DeBeers and Its External Environment

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Abstract

Many factors can shape the performance of an organization externally. Some of these factors may come from politics, regulation, technological advances, or competitive forces. One study is the PESTEL analysis reflecting the effects of the political, economic, social, technological, environmental, and legal environments on a firm (Ketchen & Short, 2012). Another is Michael Porter's Five Forces that analyzes how traditional competition, new entrants, the threat of substitute products, bargaining power of suppliers, and customers, can shape an organization (Ketchen & Short, 2012). This presentation will use these two tools to analyze the strategic vulnerability of DeBeers and the corrective actions for the firm to take.

Keywords: Five forces model, Michael Porter, PESTEL, DeBeers, Strategic management

DeBeers and Its External Environment

Famous for the marketing adage "A Diamond is Forever," established in 1888, DeBeers' headquarters is in London and has mines in Botswana, Canada, Namibia, and South Africa ("Diamonds," 2019; DeBeers Group, n.d.). Until the late 1990s, the firm would control the world's supply of diamonds either by mining them directly or buying them in the open market from competitors, often at inflated prices (MacAdams & Reavis, 2008). Yet, a series of events in the late 1990s shook the business model of DeBeers and re-shaped the diamond industry forever.

PESTEL Analysis

Politics shaped DeBeers in many areas across the globe. In the early 1990s, the collapse of the Soviet Union meant the disintegration of specific contracts between the Soviets and DeBeers, and a flood of Russian diamonds was smuggled onto the international market, causing prices to fall (MacAdams & Reavis, 2008). Also, Russia's joint venture with Lev Leviev (creating Alrosa) created a competition for DeBeers (MacAdams & Reavis, 2008). Also, in efforts to control global diamond supply, DeBeers was forced to purchase "blood diamonds" from Angola that funded armed conflict, which was later exposed in the late 1990s (MacAdams & Reavis, 2008).

In addition to politics, economic factors were monitored by executives at DeBeers. One example is its strategy to control supply and thus, manipulating global prices (MacAdams & Reavis, 2008). Events like Angolan rebels flooding the market with $1.2B, the smuggling of Russian diamonds onto international markets, Australia's Argyle diamond mine terminating its DeBeers' contract, and the emergence of Canadian mines all increased the supply of diamonds onto the market, dropped prices that hurt DeBeers' profitability, market share, and vulnerability (MacAdams & Reavis, 2008).

The blood diamonds purchased from Angolan rebels were not the only social factor affecting DeBeers. A 1998 report by Global Witness accused the company of "operat[ing] with an extraordinary lack of accountability," questioning how DeBeers can mine natural resources from Africa but provide no benefit for the people doing the labor (MacAdams & Reavis, 2008, p. 8).

Technological advancements in the industry created synthetic or cultured diamonds (MacAdams & Reavis, 2008). Because diamonds take millions of years and enormous heat and pressure to make, the process can be simulated in a lab, making them more affordable and accessible to the general public (MacAdams & Reavis, 2008). Due to the difficulty in distinguishing diamonds that were mined from those grown, further investments in technology were necessary that could determine the difference (MacAdams & Reavis, 2008).

The environment factors heavily into DeBeers' decision-making. As the natural process takes millions of years, there is a finite supply, and as countries discover and mine diamonds, they control where it's sold. For example, as Canada emerged as a global diamond mine who opted not to supply DeBeers, they became a threat to the organization's profitability. Besides, the arrival of synthetic diamonds further dilutes the market, making diamonds more affordable and thus, accessible to those who couldn't usually afford one that was mined (MacAdams & Reavis, 2008).

DeBeers enjoyed a monopoly in the diamond industry for many years until the 1990s, by either mining diamonds directly or buying them in the open market from competitors, often at inflated prices (MacAdams & Reavis, 2008). Still, they faced legal challenges from the United States and the European Union for price-fixing as a result of the monopoly they had (MacAdams & Reavis, 2008). While the United States ultimately couldn't prosecute DeBeers for conspiring

with GE, DeBeers was prohibited from conducting business in the US (MacAdams & Reavis, 2008). Furthermore, the FTC's involvement regarding the proper naming convention for synthetic diamonds affected how the market perceives the new technological advancement, playing a factor on whether or not to enter this new arena (MacAdams & Reavis, 2008).

Five Forces Model

At one point, DeBeers had a monopoly of the industry, enjoying low threat level and a 90 percent market share (Maduekwe, 2008). Today its market share is around 40 percent, and it can be separated into three strategic groups facing high-level threats in each: small and medium enterprises (SMEs), synthetic diamonds, and top diamond firms (Maduekwe, 2008). Small and medium enterprises include Le Leviev Diamonds (LLD), Petra Diamonds, Gem Diamonds, Aber International, and others (Maduekwe, 2008). Synthetic diamond producers include Gemesis and Apollo Diamonds (Maduekwe, 2008). Top diamond firms include Rio Tinto Diamonds (RTD), Broken Hill Proprietary Billiton (BHBP), and Alrosa (Maduekwe, 2008). Industry trends, such as a shift from monopolistic to oligopolistic and producing countries becoming more involved, have also created competition in the industry (Maduekwe, 2008).

These industry trends foster a "cartel like character of the diamond industry" that creates barriers for entry and, therefore, makes it nearly impossible for new entrants (Maduekwe, 2008). Mining diamonds comers with burdensome government regulations, social responsibility, and legal responsibility that requires a massive upfront capital investment. Because diamonds are a scarce resource, the other option to mining is producing them in a lab, requiring significant capital investments for machinery, in addition to cutting and polishing. Therefore, the threat level is considerably low.

DeBeers face a high threat for substitute products because while diamonds remain a scarce resource, technological advancements allow them to be lab-grown, making them more affordable (Maduekwe, 2008). Furthermore, demands for other gems, like rubies, emeralds, or sapphires, while cannot replace the demand of diamonds, can remain a threat is ever-changing fashion trends.

The bargaining power of suppliers for DeBeers is low due to its efforts in vertically integrating its supply chain. Not only does it operate mines in Botswana, Canada, Namibia, and South Africa, it opened 22 stores globally by 2007 (DeBeers Group, n.d.; MacAdams & Reavis, 2008). As a result, it can control demand by operating push marketing tactics and control supply only by leaving diamonds in the ground (Maduekwe, 2008).

Finally, the threat from the bargaining power of customers is also low. Because DeBeers can control supply so carefully, instituting "second-week sights," supply of diamonds can come to a halt until demand exceeds supply, protecting it from an economic downturn (Maduekwe, 2008). Through price control and push marketing tactics, demand can drum up quickly, relative to other industries. Furthermore, due to the scarcity of diamonds, unlike other gems, the secondary market de-values diamonds greatly, turning buyers away who want the real thing ("Diamonds," 2019).

Conclusion and Recommendation

Per the PESTEL analysis, there are significant political and technological factors that must be navigated. As governments are looking to become more involved in the diamond industry, they are not only regulating mines but becoming competitors in many instances. Technological advancements are making what was once a scarce resource more affordable and resilient to fluctuating market conditions. Because resale markets de-value diamonds and the

looming threat of counterfeits, mined diamond prices are likely to increase, making the attractiveness of synthetic diamonds more appealing to consumers. Furthermore, its application in industrial fields will make production more scalable and, ultimately, more affordable to consumers. Governments aren't likely to establish companies to create and sell synthetic diamonds, and as a result, legal, environmental, and political exposure would be minimal than mining.

DeBeers once enjoyed a global monopoly in the marketplace, and now, they seek profits over market share (MacAdams & Reavis, 2008). Applying the Five Forces model, there is a high threat of competition and substitute products while facing low threat levels from new entrants, suppliers, and customers. One reason for this success is its ability to vertically integrate, owning mines, and entering a joint venture to open retail stores around the world (MacAdams & Reavis, 2008). Its strategy to innovate, creating diamond products, and memorable marketing campaigns has fueled its successful positioning as branded luxury items.

Yet, DeBeers remains vulnerable to political shifts in any of the countries they operate its mines and to the growing trend of synthetic diamonds. The need for joint ventures with Botswana, Canada, Namibia, and South Africa is paramount. Even in the face of the shift from mined diamonds to synthetics, the rarity of natural resources will keep demand consistent and, therefore, ongoing mining operations. In 2006, DeBeers and Botswana entered into a joint venture, and a similar agreement was made with Namibia (MacAdams & Reavis, 2008). The first directive would be to enter collective agreements with Canada and South Africa to solidify the supply chain.

Due to the growing popularity of synthetic diamonds, DeBeers should also get ahead of the trend and position itself as a pioneer in the field. Since the market has little knowledge of the

availability of synthetic diamonds, DeBeers can educate people on the industry and invest to be the leader in synthetic diamonds. Lastly, a directive should be made to invest in technology in the identification and classification of diamonds – synthetic, mined, and counterfeit. As the industry will no doubt be saturated with synthetic and mined diamonds, there will surely be a black market that will blur these lines in the future. Investments in the prevention of this would be of paramount importance, so it doesn't dilute the value of all diamonds in the industry.

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