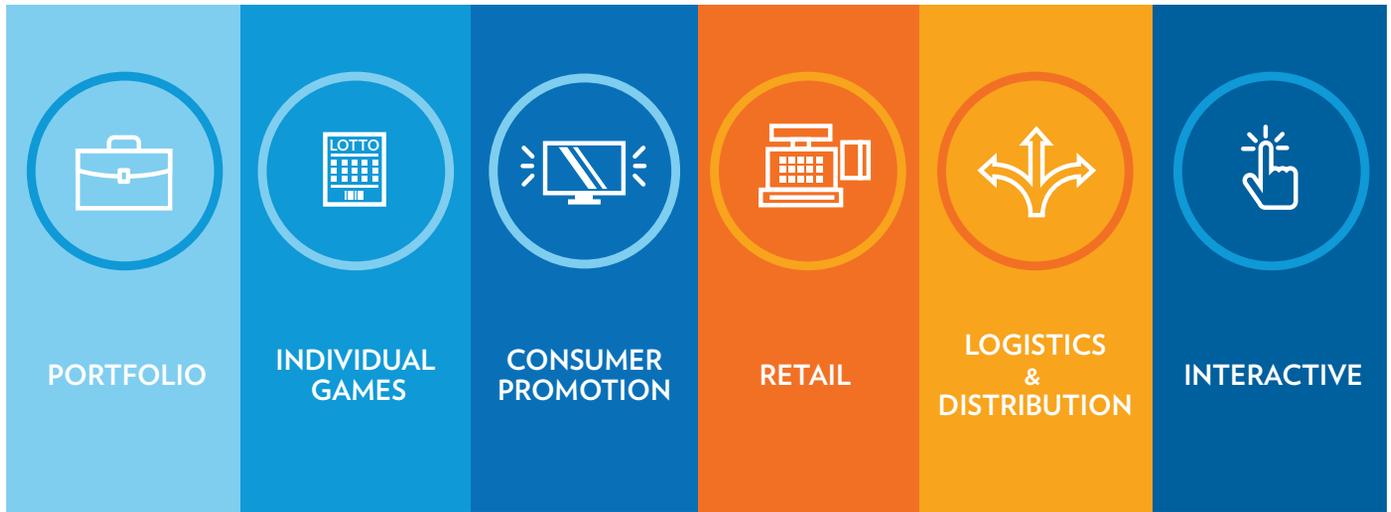


The Six Pillars of Instant Success

by Stefano Monterosso



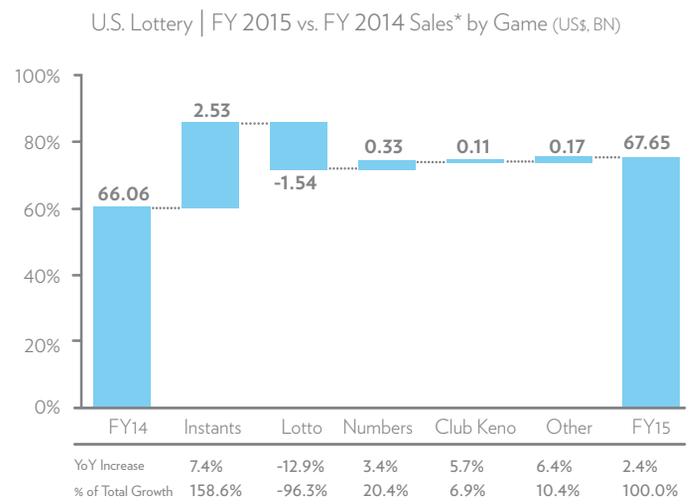
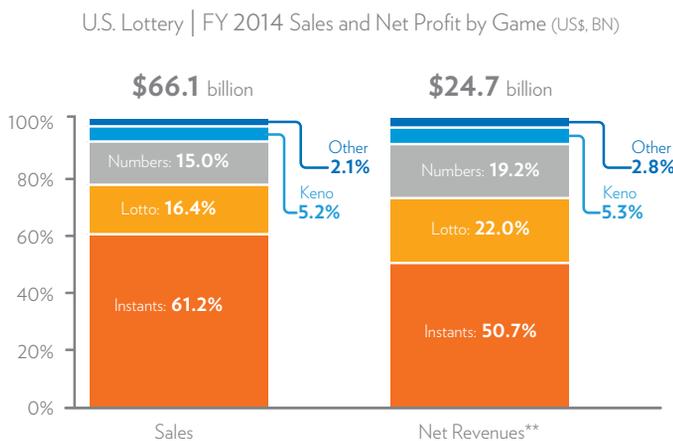
Instant Games: An Outstanding Growth Opportunity for Traditional Lottery

Instant games play a key role in U.S. lottery portfolios (see Figure 1):

- Instant games in FY 2014 generated more than \$40.4 billion of lottery sales (about 61% of total U.S.) and more than \$12.5 billion of net revenues¹ (about 51% of total U.S.).

- Instant sales are continuously growing. In FY 2015, U.S. instant sales increased by \$2.5 billion, contributing to more than 100% of total lottery growth.² Unaffected by the volatility of jackpot activity, instant games provide a consistent source of revenue to good causes. Instant games also offer the largest growth opportunity in international markets, where (with the exception of France,

Figure 1. The Role of Instant Games in U.S. Lottery Portfolios



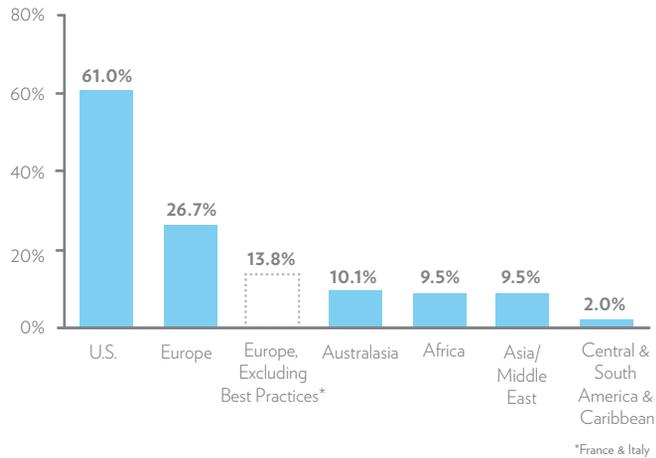
Note: Lotto includes Powerball, Mega Millions, In-State Lotto, & Cash-5 games. *Data for non-IGT sites are estimated. **Sales less prizes paid.

1 Net revenues = sales less prizes paid. By comparison, in FY 2014, Lotto Games generated in total sales about 22% of total net revenues and numbers games about 19% of total net revenues.

2 Total Lottery sales in FY 2015 increased by \$1.6BN vs. the prior year, due to the decline of multistate jackpot games (data preliminary for non-IGT customers).

Italy, and a few other markets) instantly remain significantly underpenetrated (see Figure 2).

Figure 2. Instant Sales Penetration over Total Lottery FY 2014



As the world's leading lottery supplier, IGT is privileged to serve customers in 100 jurisdictions globally:

- ▶ We are proud to partner with 38 of the 45 U.S. lotteries, cumulatively representing 79% of total U.S. lottery sales.
- ▶ As the global leader in lottery management contracts, and the only one with contracts across three continents – Europe (Italy), North America (Indiana and New Jersey) and Latin America (Antilles, Colombia, Costa Rica, and Trinidad and Tobago) – working with our customers/governments, we manage approximately \$30 billion in lottery business annually.

We deeply understand local markets and consumers and the nuances of the very diverse regulatory environments. Our global footprint and dual role of lottery supplier and lottery growth services partner allows us to provide lotteries with unique value: we have relentless focus on cross-pollination of best practices across businesses and markets. In those jurisdictions where we are supply partners, our revenues depend primarily on our customers' ability to grow the market and, therefore, our interests are perfectly aligned with those of our lottery partners.

A global leader in managing and advising on instant ticket programs, we run the world's largest instant program in Italy, *Gratta e Vinci*, and also have lottery management contracts in the U.S., all of which have experienced significant growth in the instant category. Our capabilities driving instant growth include the following results:

- ▶ In FY 2015, our U.S. customers' instant sales increased on average by +7.8%, significantly higher than the non-IGT U.S. customer average.
- ▶ In CY 2014, all of IGT's international customers experienced double-digit growth, at an average rate of 24.7% mathematical average and +18.9% as weighted sales average.

IGT's Vision: Six Pillars of Instant Success

Based on this experience, IGT has identified six key success factors in instant games, as shown in the graphic on the following page.



Pillar 1: Game Portfolio

Fundamental to an effective portfolio is ensuring that the needs of each consumer segment are fulfilled.

Our team has deep experience integrating industry best practices with jurisdiction-specific consumer and retailer insights to design the optimal target portfolio. This includes specifying the price range and optimal number of games to offer, the distribution of themes, which families to offer, the approach to seasonal games, and the "refresh frequency" for each component of the portfolio.

Once the optimal target portfolio is determined, a comparison to the current offerings is conducted, and a plan is developed to close the gaps. This also enables long-term planning and responsible growth of revenues to good causes.

The planned initiatives often include strengthening the portfolio at specific price levels and evolving the theme mix. In addition, different price points or additional play styles (or play mechanics) can be recommended.

Particularly critical is the role of the lowest price points (\$1 and \$2 in the U.S.). These lower price points encourage the continuous influx of new players (and/or the return of lapsed players), a key strategic lever for expanding the player base and responsibly driving lottery transfers to good causes.

Internationally, the range of price points offered in some markets still includes levels which are too low (equivalent to \$.20–\$.35). This makes it difficult for lotteries to absorb the fixed printing and distributions costs, and limits market potential, because retailers do not fully embrace the instant category due to low commissions.

The optimal target portfolio is not a static entity, but should and will evolve over time. Each jurisdiction has its own specificities to be taken into account. For example:

- ▶ Smaller populations or lower sales per capita will dictate fewer games on the market.
- ▶ Regulation and local context have a great impact. For example, in Italy, the Regulator's game approval process limits the number of new games introduced; in the UK, the Lottery must comply with a minimum share/number of £1 games.

In addition, the set of recommendations can vary substantially by maturity level. Younger lotteries will still have opportunities to introduce higher-priced games, while in more mature markets, the typical focus is on better satisfying consumer segment needs not yet fully addressed, and on leveraging product innovations.

The definition of the optimal target portfolio has great strategic

Figure 3. The Six Pillars of Instant Success Framework



value and, when well executed, the transformed offerings can actually assist in market development. IGT’s insight and expertise in this area can provide great value to lottery customers.



Pillar 2: Individual Game Development

Once the general structure of the portfolio has been optimized, each individual game must be designed to deliver a compelling player experience.

Game characteristics such as brand, price, theme, play mechanics (play style), payout percentage, callouts, and graphics, including the colors, will have to be specifically designed to differentiate each unique game from the rest of the portfolio, so that all the potential players’ needs are addressed and fulfilled. At the same time, it is important to secure enough variety in price/theme/play style combinations to satisfy core players.

Thoughtful, well-designed prize structures are critical for driving

lottery success. Odds of winning \$500+ or \$1,000+ prizes and the frequency of 5x, 10x, 20x prizes are crucially important. Over time, players will develop a perception of how winnable a game is, and will consequently either adopt or abandon the game. Prize structures decide the game’s credibility and will ultimately contribute to effective word-of-mouth winner awareness.

Because IGT captures and analyzes the performance of hundreds of games launched globally every month by its customers, we learn rapidly what does and does not work, what factors contribute to success – or failure. This allows us to provide reliable guidance when collaborating with our customers on portfolio and prize structure decisions.

Much of the recent success in New Jersey can be attributed specifically to the transformation of prize structures. Working with our customer, we increased the payout differentiation across price points and optimized the prize pool allocation for higher prices. Recently, this enabled the Lottery to introduce the new \$30 ticket

at the same payout percentage as the \$20 ticket. In October 2015, we will launch a new \$20 game at a payout of 1.4 percentage points lower than any other \$20 game previously launched in New Jersey, while still improving the player experience.

We provide recommendations for prize structure optimization even when the customer has chosen another print vendor. The Michigan Lottery is one such example. After experiencing flat sales for two years, the Lottery applied our recommended prize structures (developed in collaboration with the Lottery and its print vendor) to their portfolio in Q1 2012. The sales trend immediately turned positive, resulting in multiple years of double-digit growth (a total increase of 42%).



Pillar 3: Consumer Promotion

Among lottery games, the instant ticket category is where effective marketing and advertising initiatives can generate the quickest sales results. At the same time, it is difficult to quantify the actual advertising ROI accounting for cannibalization of the other instant games offered, but not promoted, in the portfolio.

Best practices and international benchmarks provide great insight on how to enhance the efficiency of advertising and promotions. It is typically most effective to spread the promotional investment across multiple price points; for example, promoting a Holiday Suite or a Family of games.

In 2004 in Italy, we paved the way in establishing an umbrella brand and logo for the entire instant category with the introduction of the *Gratta e Vinci* brand. Expanded in 2007 to include elstants, *Gratta e Vinci* is still among the most recognizable brands for Italian consumers. Most recently, La Française des Jeux (with Illiko, in 2014) and Camelot (with Game Store, in 2015) both adopted a single umbrella brand for scratch tickets and elstants.

Successful, responsible umbrella promotional campaigns have historically stressed the favorable differences from draw-based games, focusing on ease and convenience of play, frequency of wins, and immediate gratification...win or lose. Several jurisdictions, both internationally and in the US, have experienced great success through the appropriate use of humor in high-production value TV commercial advertising.

We typically do not encourage running TV promotions limited to games at \$20+ price points for a variety of reasons, including responsible gaming. While often these promotions result in great sales for the promoted games, net sales increases are much less favorable, and it is highly unlikely that many new players will be attracted at the high price point. We encourage instead seeking long-term sales growth through promotion of tickets at price levels that are more likely to get the attention of non/lapsed players. The exception to this rule is promotion of a product with features that offer a uniquely different playing experience and in-store visibility (for example, the Texas Lottery Commission's recent IGT Super Ticket offering).



Pillar 4: Retail

Player convenience is a key success factor. The strong correlation between retailer density and sales per capita is well established throughout our industry. Two of the highest-performing instant lottery programs in the world – Massachusetts and Italy – have retailer density of more than 1 retailer per 1,000 inhabitants.

We have a proven track record of success in expanding retailer networks.

Since 2004, when Lottomatica/IGT started operating *Gratta e Vinci* in Italy, the network expanded from 20,000 to more than 65,000 retailers. In our first nine months of operation in New Jersey, from October 1, 2013, to June 20, 2014, Northstar New Jersey expanded the retailer base by 7%, or 461 locations – including more than 240 Wawa convenience store locations, a key growth driver for the New Jersey Lottery. On average, the Wawa locations are selling over \$6,000 per week through a Gemini® self-service solution. When several of our U.S. customers introduced keno, they asked for our recruiting expertise. These include Michigan, one of the world's top-performing Club Keno lotteries, and Kentucky, which launched keno in 2014.

Our support in the recent retail expansion of Camelot in the U.K. was helpful in mitigating retailer resistance due to counter space concerns by providing innovative, small-footprint terminals.

In addition to retailer density, additional factors are critical to the success of instant programs:

- ▶ *In-Store Displays*. In California, we provided the Lottery with modern equipment solutions to increase in-store instant POS: our self-service equipment deployments increased facings by more than 12,000 and the total facing count plan generated an incremental 45,000 instant ticket facings in just one year (July 2014–June 2015).
- ▶ *Incentive Programs*. In all of our lottery growth services contracts, collaborating with each Lottery, we design performance-based incentive programs for both retailers and sales representatives, with the goal of increasing in-store product visibility. We also provide our global customers guidance on an ongoing basis on effective sales incentive programs to help them improve retail.
- ▶ *Sales Force Effectiveness/Optimization*. In Indiana, we completely transformed the role of Sales Representatives from simply managing instant ticket reordering (now a completely automated process) to focusing on value-added activities aimed at improving visibility and display of the product.
- ▶ *Sales Force Training Programs*. We periodically present tailored Sales Training Programs for our direct management operations (Indiana, New Jersey, Colombia, Costa Rica, Italy, etc.) as well as for jurisdictions in which we manage the sales operations (Texas, Poland, Czech Republic).
- ▶ *Partnership with Large Corporate Chains*. Our global retail strategy group is actively involved in recruiting large national retailers and has been proud to play a supporting role in the recent agreement among NASPL members to offer standardized accounting terms to large national chains, which has long been a key barrier to entry for that retail segment.



Pillar 5: Logistics and Distribution

Ticket distribution is a sometimes overlooked element of the value chain; in fact, *product placement* is critical. **Consumers cannot buy what they cannot see.** Retail shelf space is often the single greatest bottleneck that lotteries face in their instant operations and optimizing its use is a fundamental enabler of lottery profit growth.

A best-practices distribution operation is based on:

- ▶ *Insightful Analytics*. Analytics are a fundamental part of optimizing performance and an important tool in translating and condensing vast amounts of game and retailer data into *actionable insights*.
- ▶ *Game Performance Assessment/Analysis Tools*. Sales should be assessed at the micro level, based on an individual retailer's overall portfolio of games, trade style, and store location, as well as at the

macro level, based on the total number of retailers that are actually carrying the game.

- ▶ **Careful Planning.** Goals and objectives in terms of which games should be displayed by each retailer should be continuously set and maintained.
- ▶ **Optimal Communication.** The people in the field – both sales force and retailers – will be most effective if they are included in the planning. **Listening** to retailers is imperative, and vital information can be gained by holding regular Retailer Advisory meetings.
- ▶ **Compliance Measurement.** Having KPIs in place to monitor the quality of the execution vs. the goals is a recommended practice. We have developed simple, transparent, and effective KPIs aimed at tracking the effectiveness of distribution. KPIs can be articulated for retailer, sales district, tel-sell operator, etc., and used as an effective marker for incentive programs.
- ▶ **Automatic Ordering System.** An automated ordering system leverages data-driven analytics to maximize the effectiveness of the order prepared (either for review or for direct ordering, based on your lottery's requirements and retailers' preferences).
- ▶ **Continuous improvement.** An attitude of laser focus, coupled with relentless execution and drive to increase value chain effectiveness, is key to a best-practice distribution operation.



Pillar 6: Interactive

Due to regulatory restrictions, the United States lags behind Europe in the development of the interactive channel, with few U.S. lotteries able to offer interactive sales.

The first lottery to offer Internet sales was the Illinois Lottery. The State of Illinois authorized the Lottery to offer sales of draw-based games online in March 2012, just three months after the Department of Justice ruling that legalized sales of lottery tickets via the Internet. We were privileged to support that startup. As of 2015, Georgia and Michigan offer eInstants, and Georgia also offers Internet sales of draw-based games and is the world's most successful distributor of the traditional keno game on the interactive channel. Kentucky plans to launch its interactive offering in Q4 2015. On the other end of the spectrum, the Minnesota Lottery unfortunately was forced to cease Internet ticket sales upon being banned by the State Senate.

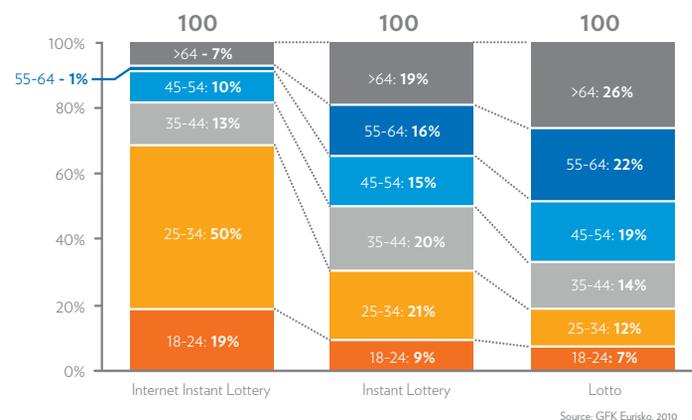
Owing to this scenario in the U.S., the interactive channel has been mostly limited to Internet subscriptions and second chance programs. There is no doubt that the Internet will be a major distribution channel for lottery products in the future. Given the prevalence and success of Internet sales in the traditional retail/ecommerce space, it is clear that Internet sales will act as a complement to retail sales; cannibalization is not a concern, with evidence proving both channels will grow together.

Data from the most advanced jurisdictions offering Internet lottery sales shows that this channel attracts new players and appeals to a younger demographic, as compared to retail lottery sales.

Figure 4 illustrates the demographics of *Gratta e Vinci* players via Internet as compared to *Gratta e Vinci* and Lotto players at retail.

Three years after the launch of interactive *Gratta e Vinci* in 2010, we saw that approximately 69% of interactive players fell in the 18–34 age group, compared to 30% for *Gratta e Vinci* retail sales and 19% for Lotto in that same age group. This compelling data proves that interactive will be one of the key drivers for attracting these currently less-engaged segments of the population. IGT is actively working with its customers currently able to

Figure 4. Age Distribution of Customer Base – Internet vs. Traditional Lotteries



offer Internet sales to identify the most effective business model to keep brick-and-mortar retailers engaged and benefiting from the concurrent sale of lottery via interactive channels.

Vision

The instant ticket category allows for the shortest lead-time for introducing innovation, which in turn enables immediate visibility into the results of different courses of action. Significant improvements can be executed only when real program transformations are applied. We deeply respect the knowledge each lottery has of its unique market and players. However, the further current operations are from adhering to best practices, the more dramatic and transformational the results will be once those best practices are incorporated. IGT's global expertise and deep understanding of diverse markets at very different stages of development can provide unique support in this assessment. The exponential growth in instant game performance in Italy (30x) and the dramatic growth in our three U.S. lottery management contracts following incorporation of the Six Pillars clearly illustrates our capabilities to drive lottery growth to good causes.

Consumer, Retail and Operational Insights

Incorporating analytics – *and translating them into actionable insights* – is a fundamental part of the planning process. This includes results from consumer research, characteristics of the retail network, point of sale space available at the retailers, retailer trade styles and locations, penetration of vending machines, impact of consumer promotions, return of investment of marketing actions, and entertainment and gaming activities available to consumers in potential competition with lotteries.

“Player Insights’ enables lotteries to better understand their players’ needs and expectations. Research and analytics continuously reinforces this bond, informing all aspects of product development, marketing and promotion.”

- Todd Bauman, Director, Business Intelligence, IGT

These critical insights are also a key element in understanding actual performance of games. Although this seems an easy task, it is not uncommon to see that themes that perform well in the market are not offered consistently on the market, because the additional value that they bring to the portfolio is not fully recognized.

Our years of experience in the industry have allowed us to develop unique methodologies for analyzing market trends, year-over-year comparisons, retailer and trade style performance, the contribution of vending machines, the effectiveness of the replenishment process and of the sales force in distributing the tickets, and the proper alignment of the portfolio with the consumer insights provided by market research.

Market research is essential to testing games prior to launch and determining their appropriate role in the overall portfolio. Other valuable consumer insights to be gleaned through research include the “consumer experience,” which is aimed at mapping the consumer’s purchasing decision process. For example, answers to questions such as, “When do you decide which game to buy – before entering the store or only when inside? Do you decide in advance which price point you will buy? If you change your mind once in the store, what influences your decision?” allow lotteries to better segment the current offering, understand the role of the different games in the consumer’s mind, and assess the optimal balance between core and rotational games.

Actionable insights are invaluable in identifying the initiatives that will further enhance a lottery’s portfolio. In addition, they will support lotteries in crafting effective incentive programs for retailers and sales representatives. The end result: increased revenues to good causes.

Planning and Monitoring

The instant tickets category is complex, with multiple variables affecting performance. Factoring in the impact of these variables (e.g., different games/themes across the portfolio, evolution of the retailer network,

jackpot activity of multi-state games, different timing and intensity of consumer promotions) to year-over-year results can be a daunting task.

We have developed rigorous methodologies for analyzing the market, some of which we apply weekly, others that we leverage in specific circumstances. We maintain a relentless focus on continuous improvement and optimization of our customers’ operations, understanding that the more mature a market is, and the less low-hanging fruit exists, the more such an attitude is critical to success. The importance of planning ahead and across the whole value chain, of measuring performance across several operational tasks, and not just limited to sales or profitability, cannot be overemphasized. Our large set of operational KPIs tells us how healthy a program is and helps us to highlight opportunities for further improvement.

Success Case Studies: IGT as Lottery Management Service Provider/Operator

Thanks to the trust our customers and their governments have placed in us, coupled with a clear understanding of full market potential, we have a strong track record in transforming instant programs to deliver responsible growth to good causes.

Figure 5. Case Studies – IGT as Lottery Management Service Provider/Operator

	Key Drivers for Success	Results
	<ul style="list-style-type: none"> • Product transformation (price, prize structures, graphics, colors, etc.) • New brand and consumers’ communication • Retailer expansion from 20K to 65+K retailers • New logistics and distribution • Relentless in-store and sales force optimization 	<ul style="list-style-type: none"> • Gratta e Vinci grown to become the world’s largest instant program • Sales grew from about €300M in 2003 to above €10BN in 2011 • Revenues to good causes grew from less than €100M to more than €1.7BN in same period
	<ul style="list-style-type: none"> • Brand transformation • Refreshed portfolio / Product innovation • Reduced # of games launched per year to <50 • Maintained focus on prize structure optimization • Reduced launches of same-price games at same time • Moved retailer to centralized automatic ordering 	<ul style="list-style-type: none"> • 2nd fastest growing U.S. instant lottery among top 20 U.S. lotteries in instant sales per capita from CY2011 to 1st half CY2015 (Source: IGT Global Analysis) • Weekly sales per capita from \$1.53 in CY2011 to \$2.35 in 1st half CY2015
	<ul style="list-style-type: none"> • Further leveraged extended play games • Increased focus on \$10, \$20. Introduced \$30 • Transformed prize structures (within the very restrictive regulatory payout constraints). In progress \$20 payout reduction • Optimized distribution and retailer display • Moved from bimonthly to monthly launch cycle 	<ul style="list-style-type: none"> • Achieved #3 in U.S. ranking in sales per capita in 1st half 2015 (was #6 in CY2012) • 1st half CY2015 sales per capita +42% vs FY2013



Stefano Monterosso is Senior Vice President of Global Lottery Same Store Sales at IGT.