sustainable development policy. In 2010, it redistributed 95% of its gaming proceeds, representing almost €10 billion, to its customers and retailers, sport and the community.

The scratch games range posted a 10.6% increase

in sales to €4,290 million. The growth of the lottery activity is being driven by a range of 19 scratch games with 21 million customers, with, in particular, €1,189 million in sales for Cash 500,000€, which is now FDJ’s third most popular game.

The draw-based games range continues to set the standard. The 3.7% decline in sales to €3,490 million reflects a calendar effect (1 Friday 13 in August 2010 compared with 3 Friday 13s in 2009). With €1,538 million of sales, Loto is set to become the leading lottery game. Euro Millions sales were up to €1,104 million thanks to the effect of super draw rollovers.

Rapido, a fast keno game, with €1,552 million in sales, continues to be penalised by the difficult operating conditions following implementation of the smoking ban in bars. The company’s testing of Amigo, a new generation of point-of-sale games, continues in four regions.

The 24,700 ParionsSport outlets recorded €1,051 million of sports bets, a 42% increase from €741 million in 2009. These products, which are simple to use and well adapted to leading public POS betting (800 bets per week on five different sports), were used by some 2.9 million customers.

The company successfully negotiated the opening up to the competition of online sports betting by prioritising operational and technological performance and preservation of core values. The surge of ParionsWeb, an online service which caters for experienced gamblers (5,000 bets per week, including live betting, on 12 different sports), boosted the company’s online sport betting sales by 112%, thereby quadrupling its market share and furthering its aim of winning a quarter of the online sports betting market by 2012.

Winnings up 7.6%

95% (almost €10 billion) of all gaming proceeds were redistributed. Players’ winnings rose 7.6% to almost €6.8 billion and FDJ paid out on 800 million prizes. 92 winners became millionaires and in July 2010 there was a record win of €42 million in Euro Millions.

FDJ redistributed €177 million to the national sports development centre (Centre National de

Développement du Sport - CNDS). This brings the total it has redistributed into grassroots sport over the last 30 years to €4 billion.

It has redistributed over €500 million to 35,800 FDJ retailers located in 12,100 towns and villages, equivalent to more than 25,000 jobs.

Digital plan: a goal focused on 28 million customers

Priority to the network: The FDJ gaming model relies on the 27.8 million customers who actively frequent its unique network of local points of sale. The plan prioritises these points of sale, with the aim of promoting them, boosting their effectiveness through new technologies and continuing with their digitalisation. The group will invest €170 million in this network between now and 2015. The first new-generation lottery terminals will be installed in the coming months, and location search software, dynamic jackpot display systems and the first elements of a local community programme will also be gradually put in place.

Development of fdj.fr: Another aim under the plan is to raise the lottery website’s profile and boost its supporting role for the points of sale (96% of visitors to the site are network customers) while using it to promote a gaming model based on the values of local access and responsible, recreational gaming. The company will continue to make the website more user-friendly and to promote it through new services and innovative products, such as the revamped online bingo, smartphone applications (2011).

FDJ’s commitment to customer service will be similarly evident in its efforts, through its 2011-2015 digital plan, to ramp up sales through its extensive network covering some 27.8 million customers and to support its increasingly successful multimedia gaming service, which has 900,000 registered users. ♦