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MSL Lottery in the Ukraine: A study in overcoming adversity in a market disrupted by political and economic turmoil.

PGRI Introduction: The Ukraine is the largest country in Europe by land mass, and has a population of 46 million. MSL is the state-owned lotto for Ukraine. It was launched in the middle 1970s to raise funds for the development of sports in the Soviet Union. That mission changed when the Ukraine became independent in 1991. MSL was originally an abbreviation for “Molod Sportloto,” but is now the brand name. After the Ukraine gained independence in 1991, there was a period of time when government regulatory structures were not fully intact. There were no regulations and private operators were free to start lotteries, sell tickets and take in money, then close without paying out prizes. Public trust in lotteries was destroyed. In the year 2000, a regulatory system was implemented. Even so, and even though MSL always operated with integrity, the entire industry was tainted and it was very difficult for MSL to reestablish public trust and confidence. But they succeeded, step by step, in re-establishing consumer confidence that its operations are totally transparent and prize monies are paid out promptly and the games always operated with integrity. The business of lottery relies not just on the confidence of the consumer. Retail and advertising partners also need to be confident that the time and resources allocated to lottery will generate a positive ROI for them, and that the lottery operator will be a good business partner in every way.

Before the political and military turbulence which began in 2014, when Russia annexed Crimea and turned eastern

Ukraine into a war zone, the market was growing considerably. MSL sales were increasing at an annual rate of 50-80% between 2010 and 2013. Total revenue in 2013 was over 2.5 billion UAH (approx. \$150 million euro today but twice that before the devaluation of the Ukrainian currency last year). The lottery business has since declined amidst this turmoil. Among classic lotteries, bingo ranks first at 30% of revenues, scratch cards second at 24% and growing fast, and Lotto third at 6%. Sports-betting and toto is 40% and is the fastest growing category. Only 18% of the population in the Ukraine plays the lottery at least once a year. That compares to 70% in the UK. Illegal online gambling is vast. There are more than 270 sites accessible to the Ukrainian customers. They are not properly regulated or taxed.

97% of MSL's sales are at land-based stores. Transitioning from a state-owned economy to a capitalist system is a big transition. It is not just a matter of installing modern business practices and models. The cultural adaptation as well as economic and logistical transformation is not so easily accomplished. Of course, Ukraine is over twenty years into the process. The cultural transformation has largely been accomplished and so now it is largely a matter of executing on fundamental business plans to develop a network of dynamic entrepreneurs to operate the stores.

Evgeniy Vlasenko has led MSL since 2011.

Paul Jason: *How have things changed since our last interview of September 2014?*

Evgeniy Vlasenko: The last two years were a time of unrealized hopes. A western-minded government came to power. We expected this to improve cooperation from the Ministry of Finance, and facilitate the development of the market based on the principles which the EL (European Lottery Association), and the European Union as well, proclaim. But after a succession of three Finance Ministers, each bringing in a new agenda and new set of priorities, not much has changed. New taxes were introduced in January of 2015. Before that, lottery operators paid tax based on GGR and now it is based on turnover. In parallel with that, a tax on winnings was applied. The operators, not players, are responsible for correct calculation and collection of this tax. The tax is applicable for all wins, even minimal prizes. And on top of all that, a new tax on profit for the operators was introduced. These changes that may have been intended to increase net proceeds to the government have had, not surprisingly, the opposite effect.

Our costs have increased to manage these changes. Imagine the burden on the operator to adjust the central system and ERP system to correlate all prize payouts with the winner, calculate the tax that is due, withhold the correct amount from the payout, and report and remit the taxes to the government. We had to do that in two days! And changing the tax from GGR to turnover crippled our high-payout games like sport-betting and video lottery. Players are not happy that they do not get their prize in full as before.

One might have decided to simply discontinue business operations under those conditions. But not us. We hoped that once the negative impact of these new conditions was observed by the government officials, i.e. the drop in sales and taxes collected, they would

amend the onerous rules and tax structures back to what it was in 2014. That would enable us to generate more sales and net taxes again. It was in 2014 that Crimea was annexed by Russia and war in the East caused despair, uncertainty, and lack of confidence about the future in Ukraine. This provoked a decline of the market and decreased the interest that people had about lotteries.

EU Sanctions against Russia for its failure to comply with the Minsk peace agreement which calls for Russia's withdrawal from Ukraine are still in effect. And I just read today that EU and NATO officials do not expect Russia to fully comply in the near future. What is the condition in the Ukraine now? Are people able to go about living normal lives or is there fighting and disruption? What does the future look like to you?

E. Vlasenko: In terms of the Minsk agreements and obligations of the opposing sides, I would leave conclusions to the politicians and governments. One thing is factually clear—norms of international law are not followed, Ukraine does not control 450 km (300 miles) of its eastern border, and Ukrainian Hrivna is replaced by the Russian ruble in the territory which is under terrorist occupation. These are facts which also point at who is responsible for financing and managing the actions which create such political and economic instability.

Ukraine is in a very unusual situation. People from all different nationalities, religions, and cultural backgrounds have been living peacefully here for so many years. Nobody thought about the different backgrounds, we all just lived as equals, as friends and countrymen. Now we just want this military turmoil to stop so we can return to normal life.

Ukraine borders with Moldova on the south. And between them there is an unrecognized territory called TransDnister republic. It had been a part of Moldova but is now going

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GEORGIY LOZHENKO: LEADING MSL THROUGH 25 YEARS OF CHANGE

Credit for navigating MSL through these many years of adversity goes to one person—Georgiy Lozhenko. MSL success is possible due to his leadership, moral sense of purpose and strong will, and strategic vision. Mr Lozhenko practically saved the Ukrainian lottery market in the 1990s, navigating the transition from government-owned and operated to private ownership and market-driven economy. There being no mechanism for an orderly transition resulted in severe economic and political insatiability. Mr Lozhenko continues as the President and Chair of the Board of MSL.

January of this year was a most difficult time. New high taxes were introduced and then financial sanctions were imposed against MSL and another Ukrainian lottery operator, with the intention to block our activities and provide exclusive conditions for another operator in the lottery market. Mr Lozhenko held fast to our principles with confidence that doing the right things and with commitment to the principles of the European Lotteries, the Ukrainian lottery market would return to a normal situation. His energy and mission were embraced by all employees and helped to us survive and protect the company and the team of professionals who are dedicated to operating MSL with integrity and dedication to serving the people of Ukraine. Over the last two years, the Ukrainian Army and the Ukrainian people harnessed an iron will to resist the forces of terrorism and disruption. So too has MSL. I am pleased and honored to serve the people of Ukraine with Mr Lozhenko. On the eve of Georgiy's jubilee, and on behalf of my colleagues in MSL, I wish him all the best. I believe that it is important that young professionals who come to work in our industry know about the work ethic and fortitude of legendary individuals who have done so much to protect the integrity and sustainability of lotteries all around the world.

—Evgeniy Vlasenko

on its 25th year as being under separate rule. It would be very sad if anything like that would happen in the eastern part of the Ukraine.

But this does not mean that the people of Ukraine know only stress and adversity. Our every-day lives have lots of positive and happy things—and playing the Lottery is one of them! Playing a small amount of money for the hope and dream of changing our life is as appealing here as it is everywhere else in the world.

How has MSL adjusted to these extraordinary circumstances? How has the business of operating a government lottery been affected and how have you adapted to it?

E. Vlasenko: Like our country of Ukraine, MSL obtained its independence in 1991, and now we are fighting to protect it. Today is a very difficult time for our company. But we do not give up. We increased prize payouts of our games to

soften the negative consequence of the winning tax. We launched terminal instant games which is a completely new category for us. And now they comprise close to 40% of the total turnover.

Our company has over 45 years of history. When the USSR collapsed in 1991 many decision makers and citizens of Ukraine lost hope and did not know what to do. Old economic and political ties became disconnected and new ones had yet to be established. Many companies and enterprises were closed. But life was still going on. And MSL, which had been a branch of the Soviet Sportloto, came through all these problems and successfully continued to operate, launching new games and distribution channels. We will continue to persevere.

We continue to cooperate actively with EL and very much appreciate its support. And now we just joined the WLA in July. We cannot imagine what it would be

like without the community and support of our colleagues in the world of Lottery. We believe it is important to follow the moral principles of EL and be a leader in setting high social standards in Ukraine. So, in June of this year, we successfully passed audit and confirmed our Responsible Gaming certificate.

In the fall of 2014 we opened a winter sports palace in the town of Boguslav which is in the Kiev region. We had been building it since 2012. All financing of the construction was funded from MSL profits. There is not much when it comes to modern social infrastructure in the smaller cities of Ukraine. Therefore our palace, called “Liodogray” (play on ice), became the center of activities in Boguslav. Now it operates successfully and without financial support from the state. Ice hockey and figure skating schools and international tournaments are made available for local kids. ■

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At Kambi, our empowerment business model echoes these statements. Kambi adds value by constantly inventing, crafting and packaging the most engaging sports betting experience for end-users—across all channels. This scalable, but flexible model reads through to a personalised experience for consumers.

Retail rules supreme

What about Mobile? Isn't that the key to the future? Yes, but not as an isolated channel that enables gaming on your smartphone. The importance of Mobile is in its role as unifier of all channels and interactive experience. Mobile has become the intermediary between the consumer and the world, the link to everything we do.

It's not about a Mobile strategy any more than it is about a Digital strategy. It is about a Business strategy that integrates all channels of distribution, communication, the modern lifestyle, and our products in ways that optimize the entire consumer experience.

The cross-over appeal of sports betting

Sports-betting is not only the fastest growing gaming

category, it also has the social component treasured by the modern consumer. Everyone loves to watch sports together and bet on sports together. And they want a venue, be it the land-based store or online, that enables them to play other games (like Lottery) while they bet on sports.

Adopting sports betting can help state lotteries to grow other business verticals, depending on licensing rules and conditions. Introducing sports betting products can attract a younger audience and encourage cross-over appeal.

The above has brought Kambi and Novomatic Lottery Solutions (NLS) together; in joining forces, we will help the lotteries to fulfill the modern challenges they are facing in an ever changing world.

For more information about the most trusted brand within government gaming and or sports betting, we look forward to seeing you at the World Lottery Summit in Singapore, Stand C1.

Bio: *Joni Hovi is the Executive Director for the lottery sector at Kambi. He has worked in the lottery sector since 2003 and joined Kambi in January 2016.* ■