



## From the Publisher

*Network Externalities* sounds like something that business school students may want to philosophize about. For the rest of us, we mostly have jobs that require us to focus on the concrete tasks that produce results right now, this quarter, this FY. Not much time for pondering matters that don't do that. Until we consider that *Network Externalities*, also known as Demand-Side Economies of Scale, are the underlying economic dynamic behind the success of Google, Facebook, Amazon, Twitter, Instagram, Pinterest, Apple, Airbnb, Uber, e-Bay, Youtube, and more. They all leverage the dynamic in which adding customers adds value to the product or service which in turn attracts more customers. Additional users of a product add value to all the other users. Scale begets scale. The operator with dominant market-share gets bigger, everyone else gets smaller.

**How can Lottery apply the principle of *Network Externalities/Demand-Side Economies of Scale* ... and derive more value from what is by far the largest customer base in the games-of-chance industry.**

The telephone is the iconic example of a tool that becomes more valuable as more people owned it. Facebook—Why join a social network that doesn't have the largest and/or most relevant membership, or post a video anywhere other than Youtube? Pokerstars came to dominate the world of online poker (albeit illegally and before Black Friday) because if you were going to play online poker, you wanted to go to the site that had all the players. The positive feedback loop drives more business to the companies that have the largest customer base.

IBM expected Bill Gates to charge much more than \$430,000 to create an operating system (OS) for the PC, back in 1981. Then they knew they were dealing with a naïve greenhorn when Gates charged only \$40 per copy/unit. By holding fast to the right to license the OS to others, Gates positioned Microsoft to practically invent platform economics and carve out the most powerful monopoly in modern times. The explosion of new programs, applications, and utilities was all written for Microsoft's OS that ran the PC and its clones, leaving all other platforms, like Apple, in the dust. Ironically, Steve Jobs returned to Apple 15 years later to reinvent *platform economics* for the era of the smart-phone.

Bill Gates was ridiculed for charging too little for software. Google, Amazon, and Facebook were famously chided for not making money in their early years. The investment community saw no

pathway to "monetization." In hindsight, now everyone is waking up to the incredible power of *Network Externalities*, using the existing customer base to enhance the value proposition which in turn attracts more customers and so on.

How can Lottery apply the principle of *Network Externalities/Demand-Side Economies of Scale*? We might think about how the assets of Lottery can be leveraged to derive *Network Externality* value from what is by far the largest customer base in the games-of-chance industry. Combine that with a proprietary retail network, products that have more enduring appeal than anything else in the gaming industry, a reputation for Integrity and Brand Value that is almost priceless ... add CRM and games that promote social networking and a Mobile experience to reinforce community and sharing—it will be interesting to see what Lottery will become over the next few years.

Regulatory change has always happened at a snail's pace in the U.S. Now, with the advent of Daily Fantasy Sports (in spite of losing some of its sheen) and the introduction of new game concepts and the pressing need to rationalize the online gaming world, we can hope (!) that the wheels of progress might start to turn. The confounding issue has always been and continues to be about jurisdictional authority. The main thesis of CEI, Geoff Freeman, and Mark Hichar is that the federal government should just clarify once and for all that regulatory and taxation policy as applies to gambling of all types resides in the province of the states. That alone would break the gridlock and enable state governments to decide on the model that would best serve the interests of their citizens. At least some states would opt for the legalize, regulate, and tax model that protects the consumer and channels economic benefit back to society instead of enriching criminals. Then, as regulatory models evolve, the efficacy of allowing more flexibility for state-owned lotteries to be the agent that protects the consumer and maximizes economic benefit for society would become more apparent to everyone. We do live in interesting times, though, so who knows how long it will take for any of this to actually happen!

We hope to see you at Lottery Expo in Miami. Visit [PublicGaming.org](http://PublicGaming.org) for conference info, updates, and registration and room reservations links. ■

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