

De Beers :
A Monopoly in the Diamond Industry

"A diamond is forever. De Beers."

De Beers advertising slogan "A Diamond Is Forever" has been the center of its effort to establish the stone as the only appropriate gem to symbolize lifetime love and commitment.

The more ad money spent, the more diamonds people buy. And when people buy diamonds, De Beers profits. It is the reason the company spends \$180 million a year worldwide to advertise cut diamonds--a product it doesn't even sell ...

There are very few companies ... you may struggle to find even one, that has been the leader of its industry for its entire history.

De Beers is such a company!!!!

What is De Beers

- not retailer
- not manufacturer

BUT

- miner and buyer of 70-90% of the world's rough diamonds
- arbiter of their prices.

It is an international company that:

- buys rough diamonds directly from the diamond mine owners
- resell them to the cutters
- cutters sell the cut diamonds to the dealers who in turn sell them to the jewelry stores.
- And still De Beers spends \$180m a year worldwide to advertise cut diamonds--a product it doesn't even sell !!!

Outline

- its origin
- how it achieved its market power
- how it has managed to control the market
- inefficiencies created by monopolies and Antitrust regulators in the U.S.
- "Blood" Diamonds

A) Facts about De Beers

◆most successful monopoly of modern trade

- other commodity prices (e.g. gold, silver, grains) fluctuate greatly in response to economic conditions
- diamonds' prices are constantly rising.

◆20th century, De Beers sold 85% to 90% of the diamonds mined worldwide

◆ Rockefeller's Standard Oil and Gates' Microsoft may have briefly approached this kind of dominance, but the length and extent of De Beers' supremacy is unprecedented.

◆ artificially keep diamond prices stable by matching its supply to world demand.

◆ De Beers acts like the theory of monopoly predicts:

- It is almost the sole seller of diamonds (sells almost 90% of world production).

- Sells a commodity with no close substitutes (created this illusion by advertising)

- It restricts output and it responds to changes in market demand. When demand contracts De Beers cut back on its sales and vice versa.

GOAL: S=D for diamonds at a high Price

B) HISTORY(CREATION OF THE DE BEERS EMPIRE)

Before the 19th century,

diamonds were exceptionally rare

-small quantities in India and Brazil

- no diamond mines were discovered

Now: Diamonds/Mines

Republic of South Africa

Sub-Saharan countries

Siberia

Australia

Canada's NWT

But De Beers still manages to control the world Market and still manages to make us believe that diamonds are rare!!!

Mid 1860s-1890s

1869 :

♣ first diamond mines in the colonies of southern Africa

♣ drastically increased the number of stones available.

1870

♣ Many diamond hunters bought mines.

♣ **Cecil Rhodes** bought the rights to two mines on the farm of **Nicolas and Diedrick DeBeer** in the Cape Colony (now South Africa).

♣ Diamond hunters realized that their price depended on their scarcity.

♣ Had no other alternative than to merge their interests into a single entity

- control the mines' production

- keep the scarcity illusion

- ♣ **De Beers Consolidated Mines Limited** was established on 12th March 1888 with Rhodes as its founding chairman.
- ♣ It is a South African company and granted an official listing on the Johannesburg Stock Exchange in August 1893.
- ♣ By 1890, De Beers controlled more than 95% of the world's diamond production (buying any new mine discovered)

- ♣ In Feb. 1890, Rhodes decided for a single channel of diamond distribution.
 - group of 10 Jewish merchants (called London Diamond Syndicate)
 - agree to be purchasing the entire production from all the De Beers mines and then resell them to cutters and wholesalers in Antwerp .

♣ One of these merchants, **Ernest Oppenheimer**

- started buying his own mines(Consolidated Diamond Mines)
- started competing with De Beers.
- took over De Beers
- Chairman in 1929
- Oppenheimer family still controls De Beers

His thinking was :

“The only way to increase the value of diamonds is to make them scarce, that is to reduce production”

De Beers acts like the theory of monopoly predicts:

It restricts output and it responds to changes in market demand.
 In case of new diamond discoveries De Beers buys them so that the new supply does not enter the market. (avoid the shift of S right and lower price).

Example: Great Depression

1. Public stopped buying diamonds (demand shifted left)
2. London Diamond Syndicate could not absorb the world's diamond production at the high prices
 - huge stockpiles
 - wanted to put them in the market
3. Oppenheimer realized that
 - prices will fall
 - people will lose faith in diamond
4. Took over the Syndicate and rename it Diamond Trading Company(DTC). Then sell the diamonds to a selected group of cutters that abide De Beers rules.
5. To eliminate excess supply
 - closed all major mines in South Africa
 - cut supply
 - 2,242,000 carats in 1930
 - 14,000 carats in 1933
6. New discoveries in Belgian Congo and Angola
 - DTC bought them to avoid ↓ in P
 - 1937 De Beers stockpile of diamonds had grown to 40 million carats (20 years supply).

7. De Beers wanted to control Congo's diamonds.
- Signed a deal with Belgian government
 - Diamonds from Congo will be sold only to De Beers
 - In exchange Antwerp will remain the main center for cutting diamonds.
 - Production from Congo mines was in accordance with a quota set by De Beers.

8. Similar situation happened with discoveries in Australia, Siberia and Canada. De Beers made arrangements with the mines to be the sole buyer of their production at guaranteed high prices so as to safeguard the control of world supply.

C) How the Monopoly Functions

- sends invitations to 250 chosen clients (diamond cutting factories in NY, Tel Aviv, Antwerp etc.) to attend the 10 annual "sights"
- "sights": gathering in London to transfer a pre-selected number of diamonds from De Beers stockpile to the client
- client receives a small box containing
 - uncut diamonds
 - a paper with the price of the box (\$1-\$25 million)

Rules of the Game

Rule #1:

Diamond Trading Company decides who gets which diamond

Rule #2

No Haggling over price

- Prices are fixed by De Beers (usually 25% less than the wholesale prices for uncut diamonds)
- If refuse to pay the price, do not get the box and may not receive future invitation (may be forced to close down)

Rule #3

Take the entire Box or None

Clients must accept the whole box(containing profitable and not very profitable diamonds)

Rule #4

No client may resell the diamonds in his box in their uncut form

- want to control the world stockpile of diamonds.
- if uncut diamonds can be resold then someone might buy huge amounts and compete with De Beers
- This happened in 1977 where Israeli dealers bought unopened uncut diamonds boxes and got a stockpile similar to De Beers one.
- De Beers managed to force diamonds out of Israeli hands by managing Israeli banks

Rule #5

Clients will provide any information to assess the diamond market

- a) Before the sight, clients fill a detailed questionnaire
- number of uncut diamonds in inventory

- diamonds in process to cut
- future sales)

b) De Beers audits their cutting factories in surprised visits

Rule #6

Diamonds must never be sold into “weak hands”

Goal: Keep prices high

- clients cannot sell diamonds to retailers that offer discounted prices
- if a client sells to such retailer, penalized.

Thus, De Beers decides:
 ♠ How many diamonds of each quality will be distributed in total
 ♠ How this supply will be divided among the clients
 ♠ Price of diamonds.

How do they make these decisions?

1) **Predict world demand for diamonds**

- Information about rate of family formation in USA and Japan
- Economic conditions

2) **Predict unsold supply of diamonds**

- Calculate number of diamonds jewelry stores have in inventory

3) Find the categories that are in excess supply and those in excess demand

e.g. if yellow diamonds appear to be in excess supply, omitted from the boxed in next sight.

**De Beers Tactics in Summary:
 Decrease Production and Increase Demand**

Increase Demand via ads

Japan :

1968

less than 5% of Japanese women getting married received a diamond engagement ring.

1981

60% got a diamond ring

Eternity Ring-for married women

De Beers needed to buy the Russian small diamonds. Thus created a market for them: “*eternity ring*”

Decrease Production via control of mines

Take over mines in Canada, Angola

Agree with the Russians to buy all of their production

Decrease production so that it matches demand

D) **Monopoly and Inefficiencies**

i) HIGH PRICES FOR AN ACTUALLY ABUNDANT COMMODITY

USA and Anti-Trust Regulation

- ◆ half of the world's \$56-billion retail diamond business industry
- ◆ Only activity in USA: advertising

Since is a monopoly

- cannot operate in the US due to the anti-trust legislation
- represented in the US by Ayer's, a marketing firm.

ii)Angola and “Blood Diamonds”

- 25-year civil war
- Begun as a struggle against the Portuguese occupation
- now it is over the country's natural resources: oil and diamonds (\$600-800 million annually)
- De Beers so as to control the world's diamond supply, bought lots of diamonds from areas controlled by rebels.
- Rebels used the money to finance the war
- By 1998, De Beers' Angolan adventure threatened to become a PR nightmare.
- Fearful of a consumer backlash, De Beers closed its buying offices in Angola and the Democratic Republic of Congo (DRC).

E) Conclusion

"A diamond is forever. De Beers."

De Beers will keep being a monopoly as long as women regard them as their “best friends” and De Beer manages to sustain control of all diamond mines in the world.