

## Market advice on the lottery sectors

1. You have asked the Gambling Commission (“the Commission”), in its capacity of the Secretary of State’s statutory adviser on gambling and its regulation, to provide advice, on a range of matters relating to the operation of regulatory policy in the lottery sectors. In particular, the Department has set out its concerns that a potential blurring within the boundaries of the gambling market, including all lotteries, could have an adverse impact on funding for good causes raised by lotteries of all types. This paper provides advice in three specific areas:
  - An account of the ways (if any) in which boundaries between the National Lottery, society lottery and commercial gambling markets may be being eroded;
  - An assessment of the impact any erosion may be having both on public perception<sup>1</sup> and on return to good causes from the National Lottery and society lotteries; and
  - Our assessment of what new products may be entering the market (insofar as commercial sensitivities allow).
2. In considering the scope for existing and new product development affecting the return to good causes and public perception we have considered both the likely changes in delivery mechanism and in potentially competing products.
3. The discussion looks first at the market for draw-based products, traditionally reserved for lotteries with limits on prizes and total proceeds distinguishing the territory reserved for society lotteries from that reserved for the National Lottery (TNL) with no limit on turnover and extremely high prizes. Worldwide national/state lotteries are having to work hard and innovate to retain interest in weekly or biweekly draws and grow the return to good causes; their ability to generate significant life changing prizes, through roll overs and promotions being key features. It then considers instant win products where lottery scratchcards uniquely are available in retail premises and to 16/17 year olds<sup>2</sup> but where a range of similar products are available online to those 18 and over.
4. It argues that the market for draw-based games is not being eroded significantly at present by boundary incursions, though there are long term risks to return to good causes from competing demands for disposable income, the move online and to mobile, and other trends such as the growth of social gaming. There are also some slight but unlikely risks of erosion from products betting on other national lotteries or from ‘umbrella’ marketing schemes for society lotteries. These risks look unlikely to be significant presently but could potentially be addressed pre-emptively, such as by deterrent regulation.
5. There are also issues about the development of more ‘professional’ society lotteries crowding out other society lotteries which may change the nature and range of good causes supported by lotteries. This risk looks small at present, given evidence of growth across the society lottery spectrum, although it may merit further consideration in any wider consultation.
6. The position is very different with instant win products where TNL and society lotteries’ products (scratchcards and interactive instant win products) may need to move more into territory already occupied by very similar commercial gambling and new areas such as freemium products if they are to grow revenue for good causes. There are issues as to whether ‘good cause’ branding should be allowed to or is effective in promoting harder forms of gambling.

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<sup>1</sup> We have considered perception from three perspectives: i) consumer comprehension of products, ii) Legitimacy of TNL to operate, given monopoly and regulatory advantages iii) the importance of good causes to differentiate and market lotteries. These aspects are covered within discussion in the sections.

<sup>2</sup> Noting that pools betting is open to 16 year olds also.

7. Our analysis of an increasingly complex market, with both players and operators sometimes pursuing for different ends than personal or commercial profit, has underlined the need for any policy consideration, on whether and how to best use the lottery markets to raise money for good causes, to go beyond narrow society lottery related questions, such as around a minimum level of return to good causes.

Not only would such a narrow focus risk missing unintended consequences for both the nature of good causes supported and the amounts raised in total but it would ignore the impact of more general changes in the environment affecting the attractiveness of lottery products such as the move to digital and competing attractions for the leisure pound and time.

8. DCMS' forthcoming consultation offers a real opportunity to inform the debate on the future of the National Lottery and society lotteries and ways of raising money for good causes. It could provide a sounder basis for decisions on whether, and if so how and how far, to maintain or bolster the 'clear blue water' for TNL and society lotteries.

## **Market analysis**

9. We have identified the following elements as relevant to an analysis of the gambling market for the purposes of this advice:

### *Draw-based products*

- a) Market potential for TNL draw-based sales over time
- b) Growth in the society lotteries sector
  - i) The growth of umbrella schemes eg The Health Lottery (THL), People's Postcode Lottery (PPL)
- c) Presence/ growth of products that involve betting on the outcome of lotteries

### *Instant Products*

- d) Growth in retail instant products ("Scratchcards")
- e) Growth in online instant products: (eg interactive scratchcards; on line slots; bingo)

### *Brand Leverage*

- f) Wider brand utilisation across the gambling spectrum.

In each case characteristics of the product are considered, along with the potential sources of erosion, current impact and factors that should be borne in mind when considering how the product and its market may develop in future.

### *Draw-based products*

#### **a) Market potential for TNL draw-based sales over time**

#### **Characteristics:**

10. TNL has offered a growing range of draw-based products and draw days since it started with the single Saturday Lotto in 1994. In recent years change has been seen with extra draw days (EuroMillions and Thunderball) and in-game innovation (Lotto) rather than new games.<sup>3</sup>
11. The products are characterised by low ticket price, infrequent draw frequency (though currently only Sunday, Monday and Thursday are non TNL draw days), wide retail distribution across a range of general retailers as well as a growing online presence, very high prize levels<sup>4</sup> and non-specific good cause association. TNL also benefits from a prime-time BBC Saturday night draw show and the capacity to advertise on TV widely.

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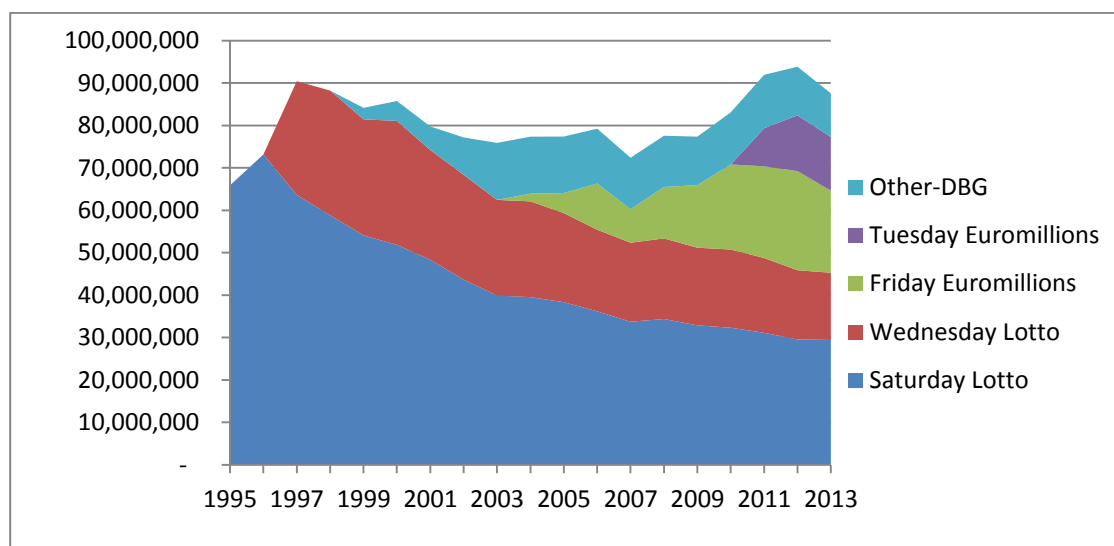
<sup>3</sup> Indeed Lotto Plus 5 was removed with no replacement at the launch of new Lotto in October 2013.

<sup>4</sup> Currently £190m is the top prize possible, on the EuroMillions product

Consumer play is driven by the size of the prize with the good cause element part of the post-rationalisation process for maintaining play.

12. UK draw-based products, which follow international experience, launch, reach a peak and then decline. Camelot's strategy has been, as noted above, to introduce new games, innovate within game or add draw dates to counter decline.
13. In addition, Camelot has been building the instants category. However, we note that, given the smaller return to good causes per pound from the instants category compared to draw-based games the careful management and monitoring the portfolio needs, in particular to determine to what extent scratchcards provide synergy and to what extent they may prove cannibalistic.

**TNL Draw-based games (DBG): Average weekly sales £m**



Source: Commission NL Sales data

**Potential sources of market erosion:**

Beyond the gambling market

14. In addition to lottery and gambling products as a source of market erosion which are dealt with in subsequent sections, TNL products also face competition from the products sold in the same FMCG<sup>5</sup> environment, as well as gambling products more broadly. Supermarkets for example have sometimes used lottery language in prize promotions run and prize promotions themselves may potentially divert lottery spend. The greater consideration that all brands are starting to face up to is the battle for consumer time, as much as spend.

Other relevant trends include the growth of social gaming, which, while these trends have not yet demonstrated direct complementarity with gambling brands, have potential to influence consumer time and spend either away from the sector or to be monetised better by one part of the sector compared to another<sup>6</sup>.

General Economic Factors

15. There is no evidence of a clear relationship between TNL and macro-economic factors. That said Mintel note the probable impact of the economy in 2013 and the benefit of improved economic conditions in the medium-term<sup>7</sup>.

<sup>5</sup> FMCG – Fast Moving Consumer Good

<sup>6</sup> The Commission has also noted that as penny auction sites continue to evolve, we will continue to monitor the way in which they operate to ensure those providing facilities to gamble are properly licensed to do so. This could be another example of competition for consumer spend.

<sup>7</sup> Mintel Lotteries Review UK, March 2014

## Management of the portfolio

16. We have noted above how the draw-based portfolio has been managed over time to maintain or improve sales. It is now quite a mature portfolio which covers a range of prize levels.

The increase in the level of jackpot in EuroMillions has been a key driver in improving sales over recent years. Players respond well to big jackpot events, though care has to be taken to ensure that ennui over such occasions does not set in, reflecting the difficulty in maintaining a draw-based product.

17. Clearly Camelot has the key role in terms of ensuring that the total portfolio (draw-based and non-draw-based) is complementary and not overly cannibalistic. The Commission challenges Camelot on its forward strategy regularly to ensure it understands how Camelot is likely to maximise return to good causes and the role of draw-based game proposals as part of that. That said there must be a real risk that sustained returns to good causes over the mid-term period becomes more and more challenging and more dependent on non-draw-based products; and the draw-based product sector internationally is not recognised for great innovation, perhaps unsurprising given a product of limited scope.

### **b) Growth in sales of the society lotteries draw-based product sector**

#### ***Characteristics:***

18. Successive legislative regimes have provided limited permission for non-commercial organisations to use gambling (in the form of lotteries) to raise money for their own good causes. Strict constraints are placed on the scale of this gambling activity, on the nature of those organisations permitted to supply it and on how proceeds may be used. The society lottery market comprises a wide range of providers from the very small eg the local Parent Teacher Association to organisations of national significance eg leading national charities like Cancer Research. This reflects the two classes of society lottery – large and small scale.<sup>8</sup>
19. The gambling activity provided typically has the following characteristics – low ticket price, slow draw frequency (often weekly or monthly), in person distribution or subscription entry (as well as some retail distribution), low prize levels within regulatory caps and a specific good cause association. The relatively low prizes and generally limited distribution footprint are key factors that have traditionally differentiated the sector from TNL.

#### ***Potential sources of market erosion:***

##### Growth of the sector

20. The large scale society lottery sector has grown in terms of proceeds (sales) from £178.7m to £355.1m, from 08/09 to 12/13<sup>9</sup>. Even stripping out the two largest schemes, it is still a sector in growth. However, the sector remains small relative to TNL, which generated £1.7bn for good causes in 2013/14<sup>10</sup> with sustained recent growth until the decline seen in 2013/14.
21. As far as participation is concerned, Commission research shows that the growth in proceeds, almost doubling from 2008/09 to 2012/13 (see chart below) has been achieved, even with a reasonably stable proportion of the population playing society lotteries – c.13% claim to have played recently (in the past four weeks)<sup>11</sup> with a slight upturn attributed to the arrival of The Health Lottery (THL).

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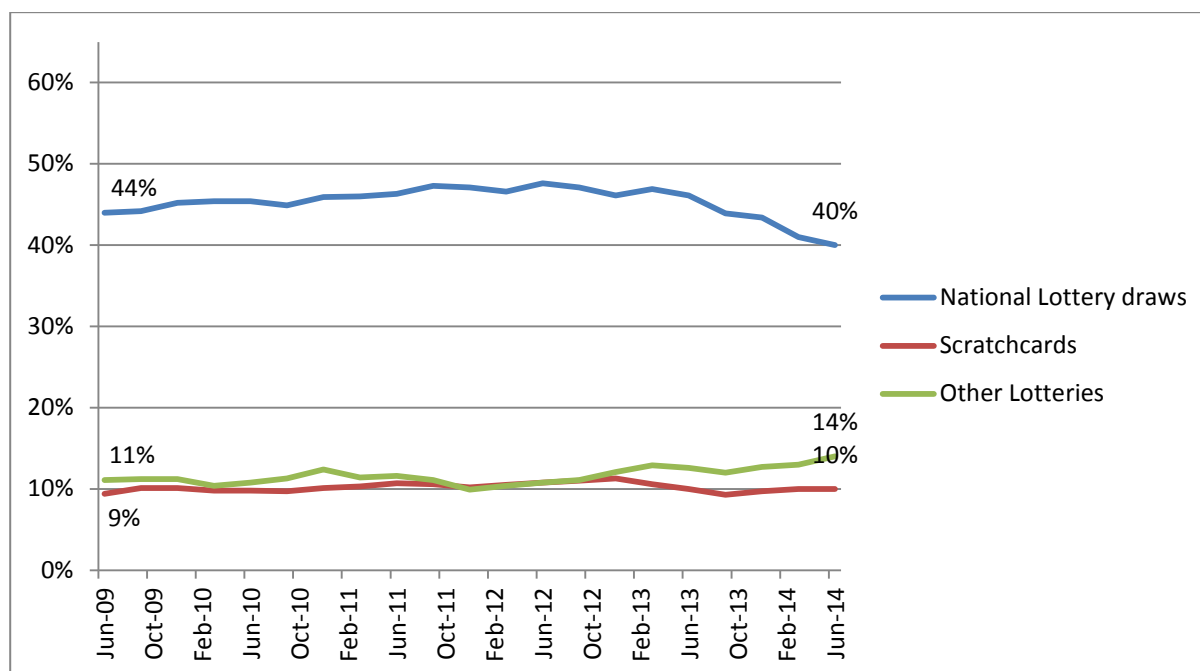
<sup>8</sup> The classification is based on the proceeds, with large society lotteries requiring a licence from the Commission and having higher limits on annual aggregate and individual draw proceeds and small society lotteries being subject to lower proceeds/prize limits and having to be registered with an LA.

<sup>9</sup> Commission RR – Gambling Commission Industry Statistics

<sup>10</sup> Ref Commission – NL Stats

<sup>11</sup> Commission Omnibus Tracker

## National Lottery and Society Lottery Penetration: Claimed Last four weeks play



Source: Commission Tracker data.

Notes: New methodology in June 2012 has comparatively slightly higher claim rate. The trend still shows long-term stability, increasing slightly with the introduction of the Health Lottery. 'Other lotteries' cover 'tickets for charity and other lotteries'. Data is taken at quarterly points, annualised and is indicative.

22. While increasing sales could theoretically impact TNL (and vice versa), a point discussed in research commissioned by DCMS on the impact of THL in 2012<sup>12</sup>, we note that TNL sales have grown at same time as those of society lotteries (even excluding THL). Overall return to good causes (total returns from TNL and society lotteries taken together) have continued to grow. NERA notes that in its view there is currently no real evidence of significant erosion in either direction as a result of general growth in sales and participation<sup>13</sup>. Given a similar environment, in particular of stable consumer penetration, we see no reason why this should change dramatically imminently, given it is essentially a different market.

A combination of an increase in consumers transacting with lotteries online and more sophisticated personal marketing (making the most of specific good causes) could potentially cause some switch from TNL to society lotteries but the barrier of life-changing prizes will remain and we do not currently see this as a large risk to TNL.

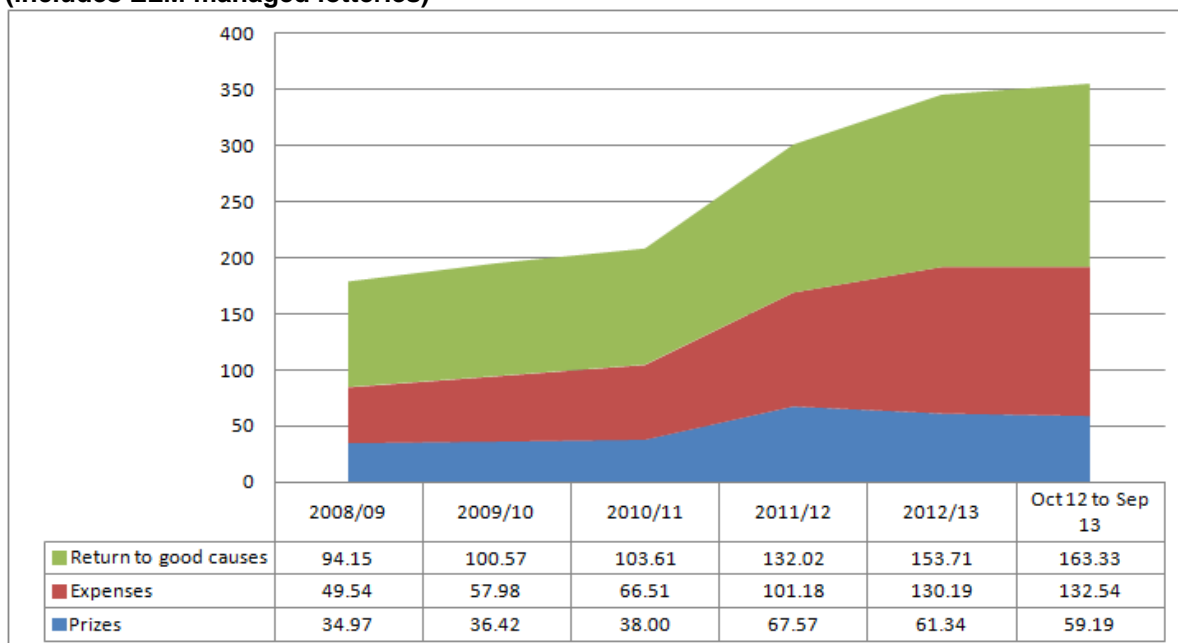
### "Professionalisation/commercialisation"

23. In recent years the large society lottery sector has become, arguably, increasingly professionalised and commercial in feel. This is driven largely by the increased use of lotteries by major charities as a fundraising mechanism, bringing with it more expert brand management and distribution power, but also by changes in technology and use of social media and the increasing prevalence of external lottery managers (more on this topic later). This is characterised by the fact that although return to good causes from society lotteries have increased over time, their share of the overall proceeds (sales) has declined in percentage terms, while expenses have increased. In other words there appears to be a move to spending more as a proportion of proceeds on marketing and other expenses to raise more absolutely but not proportionately for good causes.

<sup>12</sup> NERA 2012 report "Assessment of Lottery Market Issues"

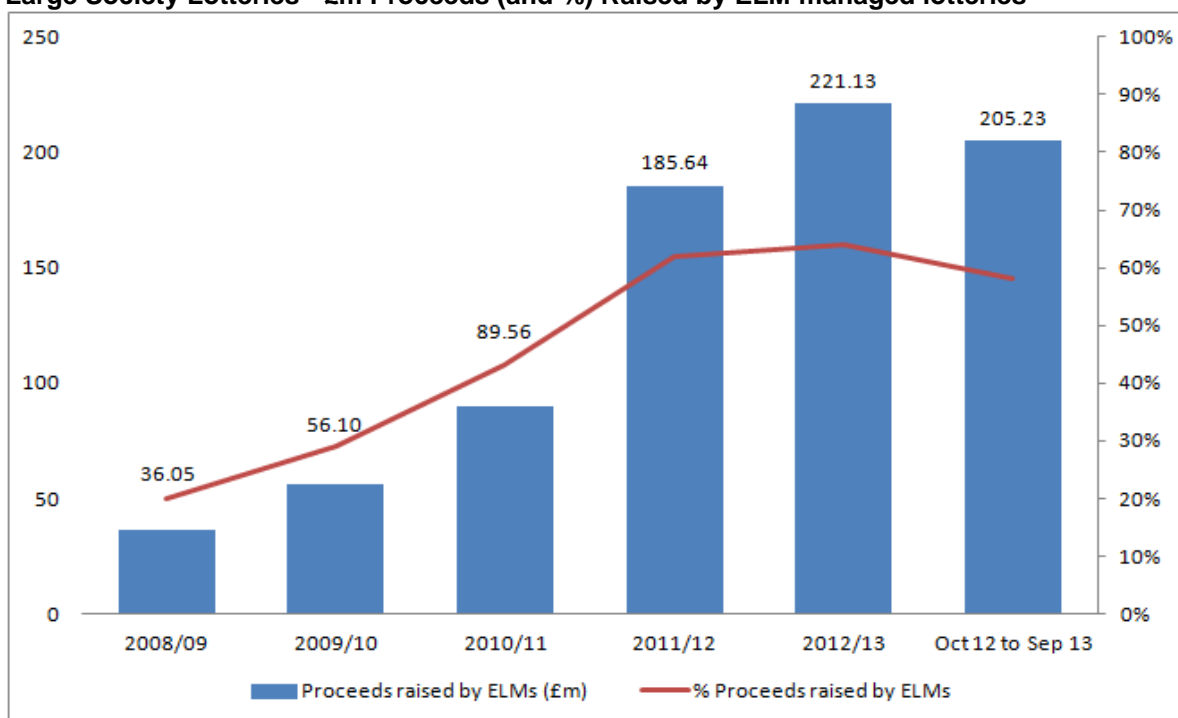
<sup>13</sup> NERA 2012 and 2014 reports. NERA noted an impact in 2012 of up to £300k a week

**Large Society Lotteries - £m Proceeds (sales), Expenses, Prizes and Return to good causes (includes ELM managed lotteries) <sup>14</sup>**



Source: Commission Industry Statistics

**Large Society Lotteries - £m Proceeds (and %) Raised by ELM managed lotteries**



Source: Commission Industry Statistics

24. Even given an increasing commercialisation, consumers continue to regard society lottery products as more or less distinct from TNL products and from other forms of gambling<sup>15</sup>. They see society lotteries primarily as a fun way of donating usually small amounts to a specific cause, with the prize being a somewhat secondary consideration, and TNL primarily as a means of gaining a chance of a life-changing prize.

<sup>14</sup> Notes: Years shown Apr/Mar unless stated. .

<sup>15</sup> Ref. 2012 NLC/Commission Qualitative research

## The growth of umbrella schemes eg The Health Lottery, People's Postcode Lottery

25. Recent years have seen the development of a new product type in the lottery market – the umbrella scheme. This involves marketing several separate society lotteries under a single umbrella brand. The single brand provides considerable marketing efficiencies, driving ticket sales and in turn prizes (although each separate lottery is subject to the limits set out in law). The umbrella scheme is epitomised by THL (launched Oct 2011) and People's Postcode Lottery (PPL) (launched Jan 2008) and typically presents low ticket prices, a more general good cause association than a single society lottery<sup>16</sup>, low frequency draw products<sup>17</sup>, national media reach driving higher sales and therefore larger numbers of higher prizes (within the statutory limits). In the case of THL there is an extensive national retail distribution network through newsagents, supermarkets and post offices, a point of similarity with TNL.

### Impacts

26. While developments like the THL could impact public perception in terms of there being one National Lottery, there remains a gulf in scale between even the largest umbrella scheme and TNL. TNL generates weekly sales regularly in excess of £120m, off a weekly participation figure of nearly half the population. By comparison, each lottery draw within an umbrella scheme can only generate up to £4m in sales and each individual society participating in the scheme may only have aggregate annual sales of up to £10 million. So, for example the THL scheme (as a sum of all the societies participating) may only generate up to £510m in sales over the course of a year (in its current format) if each society were to achieve ticket sales to the maximums permitted.

### **Potential sources of market erosion:**

#### Public perception and subsequent impact

27. The emergence of more prominent umbrella schemes<sup>18</sup> has seen for the first time the possibility of a lottery product competing for national attention with TNL. THL in particular, with its national retail presence and relatively heavy TV and print marketing (facilitated by belonging to a significant media stable including national newspapers and a TV channel) has a similar reach on the public consciousness and therefore influence on the perception of the brands. Impacts are likely to vary from consumer to consumer but include: THL sales benefiting from TNL promotion (and possibly vice versa), THL cannibalising TNL and perhaps a general diminution in the uniqueness of the TNL brand given the comparable national style marketing. THL marketing often references TNL, for example by promoting its (now) cheaper ticket price against Lotto, for example.

28. However, there remain huge differences in the prizes available and it seems unlikely that those driven mainly by the prize – which, as we discussed earlier, typifies TNL players – will see THL as offering serious competition. This is reflected in research commissioned after launch from NERA by DCMS<sup>19</sup>, which suggests that the impact of the launch of THL on TNL sales was likely to be low.

NERA also noted in its 2012 report that it was unlikely that THL would cannibalise other society lotteries, with amongst other reasons the advantages other society lotteries have of a specific good cause (with many players supporters of that cause), ability to communicate directly with many of their players and in the main different distribution routes.

29. The residual risk is that other such schemes emerge which have both minimal incremental sales and a smaller rate of return. This overall would lead to less funds to good causes.

30. We recognise that there are significant difficulties with regard to setting up an umbrella scheme of national scale to impact TNL. NERA note that the difficulties extend beyond simply the key comparative of prize level<sup>20,21</sup>. It is worth noting that to compete with TNL a market entrant would

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<sup>16</sup> One associated risk here may be the increased difficulty of the 'smaller' charities achieving cut-through

<sup>17</sup> Though THL and PPL offer faster play instant and bingo products alongside their lottery offerings online

<sup>18</sup> It is worth noting that this concept is not new – what is new is the 'success' and scale achieved by operators recently. Other schemes have been either relatively low level or limited in duration

<sup>19</sup> NERA 2012 report "Assessment of Lottery Market Issues"

<sup>20</sup> NERA 2104 report

require significant consumer penetration. This would need to be driven currently (while online remains in its infancy in this area) by a significant retail infrastructure and a commitment to consistent expensive marketing spend (in particular during start-up<sup>22</sup>).

31. Those who currently have access to significant retail infrastructure, such as supermarkets, may balk at the return on investment for lottery products through advertising compared to other products they sell. Those without such an infrastructure may find it hard to set up or maintain, where sales and return to retailers are potentially comparatively very small.

### **c) Presence/ growth of products that involve betting on the outcome of lotteries**

#### ***Characteristics***

32. Most major bookmakers have offered products that involved fixed odds betting on the outcome of lotteries for many years. The lotteries involved tend to be foreign national lotteries, with the Irish Lotto being a common subject. It is illegal to offer a bet on any lottery that forms part of the (UK) National Lottery<sup>23</sup>.
33. It is important to understand that the products in question are betting products and not lotteries and not therefore subject to any of the statutory limits that apply to lotteries. This point becomes particularly important in light of the commercial pressure that appears to exist to market such products as, essentially, high prize lotteries, perhaps relying on the more favourable public disposition towards lotteries, arguably driven by TNL.
34. Mintel does note that this could be an option charities explore. It also identifies that 57% of lottery players say a lack of interest in gambling generally is one of the factors that discourages them from visiting gambling venues (eg betting shops, bingo clubs, casinos, amusement arcades), or from visiting more often than they do currently<sup>24</sup>. A lottery tone could make this product more acceptable for these consumers when online.
35. The existing regulatory framework seeks to prevent such products masquerading as lotteries in the interests of fairness and openness – indeed the Commission has taken action where it has concerns that it is not clear to consumers that they are participating in a bet and not a lottery. However, the boundary can be somewhat blurred and the Commission is reviewing its controls in this area though customary very wide use of the words ‘play’ and ‘lotto’ make this a difficult line to draw and might need legislation if a clear boundary needs to be maintained.

Putting to one side regulatory matters relating to fairness and openness, products that involve betting on the outcome of lotteries tend to be marketed on the basis of offering regular, large jackpots for low stakes. They are distributed both online and terrestrially although their retail availability is restricted to licensed betting premises. They are not available to under 18s.

36. The market is likely not a large one currently. Using industry data provided by H2 Gambling Capital and data published within the Commission’s Industry Statistics we estimate that GGY derived from betting on the outcome of lotteries across the whole UK sector may be in the region of £340m<sup>25</sup>.
37. Given the small scale of the market it is very difficult to assess consumer penetration. It would appear to be a growing market, off a likely very low base.

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<sup>21</sup> NERA 2012 report “Assessment of Lottery Market Issues”

<sup>22</sup> Media quotes for THL marketing spend at start-up were for around £20m

<sup>23</sup> Camelot has also noted that it is currently possible to bet on EuroMillions – with a loophole that it is not the UK version which is being bet on. Given the brand salience of EuroMillions consumers may find this a more comfortable offering compared to foreign lottery opportunities.

<sup>24</sup> Ref Mintel Gambling Review UK, April 2014

<sup>25</sup> Note: Accurate data on activity of this kind are not currently available but we have provided a rough estimation using available sources.



## **Potential sources of market erosion:**

### Dilution of distinctiveness

38. Lottery betting products certainly have the potential to create a similar look and feel to TNL and society lottery draw-based products. This comes from the association with lottery imagery, the low stakes and frequency of play (mirroring the lotteries on which they are based) and the larger, potentially life-changing prizes (Lotto Network, for example, has a regular base jackpot of £7m which can roll). This may combine to produce the impression of national lottery-like experience. In addition, although very limited at present, the advent of a good cause element may provide a further point of comparison. Taken together, this may conceivably place TNL, and perhaps society lotteries, in an environment in which they become less distinctive and at greater threat of cannibalisation.

### Immediate threat of cannibalisation of lottery sales

39. As noted above lottery players may find a lottery tone in a betting product more acceptable. That said there remain some key points of difference and challenges in terms of lottery betting products posing a significant threat to TNL and other lottery sales:

- No lottery betting products currently come anywhere near the level of public awareness or penetration enjoyed by TNL. The same issues faced by new entrant umbrella schemes discussed above are relevant here in terms of retail infrastructure and media spend.
- None constitutes the shared experience offered by TNL particularly around the draw-based offers, driven by live, high profile draws on the main public service broadcasting channel with attendant publicity.
- Bets that are based on a pooled market across Europe may be threatened by developments abroad which would make them illegal. This may not stop the product but would make the current offering harder to replicate.
- Some consumers may be put off by any clearer marketing of the betting nature of the product.

40. The biggest risk that products such as the Lotto Network currently poses is more of a slow-burn which would gather pace if consumer trends move to on-line and simple proliferation of providers (and specific cause to promote) increases the consumer base. NERA judge that new Charity fundraisers, or those without a lottery presently, could adopt this approach as a preferred means of raising money for good causes<sup>26</sup> given it may appear to offer a simple entry to market but there is little evidence of this beginning to happen.

41. In conclusion these products do not appear to have the potential to cause a great degree of impact currently and while there may be a future potential it would require considerable consumer trend change and challenges to be overcome.

### *Instant Products*

#### **d) Growth in retail instant products (“Scratchcards”)**

##### ***Characteristics***

42. Retail scratchcards are typified by a relatively faster speed of play in comparison to more traditional draw-based products<sup>27</sup>. They are generally low price (noting that the TNL product range extends to £10 tickets) and low margin. They are distributed extensively in retail outlets under exactly the same rules as apply to draw-based products (whether regulated as a TNL product or as a society lottery product under gambling legislation). They are available to sixteen year olds

43. TNL scratchcards have been in the market since 1995 and, particularly in recent years, have seen consistent growth

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<sup>26</sup> NERA 2014 report

<sup>27</sup> in essence, the time it takes to purchase the ticket, or numbers of tickets, and remove the foil to reveal the result

44. Other lotteries make scratchcards available on a much more limited basis, 46 operators currently offer scratchcards, such as pull-tabs. While we do not have robust data on sales by other lotteries, from participation data we would expect the market to be tiny in comparison to TNL. 16% of the population play TNL scratchcards regularly<sup>28</sup> compared with 3% who claim play other non-TNL scratchcards.

### ***Potential sources of market erosion:***

#### Competition

45. There is not currently a fully competitive retail environment for scratchcards<sup>29</sup>. Society Lotteries suffer the same distribution and prize and proceeds cap challenges as for draw-based products. Society lotteries do link with retail chains to sell scratchcards either directly through their shops or via kiosks run by the lottery themselves in some of their stores but not even collectively on the scale of TNL<sup>30</sup>.
46. That said it is a market where operators are looking to expand, there are recent examples of this happening and the current position cannot be taken for granted for the future.
47. Society Lotteries and operators may look at lottery experience around the world which considers that scratchcards do not on the whole cannibalise draw-based products and so think that the challenges existing with the product are worthwhile to attempt to overcome.
48. Regardless our view is that we do not think there is a cannibalistic scratchcard market due to prize levels and the fact that they are not sold in meaningful numbers (beyond a few kiosks currently) in the same places as TNL. If THL offers scratchcards in the same outlets there will likely be some cannibalisation, although small if experience of draw-based products was followed.

A bigger risk to TNL scratchcards may actually be changes in retail environment (such as stores moving to self-service) hampering accessibility.

#### Reduction in public support/tolerance

49. Scratchcards are at the harder end of the lottery gambling spectrum. Public concern has been raised from time to time around scratchcards as an appropriate TNL product. This has been accompanied by claims of unfairness from the wider gambling industry, given relaxations, on age and advertising for example. If scratchcards as a product become more prevalent, tolerance for the product may diminish, if the perception of overall lottery brand differentiation from the wider gambling sector narrows.

### **e) Growth in online instant products:**

#### ***Characteristics***

50. TNL was a relatively late mover into this heavily colonised market. The space is occupied by a diverse range of products from many providers covering the entire spectrum of gambling. Online bingo games, casino games (including online slots) are typical of the market and were the first movers; lottery instant win products, marketed, more or less, as online scratchcards are later entrants.
51. While society lotteries are moving into this space the dominant lottery product in this space is TNL's interactive instant win products (IIW). Historically such products have been a secondary purchase (ie play Lotto then an IIW) as opposed to the primary purchase but looking forward there may be a digital native TNL generation that do not get introduced to the portfolio by draw-based products as their parents did but primarily through such IIWs.

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<sup>28</sup> Commission NL Tracker

<sup>29</sup> NERA 2014 report

<sup>30</sup> There are also pulltab vending machines that sell society lottery and private society lottery tickets but numbers are very limited.

52. Although outward presentation can vary considerably between these products, in practice there is very little difference between them in terms of characteristics and playstyle. They tend to be available at a low stake and offer rapid, repetitive play (widely considered to be a risk factor for gambling problems) for a range of potentially large prizes. They are likely to become an increasingly mobile purchase as that channel matures.
53. In terms of market size, GGY for online slots has grown in the GB regulated market from £5.11m in 2009/10 to £24.80m in 2012/13<sup>31</sup> but of course at present the bulk of the market is regulated overseas. Including using industry data provided by H2 Gambling Capital and data published within the Commission's Industry Statistics a rough estimate for the full GB market could be in the region of £400m.
54. The market size is reflected by relatively low participation figures. Online slots, machine style games/instant wins have seen small growth in claimed last four weeks play from 0.3% in 2012 to 0.7% in 2014<sup>32</sup>.
55. The key differentiating factors, given that draw-based advantages of reach and prize level are not held by TNL in this sector, are:
- regulatory: where TNL products are available to 16 year olds compared to 18 for wider gambling but subject to greater controls, such as spend limits
  - Tax regimes – the return to player that TNL is able to offer is constrained by the 12% Lottery Duty on sales in comparison with the wider gambling industry which operates under a gross profits tax. The gross profits tax allows operators to offer considerably higher, and therefore more attractive, returns to players.
56. The level of lottery duty applied equates approximately to a GPT level of 36%, compared to 15% for remote gambling operators and 0% for society lotteries. In effect this means that gambling operators can offer games with high return to players upwards of 90% and still make profit while current TNL games are usually around 70%. TNL also obviously is required to make a contribution to good causes arguably greater than the return expected by private sector investors, which will also impact the potential level of prizes offered and attractiveness to players.

It is unlikely that experienced players, a group that may increase in size in the future, will keep to TNL offering where returns to player are not so attractive. We would note however that, as with scratchcards, identifying the complementary 'sweet spot' of return to player for return to good causes is in itself a difficult balancing act, and not simply a question of inexorably raising the rate of return to player.

The key question to understand the likelihood of this impact of 'experienced' play is to monitor the factor of brand trust, mentioned below.

- Brand trust – currently TNL will attract players to IIWs that might not consider playing the same products on gambling sites due to the fact they simply would not consider visiting gambling sites.

### ***Potential sources of market erosion:***

57. In headline terms TNL exists at a commercial disadvantage in a competitive market and runs a risk of trying to maintain a share of a growing market at the cost of losing a degree of its brand differentiation.

### **Current competition**

58. The market is already both highly competitive and crowded. Unlike the retail environment, where TNL products are facing only limited competition from other lottery products highly constrained by

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<sup>31</sup> Commission Regulatory Returns

<sup>32</sup> Commission Omnibus tracker

statutory limits, the competition in the online space comes from mature gambling products that are not facing such constraints. This is likely to mean that TNL products will find it much harder to retain a significant market share – and in fact may only be able to do so by migrating to increasingly “harder” playstyles, mimicking more closely other gambling products or innovating products beyond the current range, such as social gaming. Again, this may impact perception of monopoly legitimacy.

### Consumer migration online

59. There are two facets to consumer migration online; brand differentiation and market expansion.

60. Consumer engagement with TNL remains predominantly linked to high-profile draw-based retail products which, as discussed above, are still relatively distinct from other gambling and likely to remain so for the foreseeable future, notwithstanding the potential for change we have outlined.

However with general consumer trends pointing to increased migration online<sup>33</sup> to source a very wide range of products and services, it seems likely that primary engagement with TNL products will be online for an increasing proportion of players, in particular new players. Qualitative research carried out for the Commission suggests that historic consumer perception of brand differentiation which is clear at retail (betting takes place in bookmakers, lottery at a newsagents and so on) could be clouded online, where the look and feel may be similar. TNL and society lotteries may need to work hard at how the brand looks online to retain differentiation of the products they offer and to provide the consumer with something that compensates for the lower return.

61. Mintel notes that lotteries tread a difficult line in maintaining the good cause brand, rather than being viewed as a more ‘predatory’ brand<sup>34</sup>.

62. In terms of market expansion Mintel considers the current barrier of lottery consumer resistance to move online compared with consumers of other products but note that more exciting versions of instant games do provide a market opportunity for TNL.<sup>35</sup>

### *Brand Leverage*

#### **f) Wider brand utilisation across the gambling spectrum**

##### ***Characteristics***

63. We have noted earlier that products of a similar nature can cloud consumer perception of the market, in addition the distinctiveness of market brands are starting to be utilised with the same potential result.

64. Operators are either leveraging the branding through licensing to other operators or expanding their business to offer different forms of gambling within a brand.

65. THL in particular has demonstrated an ambition to diversify its brand into other types of gambling product, notably bingo, casino and betting. The Commission has placed some constraints on the use of established lottery branding (and association with good causes) to drive traffic to ‘harder’ gambling products.

66. There is also a different perspective where betting operators such as Lotto Network, as previously noted, are using lottery brand terminology or good cause language to promote betting products or fortify brands.

##### ***Potential sources of market erosion***

67. Awareness of what are currently fringe products, explored earlier, with operators with limited consumer penetration is naturally small. It therefore follows that any current impact is likewise

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<sup>33</sup> NERA 2014 report

<sup>34</sup> Ref Mintel Gambling Review UK, April 2014

<sup>35</sup> Ref Mintel Gambling Review UK, April 2014

limited. The risk is the cumulative impact of eroding the market between lotteries and wider gambling.

68. Our view, while consumer penetration by associated operators is limited, is that any impact is likely to be small but it has the potential to change if that penetration increases.
69. There also remain policy questions to be answered around the extent to which non-lottery gambling more generally is acceptable for use as a means of raising funds for good causes. It is interesting to note that a draft set of EC recommendations included the removal of the capacity to reference good causes in advertising. While it appears that this did not make it through to the final set of recommendations, there may be a risk that such an important differentiator for lotteries, which helps cause-specific lotteries drive sales and non-cause specific lotteries maintain sales, is threatened again in the future. Conversely it may be difficult to argue that gambling products may not work with charities to raise money for good causes as many other commercial producers do.

## **Conclusion**

70. The overall gambling market is one that is becoming more standardised in look and feel. The changing marketing and distribution modes, driven primarily by digital, has the potential to blunt consumer perceptions of previously distinct markets and to reduce the attractiveness of more traditional 'soft' gambling lottery products.
71. The market indications are that:
- While TNL stalled in 2013/14, recent trends in the generation of funds for good causes from lotteries overall has been very positive.  
  
In the longer-term, with particular regard to draw-based products, the last year has demonstrated that further positive growth from TNL is not guaranteed. It is important to remember that in quantum TNL continues to dwarf the society lottery sector.
  - For draw-based TNL and general society lottery products the impact on returns generated from potential threats posed by umbrella society lottery schemes and betting on lottery products is currently small. A larger impact in the future cannot be ruled out if such products gain genuine consumer traction but we think this unlikely, given the considerable commercial barriers to doing so.  
  
Risks also exist from more general competition for the leisure pound and time and from other gambling entities beyond the lottery sector including those deriving wider legitimacy from good cause association.
  - In the non remote instants sector TNL and society lottery products co-exist without an impact, at retail; new offerings, threaten the status quo and continue to be developed but are unlikely to be a serious threat individually so long as TNL retains its monopoly capacity for higher prizes. A cumulative impact cannot be ruled out but we still think this is improbable.  
  
Online in a competitive, growing instants market it is not clear how funds for good causes can both maintain public legitimacy as a soft product and compete successfully for market share without competing more aggressively with harder gambling products. It is also not clear how TNL can compete for consumer attention through return to player in the longer term where it pays considerably more duty than its rivals.

## Keeping gambling fair and safe for all

For further information or to register your interest in the Commission please visit our website at:  
**[www.gamblingcommission.gov.uk](http://www.gamblingcommission.gov.uk)**

Copies of this document are available in alternative formats on request.

Gambling Commission  
Victoria Square House  
Victoria Square  
Birmingham B2 4BP

**T** 0121 230 6666

**F** 0121 230 6720

**E** [info@gamblingcommission.gov.uk](mailto:info@gamblingcommission.gov.uk)