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DIAMONDS AS A CAPITAL INVESTMENT

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A diamond is one of the best-known precious metals. Diamonds have been known to humankind and used as decorative items since ancient times. Diamond is a very popular form of investment, although it bears no interest.

The hardness of diamond and its high dispersion of light – giving the diamond its characteristic "fire" – make it useful for industrial applications and desirable as jewelry. Diamonds are such a highly traded commodity that multiple organizations have been created for grading and certifying them based on the four Cs, which are carat, cut, color, and clarity. Other characteristics, such as presence or lack of fluorescence, also affect the desirability and thus the value of a diamond used for jewelry.

Perhaps the most famous use of the diamond in jewelry is in engagement rings, which became popular in the early to mid 20th century due to an advertising campaign by the De Beers company, though diamond rings have been used to symbolize engagements since at least the 15th century. The diamond's high value has also been the driving force behind dictators and revolutionary entities, especially in Africa, using slave and child labor to mine blood diamonds to fund conflicts.

Historically, the rough diamond price has been controlled by the De Beers Group, which has a 40% to 50% market share. Botswana is currently the largest producer of diamonds by value, with mines operated by Depswana, a joint venture between De Beers and the government of Botswana. However, since the 1980s, other producers have developed new mines in Russia, Canada and Australia for example, challenging De Beers' dominance (historically De Beers' market share was considerably higher). De Beers through its trading company DTC raised wholesale diamond prices three times in 2004 by a total of 14%.

The United States is the biggest consumer of diamonds in the world. It accounts for 35% of diamond sales, Hong Kong 26%, Belgium 15%, Japan 6%, and Israel 4%.Israel and Belgium in particular are important diamond-trading hubs thus their consumption numbers are misleading. In addition to print and online references, numerous institutions have varying standards which can be used to aid in diamond identification and pricing. GIA (Gemological Institute of America), HRD(Hoge Raad Diamant) and IGI(International Gemological Institute) are three such institutions. Often these organizations focus on new research and education which they pass on to their members and the public.

Polished and rough diamonds lack some of the desirable attributes of investment vehicles, including liquidity, homogeneity fungi ability. Grading and certification by recognized laboratories goes some way to redressing this. Weight and cutting proportions are parameters which can be precisely measured. Colour and clarity grades are parameters which need to be determined by gemologists.

The increasing quality and size, and decreasing price, of synthetic diamonds is presented as a threat to the value of polished diamonds as a long-term investment, but has never impacted real investment-grade diamond prices. The possibility of low-cost ultra–high-quality diamonds becoming available in industrial quantities at some time in the future has never been a hindrance for long-term investors in diamonds; synthetic diamonds have been manufactured since the 1950s and have yet to make a major impact on the market, nor is it likely to in the next decade or thereafter.

An alternative example of such a price fall caused by introduction of a new simulant strongly undermining prices was the permanent fall in natural pearl prices with the introduction of cultured pearls. The mechanism by which prices were affected is complex. In part because of the social acceptability of wearing cultured pearls to much of the market, customers migrated from the natural to the lower priced cultured product. This altered the supply and demand situation for natural pearls and perhaps the overall prestige of pearls in general was lowered. Where synthetic stones are much less socially acceptable to the market as a replacement for the natural version, the prestige of the natural stones has been retained. Thus increased availability and lowered prices of synthetics may or may not have major implications for the future price of natural diamonds. In addition, the introduction of synthetic rubies in the late 19th Century did not appear to have a permanent effect on the price of natural rubies.

There are several factors contributing to low liquidity of diamonds. One of the main is the lack of terminal market. Most commodities have terminal markets, and some form of commodities exchange, clearing house, and central storage facilities. Until recently this did not exist for diamonds. Diamonds are also subject to value added tax in the UK, EU, and sales tax in most developed countries, therefore reducing their effectiveness as an investment medium. Most diamonds are sold through retail stores at very high profit margins.

The investment parameter of diamonds is their high value per unit weight, which makes them easy to store and transport. A high quality diamond weighing as little as 2 or 3 grams could be worth as much as 100 kilos of gold. This extremely condensed value and portability does bestow diamonds as a form of emergency funding. People and populations displaced by war or extreme upheaval have utilised this portable asset successfully. In 2009 an exchange was launched by DODAQ to trade categories of polished diamonds. The DODAQ exchange is intended to be a terminal market for round polished certified diamonds (which is the most liquid part of the market) and hosts its centralised storage facility in a Freezone. The exchange is an attempt to overcome the traditional investment barriers of sales tax and low liquidity on the resale market. However, the exchange was a complete failure as no diamond traders were ready to commit their stones on a relatively unknown third-party exchange.

As diamonds in larger sizes become increasingly rare and valuable, any easily visible and readily understood pricing system has been difficult to establish. Martin Rapaport produces the Rapaport Diamond Report, which lists prices for polished diamonds. The Rapaport Diamond Report is relatively expensive to subscribe to, and as such is not readily available to consumers and investors. Each week, there are matrices of diamond prices for round brilliant cut diamonds, by colour and clarity within size bands, and also other shapes. The price matrix for brilliant cuts alone exceeds 1,400 entries, and even this is achieved only by grouping some grades together. There are considerable price shifts near the edges of the size bands, so a 0.49 carats (98 mg) stone may list at $5,500 per carat = $2,695, while a 0.50 carats (100 mg) stone of similar quality lists at $7,500 per carat = $3,750. This may appear such a large difference as to defy logic, but in reality stones near the top of a size band (or rarer fancy coloured varieties) tend to be uprated slightly. Some of the price jumps are related to marketing and consumer expectations. For example, a buyer expecting a 1 carat (200 mg) diamond solitaire engagement ring may be unprepared to accept a 0.99 carats (198 mg) diamond.

There are also fashion and marketing elements to take into consideration. De Beers expends marketing efforts to encourage sales of diamond sizes and qualities which are being produced in relatively large quantities. They have also been known to take steps to discourage investment, primarily because they perceive that bubble prices which are followed by sharp falls are bad for long term consumer confidence in diamonds as a long-term store of value.

Diamonds as investing is very profitable and useful because it is very convenient and safe. But you have to buy diamonds from certified dealers and carefully select them on the major indicators of quality.