

Paul Sternburg

Executive Director Massachusetts Lottery

PGRI INTRODUCTION: The ability of lotteries to succeed depends on lots of different factors, many of which are outside of the control of the lottery director. Working those areas that are controllable is one obvious key. Reaching out to try to influence areas that tend to be outside of our control has the potential to deliver a great ROI. Proactively enlisting the input of state legislators is proving to be a successful recipe for the Massachusetts lottery.

Paul Sternburg was appointed to the position of Executive Director of the Massachusetts Lottery in January of this year. Prior to that, he served as Vice President of Sales & Marketing at the Connecticut Lottery (since 2007), and prior to that as Director of Sales at the Massachusetts Lottery (since 1997). His mission is to put the Massachusetts Lottery back on its growth track. No small task since the MA market is by far the most developed of any in the U.S. If anyone ever implies that prospects for growth may diminish as the industry matures, just point at the MA Lottery and suggest they come back when they've reached \$167 per capita sales per year.



Paul Jason, Public Gaming: *Massachusetts has the highest per capita sales in the country. Actually, no other lottery even comes close to your market penetration. At \$167 per person per year, it's over 60% more than the second highest per cap sales. Isn't there a point of saturation wherein it becomes really hard to continue to increase sales?*

Paul Sternburg: Of course it's challenging. One tool that delivers a very predictable increase in sales is to increase the prize payout percentage. The evidence is quite conclusive that increasing the prize payout percentage produces an increase in sales. Sometimes the impact is dramatic, as in the most recent case of California. Unfortunately, we have already leveraged that option, paying 80% on our \$10 and \$20 games, 76% on \$5 ticket, 72% on \$2 tickets, and 70% on \$1 tickets. I don't know the point at which increasing the prize payout

percentage would start to have a diminishing return, but we cannot go any higher on our own prize payout percentage, so that removes one of the ways that our lottery has to increase sales. The next place to look is distribution, more retailers, more POS, increase exposure and accessibility to the consumer. We already have a retailer to population ratio of one retailer for every 933 people, which is very high. But I think we can improve on that, hopefully getting into new box stores and retail chains like CVS Pharmacies.

We are also looking at the ticket mix and how to refresh the playing experience that still appeals more to the core player while attracting new players. Extended-play tickets are definitely adding value and we can see the impact on sales already. Our extended-play portfolio is up by 34% over last year. Ultimately, that's what this business is really

about – doing the research and evolving our products so that they appeal to the consumer. That's what we're doing and we are seeing the results. Sales were up last month over the same month in the previous year and we are confident that we can continue to grow. The Mass Lottery is a mature lottery with high per cap' sales, but there is always room for improvement and growth.

How did the MA Lottery get to such a high level of per cap sales?

P. Sternburg: Increasing the Prize-payout percentage and the number of retailers are the two 'low-hanging-fruit' measures that all lotteries can and should do to achieve maximum market penetration. In addition, the Mass Lottery has always considered its retailers to be true business partners. It's so important to recognize the critical role the

retailer plays in the success of a lottery. We pay 5% commission, which is not the highest in the country, but about average. But with the high sales, the average retailer makes about \$37,000 from their lottery business. Also, our lottery products are held by the retailer on consignment. They don't pay for product up front, which helps with cash flow. And they don't pay for anything they don't sell. We feel that retailer-friendly policies generate goodwill and support on the part of our retail partners and that results in higher sales. We try to make it very easy for them to carry lottery. We also make sure the POS materials are updated and displayed properly. And we even have a secret-shopper program in which the retailer and the clerk are rewarded for pitching the product.

One thing that detracted from sales was eliminating the agent incentive program, which was done a couple of years ago under a previous administration. While it was perceived to save \$14 million, the reality is that it helped contribute to the loss of \$300 million in sales. Obviously, other factors contributed to the decline in sales. But I can guarantee you that taking away that added agent sales commission contributed to the decline in sales, and to a much greater degree than the \$14 million in cost reduction. Retailer motivation is key to selling more lottery. Retailers are our face to the consumer so keeping them happy is a top priority. We bring the retailers in to our lottery offices for them to educate us on their business and what we can do to help their businesses operate more efficiently and sell more product. Of course, we can also educate them on lottery and on things like the high correlation between lottery product sales and sales of other merchandise. We have gas stations that sell over \$12 million a year. You've got to be a motivated retailer to get \$12 million out of a gas station – that's an average of over \$33,000 a day, 365 days a year! I can definitely say that whatever is saved by cutting retailer commissions is lost 10 times over in sales. There are lots of things that lotteries would like to do but we're not able to do. Keeping our retailers happy and motivated is one of those areas that we can control and do something about. We concentrate our energies on that and other areas where our actions can make a real difference.

Now that the vote is done and the decision is made to implement changes, including raising the price of Powerball to \$2, do you feel that your fellow lottery directors are going to all work in concert to really optimize the results?

P. Sternburg: Of course. The directors are all sophisticated, forward-looking leaders. Once a decision is made, everyone gets behind it, just as we would expect the management team of our own organization to do. We're all invested in this process and we'll do everything in our power to work together to make it a success.

Do you see a potential for lotteries to collaborate on advertising and brand management, creating a truly national brand, perhaps with Powerball or Mega Millions? Wouldn't a cooperative effort like that contribute to the in-state performance of the individual lotteries?

P. Sternburg: Nationalization of advertising and marketing would probably not work well. I know it must seem that a product like Powerball is basically the same wherever you go. If they can create a national commercial for Coca Cola or Starbucks or Tide detergent, why can't they do it for Powerball? The answer is that other consumer brands have neither the wide variety of product attributes nor the legislative oversight that go with all lottery product marketing. While there are commonalities to the product and consumer buying motives, there are also big differences between Regional demographics and their preferences. What works in one state won't work as well in another. Massachusetts, Florida, Kansas, Oregon; these are really quite different consumer markets. The New York consumer might find humor in things the Midwesterner thinks is just weird. Californians may be inspired by something that Texans think is corny. Too, rules and regulations about what can be advertised and how it can be advertised differ from jurisdiction to jurisdiction. An advertisement that complies with the different rules of all the lotteries would actually be very hard to even create. I see some great commercials that would not necessarily be allowed in Massachusetts and many other states. So I believe that advertising should all be done by each individual lottery to serve its marketplace. I would not say a national campaign can never be done successfully. Just that as a rule, advertising, promotion, and brand management should all be done by the individual state lottery operator.

What about a publicist, perhaps employed by NASPL? Someone to work up interesting story angles on lottery winners, push them out to the national media, and try to gain much more press for the many tales of good fortune that are created by lottery; the publicist could also push out positive stories in general, supportive of Team Lottery, to counter the negative press.

P. Sternburg: That's a great idea. Helping to nationalize the stories of lottery winners would generate positive PR for the games, no matter what state the winners are from. And it would help to have someone to share the mission of the lotteries, like funding good causes, protecting the player, taking a more responsible approach to promotion of the games, supporting the public policy agendas instead of undermining them like offshore operators do. I agree, a publicist to promote the entire community of state lotteries, their stakeholders, and the players, could make a real difference. While each lottery has its own publicist, it would be great to have someone dedicated to nationalizing our stories, to creating national exposure so that good news is shared by all of us and not just contained in our local jurisdictions.

To push it a little bit further - A publicist costs money. Do you think that lotteries should be willing to allow for a small increase in NASPL dues to pay for the publicist?

P. Sternburg: I can't speak on behalf of other lotteries, but I definitely do. It's not like we would be talking about a lot of money overall. Look at what Las Vegas spends, or the gambling industry in general spends to influence the news and create positive press for themselves, often to the detriment of lottery. Our story is just not getting out there like theirs is. States probably need to do their own in-state lobbying. Lottery operators probably need to do their own advertising. But there's no reason that I can see why NASPL shouldn't direct an effort to shape the news on the national stage, to nationalize the stories that are currently almost all limited to local news stories. For that matter, I would support NASPL taking charge of lobbying at the federal level. States do not have the resources to do it. NASPL would need to stay focused on issues that the membership is all agreed on. For instance, defending the rights of states to decide gaming and regulatory policy would be an example of an issue that I would think all state lotteries and their political constituents would support.

We really do need to defend the interests of our stakeholders at the federal level. If it wasn't for a handful of political leaders who stood up to aggressively fight the Harry Reid bill, it could have passed and that would have been disastrous for lotteries, and all the states except for Nevada and New Jersey. Massachusetts Treasurer Steve Grossman and some others from states around the country took it upon themselves to mount an outspoken protest. Of course, the president of NASPL

at the time was Ed Trees and he also made public NASPL's position on the issue. But the need for this kind of representation is more important than ever and lotteries should find a way to be more proactive at promoting their interests. I can't say for sure that NASPL is the right vehicle to do this, but I would think the possibility should be explored.

It wasn't too long ago that legislators were concerned about the image of lottery and whether the state should be associated with gaming. Doesn't it seem like the political climate is changing such that legislators are recognizing that gaming and gambling is being offered in all shapes and sizes by all varieties of venues and operators, and that their own state lottery operator should be positioned to be the dominant player in the gaming and gambling industry? Or do legislators even think of this as a business in that way?

P. Sternburg: Of course, legislators do recognize this as a business and understand the potential of lottery to generate funds, but they have lots on their plate. They are tasked with making lots of big decisions and they do not always have as much time as they would like to pour through all the data and information related to the issues pertaining to the lottery. It is our job to communicate with them in a fashion that enables them to quickly digest lottery facts and figures. I do think, though, that legislators all around the country are paying more attention to the ability of their state lottery to play a bigger and more important role in this industry, the broader gaming and gambling industry. Lotteries are really quite unique. Unlike any state agency, lotteries are market-driven businesses operating in a highly sophisticated and complex competitive environment. Unlike any private enterprise company, lotteries serve the interests of the general public and not a limited set of private shareholders. When you think about it, lotteries are in a uniquely interesting position to deliver maximum value to the broadest range of societal interests. Lottery, gaming, and gambling are special industries. They generate huge profits and they come with the potential for social costs that need to be managed properly. Those factors make this industry really quite different from any other. I'm sure you've heard CEO's of the major casino operators complain that their industry is unfairly singled out for more oversight and higher taxes than other industries, literally asking "why can't we be treated like other industries?" The answer is that gambling is not like other industries and the fact that they don't understand that, or want to

accept that, is the very reason why state lotteries are the best vehicle for states to satisfy the demand for gambling. I think that shapers of public policy are beginning to realize this. Lottery is a special industry that requires an approach that is neither free-market capitalism nor administrative-driven government agency. That combination of core attributes calls for a special approach that state lotteries are in the best position to deliver. And society would be well-served to apply those core values to all forms of gaming, gambling, and Internet gambling.

Back to your question, if there is any lack of understanding on the part of legislators, that's our fault, not theirs. We need to communicate effectively with our political constituents. We encourage our legislators to visit our offices and operations to get a better idea of how this business works, just how much there is to it and how complicated it can be. I can say that it is always an eye-opening experience for them.

Lottery Directors are in the ideal position to understand both the interests of the state and the gambling industry. The legislative agenda is always so crowded though. How do you prevail on the legislature to even give consideration to your input?

P. Sternburg: Lotteries are doing a great job and are typically excited to talk about it. My boss, Massachusetts State Treasurer Steve Grossman, believes in transparency, openness and being straightforward. For instance, the Lottery used to meet with the legislature once every six months. That kind of semi-annual update on the performance and results is too infrequent to effectively engage the legislators in the business, and certainly not in the role of contributing to the strategic decision-making process. What good does it do anyone to come in after six months with a report that sales are down by 3%? That's no way to run a business. We send updates to the legislature once a month. We present our report with specific sets of recommendations for how we can improve the results. That way the legislature knows they are a part of the real ongoing process of weighing the pros and cons of different strategic options. I would say that our legislators have responded positively and that Treasurer Grossman has been quite effective with this approach. The legislature has approved funding for a number of exciting initiatives that we proposed and expect to keep us on a growth trend-line.

Funding for new games and such?

P. Sternburg: Exactly. Funding for new raffle games, ticket vending machines, we're looking at the possibility of entirely new games to add to the portfolio, all initiatives that will deliver a great return for the general fund. We're also increasing funding on research and product development.

On the other hand, your \$2 million advertising budget seems unreasonably small.

P. Sternburg: Of course I would like to have more. But these issues are never as simple as they seem. Yes, it is the case that doubling that amount would absolutely result in a significant increase in sales. In fact, increasing the ad' budget would deliver a huge bottom-line ROI. The reality, though, is that these legislative decisions are not made in a vacuum. Government budgets are not managed like a fluid on-going cash-flow as in private enterprise. They are allocated at the beginning of the budget year. So, legislators are faced with the decision in June of whether to cut \$1 million from social services in order to give it to the Lottery for advertising. But, you might point out, the Lottery can return \$2 million or more to whomever has been cut by the \$1 million, right? The thing is, they need the \$1 million now, in this year's budget, and can't wait till next year's budget to come around, even if the funding would double. These social services need that \$1 million on July 1 of 2011 regardless of how much you might give them on July 1 of 2012. These are difficult logistical problems, unfortunate but that's the real world.

What do you see as the most important trend-line or opportunity for lotteries over the next six months?

P. Sternburg: Every state has different demographics and are at different stages of development. In Mass., updating technology, as many lotteries have in recent years, as well as tapping social media platforms to diversify and expand our player base will be key to our success over the coming months and years. ♦