DIAMONDS BREATHING: CATCHING THEIR BREATH IN 2012

By Alan Bronstein

Pictured: The Orange Flame diamond

In 2012, the global diamond industry began a slow exhale of the deep breath it began in 2009. The gods of diamond price lists determined that the value of polished diamonds declined 12.5% from highs of 2011. This includes multiple qualities that are the core categories used for evaluating price movement. This figure does not include fancy color diamonds which have no indications other than the select few that appear at auctions each year. The few colored diamonds featured at auction showed stability for the most part but there was definitely a slowdown in demand in the trade putting some price pressure on the more mainstream fancy colors.

For the market for colorless diamonds, which account for more or less 97% of consumer sales, the 12.5% average price pullback is moderate relative to the last cycle that ended in 2008. The price of rough diamonds at that moment was in such an irrational and unsustainable speculation that the market for rough almost completely shut down to keep it from overheating and bursting. This current slowing of the market in colorless goods can be directly attributable to the inevitable contraction of growth and spending in China, considered by many a potentially inexhaustible marketplace for fine and collectible diamonds.

Many rough diamond traders buy on the belief that the demand will continue to grow and push up the value of the rough. Although these individuals have to put up the cash for this rough price speculation, it is no different than betting on futures of gold or oil. Speculation among diamond dealers themselves, to possess rough stones, is more potent in creating wide value swings than consumer demand provides. While the miners want maximum value for their goods, they are not happy when speculators drive the market.

While 2012 may not have been the best year for diamond value growth; it went through major upheavals at the mining and distribution level that will effect the way the business is conducted moving forward. First and foremost, the Oppenheimer family, creators of our “diamond desire”, sold their 100-year stake in De Beers for a comforting $5.1 billion. The giant mining group Anglo American purchased the share, consolidating what they did not already own in partnership with their largest diamond partner, the country of Botswana. With this transaction in the works, De Beers diamond distribution base was relocated from London to Gaborone, Botswana. Of all diamond producing countries, Botswana sits on the mother-load of all diamond mines that are still in production today. The transfer from selling diamonds in London will consolidate and centralize the DeBeers distribution and branding initiative called “The Forevermark”.

BHP-Billiton, the largest mining company in the world, decided to exit the diamond industry by selling its share of the Ekati mine in Canada to Harry Winston Corp. for $500 million. Harry Winston decided to separate its mining and retail operation so it could sell its retail stores for $1 billion to Swatch Corp. The mining firm sold the name and changed the mining company’s name to Dominion. Dominion is now supposedly in negotiation to buy the mining rights of Rio Tinto, which also announced it wished to exit the diamond mining industry. Rio Tinto has done a good job branding their rare pink diamonds from Australia over the last 25 years, which has been a powerful component of the surge in awareness of colored diamonds. But it is a minor industry in their portfolio and they want to focus on core commodities.

This reshuffling of the mining sector, adds strength to the industry and to the confidence that stronger companies will keep prices firm as the market ebbs and flows with demand. The last 2 diamond cycles have seen the mines step in to slow supply to the market by either stockpiling the rough (as Russia does) or leaving the stones in the ground until demand picks up. Luckily the slowdowns have been relatively short, and Chinese economic development has certainly helped push values higher over the last 10 years. However all major diamond resources have shown a decrease in profits for 2012 and have lowered estimates and growth for 2013. They do not expect to lower the prices on rough but to reduce output.

On another note, the second great run at an investment fund for rare diamonds which began in 2008 with great confidence, came to a quiet end in a forced liquidation in 2012. Although the company, Diamond Capital Circle LLC., purchased rare and desirable stones, the funds obligations for its exit strategy required for return to investors could not anticipate the softness in the market at the time it had to liquidate. It turned out to be a fairly large negative return on investment.

This is the second attempt at a diamond investment fund. The last attempt was in 1980 and also failed to anticipate price volatility and liquidity factors.

The present lull in growth in the diamond industry is a healthy cleansing breath for the stability in the short term. There are forces at work still trying to commoditize colorless diamonds and give them a marketplace beyond the jewelry sector. I think this puzzle of consumer cost and liquidity will eventually be solved and diamonds will become another electronically based trade. Branding could play a major role in this marketplace. Colored diamonds of rarity or great value could never be sold in this system because they cannot be sold strictly on quantitative data.

All things considered, diamonds look poised for another run for your money. But you got to be in it for the long haul if you want to maximize at investing and you have to invest to fit your personal requirements and exit strategy.

I say wear your diamonds and enjoy the miracle of nature that they are.