**Illustration 15.4**
**A Diamond (cartel) Is (not necessarily) Forever**

For many years, the huge South African diamond colossus, De Beers Consolidated Mines Ltd., held a virtual monopoly of world diamond sales. At first its South African mines were practically the sole source of uncut diamonds. Then, as some other parts of the world began mining diamonds, De Beers responded by buying these “outside” diamonds and selling them through its Central Selling Organization (CSO), thereby limiting sales and controlling the price of diamonds. The company put strong pressure on dealers not to buy from other sources. This policy enabled De Beers to maintain its monopoly for several years. However, in September 1992, ***Business Week*** reported that De Beers was having trouble enforcing its agreements.* Its problems were primarily with Russia, the world’s second-largest producer, but also, to a lesser extent, with producers from other countries.

At that time, top executives from De Beers were meeting with officials in Russia. At ceremonies marking the opening of the company’s first Moscow office the company’s deputy chairman toasted “the momentous event.” ***Business Week*** pointed out, “Indeed it is. De Beers’ efforts to strengthen its ties with the Russians came at a critical juncture. As the company faces its most dire business climate in a decade, its hammerlock on output and prices is loosening.” Some suppliers were bypassing CSO and selling directly to dealers. De Beers executives were planning to spend $350 million during the year to buy up rogue supplies from Angola. “Beyond that, Russia’s post-coup restructuring and its hunger for hard currency could lead to a breakup of its diamond industry, leaving the world awash in lustrous stones.” Russian producers were already dumping some diamonds in violation of a 1990 agreement.

The new deal gave Russia $5 billion over five years in return for giving CSO exclusive rights to 95 percent of its uncut diamonds for export. But a London analyst believed at the time that Russia could be dumping up to 25 percent of its annual production. The deputy chairman of De Beers believed, however, that the Russians recognized that their own interests would be best served by maintaining the “well-being and stability of the industry” by relying on CSO's marketing clout. In other words, he thought the agreement would hold.

It didn’t. On August 14, 1996, an article on De Beers in ***The Wall Street Journal*** began with these words: “Desperate for cash, Russia is flooding foreign markets with its diamonds, ignoring an informal agreement with the De Beers diamond-marketing cartel.”[†] A De Beers executive admitted there “had been substantial leakages,” and he was flying to Moscow for unscheduled talks. Russian sales had driven down diamond prices by around 3 percent over the previous few weeks. Dealers were saying that even with De Beers' huge share of the market, “without Russia . . . De Beers' elaborate hold over the market could crumble.” But

Russia appeared more interested in immediate revenue to shore up its treasury than in the long-term deal.

According to the managing director of an association of diamond dealers in Antwerp, “Nothing has changed, large quantities of Russian diamonds are still being sold independently. Russia needs the cash.” Furthermore, a large Australian producer of low-quality diamonds had begun marketing diamonds on its own, and prices of these less expensive diamonds had fallen 10 to 20 percent. De Beers still sounded optimistic. The managing director of its Moscow office said, “Once a formal agreement is signed, we’re hopeful of reducing the leakages.” It should be noted that De Beers was still doing rather well. The ***WSJ*** mentioned that the company’s earnings had risen 23 percent in the previous six months.

As this illustration emphasizes, it is very difficult to maintain cartel agreements. Cheating is almost always a problem. Also, it is even harder to maintain an agreement, formal or otherwise, when one of the parties to the agreement comes into bad times and desperately needs revenue in the short term. Such parties, whether countries or firms, are often willing to sacrifice long-term benefits for short-term gains.

*“Can De Beers Hold onto Its Hammerlock?” ***Business Week,*** Sept. 21, 1992.
†“Russia Bypasses Diamond Pact with De Beers,” ***The Wall Street Journal,*** Aug. 14, 1996.