



# **Pennsylvania Lottery Profit Report**

## **As Required by Act 53 of 2008**

2017

## **END OF FISCAL YEAR 2016-17 ANALYSIS**

The Pennsylvania Lottery had its second-best sales year on record with more than \$4 billion (\$4,001,035,373) in sales during fiscal year 2016-17, a decrease of \$134.13 million from the previous fiscal year's record total. Unlike in 2015-16, when there was a world-record Powerball jackpot of nearly \$1.6 billion, there were no record jackpots to drive sales last fiscal year.

For the sixth consecutive year, the Lottery recorded profits exceeding \$1 billion (\$1,045,731,338) during fiscal 2016-17. As a reflection of lower sales, net revenues were off by \$75.59 million year-to-year.

The Lottery paid \$2.59 billion in prizes, meaning approximately 65 cents of every Lottery sales dollar went back to players. A total of 84 players won prizes of \$1 million or more during the fiscal year.

More than 9,100 licensed Lottery retailers statewide earned \$211.4 million in sales commissions. Again, as a reflection of lower sales, this marked a decrease of approximately \$6.9 million from the prior year. This past fiscal year, under Act 39 of 2016, the Lottery expanded its retail network by adding over 300 Fine Wine & Good Spirits locations.

Operating costs were 2.22 percent of ticket sales.

The Pennsylvania Lottery remains one of the best-performing lotteries of the 45 U.S. Lotteries, ranking 6th in population, 6th in ticket sales, and 5th in profits in fiscal year 2015-16 (the most recent period for which national statistics are available). The Pennsylvania Lottery outperforms the industry in per capita scratch-off sales, ranking 4<sup>th</sup> in the U.S. It should be noted that several lotteries ranking higher than Pennsylvania have the advantage of including profits from Video Lottery Terminals (VLTs) and Keno, or both.

The Pennsylvania Lottery remains the only state lottery that designates all its proceeds to programs that benefit older residents. Since its inception in 1971, the Pennsylvania Lottery has contributed nearly \$28 billion to programs that include property tax and rent rebates; free and reduced-fare transit; the low-cost prescription drug programs PACE and PACENET; care services; and the 52 Area Agencies on Aging, including full- and part-time senior centers throughout the state.

## **LOTTERY PROFIT RETURN**

The Lottery ended fiscal year 2016-17 with a net profit percentage of 26.14 percent, down from the 27.12 percent recorded in fiscal year 2015-16. As the sale of scratch-off comprises a larger percentage of total sales, the net profit percentage declines.

By law (Act 201 of 2014), Lottery is required to return 25 percent in net profits for programs that benefit older Pennsylvanians. Using the reduction of the minimum rate of return, the Lottery is able to execute a marketing plan and product portfolio to maximize profits for senior programs.

Act 53 of 2008 granted the Pennsylvania Lottery temporary relief from the mandated 30 percent minimum return that had been in place since the Lottery's inception. The Lottery was given the latitude to return a minimum of 27 percent through fiscal year 2010-11. Act 23 of 2011 extended the 27 percent minimum return through fiscal year 2014-15. Act 201 of 2014 set the minimum return percentage at 25 percent starting with

the fiscal year 2014-15. While this lower percentage has allowed the Lottery to continue to offer its players the products they want to play, increasing demand for lower-margin games will require elimination, or further lowering, of the minimum return requirement. Without it, and the flexibility to offer the games Lottery players want, sales and profit will decline over time.

Product mix plays an important role in the overall rate of return. Product mix is influenced by many factors including shifts in consumer preferences within the Lottery’s game portfolio and the length of jackpot runs. Scratch-off products return approximately half the amount of profit for the same dollar spent. The trend of players gravitating toward Scratch-Offs, and particularly higher price point Scratch-Offs, continues in Pennsylvania and in the lottery industry as a whole.

The table below shows that as the percentage of sales continues to shift toward Scratch-Offs, the overall profit margin continues to decline.

**Scratch-Offs and Profits as a Percentage of Sales (FYs 2006-07 Through 2016-17)**

Last 10 Fiscal Years	FY07-08	FY08-09	FY09-10	FY10-11	FY11-12	FY12-13	FY13-14	FY14-15	FY15-16	FY16-17
Scratch-Offs - percent of Sales	55.25%	56.92%	57.04%	59.92%	61.32%	62.31%	64.35%	67.85%	67.53%	68.15%
Profit - percent of Sales	30.05%	29.48%	29.87%	29.95%	30.48%	28.85%	28.46%	27.77%	27.12%	26.14%

This past fiscal year, the Pennsylvania Lottery launched a new category of games called Fast Play - instant style games sold through the Lottery’s terminals along with all the other draw game products. Although purchased through a lottery terminal, the payouts on Fast Play games are similar to Scratch-Offs thus have a lower profit margin compared to most draw games.

Eventually, the Lottery will need full relief from the minimum return rate in order to maximize profits for older Pennsylvanians. Note: Most state lotteries do not have a profit percentage requirement. Pennsylvania is one of only eight states that still have a profit percentage requirement. Pennsylvania ranks 5th amongst U.S. lotteries in per capita profits - none of the four states ranked ahead of Pennsylvania have a mandated profit return requirement.

**STATE OF THE LOTTERY GAME PORTFOLIO**

The Pennsylvania Lottery maintains a diverse product portfolio, providing lottery games that meet an equally diverse consumer population. The Lottery’s product portfolio became even more diverse in February 2017 when it launched a new category of games called Fast Play. Fast Play games are instant win style games sold through the Lottery’s draw game terminals.

**Scratch-Offs**

Scratch-Off sales of \$2.73 billion were down by \$66.04 million, or 2.4 percent, from the previous year. For the first time in seven years, the Lottery saw its Scratch-Off sales decline. Much of this year-over-year decline can be attributed to the \$1.6 billion Powerball jackpot from the previous year. Large jackpots often have a positive effect on the sales of scratch-off tickets. Without a record-setting jackpot, scratch-off sales were not able to keep pace with the previous year.

Sales of \$20 and \$30 Scratch-Offs continued their strong growth trend. The two price points were up \$52.6 million or 6.4 percent over last fiscal year. However, the \$10 and below price points were down sharply: \$10

Scratch-Offs were down \$27.2 million or 4.6 percent; \$5 Scratch-off games were down \$40.7 million or 4.5 percent; and the \$1, \$2 and \$3 price points were down \$50.8 million or 10.8 percent.

As with most lotteries, the Scratch-Off sales mix is shifting toward the higher price point games. The table below shows the sales migration toward the higher price point games over the last six fiscal years. As a result, the average selling price has risen as well.

**Scratch-Offs - Percentage of Sales By Price Points**

Scratch-Offs	\$1	\$2	\$3	\$5	\$10	\$20	\$30	Avg. Selling Price
FY16-17	3.3%	6.1%	5.0%	30.8%	19.1%	26.7%	9.0%	\$5.41
FY15-16	3.9%	7.2%	5.7%	32.6%	21.1%	22.1%	7.4%	\$5.15
FY14-15	4.1%	7.5%	6.3%	30.5%	20.0%	24.7%	6.8%	\$5.12
FY13-14	4.5%	8.7%	7.0%	29.8%	19.7%	25.9%	4.5%	\$4.87
FY12-13	5.0%	9.9%	7.0%	30.6%	19.3%	28.2%	0.0%	\$4.59
FY11-12	6.0%	11.6%	6.7%	32.2%	18.7%	24.8%	0.0%	\$4.24

The Scratch-Off game category, formerly called Instant Games, accounted for 68.1 percent of total sales in fiscal year 2016-17, up from 67.5 percent in 2015-16.

**Multi-State Lotto: Powerball®, Mega Millions® and Cash4Life®**

Multi-state game sales (Powerball®, Mega Millions® and Cash4Life®) fell by over \$127 million, or 25.6 percent, from the prior year. Decreased Powerball and Power Play® sales accounted for \$105.4 million of that decline. The Lottery estimates that the run-up to a nearly \$1.6 billion Powerball jackpot generated \$130 million in incremental sales for 2015-16 that were absent last year.

All multi-state game sales were down in fiscal year 2016-17. Mega Millions® and Cash4Life® sales were down a more modest \$12.0 million and \$9.6 million respectively.

The multi-state game category accounted for 9.2 percent of total sales in fiscal year 2016-17.

**In-State Lotto: Cash 5, Match 6 Lotto and Treasure Hunt**

The in-state lotto game category was up 3.4 percent in fiscal year 2016-17 over the prior fiscal year. Cash 5 sales were down \$7.1 million or 5.2 percent. Treasure Hunt sales were up \$2.6 million or 9.2 percent. Match 6 Lotto sales were up \$12.4 million or 18.5 percent.

Together, the in-state lotto game category accounted for 6.0 percent of total sales in fiscal year 2016-17.

**PICK Games: PICK 2, PICK 3, PICK 4, PICK 5 and Wild Ball**

PICK games ended fiscal year 2016-17 up \$8.7 million, or 1.5 percent, as compared to the prior year. PICK games were up for the first time in nine years, largely because of the Wild Ball add-on introduced in September 2016.

The new Wild Ball feature for the PICK family of games was a bright spot in this segment of the game

portfolio, generating \$23.4 million in new sales. Wild Ball accounted for about 4.0 percent of PICK Game sales.

PICK games accounted for 14.7 percent of total sales in fiscal year 2016-17.

### Millionaire Raffle

In an effort to re-energize the Millionaire Raffle game, the Lottery added early bird bonus drawings this past fiscal year by increasing the prize payout from about 51 percent to 59 percent. As anticipated, Lottery sold out Millionaire Raffle #25, the January 2017 New Year’s Raffle. As you can see in the chart below, Millionaire Raffle #26, the July 2017 Raffle, sold more tickets compared to the previous Independence Day Raffle, but fell short of selling out.

While the game is still profitable, the Lottery continues to analyze the Millionaire Raffle game. Lottery has two Millionaire Raffles planned for 2017-18.

Millionaire Raffle accounted for 0.5 percent of total sales in fiscal year 2016-17.

Raffle	Fiscal Year	Theme	Added	Sell Rate
Raffles #1 through #19		New Year’s / Independence		100.0%
Raffle #20	2014-15	Independence Day		92.4%
Raffle #21	2015-16	Halloween		71.4%
Raffle #22	2015-16	New Year’s		94.9%
Raffle #23	2015-16	St. Patrick’s Day		61.9%
Raffle #24	2015-16	Independence Day		77.5%
Raffle #25	2016-17	New Year’s	Early Bird Drawings	100.0%
Raffle #26	2016-17	Independence Day	Early Bird Drawings	80.8%

### Fast Play

The Pennsylvania Lottery launched in February 2017 a new category of games called Fast Play, which are instant style games sold through the Lottery’s terminals along with all the other draw game products.

Although purchased through a lottery terminal, the payouts on Fast Play games are similar to Scratch-Offs thus have a lower profit margin compared to most draw games.

Sales of Fast Play games totaled over \$55 million in fiscal year 2016-17, reflecting the immediate and rising popularity of this new product category. In fiscal year 2017-18, the Lottery intends to launch a greater number and variety of Fast Play games. Additional price points are likely as well. For fiscal year 2017-18, the Lottery has budgeted \$100 million in Fast Play sales.

Fast Play accounted for 1.4 percent of total sales in fiscal year 2016-17.

## **FISCAL YEAR 2017-18 AND BEYOND**

The Lottery projects relatively flat growth in sales and profit in 2017-18. Sales are projected to increase by

\$59 million, or 1.48 percent, to \$4.06 billion. Profits are projected to increase by \$17.5 million, or 1.67 percent, to \$1.06 billion, with a return rate of 26.18 percent. (Note: These projections include iLottery, which is currently pending legislative approval.)

To meet its commitment in fiscal year 2017-18 and beyond, the Pennsylvania Lottery has set the following growth strategies:

- Continuing to aggressively manage its product portfolio. This includes:
  - Changing Match 6 Lotto from a twice weekly drawn game to a daily drawn game beginning in August 2017. Lottery is projecting 10 percent growth in Match 6 sales.
  - Mega Millions is changing its matrix and price point beginning on October 2017. Lottery is projecting 25 percent growth in Mega Millions sales.
  - Developing the Fast Play category of games by launching games monthly, expanding progressive top prizes to all price points, exploring play themes and second-chance drawings.
- Continuing to engage the Lottery player base. This includes:
  - Adding play value to products and increasing player engagement through second-chance drawings, promotions and interactive elements.
- Expanding points of distribution. This includes:
  - Launching iLottery – a new breed of interactive lottery games that are purchased and played on web-connected devices. (Note: iLottery is currently pending legislative approval.)
  - Recruiting quality retailers. For example, partnering with a national chain that has the potential to add over 100 new high-foot-traffic locations.
  - Piloting innovative programs such as Play at the Pump, cashless payments (i.e. debit cards), gift cards and in-lane grocery store sales.
- Continuing to optimize presence at retail. This includes:
  - Expanding the Lottery's sales makeover initiative designed to generate incremental sales at existing retail locations by increasing game displays, branding and promotional elements.
- Finally, measuring product performance and marketing effectiveness to optimize Lottery sales and profits, and identify new opportunities for growth.