6-1-1986

A Study Of Diamond Investments

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A STUDY OF DIAMOND INVESTMENTS

by

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Bachelor of Science, Oklahoma State University, 1977

An Independent Study

Submitted to the Graduate Faculty of

The University of North Dakota

in partial fulfillment of the requirements

for the degree of

Master of Business Administration

The University of North Dakota Graduate Center

June
1986

This independent study submitted by James T. Burton in partial fulfillment of the requirements for the Degree of Master of Business Administration from the University of North Dakota is hereby approved by the Faculty Advisor under whom the work has been done. This independent study meets the standards for appearance and conforms to the style and format requirements of the Graduate School of the University of North Dakota.

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ACKNOWLEDGMENTS

I am indebted to the entire faculty and staff of the Graduate Center of the University of North Dakota at Minot Air Force Base North Dakota for their support and encouragement, not only in the accomplishment of this study, but in the satisfaction of all requirements for the Master's degree.

I wish to acknowledge the understanding and moral support of my children, Christopher B. Burton and Faith L. Burton while accomplishing this paper.

ABSTRACT

A Study of Diamond Investments

James T. Burton, B.S.

The University of North Dakota Graduate Center, 1986

Faculty Advisor: Dr. R.A. Bertsch

This paper studies the feasibility of investing in diamonds in today's market. It evaluates the source of diamonds and their historical value. Next an analysis of price trends, rate of return, supply and demand, and advantages and disadvantages are made. Then an analysis of the potential to include diamond in trust portfolios and IRA'S is accomplished. Conclusions are drawn on the feasibility of individual and portfolio investment of diamonds.

CHAPTER I

INTRODUCTION

Purpose

Investing is a multi-billion dollar business. It is a business participated in by millions of people, from the sophisticated managers of five hundred million dollar funds and trust accounts to a host of individuals working at their daily tasks who have accumulated funds beyond their everyday requirements who regularly make investments.

In today's investment market there are many vehicles investors can use to meet their financial goals. Traditional standards have, been stocks, and bonds but what of the alternatives? The purpose of this paper is to educate the common investor on one of the alternatives, diamonds.

The Problem

Are diamonds a viable investment vehicle in today's market?

Justification

Thousands of investors invest in diamonds but millions have no knowledge of diamonds or of their market to make an educated decision to invest. This study will answer the question on the advisability of investing in diamonds.

Scope

This study will discuss diamonds as an investment alternative for both the individual and institutional investor. Only investment grade diamonds of between one and two carats with a color range of D-H will be discussed as to their characteristics, price trends, rate of return and investment potential. All diamonds outside this range will only be mentioned briefly.

Limitations of the Study

As in other studies of this type, its orientation is conditioned by the accessibility of data relevant to the industry. There is an abundance of data prior to 1983 but in the years immediately following data became more scarce.

Methodology

The methodology of the study is primarily empirical. In answering the problem this study will analyze market trends, supply and demand, and rate of return . In

addition diamonds in pension funds and IRA's will be analyzed as to their feasibility.

Summary of Chapter 1

In this Chapter I have stated the purpose of this study is to educate investors on an alternative to stocks and bonds, diamonds. In an attempt to satisfy this purpose this study will answer the question are diamonds a good investment in today's market? Reviewing the literature concerning the source of diamonds and their historical value will set the framework to analyze diamonds in terms of price trends, supply and demand, and rate of return. Finally pension funds and IRA accounts will be analyzed for diamond investment potential.

CHAPTER II

LITERATURE SURVEY

Source

Until the late nineteenth century, diamonds were found only in a few river beds in India and in the jungles of Brazil, and the entire world production of gem diamonds amounted to a few pounds a year. In 1870, however, huge diamond mines were discovered near the Orange River, in South Africa, where diamonds were soon being scooped out by the ton.[1] Suddenly, the market was deluged with diamonds. The British financiers who had organized the South African mines quickly realized that their investment was endangered; diamonds had little intrinsic value, and their price depended almost entirely on their scarcity. The financiers feared that when new mines were developed in South Africa, diamonds would become at best only semi-precious gems.[2]

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[1]Edward J. Epstein, The Rise and Fall of Diamonds, (New York: Simon and Schuster, 1982), pp. 66-70.

[2]Ibid.,p.72.

The major investors in the diamond mines realized that they had no alternative but to merge their interests into a single entity that would be powerful enough to control production and perpetuate the illusion of scarcity of diamonds.[3]

In 1888 De Beers Consolidated Mines, Ltd. was formed taking control of all aspects of the world diamond trade and assuming many forms. In London, it operated under the name of the Diamond Trading Company. In Israel, it was known as the Syndicate. In Europe, it was called the Central Selling Organization.[4]

For most of this century De Beers not only directly owned or controlled all diamond mines in southern Africa but also owned diamond trading companies in England, Portugal, Israel, Belgium, Holland, and Switzerland.[5] De Beers now owns about one third of the diamond mines in the world and has contracts to purchase the production of most others.[6] Even the uncut stones from the large mines of the Soviet Union and Australia filter through

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[3]Ibid., p. 73.

[4]T. Gregory, Ernest Oppenheimer and the Economic Development of Southern Africa, (London: Oxford University Press, 1962), p.35.

[5]Edward J. Epstein, "Have You Ever Tried to Sell a Diamond," Atlantic Monthly 249, February 1982, p.1.

[6]"Diamond Deal to Remain Secret," New York Times, January 20, 1960, p. 43.

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[6]"Diamond Deal to Remain Secret," New York Times, January 20, 1960, p. 43.

De Beers.[7] Diamond producers locate and mine diamond-bearing ores, develops extraction methods, cleans, grades, and sorts the rough stones. A diamond crystal in the state in which it is recovered from the earth is called a rough diamond or rough. Rough diamonds occur generally in two types of deposits: (1) in igneous rock masses of kimberlite known as pipes; and (2) in alluvial gravel, both inland and marine, into which they were washed from the Kimberlite through some volcanic action or underground pressure.

Recovery from Kimberlite rock or sea deposits require large scale mining processes, while from alluvial surface fields may be operated on a small scale and worked by individual diggers.[8] To recover just one carat weight (1/5 gram) of diamonds requires digging four tons of gravel from an underground mine, twenty tons from an open air mine.[9]

Figure 1 shows that seventy-five percent of all

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[7]Patrick J. Regan, "The Shattering of the Diamond Market," Financial Analysts Journal 37, July-August 1981, p. 15.

[8]P. Fisher, The Science of Gems, (New York: Charles Scribner's Sons, 1966), p. 115.

[9]S. Tolansky, The History and Use of Diamonds, (London: Methuen and Co., Ltd., 1962), p. 124.

Diamonds are mined in Australia, the Soviet Union, South Africa and Zaire.[10]

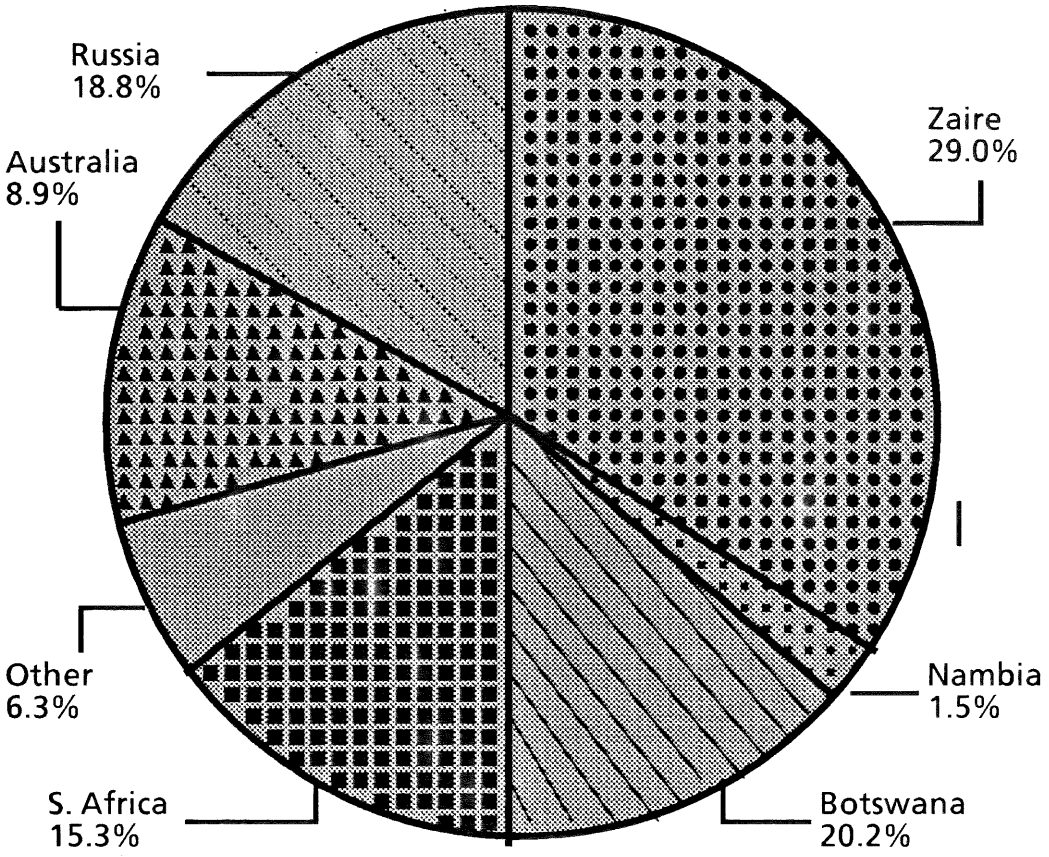

Fig. 1. Natural Diamond Production Percent Breakdown by Country, 1984 [11]

About 85 percent of all rough diamonds mined each year are sent to the Central Selling Organization. The CSO sells the rough diamonds at ten annual "sightings" in

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10 "Flawed, "Economist 296, 10 August 1985, p. 66.

11 Ibid., p.66.

London at non-negotiated "all or nothing" price to a select group of about two hundred and ten rough diamond brokers.[12]

The brokers then sell the diamonds via a club or bourse to diamond cutters, or polished diamond manufactures. Cutters then sell the cut and polished diamonds to dealers, exporters, jewelry manufactures or professional investors through diamond bourses.

There are fourteen bourses or exchanges in the world each containing a trading floor similar to a stock exchange where members buy and sell diamonds. Membership in these exchanges is by sponsorship only and is restricted to individuals who have proven integrity, financial qualifications and extensive diamond expertise. There are about ten thousand club members worldwide, including brokers, cutters, dealers, exporters, and importers, out of and industry that numbers in the hundreds of thousands.[13]

Jewelers and professional diamond investors buy and sell to club members, or commission members on their behalf. It is unusual, however, for bourse members to deal

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[12]S.Q. DellaGrotta, "Diamond Investments -- A Different Perspective," Pension World 17, March 1981, p. 20.

[13]Ibid,. p. 78.

directly with the general public.

Historical Value

Historically diamond values are determined by the "Four C's" of diamond buying: Carat, color, clarity, and cut. Carat is the measure used to designate weight of a diamond. The rarity of a diamond greatly increases with size, and shows a geometric progression of price to carat size. Carat weight of one-half to five carats are considered investment quality though stones between one and two carats are the most liquid because they represent an optimum combination of liquidity and investment appreciation. Large stones are less liquid, since the higher the value, the fewer the potential buyers.[14]

Color is actually the most important determinant of value. A colorless stone with no flaws may sell for more than 10 times the price of one with a yellowish tint. The most widely accepted color scale ranges from D, the purest and therefore the rarest, through Z. Investment diamonds are considered in the D-H range.[15]

Clarity is the degree to which a diamond is flawless. An imperfection may be an impurity or flaw inside the diamond (an inclusion) or a blemish on its surface.

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[14]Ibid., p. 19.

[15]Ibid., p. 20.

Each imperfection impedes the passage of light through the diamond thereby lessening the brilliance. Clarity grading is accomplished using a precision ten-power magnifying glass. If no flaws are visible the diamond is termed flawless. The scale ranges from Flawless (FL), to Imperfect (I3). Investment grade diamonds fall between FL and VS2.[16] Table 1 summarizes color and clarity scales.

Cut refers to the shape and proportion of the diamond. The cut enhances the beauty which increases the value. A round brilliant cut as described by the Federal Trade Commission regulations has fifty-eight facets polished (thirty-three on the crown and twenty-five on the pavilion) and is the most valuable. Other cuts may be used, such as oval and pear shape, to increase the 11weight of the finished diamond.[17] Figure 2 shows a clear picture of cut and the dimensions of diamonds.

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[16]Ibid., p.20.

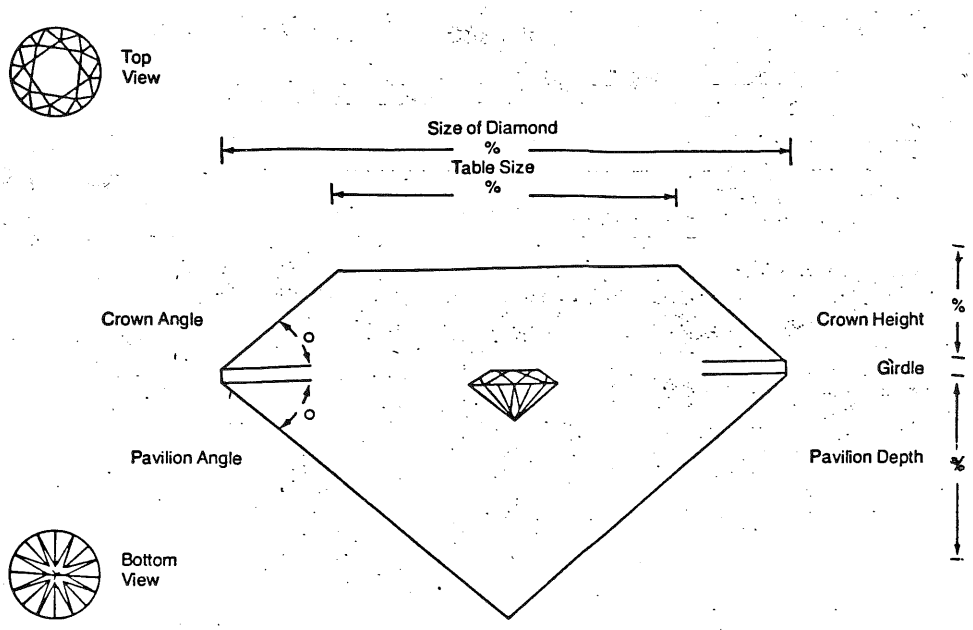
[17]Ibid., p.20.

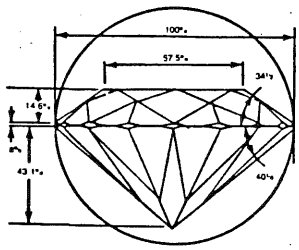
TABLE I

COLOR AND CLARITY GRADING SCALE

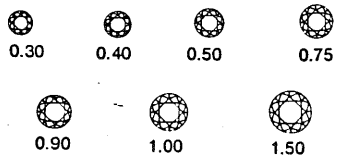
COLOR		CLASSIFICATION	CLARITY	
Exceptional white +	D	Investment Quality	Flawless	FL
Exceptional white	E		Internally Flawless	IF
Rare white +	F		Very, very slight Inclusion	VVS_1 VVS_2
Rare white	G		Very slight Inclusion	VS_1 VS_2
White	H			
Slightly Tinted White	I J	Better Gems	Slightly Imperfect	SI_1
Tinted White	K L	Better Gems	Slightly	SI_1
Tinted Color 1	M N	Fine Jewelry	Slightly	SI_2 I_1
Tinted Color 2	O P	Typical Jewelry	Imperfect	I_1 I_2
Tinted Color 3	Q R	Typical Jewelry	Imperfect	I_1 I_2
Tinted Color 4	S-Z	Jewelry/ Industrial	Imperfect	I_3

SOURCE: S.W. DellaGrotta, "Diamond Investments -- A Different Perspective," Pension World 17,March 1981, p.20.





THE SCAN. D.N. STANDARD CUT
The diagram shows the proportions a modern, well-cut diamond should have.



This illustration shows the sizes of stones of varying weights.

Popular Diamond Shapes

Brilliant — the round diamond that is a favorite in engagement rings. In tiny sizes, with only 16 facets, this shape is called a single cut and is used as a side stone in rings.

Emerald Cut — so-called because emeralds are cut this way, rectangular or square, with facets polished diagonally across the corners.

Marquise — pointed boat-shape, usually long and narrow. In a ring, it tends to make fingers look slim. This shape costs slightly more than a brilliant of the same size and quality because of additional labor in cutting.

Pear Shape — popular in rings and often used in pendants. The world's largest cut diamond, Cullinan I, mounted in the British Royal Sceptre, is pear shaped.

Oval — adaption of the brilliant shape. The marquise, pear shape and oval all appear to be larger than a brilliant of the same carat weight.

Baguette — means "little stick"; a small diamond used as a side stone in rings.

Fig. 2. Diamond Shapes and Cuts[18]

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[18]Ibid., p. 20.

CHAPTER III

ANALYSIS OF PROBLEM

Market Trends

The dimension of time is important when analyzing any organization or product line.[1]

Historically, diamond prices have risen and fallen due to such factors as the discovery of new diamond deposits, fluctuations in demand and changes in the diamond industry. Investment grade diamonds have generally increased in value from 1905 to 1976. Figure 3 shows a dramatic increase over time of investment grade diamonds having continued with few exceptions, to advance upward in price every year since the depression. Diamonds have faired better than both the Dow Jones Industrial Average and gold another tangible asset by a considerable margin.

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[1]J. Fred Weston and E. F. Brigham, Managerial Finance , 5th ed., (Illinois: Dryden Press, 1979), p. 77.

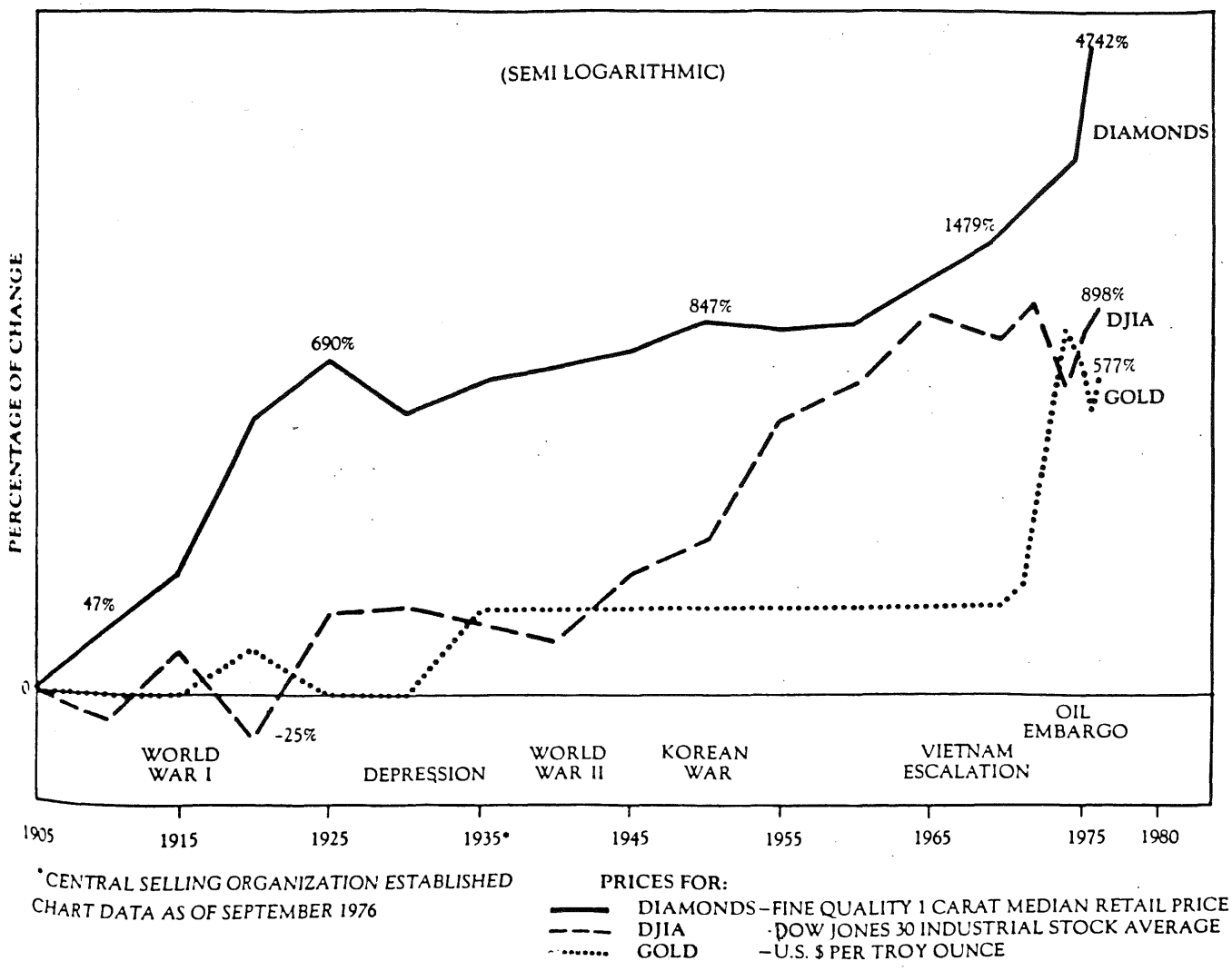

Fig. 3. Historical Values[2]

2Stanley Urlaub and S. Q. DellaGrotta, "Are Diamonds Your Estate's Best Friend?," Trusts & Estates, September 1978, p. 524.

In the late 1970's roaring inflation prompted nervous investors, disgusted with paper money, to flock in unprecedented numbers to such tangible assets as gold, silver, and diamonds. By early 1980 the price of a one-carat D-flawless diamond, the benchmark of quality in the trade, had double in one months time to sixty-two thousand dollars. Then interest rates sky rocketed and the bottom fell out of the market. Investors yanked money out of hard assets and poured it into money funds. The price of the D-flawless plummeted in late 1980 to eight thousand dollars.[3] Prices started to rise as interest rates came down and the D-flawless regained some of its loss and is now selling for approximately fourteen thousand dollars.[4]

Supply and Demand

It is common knowledge that supply and demand influence prices. In the diamond market De Beers is in control of supply and has "manufactured" demand. Only one percent of the total world diamond production is of investment quality with the rest going for industrial

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[3]"Flawed," Economist 296, 10 August 1985, p. 66.

[4]"Why the Diamond Market is Still in the Rough," Business Week, 30 July 1984, p. 100.

purposes and jewelry.[5] George Sweitzer, director of the Smithsonian Institutions Department of Mineral Sciences says "...the supply of newly mined diamonds could dwindle to nothing within the next fifty years."[6]

As mentioned in Chapter II, De Beers owns about a third of the worlds diamond mines and has contracts to purchase the product of most others. De Beers has maintained an iron grip on supplies by serving as the middle man between the world's diamond producers and dealers. Through its management of the Central Selling Organization De Beers controls between eighty to eighty-five percent of the worlds diamond market.[7] The purpose of the CSO is to regulate both the supply and price of rough diamonds to compensate for inflation and to insure a steady increase in diamond values. If any country could upset the carefully orchestrated ebb and flow of diamonds, it would be the Soviet Union. As the second largest producer of gem diamonds, after South Africa, the Russians could, if they chose, involve De Beers in a price war by flooding the market. However this would

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[5]"De Beers Again Cuts Diamond Supplies to Bolster Market," Wall Street Journal, 23 March 1981, col. 1, p. 27.

[6]George Adcock, "A New Appraisal for Estate Planners," Trusts & Estates 119, January 1980, p. 53.

[7]"The Diamond's Best Friend," Forbes 130, 2 August 1982, p. 10.

seem unlikely because of the foreign currency it depends upon from the diamond industry.

The CSO controls supply at each of its annual ten sights where it chooses what stones are to be sold and assign a price to each box. The sightholder must accept or reject the entire box; he may not haggle over cost. If the dialer doesn't buy, he risks not being asked back to the next sight. Thus, De Beers parcels out diamonds in a way that almost assures supply will never exceed its own perception of demand thus simplifying its task of maintaining prices. With its control of production and distribution, the only element that is not directly controllable is demand.

In the late 1930's De Beers enlisted the advertising agency of N. W. Ayer, which embarked on a multi-billion dollar campaign that has span decades, institutionalizing diamonds as a symbol for the marital pledge and everlasting love.[8] De Beers pitch, "Diamonds are Forever," immortalizes diamonds as a prized possession which no proud owner would dream of parting with and effectively inhibited the public from reselling them. De Beers' U.S. strategy was so successful at creating demand and keeping a strong resale market from developing

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[8]Edward J. Epstein, "Have You Ever Tried to Sell a Diamond,"Atlantic Monthly 249, February 1982, p. 25.

that Japan was invaded with advertisements. In the 1960's only about five percent of Japanese women received engagement rings. In the early 1980's nearly sixty percent of all Japanese engagements were sealed with a ring.[9]

De Beers is also waging a successful campaign in the U.S. to get men to renew their commitment to their wives in later years, with more diamonds and are also marketing to men themselves.[10]

In the late 1970's speculators entered the market and De Beers temporarily lost control of supply. The speculative binge had begun in Tel Aviv, where banks had lent diamond cutters huge sums of money at low interest rates to encourage the diamond industry, the country's major source of foreign currency.[11] The cheap money tempted dealers to buy and hoard virtual mountains of diamonds. The fever spread to cutting centers in New York and Antwerp. Dealers began to openly flaunt De Beers' commandment "Thou shalt not speculate," by reselling the gems CSO released to the highest bidders . Ultimately,

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[9]Ibid., p. 26.

[10] "De Beers Digs Deep to Mine New Markets," Marketing & Media Decisions 16, March 1981, p. 69.

[11]Peter W. Bernstein, "De Beers and the Diamond Debacle," Fortune 42, 6 September 1982, p. 48.

many of these diamonds were stashed in people's vaults, all of them beyond the cartel's control.

De Beers first tried to cool the speculation by flooding the market with stones. But speculators kept buying and prices kept rising. Each new stone the CSO sold diminished De Beer's leverage over the trade. Despite the enormous profits it was raking in De Beers moved to squelch the speculation by slapping a forty percent surcharge on sight boxes. The surcharge could quickly be applied to all producers. It checked speculation once dealers knew the surcharge could be as quickly removed in effect bringing prices back down. In five months the surcharge was removed. Prices on small stones dropped the larger ones continued to rise. Then De Beers make a mistake and started raising prices until the bottom dropped out. Manufactures and dealers were left with large inventories of fine diamonds. Many Israeli firms went bankrupt leaving banks with the stones who, in turn threatened to dump the stones onto the already depressed market.

Holding fast to its policy of not cutting prices, De Beers began to reduce production and started buying the loose diamond stockpiles. Even at depressed prices the firms diamond inventory went form three hundred sixty

million dollars in 1979 to over two billion dollars in 1983.[12] If De Beers had not withheld inventories, diamond prices would have plummeted even more than they did and the "diamonds are forever" ad line would have been laughable.[13] It is now apparent that De Beers is back in control and supply and demand have stabilized. With increased advertizing De Beers hopes to increase demand for its diamonds.

Rate of Return

Unlike stocks and bank accounts diamonds do not pay dividends, the profit from investment is derived from three factors: (1) the difference between the initial cost and the resale price, as determined by (2) the length of time the stone is held multiplied by the yearly increase in value, minus (3) resale commissions and other sales costs and taxes. In other words profits are capital gains not income.

In 1973 a one-carat D-flawless diamond was priced at approximately two thousand dollars in 1985 it was worth fourteen thousand dollars.[14] This change represents a

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[12]"Flawed," Economist 296, 10 August 1985, p.66.

[13]Dennis Chase, "De Beers Changes Ad Tack," Advertising Age 54, 18 July 1983, p. 43.

[14]Neil Behrmann, "Diamond Sales Slump Has Touched Off Dealer Bankruptcies, Losses for Lenders," Wall Street Journal, 4 February 1985, col. 1, p. 35.

three hundred and fifty percent increase over a twelve year period or a twenty-nine percent annual return on investment before capital gains tax and commissions. Before the crash diamonds went up to sixty -five thousand dollars. If an investor had bought in 1974 and sold in early 1980 he would have had a total appreciation of sixteen hundred twenty-five percent.

Trust Portfolios

Sound financial planning generally directs wealth into three kinds of investments: Highly liquid assets, store of value assets and speculative assets. Liquid assets provide cash reserves available for emergencies and other expenses. At the other extreme, speculative investments such as commodities contracts are designed to provide large profits within an expected high degree of risk. Store value assets such as real estate are intended to provide protection of total wealth against inflation, currency devaluation, and taxation.[15]

The Employee Retirement Income Security Act of 1974 (ERISA) has imposed upon trust administrators a strict

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[15]Stanley Urlaub and S. Q. DellaGrotta, "Are Diamonds Your Estate's Best Friend?," Trusts & Estates, September 1978, p. 523.

standard of conduct.[16] Trust managers have been tempered by ERISA and their objective is to arrange a portfolio in a way to reserve capital investments and obtain a better-than-average performance by manipulating the three types of assets to achieve the proper mix.

In order to accomplish this managers must determine the long and short-term needs of a trust account and set realistic and attainable goals. It includes the efforts of diligent identification, analytical research, and prudent qualification of all possible investment vehicles, and the blending and portfolio balance of their complimentary characteristics.[17]

For many years, trust administrators have dealt primarily in stocks and bonds. Only since the late 1970's did they consider other types of investments such as real estate and diamonds. It would appear that store value investments that would stabilize the portfolio, provide asset protection, and consider tax implications would be in demand. Tax implication usually means to minimize taxes as much as possible. Often overlooked is

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[16]S. Q. DellaGrotta, "Diamond Investments -- A Different Perspective," Pension World 17, March 1981, p. 19.

[17]Stanley Urlaub and S. Q. DellaGrotta, "Are Diamonds Your Estate's Best Friend?'" Trusts & Estates, September 1978, p. 526.

the fact that financial assets such as bonds and stocks produce interest and dividends which are taxed as income with capital gains payable on the transfer. Diamonds do not produce income but are for the long term to take advantage of capital appreciation. Consequently, investment diamonds are a natural inclusion in a portfolio of long-range goals and preservation of assets.

Managers have often overlooked diamonds as an investment alternative because they did not have the necessary skills for evaluating investment gems and also lacked reliable information sources and reliable channels for acquisition and sales.[18] To become knowledgeable the trust manager could study the market by extensive reading, contacting diamond experts and dealers for their knowledge. This path would take months if not longer to become knowledgeable enough to make sound decisions. An alternative is to hire a professional diamond investment advisor who is trained on the value, quality and liquidity of diamonds. He buys at the bourse or from a cutter's inventory at the lowest prices and is able to liquidate at any level in the diamond industry (the closer the the retail level, the greater the profit). His income is normally derived from a negotiated fee

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[18]Ibid., p.523.

schedule or for actual services rendered.[19] To keep abreast of prices the trust manager should consult the Precious Stone Newsletter, Diamond Registry Bulletin, Jewelers' Circular Keystone, National Jeweler, and diamond dealer offerings in the Wall Street Journal.[20] Several wire services are also available but all of these are price guides only, actual valuations should be based on last transaction at the cutter's bourse.[21]

Individual Retirement Accounts

Individual Retirement Accounts (IRA'S) are set up to provide a retirement nest egg and to defer taxes until an investor is in a lower tax bracket. In early 1979 some banks across the country allowed diamonds to become part of IRA's as a hedge against inflation.[22] Other refused to allow diamonds as part of their clients accounts because "self directed accounts are labor intensive and that tangible assets like diamonds do not readily fit

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[19]S. Q. DellaGrotta, "Diamond Investments -- A Different Perspective," Pension World 17, March 1981, p. 23.

[20]Ibid., p. 26.

[21]Ibid., p. 26.

[22]"No IRA Now," Wall Street Journal , 5 August 1981, col. 5, p. 1.

into accounting techniques developed for financial instruments."[23]

This is a mute point since as of December 31, 1981 the Economic Recovery Act of 1981 became effective. Section 314 (b) of the Act prohibits investment in tangible and collectible items such as diamonds in self-directed plans such as IRA's and Keogh's.[24]

Advantages

Diamonds have been a haven for wealth for many decades. As shown in Chapter III diamonds have preserved wealth in economic upheaval (inflation) and social disorder.

Diamonds can be liquidated at a desired rate without damaging the over all investment. Unlike a group of rare coins which could destroy the overall value.

Diamonds are portable weighing next to nothing and are easy to transport for selling or other needs. A small handful could be worth a fortune but require no special storage facilities.

The world is the market for diamonds. If the market is poor for diamonds in one region then the potential

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[23]"Diamonds Cut a Path into Retirement Plans," Business Week, 16 April 1979, p. 30.

[24]Joel E. Arem, "Gemstones as Investment Vehicles Are Often Part of an Estate," Trusts & Estates, February 1982, p. 85.

exists that other world markets would be better.

Tax advantages over stocks and bonds exist in that only capital gains tax at liquidation is applicable. Also tax provisions exist in tax law that allow for the deduction of the current appreciated value of diamonds as charitable contributions.[25]

The rate of return on a diamond has historically been high with low associated risk with the only real exception occurring in the late 1970's and early 1980's during the speculative diamond years.

De Beers keeps tight reign over diamond supply in the market and overall diamond supplies are dwindling. This should assure prices continue to climb due to the scarcity of diamonds.

Demand for investment grade diamonds, though currently depressed will continue to rise through renewed marketing efforts by De Beers

Disadvantages

Limited data on current day-to-day prices hinder the common investor. Fund managers have a greater access to information because of their diamond investment advisors

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[25]The Week in Review, June 1980, cited by, "Investing in Gems," CPA Journal 51, (March 1981): 10.

and computer price listings.

It takes an expert to deal effectively in the diamond market unlike stocks where the buyer has internal data concerning the company whose shares he is buying.

Diamonds can't be used in IRA accounts thereby closing one avenue to the common investor.

Investment grade diamonds are much more expensive than many individual investors can afford with prices ranging from two thousand dollars to fourteen thousand dollars in today's market.[26]

Markups at point of sale and commissions could add up to thirty percent to the cost of sale making diamond investments a long term proposition.

Of the hundreds of companies that were formed in the speculative years to buy and sell diamonds only a few exist today. The individual investor has only a limited access for acquisition and sales of diamonds.

Diamonds are not liquid. It takes a minimum of two weeks from the date a transaction is initiated if the seller has "inside" connections.

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[26]Neil Behrmann, "Diamond Sales Slump Has Touched Off Dealer Bankruptcies, Losses for Lenders," Wall Street Journal, 4 February 1985, col. 1, p. 35.

CHAPTER IV

CONCLUSIONS

Are diamonds a viable investment vehicle in today's market?

Conclusions

Diamond investment is a risky business and is not a viable investment vehicle for the individual investor. The individual investor does not have the expertise nor the resources to fair well in the diamond market. The individual has little choice but to buy at retail and sell at wholesale or below and normally only through the company he purchased them from. The old problem of unscrupulous companies which were abundant during the speculative years have been dealt a blow by the Federal Trade Commission which in 1981 issued a consent order which made the full and fair disclosure mandate of securities laws applicable to the diamond industry. This in effect minimized the potential for misrepresentation

which had been taking place in the industry.[1] Only investors with expertise in the field of diamonds should attempt to invest.

Diamonds can be a viable investment when included in a trust fund portfolio. Supply and demand factors are favorable for long-term investment with a high rate of return at small risk, appreciation of capital and tax advantages.

Prior to investing a decision should be made by the trust manager or diamond investment advisor as to what percentage of a portfolio should be assigned to diamonds. This will depend on overall investment objectives. Many experts conclude that not more than twenty percent of a portfolio should be comprised of diamonds.[2]

Diamond investment should meet long-term requirements (at least five years) and should be liquidated only when cash is needed to meet benefits or rolled over to pyramid their investment values. Diversification is also important and should be based on

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[1]S. Q. Della Grotta, "Diamond Investments -- A Different Perspective," Pension World 17, March 1981, p. 26.

[2]David E. Robbins and Joseph H. Abramoff, "Government Sets Guidelines for Gemstone Investing," Pension World 18, February 1982, p. 19.

the four C's of diamond investing as explained in Chapter II.

The following guidelines should be followed:

(1) Always obtain a written agreement and warranties regarding cost of services, standards of quality and terms of payment.

(2) Insure the diamond portfolio against theft.

(3) store diamonds at a financial institution near a diamond bourse for market accessibility and maximum liquidity.

(4) Verify authenticity with the GIA or EGL laboratory certificate. The certificate should have a registry number over an authorized signature. The second document should be a gem print which is a laser photograph which captures the reflection and refraction pattern of a diamond, and since not two are alike it precisely identifies the diamond.[3] A new method of identification is inscribing the GIA grading report number on the outer edge of the diamond with a laser. GIA developed this method and it has no effect on the

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[3]S. Q. DellaGrotta, "Diamond Investments -- A Different Perspective," Pension World 17, March 1981, p. 27.

color or clarity grading.[4]

(5) Gain access to diamond experts who are in regular and frequent contact with the diamond industry and market for information and sales.

(6) Obtain regular information about the diamond industry prices of the portfolio.

(7) Stay abreast of developments that could affect investment objectives such as changes in demand, supply, price, or industry structure.[5]

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[4]Ibid., p. 24.

[5]"New Gem Inscription Offers Security to Owners," National Underwriter, 13 May 1983, p. 8.

APPENDICES

APPENDIX A

Terminology Used In Paper

Alluvial gravel - rock formed by volcanic activity

Bourse - a diamond exchange

Cutter - a person who cuts and polishes rough diamonds

Igneous rock - combination of sand, gravel, clay, and other materials

Liquidity - ability to convert diamonds to cash

Rough - an uncut and unpolished diamond

sightholder - a diamond broker invited to one of the ten annual sightings

Sightings - gathering of diamond brokers invited by CSO to purchase rough diamonds

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