



Lottery Growth: Seeing and Adapting to Change in the Retail Markets

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For many people the “face of the lottery” is reflective of where they buy and see lottery products on sale.

During 2009, in the U.S., these impressions continued to be shaped predominantly by three types of retail trade class accounting for almost 73% of the outlets selling lottery products and over 75% of the \$47.3 billion annual lottery sales reported by retail class: grocery, convenience and gas/convenience. (Figure 1)

Fig 1: U.S. Lottery CY 2009 Sales by Key Retail Trade Class

| Trade Types | Clerk-Assisted and All Self-Service | | |
|-------------------|-------------------------------------|-------|----------------|
| | Outlets | Sales | |
| | # | % | % |
| Grocery | 30,229 | 15.6 | 17.6 |
| Convenience Store | 37,080 | 19.1 | 23.5 |
| Gas/C-Store | 73,329 | 37.9 | 34.1 |
| Sub-Total | 140,638 | 72.6 | 75.2 |
| Total Retailers | 193,718 | 100.0 | \$47.3 billion |

Total Outlets and Sales are for those U.S. lotteries providing a breakdown of sales by retail business class. Total CY 2009 sales all reporting U.S. lotteries were \$53.8 billion. Total CY 2009 retailers, including full service and instant only, were 199,419.

Source: LaFleurs 2009 Annual Industry Survey

These impressions are likely to vary widely since for many jurisdictions the majority of outlets are independent or “Mom and Pop” local operators compared to multi-state chain operators with reasonably uniform branding and presentation.

Yet, opportunities to enhance the lottery shopping experience while reaching a broad player and prospect audience through expanded distribution very much exist. As recently pointed out by Don Stanford, GTECH Acting Chief Technology Officer, within the Top 100 U.S. retailers there are at least ten with over 45,000 stores representing over \$854 billion annual sales — and do not offer lottery products. (Figure 2)

The challenge is: how do lotteries realize these opportunities to grow sales?

Fig 2: Select Non-Lottery U.S. Retailers

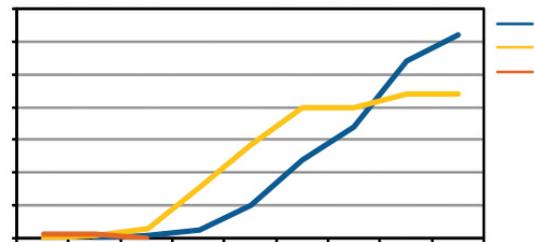
| Top 100 Retailer Rank | Title | Annual Revenue | Store Count |
|-----------------------|----------------|----------------------|---------------|
| 1 | Wal-Mart | \$405,607,000 | 7,873 |
| 3 | Costco | \$72,483,020 | 544 |
| 4 | Home Depot | \$71,288,000 | 2,274 |
| 5 | Target | \$64,948,000 | 1,682 |
| 6 | Walgreen | \$59,034,000 | 6,934 |
| 7 | CVS Caremark | \$48,989,900 | 6,981 |
| 8 | Lowe's | \$48,230,000 | 1,649 |
| 9 | Sears Holdings | \$46,770,000 | 3,918 |
| 13 | Rite Aid | \$26,289,268 | 4,901 |
| 35 | Dollar General | \$10,457,668 | 8,362 |
| Total | | \$854,096,856 | 45,118 |

Source: July 2009 Stores Magazine

A Brief History of Change

During the late 1960's when modern U.S. lotteries came into being, independent stores with personal relationships between the owners and customers were prevalent. Lottery equipment, systems and programs were accepted as necessarily “outside” the individual store accounting and management system for various reasons, not the least basic cash drawer management of high volume lottery product sales. This assumption continued with the growth of Instant Games and their more complex inventory and labor requirements. (Figure 3)

Fig 3: U.S. Lottery Sales Mix Trends



Source: GTECH

However, as personal lifestyles changed with dual-income families and more mobility, customer shopping needs have focused on speed, convenience and ease. The retail direction shifted and continues to focus on one-stop shopping. Chain operators have taken this response several steps further.

The Three C's

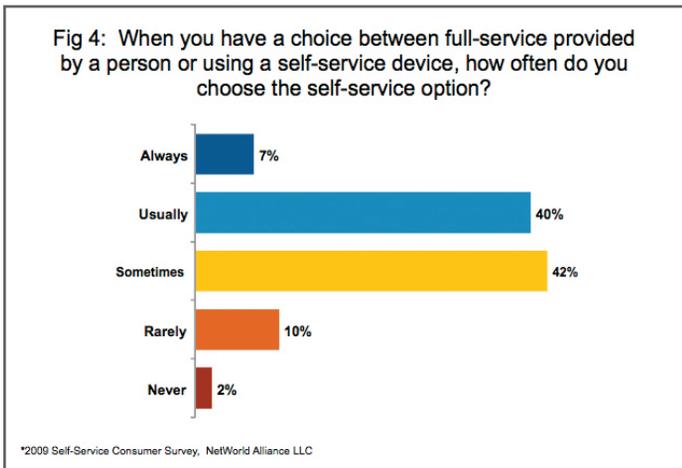
Motivated by competition, cost-efficiency and customer service (the three C's), chain store groups have been updating and streamlining the customer shopping experience for not only merchandise, pricing, promotion, loyalty programs but also its management. As multi-state operators, their efforts have led to:

- More uniform branding and store presentation
- Store automation
- Supply chain management
- Inventory management at the SKU level
- Right-sizing store formats for different local situation
- Adoption of industry-wide operating standards through associations such as PCATS (Petroleum Convenience Alliance for Technology Standards) and ARTS (Association for Retailing Technology Standards – at the National Retail Federation).

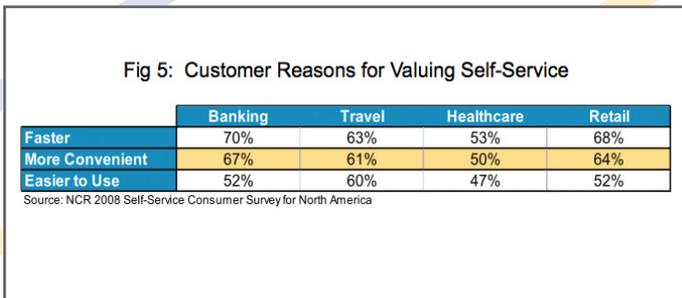
During recent years with rapid consumer technology adoption and severe economic stress the chains have offered more options to help customers “shop smart:”

- More self service
- Branded gift cards that have become an \$87 billion industry almost overnight
- More personal service through improved staff knowledge (an attitude shift from “Do-It-Yourself” to “Do-It-With-You”)

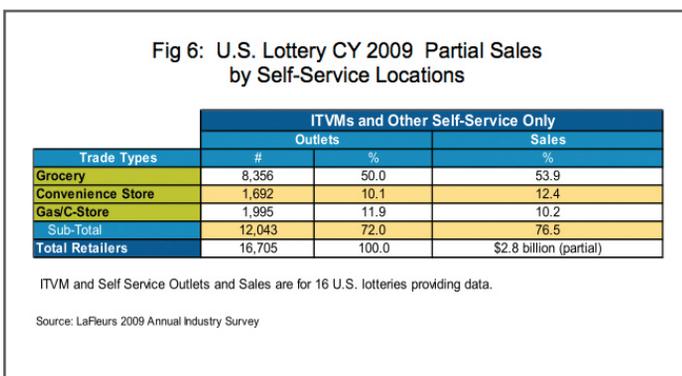
Customer preference for self service has been expanding with almost 90% of people opting for a self-service solution at some point in a 2009 survey. (Figure 4)



Across several different industry segments the values customers seek in self service are the familiar ones: speed, convenience and ease. (Figure 5)



The impact of self service in the lottery industry is showing up. Even with only partial results reported, at least 5% – 6% of sales — and probably as high as 10% — are originating from Instant Ticket Vending Machines (ITVMs) and other self service machines, including both Instant and Online Games. (Figure 6)



The Three L's

While some chain store groups have been willing to have lottery equipment and systems outside of their systems, other major players noted above have continued to resist. Their concerns are that lottery products, especially Instant Games, do not fit their operating models and will contribute to inefficiencies they have worked to overcome: lines, labor and loss, or shrinkage (the three L's).

They are looking to lotteries to work inside their systems so they can sell, manage and account for lottery products like any other product or SKU within their stores.

Of course, not all chain store groups are the same and may require different approaches to accommodate their management approaches.

That's why GTECH has been devoting time, money and resources to developing suites of solutions to help lotteries achieve this potential growth:

- Lottery Inside integrates Online Game Quick Pick sales into multi-lane third-party POS equipment with options for using the store printer and paper and enables accounting into the retailer system.
- Gemini Family of Self-Service Terminals sells Instant and Online Games, of Instant Games only, with push-button ease with configurable peripheral options in the industry's narrowest footprint.
- DASH Store Services (Display and Service Handlers) offers a store-within-a-store concept for retailers seeking route service, manned kiosk and merchandising management.
- ES Lottery Services Portal can provide web-based lottery reporting for Instant and Online Games that can be downloaded into back office systems and allow chain managers to see reports for all stores, including those across state lines.

The company is also going beyond its patented Smartcount Instant Games inventory management system for individual retailers to find answers for ticket accounting and management that meet chain store requirements.

The end goal is to achieve a win-win plan of flexible retail solutions that benefit lotteries and address chain store group concerns with the three L's plus back-end accounting.

A Final Thought

Individual lotteries may have been at a disadvantage dealing with some of these chain store groups. After all, they are multi-state marketers and operators and used to working with similar organizations. With the recent collaboration between the MUSL, Powerball and MegaMillions groups to cross sell the two largest U.S. jackpot games perhaps there is now a way to offer broad lottery retail management solutions, still adaptable to local business requirements, at the multi-state level.

The potential for increased distribution and sales within contemporary customer-friendly environments for most, if not all, lotteries should provide plenty of incentive to consider this approach. ♦