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PGRI Introduction: The U.S. Lottery industry is on a roll. Results are coming in for fiscal 2011 and the trend is clearly positive. The cross-sell initiative is beginning to fulfill its original promise, and the U.S. lottery directors are forging onward with new and ambitious plans. Most recently, the directors announced that the price of Powerball would double in January. Having been at \$1 per ticket since its beginning in 1992, the enriched Powerball is scheduled to launch in January 2012. Powerball is the most successful lottery game in history and the most powerful lottery brand today, so working through the countless details of a change like this is no easy task. Terry Rich credits his colleagues for their insight and direction of “looking at the big picture” in making this breakthrough happen. I asked Mr. Rich to give us some perspective on what enriched Powerball will mean to the 44 state lotteries which depend on this great product.

Paul Jason, Public Gaming: Congratulations to you and all the lottery directors for overcoming the obstacles to collaboration and raising the price of Powerball to \$2. Why was it so important to make this price-point change?

Terry Rich: Products can't stay the same forever. In my opinion, they need to be refreshed periodically. Powerball has been priced at \$1 since its introduction over two decades ago. It frankly was overdue for an update. But not just any reboot or change for change's sake. The change really is an enriched game. “More, Bigger, Better” has become the theme, and I'm confident we will be delivering on that vision.

“New and improved” has always been the mantra of premier consumer marketers like Proctor and Gamble. The customer expects it. Their needs change and they expect products to change with them. Just like any consumer products business, a Lottery is required to continually monitor consumer tastes, anticipate the direction they are going, and adapt to changing player preferences. The operative question for progressive businesses is never “Why fix it if it isn't broken?” If you wait until it breaks, it may be too late. We need to stay out in front of the trend-lines,

make the changes before they become necessary and always be improving and updating our products to keep players engaged.

More specifically, the research was telling us that changes were needed. When surveyed, many players asked why we gave all the money to one person and why we couldn't have more millionaires. But at the same time, lottery sales figures show that in reality, it's higher jackpots that cause players to buy more lotto tickets and buy them faster. Powerball is a jackpot-driven game, but the player perception is that they would like to have more millionaires. The change that the development committee of MUSL made gives the players both. We will have up to three times more millionaires with the match-five second prize. The \$2 price point brings a lot more money into the pot, raising the jackpot more quickly, so we can double the starting prize to \$40 million. So in one fell swoop, we're doubling the price, doubling the jackpot, providing more millionaires, and providing better odds. And the better odds come in with the matrix change from 39 balls in the Powerball pool down to 35. Reducing the number available in that pool improves the chance of winning.

Another important benefit to the change is

to differentiate the products. The other big-jackpot game, Mega Millions, is priced at \$1. Many states have in-state lotto games that also are priced at \$1. It really does not make sense to price everything the same. This gives us a much richer canvas with which to differentiate the value propositions of the different games. So those are some of the reasons for the change and we hope to build on the excitement and anticipation between now and the January launch.

Do I have concerns? Sure. Jackpots could roll up so fast that players will need to get used to buying at the beginning of the game to even get in on it. We're actually pretty excited about the launch and confident the consumer will share our enthusiasm.

Remember, we are not trying some untested strategy with our most important product. We're taking an already successful business model from the scratch-ticket category and converting that to the Powerball game. In the early days of scratch tickets, it was thought by everybody that all you needed was one \$1 scratch game. The thought was that offering more than one game at a time would confuse the consumer and oversaturate the market, being terribly destructive to the whole business model. In fact, the oppo-

site is true. The consumer wants more options and we need to implement a wider variety of products with different attributes to differentiate them, beginning with different price points. Not only can the market absorb more products, the consumer is used to a constant influx of new options. The scratch ticket model really took off when the consumer was given multiple choices, more games, and different price-point options. Of course, brand-licensing also played a big role. But, who would have thought back then that it's possible to have the number and variety of scratch games we have now? Or that there would be \$10 and \$20 tickets. Or that the biggest growth sector would actually be the higher priced tickets. So creating a \$2 option in jackpot games became an easier decision, especially when everyone continues to have a \$1 option, whether it's with Mega Millions or their own in-state lotto game. When the evidence is in that the market will absorb this new price-point, the next step will likely be to offer a \$5 multi-state game or even create a \$10 lotto game. We should replicate the huge success of scratch-offs in the lotto games. And truly, when you think about games here, you have to think options, refreshing the games so that players want to continue to play.

Why raise Powerball – and not Mega? Or, do all states also have the option of creating a \$2 game on their own if they want?

T. Rich: For the simple reason that Powerball is the most recognized lotto product across all lottery states, the one with highest brand recognition and most consumer appeal, one that I believe is perceived as the product of highest value. Products should be priced to reflect their perceived value to the customer. If you look at the business model on the scratch side, that is the way scratch tickets are priced. Bingo and Crossword are our top two selling scratch game, so we price those at the \$3, \$5 and \$10 price levels. Your best brands, your best known products, are the ones that have the most perceived value for the consumer and should be priced accordingly. Powerball appears to be the best brand in the lotto category and so it is the one that should have the highest price.

It all makes so much sense. Why was there uncertainty on the part of some directors?

T. Rich: I can't presume to speak on anyone else's behalf. But I will say that this is a very big step for all of us and extensive research and due diligence was warranted. And, some states have a very high percentage of their revenue derived from Powerball. It's only right that they be concerned about doubling the price of their bread-and-butter product, and the effect that will have on their overall revenues. But the research was done and shows that the effect will be positive. History will be the ultimate judge.

And the example of the history of scratch-offs is so illuminating. Of course, this is all quite consistent with the brand, price, and product development strategies of all consumer marketing companies.

T. Rich: Nobody has a crystal ball. But I think that raising Powerball to \$2 will clearly be a big positive for everyone, a calculated risk well worth taking. Again, lottery tickets are about choice and options. Players ultimately decide the success of all our games. And when we decided to cross-sell Mega Millions and Powerball, many players quickly realized the games were very similar. So you need choice, a fresh and updated approach. And the players will all still have their \$1 option. The choice is theirs, but only if we give them the option.

It's impossible to imagine that Powerball revenue could decline when you double the price. Individual ticket sales maybe, but not revenue.

T. Rich: After doing research, that is the conclusion of the group. Many of us are very optimistic that this is just a start, that we are creating a platform from which we can grow this category like scratch-offs were grown over the past twenty years. The first big step was cross-sell, selling both games in the same market at the same price. Then one of them is changed to the higher price point. Next we introduce an even higher priced multi-state game that could have new attributes, different plays. And then an international game with a completely new and different consumer appeal.

There are directors who have been in this industry a long time. Their perspective is formed by many years of experience. They shared their experiences with pricing strategy and the evolution of scratchers and were able to put this decision into proper context. But a decision like this is not made without extensive debate and cooperation to substantiate the historical lessons and data.

What will MUSL and/or the individual state lotteries do to really optimize the impact of this change?

T. Rich: "More, Bigger, Better" is going to be the theme that most lotteries will embrace for the launch of \$2 Powerball – more millionaires, bigger starting jackpots and better odds. That really captures our plan in a nutshell. We are also exploring innovative ways to do promotional add-ons to Powerball. Borrowing from the playbook of scratchers again, we are looking at ways to provide a second-chance feature or an extended-play option. We are also looking at creative ways to leverage the power of the brand to collaborate with other consumer brands and leverage that into free publicity and national promotion. We're looking for ways to promote nationally that will not cost the states any money.

There are also a number of "More, Bigger, Better" benefits that we look forward to being

able to promote when we have the specific hard data to support our claims of a better-value proposition. If the research is true, we will have additional sales points as facts for states to promote in the future. For example, we believe that as the game unfolds, it will be demonstrated that the number of millionaires created will be more than three times what it is today. But we don't want to say that until we can actually point at the facts. We expect the jackpots to roll up much more quickly. But we don't want to say that now because it will be a much more powerful promotional tool when the players see for themselves that's how the game works. We believe that the numbers show that Powerball will deliver an intrinsically more exciting play experience for all those reasons. And of course, we would like to promote that and we will. But not until we have some history to which that the players can relate. Give us a couple months into the new year and you'll begin to see a steady ramp up of these kinds of promotional directions that should add even more momentum to the excitement of the game.

Once the players realize that the jackpots roll up quickly, won't they be more anxious to jump on the bandwagon earlier than before?

T. Rich: That is what we hope and expect. Most people, I think, have a perception that you tend to get what you pay for. Or they are at least going to ask 'what's in it for me if I pay more'. Either way, that is what we want because they do get more for their \$2 over the \$1 they were paying before and so we welcome the opportunity to tell them about it. Then it's up to us to create the game changes in the matrix and otherwise create the value, and the perception of added-value, to close the deal in the customers' minds. High jackpots also are what really pull in the casual player. There will be more high jackpots, we will get to those high jackpots more quickly, and the consumers will buy the 'hope and dream' whether it costs \$1 or \$2.

We are confident that the jackpots will roll fast, which translates into a higher frequency. We're just not going to promote that until the reality is there for everyone to see, which should be accomplished in the spring of 2012. And once that happens, and the consumer is back into the routine of following the jackpots and buying in when it reaches their preferred threshold, I think the price increase will be completely forgotten and the \$2 ticket will be perceived as the norm.

But fortunately, it is not an either/or proposition. The players will likely always buy \$1 lotto just as they buy \$1 scratchers. It's a matter of more options, more consumer choices, empowering the consumer to be the 'decider' and that's the way it should be.

Why shouldn't MUSL have a publicist who focuses and works hard to nationalize the winners,

all winners, and nationalize the overarching story of why Lottery is such a great and inspirational thing? Maybe Lottery could replace baseball as "America's Game"!

T. Rich: States do like to control their own public relations. Nationalizing the public relations and publicity machine is a tough sell. In fact, the current announcement of enriched Powerball that is "More, Bigger, Better" may be the closest we have come to a coordinated national campaign. I'm sure we will do more in the future, but nothing like what you seem to be suggesting. The states are not all supportive of it, and we do not have the funding for it. And to anticipate your next question, even though the cost could be limited by having the lotteries all pitch in a small amount, most states do not want to pool the resources to nationalize the PR of our multi-jurisdictional brands. They prefer to think of it as national in the sense of collaboration on the game, but the market is still local and specific to their own state. The vendors support us with many of these things, but we have already asked them to pitch in a lot and there is a limit to how much we should expect the commercial community to provide.

We will continue to standardize and nationalize where we are able, when it can be done consistent with the agendas of the member-state lotteries. The next step might be that that somebody creates a really great concept for a television commercial or an ad campaign of some kind that really captures everyone's support so that we all kick in the money to make it happen. Another way is to leverage the power of our brand by entering into a cooperative deal with another major consumer brand, perhaps like we do with some scratch-off campaigns like Monopoly, and let the other consumer brand bear the cost of promotion for a tiny slice of the profits. I'm sure there will be things we do to kickoff enriched Powerball in a really big and exciting way.

I still don't see why all the states would not agree to pitch in for a nationalized approach to advertising, promotion, or at least publicity. I know they want to control the messaging for their states. But they can still do that. A nationalized effort would just augment it and reinforce the brand and really give it a different kind of look and feel that comes with a truly national brand presence like Coca Cola and McDonald's and Starbucks and such.

T. Rich: You know you're preaching to the choir here. I agree but would also say there are obstacles that need to be overcome to get everyone on board and supportive. Every state does want to control their messaging because it is their lottery. I don't have a problem knowing that each state wants to control all the marketing that is specific for their state. But there is no reason why a program to distribute copy points

nationally and publicize winners nationally needs to conflict at all with the in-state messaging. And I know it seems odd, what with the margins this industry works with, that funding is a problem. But the reality is that many states have an advertising budget that is small and they do not want to part with it. The other reality is that state lotteries enjoy their autonomy and their role of crafting campaigns that appeal to their markets in perhaps a unique way. For example, Buddy Roogow just did a spot that was off the wall. It showed a lady stepping in some dog doo-doo as she walks out the steps. That worked really well in D.C. and he's getting great buzz on that. People in other places might not have the same sense of humor. So in one way, we may even have an advantage over the giant consumer brands by having the benefit of scale that collaboration provides, while preserving the benefit of a more targeted marketing approach that autonomous state lotteries provide. But we do definitely want to have at least some national coordination and messaging to complement the state-specific agendas.

Digression: Any progress towards standardizing transaction processing mechanisms?

T. Rich: A big challenge is that the lotteries all have different systems and different costs related to upgrading to make them compatible with a single standard. Everyone senses that we need to do it. We are all agreed on that and it is a high priority, but it will still take time, a few years actually.

Your legislature in Iowa is actively discussing the options to regulate Internet gaming.

T. Rich: Yes. Legislation was passed during the 2011 session calling for a study of the issue to be completed by late this year. We've been asked to be an active part of that. The knowledge we have from the lottery industry perspective will be relevant to this effort. But the business and professional opinions we render will be as citizens of the state and not as lobbyists for lottery.

I've noticed, though, that people refer to this as a potentially huge incremental expansion of gaming, the Internet working its transformational magic on the world of gaming and lottery. I think it should be kept in proper perspective and that characterizing it in a way to say it's the next "huge dollar" is not only inaccurate, it probably isn't helping us to get down to the serious business of focusing on the lottery to handle regulation and oversight. The numbers I've seen from other countries do not support the notion that the "Internet changes everything." It should be seen as incremental (not gigantic) revenue, and regulated for the safety of the players. I see it as a way to provide a convenient channel for distribution to the players, and to enable the state to properly tax it. It will

certainly make our products more accessible and appealing to everyone. At this point, though, we need to start looking at the mobile, smart-phone, and personal communications world. And how do we make everything easier, more convenient, and more accessible, while maintaining the integrity and social responsibility of the industry. We need to think of regulations of new channels like Internet and mobile not so much as a means to increase sales, but as a means to create a climate of sustainable growth. It appears the answer is not to prohibit electronic delivery systems because the problem gambler will easily find other outlets. The answer is to regulate all channels and focus on creating a healthy recreational gaming environment. We try to strike a balance between meeting the demand for gaming, delivering funds for good causes, and protecting the players.

It seems like that's the power of the government-lottery mode: the ability to strike that balance between agendas that are not naturally aligned with each other.

T. Rich: We try. Lotteries and their directors really are progressive and entrepreneurial. We are operating within a set of expectations that are more complex than the commercial community works within. We would like to accelerate the rate of change and adaptation, but we also need to respect the political process that governs this industry. Likewise, most legislators respect the fact that we are them, that we are on the same team and we are all pulling for the same objectives. That's why they are turning to us for objective input on the ramifications of different approaches to governing this industry. We are not just the lottery, we are a part of the state and we want to help the state accomplish its fiscal and public policy objectives.

There is a new Powerball logo.

T. Rich: We passed a resolution last year that all lotteries will use a uniform Powerball logo by the end of 2011, but state lotteries are reluctant to lose their state-specific identity. They do like to differentiate their Powerball from their neighboring states' Powerball. We agreed to enable states to do that in a fashion, but hope that we can create a template that will be used by everyone and also create a national consistency to the brand. It is actually not a simple matter – it costs a lot of money. Add up the costs for everyone to change their logos in all of their advertising, POS materials, everything else; we're talking over \$20 million. So, many of these things might seem easy and we sometimes wonder why they can't be done yesterday. Collaboration by a committee of 44 is tough, interesting and fun. We have made huge progress over the past two years and will continue on this positive track, so stay tuned. ♦