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PGRI Introduction: Clarifying the basic building blocks of a business plan (mission, objectives, strategies and tactics) requires answers to some basic questions. What business are we in? Who exactly is our customer? For lottery, the issue is how to optimize a most unique business model. The cost of operating the business and generating sales is, as a percentage of sales and profits, constrained such that it is extremely challenging to wrest the full potential of the business. In the commercial world of efficient capital allocation, resources and funding would flow into a business that generates the kind of ROI that lottery does. For a variety of reasons, that does not happen with lottery, which means that increasing the leverage of those limited resources has a hugely disproportionate impact on sales and net funding to Lottery beneficiaries. Finding ways to eke out an extra measure of productivity from every dollar spent is the Holy Grail of this business.

The commercial world of consumer products has discovered that migrating from a brand management to a category management approach is yielding significant increases in sales and profits. A focus on the performance of individual brands is being replaced by a focus on optimizing the entire category of products. Fortunately, lottery does not need to be first with the paradigm-shifting strategy du jour. The category management approach began to gain traction some 15 years ago, which means that we in the lottery industry now have the benefit of learning from the pioneers who have perfected the category management approach. Lotteries have become quite adept at the fast-follower role, identifying and assimilating the management strategies and business process that have been vetted outside of our industry.

One of the obstacles for consumer products companies to moving into a category management partnership with retailers is that the brands within the category are owned by different companies and so they compete with each other. One might wonder what an amazing thing it would be to own the entire category. Oh, wait, Lottery does own the entire category!

This is new territory for me, so I asked Scientific Games' Jim Kennedy to help me sort it all out.

THE STRATEGIC APPROACH TO MAXIMIZING VALUE

Paul Jason, Public Gaming: *Unlike the terminal game side of the lottery business, the instant game business has traditionally operated like the old P&G brand management model. And the results have been very good. Sales of instants have increased at a much faster rate than lotto over the last two decades. Why not stick with what works?*

Jim Kennedy: We are sticking with what works. It's just that what has created the best results for our Lottery customers worldwide is a focused category management approach. It's a true and proven approach for other consumer product categories – and in fact most major retailers have dedicated category managers and expect to have this type of close business relationship with their category suppliers.

The instant product category is growing and evolving around the world; in the U.S. alone it's grown over $6 billion incrementally in just the last two and a half years. Over time, we've gone from selling single games to multi-themed games, to higher price points games, to multi-themed multi-price point games. Then that evolved into the game management approach of launching more and more games, making the consumer decide which games they liked the best, then turning that consumer feedback into creative product development and results-based innovation.

As an industry, I think we're shifting into a new place, a category management environment. Sheena Iyengar's research in her book "The Art of Choosing," suggests that too much choice can actually reduce sales; people confronted with too much unstructured choice choose not to buy. In the instant games business, our goal is to build excitement without introducing confusion. Getting this right requires a deep understanding and a development of the consumer experience over time. A few seconds of play on each game can accumulate into hours of learning about consumer behavioral patterns. The best performing Lotteries harness each encounter with games into an on-going, developing relationship with the consumer's value choices.

Lotteries own the whole category. That's an amazing concept. No other product marketer is in that position. That would seem to provide quite the convenient platform for applying the principles of category management. Manage the category, the promotions, the merchandising, the launch cycles, the game content, etc. for optimal synergies instead of a haphazard Darwinian competition between brands.

J. Kennedy: Exactly. There has been the assumption that the success of the lottery instant games business is driven by the individual performance of the games. But games are individual parts in an overall consumer and retail experience. Of course, we must have great individual games but it is the masterful combination that makes all the difference. Lottery, like all consumer product categories, is moving into a category management approach that focuses on category optimization instead of just individual game optimization. The elements of the marketing mix have a force multiplying effect on each other when managed strategically as a category. The results support this. The highest performing Lotteries in the world are the ones that have evolved from the game management approach to the category management approach. They may not call it by that name but that is what is going on beneath the surface. At Scientific Games, we call it Co-operative Services Programs (CSP) and it is a programmatic approach that provides our customers with a proven instant game partner that has helped grow their instant game sales on CAGR average of nearly 8 percent for the past 10 years and helped their retailers sell more games and increase their profits.

What does category management mean exactly, as we apply that concept to Lottery?

J. Kennedy: It means managing the entire product line as a business instead of a collection of competing games; so that all aspects of the program are coordinated to work synergistically and be mutually supportive. For many years we have identified and integrated 15 determinants of demand into our category management approach. These determinants complement and reinforce each other to produce an aggregate result that is far better than the sum of the parts.

But our capitalist system is based on competition. Competition of ideas and competition between products in the market-place giving the consumer the power to choose the winners and losers, and the marketer the feedback they need to continually improve the product and promotion.

J. Kennedy: This is the fundamental difference between the lottery instant game category and traditional consumer brands. In a product brand environment, companies are driving choices WITHIN a category BETWEEN competing companies' products at the consumer level. Buy Coke or buy Pepsi. An enormous amount of effort and expense goes into shifting market share a percentage point in one company's direction or the other; it is a zero sum game. Unless there are competing Lotteries selling instant games at the same retailer (and in some countries there are), the Coke versus Pepsi branding assumptions don't apply and are actually destructive to the growth and development of the category. We don't want a consumer to choose one game over another game; we want them to enjoy the benefits and excitement of multiple experiences across multiple games. Category management orchestrates the demand drivers that create breakthrough performance.

The business of coordinating all these moving parts would seem to require a different kind of working relationship between Lottery and Supplier; one in which the supplier plays a bigger role in the process of managing the category.

J. Kennedy: It's absolutely different. And the role of a supplier or business partner is a critical strategic choice by the Lottery's senior management team. Is the Lottery's

TRANSITIONING FROM BRAND MANAGEMENT TO CATEGORY MANAGEMENT

The management processes that produce optimal results in retailing have evolved greatly since Proctor & Gamble discovered the benefits of the 'brand-management' approach back in 1935. Ivory soap had made P&G the leader in soap sales. P&G wanted to introduce a new brand of soap, called Camay. Thinking that the team responsible for maximizing the sales of Ivory might not do the best job for Camay, P&G assigned an independent team of managers to launch the fledgling brand. The success of Camay led to a brand/product management philosophy which has persisted in large part to this day (or until enlightened marketers began to adopt the category management approach, beginning in the 1990s). Brands fought it out on the retailers' shelves for the attention of the consumer. Competition between brands was thought to be the perfectly logical foundation for a capitalist system that gives the consumer the power to decide the winners and losers. Supply chain relationships were driven by simple, albeit adversarial, negotiations over costs and service levels. But times have changed.

The most successful retailers and their suppliers have discovered that the outcomes produced by focusing on the newer concept of 'category maximization' are outperforming the mode of pitting brands in competition with each other. An ancillary benefit of the category management approach is that it depends upon cooperation between the retailer and all supply chain partners.

BusinessDictionary.com: Category management is a marketing strategy in which a full line of products (instead of the individual products or brands) is managed as a strategic business unit. It is based on the concept that a marketing manager is better able to judge consumer buying patterns and market trends by focusing on the entire product category.

Actually, category management is much more than a marketing strategy. It is a different way of doing business and managing supply-chain relationships. Under the old P&G brand management model, manufacturers were managing the business with the singular goal of making the most profit for themselves. Retailers then came to recognize that the resources and expertise of their suppliers could be applied to improve their own business operations; that engaging the active participation of their suppliers in the business of marketing the products would reduce the retailers' costs, increase sales, and improve profitability. Suppliers recognized that helping the retailer sell more is a sustainable strategy for expanding the market and improving efficiency in operations. As a catalyst for binding the strategic interests and planning processes of manufacturer and retailer, category management has birthed a new age of cooperation. Or, in the case of the lottery industry, created the platform for cooperation and teamwork between Lotteries, retailers and commercial partners. The result is that negotiations over who gets what percentage of a static profit pool has turned into a collaborative approach towards improving customer satisfaction and increasing that profit pool for the benefit of retailers, Lotteries and supply-chain partners alike. Actions to increase sales and improve profitability are now undertaken as a team. The one binding principle is that everything revolves around the consumer, setting the stage for a new age of a genuinely holistic, customer-centric relationship between all factors of production and supply chain partners. ◆

mission best served by a business partnership or a game supply relationship? The category management approach fundamentally works best when the Lottery aligns in a primary business partnership for the category. Of course, the Lottery is still the decision-maker. It's just that a full business partner can support the Lottery with the resources, expertise and operating capacity to optimize results for all stakeholders. The instant category is a major business in most jurisdictions – hundreds of millions and in some cases billions of dollars each year in sales. A lottery launches an average of 60 new games a year. An instant game product manager is at the center of all of this at the Lottery. Consider the workflows and the volume of this annual activity and the financial consequences of the decisions and results. This is a category that demands the highest levels of support and requires the deepest resources for success with business alignment at the category level not just the game level.

But no single supplier is the sole source for all the very best game content. Couldn't a contract with a primary supplier allow for the inclusion of hot new games from other suppliers?

J. Kennedy: This is a very common question. I can only say that if the Lottery's mission is to have a variety of games, then, of course a game-by-game selection approach is appropriate. However a Lottery's mission is to maximize returns for their stakeholders. And a game-by-game selection model is not the practice of the best-selling Lotteries in the world. First, when a Lottery selects one primary strategic partner as category manager, the organizations are aligned for best category results. Second, while it is true that there is a difference between the performances of individual games, the marginal performance of individual games is not what drives the ultimate outcome that global Lotteries are trying to achieve. A partnership that creates and executes a coordinated strategic plan to optimize the performance of the entire category is a way to maximize sales and net funding. Maximizing sales is much more about how the games, promotions, merchandising and distribution work together than it is about just capturing value from a contest of games.

I think an example of this approach is that Lotteries don't invite a variety of advertising agencies in to pitch on every ad campaign. If they did, they might be exposed to one or two great TV commercials or promotional ideas. But they don't do this because it is just not a strategic, balanced approach. Advertising needs a very strategic approach to manage continuity and flow in order to maximize the impact over a period of time. All the same reasoning applies to the management of the instant game category.

The original catalyst to migrate away from the brand management model and over to the category management approach was the desire of retailers to enlist more support and expertise from their suppliers, to offload some of the costs to their suppliers. Like retailers, Lotteries operate with extremely limited resources to produce the sales results. Like retailers, wouldn't Lotteries benefit just from the point of view of leveraging its limited resources, and relying on their suppliers to take on a more active role in managing the category helping to sell the product?

J. Kennedy: I think so and more importantly, major retailers think so too. Suppliers have tremendous resources at the ready to apply to the mission of helping lotteries increase sales and net funding. The suppliers' depth of resources and capabilities are a strategic asset for enabling on-going success for a Lottery. Today, Lotteries are operating with even less capacity than they did five years ago due to budget cuts and restrictions on hiring, and on top of this, the business is getting more complex, the old model is maturing and the demands for revenue growth are often increasing. With so many games and the increased variety of promotional strategies and media options, Lotteries can easily become consumed with the operational tasks of just keeping up with the job of project management, getting the products out the door and staying on top of all the media relationships. There may not be enough time left over for the strategic management of the multi-billion dollar business. The instant game product is a growing category for profits, and a strategic alignment generates the best results for all stakeholders in the Lottery's very demanding world. ◆