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Diamonds may be an investor's best friend

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For the first time in 25 years, diamond production is declining and that may make the world's most coveted stones a better investment than copper, nickel and zinc, this year's top-performing commodities.

Output from diamond mines worldwide is likely to fall two per cent by 2015, says James Picton, a diamond analyst at W.H. Ireland who's been following the industry for 35 years. Production has increased about nine per cent in the past five years, according to the New York-based World Diamond Council, as mining companies hurried to find new deposits to meet soaring demand.

A rally in prices will fuel earnings for producers African Diamonds PLC and Petra Diamond Ltd., according to Merrill Lynch & Co. and JPMorgan Chase & Co. The drop in production comes as purchases of the stones rise, helped by the booming economies of China and India. China alone doubled jewelry purchases since 2001 and may buy 20 per cent more this year, according to www Diamond Forecast Ltd., a London-based research firm.

Diamonds have "the best fundamentals," said Evy Hambro, who manages the \$6.6-billion World Mining Fund in London for Merrill Lynch. "The gap between supply and demand is much bigger relative to other commodities."

Rough, or uncut, diamonds don't trade on commodity exchanges. Instead Johannesburg-based De Beers, which sells 60 per cent of the world's uncut gems, holds 10 sales a year, known as sights, to a select group of customers called sightholders from countries known for diamond cutting, including Belgium and Israel.

Hambro, with 1.5 per cent of his assets in diamond companies, said he will buy shares of Germiston, South Africa-based Gem Diamond Mining Corp., which goes public this year, and Toronto-based Aber Diamond Corp. Ian Henderson, who manages \$2.5 billion in natural-resource assets for JPMorgan in London, said he has increased his diamond-share holdings to four per cent from one per cent in the past year.

"I am very positive about diamonds, given the overall supply-demand situation," said Henderson. "Of the 170 diamond companies out there, only 25 are actually producing."

One of those is Dublin-based African Diamonds, whose shares almost tripled this year. Another is Sierra Leone Diamond Co., a Hemel Hempstead, U.K.-based company operating in West Africa, whose stock has also tripled. Shares of Petra Diamonds, a Jersey, U.K.-based explorer in Angola, South Africa and Botswana, have risen 52 per cent.

"There are no big mines out there in the foreseeable future," said John Teeling, chairman of African Diamonds, which made its first and only diamond-mine discovery two years ago in Botswana. "We'd be very lucky to find a second."