AllanHochreiter

# Diamonds Africa 2007

## Diamond Export Levy and Beneficiation

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**23 April 2007**

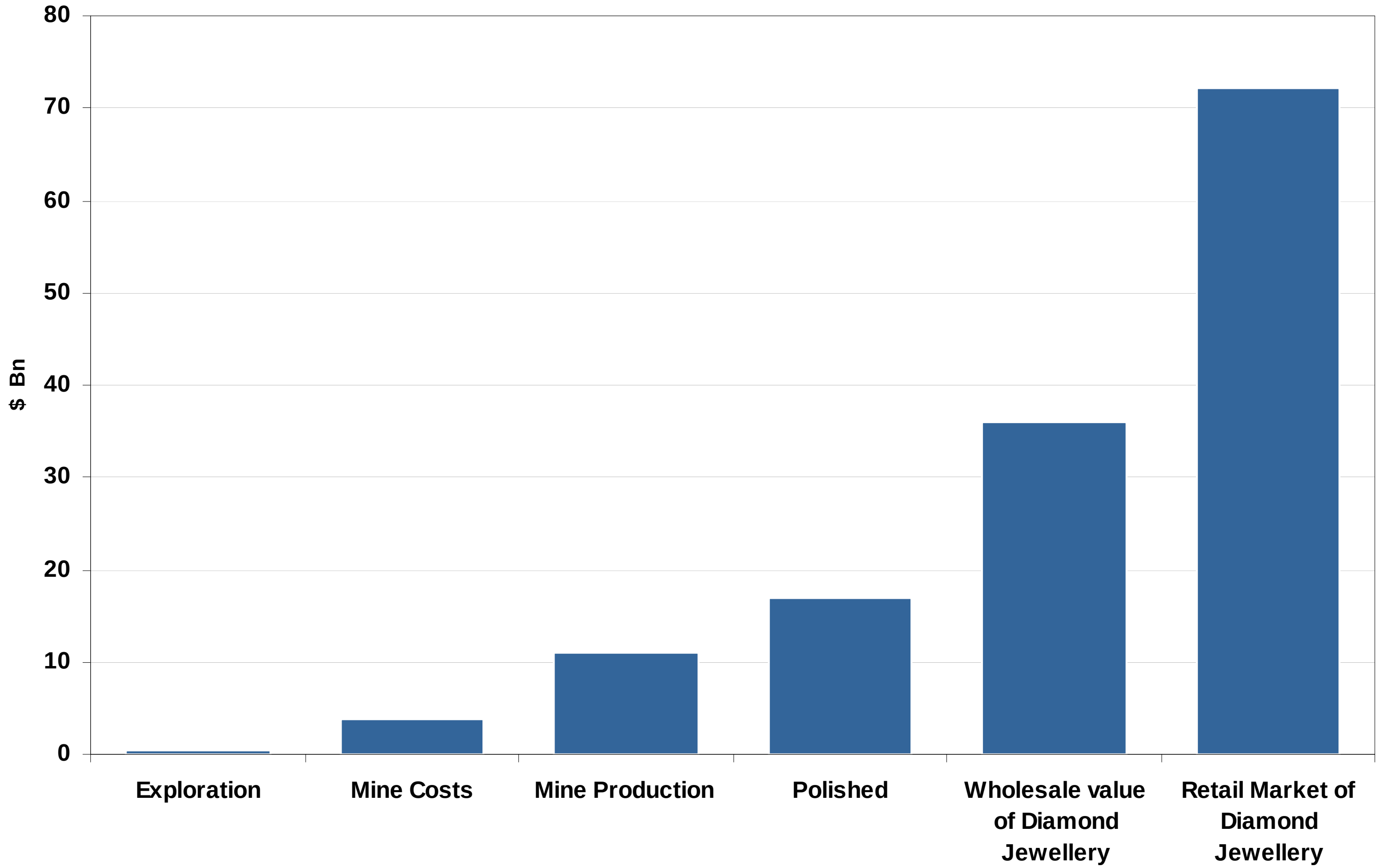
# Outline

- Objectives of the Diamonds Amendment Act
- Global diamond overview
    - Mining
    - Cutting and polishing
    - Retail markets
- SA cutting and polishing
    - Structure
    - Costs
    - Mine supply
- Implications and recommendations

# Diamonds Amendment Bill Objectives

- **Increase access to rough diamonds for manufacturing in South Africa**
- **Grow beneficiation industry in South Africa to create jobs**
- **Increase participation through the value chain**
- **Make South Africa a major international diamond beneficiation centre**

# Diamond Pipeline 2006



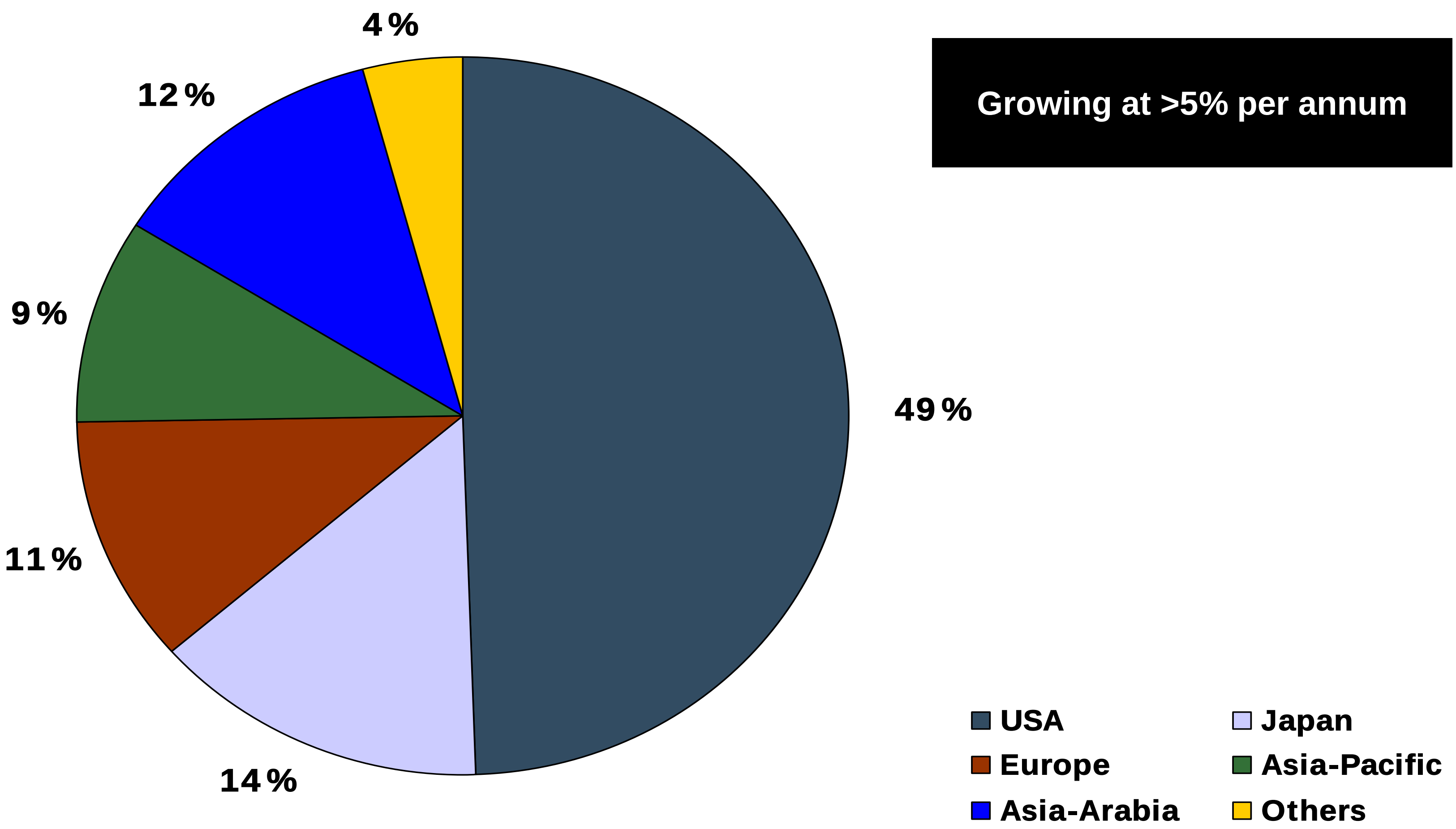
# Mine Supply Estimates (2005 – 2010)

| Production ($m) | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 |
|---|---|---|---|---|---|---|
| **South Africa** | 1,560 | 1,600 | 1,614 | 1,631 | 1,636 | 1,642 |
| **Botswana** | 2,810 | 2,810 | 2,810 | 2,810 | 2,810 | 2,810 |
| **Canada** | 1,395 | 1,453 | 1,515 | 1,724 | 1,977 | 2,175 |
| **Russia** | 1,698 | 1,698 | 1,698 | 1,698 | 1,698 | 1,698 |
| **Angola** | 1,166 | 1,166 | 1,166 | 1,166 | 1,166 | 1,166 |
| **Namibia** | 616 | 616 | 616 | 616 | 616 | 616 |
| **DRC** | 442 | 451 | 461 | 472 | 484 | 498 |
| **Australia** | 596 | 536 | 434 | 434 | 248 | 281 |
| **Tanzania** | 29 | 35 | 41 | 58 | 87 | 87 |
| **Sierra Leone** | 76 | 97 | 111 | 122 | 135 | 148 |
| **Other** | 319 | 383 | 383 | 383 | 383 | 383 |
| **Total Supply** | **10,707** | **10,845** | **10,898** | **11,116** | **11,240** | **11,504** |

# Global Diamond Production ($:+1.5% per annum;Carats -2.5% p.a.)

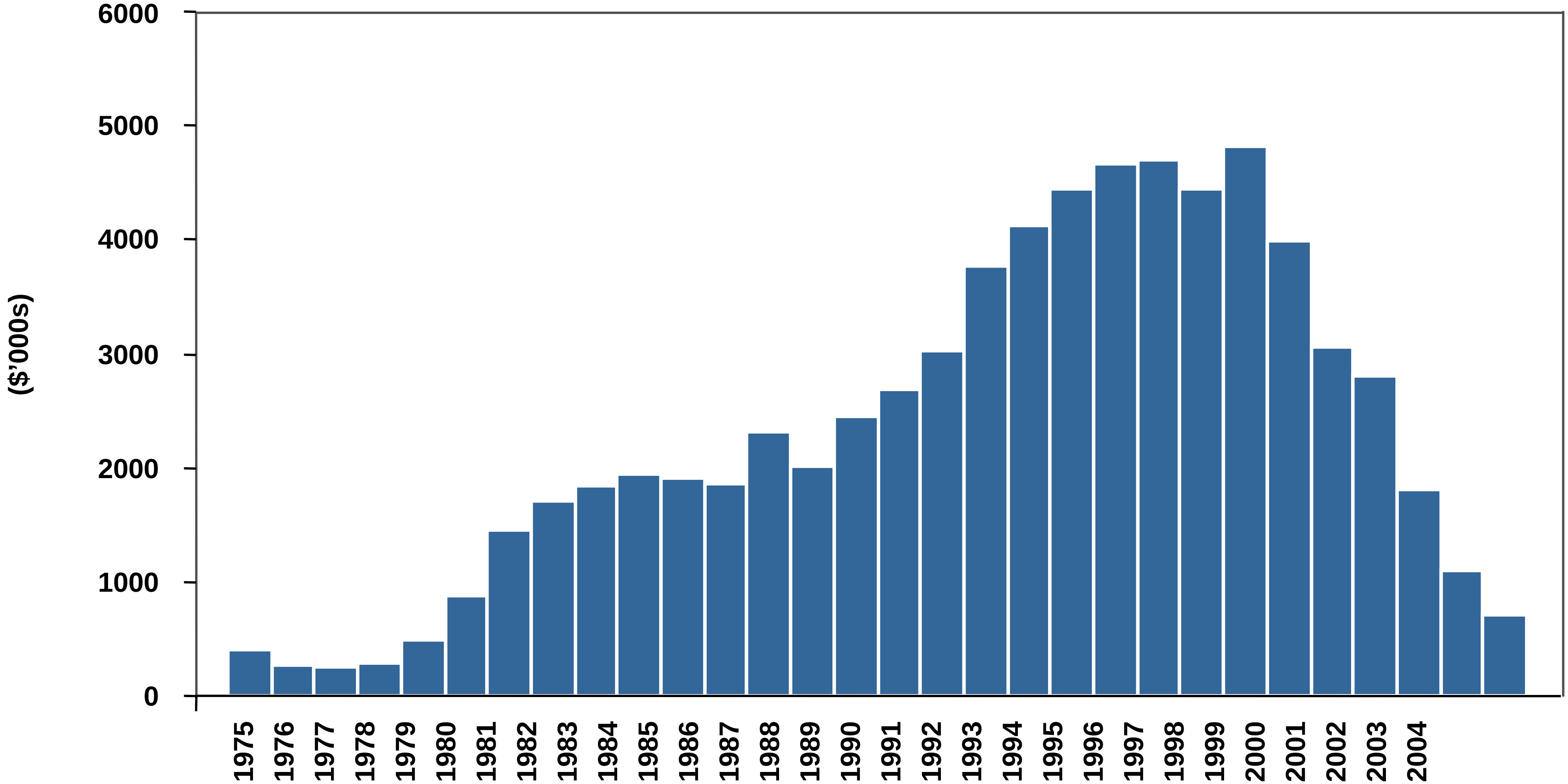
| | 2005 (E) | | | 2010 (F) | | |
|---|---|---|---|---|---|---|
| | Carats (000's) | $/carat | Value ($m) | Carats (000's) | $/carat | Value ($m) |
| **South Africa** | 13,952 | 112 | 1,559 | 14,643 | 112 | 1,642 |
| **Botswana** | 32,350 | 87 | 2,809 | 32,350 | 87 | 2,809 |
| **Canada** | 13,527 | 103 | 1,395 | 20,880 | 104 | 2,174 |
| **Russia** | 15,888 | 107 | 1,697 | 9,886 | 172 | 1,697 |
| **Angola** | 4,400 | 265 | 1,166 | 4,400 | 265 | 1,166 |
| **DRC** | 24,200 | 18 | 441 | 24,200 | 21 | 497 |
| **Namibia** | 1,990 | 310 | 616 | 1,990 | 310 | 616 |
| **Australia** | 36,000 | 17 | 595 | 17,000 | 17 | 281 |
| **Tanzania** | 250 | 117 | 29 | 750 | 117 | 87 |
| **Sierra Leone** | 370 | 206 | 76 | 455 | 325 | 147 |
| **Other** | 3,263 | 98 | 319 | 3,263 | 118 | 383 |
| **Total** | **146,188** | **73** | **10,707** | **129,816** | **88** | **11,504** |

# Retail Sales of Diamond Jewellery – 2006 ($72bn)




**Growing at >5% per annum**

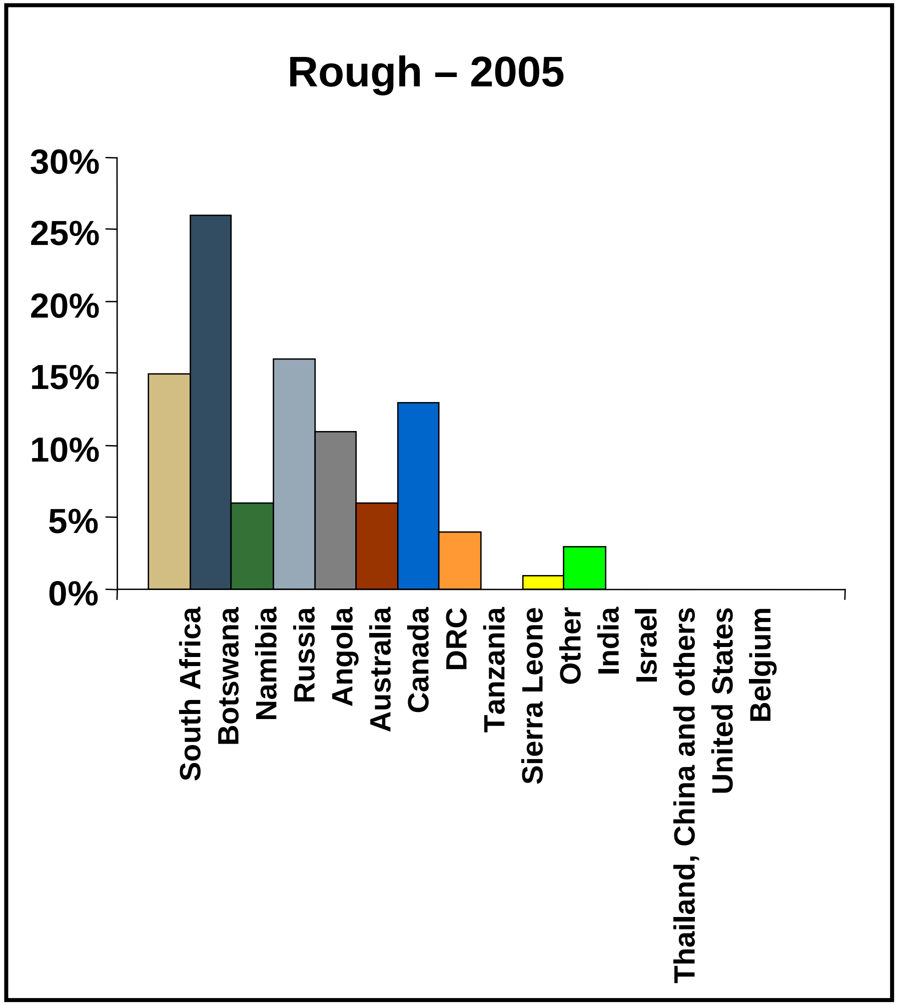
# Supply and Demand Reflected in De Beers Stocks

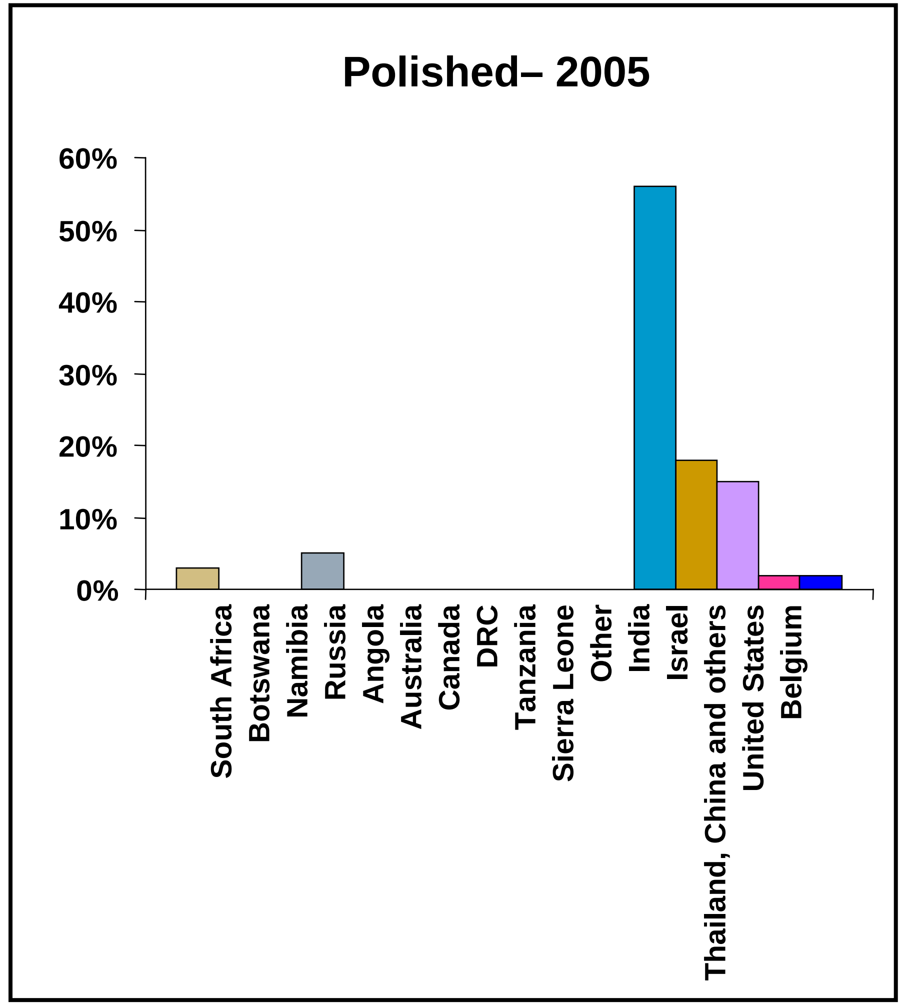


# Global Overview

- Rough Diamond Prices up >35% since 2002
- Production decline of 2.5% (carats) per annum to 2010
- Argyle production to halve by 2010
- Growth in supply value of 1.5% per annum to 2010
- Demand growth 5-6% per annum
- Upward pressure on rough prices
- Less carats to cut and polish!

# Global Share of the Diamond Industry

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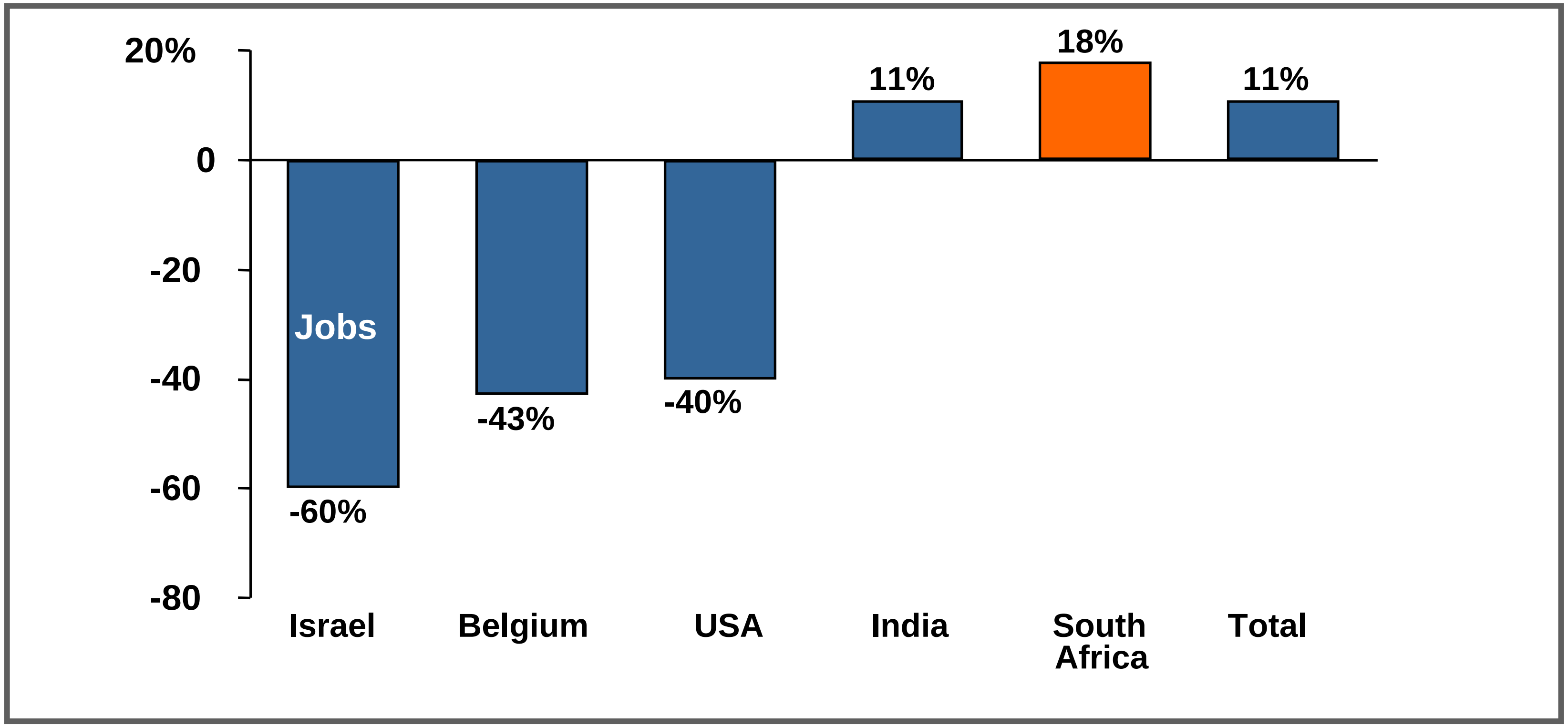
# SA Cutting Industry

- 370 licensed Cutters
- Not all of them are active> 120-180 in any one year
- +-2 000 employees
- Output of around $500m

# In contrast to South Africa, Israel and Belgium have seen falling job numbers since 1996

Change in number of cutting jobs (1996-2002)




Note: China has grown from a low base over the last six years – estimated 100% increase in jobs over this period

# SA Cutting Industry – Exports(+13%per annum)

| | 1999 | 2000 | 2001 | 2002 | 2003 |
|---|---|---|---|---|---|
| **Carats** | 180,987 | 253,457 | 243,366 | 321,046 | 353,305 |
| **Dollar value** | 295,883,809 | 474,447,826 | 476,447,826 | 510,641,022 | 550,323,720 |
| **Per carat ($)** | 1,635 | 1,872 | 1,872 | 1,591 | 1,558 |

# Average Value of Polished by Cutting Centres

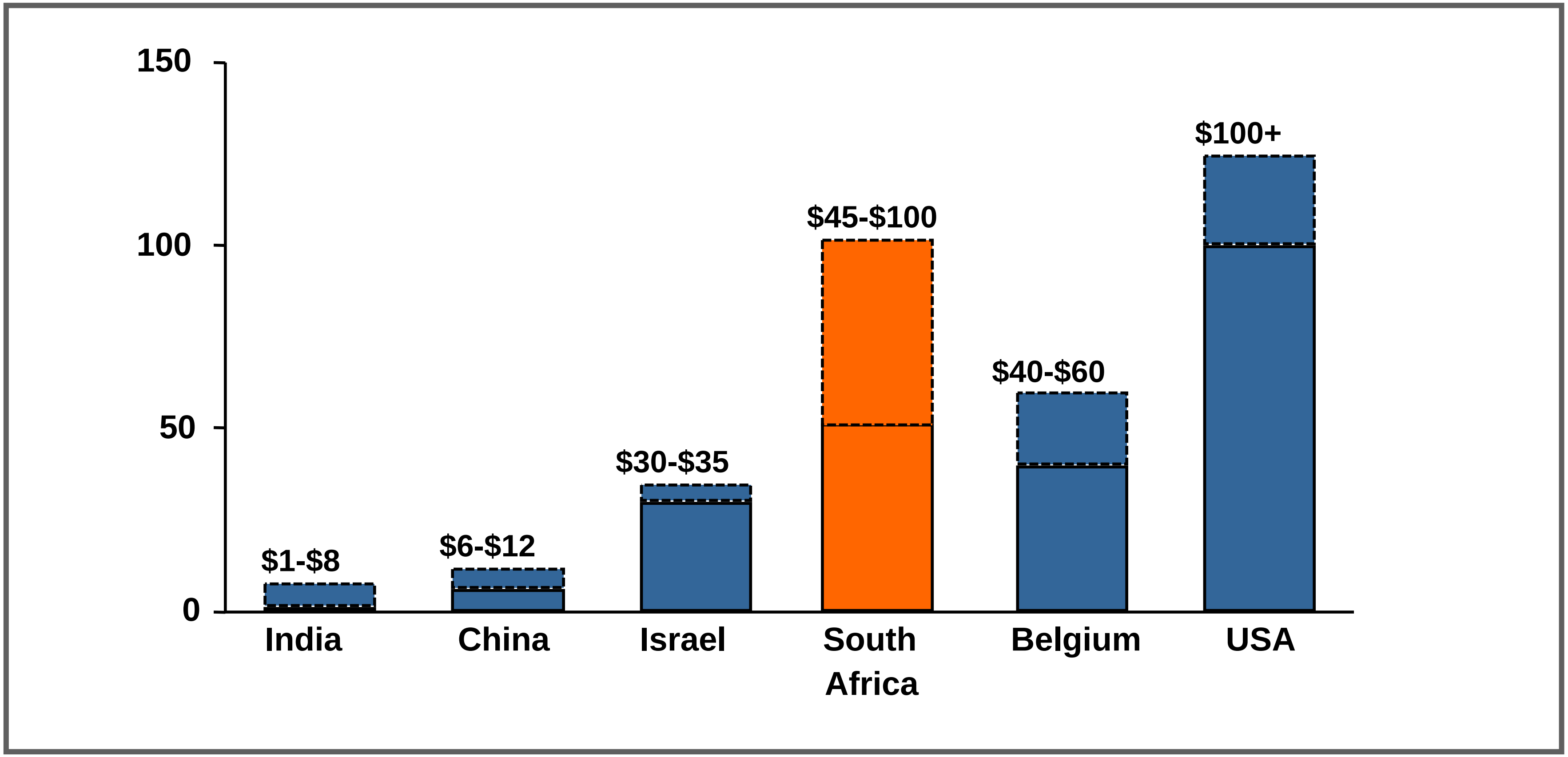
| Region | Average Price of Polished ($/ct) in 2001 |
|---|---|
| New York | 1600 |
| Antwerp | 1100 – 1200 |
| Tel Aviv | 1000 |
| India | 250 – 300 |
| South Africa | 1600 |

# SA Cutting Industry Compared

| | New York | Belgium | Israel | South Africa | Thailand | China | India |
|---|---|---|---|---|---|---|---|
| **Manufacturing cost $/ct** | 100 | 40 – 60 | 30 – 35 | 30 – 100 | 15 | 6 – 12 | 1 – 8 |
| **Salary: $/month** | 4500 | 2500 | 1500 – 2000 | 1300 | 120 – 135 | 50 – 120 | 80 – 140 |
| **Range rough size** | 2ct to +10.8ct | 1ct to +10.8ct | 0.75ct to +10.8ct | 0.75ct to +10.8ct | 2ct to 10ct | 0.5ct to 20ct | 0.01ct to 10.8ct |

# The South African Cutting Industry is Significantly Higher Cost than in India and China

Average cutting and polishing cost ($/carat)



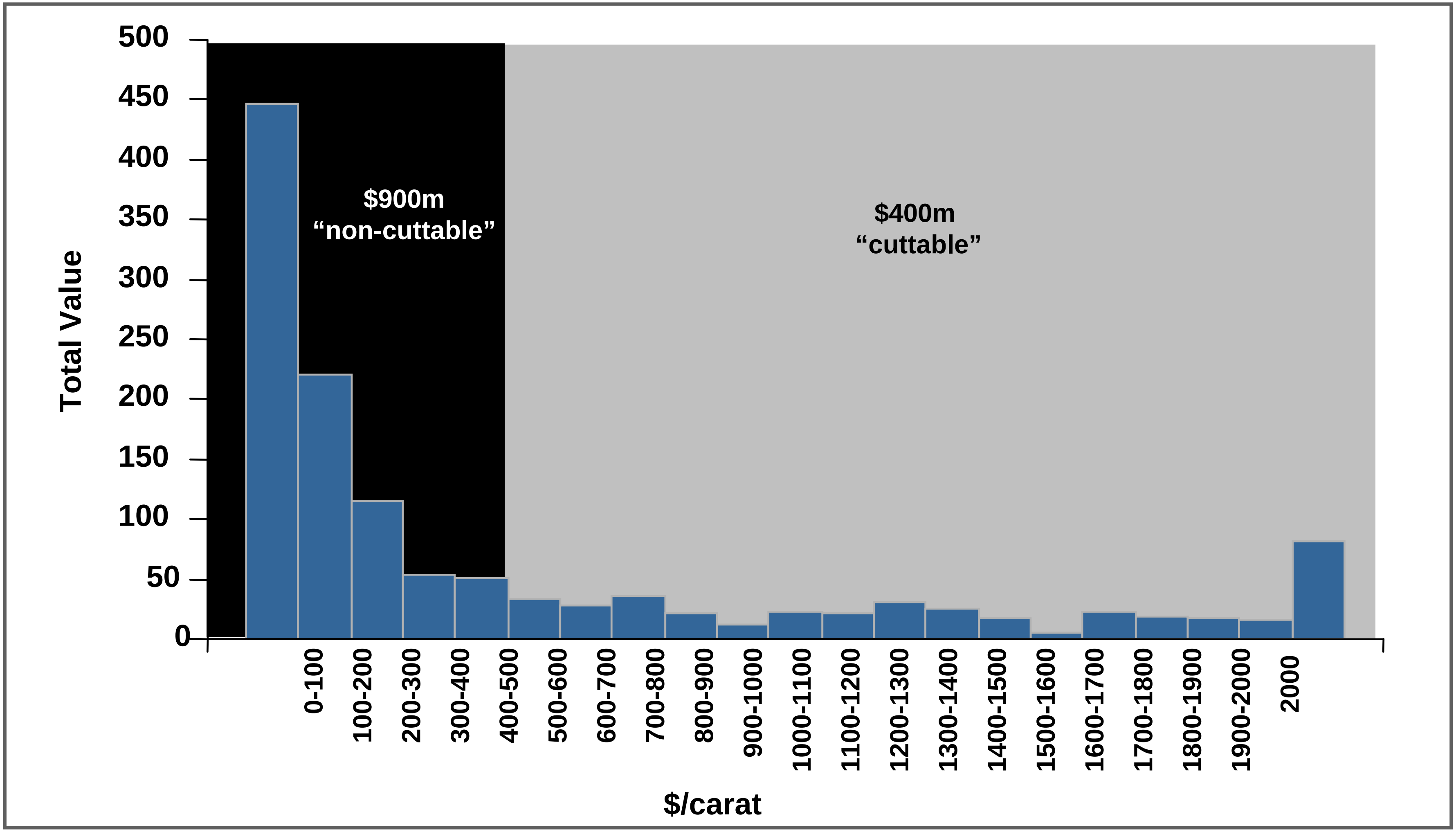
# Some points on INDIA

- **Minimum wage $50/month**
- **Average wage $100/month**
- **Most small businesses family owned**
- **No salaries> profit or production bonuses**
- **Zero tax to 2000!**

# Some comments on the small business Abbey Chikane

- Small business $50 000 turnover per annum
- 5 Employees
- Turnover $833 per employee per month
- If labour is 10% of turnover
- Labour cost $83/month
- This is lower than SA minimum wage and
- We should not be developing a “sweat shop” industry
- Turnover needs to be higher per employee

# De Beers South African Mines Production Split (2004)



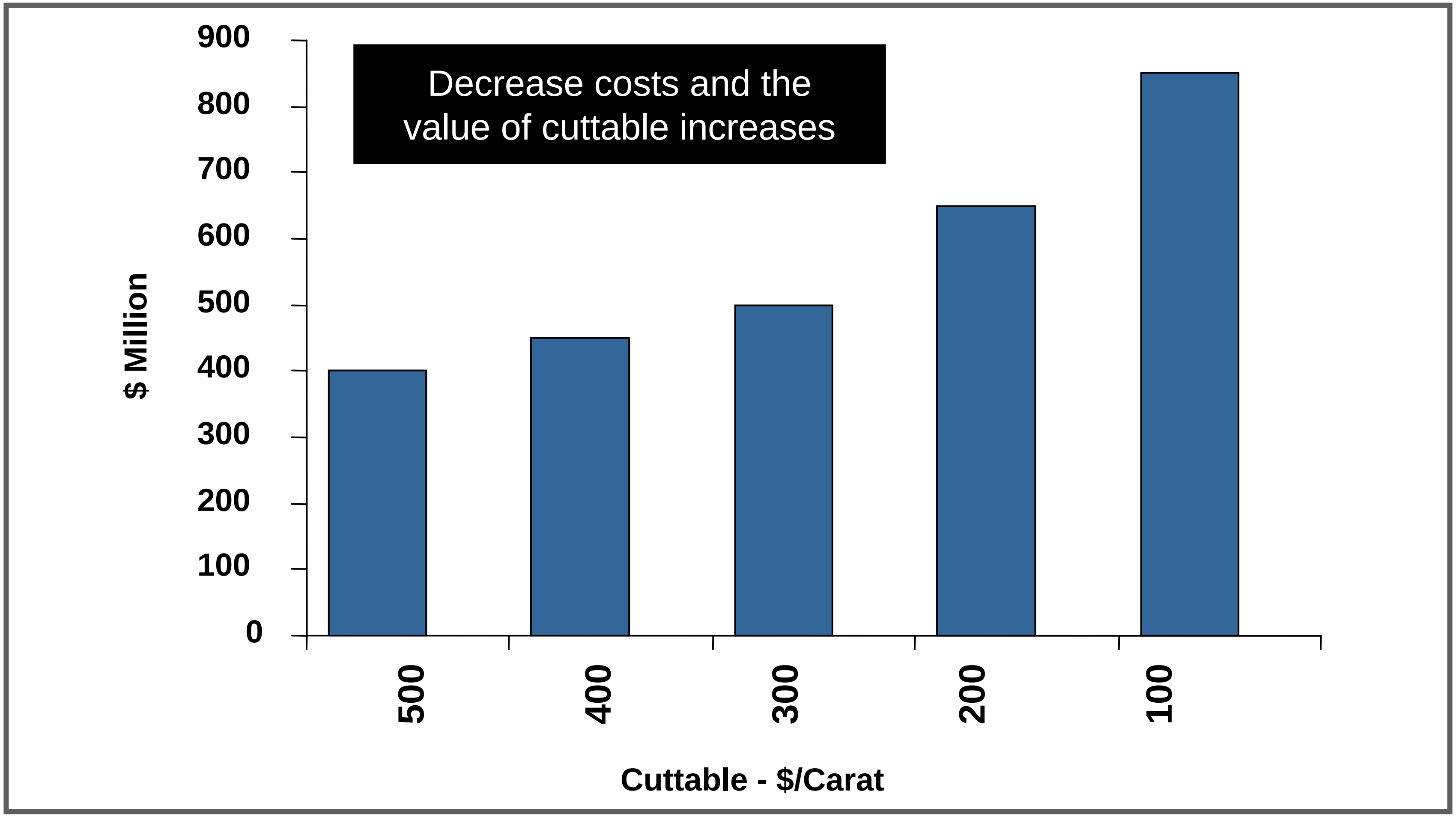
# Impact of an Export Tax

- Imposing a 5% export tax reduces the price received in SA by 5%
- Diamonds are a global commodity priced internationally by the market.
- An export tax does not add to the value of the diamond….
- A $400 diamond in Israel or Antwerp will be  worth $380 in SA
- A $100 diamond in Mumbai will be worth $95 in SA

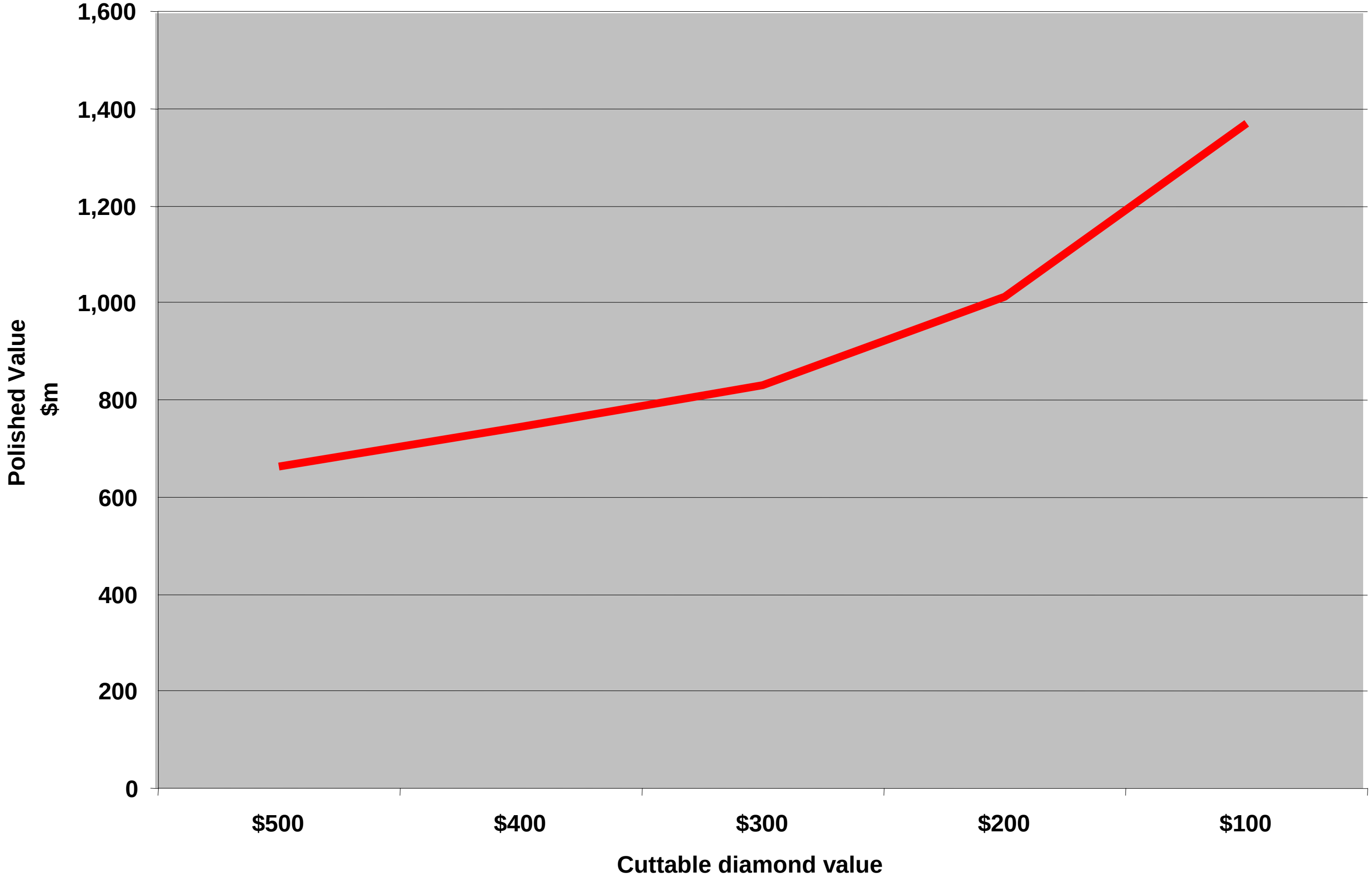
# Impact of an Export Tax

- **The price barrier for cutting and polishing will drop from $400 diamonds to include those down to $380 diamonds**
- **Possible additional available for cutting: $25m**
- **Possible additional available for cutting: 75 000 cts**
- **Increase of 20% in carats and 5% in value…..**
- **Perhaps another 400 jobs….**
- **And an additional $25m in the pockets of the SA cutting industry**
- **And at least $25m less to the mining industry !**

# South African Production Cuttable Value Versus Cuttable Value Per Carat



# Polished value vs. Cuttable Diamond value



# SA Cutting Industry

- **The chances of competing with India are slim (SA labour costs ten times India)**
- **SA labour ($1300) is cheaper than Israel (>$1500)**
  - **Quantity of cuttable goods is governed by costs of production**
  - **Israel cuts smaller diamonds ($1000 polished vs $1600)**
  - **Israel employs 50% more people but polishes 6 times more**

# SA Cutting Industry

- The challenge to the cutting industry is to reduce costs
- S59A The State Diamond Trader shall
  - (a) acquire and supply unpolished diamonds to local diamond beneficiaries ; and
  - (b) promote the diamond industry through the necessary research, support and development as deemed necessary from time to time
- CHALLENGE TO REDUCE LABOUR COSTS TO $20/CT!

# Diamonds Amendment Act
# State Diamond Trader (SDT)

- **Can buy a percentage of rough but..**
- **10% by carats could equal 90% by value**
- **SDT can pick the eyes out of the production**
- **How will a fair value be achieved?**
- **No incentive for buyers to attend tenders**
- **How does a SDT  provide "cheap" rough to the industry and not pay lower prices to the miners?**
- **Why would neighbouring countries sell rough to us at a cheaper price than they can achieve in Antwerp?**

# Diamond Amendment Act

## Mines likely to close/rationalise:

| | 2005 | | |
|---|---|---|---|
| | Cts ('000s) | $m | Jobs |
| **Cullinan** | 1300 | 120 | 1300 |
| **Namaqualand** | 900 | 250 | 2500 |
| **Koffiefontein** | 50 | 8 | 550 |
| | **2250** | **378** | **4350** |

- **SA could lose 30% of production**
- **>30% of cuttable production could be lost**
- **>50% of large mining jobs may be lost**
- **Sale to leaner/meaner operators- job losses?**

# The Act Will Achieve the Following

- Reduce the prices for rough diamonds in South Africa leading to
- Increased employment in the cutting industry 400-500 jobs
- Closure of mines, decrease investment into the mining sector
- Lose up to 5 000 jobs in the mining sector
- Decrease the availability of rough by up to 30%
- Provide a margin for unscrupulous operators
- Increase statistics on polished exports and create a false sense of achievement
- Provide an environment where South Africa could become a diamond smuggling centre

# Conclusion

- **The South African diamond industry competes in a global market for capital and job creation**
- **Beware of "unintended consequences that result in NET JOB LOSSES"**
- **Growth in the cutting industry requires lower costs to make more rough cuttable**
- **But this should not happen at the expense of the mining industry!**
- **The Challenge to the SA cutting industry is to reduce costs; improve productivity- REDUCE LABOUR COSTS TO $20/CT!**
- **Only then will SA become a major diamond beneficiation centre**