The Dynamics of Diamond Pricing and Marketing in Sierra Leone

This Policy Brief summarizes a report entitled ‘The Dynamics of Diamond Pricing and Marketing in Sierra Leone’. It also describes some of the policy implications for government, donor agencies and development organizations arising from the report.

The report describes the reality – and the incredible complexity – of the largely informal diamond-buying network in Sierra Leone, and the wide range of players involved. It describes a system that thrives because it is based to a large extent on secrecy, favours, trust and mistrust, dependency and disinformation. Many of those in and around the diamond pipeline do not know the true value of their product, and are therefore vulnerable to unfair exploitation. It is a system where very few rules apply, where product knowledge is limited, and where many influences and considerations interact to form a complex web of activity.

The report studies the structure, dynamics and idiosyncrasies of the value chain that currently exists within the artisanal diamond mining industry in Sierra Leone – ‘from earth to export’. The report emanates from the aims and objectives of the Diamond Development Initiative: to improve understanding of this sector in order to help provide ways in which artisanal diamond mining can provide a sustainable livelihood and encourage development.

Official diamond exports for 2005 were the highest since 1979: 540,732 carats valued at $142 million. There is currently one industrial-scale kimberlitic mine, one large-scale alluvial operation and a number of smaller companies. In total they account for about 20% of the country’s diamond exports, the remainder being mined artisanally. It is not known what percentage of the artisanal alluvials are fully legal in the sense of all licences and taxes being paid, but many are not.

Part One of the report provides an overview of the artisanal diamond industry in Sierra Leone and explains how artisanal miners and mining are financed, including a description of the systems and channels by which diamonds are distributed and sold from the digger, through various middlemen, to the exporter. The report examines the most common systems in use.

The system is a pyramid with as many as 120,000 diggers at the bottom and a dozen exporters at the top. The logic is simple – everyone attempts to buy the goods for the lowest possible price and sell for the highest. Middlemen act as...
either brokers or dealers and use the same business model. Artisanal miners are generally labourers who are employed to remove the overburden and to extract and wash the gravel. They are paid for their services in one or a combination of the following ways:

• They may work as contract labour, paid on a daily wage in rice and cash (Le.500-Le.5,000 – between US 20 cents and $1.80);
• they may be given a share of the gravel and can sell what diamonds they find;
• they may be paid a share of the money received when the stones found on their plot (if any) are sold on to the next step in the value chain.

Artisanal alluvial diamond digging is labour intensive. It employs people with very limited livelihood options. Luck, the belief that diamonds will continue to be found, and the shortage of alternatives keep diggers going. The vast majority are itinerant, swelling local populations.

In 2005, about 2,400 mining sites were licensed for artisanal mining by the Ministry of Mineral Resources. The average per acre cost of working a site in Kono District is $20,000. It may be much less elsewhere, meaning that the total expenditure on licensed mining alone in 2005 would have been $12 million or less. ‘This,’ the report says, ‘is a small investment against an export value of $116 million in artisanally mined diamonds.’ There are, of course, many more mining sites than licences. Local paramount chiefs and their families, for example, have a fair degree of autonomy, and numerous illicit diggings take place in the diamond areas.

In recent years, USAID has implemented a micro-financing plan under a cooperative scheme called the Integrated Diamond Management Program (IDMP). To date the scheme has had limited success. Issues of local management have been raised, however a more profound reason for early problems may be the fact that no prospecting work took place before digging commenced.

Part two of the report examines diamond pricing and revenue flows within the systems explained in Part One. In order of importance, buyers base their prices on:

• the quality of the diamond and its estimated value on the international market (factoring in their own buyer’s preferences and valuing style);
• the seller’s knowledge;
• the seller’s position in the chain (and what he is likely to receive from the competition);
• costs (taxes, fees, supporting, bank/currency charges, office costs, handshakes and tips);
• whether the stone is of dubious progeny, i.e. if it is stolen, smuggled in from another country, or illegally mined.

The value and price of diamonds increase exponentially with the size of the diamond. Although there is no ‘typical’ diamond, in very approximate terms, a good quality, one carat rough gem may bring the digger $130, the holder of the mining licence $370, the supporter/dealer $1000, and the exporter $1,100. (Most diamonds, it should be noted, are much smaller than one carat, and are not ‘good quality’. Several tons of earth may have to be moved in order to produce several stones weighing a single carat.)

Most of the internal diamond trade operates outside the formal banking system, and some of the profits in the sector are made on exchange rates that can fluctuate by as much as 30%. If 90% of all diamonds in Sierra Leone are purchased in cash, the question arises as to where the cash comes from, as formal banking system
records do not tally with diamond exports. A further question arises: how do importers pay their offshore commitments when the country is a net importer, when there are very limited reserves in the Central Bank, and when the local currency is not internationally tradable? The report examines the problem of capital flight, and how this relates to the fact that many of those involved in the diamond trade are either nationals of other West African countries, or are of Lebanese extraction and treated as second-class citizens.

Part Three contains conclusions and recommendations on land allocation and use, organisation and financing of production, alternative modes of purchasing, and alternative and complementary livelihoods.

Policy Implications

In designing interventions aimed at reducing poverty in artisanal diamond mining areas, policymakers should consider the interconnecting problems raised in this report. They must consider carefully where the greatest pricing mark-ups lie, and why. They must also consider – in addition to who might ‘win’ in any proposed change – who might lose. History has shown that small piecemeal changes are unlikely to have any major impact. A much more holistic approach is essential, one that recognizes artisanal diamond mining as a development and human security challenge, not simply a mining problem.

The simplest change would be to remove or consolidate the vast intermediate level of dealers, financiers, agents and coaxers. Dealers argue, however, that they are necessary to the industry as it currently stands because they are the only source of financing for diggers and those with mining licences. If they were to disappear – assuming this could be made to happen – exporters would make more money, but there is no guarantee that diggers would. A further likelihood is that if they were legislated out of business, dealers would simply go underground, and smuggling would increase.

The real challenge in reducing the massive middle is to give those at either end of the chain real economic incentives to act differently, and to provide opportunities for them to negotiate directly with one another. Several basic concepts that could help make this possible emerge from the study:

1. Knowledge and information: It is important to build better knowledge among diggers about the viability of potential mining sites (i.e. good geological information); about diamond values and prices; and about better technologies for artisanal mining;

2. Organization: several experiments have been undertaken with cooperatives, model contracts for diggers and strengthening the mineworkers union. It is important that lessons from these experiments, both positive and negative, be widely circulated, learned and remembered in the creation of new ventures. The re-invention of wheels will not advance what is known about this issue;

3. Scale: Many mining sites produce few diamonds, and do not cover their costs. Financiers spread the risk by supporting several, if not many operations at a time. Small interventions aimed at changing the status quo may not be financially viable; scale must therefore be a consideration in new ventures.

4. Financing: Breaking the cycle of dependency between diggers and dealers will be key to advancing this issue. New ways are needed to make working capital available to diggers and to those with mining licences. Lessons from the formal banking community and existing cooperative ventures suggest that there are no simple or obvious answers;

5. Transparency: In order to reduce the influence of the vast middle layer, it will be important to move exporters and international buyers closer to those who produce the diamonds. The creation of a multi-functional diamond centre or centres that could house a bourse where those with diamonds to sell would have
alternative and more transparent opportunities. Such a centre could also provide facilities for banking, licensing, independent valuation, training and other developmental activities. Greater transparency should also reduce rent-seeking opportunities for under-paid government officials and others;

6. **Levelling the playing field:** If sellers have better information and other sources of financing for their mining operations, they will be less dependent on the support offered by dealers. If they have direct access to exporters in a bourse, that too could reduce the influence of the middleman. In order to attract exporters to the bourse and to widen the number of exporters, the government could reduce the cost of export licences, but increase performance requirements, making it easier to enter the business – but in the absence of performance, more difficult to remain.1 With direct access to exporters, sellers could decide for themselves whether the support system offered by dealers has any continuing attraction.

7. **Formalizing the informal:** It is important in any change to consider whether it will reduce or expand the number of diggers. Better returns to diggers could attract more people into the business, which would only dilute any gains. If numbers, however, can be reduced, the available share will increase. A possible option is to make alluvial mining more attractive to small, developmentally acceptable mining enterprises. Formalizing as much as possible of what is today informal could help to regularize many of today’s difficulties in the sector.

Fundamental change, therefore, will require a change in the mindset of both government and international organizations. Government must see the artisanal diamond mining ‘problem’ as a challenge for all departments, not just the Ministry of Mineral Resources. This is a development and a human security challenge in which mining and diamonds are only two aspects of a much larger whole. The government must view diamonds as an engine of long-term development, rather than as a generator of short-term income.

International organizations, especially donors, must be willing to engage on the issues raised in this study. They must be prepared to make longer-term commitments than are normally the case, commitments that will survive isolated and compartmentalized pilot projects.

Sierra Leone’s diamond mining areas are among the least developed places in the country. Many of those who dig for diamonds would do almost anything else if opportunities were available. In the absence of these opportunities, and in the absence of the infrastructure needed to encourage and sustain them, they will not appear. If the areas that produce so much of Sierra Leone’s wealth are to live in peace and to develop, some of that wealth – and perhaps in the short term even a disproportionate level of donor assistance – must be invested there.

---

1 Government could reduce the license fee by 50% and receive the same net revenue if the number of exporters were to double. The loss in revenue from a reduced number of dealer licenses could be compensated by creative changes in other areas. The total revenue from all dealer and dealers’ agent licenses was less than 0.5% of all artisanally produced diamond exports in 2005.

Further information on the DDI can be found at www.pacweb.org.