

THE MODERN DE BEERS
and
THE SIGNIFICANT CHANGES TO THE DIAMOND PIPELINE OVER THE
PAST DECADE
A literature review

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ABSTRACT

In the past decade De Beers and the diamond pipeline have changed dramatically. De Beers, ‘the guardian of the industry’, once controlled over 90 per cent of the world’s rough diamond supply. In the face of increased competition, plummeting share prices and the financial pressure of holding large buffer stockpiles, De Beers suffered reduced profits and decreased shareholder confidence. In addition their control of the rough market fell to an all time low of 60 per cent.

Not content to let their empire slip away, De Beers have reinvented themselves and introduced a whole new range of strategies and policies to control their company and possibly the diamond industry as a whole.

De Beers are now a privately owned company and have stated that, rather than being supply driven they intend to operate by letting consumers drive demand. They are becoming more involved further down the pipeline and are asking their Sightholders to do the same. Sightholders are being encouraged to drive consumer demand by creating more brands through increases in marketing and advertising. Not to be left behind in the race to create these brands De Beers have created their own *De Beers LV* brand, in conjunction with Louis Vuitton Moet Hennessy.

All these dramatic changes, within a very short time, have upset many in the diamond industry and are raising questions as to De Beers motives for such momentous change. What the end result will be remains to be seen, however, the changes are underway. Those working within the diamond pipeline must now decide if they will embrace these changes or formulate their own model.

INTRODUCTION

Mention the name De Beers and you automatically think diamonds. So why, after decades of being synonymous with diamonds, has this giant of the industry almost completely reinvented itself? The modern De Beers is telling the world that it is giving up it’s role as guardian of the industry and is instead, by its restructuring, giving the power to drive the diamond industry to the end consumer. So is this move as selfless as portrayed, or is it part of the age-old saying “Offence is the best form of defence”.

HISTORY

De Beers

In 1888 De Beers Consolidated Mines Limited was established. This company set about doing what many would have thought impossible. It consolidated the world's diamond industry and set about creating a place for itself in diamond history. De Beers achieved this on a number of fronts including: the mining and distribution of diamonds, the control of supply within the 'pipeline', and the generic marketing of diamonds. Such was the strength, innovation and dominant control of De Beers, in these aspects, that the title of guardian or custodian of the industry has been used by many when describing the organization.

Mining and Distribution

For over 100 years De Beers has been a publicly listed company with its primary shareholder being the Anglo American Corporation of South Africa. It has been heavily involved in the prospecting and mining of diamonds from its own mines in South Africa. In addition, De Beers has built up a large portfolio of mines including mines that it controls in other countries and mines in which it has a joint partnership or share.

The rough from these mines has been sorted and distributed, through its subsidiary, the Central Selling Organisation (CSO), to individuals and companies known as Sightholders. In addition to rough from its own mines, De Beers has purchased rough on the open market, and up to a number of years ago purchased diamonds on a contractual basis from other companies, such as from Argyle between 1983 and 1996¹ and up to the end of 2002 from BHP Billiton⁵².

These mines and purchase agreements ensured De Beers handled approx 90 per cent of the world's rough diamond sales—all of which it distributed through the CSO.

Control of supply

As De Beers handled approximately 90 per cent of the world's rough diamonds, it was always able to control how many diamonds were on the market at any one time. Hence was able to control the price being asked. De Beers, through the CSO, operated a buffer stockpile of diamonds and mopped up any extra diamonds that ever leaked onto the market from channels other than the CSO.

Generic marketing of diamonds

In 1939 De Beers took that great step into marketing its product to the end consumer and set in place the 4 C's. These grading and selling criteria are still used for diamonds to this day. In 1947 De Beers went even further and commissioned a US advertising agency to promote diamonds. Francis Gerety, a copywriter for this agency, coined the phrase *A Diamond is Forever*. Such was the impact of this one phrase that it was voted the slogan of the century in 1999. For decades De Beers has undertaken to do the promotion and marketing of diamonds for the industry as a

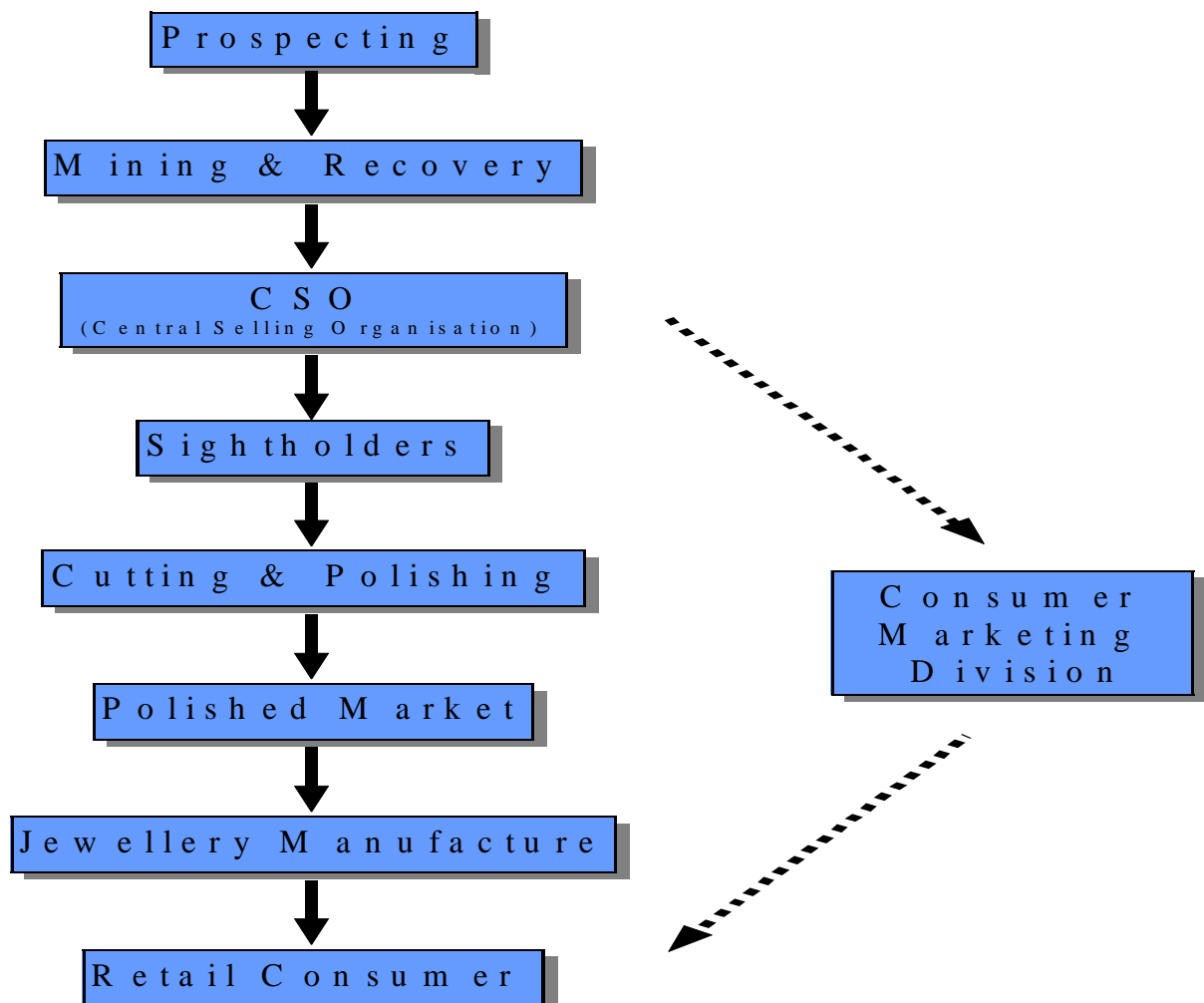
whole. It has had extensive campaigns and promotional offices in many countries around the world. It has produced literature, point of sale material, television & press ad campaigns and huge promotional events.

Such has been De Beers role in advising consumers on diamonds, that it even came up with the figure of how much consumers should spend on buying an engagement ring. (the famous 2 months salary rule).

The Diamond Pipeline

The term *Diamond Pipeline* is used to describe the flow of diamonds from prospecting to the end consumer.

O r i g i n a l D i a m o n d P i p e l i n e



This pipeline has operated in this form for decades, with participants along the way specializing in their particular fields. After each step the diamonds are passed onto the next participant in the next stage. De Beers itself has historically been the one to do generic diamond marketing to the end consumer with the famous 'A diamond is

forever' campaign and their extensive promotion of the 4 C's,. These are just some of their approaches. Despite the advertising campaign run by De Beers, overstocking of the diamond pipeline has occurred from time to time—when supply of diamonds exceeded the demand by the end consumer. Historically though, De Beers has controlled the flow of the diamond pipeline either by reducing the amount of diamonds the CSO would allow for sale, or by imposing production quotas on its mines.

THE TRANSFORMING OF DE BEERS (1998 – 2000)

Sometimes it's hard to pick a defining moment in a company's history, but for De Beers that moment is clear. In 1998 De Beers formally separated its management and operations from Anglo American, a tie they had had for over 60 years. It created, as Nicky Oppenheimer described it:

*“an organization with its own management team and with all the energies and skills of its human resources dedicated to one company and one product”*⁸.

De Beers began that year with a team headed by a new chairman (Nicky Oppenheimer) and a new Managing Director (Gary Ralfe).

Together Oppenheimer and Ralfe looked closely at the De Beers Group. Dramatic changes had been taking place in the world. Changes to the diamond pipeline and De Beers's dominance were happening around them.

In 1992, serious concerns had risen about the glut of diamonds coming onto the market that were outside De Beers CSO, and hence, their control. When a truce was declared in the Angolan war, a large quantity of diamonds were uncontrollably released into the market. This continued intermittently and was compounded by substantial leaks into the market of Russian diamonds. Rather than having world prices for diamonds plummet, De Beers absorbed this huge influx at great cost. Such was the extent of this excess in the CSO's buffer stockpile that De Beers were forced to impose production quotas on its own mines. With the crash in the Asian economies in the late 90's. De Beers again had to cut back on its own sales to ensure there wasn't a flooding of the 'Diamond Pipeline'. At this time earnings plunged by 40 per cent. This resulted in record lows in share prices and shareholder confidence.

Compounding this was the entry into the market of strong competitors. From 1983 to 1996 De Beers had an arrangement with Argyle diamonds to sort and market their rough. These agreements helped provide confidence in the mine and allowed Argyle time to gain expertise in the areas of mining, sorting, valuing and marketing. During this time Argyle conducted extensive industry analysis and created a direct sales office in Antwerp. In 1996. Argyle began marketing their entire production themselves with more than 90% of their rough being exported to the Indian diamond manufacturing industry. Argyle worked closely with these Indian companies to break down barriers into new markets such as the USA. Argyle's historical ending of their ties with De Beers, and their subsequent actions, were deemed risky at the time but they have flourished and developed into a strong competitor for De Beers. In the process they have created a change in the industry and become a role model for others to follow.

Enter then into the market BHP (now BHP Billiton). BHP Billiton are mining the extensive Ekati mine in Canada. BHP, following Argyle's example, entered a supply agreement with De Beers by which De Beers guaranteed to purchase 35 per cent of the mines rough. BHP Billiton proceeded to develop their own sorting, cutting and marketing of rough during this time. Unlike Argyle, who deal predominately in rough (more than 90% of their production going to India alone), BHP Billiton decided it would look further down the pipeline and investigate cutting and selling their material in the polished market rather than in the rough market alone⁵².

Then to top it off—Russia. The potential of the mines in Russia to threaten De Beers control of the world diamond market could not be underestimated. Not only was there considerable new mine production, but over the past three decades they had also built up extensive diamond stockpiles. The break-up of the former Soviet Union, and the following internal government problems in Russia, meant the country was desperate for revenue. There were considerable leakages (or dumpings) of rough diamonds into the market and these were causing problems for De Beers.

Above all, De Beers were beginning to feel a shift in consumer confidence. *Conflict diamonds*, as they were soon known, were receiving extensive negative publicity. In 1999 De Beers ceased the practise of buying on the open market, in order to curb the possibility of dealing in conflict diamonds. De Beers has always maintained that diamonds have an image, which is important to be upheld, and in order to maintain consumer confidence; they took on the costly decision to only carry diamonds whose origin of which they were certain.

It was at this time, after the turmoil of the late nineties, with costly decisions coming into effect and with buffer stocks at an all time high, that De Beers, headed by its new team, stopped, and looked at itself and its future.

In 1999, De Beers launched a strategic review, which focused on creating and enhancing stockholder value. This strategic review resulted in a fundamental shift in thinking. De Beers decided that it was no longer sustainable to play the 'custodial' role to hold large buffer stocks and to undertake expensive advertising on behalf of the industry as a whole. It decided that it was time for things to change.

The Strategic Plan

In 2000, De Beers launched its strategic plan outlining its four key action areas:

1. As is, plus improving operational efficiency and effectiveness
2. Supplier of Choice
3. Growing diamond demand
4. Realising the potential of the De Beers brand

As is, Plus

The De Beers group realised that in order to remain profitable with increased competition, and with world wide economic changes and events, it must look at improving its overall operational efficiency and effectiveness. This was an essential part of the necessary path if De Beers wished to meet its strategic goals and bring about its own transformation. It has started to do this on a number of fronts.

Firstly, mine productivity was considered. This involved looking at a number of key performance indicators. These included the number of diamonds recovered, the tons treated per man-hour, and the working costs per ton treated. Thanks to their innovative use of technology in all steps (e.g. mining, processing, sorting) and their new performance culture, De Beers have found productivity is improving. De Beers emphasis on increased productivity has also meant they have redefined their accountability and performance requirements for all their staff, from boardroom to mine shaft. De Beers are making people more responsible for what they do and are rewarding them for doing it.

In 2000, De Beers introduced performance scorecards for the management team. These focus on explicit targets and value creation. They have also tied a significant proportion of the management's remuneration to reaching target reward levels, so creating a performance driven team⁴.

De Beers have also looked at their lost-time-injury frequency rate and are seeking to continually improve this. In addition, as De Beers primary mining interests are in Africa, they have realised that the increase in the effects of HIV/AIDS on their workers cannot be overlooked and is one of their serious challenges. They have urgently been working on defining a comprehensive corporate policy to show their commitment to the welfare of their employees and their partners.

The Diamond Trading Company, the rough diamond marketing arm of De Beers, sorts and values about two thirds of the worlds annual supply of diamonds, by value. It has introduced an Integrated Stock Management System in order to monitor the flow of diamonds through the purchasing, sorting and valuing processes. This will reduce the time it takes to deliver them to their clients thereby increasing efficiencies.

Supplier of Choice

De Beers has decided that rather than being the buyer of last resort; they will become the *Supplier of Choice*. Of all the strategic changes bought about by the action plan, this is the most significant.



"To be the 'Supplier of Choice' in a world of great opportunity, De Beers will provide the best value-added service to clients and, through them, their downstream partners. We believe that this strategy will make our DTC marketing arm the first choice for rough diamonds," said the Chairman of De Beers, Mr Nicky Oppenheimer^{12, 16}

Essentially what De Beers is saying is that, if you are a diamond dealer, with the opportunity to source diamonds from any number of producers, they are going to offer

you a package of value added services which will make you want to deal with them and not other suppliers. De Beers wants people to want to be sightholders.

Apart from the obvious benefit of having access to more than 60 per cent of the world's rough, the four main cornerstones of the Supplier of Choice Strategy are the powerful new identity of the Diamond Trading Company, a package of value-added services, the establishment of the Best Practices Principles and the introduction of a policy statement ²⁵.

1. The Diamond Trading Company (DTC)

As part of SOC the Central Selling Organization (CSO) was renamed and combined with De Beers Consumer Marketing Division to form the DTC. This brings together more than 70 years of sales experience with over 40 years of marketing and promotion skills.

The DTC is responsible for obtaining rough from the De Beers Group mines, and those of its producer partners. Incorporating the universally recognized slogan 'A Diamond is Forever' this new identity will have the forever mark as its logo. This DTC identity will be supported by an international marketing campaign by De Beers, valued at approximately US\$180 million^{9, 41}, which will help drive the demand for all diamonds.



“It will also reinforce DTC sightholders as the leading diamantaires of the world operating with globally recognised distribution channels for diamond in which consumers can be confident”.¹⁶

2. Value Added Support Services

The DTC will provide an extensive package of extra support services for its clients. These will include marketing, training, business planning and market research. They will also continue to have the benefit of De Beers research and development division and the powerful use of the Forevermark logo and the phrase 'A Diamond is Forever..

3. Best Practice Principles

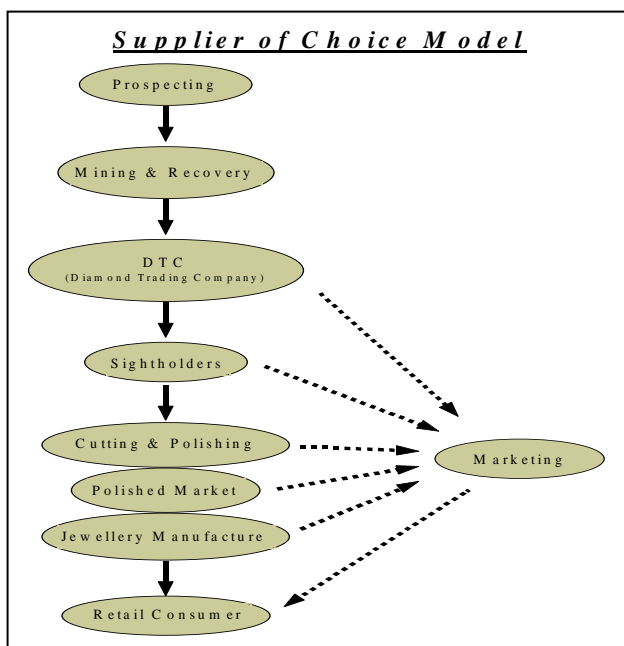
De Beers are committed to maintaining the identity of diamonds in consumer's eyes. The establishment of a code of professional and ethical standards will ensure continued consumer confidence in the allure of natural untreated diamonds through the industry's commitment to the highest standards.

The DTC knows consumers expect to purchase diamonds in their natural state and hence wants to ensure clear disclosure of treatments, simulants and synthetic diamonds. The DTC also wants to reassure all customers, both their sightholders and the end consumers, that the diamonds they are purchasing have not been sourced from conflict areas, are neither responsible for the exploitation of children nor endangering the health and welfare of any individuals²².

4. Policy Statement

A policy statement was introduced for sightholders outlining objective operating criteria, with emphasis on efficient distribution and marketing abilities. Essentially DTC selection of sightholders and supply decisions will be based on six key criteria, these being: financial standing, market position, distribution abilities, marketing strengths, technical and manufacturing ability and compliance with the Best Practice Principles and other standards¹³. The DTC also introduced a new sales planning system which will help in refining the supply of the right diamonds to the sightholder best able to market and distribute them.

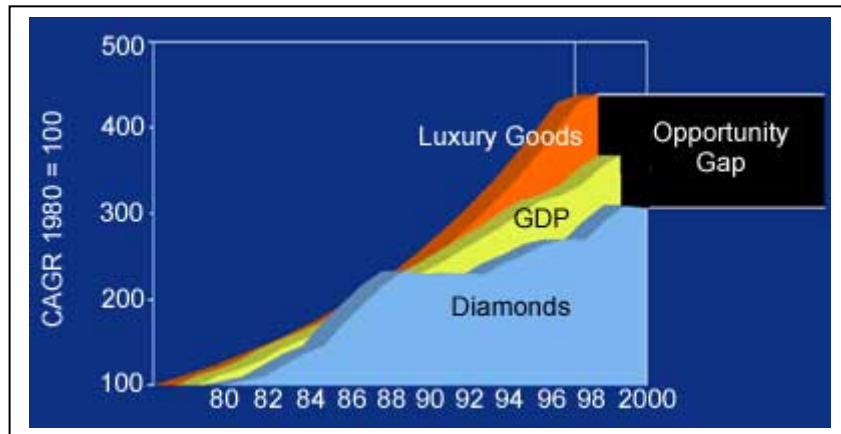
De Beers, through the Diamond Trading Company, is offering this major suite of sales and marketing strategies with the goal of growing both their business and that of their sightholders. They are offering a package, which is virtually irresistible to potential clients. Such is the appeal of the package that dealers throughout the world have been clamouring to become part of 'the movement'.



'Supplier of Choice' is a multifaceted approach to the rough diamond industry unlike anything the industry has experienced before from De Beers. This strategy has been designed to equip De Beers' clients to drive consumer demand. De Beers is hoping that by working with their clients they will create a competitive, customer focussed diamond industry. This is a major change of direction for De Beers who previously worked on controlling the industry from the supply end.

Growing diamond demand

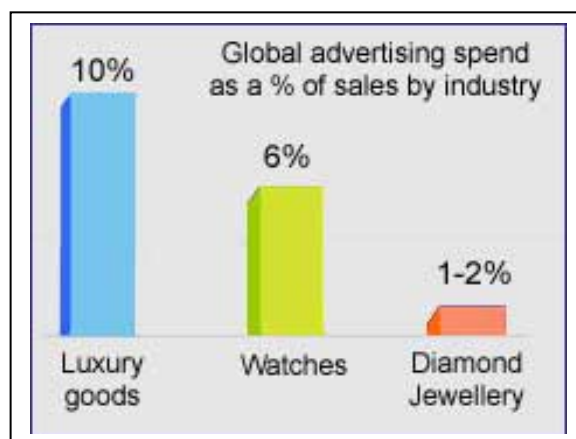
Supplier of Choice and other strategic plans of De Beers aim to grow global diamond sales by stimulating growth in the demand for diamond jewellery. They have been designed to invigorate and awaken the marketing and entrepreneurial skills of those in the industry. Parts of the strategic plan works on the premise that diamonds are part of a larger sector, that of luxury goods. It also surmises that during the 1990's diamond underperformed in relation to its other luxury goods counterpart's¹³.



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It has also shown that the industry needs to stimulate demand by bringing marketing and advertising investment to a level that diamond jewellery deserves, something on a par with the rest of the luxury goods sector. The DTC is working closely with sightholders to generate an incremental \$200million in trade advertising by 2004.⁴¹ This is in addition to De Beers \$180 million on generic advertising.



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Branding

Hand in hand with increases in marketing and advertising investment goes the need to create internationally recognizable brands. Branding is extremely important in any industry because multiple competing brands create excitement and bring new consumers to the market. Part of the SOC package requires sightholders to actively market diamonds and work with their downstream partners to create brands. At present there are a few famous names in the Diamond industry such as Tiffany and

Cartier but De Beers is hoping that emergence of other brands will drive consumer demand.

While the industry as a whole agrees with this philosophy De Beers has created controversy by indicating that they intend to be one of the competing brands. De Beers has joined with LVMH (Louis Vuitton Moët Hennessy) to create De BeersLV.

“While our core business will remain the mining and marketing of rough diamonds, in five years time we envisage an industry in which there are multiple and competitive brands. As we have learned from other industries, competing brands stimulate global demand. In due course, we hope that the De Beers brand will be one of those,” said Mr Ralf¹⁶

THE MODERN DE BEERS

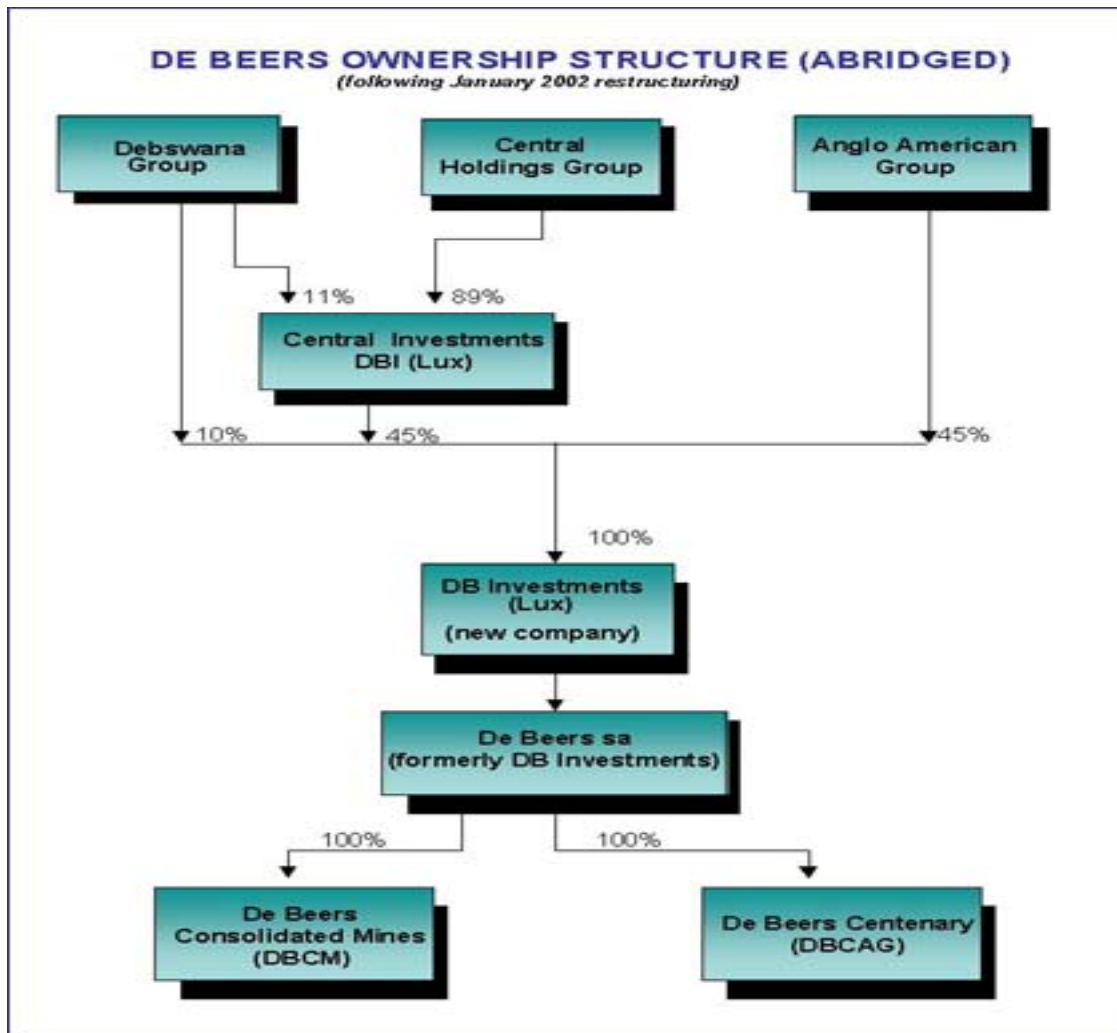
De Beers has been dishing out its share of shocks to the diamond industry over the past six years. In 2001, it hit the industry with another. After 113 years, the world's leader in diamonds became a privately owned company. It was a momentous move.

As Nicky Oppenheimer said,

“There were – beyond all financial considerations – two powerful and dominant motives. One was the conviction that De Beers should be liberated from the inherent short-termism of the stock market, thus enabling it to take the long view and tailor its decisions more closely to the needs of the diamond industry. Another was the need to reinforce and enhance De Beers’ great singular strength that sets it apart from other mining groups- its total and exclusive dedication to one product. This extraordinary focus has been, I believe, the reason for its expertise and leadership in all aspects of diamond mining, research and marketing. This single minded, almost obsessive, dedication is mirrored by those, like myself, whose fate and fortune is now inextricably bound to the De Beers Group of companies and to the product we mine and sell”.⁴¹

The De Beers structure

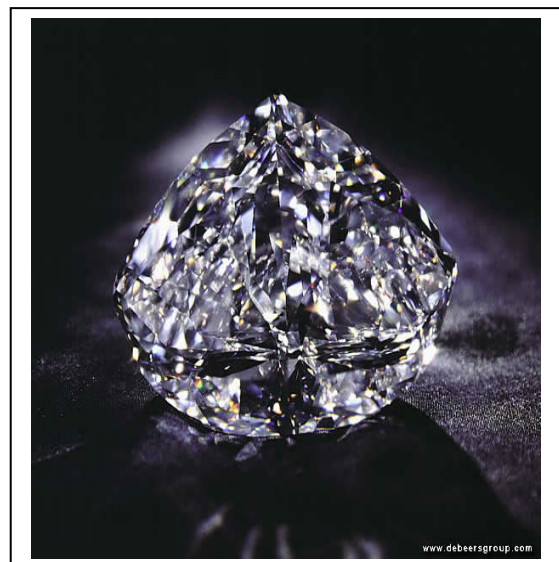
De Beers is now owned by a consortium known as DB Investments (DBI) consisting of: Anglo American Corporation (45%), Debswana, a company jointly owned by the Government of the Republic of Botswana and De Beers (10%) and Central Holdings Ltd, an Oppenheimer family company (45%)^{6,8}. Nicky Oppenheimer continues as the Chairman and Gary Ralfe as the Managing Director. DBI is then broken down into two separate groups: De Beers Consolidated Mines Limited, which comprises of all the South African interests of De Beers, and De Beers Centenary AG which comprises of all the non-South African elements of De Beers and also deals with purchases from other producers.



From De Beers Group Website

Since going private De Beers has weathered some unsettling moments in world events, which could have undermined consumer confidence, such as the War in the Middle East, SARS and the dramatic events of 9/11. They believe however that there has been a swing back to traditional values and recognition of the role diamonds play in life and love. De Beers and the world diamond market were buoyed by increased jewellery sales in the US that occurred during the 2001 Christmas period.

“In a materialistic world, gem diamonds are, after all, of no practical use. They are not used in the making of things or the breaking of things; they don’t make cars go faster or planes fly higher. They are not used in the production of anything – except happiness. And therein lies their secret: they don’t feed our bodies, but they do feed something in our soul. And, because of this, we have come to understand that, while they may not be necessary to our physical survival, they are essential to our emotional well being. A thing of beauty in its own right, the perfect marriage of the art of man and the art of nature, the diamond is also an enduring symbol of all that is best in us and our aspirations: purity, love and commitment”. Said Nicky Oppenheimer.⁴¹



Since that time De Beers has experienced exceptionally strong operating cash flow and as a result have made voluntary loan prepayments to the banks reducing their loan, from their buyout of minority shareholders, from \$3.55billion down to \$2.485 billion. This payment covers those due in March 2003 and 2004.^{6,17,48}

De Beers have also dramatically reduced their excess buffer diamond stockpile by over US\$600million, which has resulted in increased operation cash flow¹⁷. This is helping them work towards their goal of reducing the diamond stockpile, down to the point where they carry only required working stock levels.

De Beers LV

De Beers LV brings together the unique combination of De Beers, the world's leading mining, marketing and diamond company, with Louis Vuitton, the world's leading luxury goods company. De Beers LV has been formed by De Beers as part of its strategic plan to build on the significant untapped potential of the De Beers name. De Beers first began building a relationship with consumers back in 1939 when it initiated the '4 C's' and focussed marketing in the US on diamond engagement rings (diamond engagement rings are now purchased by approx 74 per cent of couples in the US)³. It continued to build on this in 1947 with the term 'A Diamond is Forever'. In 1953 De Beers launched the 1st Diamond International Awards, which ran until the Year 2000, promoting diamonds and diamond jewellery throughout the world. In recent times they have had the campaigns 'How can you make two months salary last forever?' and 'The Diamond Engagement Ring'.

Together all these campaigns successfully worked to develop the 'diamond dream' and to make De Beers synonymous with diamonds. De Beers strong relationship with consumers, is a result of De Beers' marketing and history and their role as mentor to consumers in their choice of diamonds. This relationship and brand awareness is what De Beers LV plans to capitalize on. (With the added benefit that LVMH itself already has an existing network of exclusive boutiques and in itself a strong customer following).

De Beers LV is independently owned, managed and operated by a newly formed company, Rapids World Limited ("Rapids World"). This company is jointly owned by Riverbank Investments Limited (controlled by the De Beers Group), and Sofidiv UK Limited, (controlled by LVMH Moet Hennessy Louis Vuitton)³. Together they will have joint control of the new Rapids World Company.

The first retail store opened on the corner of Old Bond Street and Piccadilly in London, with other stores planned for strategic locations around the world. Many people are saying it will set the benchmark for 21st century shopping. Showcases are set around the store so customers can view the jewellery from all sides—a 360 degree view and the emphasis is being placed on high end, better quality pieces³. In keeping with this image De Beers LV purchased the 'Millennium star' to be the flagship of the new De Beers jewellery collections.



Iman, the face of De Beers, wearing the 'Millennium Star' at the Cannes Film Festival in May 2002

No one doubts that De Beers will certainly be the leader in the diamond market in the not-too-distant future. Concern has been expressed though about the obvious dominance of De Beers in the diamond market and its ability to manipulate its competitors by controlling supply. Because of this concern De Beers have responded publicly on a number of occasions stating that De Beers is only supplying this newly formed company its name, not its diamonds.

It has also stated that De Beers LV will have to go to the marketplace for its diamonds⁴¹. At present too the EC has specified that Rapids World will be expressly forbidden from purchasing polished diamonds from any De Beers owned company³.

Supplier of Choice

The radical new structure, *Supplier of Choice*, that was part of the action plan, is now reality. In May 2003 applicants were advised whether they were successful in becoming *sightholders* under the new system. July of 2003 saw the first sight held under the Supplier of Choice system. New sightholders were supplied with material at this time, as were previous sightholders. The DTC has advised that any existing clients who did not qualify as sightholders under Supplier of Choice will continue to be offered stock throughout 2003 in order for them to meet their current supply commitments and to allow them time to make alternative arrangements for future supply.

In 2004 the DTC published a list of sightholders but until then would not make public comment on the list, in order for unsuccessful sightholders to be able to speak with their clients first.

The DTC has been very specific in pointing out that all applications and selections were performed under a process approved by the European Commission (EC) and that not qualifying for SOC is not a reflection on the company concerned. They have stated that, in most cases, the DTC no longer being able to supply them is due to competition for limited supplies of particular goods. Under EC requirements De Beers have appointed an Ombudsman to investigate any complaints from clients who have been removed as Sightholders. De Beers will continue to supply Diamdel, the wholly owned subsidiary of The Diamond Corporation (Pty) Ltd, who in turn is a wholly owned subsidiary of De Beers. Individuals and companies who are not Sightholders are able to purchase rough from Diamdel.

THE RAMIFICATIONS OF CHANGE AND OTHER POSSIBLE AGENDAS

There has been much speculation as to the effect all these changes, in a short period of time, will have on the diamond industry as a whole. Many are concerned that although De Beers appears to be giving up its 'cartel' image that it is in fact strengthening its hold on the market. Although De Beers rough share has dropped from almost 90 per cent to 60 per cent, it does still hold the market share and the 40 per cent balance it does not control is divided between a number of other companies, none of who are in a position individually to takeover De Beers role. De Beers now also has greater access to information on its sightholders and through them the market place. In order to become a sightholder these companies had to agree to provide De Beers with very personal and detailed information about themselves and their client bases.

Is it possible that these sightholders received their status because they fit into De Beers's master plan to dramatically shorten the diamond pipeline and to increase profits for De Beers at the expense of those further downstream? It is well known that greater profits occur as you go down the pipeline. Could it be that this is De Beers's ultimate goal?

Also of concern are the free market (non DTC rough market) and the unregulated application of Supplier of Choice. The main concern being the continued existence of Diamdel, a De Beers company, which is in fact a sightholder. Many are concerned that Diamdel can purchase from De Beers sights and also from the open market at the same time. People, like Martin Rapaport, believe that in order for SOC to work that:

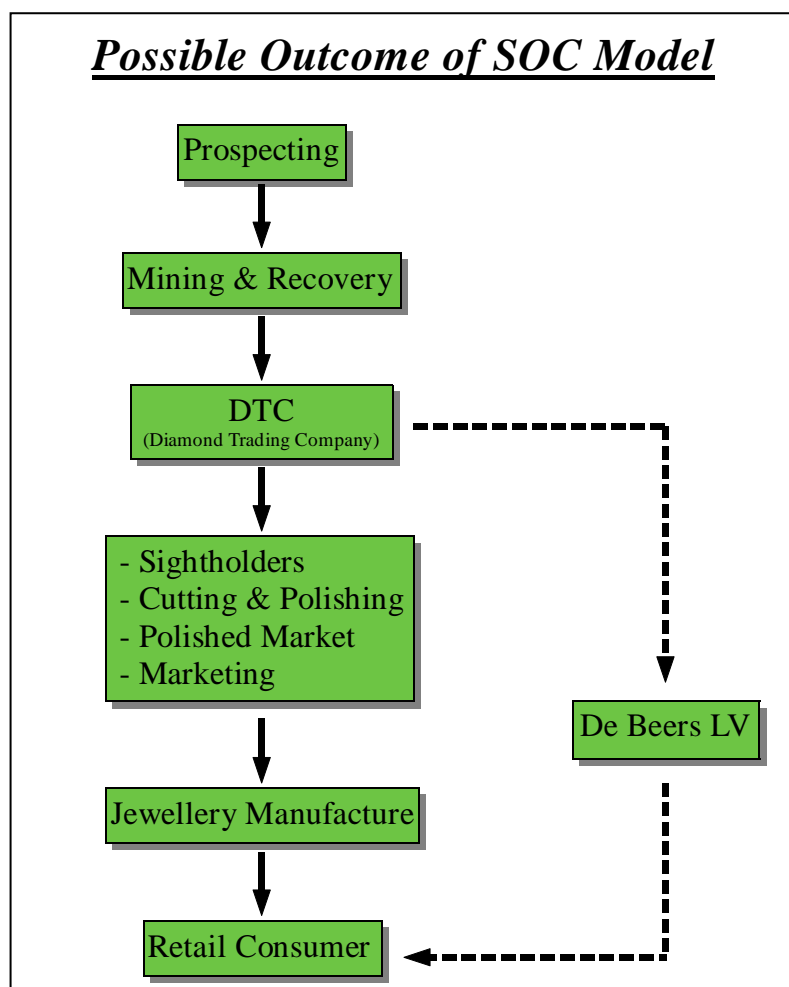
“the DTC should be able to do whatever they want with their rough – even if it is 50 to 60 percent of available world supply. On the other hand, it should keep its hand off rough that is not its own. Outside rough should belong to the free market and should be left alone by the DTC and their agents to ensure that nonsightholders have enough rough to stay in business and compete with SOC clients”⁴⁶.

Although the EC investigated SOC it really only did so by looking at the effect SOC has on sightholders, not on the market as a whole. Therefore regulatory controls were not specified relating to competing in or with the free market.

Another major concern is the absence of large rough on the market. With Diamdel being able to buy 5 ct and larger rough on the open market it is possible that the DTC could corner the market with rough of this size, while its clients corner the market of larger better quality polished goods. What non-sightholders and the free market are concerned about is how a non-sightholder is able to get large rough. Martin Rapaport also asked:

“Will retailers who want to buy large polished be forced to buy only from sightholders? What happens when a sightholder tells a retailer calling him that he will sell him the larger polished only if he also buys the smaller carat sizes from him? What happens to the retailers who buy from nonsightholders? What happens to their supplier? What happens to the free market?”⁴⁶

Rumours circulating at present indicate that many of the past sightholders who were dropped by De Beers and the DTC are those who deal in the larger size rough. Thus fuelling theories that the DTC intends to take this end of the market for De Beers.



Although the EC expressly forbade De Beers from selling directly to its new retail company De Beers LV, there is nothing stopping De Beers sightholders from doing so. As De Beers know who the sightholders supply and the DTC determines who gets what rough, it is not difficult to surmise that De Beers could supply larger better quality rough to sightholders who in turn could supply it to De Beers LV.³ Of course there is also nothing to stop the EC removing this restriction altogether down the track.

While it is hoped that the increased advertising required by the DTC for companies to remain sightholders benefits the industry it is hoped that these companies have fully investigated the costs involved. They have had many changes in a short period of time and for many of them this is a new aspect to their business and a costly addition.

De Beers itself will vouch for the expense involved in marketing a product successfully. If nothing else it will soon sort these new sightholders out. One would presume however that De Beers took this into account in the selection process. Time will tell though. But it does go with the theory that there will have to be closer affiliations downstream in order to increase profits to fund these extra expenses.

Whether the free market likes what is happening or not the fact remains that in order for them to change anything that is happening they will need to be creative. Taking De Beers on in a price war will benefit none of the industry and let's face it; De Beers are situated to survive a price war better than anyone else.³

WHERE THE INDUSTRY AND PIPELINE STAND AT PRESENT

The industry at present seems to be in a 'sit back and see what happens' phase. There is a lot of talk but at present very little actual action. The WFDB President Shmuel Schnitzer, in his address to the Sun City, South Africa Meeting, said that:

“the DTC’s Supplier of Choice (SOC) program is undermining the stability of the diamond industry by concentrating rough supplies into a very few hands.”³⁷

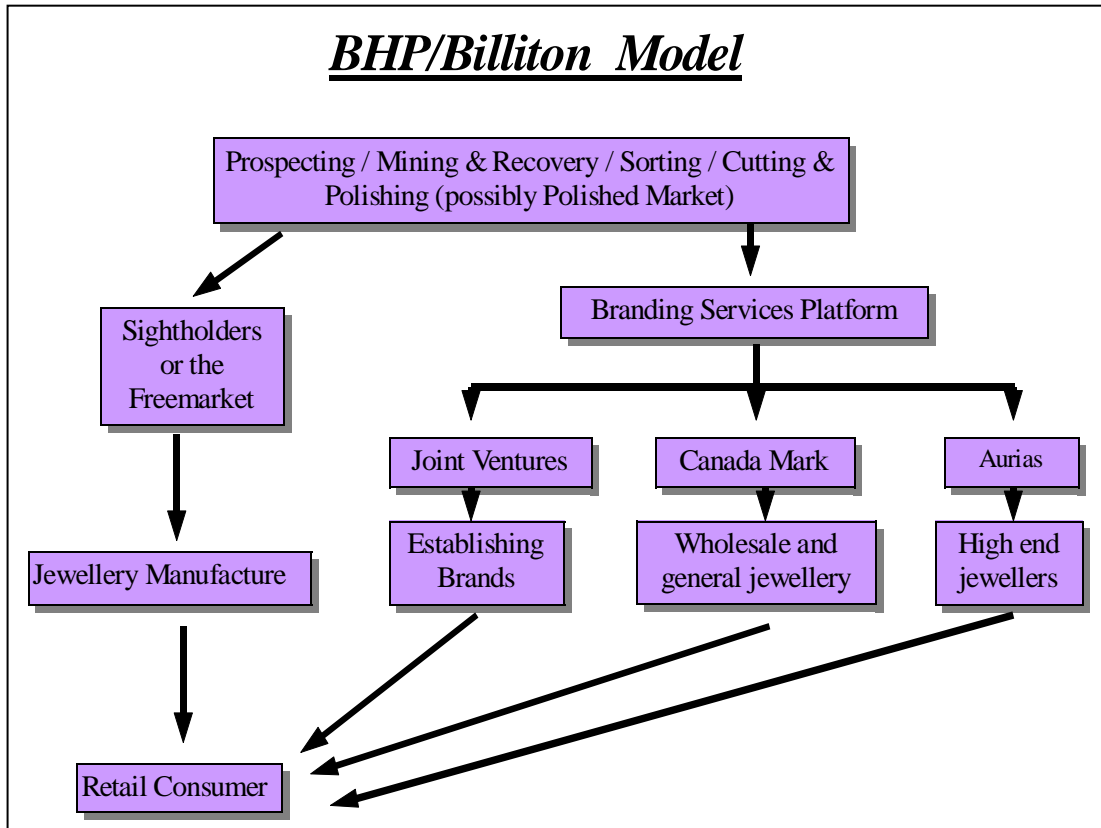
The WFDB issued a resolution that it will “ approach all major diamond producers to discuss their further commitment to the overall health of the international diamond market, and more specifically, the future continued supply of rough diamonds to the open market”³⁷.

Shortage of rough

There is definitely need for concern with genuine shortages in the supply of rough over 2ct. The July sight saw a trimming of this type of material and it looks like this trend will continue. As availability of rough supplies in the pipeline continues to be speculated on the Industry bankers are concerned that rough diamond prices are rising to a point that the polished market can't sustain. At present low interest rates are making debt management possible, but if the market continues to be weak, then low profits could put some companies in difficulty.

De Beers’ competitors

Companies such as BHP Billiton’s *Aurias Diamonds* attempted selling their product directly to the end consumer via their dot.com business. Although this dramatic attempt at shortening the diamond pipeline was not as successful as they had hoped, they have shaken up the traditional ways of thinking about the pipeline. They are waiting to see what effect the De Beers push for increased branding and instigation of their *Forevermark* will have on them. They have established the Branding Services Platform through which they are pressing on with their own product and branding development. As a consequence, they have also recently released the *Canadamark* to increase consumer confidence in their product⁴². However, September 2003 saw BHP Billiton close their Australian office. From the first week of October they will operate the *Aurias* brand from their Vancouver office. For now they are saying they will keep the brand alive but how logistically this will work is still unknown. Apparently low return for capital outlay and return on stock holdings are the rumored causes⁴².



RioTinto has formed a separate division known as Rio Tinto Diamonds to look after all their diamond mines and their rough clients. They will also continue with their successful Argyle Diamonds Polished Sales Division based in Perth (who look after their valuable pink production)³⁶. Their relationship with Indian diamond cutters is thriving and currently 90 per cent of their rough is exported to India. Diamond Manufacture in India is growing and they now account for over 70 per cent by weight and 35 per cent by wholesale value of the worlds polished diamond market, compared to the mere 6 per cent that they manufactured in 1966. As India is able to cut small, low quality near-gems at a very economical rate they have almost cornered this end of the market.

Alrosa and others in the Russian diamond industry are also heading towards a more vertically integrated pipeline with the establishment of the Diamond Court project to increase cooperation between production and major jewellery manufacturers in Russia. Alrosa continues to wait on the outcome of the EC ruling on the De Beers/Alrosa agreement by which Alrosa sells De Beers 50 per cent of its production. Although they won't comment on it directly Alrosa have a contingency vision of how they will continue if the EC ruling is not favourable.

Conflict Diamonds

The Kimberley Process has been passed by the United Nations and they have called on all nations with strategic interests in the diamond industry to join the Process. The Kimberly Process ensures that conflict, or illicit unofficial rough, diamonds will be

excluded from the legitimate distribution channels. It works on Government organization monitoring rough shipments and all those in the diamond pipeline offering a serious of written guarantees as to the origins of their diamonds. This has been a momentous step in preserving consumer confidence and the image of diamonds.

The Diamond Pipeline

The diamond pipeline is definitely shortening, while Argyle and BHP Billiton were the first to take steps on this path, De Beers is now following. De Beers continue to maintain they do not wish to cut out steps in the pipeline but wish instead to increase efficiencies and the speed in which goods pass through the pipeline. They are also working, through SOC to create closer links between those along the pipeline. In a turnaround too, Tiffany's, the famous jewellery chain, has taken it's supply of diamonds into it's own hands. In one of the most dramatic shortenings of the diamond pipeline it has established a relationship with a mining company, ensuring it gets a set percentage of the rough produced.

De Beers itself

The De Beers group is continuing to go from strength to strength with new mines due to open in Canada soon and existing mines continuing to improve in efficiency. De Beers has wholeheartedly embraced their new Choice program and are committed to becoming the Miner of Choice, Supplier of Choice and Employer of Choice. They are broadening their ties with other companies and have set about creating partnerships with companies in South Africa to undertake smaller scale projects. De Beers are continuing their restructuring in all divisions of the group, having just completed the restructuring of Element 6 (their synthetic diamond arm).

De Beers LV

De Beers LV's flagship store in London has opened. In addition three more stores have just opened in Tokyo, with other stores scheduled to follow around the world. Whether the DTC starts supplying the larger rough in such a way that it only ends up in the De Beers LV stores remains to be seen.

De Beers advertising

De Beers is continuing with its advertising but now it is aiming this at the Forever Mark and promotion of its DTC sightholders. Those riding on the coat tails of its generic promotions will now find they have to go it alone.

CONCLUSION

Whether you love them or hate them you have to sit back and admire the De Beers Group of Companies. Faced, back in the late 90's, with what could have been one of the lowest potentially financially fatal points in their history, they took their company,

reinvented it and forced it and the rest of the diamond industry into one of the most tumultuous series of changes imaginable. At the end of it all it looks like De Beers, who were at one point drowning themselves in diamond stockpiles, struggling with the onslaught of new competitors and facing consumer backlash has come out on top.

Now the rest of the industry is trying to catch its breath and work out where they fit in. De Beers has cleverly removed itself as guardian of the industry and set itself up as the driving force of the industry. No longer does it have to protect the industry as a whole but instead is saying to the industry protect yourselves. Whether De Beers is giving up its role of controlling the industry by supply still remains to be seen but it is certainly saying to the industry the consumer is the end target. Compete for them if you want to compete. Nicky Oppenheimer said:

“We are not afraid of competition and neither should anyone in the retail industry be wary of its capacity to invigorate and energise demand for a product that speaks so eloquently to man in its beauty and purity”⁴¹.

De Beers is definitely working on speeding up, (maybe shrinking), the diamond pipeline. What many people are forgetting though is that De Beers didn't start the shrinking of the pipeline. Argyle and Aurias started that processes many years ago, now Tiffany's have jumped on the bandwagon. Is this a surprise? After all Vertical Integration is a known business strategy, one that occurs all the time in other industries. What De Beers appear to be doing is acting like a business that wants to grow.

Could it be that the diamond industry is now reaping what it has sown? For decades everyone has been happy to let De Beers have the expense of industry advertising. They have been happy to let De Beers spend money on research. They have been happy to let De Beers carry stockpiles. Now they want to cry foul when it starts to take the benefit of doing what it has spent hundreds of millions of dollars working on over the years.

How ironic that the industry was happy to use De Beers's advertising campaigns to promote their products and now even smaller retailers are lamenting the possible effect a company with the De Beers name may have on their business. After all every time that retailer handed out a brochure they were in turn promoting De Beers. For years we have been building their brand for them. Is it not a sound business move on De Beers part to now capitalize on their investment in their name?

De Beers has promoted SOC as necessary for the industry to grow and I believe this is correct. Marketing and growing consumer demand is the only way the diamond industry can survive. If De Beers shares had continued to plummet that alone would have done irreparable damage to the diamond industry.

What the industry now needs to do is to work together to ensure that in 50 years time it is not in a position where the action of one company affects all. We need to get into action and create a true diamond industry – a living entity made of many parts that operate together for the good of the whole body.

De Beers are after all one company. A large one certainly, but one company. They are controlled, regulated and overseen by relevant government bodies. Maybe the industry needs to approach these government bodies and lobby to have restrictions put in place to protect the free market and create a playing field in which others can compete.

These are times of incredible change. De Beers took the challenge head on and attacked the problem facing them as a company. There is a lot to be learned from their strategy and willingness to change. We should all take this onboard. Just because something has always worked one way it does not mean it is the best way and it does not mean it can't be changed. If the diamond industry is still at the mercy of De Beers in 50 years then we have no one to blame but ourselves.

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