The Next Stage **of Lottery Industry Marketing** and Advertising

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One of the great strengths of the lottery industry is its vendor community. The industry giants that dominate this business—GTECH, Scientific Games, Intralot and Pollard—bring a national and international perspective to the work they do for individual lotteries. They provide the institutional memory, the history and the expertise gained over decades of work around the world to bring us best practices, sophisticated technology and the infrastructure that underlies everything we do. Lottery directors come and go, and few have prior lottery industry experience, and so it falls to the vendor community (and long-time lottery staff) to keep lotteries operating smoothly and efficiently. In fact, much of the debate about "privatization" of lotteries misses the fact that most lottery work is, and always has been, outsourced to private vendors.

For example, we almost take for granted that lotteries operate with an incredible level of security, integrity and accountability. But when the modern lottery business began in the 1960's, many lottery directors came from a background in law enforcement because of a serious concern about the potential for abuse or compromise of security. Today, the modern vendor community provides incredibly robust and ironclad security systems, as you would expect of very professional large international companies.

These companies also provide lotteries with a remarkable level of efficiency, with many lotteries operating their entire administrative and operating apparatus with a total cost (as a percentage of sales) in the low single digits. No other business, even in the private sector, operates with such a tiny cost base. In fact, I have often argued that lotteries have no leverage on the cost side and therefore all gains must come from the revenue side. Many state officials don't seem to understand this dynamic and insist on lotteries "cutting costs" to increase profits. It simply doesn't work that way. The amount of cost savings could never be more than a fraction of the profits generated by even a modest increase in sales.

Within this cost base, there are roughly four buckets of expense—the lottery's own staff, the central system vendor, the instant ticket printers and the advertising agency/marketing expense. Lottery staff tends to be a very small expense (I used to joke that the entire payroll of the New York Lottery was paid for with less than one day's sales. The vendor community, with its competitive industry dynamic, also runs very lean. That leaves the last bucket, with advertising agencies and marketing, as an interesting candidate for some efficiency-improving measures. Perhaps more importantly, changes in the way that advertising and marketing is managed represents a significant revenue opportunity. Let's explore this opportunity.

First, a side note about advertising effectiveness, since lottery directors are constantly fighting for more advertising and marketing dollars. In New York, we used a rule of thumb of 1 to 5 for the ratio of ad spend to incremental profit (not sales). In other words, a dollar of ad spend produced $5 of incremental profit. This rule of thumb was actually confirmed by a rigorous econometric study done by brand researchers for the New York Lottery. But, it also made sense intuitively given the very low level of ad spending, both in New York and nationally, at barely above 1% of sales. By comparison, total industry advertising nationally represents about 2% of GNP. Some segments, for example casinos and pharmaceuticals, spend over 20%. For lotteries, the challenge is to get the most out of the limited advertising funds we have.

This raises the question of why the advertising industry has not tried to replicate the success of other lottery vendors, to dominate this industry category with a few large, experienced firms that produce lottery advertising for multiple jurisdictions. Why haven't two or three large agencies emerged with a corporate strategy to concentrate on the lottery industry? I have had this conversation with agency executives and the answer has several components.

One critical factor is the structure of the ad agency business itself. Interestingly, there are roughly only four very large ad agency holding companies that dominate the industry worldwide; companies that themselves are less well known than the agency brands within their portfolios. These companies include Omnicom (with agency sub-brands such as DDB, BBDO, TBWA and many others, as well as media buying firms, PR firms, crisis management firms and more), Publicis (with Leo Burnett, Saatchi, Fallon, BBH and other communications firms), WPP (with Grey, JWT, Ogilvy, Young & Rubicam, et al) and Interpublic (with McCann, Lowe, FCB, IPG, Campbell Mithum, Deutsch, Hill Holliday, etc.). Interestingly, these large holding companies do little to encourage cooperation among their portfolio companies; instead, they actively support their firms competing directly against one another. Recently, the New York ad contract was out for bid, and two of the final three companies were both IPG firms, FCB and McCann, along with incumbent Omnicom's DDB.

Independent ad agencies still play an important role in the advertising universe, and it is perhaps here that we may see the beginning of a lottery-centric ad agency business. California's David & Goliath, an independent firm that swept the industry's Batchy advertising awards a year ago, has recently been contracted to produce national advertising for the Monopoly Millionaires Club game. Perhaps David & Goliath, or firms like them, will pursue a more aggressive strategy to become the leading lottery advertising firm.

However, there is an even more daunting roadblock to such a development and it lies within lotteries themselves. Many lotteries, when issuing RFPs for their advertising services, require firms to be local, to be based within their jurisdictions. Such requirements often are simply a political reality and difficult to overcome. And since lotteries themselves need constant interaction with agency personnel, a physical presence in the state has clear day-to-day advantages. Many lottery marketing managers also feel that their markets are so unique that local knowledge is critical to effective creative development. But for all of us who have looked at lottery advertising from across the country, or around the world, it is obvious that many good ads could be used in a variety of different locales. The commonalities of markets and player behavior far exceed the differences. Indeed, some of the demographic differences within our states (especially the larger ones) are as wide as the differences between states themselves. Good lottery advertising can be effective over a much larger audience base than it is today. The benefits in terms of cost-savings, and enhanced production values, make it worthwhile to explore ways to overcome the obstacles to a multi-market, collaborative approach towards advertising and marketing.

Another complication to this potential scenario is that several lotteries are beginning to separate their creative and media-buying contracts, since the work is actually quite distinctly different. The creative side is subjective, high-concept, high-value-added and high margin; the media buying side is objective, quantifiable, fiercely competitive, low-margin and more local-knowledge-specific. The separation of the two sides (I.e. creative and media-buying) means that it is entirely possible for a lottery-centric ad agency to scale-up and develop creative that would work on a multi-market/multi-state basis. The media-buying side of the business could continue to be served by local agencies. Creative, though, could migrate towards those advertising agencies which invest in lottery, develop better creative, and provide it at a lower cost.

Insofar as superior advertising could be produced at a lower cost to individual lotteries, lotteries can and should make the argument for quality and efficiency over localism. The need for the state to optimize its advertising and marketing communications should trump the desire of local ad agencies to keep the creative in-state. Quality would come from using national ad production capabilities (which are too expensive for most lotteries to underwrite). Efficiency would come from spreading these production costs over multiple clients, as well as from national advertising spot buying (primarily for national games). And to the extent that the instant ticket vendor community can encourage their clients to coordinate instant ticket launches, national advertising could also be used to promote certain instant tickets, especially licensed games. Localism would continue to be served by local media buying and, importantly, local promotion activity.

So how will lotteries benefit from such a revamped, and concentrated, ad agency national strategy? First, the quality of advertising will drive revenue growth. As new game developments and launches become a larger component of portfolio expansion, the role of advertising to inform and educate our customers will become even more important. Customers are used to seeing national-level quality in almost all advertising and product categories. Most products sold in our retail stores have national quality advertising support (beverages, snacks, gasoline, etc.) while purely local spots can appear amateurish and can occasionally generate skepticism (car dealers?).

A national ad agency could create several spots for the same game, to be used by different jurisdictions as they see fit for their particular local demographics. Larger states even might experiment with different spots for different markets within their states, based on similar considerations of local demographics. In creating multiple spots for the same game, agencies would benefit by being able to assess the effectiveness of different spots. Much like the instant ticket vendor community provides "index" performance measures for various games, agencies would have data to support the use of different spots (e.g., "This spot indexed at 170 in these three states, but this spot did 220 in this other state."). The entry of Big data into the realm of advertising effectiveness evaluation would have a profound impact on the tools we use to analyze and improve upon the entire scope of lottery advertising.

It's true that changing the business dynamic of lottery advertising involves a lot of separate moving parts. And this being the lottery industry, nothing moves quickly. The first step is for lotteries to begin to remove any localism requirements from future ad agency RFPs. This will open the door for existing agencies, whether holding-company-owned or independent, to build their competencies, invest in the lottery sector, and pursue multiple contracts in multiple states. Parallel with such a change, lotteries should begin to give weight in their RFPs to firms that have current and prior industry experience. Demanding that a firm know our business and have had relevant experience will go a long way to creating larger lottery agencies. (We would never entertain a central system contract bid from anyone but

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GTECH, Scientific Games or Intralot, would we?) Agencies with no lottery experience need not apply!

Next, lotteries need to continue to expand funds available for advertising and marketing, perhaps by employing new approaches to funding. Some of these techniques have already been used successfully. For example, the Monopoly Millionaires Club had its marketing budget embedded in the game design; if a state wanted to join the game, it was required to accept the game as designed, along with its marketing requirements. MMC, unfortunately, did not succeed, at least not in its initial iteration, but the game design points the way for future funding of national games. Similarly, the marketing of licensed instant games can be funded by the licensor instead of the lottery, avoiding any impact on state restrictions on advertising budget. Examples include various NFL game tickets that were advertised by the teams themselves in cases where the lottery had no budget. And, marketing spending can be required and embedded in other vendor contracts, such as the central system vendors, to provide funds outside of the state budget itself. More spending in itself will provide incentives for agencies to be more aggressive in seeking our business, which is a core purpose of this effort—to attract the human and capital resources to create world-class advertising at a price that works for even the smallest lotteries.

Finally, is there a risk of "creating a monster?" If advertising is dominated by only a handful of firms, will prices rise and our negotiating clout be reduced? To respond, I would only refer to the existing example of the major lottery-centric firms: does anyone really think that price competition in lottery competitive bidding is weak? GTECH vs. Scientific Games vs. Intralot vs. Pollard answers that question. And keep in mind that lotteries cannot grow profits from the cost side; revenue growth is the only viable driver. Squeezing a tenth of a percentage point out of the cost side is misplaced effort; managers need to spend money to make money, and the ROI on effective advertising in the lottery business is strongly positive.

Hopefully, as lotteries mature and profit growth becomes more and more of a challenge, lottery directors can demand the same efficiencies, best practices, quality and effectiveness from their advertising agency partners as they currently enjoy from their central system and instant ticket providers. At the same time, far-sighted advertising agency executives will need to consider radically different business models to sustain their own growth and profitability. Both trends need to develop simultaneously. ■

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loss or time limits for each type of game offered by the site.

- **Time Out:** Players have the option of setting time limits (or time-outs). Time-outs are defined as instant stops in play that are at least 1 hour but less than 30 continuous days.
- **Personalized information:** The site provides players information on their play. Players have access to their gambling history including time and money spent, games played, net wins/losses as well as session information. Players have access to their account details including all deposits amounts, withdrawal amounts, movement of funds between products, bonus information, restrictions such as exclusion events and limits.
- **Self-Exclusion:** Self exclusion is a player-initiated restriction on their ability to play on the site.
- **Passage of Time:** There is a clock visible on the site at all times.
- **Display Cash:** Games always display bets, wins, losses and account balances as cash.
- **Game Features:** The site does not allow players to play games automatically using an auto play feature.
- **Free Games:** Free or demonstration games have the same payout percentages and odds as paying games. Free games should not permit play by underage players.
- **Encouragement to Continue:** The site does not induce players to continue gambling when play is in session, when the player attempts to end a session, or wins or loses a bet. Communications with players do not intentionally encourage players to increase the amount they play with, gamble continuously, re-gamble winnings and chase losses.
- **Underage Gambling:** Sites have an obligation to put in place technical and operational measures to prevent access by those who are underage. The age verification process should be required as a part of registration.

Again, these are just a handful of the best practices recommended by the National Council. The full document listing their Internet responsible gambling standards can be found at ncpgambling.org.

The National Council hopes to soon have in place a tool to help lotteries make sure they're adhering to best practices in their Internet offerings. A certification program set to be launched in 2015 will use third-party assessors to examine an Internet gambling site to see what controls are in place. According to the National Council's Executive Director Keith Whyte, *"Participating sites will have their responsible gaming programs assessed against our Internet Responsible Gambling Standards, and those who are in compliance receive a certificate. This helps regulators, operators, and especially the public recognize sites that meet our standards."*

While research appears to show Internet gambling doesn't create a new wave of problem gamblers where offered, it does become yet another venue for those who already suffer from the disorder. Having the correct controls in place helps your customers play responsibly, and establishes your lottery as one that is responsible and working to lessen the social impact caused by this new gambling outlet. ■