



M E M O R A N D U M

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To: California State Lottery Commission

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Subject: Item 8(g) – Strategic Plan and Fiscal Year 2020-21 Business Plan

ISSUE

The California State Lottery (Lottery) establishes strategic plans to provide direction to the organization for long-term objectives and strategies. With the strategic plan as a guidepost, the Lottery develops a Business Plan to cover the tactical details for one specific fiscal year in support of the long-term objectives and strategies.

Most of the prior strategic plans covered a period of three years, and it is now time to refresh the Lottery's plan and provide guidance for FY 2020-21 through FY 2022-23.

BACKGROUND

The process to develop the next strategic plan began in the summer of 2019 with an extensive analysis of California Lottery business, a review of the U. S. lottery industry, and an examination into other external consumer and retailing trends. This information included not only sales trends but also insights into the sources behind these changes in sales, industry comparisons of playership rates and spending amounts, consumer perceptions, and implications from demographic and generational changes. This Business Review was presented to the organization in a series of meetings during the months of October and November.

With this background and information, the Executive Management Team worked with their key staff in December to identify the Lottery's internal strengths and weaknesses along with its external opportunities and threats. This SWOT analysis led to isolating the Key Priority Issues that the Lottery must address in the upcoming three to five years to maximize its success.

Over the next several months, groups from the Executive Management Team worked with different Key Priority Issues to create the direction and key objectives for this area. During this time period, the COVID-19 pandemic struck California and impacted Lottery operations, sales, and the direction of this strategic plan. The work from the teams exploring a specific Priority Issue along with new elements to help adjust and recover from the public health emergency were then integrated to create a cohesive strategic plan.

DISCUSSION

As a result of this process, the strategic plan outlines a general vision for the period encompassing FY 2020-21 through FY 2022-23. While overall themes, major goals and key strategies are provided, the specific tactics including annual financial objectives will be set in the Annual Business Plan for each year. This issue memo will detail the key elements of the strategic plan and discuss specific Business Plan tactics for FY 2020-21 in each major section of the strategic plan.

During this three-year period, this plan envisions the Lottery's contributions to public education surpassing the \$2 billion threshold for the first time in its history and sets a trajectory to ultimately become the largest lottery in the nation in terms of sales and profits. To attain the \$2 billion in profits that will go to California public schools, this will likely require sales to reach about \$8.25 billion by the end of this three-year period. However, in developing this plan, the sales growth envisioned will be attainable in a responsible manner.

Sales in the current fiscal year will be lower than in the prior fiscal year. This is due to a combination of the absence of large jackpots in Powerball and Mega Millions and the impact from the COVID-19 pandemic. The sales growth that was seen during the three fiscal years ending in FY 2018-19 resulted from both gains in the number of Californians playing Lottery games as well as increases in the amount players spent. In terms of which games fueled this growth, Scratchers were the primary driver; but Mega Millions also had strong gains.

About two-thirds of all California adults now play the Lottery at least once during the year. Analysis of other large U. S. lotteries showed that estimated player spending in these other jurisdictions was typically higher than found in California. In assessing alternate approaches, profit growth seems to be maximized by having sales growth over the next three years primarily coming from increased spending by existing players – particularly from casual players. However, objectives in the strategic plan also create the ground work for expanding the total player base even further in the future.

Based on the preceding financial objectives and incorporating the insights learned during the review of the Lottery's business and general retail and consumer trends, the objectives and strategies outlined in the strategic plan revolve around three different

themes. These elements will provide a focus for the Lottery's efforts over the next three years:

- Adapting to the "New Normal" that resulted from the pandemic
- Transforming the Lottery into a mature yet modern and nimble organization
- Building trust and confidence among stakeholders and the public in general

The emergency health crisis has left its imprint not only on how the Lottery moves forward in the next couple of months but also how it approaches changes over the next several years. The COVID-19 pandemic along with the societal changes necessary to stem the spread of the virus will have long lasting effects. Consumers have adjusted their lives, and this will change businesses, particularly the retail sector, moving forward. It appears that the pandemic has accelerated some of the changes and trends in the retail landscape that were already occurring. This will require the Lottery to make changes even more quickly to adapt to the new reality.

The Lottery has been in existence for more than 34 years. While that may be young compared to some departments of state government, the Lottery is no longer a start-up operation. As such, it needs to evolve into a more mature organization with more structured processes, procedures, and controls. At the same time, these changes need to be assisted by current technology to ensure the processes do not become slow and burdensome. The organization needs to retain its ability to be nimble and quickly adapt to changes in sales, marketplace conditions, and shifts in consumer attitudes and preferences.

Few Californians know much about the Lottery beyond its products. Most do not know how much the Lottery provides to its beneficiary and some are not certain if money actually reaches schools or makes a difference. They are not aware of the Lottery's positive contributions – not only in terms of funding education but also how the Lottery provides significant dollars to local businesses, ensures the integrity of its games and maintains environmentally-friendly facilities. With this lack of understanding, many are skeptical about the Lottery organization and feel it may be hiding something.

The details of the proposed strategic plan and the FY 2020-21 Business Plan, including the key insights that provided the rationale for its major themes and directions, will be presented at the Commission meeting. These objectives are supported by a combination of multi-year projects, some of which were part of last year's approved business plan, and new tactics proposed for the upcoming year.

The key objectives in the strategic plan and the FY 2020-21 Business Plan include:

Modify Operations to Ensure Health and Safety and Recover from Depressed Sales

This objective will be associated primarily with FY 2020-21 as the Lottery continues adjusting operations to ensure the health and safety of employees, retailers, and players while trying to recover from depressed sales as a result of the pandemic and some of the restrictions imposed.

The Scratchers product plan provides one example of how this objective will be achieved. In the last quarter of this fiscal year, only one set of new games will be launched due to changes in the distribution centers to create social distancing. It is anticipated that with additional solutions coming into play, the first six months of this coming fiscal year will contain a total of five sets of new game introductions.

Revisit Retail Strategies Adapting to New Consumer Preferences

The types of retailers where the Lottery sells tickets and the process for buying a ticket have not materially changed from practices in the 1990's. Yet, much has changed in the retail landscape over the past 20 – 30 years not only in terms of the types of stores people shop but also the way consumers prefer to select, purchase, and pay for their items. Shifts in consumer preferences have accelerated with the pandemic. The Lottery must revisit its practices in these areas to determine how it can adapt to the new landscape.

In FY 2020-21, consumer research will be conducted to better understand consumer behavior and perceptions related to shopping at retail and online in a post-pandemic world. Additionally, an analysis of the current Lottery Act restrictions on technology will be undertaken prior to developing potential solutions for some of these retail issues.

Grow Draw Game Sales Particularly Jackpot Games and Hot Spot

Jackpot Games and Hot Spot were negatively impacted by the pandemic to a greater extent than other products in the Lottery's portfolio. On top of that, players of Draw Games have typically spent fewer dollars during the year on these products compared to the spending Scratchers players do in buying Scratchers tickets.

A solid focus on improving sales in the Draw Game portfolio is needed, particularly for Jackpot Games and Hot Spot for the short-term, to revive sales to pre-pandemic levels as well as for long-term growth. In FY 2020-21, a cross-division team led by Sales & Marketing will develop potential tactics to be implemented over the three-year period and assess which ones are the most promising in terms of generating additional profits for public education in the long-term.

Defuse the Barriers to Play by Changing Perceptions

The barriers to playing Lottery have been identified from consumer research. With the exception of having to buy Lottery tickets with cash, the key constraints California adults

have about playing the Lottery a bit more often or at all involve their misperceptions or negative associations with lottery in general. Marketing communications are in development that highlight the fun and entertainment value of playing that can begin overcoming these barriers to play. This effort is slated to begin in FY 2020-21.

Inform the Public and Stakeholders about the Lottery

Based on a thorough analysis, a strategic approach to communicate about the Lottery organization is being developed. The strategy outlines a need for this effort to be rolled out in stages to various audiences. When a member of the general public hears a message about the Lottery, they are likely to ask a retailer or a friend/family member who is an avid player about it. Therefore, it is important that the initial efforts in FY 2020-21 are focused on informing retailers, employees, and the Lottery's most loyal players who participate in the 2nd Chance Program. Additionally, reaching these audiences is cost-effective by using channels owned by the Lottery, such as email.

Shift the Corporate Culture in the Lottery Organization

There will be many elements in the effort of transforming the Lottery. To do this successfully, it must be more than just changes in processes and procedures; the change needs to be within the DNA of the organization itself. To achieve this type of culture change within a company, the firm must look to its people – they are the ones who will create the change in the organization. In this endeavor, the Lottery's biggest asset is its people. Rather than focus on individual divisional needs, staff need to see how their collective effort leads to the Lottery's contribution to public education.

Other components in this Lottery transformation involve prioritizing quality customer experiences while also maximizing profitability and standardizing the decision-making process throughout the organization, to name just a few.

RECOMMENDATION

Lottery staff recommends that the California State Lottery Commission approve the proposed strategic plan and FY 2020-21 Business Plan.