Maryland Lottery and Gaming Control Agency
Larry Hogan, Governor • Gordon Medenica, Director

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State Lottery and Gaming Control Agency
Fiscal Year 2022 Operating Budget
Response to Department of Legislative Services Budget Analysis

House Appropriations Committee
Transportation and The Environment Subcommittee
Delegate Marc Korman, Chair
February 15, 2021 - 1:30 p.m.

Senate Budget and Taxation Committee
Public Safety, Transportation, and Environment Subcommittee
Senator Cory V. McCray, Chair
February 15, 2021 - 1:30 p.m.

Testimony of Director Gordon Medenica

Good afternoon, Chairs Korman and McCray and members of the House and Senate subcommittees. I appreciate the opportunity to appear before you today to present the Maryland Lottery and Gaming Control Agency's ("Agency" or "Lottery") FY 2022 budget. I would like to thank the Department of Legislative Services ("DLS") and, in particular, Emily Haskel for her excellent work and analysis of this budget. I would also like to thank Jesse Rao of the Department of Budget and Management for his assistance in developing the Agency's FY 2022 budget.

Operating Budget Recommended Action

1. Reduce funding for lottery advertising to a level more in line with historical spending. Total special fund reductions of $3,000,000.

Agency Response:

Although the Agency appreciates DLS' thorough review of the FY 2022 proposed budget, the Agency respectfully disagrees with the recommendation to cut the lottery advertising budget by $3 million, or approximately 14%. Such a drastic reduction would bring the Agency below the advertising budget number from as far back as 2010, and much less than industry standards. Advertising spending drives sales and profits, with several studies showing that each dollar of advertising generates $3 to $5 in profit. Cutting advertising by $3 million could result in the Lottery delivering $15 million less profit (revenue) to the State. It is a perfect example of penny-wise, pound-foolish, by simply looking at the cost of advertising and not the resulting profit impact. The Lottery is a $2.4 billion consumer business that will produce over $600 million in revenue to the State in FY '21. Across the US lottery industry, advertising expenditures average about 1.2% of sales; with this proposed reduction, the Lottery ad/sales ratio would fall to 0.77%, or roughly 40% below industry average. *See* Attachment A for an excerpt of the Agency's FY '20 budget presentation.

The Agency is quite aware of the very unusual period we are in during this pandemic. Lottery sales are booming, not because of less advertising, but because consumers have no alternatives for the discretionary entertainment spending. There are no movies, no concerts, no sporting events, no travel, no vacations and limited bars and restaurants, which has allowed lotteries to do relatively well. When the environment comes back closer to normal (i.e., FY '22), the Lottery will need to advertise to maintain its sales levels at the high level of recent years. It would be the absolute wrong time to cut ad spending. The Agency respectfully requests to retain its lottery advertising budget as proposed.

The Agency is grateful for the Maryland General Assembly's continued support of the Agency's lottery and gaming operations, as well as its mission of generating revenue for the State and its residents. The Agency also is grateful for the opportunity to respond to the budget analysis and is happy to address any additional questions the subcommittees may have.

Attachment A

Excerpt from FY 2020 Budget Presentation E75D0001

SLGCA should comment on the rapid increase in lottery advertising spending and the assumptions used to generate the projected fiscal year 2020 revenue increase.

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The Maryland Lottery has been chronically underfunded in its marketing and advertising budget for several years. Ten years ago, the marketing budget was roughly $20 million, but was cut about 40% to $12 million in subsequent years. The result was that lottery sales actually declined in 2013 and 2014. Beginning in 2015, the marketing budget began to be gradually restored each year, generating record sales in years 2016, 2017 and 2018. The 2020 recommendation is for a total marketing budget of $21 million, finally getting back to the level of ten years ago. The marketing spend in recent years has been focused on our instant game category, which is a strategic priority for the Maryland Lottery based on performance comparisons with other high-performing US lotteries. In the lottery industry, instant ticket sales represent about 50% to 60% of sales; in Maryland, we were only at 30% four years ago. But we have increased instant ticket sales by double-digit percentages four years in a row, with the category now generating 37% of sales.

For several years, we have strongly advocated increased marketing spending, referencing excellent research done in other states that demonstrated the positive incremental Return-on-Investment (ROI) of increased advertising and marketing. Advertising spending is usually expressed as a percentage of sales, a metric known as the ad/sales ratio. In the lottery industry, the average ad/sales ratio across all U.S. lotteries is 1.2%. In Maryland, it was only 0.7%.

For example, the New York Lottery engaged an econometrics-based brand research agency to study the relationship between advertising, sales and profits. The findings actually showed that an incremental dollar of advertising generated $3 to $5 of incremental profit. (As an aside, the New York Lottery is the largest and most profitable in the country, with a total marketing budget of $92 million.) The research findings showed that advertising spending had a strongly positive ROI even at levels of ad/sales ratios up to 3%. The Texas Lottery conducted a similar study and the results were even higher ($1 ad spend = $7 profit).

With our strong track record of driving sales growth with higher advertising spending, we believe there is more opportunity to generate even higher sales, particularly in instant tickets, with increased advertising. The Agency is committed to producing $12 million in higher profits from the $3 million increase in advertising spend.