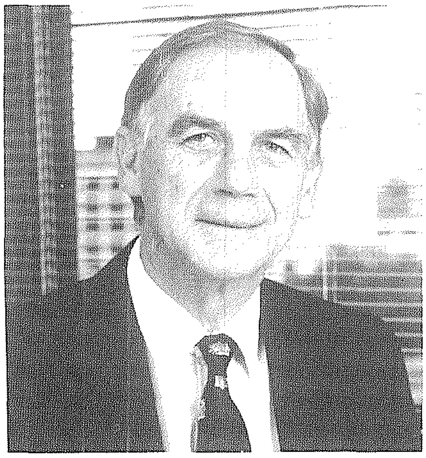
DIAMONDS IN DEMAND

A GIRL'S BEST FRIEND IS BACK



by ALAN K. JONES

Australia is a newcomer to a world diamond industry that has survived the threat of a wounding recession. The industry looks to a more settled future.

During the early 1980s the American author Edward Jay Epstein predicted in his book *The Diamond Invention* the demise of the diamond industry. The author's doomsday forecast received wide media coverage which was damaging to the diamond industry's image.

Mr Epstein badly underestimated the financial strength of the De Beers group and the resolve of diamond producers to prevent an oversupply of rough diamonds to the depressed world cutting centres. The diamond industry has survived, with flying colours, the most serious recession since the 1930s, thanks largely to the effectiveness of the De Beers centralised selling system.

The polished diamond market in the past decade has been one of robust demand. One of the most encouraging features of the retail diamond jewellery market was that even during the height of the recession between 1980 and 1983, sales remained remarkably buoyant.

It was during this period that the price of the perfect "D" flawless one-carat stone plummeted from $US60,000 to about $US8,000. The prices of the larger, high-quality stones had been driven up by speculative demand in the late 1970s, a period of high inflation and easy bank credit, and it was not surprising that, when the world's major trading countries mounted an attack against inflation by raising interest rates and tightening lending, the prices of the larger, better-quality diamonds collapsed from their unrealistic levels.

The prices of smaller-sized diamonds did not fluctuate greatly during the recession years, as consumers generally moved down-market.

The growth of diamond jewellery sales in the past three years has been very encouraging. In 1986 there was good demand for the larger, better-quality diamonds, especially in Japan, where sales of these stones are reported to have increased by about 50 percent. Diamonds are priced in US dollars, so strong demand for diamonds in Japan and Europe was expected because of the strength of their currencies.

The US accounts for about 38 percent of world diamond jewellery sales and it was pleasing to note that US sales in 1986 grew by some 10 percent. Japan is the second-largest consumer country with about 19 percent of world sales, while Europe accounts for about 18 percent.

Demand for luxury goods is driven by disposable incomes and, provided that world disposable incomes continue to increase, demand for diamond jewellery can be expected to follow the historical upward trend. Demand is further stimulated by a skilful promotion and advertising program organised by De Beers at a cost of more than $US100 million a year. It has been forecast that sales of diamond jewellery will increase by about 6-to-10 percent a year, with the number of carats of polished diamonds increasing by 4-to-5 percent a year.

Alan Jones is chief executive of Ashton Mining Ltd. This article is adapted from a presentation made in May 1987 in Tokyo, Hong Kong and Singapore.

The rough diamond sector presents a very different picture from the retail market. The Central Selling Organisation (CSO) accounts for about 80 percent of the world's supply of rough diamonds and therefore it is relevant to study their sales experience during the past decade.

Buoyant sales were achieved in the late 70s and the first half of 1980, when there was an excessive build-up of speculative stocks in the major world cutting centres — Antwerp, Tel Aviv and New York. In the following years to 1984, the CSO drastically reduced sales to the cutting centres to enable the cutting, polishing and manufacturing sectors to adjust their overstocked positions. The high level of retail diamond sales eventually affected the rough market, and in 1985 sales of rough gems rose by 13 percent above the 1984 figure, while 1986 saw an even more impressive sales increase of 40 percent above the 1985 results.

WORLD DEMAND FOR DIAMOND JEWELLERY

	PIECES (millions)	VALUE ($ billions)	CARATS (millions)
1978	40	14.3	7.6
1979	42	16.1	7.9
1980	40	18.6	7.5
1981	43	19.3	7.8
1982	43	18.6	7.9
1983	43	19.8	8.5
1984	46	21.1	9.0
1985	47	21.6	9.9
1986	49	25.0	11.1

There has been a small build-up of stocks in the cutting centres from a very low base to service the greater consumer demand, but it is encouraging that the higher level of purchases at the cutting centres has been largely financed internally by the industry.

Provided that world disposable incomes continue to increase, demand for diamond jewellery can be expected to follow the upward trend.

During the period of de-stocking at the cutting centres from 1981 to 1984, the CSO assumed its traditional role by purchasing surplus supplies of rough diamonds in the open market, and producers selling through the CSO also played their part by stockpiling. The substantial increase in demand for rough diamonds towards the end of 1985 and in 1986 enabled producers to dispose of nearly all their surplus stocks, while the CSO diamond stocks had been lowered from a figure slightly above $US2 billion, to $US1.85 billion at the end of 1986.

The substantial increase in demand for rough diamonds towards the end of 1985 and in 1986 enabled producers to dispose of nearly all their surplus stocks.

The chairman of De Beers stated in his company's 1986 annual report: "Our stockpile is soundly and adequately financed and we remain entirely willing to carry large stocks to ensure that unsound trading and speculation does not arise again as it did in the late 70s."

Total world production averaged about 47 million carats a year in the period 1980-1982. In 1983 alluvial diamond production started at Argyle, and this, with increased output from Zaire, caused production to increase to 66 million carats by 1985. The full impact of Argyle production occurred last year when world production increased by 22 million carats, or 33 percent, to about 88 million carats.

There was concern about the ability of the market to absorb this substantial increase in diamond production, but it must be remembered that the quality of Argyle diamonds is generally low. After cutting and polishing, the increased output added only about 2.5 million carats of polished diamonds to world supply, which is equivalent to the growth of US imports in 1985. The value of Argyle's gem production represents only 5 percent of the world's polished market, a relatively small addition.

It was indeed fortunate that Argyle's first full year of commercial production coincided with a surge in demand for rough diamonds, and this new supply has been well absorbed by the market, except for some of the small, lower-quality stones.

It is expected that some diamond producers will be able to increase output in 1987, and some mines closed down during the recession may be re-opened, but increased production from these sources will probably be modest.

No large deposit of diamonds has been found in the world since the Argyle discovery in 1979, and there are no large deposits about to be developed. In view of the time frame between discovery and commercial operations, there is unlikely to be a large increase in diamond supply in the next 4 to 5 years. Indeed, it is probable that world diamond production will peak in 1987-88, and then gradually decline until the next new large deposit is brought into production.

The industrial diamond market has not rated much of a mention because, although Argyle production contains 55 percent of industrial diamonds by volume, they represent only 9 percent of the gross revenue. Synthetic diamond producers dominate the industrial market and as such, they are the price setters. The Argyle industrial stones should be regarded as a by-product of the mine output. □

WORLD DIAMOND PRODUCTION
(million carats)

	1980	1981	1982	1983	1984	1985	1986
Australia	—	—	—	6.2	5.7	7.1	29.0
Zaire	14.0	12.5	12.2	13.0	18.5	19.6	20.0
U.S.S.R.	12.0	12.0	12.2	12.0	12.0	12.0	12.0
South Africa	8.7	9.5	8.9	10.0	9.8	9.9	10.1
Botswana	5.1	4.96	7.8	10.7	12.9	12.6	12.9
Namibia	1.6	1.25	1.0	0.96	0.93	0.91	0.94
Other	5.8	5.20	5.0	4.34	4.07	4.39	3.76
Total	47.2	45.5	47.1	57.2	63.9	66.5	88.7*

* Projected