

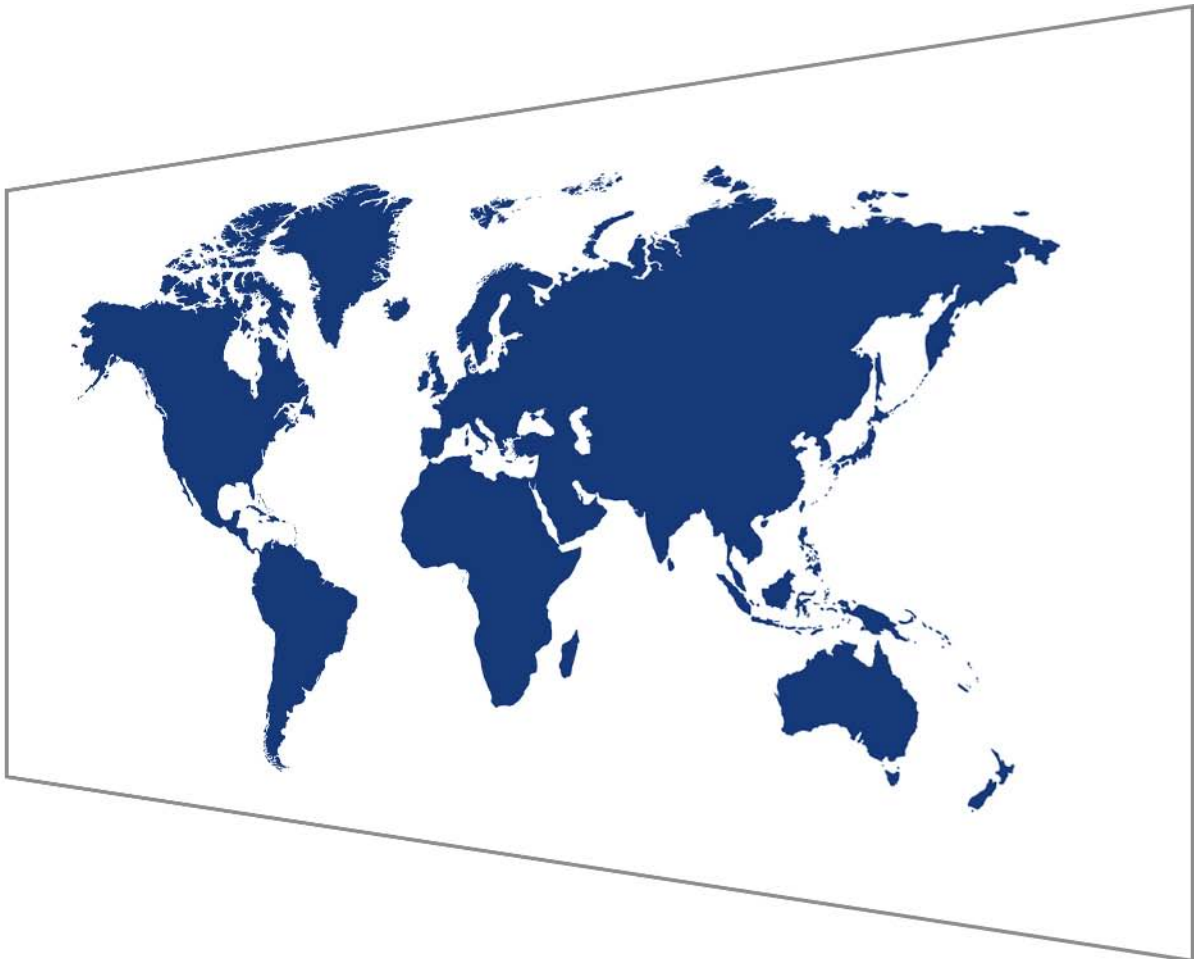


Bonas

Diamond Brokers & Consultants

Market Report

February 2010





Rough

DTC's price increases this month initially stunned some sight holders by their extent in some of the boxes, but they seemed to adapt pretty quickly. Only those in Botswana, where high labour charges and self-assessment requirements add extra pressures, remained visibly concerned by the raise.

Some of the froth on the rough market has evaporated as a result of the increase and of the second sight in quick succession. People are also very aware that current goods will emerge into a quiet polished period. DTC's publicized statement regarding price stability has had a further calming effect.

A smaller March sight is now expected by the market, which would help underpin the quiet market, though individually people want more goods.

ANTWERP

The reason for accepting DTC's price increase without much objection is that, in spite of the increase, premiums continued to be paid, albeit at a lower level. Secondly, there are few alternative rough sources around:

- BHP: often considered not attractive and pricing has perhaps gone too far
- Alrosa: often considered expensive, but cheaper than DTC after the premium
- Angola: apart from some Catoca, hardly any around
- Ad hoc tenders from various sides continue to fetch very high prices and are therefore unattractive to most manufacturers.

The official announcement from the DTC about price evolution in the last few months, and for the months to come, has certainly helped and given strength to polished price increases. At the same time though, retailers and jewellery manufacturers are putting their foot down, and after several months of continued increases, they seem to have drawn a line.

The market has become a bit nervy in its behaviour and we maintain our view that it is more important than usual to continue to look at polished performance in order to avoid a possible rough slump. After the February increase, manufacturers have seen their margins shrink sharply or even disappear, and those buying second hand are buying futures.

Mumbai

DTC's actions seem to have hit the mark as the mood in India remains positive, with fewer carats changing hands. Premiums in the Indian range of goods continue to be offered and vary from list (MB H -7+5), to single digits (Cubes -3gr+5, MB H 3gr+7), to double digits (MB -5+3, MB Low -7+5 etc).

For the secondary market, the recent price increase, with the added premiums, has made DTC goods very expensive. Buyers are finding better value in Russian goods, especially in the Rejections area. No wonder then, that a recent sale of Alrosa goods in India by DIL saw all the goods being sold out by early afternoon.

Concern remains that prices in both rough and polished have gone up too quickly, creating another potential bubble. However, all agree that the importance of the Indian market as a diamond hub has grown substantially since the economic downturn, and mining companies like Alrosa and DeBeers have both publicly acknowledged that India's share in the rough market will grow even further this year. This comes on the back of January import figures for rough diamonds which show a 302% y-o-y growth.



Tel-Aviv

The local rough market has cooled significantly since the February sight. This is due to:

1. The second consecutive sight larger than \$500m
2. Only 8 weeks between the first 3 sights of the year
3. The polished market traditionally being relatively quiet between Pesach and August
4. Far fewer Indians here shopping for rough
5. The DTC's official announcement on prices and stability reducing speculation.

Some manufacturers prefer to buy Russian goods at the moment - even second-hand - as they see better value. That said, there are very few alternatives to DTC or Russian goods on the market.

It appears demand as well as prices for rough will remain relatively stable in the coming months with some expecting a small correction in 1-2 months.

New York

The DTC's announcement of the price increase this month was expected to put a stop to the wild speculation and high premiums on boxes, but it didn't pan out that way. Premiums on most articles before the announcement were well into double digits; after the announcement they fell back to 5-7%, but increased again by the end of the week. Polished demand is stronger, but even with the state of the diamond market much improved it certainly doesn't seem to warrant such frenzied buying of rough.

South Africa

The market is pretty hot as witnessed by the increasing demand for rough. Recent rough price increases have done very little to slow down demand. Even at the prices rough boxes were sold during the February sight, non-sightholders are sometimes still prepared to pay double digit premiums to lay their hands on DTC boxes.

Equally, attendance at most tenders has peaked at over 150 attendees - more than 80% of these being overseas players. As a result, South African beneficiaries feel at a huge disadvantage. Diamantaires in producer countries are calling for a proper supplier to the secondary market where anyone with the financial capability can buy rough at stable prices to feed their factories.

South Africa has announced that it will be increasing electricity charges by roughly 25% every year for the next 3 years.



Polished

ANTWERP

Polished feedback from traders ranges from slow to “on a strong footing”, depending on what type of goods and price expectations. Polished business today is directly related to price; those who ask 1 to 3% more compared to last month can move goods, others who want to fetch an extra 4 to 6% are forced to refuse sales or give in on price. It is very clear; polished prices cannot follow the current rough price increases. On top of that, in many cases it is the first time - after months of inaction - traders see their clients again and we’re also entering a traditionally quiet trading period. Most people are now waiting for the upcoming shows to see what direction polished is taking.

People suffered a lot on inventory last year. As a result of that, the whole market today is stock-shy. Buyers buy a lot more selectively and in much lower volumes than they used to. There is overall good demand for VS-SI quality in all sizes. Most people feel there is still a lot of polished on the market, mainly in large and small cleanish. At the same time, there are shortages appearing in a few areas, such as 4gr and 6gr, VS-SI quality. Piqué quality seems to have reached its limit, mainly due to a wider choice of goods now being available on the market. More polished is expected to come to the market in the next few weeks and months.

Traders continue to try to sell only to customers with a good record. Payment terms have shortened from 90 days pre-crisis to 30 - 60 days now.

TEL-AVIV

Demand for polished is reasonably good with retailers restocking after the season, although things have slowed a little of late. Sales are still far from pre-crisis levels but compared to last year no one is complaining.


Prices are a little bit higher for products in demand. Mainly rounds from 0.25 – 1.90 ct. Some of these items are very close to pre-crisis levels. However, in the weaker areas, they are still up to 20% off, for example 3+ cts (weak demand) and 2 caraters (mediocre demand). Despite a moderate improvement in prices and higher turnovers, the increases in rough prices have significantly reduced profitability.

Demand is coming from all over: America, Asia, and Europe. HK/China is experimenting with polished products they didn’t traditionally buy such as fancies, lower colours and clarities.

Many Israeli companies are preparing for the March HK show with the largest delegation to date. The feeling is that the Israelis will be sending a lot of polished.

MUMBAI

With no major event coming up on the diamantaire calendar after the Hong Kong fair in March, the Indian market seems to be slowing down slightly. Payment terms, which were 30 days or cash, are also starting to become more flexible. The large volumes that were transacted both in polished and rough have eased considerably. Wholesalers are anticipating polished from the December and January sights to come on to the market in March. As these were bought at higher prices, the market expects polished prices to go up further, but is simultaneously worried about lower demand and price resistance.



Demand continues for caraters, though battles rage over prices. Good demand for 2pc in SI clarity and down. Naats, silver, and browns also moving well.

NEW YORK

Reports from most American retailers contained better than expected results from the holiday season, and with retailers selling from a very low stock position, there is buying activity. 4grs and up in better goods, especially in top makes, are in very short supply and gobbled up by the market at ever increasing prices. An improvement in demand for large stones (4+ct) is partly fuelled by Rapaport's increases in the list. Strong demand for 1-2 ct rounds in better colours/claritys/makes. What a change in mood from last year! All eyes are now on Hong Kong and with Far Eastern demand being extremely strong all are expecting good things from the show.

HONG KONG

In February the Hang Seng index reached a six month low at just over 19,000 points and down from a November high of nearly 23,000 points. The Hong Kong government is concerned by the overheating economy and property market. Property prices surged by 28 percent overall in 2009. As in many other countries there is a worry about inflation and more and more banks are holding back on lending. Above all, the government would like the economy to be stable.

On March 5th a new five day HK Watch and Jewellery Fair will start. It is the first one after Chinese New Year and it will be a test for new polished prices. The other thing that people will be watching is whether the seriously bruised and battered jewellery manufacturing industry will be able to make its come back this year. The advantage of a cheap currency (pegged to the US\$) is now slowly fading.

Caraters in DE colours in VS2+ clarity (and even some SI) continue to move well though there is price resistance. 0.50+ cts with GIA certs also moving well for HK and China.




Retail

EUROPE

While the mood in polished is markedly more hopeful, people at jewellery retail level need more evidence to believe that the market is on a recovery path. Although signs of improvement have appeared recently, recovery and confidence remain uncertain and fragile, not helped by the shaky state of some European economies.

Overall demand for jewellery in Europe remains weak and people expect it to only pick up from the summer onwards. There is some purchasing activity but it is mainly to fill gaps. Buyers are very cautious and refuse to buy big quantities or try new things. The weakening € doesn't help their buying power. Diamond jewellery is performing slightly better than plain gold items. In the higher price points, consumers prefer classically styled jewellery as it preserves value.

People report good activity at the recent Inhorgenta show in Germany. The situation in Switzerland remains difficult; traders report the market is improving a little bit but volumes remain very low and so are the prices they are prepared to pay. No demand has been seen from watch contract manufacturers yet.



Swatch Group's management mentioned an "excellent start in 2010" and "increasing order entries". The group feels that its decision to maintain production capacities throughout the downturn (no lay-offs) will position them very well to take advantage of the recovery in demand in coming months.

Payments in Italy are said to be very difficult to collect. Damiani enjoyed a marked improvement of trading environment in December. It is expected that the brand will report in March a loss of about €3m at operating income level. The positive swing is expected for March 2011. Bulgari said 2010 had started well and would prove a better year than 2009. Sales at its own stores rose 12% in the first three weeks of January, continuing the trend seen in the last quarter. Bulgari's Q4 revenue fell 5.1% (€297m) and full-year revenue fell 13.8% (€926.5m).

USA

Centurion announced its 9th jewellery show, at Tucson, Arizona, saw attendance up 14%. Despite more selective invitations, 206 retailers were present and exhibitors reported positive sales.

Zale Corp released its results for the accounting quarter finishing Jan 31st. It reported a profit of \$6.7 million, compared with a loss of \$31.8 million in the equivalent period last year, Zale's first quarterly profit in two years. Revenues were down 14.3% at \$582 million, compared to \$679 million the previous year. Same store sales decreased 11.2 percent.

Rumours emerged in the Wall Street Journal that a number of private equity firms were looking to buy stakes in the troubled retailer. The *WSJ* reported that private-equity firm Apollo Management have submitted a proposal which, if approved, would see Apollo installing its own management team, headed by former Zale chief executive Robert DiNicola. The *WSJ* went on to say that private-equity firm Centerbridge Partners LP and Gordon Brothers Group, a Boston-based financial firm had also both declared interest.

Meanwhile Zale Corp. announced that it had hired independent investment banking advisory firm Peter J. Solomon Company, as advisors.

Blue Nile Inc. reported fourth quarter revenues, up 20% at \$102.9 million. The full year's results, were about flat at \$302.1 million, up 2.3% over from 2008. Profit for the quarter was \$5.4 million, up 54.6% year on year.


Birks & Mayors Inc. reported \$89.3 million turnover for the quarter ending Dec 26th, up 1% on the previous year.

Hearts on Fire will withdraw from more than 120 underperforming stores, the diamond brand announced. The company justified its decision by quoting a need "to consolidate and strengthen its family of independent retail jewelers."

HONG KONG AND CHINA

It is really too early to draw conclusions about retail sales for Chinese New Year. At the moment there is little polished activity and real business will not resume until March 1st. Equally, some factories re-opened on the 24th of February, but certainly not all.

Therefore, mixed messages at the moment: some saying business up 15-20%, but that obviously compares to a low in 2009. Also, when people say business is up, we should look at organic growth, since most of them have expanded their retail network substantially! A remark



we keep hearing is that volumes were somewhat disappointing because there were two events on one day: CNY and Valentine's Day.

The other thing is that retailers are now trying to pin down vendors to six month contracts, in which period they are not allowed to increase prices further. Some accept, some don't.

The upcoming HK show will tell us how much appetite Chinese retailers have at the start of the year of the Tiger.

INDIA

The growing middle classes of India, many of who aspired to diamonds are now buying them on the back of very high gold prices. Backed by a healthy economy and changing tastes, India's diamond retail business is expected to grow by 30% to touch US\$6 billion in financial year 2011.



Free subscription

If you wish to receive Bonas Monthly Report for free, please email us at subscribe@bonasgroup.com, stating the following details:

- Surname and name of individual(s)
- Company name
- Country of residence
- Email address
- Segment in the diamond pipeline
 - o Rough mining
 - o Bank and finance
 - o Diamantaire (rough trading, manufacturing, polished distribution)
 - o Manufacturing technology supplier
 - o Jewellery manufacturing
 - o Retailer and brand
 - o Governmental and non-governmental body
 - o Consulting
 - o Other (please specify)

If you wish to unsubscribe, please email us at unsubscribe@bonasgroup.com.



About Bonas

Bonas is a 140-year-old diamond broking and consulting firm represented in every trading centre. Bonas is a member of the Responsible Jewellery Council and provides industry-focussed services, which reflect a shared knowledge of the diamond pipeline and its business environment.

For more information about our company and services, please visit us at:

www.bonasgroup.com.

DISCLAIMER

The information contained in this report has been compiled by the different affiliates of the Bonas group from sources believed to be reliable, but no representation or warranty, express or implied, is made by Bonas, its affiliates or any other person as to its accuracy, completeness or correctness. All opinions and estimates contained in this report constitute Bonas judgment as of the date of this report, are subject to change without notice and are provided in good faith but without legal responsibility. Nothing in this report constitutes legal, accounting, tax or investment advice.

This material is prepared for general circulation and has been prepared without regard to the individual financial circumstances and objectives of persons who receive it. No matter contained in this document may be reproduced or copied by any means without the prior consent of Bonas.