

Online Gambling: All In?

How the Opening of the Online Gambling Market Across Europe Can Benefit Media and Telecom Companies



The online gambling market is progressively opening throughout Europe, with annual revenue forecast to reach €8 billion within three years. Many telecom operators and media companies looking for new revenue opportunities have a card to play, thanks to their privileged access to customers. However, these players need to carefully elaborate an entry strategy leveraging their core capabilities and protecting their brand image.

The cowboy days of online gambling, which saw some spectacular arrests of key executives and fraud scandals, are now over. Following the example of UK and Italy, and under the pressure of the European Commission, most countries in Europe are preparing the controlled opening of the online gambling market. Formerly reluctant governments now recognize the necessity of regulating a service, which has already been used by many of their citizens; consumers are already in great numbers playing on gambling websites operated under the jurisdiction of more liberal countries and independent territories. Additionally, these foreign websites earn revenue on which governments fail to capture any tax income, and also gain local market share against State monopolies, negatively impacting tax revenue. For governments, opening the online gambling market has thus become a societal, as well as economic, necessity.

The French and Spanish gambling markets are expected to be opened in 2010 and should boost the total European Gross Gambling Revenue (total bets placed minus customer winnings), which is forecasted to grow at 13% annually to 2012, increasing from the current €5 billion to approximately €8 billion.

In this context, some media and telecom companies, which are looking for both new revenue opportunities in an increasingly saturated market, and ways to differentiate from their competitors, are assessing the online gambling opportunity, balancing risks and opportunities.

Arthur D. Little has worked side-by-side™ with leading European media & telecom companies to design their entry strategies. Our experience shows that success is dependent on three main parameters: the mix of games and platforms, value chain positioning and the mastering of three key operational levers.

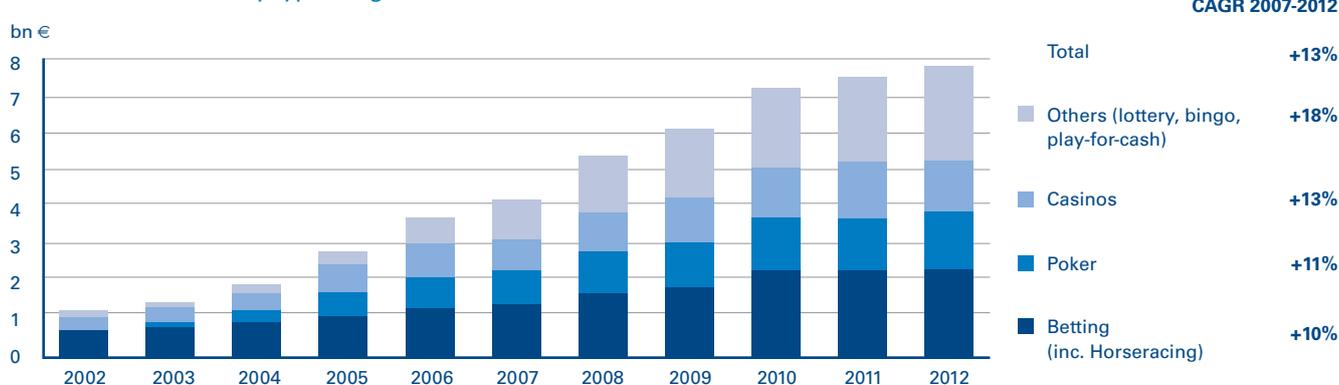
1. Getting in the games

The online gambling market is composed of several types of games, each one bearing its own specific set of advantages and risks in terms of customer targets, business models, potential impact on the brand image and barriers to entry.

1.1 The winning hand of gambling games: three-of-a-kind?

Sport betting began to be offered by specialized online companies in the late 1990s and the market has since enjoyed tremendous growth, leading to the advent of powerful companies like Bwin, the European leader with €408 million in revenue in 2008 (approximately 50% of which was from sport betting). With an expected annual 8% growth rate, revenue from sports betting is expected to reach €2.3 billion in Europe by 2012. While sport betting is a promising segment, developing an offer represents a significant financial risk since the gambling operator has sole responsibility for setting odds, with a direct impact on the company's revenue.

Figure 1. Evolution of the European online gambling market (Gross Gambling Revenue) from 2002 to 2012
Breakdown by types of games



GBGC, Arthur D. Little analysis

Online poker has developed significantly over the past few years, grossing $\text{€}1.1$ billion in Europe in 2008, and is expected to grow at a rate of 8% to reach $\text{€}1.5$ billion in 2012. One of the leading companies on this market is Partygaming, which grossed $\text{€}200$ million in revenue from online poker in 2007. The business model for online poker is based on a commission taken from the wagers (also called the rake) and is far less risky than odds betting. Online poker is also a relatively easy business to setup, if a partnership is made with an existing network. It can be very difficult, however, if the company wants to develop and manage its own network, due to technological barriers and a tough competitive environment

Casino games are based on the same business model as traditional casinos; the company earns a gross margin on amounts bet (a calculated risk due to fixed algorithm). Apart from Gibraltar and the likes, the UK is today the only European country which grants licenses for casino games in a market which grossed approximately $\text{€}1$ billion in 2008 and is expected to grow at a rate of 11% by 2012 to reach $\text{€}1.5$ billion. The key difference between casino games and other types of games is that their audience tends to be made up of a greater percentage of women. Because they are fully based on luck, online casinos are bound to be legally more restricted than other games. Casino games also suffer from a poor reputation, due to past cases of money laundering and tax evasion, making casino games harder to integrate into the offer of media and telecom companies.

1.2 Mobile gambling and iTV: jokers or trump cards for media and telecom companies?

While some forecasts predict spectacular growth in gambling on mobile phones and interactive TV (IPTV or cable), most existing online specialists seem more cautious, and expect the market size to cap at a conservative 10-15% of the total online market by 2015.

Skybet's multichannel integration

Sky's customers can watch sport content on the Skysport channel and bet through the interactive TV feature at the same time. Without a TV, Sky customers can also watch major events live on the Skybet website through the online betting platform on the same account. If customers have neither access to Internet nor interactive TV features, they can still place bets through a dedicated application on their mobile phones.

Sky in the UK operates a sport betting offer under the Skybet brand through Internet, TV and mobile phones, in order to leverage its existing sport channel audience and enrich the overall customer experience. For the fiscal year 2008, Skybet contributed to 1% of BSkyB revenue, or $\text{€}60$ million (approximately $\text{€}6.5$ per DTH subscriber).

However, media & telecom companies could efficiently take the lead on the development of mobile and interactive TV gambling by leveraging their existing activities. Companies having a multi-play offer (mobile, fixed, Internet and TV) could easily bundle a well-integrated gambling offer across platforms. Media companies and telecom operators can also leverage controlled content such as sport news and events. Beyond the direct (but minor) revenue upside, they would be able to enhance their core activities and differentiate against online competitors.

2. Balancing risks & rewards: choosing the best position on the value chain

For telecom and media companies, defining the targeted gambling offer is one issue, but actually launching the service is another crucial one. A primary question is where to position the company on the value chain.

An affiliate transfers its online customers to a partner gambling operator's website, so that the gambling service is neither performed on the affiliate's site nor under its own brand. The affiliate gives the whole responsibility to the partner, and therefore maintains the lowest level of risk, but also reward, on the value chain. This positioning also has the lowest possible impact on the brand and enables the freedom to make multiple partnerships. However, the affiliate has neither control over nor ownership of the customer database and very limited control over the financial transactions.

A retailer distributes a partner's offer on its own website, without the need to own a gambling license itself because it does not actually operate the service. The retailer's revenue depends on its bargaining power and its level of integration with the partner gambling operator. The highest level of integration is a white label partnership, where the gambling service is completely customized under the retailer's brand, even though it remains hosted on the partner's servers. Overall, the retailer position allows for an attractive revenue share, limited technical costs and a reasonable control over the marketing, but it often requires exclusive partnerships on all types of games and provides limited control over fraud and addiction.

The operator owns the gambling license granted by legal authorities within the country of operation. More importantly, the operator also owns the customer database, which is considered a fixed asset and could potentially be resold to a third party. The operator, however, bears the financial risks and the legal responsibilities related to all operations performed on its servers. Owning a license and operating a gambling website remains a bold move in the market in terms of brand exposure and responsibility, and requires thorough industry expertise. This value chain positioning also implies that all potential partners become competitors. A valuable alternative for new entrants lies in joint ventures where a specialized online gambling company brings industry expertise and another company, such as a media or telecom company, brings a large attractive audience.

ITV-Partygaming partnership in the UK

With a gambling service under its own brand, but powered by Partygaming, ITV is a key example of a successful white label partnership. It leverages its audience with an off-the-shelf, but customized, quality product and is able to cross-promote it through dedicated poker shows relayed on its TV channels.

3. Mastering the rules of the game

Preparing to launch the optimal offer and knowing exactly where to position on the value chain is not enough. Three crucial operational issues have to be mastered in order to provide best-in-class services to customers and maximize value creation.

3.1. Brand: Bet on it... but carefully

In a market suffering from a controversial reputation, developing a trusted brand is a critical condition not only to acquire and retain gambling customers, but also to maximize their spending. Putting the generally well-known and trusted brands of telecom and media companies forward can make the difference. But how much can the brand be integrated without doing any damage? In France, ISP Free, an innovative and disruptive challenger, has recently announced a partnership with Chiligaming, an outsider on the market, while Amaury Sport Organisation, the organizer of the famous, 100-year-old Tour de France, has chosen to go with Bwin, the European leader, known for its transparency and credibility. When designing an offer, the branding issue must be addressed for every type of game and platform, and its impact on the customers must be assessed. Also, the choice of the partners must be largely guided by their reputation on the market and the compatibility with the telecom / media brand. Using a sub-brand or a new specific brand are potentially interesting alternatives, but the marketing resources necessary to obtain the same visibility as with the main brand are bound to be significantly higher.

3.2. Customer experience: Don't aim low, go for the best

The European leader in online sport betting, Bwin, has developed an environment enabling first-time users to get started very easily, with clear tutorials, continuous portfolio follow-up, a wide range of odds and an advertising-free, easy-to-use interface. With this approach, Bwin concentrates on its mission of delivering competitive sport betting odds for the masses in an easy and secure environment, and gains true market recognition that not only positively impacts its brand image, but also directly contributes to optimizing its business model. In fact, only a few current market leaders provide their customers with gambling platforms that are consistently and concurrently:

- secure (against fraud, theft, etc.)
- entertaining (including videos, news, etc.)
- user-friendly (simple & clear to use)
- hassle-free (without any disrupting ads, any complex registration process, etc.)

This is, however, extremely important in order to maximize acquisition, retention and revenue-per-user metrics. Telecom and media companies will certainly have to partner with experts to develop such key features.

3.3. Operations: Do not fire and forget

Many telecom and media companies, especially incumbents, have launched music download services, video services or community features in the recent years, but failed to market aggressively enough, nor invest sufficient time and resources to manage these services on a daily basis. The way gambling services will be integrated within the website portfolio of the telecom or media company, and how it will be promoted internally, is essential to its success. It is crucial for telecom operators and media companies to manage Customer Relationship Management (CRM); maximizing retention and revenue per user, and leveraging powerful customer knowledge and relationships is key. Last but not least, the collaborative relationship with partners must be well-managed in order to keep maximum control over operations and the development of the gambling offer.

Conclusion: Place your bets safely!

For media companies and telecom operators, it is now the right time to place their bets on the online gambling market. Many benefits are at hand: they can strengthen their relationship with customers and expand into a very attractive market at the same time; they can be among tomorrow's leaders and expect, at a European level, several hundreds of millions of Euros of additional revenue annually, matching today's best practice players like Bwin or Partygaming.

In the soon-to-be opened markets, like France or Spain, however, numerous players from all horizons will fight to rapidly build their customer base. As in the telecom industry, late-comers will only have the few crumbs left by the leaders.

In this fight, telecom and media companies have strong assets to leverage: a trustful brand, a large customer base, strong investment capabilities, multi-channel distribution, Internet expertise and international reach.

However, as for many opportunities outside their core business, telecom and media companies should be aware that the devil is in the details and that the boundary between success and failure is thin. For them, it is therefore essential to carefully prepare their entry. Even in countries in which online gambling is not yet open, first steps need to be made in order to have a head-start.

A precise analysis of the local competitive and regulatory environment, and of the internal assets that can be leveraged, is key. Only then will these new entrants be able to define an appropriate online gambling offer and the associated position on the value chain for each type of game and platform... and put all the odds on their side to succeed!

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Arthur D. Little

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