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Value Creation and Sustainable Profitability in the  
Diamond Industry: Ingredients of a Successful Diamond  
Manufacturing Business  
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Ladies and Gentlemen,

It is my pleasure and honour to be here today and talk to you about running a successful diamond manufacturing business, a topic I am passionate about.

Our industry has seen tremendous change in the last five years and is likely to continue to change in the years to come. With change come challenges and opportunities; and some of these, such as: compliance and the threat of substitute products such as synthetics, are close to my heart and deserve the necessary attention, but are not part of my short presentation today.

The global diamond jewellery market has grown to some \$67bn, the environment we all operate in has become extremely competitive and most manufacturers have seen margins shrink.

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The coloured cubes on the slide tell you that the big margins are not being made at the manufacturers' level of the diamond pipeline.

Many of us tend to focus too much on trading and cost reduction in our own organisation, not to mention the fact that a diamantaire often has the tendency to blame everyone else but himself.

The real problem is - and that is exactly the topic of my presentation today - is that people don't pay enough attention to value addition. What I hope to illustrate to you today is that, with more focus on how we add value, comes better margins in a sustainable way.

So looking at some of the challenges today, we see that for a manufacturer obviously SOURCING is very important. Being able to rely on one or more sources for regular and consistent intake of rough is key for any manufacturing business.

The second important thing is of course at which PRICES we can buy from these sources, and that's when we are struck by an interesting phenomenon: rough diamonds often (and certainly over the last 3 years) command a premium, whereas the polished - coming from the same rough - don't fetch that premium and are subject to severe price

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competition. Indeed, polished and rough markets are often NOT in sync with each other. Why is that?

Surely at a producer level there is concentration in a few hands only, which creates the abstract feeling of 'scarcity'. At the other end, lots of people are - in a generic way - competing for the same customers with the same product. At this end there is no feeling of scarcity but rather a feeling of abundance; and we know that abundance is never a good basis to grow prices from.

Diamond manufacturing businesses from all over the world today are feeling industry pressures from many different angles, some more so than others. Diamond producers however also have a business to run and are there to maximise prices and make money; it is therefore up to us, manufacturers, to add value at our end and make money from that.

## COMMODITISATION

Commoditisation occurs when a product becomes indistinguishable from others like it, at which point Price becomes the main differentiator in the buying process.

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That's when goods become labels, when people stop looking at goods but merely limit themselves to list prices and price lists

Commoditisation is any manufacturer's worst nightmare as it clearly undermines profitability for all players in an industry.

Price wars often occur in industries with heavy commoditisation, foreshadowing a vicious cycle involving the erosion of profit margins at all ends of the supply chain as well as market instability.

Price wars often indicate over-saturation in a market - in other words when there is weak demand for a product.

The next slide is a visual illustration of that ...

The key take-away from this slide is that commoditisation leads to the erosion of profit margins, which in turn intensifies commoditisation, leading to further profit erosion.

The cycle is non-stop if it is not uprooted at the cause. And the cause is clearly relying on price alone as a selling point.

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What needs to be done is that we should look at our industry in a different way: away from commoditisation, towards differentiation and adding value.

For us at Eurostar the starting point for that is manufacturing, which is the first place in the pipeline where we as a manufacturer can add value and differentiate.

Manufacturing is something I am absolutely passionate about. I have always maintained that successful manufacturing can be a source of competitive advantage and truly can add value to the business overall.

To us, the ingredients for successful manufacturing are: scale; a trained and stable workforce; high productivity; precision of work and follow up; and finally the use of technology and engineering.

We now employ 6,000 people in China and consider all those people to be our most important asset. As such, we do all we can to ensure their well being, which helps to facilitate trust between employees and the company. We have created a friendly and healthy environment to work in, integrating work and living by providing shops, apartments and leisure & sport facilities. All this helps

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minimise employee turnover, allowing us to maintain the scale we need to remain competitive.

A second very important tool is IT, which allows for tight control on the entire manufacturing process. We run a centralized MIS with real time production figures. Our supervisors have on-line follow up of the production and keep track of every stone's optimum value, as well as enable security control, stone count, quality and value calculation of every diamond polished.

Obviously, running a large scale operation successfully requires leadership. But does that leadership communicate a passion and excitement for the future? Do the leaders running the particular organisation inspire motivation and commitment in its employees? If we want commitment to our strategy, the first question we have to ask is whether our people support our corporate strategy? Do they understand how that strategy translates to their job and how their contribution in turn affects the company? Will they whole-heartedly and passionately embrace that strategy as if it is their very own?

In order to achieve that we implemented Art & Science, a set of customised management procedures linked directly to our corporate strategy.

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Art & Science starts with a selective intake of new workers, and once they are there, extensive and continuous training. What we aim for is unsurpassed quality and craftsmanship, and we achieve this with the help of technologies and intense training.

The extensive training that takes place is what I would call the Art.

Science is equally important to us and that is why we have proprietary, self-developed systems; why we have an in house engineering team and why we manufacture our own tools and equipment. All of this allows us to differentiate our diamonds from other diamonds.

Putting together the Art and the Science seamlessly to ensure that they support your corporate strategy is the key here, making sure that both parts of the equation do indeed add up to a sum that is greater than its parts.

Now I would like to take you a few slides back. To us manufacturing is the starting point, an important way to add value and therefore partly an answer to commoditisation.

Manufacturing is not enough though, because once a diamond is polished you need to bring it to the market and

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sell it. Understanding the customer's needs and having the right value proposition is essential.

In no way would I like to be prescriptive but strategic alliances and partnerships have worked well for Eurostar, and in the next slides I would like to present you with a few case studies that illustrate possible routes to market, each of them is different but all of them have one thing in common: value addition.

Here we see examples of companies that have differentiated themselves through a unique product offering, marketing, distribution, or all three. We also see here some highly inspiring success stories in the making in our industry today.

The first one is on Hearts on Fire, where I can talk from my own experience; the next two are also in the diamond business, but one is my competitor and the other one a client. And lastly I would like to quickly show how Apple has reinvented itself with the iPod.

Nearly 8 years ago I met with Glenn Rothman of Hearts on Fire. We formed a strategic partnership and today Eurostar is the co-owner of HOF, supplying the company with 97% of its diamond requirements.

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Surely at that time H&A were not new - it existed a long time mainly in Asia - but we co-developed a H&A concept for the US, created a new desire, and today HOF is one of the largest AGS000 consumers in the world.

Globally, HOF sells to over 650 retail doors and the company has maintained double-digit growth for the past five years.

And above all, this new desire has brought us better margins.

The second example is Chopard which was mainly known as a luxury watch brand, but then leveraged on the company's strong brand equity to introduce a jewellery line which has turned out to be another major success for the company, creating added value for all its stakeholders.

The third one is also an industry example, where the Leo Diamond brought a differentiated cut to the market. Thanks to an enticing and significant marketing campaign, the Leo is distributed in about a 1,000 doors in the US, UK and HKG.

In 2002, Apple broke new ground with the introduction of the iPod. Today, the company sells over 39 million units a year, which accounts for nearly half of overall Apple sales.

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From these four case studies, we see that commoditisation can be overcome and that value creation can be achieved even in seemingly saturated markets.

Bringing us back to the diamond business, we can see that synergies between Manufacturing and Polished Distribution/Marketing work extremely well to fight commoditisation. One doesn't work without the other, they are inter-linked and symbiotic, keeping each other alive. At both levels of the pipeline it is necessary to create added value, thereby commanding higher margins.

Speaking from a manufacturer's point of view, I am sure I am not alone when I say that we need stronger cooperation from miners to ensure value addition at all ends of the supply chain. For the welfare of the industry, all players in the industry from miners to polished manufacturers to retailers must all take part in ensuring that the value of diamonds is safeguarded.

So what we want is:

- Differentiation, and several options are available: a premium product, process innovations, a customer specific solution such as a brand extension, or even a new buying experience...

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- That should allow us to create added value and avoid a price war. Too often price is the main differentiator when selling diamonds.

When we do those things well, it leads to sustainable profitability and bottom line growth instead of just top line growth.

The benefits are not only limited to bottom line growth, but clearly brings added value to other stakeholders in the industry:

Banks surely want to work with the most profitable companies as this is a way to minimise risk.

Mining companies are there to maximise profits as well and prefer to sell their product to companies that are able to pay good prices

And because our product is the backbone of their business, new product innovations that allow clients to differentiate their end-product and bring them away from price as a selling point allows them to make more money as well.

By adding value through manufacturing and polished distribution/marketing, commoditisation can be curtailed and in the process, incremental value can be created for the company as well as for stakeholders.

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And the way it can be achieved is through differentiation and introducing ground-breaking techniques at different levels of the business. In many instances, it requires looking at a problem at all angles and then using an unconventional way to solve it.

In conclusion, I would like to quote Einstein's definition of insanity, which is: "doing the same thing over and over again and expecting different results." I am sure we will all agree that this is not possible.

Thank you.

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