

Executive Summary**Polished Uptrend Continues**

- RapNet Diamond Index (RNDI)[™] for one caraters rose 7.5 percent to 101.63 in May.
- RNDI increased by 25.1 percent in the first five months of the year.
- Growth in manufacturing centers supported by strong trade in U.S., but U.S. net polished imports, representing local consumption, still lag behind pre-recession levels.
- Auction market displays strong demand in high-end market.

Rough Softer But Strong

- Demand for rough fell back slightly in May compared to previous months, but remained buoyant.
- De Beers raised prices by an average of 3 percent at its May sight, with increases also reported from ALROSA sales and at BHP Billiton's spot tenders.
- DTC's May sight had estimated value of \$600 million.
- Indian diamond manufacturing relatively slower during summer vacation period.

Resilient Retail

- Strong fiscal quarter that ended April 30, 2011 for jewelry retailers – Signet Jewelers, Tiffany & Co. and Zale Corporation, with sales growth in all geographical regions.
- Jewelry price inflation continues to rise.
- Pace of U.S. retail growth slows from previous months in May.
- Reports of strong jewelry sales during China's May Day holiday.

Conclusion

A number of factors influenced the diamond trade, which remained upbeat in May. Indian diamond cutters and dealers took their annual summer vacations, which impacted trading and manufacturing levels. Still, activity in the trading centers was strong, with many gearing up for the JCK Las Vegas show that took place in early June.

Most encouragingly, there has been a clear positive trend emanating from the retail market, both in the U.S. and the emerging markets of China and India, compensating for any sales shortfall experienced in post-tsunami Japan. Despite the positive trend in U.S. retail sales, there remains some caution regarding the economic recovery there as unemployment remains above 9 percent and consumers are increasingly limited by high oil prices and inflation.

Polished prices are expected to continue their upward pressure as long as there is growth in consumer markets and rough prices continue to increase. However, with rising jewelry prices, it remains to be seen whether the buck will soon stop at the consumer level, putting the brakes on the steep uptrend seen so far in 2011. As a result, a more stable price trend is expected across the rough, polished and jewelry sectors in the second half of the year.

The Polished Market

The RapNet Diamond Index (RNDI)[™] for one carat polished diamonds rose 7.5 percent to 101.63 in May, continuing the positive trend seen during the year so far. The RapNet Composite Index increased 7.7 percent during the month to 166.63. The trade was focused on preparing for the JCK Las Vegas show, which began on June 2, while activity in India was subdued due to the annual summer vacation period in the second half of May.

There were widespread reports of shortages of polished goods, particularly for fine, excellent-cut stones. Dealers complained about finding the right stones at the right price as sellers continued to push price levels higher.

Demand was driven by good consumer demand in the Far East and India, supported by strong sales by large retailers in the U.S. While the established U.S. jewelry chains appeared to be raising their inventory levels, smaller and mid-tier companies continued to avoid large inventory purchases as buyers' caution increased with the rising prices. Wholesale inventories therefore remained relatively low.

The average price of 0.5-carat stones rose 8.3 percent during the month, while 3.00-carat stones grew 7.7 percent (see Figure 1).

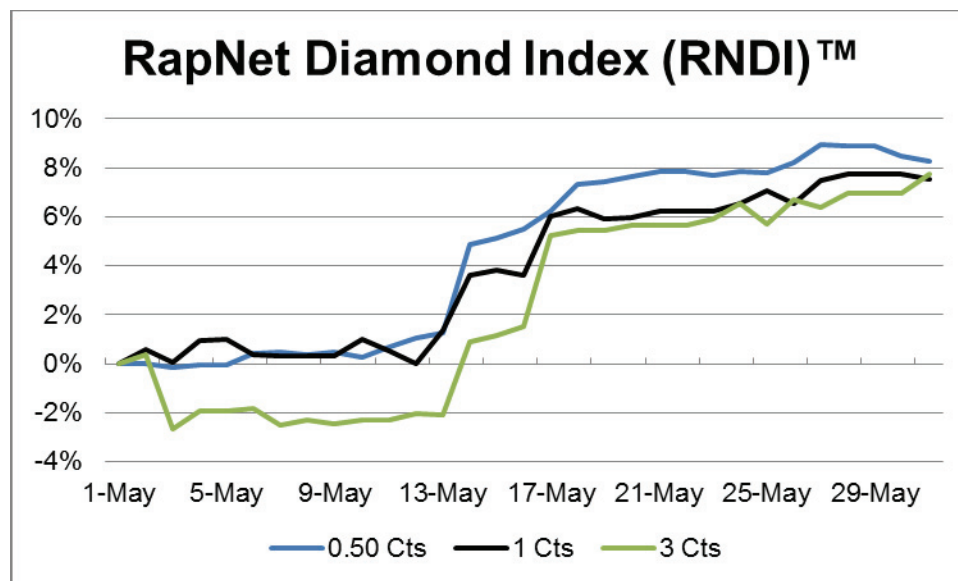


Figure 1

RapNet Asking Price index (RAPI) is the average asking price for D-H, IF-VS2, VG diamonds on RapNet. Rapaport Spec 2, Round, D-H, IF, X, X-VG, GIA-HRD-AGS.

The extended uptrend from the beginning of the year fueled some concern that retailers would not be able to absorb further increases. The RNDI rose 25.1 percent during the first five months of 2011 (see Figure 2, second column titled "January 1 – May 31"), and has increased by 28.2 percent from a year earlier (see Figure 2, third column titled "Y2Y Changes at May 31").

RapNet Diamond Index			
	May	January 1 - May 31	Y2Y Changes at May 31
RNDI (1 Cts)	7.5%	25.1%	28.2%
0.5 Cts	8.3%	21.5%	23.8%
3 Cts	7.7%	22.2%	21.0%
RapNet Composite Index	7.7%	22.7%	22.6%

Figure 2

RapNet Asking Price index (RAPI) is the average asking price for D-H, IF-VS2, VG diamonds on RapNet. Rapaport Spec 2, Round, D-H, IF, X, X-VG, GIA-HRD-AGS.

Strong demand in the main trading centers this year has been supported by a sharp rise in gross polished imports to the U.S., which were up 26 percent year on year to \$5.16 billion in the first quarter of 2011. Gross polished exports rose even more sharply by 40 percent to \$4.33 billion, while net polished imports, representing imports less exports, fell 16 percent to \$831 million (see Figure 3). The average price of these imports rose 13 percent against the previous year, while the average price of exports jumped 172 percent.

While the import and export data shows that the trade in polished diamonds has surpassed pre-recession 2008 levels, albeit boosted by strong price inflation, the net polished import trend, which indicates the value of goods that remain in the country for consumption, suggests that the local market still has a way to go before reaching a full recovery.

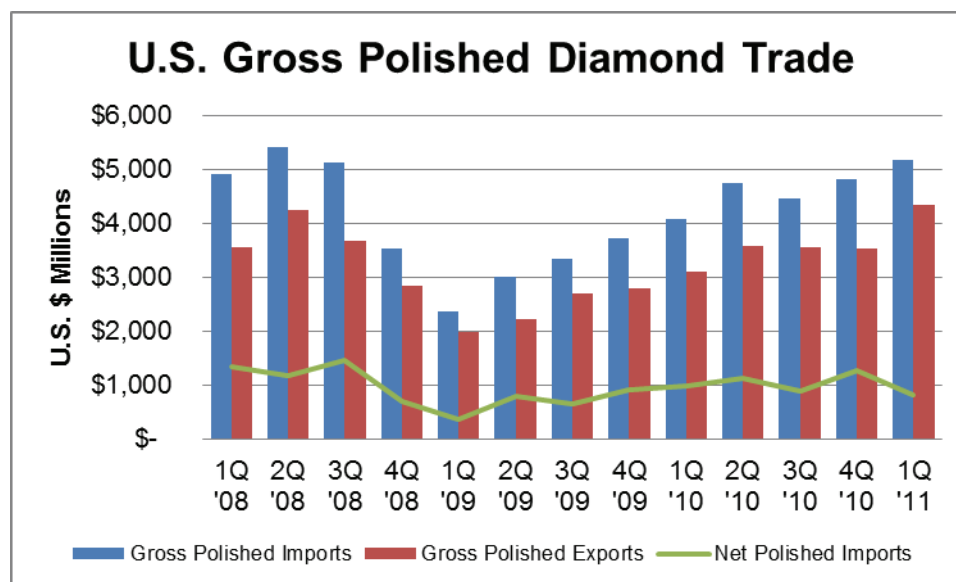


Figure 3

Source: U.S. Commerce Department.

Japan's polished imports fell 6 percent to \$61 million in April, in line with March imports. While some expected a sharper drop following the tsunami and earthquake that occurred in March, others believe it is still too early to gauge the long-term impact the tragedy will have on the market.

Auctions

The jewelry auction market also displayed strong demand for high-end polished diamonds in May. The auctions were characterized by high number of bidders vying for the pieces. Among the top lots sold at Christie's and Sotheby's were:

	Shape	Size (Ct)	Color & Clarity	Price	Price / Ct	Buyer
Christie's HK	Cushion	23.49 + 23.11	D-IF	\$ 9,295,690	\$199,478.33	Anonymous
Christie's HK	Marquise	13.39	Fancy Blue - VVS2	\$ 7,568,650	\$565,246.45	Leviev
Christie's HK	Round	18.88	D-IF	\$ 3,970,650	\$210,309.85	Asian Pvt
Christie's Geneva	Heart	56.15	D-IF	\$ 10,946,422	\$194,949.63	Graff Diamonds
Christie's Geneva	Rectangular	6.6	Fancy Intense Blue - IF	\$ 5,465,814	\$828,153.64	Private
Sotheby's Geneva	Radiant	10.99	Fancy Intense Pink - VS1	\$ 10,840,358	\$986,383.80	Leviev
Sotheby's Geneva	Cushion	16.53	D-IF	\$ 2,874,769	\$173,912.22	Anonymous
Sotheby's Geneva	Marquise	15.76		\$ 1,483,952.00	\$ 94,159.39	Private

Figure 4

Source: Christie's and Sotheby's, respectively.

The Rough Market

Rough demand was relatively softer in May compared to previous months, but remained strong as dealer trading continued to spur the market. Output from India's cutting industry slowed slightly through the summer vacation period.

Rough diamond prices continued to rise, with De Beers Diamond Trading Company (DTC) increasing levels by an average 3 percent at its sight at the beginning of May. The price hike helped cool premiums on the cheaper, low-quality Indian-type goods, while premiums on better-quality goods remained relatively high. Reports later in the month indicated similar hikes from ALROSA and increases at BHP Billiton's spot tender.

Rapaport estimates that the DTC's prices have increased by about 20 percent so far in 2011.

The DTC's May sight had an estimated value of \$600 million (see Figure 5). Sales through the first four sights of 2011 increased 12 percent year on year to an estimated \$2.35 billion, boosted by the price increases. It appears that the volumes supplied by the company have basically been in line with 2010 volumes, as expected.

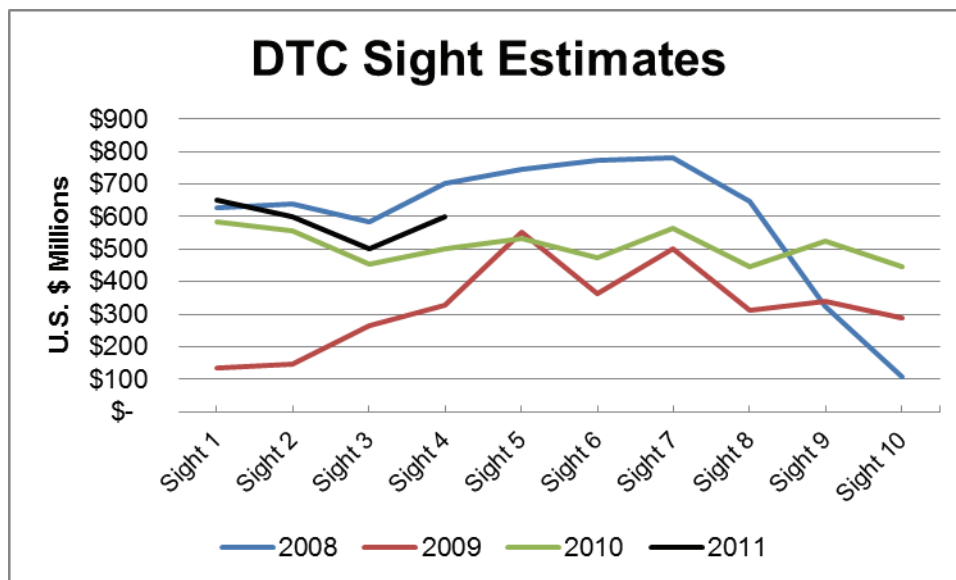


Figure 5

Source: Rapaport estimates. Estimates for 2008 – 2010 adjusted to reflected De Beers sales as reported in its financial statements.

Pressure has increased on the Kimberley Process (KP) to approve exports from Zimbabwe’s controversial Marange mine. The South African Diamond and Precious Metals Regulator (SADPMR) has reportedly told members that it intends to allow Marange imports to the country, with a parcel of goods already waiting final approval.

Discounting the moral debate surrounding the Marange goods, it remains difficult to assess the impact these goods will have on the market as the industry has no access to data regarding volumes of production and sales at Marange. Negotiations are scheduled to continue in June at the KP’s intercessional meeting in the Democratic Republic of the Congo (DRC).

The Retail Market

Jewelry retail sales continued to rise, with the large brand chains posting strong first-quarter results for the three months that ended on April 30, 2011. Sales at Signet Jewelers, Tiffany & Co. and Zale Corporation increased in all of the geographic regions where they operate (see Figure 6).

Sales were strong in the high-end sector, with Tiffany’s sales growth outpacing others, reflecting an increase of 20 percent, while sales at Signet’s Jared stores grew 12 percent.

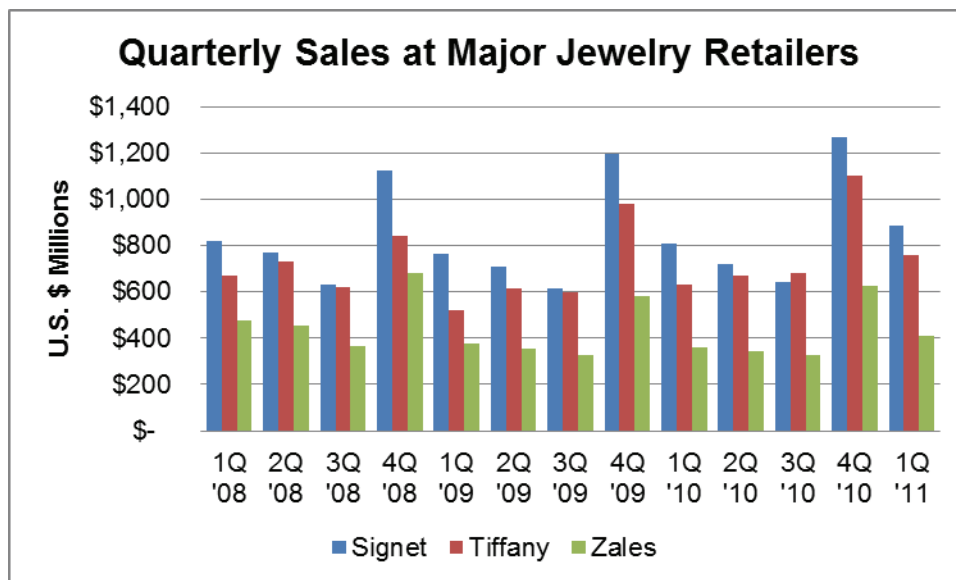


Figure 6

Source: Signet Jewelers, Tiffany & Co. and Zale Corporation's quarterly reports.

Jewelry prices continued to increase, with the U.S. Consumer Price Index (CPI) for jewelry rising 2.1 percent in April (see Figure 7). Average sales across Signet's U.S. and U.K. operations combined rose 12 percent year on year in the first fiscal quarter, while Zale reported that it increased price points on select items during the quarter and that it planned further increases in June.

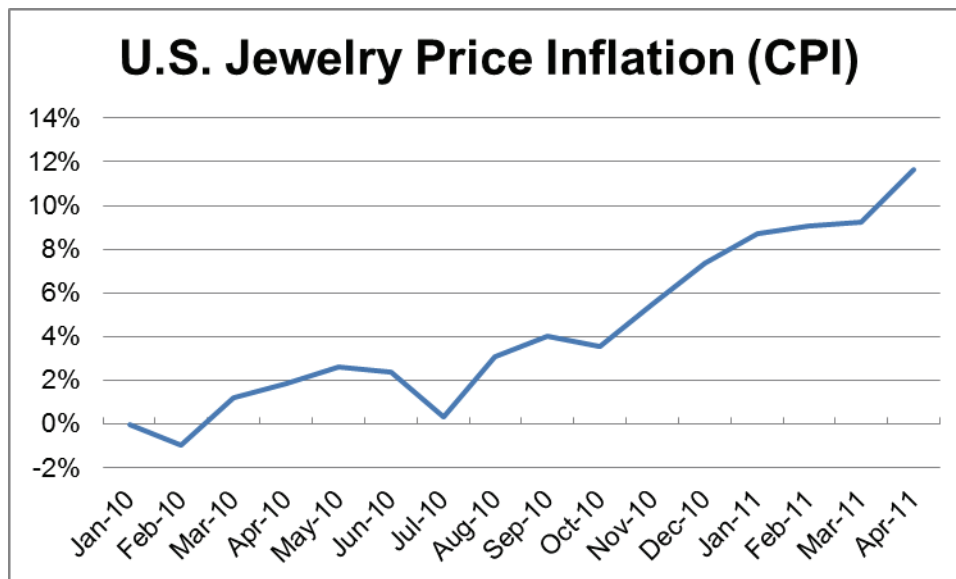


Figure 7

Source: U.S. Bureau of Labor Statistics

General U.S. retail sales increased 5.4 percent in May, according to the International Council of Shopping Centers (ICSC), slowing from the 9 percent growth recorded by the group in April. Sales were boosted by the Mother's Day selling period. MasterCard Advisors' SpendingPulse likewise reported a slowdown in the pace of growth during the month, but noted that jewelry sales rose by their strongest rate so far in 2011. SpendingPulse did not disclose data for general retail and jewelry sectors for the month. The SpendingPulse Luxury Index, which excludes jewelry, rose 4.7 percent in May.

Retail growth continued to be driven by consumer spending in China and India following reports of a strong May Day retail season in China, with jewelry being a top seller. Luxury brands continue to monitor Japan's recovery from the earthquake and tsunami, with modest sales declines expected for the remainder of the year.

Economic Factors

- Additional austerity measures were implemented in Europe's strained economies.
- U.S. unemployment rose from 9 percent to 9.1 percent in May.
- Spot gold fell 1.2 percent during the month to close on May 31 at \$1,529.90/oz.
- Spot platinum fell 2.8 percent to \$1,819/oz.
- Spot silver declined 20 percent to \$38.150/oz.
- Spot crude oil dropped 9 percent to \$102.7/barrel.

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