

Gems & Jewellery Industry
Subdued sales volume amidst rising input costs

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Background

The Indian Gems & Jewellery (G&J) industry is one of the most prominent industries in the country and is characterized by a significantly large unorganised sector, labour-intensive operations, high working capital and raw material intensiveness and export-driven operations. India is the world's largest processing centre for G&J with the industry contributing about 17.5% to the total export earnings of the country during FY11. In FY11, total exports by the G&J industry grew robustly at 47% y-o-y to USD 43.14 bn (Rs.1,964.7 bn). Further, the size of the Indian domestic G&J industry was valued at approximately USD 27.5 billion (Rs.1.22 trillion) during FY11.

Diamonds and gold are the two main segments of the G&J industry with the former constituting nearly 80% of the entire sales of the industry in value terms. Further, the organised market accounts for a mere 4% of the jewellery retail market. Though India plays a prominent role in the G&J industry in terms of processing and consumption, it significantly lags behind in mining of gold and diamond because of meager reserves.

Export Performance during H1FY12

The G&J exports grew by 17.4% in H1FY12 on a y-o-y basis which was mainly driven by a 41% y-o-y rise in export of gold jewellery, coins and medallions which was in turn largely due to higher realisations on the back of increase in price of gold (which was about 30% higher during this period over the same period a year ago).

However, the export of Cut & Polished (C&P) diamonds, the key product in the G&J industry, increased by a meager 4.4% in value terms during H1FY12 on a y-o-y basis. In fact, in volume terms, export of C&P diamonds witnessed a 5% decline. The value of export has shown an increase despite sluggish demand in the US and European markets, largely because of rise in raw material cost.

The demand for rough diamonds has remained robust globally in the recent quarters while supply has remained restricted and intermittent leading to a sharp increase in global rough diamond prices. Further, Indian diamond processors have been facing a shortage of rough diamonds which has also resulted in a sharp rise in prices. On the other hand, owing to a strong resistance to increase in polished diamond prices by both the domestic and international buyers, the increase in average price realization per carat of C&P diamond during H1FY12 has been marginal and has not kept pace with that of the rise in rough diamond prices.

Outlook

The Indian G&J export growth will be impacted given the ongoing economic uncertainty and rising unemployment levels in the US and EU. The same is also reflected in half-yearly trend where the growth has come mainly due to increased export of gold medallions and gold jewellery (which are considered to be safe investment options) while C&P diamonds witnessed a decline in volume terms. The operating margins, especially in the C&P diamonds segment, are expected to remain under pressure.

The growth in the domestic G&J sector in India is expected to be driven mainly by higher disposable income, rising young population, higher number of working women and conscious marketing efforts of companies with greater focus on branding and organised retail. However, record high gold prices and high inflation may act as demand dampeners for G&J products - being a discretionary product.

Going forward, larger players with strong sourcing relationships (e.g. DTC sight holders or those having direct arrangement with mining companies) for raw materials, those with geographically diversified clientele, with higher value addition and a more conservative forex/liquidity management policy, are likely to exhibit more stable credit profiles.

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