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DIAMONDS

WHAT TO LOOK FOR IN 2020

By Paul Zimnisky - Diamond Industry Analyst

Following a strong first half of 2018, the balance of the year and most of 2019 was disappointing for the diamond industry. The most recent 18-month stretch has been described by some in the industry as a "very challenging environment" and even a "crisis". The third significant industry lull in the decade and a half since the dismantling of the De Beers monopoly seemingly indicates that the diamond industry is yet to find sound, sustainable footing in a new era.

A tightening of credit to diamond manufacturers following the widely publicised alleged $2-billion fraud by well-known Indian industry titans Nirav Modi and Mehul Choksi in mid-2018 in part led to accelerated industry-wide mid-stream inventory deleveraging through 2019. An estimated at $10bn, or approximately 25% of all inventory held by the mid-stream segment of the industry, was forced to downstream as many manufacturers couldn't retain previous levels of finance and were pressured to scale down operations and shrink balance sheets. The flood of excess mid-stream supply more than offset a 5% year-over-year decline in mined diamond volume in 2019.

While the industry has since actively worked through the indigestion, demand challenges including an acceleration of the trade war between the United States and China, the industry's two largest end-consumer markets, has stifled the process. Further, widespread, multi-month protests in Hong Kong, referred to as the Anti-Extradition Law Amendment Bill Movement, have impacted retail sales in the ever-important market and also interfered with business-to-business industry trade. In addition, a broad economic slowdown in Europe and a global trend towards negative interest rates have boosted the US dollar which has also pressured global end-consumer diamond demand in recent quarters.

$100-million

Value of DPA marketing budget for 2020

Looking to 2020, if the global economic picture stabilises or hopefully even improves, the US would need to avert a recession and China would need to maintain a mid-single-digit growth rate, and the diamond industry could finally be on a more stable footing by mid-year as industry-wide inventories approach much more sustainable levels. At an estimated $30bn of inventory, mid-stream stocks are the lowest since 2011, coincidently the last time diamond manufacturing was notably lucrative.

Upstream players, led by De Beers and ALROSA, began building inventory in the second half of 2019 in order to support the market. However, both players were starting from relatively normalised inventory levels at the time and the excess stock recently accumulated should be manageable as it is not estimated to exceed 2015 levels, the high watermark in recent years following the mid-decade slowdown in China.

While macro-economic developments, including some of those mentioned above, will continue to impact end-consumer diamond demand and play a major role in the health of the industry in 2020, here are three industry-specific catalysts that could have a noticeable impact on the trade as well:

THE DPA'S THREE BILLION YEARS IN THE MAKING CAMPAIGN

In Q4 2019, the Diamond Producers Association (DPA), the diamond industry's joint category-marketing effort, debuted its latest campaign titled The Diamond Journey with the tagline Three Billion Years in the Making. 2020 marks the fifth year since the group was established and the third consecutive year that the budget has exceeded $50-million. The 2020 budget alone is estimated to approach $100m, the highest yet, but is still short of the estimated $200m to $250m that De Beers was spending annually during the monopoly era via the A Diamond is Forever campaign. The result of large category marketing strategies such as this can be slow and gradual in nature but can leave a lasting impact on a consumer's perception of a product if communicated effectively. It has now been over a decade since the A Diamond is Forever campaign was retired and consumers' positive perception of diamonds has faded. However, now a few years into the reintroduction of generic diamond marketing, results should begin to show especially in the three primary markets being targeted: the US, China and India.

Rough and polished diamonds from Rio Tinto's Argyle mine.

© Rio Tinto

ALROSA'S LUMINOUS DIAMONDS CAMPAIGN

In September ALROSA said it was in talks with several jewellers about joint-marketing the company's strongest fluorescent diamonds as Luminous Diamonds. Fluorescence is most prominent in Russian and Canadian diamonds, which notably tend to be found near the Arctic, but fluorescence is also found in stones outside of the far north and is estimated to be present in as much as a third of all diamonds globally. Diamonds with "strong" fluorescence, the focus of ALROSA's campaign, represent as much as a 5-10% of global supply. While traditionally fluorescence has been seen as a negative attribute as it can make a diamond appear "milky" or "oily" in direct sun or UV light, the characteristic also makes a diamond mysteriously glow under a black light, ideal for a club or party scene. This fits well with the industry's intention of directing more marketing towards younger demographics. Further, most natural diamonds fluoresce blue, while most man-made diamonds fluoresce orange, green or blue-green, so fluorescence is potentially another attribute that the natural diamond industry can use to differentiate its product from man-made. ALROSA says it expects the product line to be available in early 2020, with the US and China being the initial target markets.

ARGYLE OFFICIALLY CLOSING

Easily the industry's most anticipated supply catalyst, Rio Tinto's Argyle Diamond Mine in Australia is finally set to officially close in 2020. In June 2019, management told media outlets that in "late 2020 we'll be stopping operations and will start the rehabilitation of the site". The mine, which at one point accounted for almost half of global diamond output in volume, has produced 10-15 million carats in recent years, representing a high-single-digit percentage of the world's output. An estimated three quarters of Argyle's output is brown in colour, lower in quality or smaller in size – the categories of diamonds that have been under the most price pressure in recent years. Argyle supply coming offline will further balance what has been an oversupplied diamond market for most of the last decade. The implication, which will probably be seen as a positive catalyst for the industry, will probably garner a sizable amount of media attention which could boost industry sentiment and reinforce consumers' perception of natural diamonds – that they are a fleeting, non-renewable resource, and thus are rare and valuable. ■

"Argyle mine will officially close in late 2020." – Zimnisky

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INDUSTRY CATALYSTS IN 2020

- **The DPA's Three Billion Years in the Making campaign.**
- **ALROSA's Luminous Diamonds campaign.**
- **Argyle officially closing.**

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