

World Diamond Market Down by 26 %

Sales of diamonds at De Beers, the world's leading diamond supplier, have fallen by a quarter over the past 6 months as the global economic slowdown hit consumer spending on luxury items. The sales of uncut gems (diamond stones) in the 5 auctions (open market sale where highest bidder receives the good) it held in the last 6 months fell 26 % to \$2.6 billion.

Cutters and polishers of diamonds have bought fewer rough stones as demand fell dramatically from retailers (jewellery shops) particularly US jewellers. The Japanese retail market also remains subdued although sales in Europe have risen modestly with the UK and France performing particularly well. However, world demand is significantly down overall.

The company which controls 65 % of the world market is likely to resist price cuts by holding back the supply of diamonds from the market in an effort to protect its market for diamonds. .

Questions: (write your answers on this sheet)

- A. Write down the demand function for diamonds and select what you think would be one of the most important non price determinants in the demand function for diamonds.

- B. Why would the markets in the United States and Japan be relevant to the sale of diamonds?

- C. Draw a supply curve and demand diagram to illustrate the effect of the global slowdown on the diamond market if:
 - 1) De Beers takes no action
 - 2) De Beers resists price cuts by holding back the supply of diamonds

Draw your diagrams here:

Answers:

A) Demand function for diamonds: Q_d (diamonds): function of (P (price of diamonds), P of complements (e.g. expensive clothing), P of substitutes (e.g. other precious stones, gold jewellery etc), Y (income), T (taste, how fashionable are diamonds), P (population e.g. size of wealthy population), A (advertising e.g. supporting market for diamonds), etc.

Non price determinant **INCOME**: Key component in the demand function for diamonds is the level of Income (Y) as these are expensive luxury items that sell for high prices. Higher incomes support higher demand.

B) The USA and Japan are two of the biggest and richest economies in the world so with higher incomes and a large wealthy population with a strong diamond market and there is more likely to be higher demand for diamonds which are an expensive luxury good.

