Polygon

the jewelry industry's largest e-marketplace™

MAR. 2014
www.Polygon.net

INDUSTRY REPORT

Retail Jewelry Industry in the U.S. 2014

A Current Portrait:

Retail Jewelry Sales
Wholesale & Retail Price Trends
Brick and Mortar vs. Online
Industry Mergers & Partnerships
New Technologies

Nathan Munn - www.polygon.net

www.Polygon.net

THE RETAIL JEWELRY INDUSTRY IN THE U.S.

A CURRENT PORTRAIT: 2014

In 2013, retail and wholesale jewelry prices declined, while total sales grew.

EXECUTIVE SUMMARY

In 2013, the American retail jewelry industry enjoyed significant growth while facing renewed challenges to traditional business and marketing models. Growth of fine jewelry and watch sales paralleled modest declines in wholesale and retail jewelry prices, while the arrival of new technologies and important developments in the U.S. retail sector combined to make the past year very eventful for retail jewelers.

Total fine jewelry and watch sales in the U.S. grew to $80.1 billion in 2013, an increase of 12.35% over total 2012 revenues ($71.3 billion). Of the total, jewelry sales increased 6.7% over 2012 to reach $70.65 billion, while revenue from watch sales grew by 7.6% to reach $9.46 billion.

Wholesale and retail jewelry prices declined in 2013. The Jewelry Consumer Price Index (JCPI) sat 1.1% lower in January 2014 than January 2013; similarly, the Jewelry Producer Price Index (JPPI) was 3.4% lower in January 2014 than the year previous. These significant decreases can be attributed to declining prices for precious metals used in jewelry manufacturing, specifically gold, silver and platinum.

In the retail sector, total sales by U.S. jewelry stores rose 8% year on year to reach $34.01 billion in 2013. Several high-profile mergers, acquisitions, partnerships and store closures by retailers continued to dominate the headlines of trade publications, with the acquisition of Zale Corp. by Signet Jewelers in February 2014 being one of the most significant business developments in the modern history of jewelry retailing.

China has become the world's top consumer, importer and producer of gold.

EXECUTIVE SUMMARY (CONT.)

Online sales of jewelry also continued to trend upward in 2013, with significant growth occurring in online retail sales as well as the use of mobile devices to make purchases.

2013 saw several companies and laboratories work to address concerns regarding the increasing number of synthetic and treated diamonds being discovered during inspection of parcels of supposedly natural stones, with the Gemological Institute of America developing a device with which retailers can detect fraudulent diamonds. A testing method was also developed by the Swiss Gemmological Institute SSEF to determine the true origin of a pearl, using a DNA extraction method that does not damage the pearl.

China continued to increase its precious metal consumption, displacing India as the world's top consumer of gold, as well as becoming the world's top producer and importer of gold in 2013.

The past year also provided important insights into the attitudes and buying habits of younger customers, with studies indicating that jewelry customers under 30 years old are far more likely to take social, political and environmental concerns into consideration when making large-ticket purchases.

Total fine jewelry and watch sales in the U.S. grew to $80.1 billion in 2013.

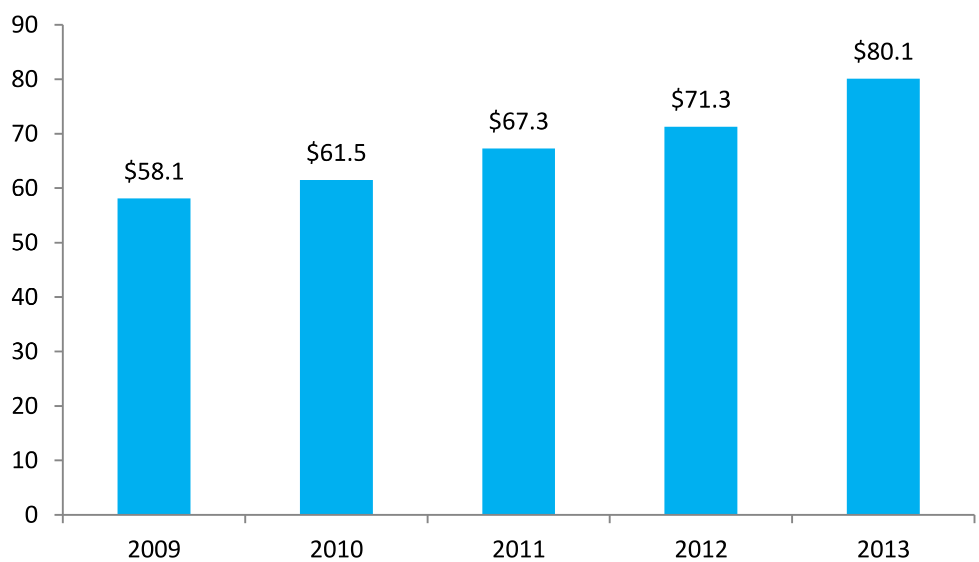
U.S. FINE JEWELRY AND WATCH SALES

Total U.S. fine jewelry and watch sales grew considerably in 2013, with year-over-year jewelry sales up 6.7% to $70.65 billion and watch sales up 7.6% to $9.46 billion, for total sales of $80.11 billion.

In 2012, total fine jewelry and watch sales were $71.3 billion - indicating that measured as a single sector, jewelry and watch sales in the U.S. grew by 12.35% in 2013.

Monthly fine jewelry sales generally enjoyed large year on year gains during every month of 2013, with increases of above 9% for each of the months of November, October, June, March and January. Monthly sales jumped the most in April 2013, with an increase of 11.1% over April 2012, for total sales of $4.94 billion.

TOTAL U.S. FINE JEWELRY AND WATCH SALES (BILLIONS)



Source: U.S. Dept. of Commerce, U.S. Census

Polygon

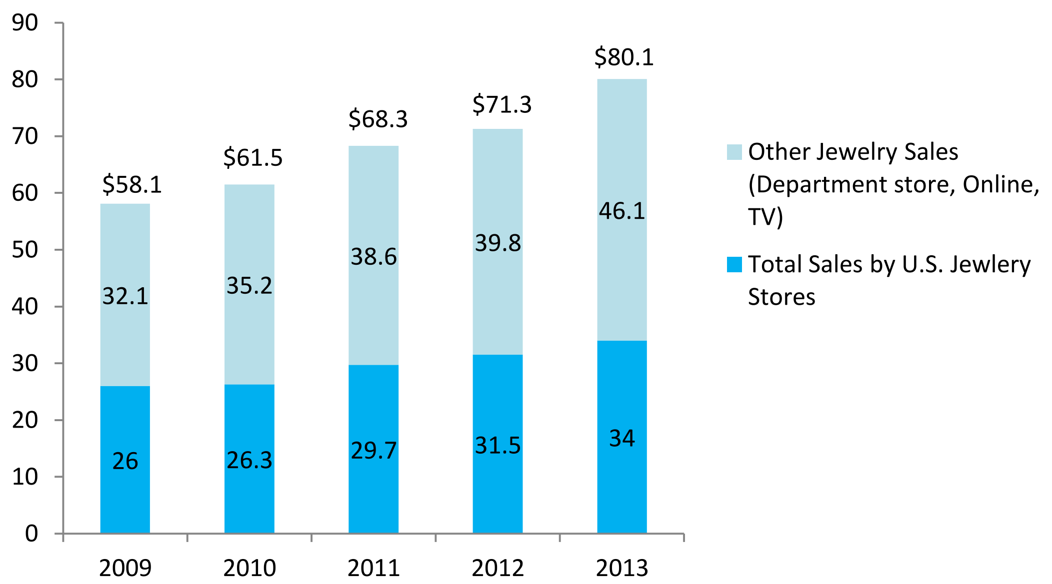
U.S. retail jewelry store sales increased by 8% in 2013, reaching $34.01 billion.

RETAIL JEWELRY STORE SALES

Between January and December 2013, total U.S. retail jewelry store sales rose 8% year on year to reach $34.01 billion, compared with $31.49 billion in 2012. This healthy growth is in stark contrast to the declining fortunes of U.S. department stores, who collectively reported a combined decline in sales of 4.7% in 2013 compared with 2012.

While U.S. retail jewelry stores experienced impressive revenue growth, other channels including wholesale, online and TV enjoyed overall growth as well, with combined revenues increasing from $39.8 billion in 2012 to $46.1 billion in 2013.

TOTAL U.S. JEWELRY SALES VS. SALES BY JEWELRY STORES (BIILLIONS)



Source: U.S. Dept. of Commerce, U.S. Census

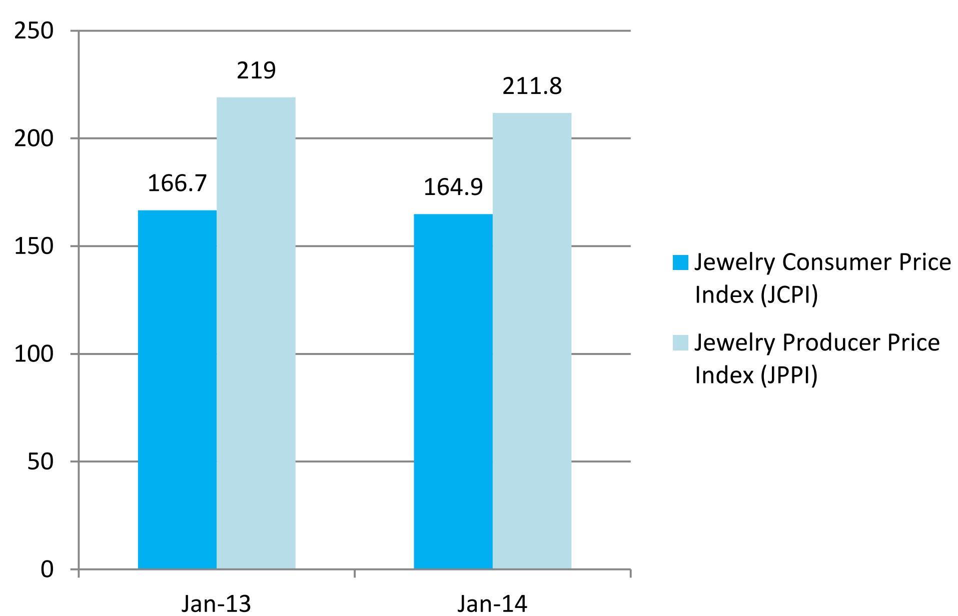
Lower wholesale jewelry prices are due to declining prices of precious metals.

WHOLESALE AND RETAIL JEWELRY PRICES

The Jewelry Consumer Price Index (JCPI) was 1.1% lower in January 2014 than in January 2013, after a sharp decline in retail jewelry prices during the last three months of 2013 negated modest price increases experienced during the first nine months of the year.

On the supplier side, wholesale jewelry prices as reflected by the Jewelry Producer Price Index (JPPI) were 3.4% lower in January 2014 than January 2013. Generally, the reduction in wholesale jewelry prices can be attributed to declining prices for precious metals used in jewelry manufacturing, specifically gold, silver and platinum.

JCPI - JPPI: JAN. 2014 VS. JAN. 2013



Source: Bureau of Labor Statistics

In February 2014, Signet Jewelers acquired their largest rival, Zale Corp.

MERGERS, ACQUISITIONS AND PARTNERSHIPS

In February 2014, Signet Jewelers acquired rival Zale Corp. in the single largest merging of retail jewelry chains in the industry's history. The purchase of Zale shares at $21 by Signet, a 41% premium over market value at the time, capped a dramatic change in Zale's fortunes since 2009 when Zale stock was valued at less than $1 per share.

As a result of the acquisition, Signet becomes the owner of approximately 1,680 Zale retail stores in the United States, Canada and Puerto Rico, as well as all People's Jewelers and Mappins Jewelers outlets located in Canada. Signet also absorbs the retail jewelry chains Gordon's Jewlers and Piercing Pagoda as part of the deal.

Shanghai, China based Yinren Group announced the purchase of the Antwerp Diamond Bank in December of 2013. No financial details have been disclosed and regulatory approval of the deal is pending, however it has been announced that ADB will be closing its New York City offices.

In what some referred to as "adding bricks to their clicks", leading online jewelry retailer Blue Nile began selling products in the Wedding Suite at the flagship Seattle location of Nordstrom's, the high-end American retail chain. The initial partnership is slated to last for six months, and may be expanded in the future.

Luxury retailer Neiman Marcus took a bold approach to emerging technologies by collaborating with the prominent 3D-printed goods manufacturer Shapeways to develop a line of 3D printed jewelry, the first two pieces of which were introduced in time for the 2013 holiday season.

Major retail jewelry chains experienced relatively modest growth in 2013.

CHAIN STORE SALES

Signet Jewelers, the largest retail jewelry chain in both the U.S. and the U.K., experienced modest overall sales growth in 2013. Same-store sales increased 3.3% year-on-year, considerably slower than the 9% same-store increase Signet posted for 2012. Total sales for all Signet properties, including the Kay Jewelers and Jared the Galleria franchises, grew to $3.98 billion in 2013, a 6.2% increase from 2012. Signet also opened a total of 53 new retail outlets in 2013, all of which are either Kay or Jared stores.

Signet's e-commerce sales grew by more than 40% in 2013 to reach $129.8 million, up from $92.3 million in 2012. This rapid growth of online sales for a major retailer shows how jewelry customers are becoming more comfortable with making online purchases a normal part of their shopping routine. However, it is important to note that despite impressive growth, online sales still only made up 3.24% of Signet's total revenues in 2013.

While it is not known what percentage of these sales can be attributed to mobile devices, increasing rates of mobile purchases in general indicate that mobile technology will continue to play a ever-larger role in jewelry retailing. Signet's success in online retailing undoubtedly stems from investments the company has made to improve its online and mobile retail strategy, including better e-commerce capabilities for store-branded websites and social media initiatives to drive engagement and branding with younger customers.

Luxury jewelry retailer Tiffany & Co. reported a worldwide net sales increase of 6% in 2013, with total sales reaching $4 billion. Excluding the effects of foreign currency translation to U.S. dollars, worldwide net sales increased by 10%, with comparable store sales up 6% year on year. Of these amounts, sales in the Americas rose 5% for the year, totaling $1.9 billion. Comparable store sales in the Americas rose by 3% year on year, led by strong sales performance at the New York flagship store and modest increases at branch store locations.

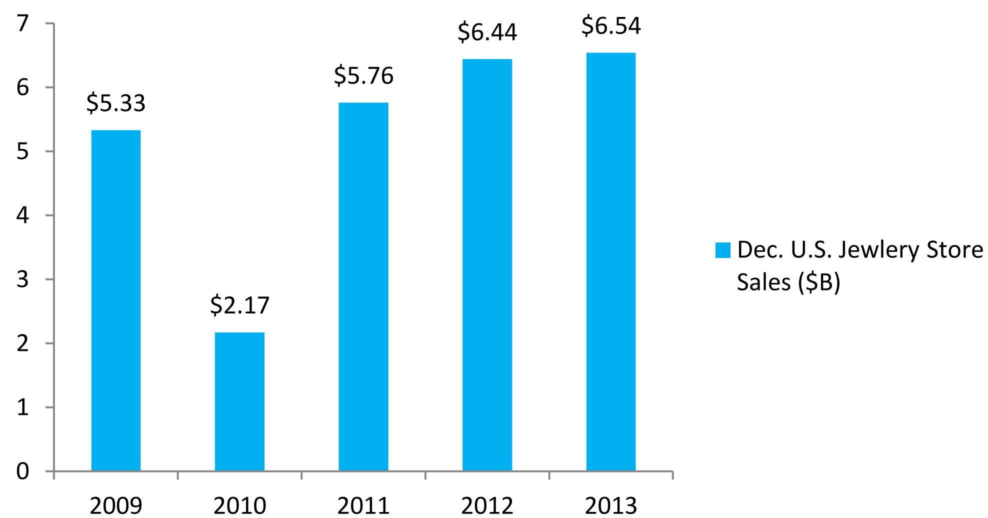
Retail jewelry stores remain at an advantage during the holiday season.

HOLIDAY SEASON SALES

Total U.S. jewelry and watch sales for December 2013 rose 6.6% year on year to reach nearly $17 billion. Jewelry store sales in December experienced a slight increase, from $6.44 billion in 2012 to $6.54 billion in 2013, accounting for 38.5% of total U.S. jewelry and watch sales for the month, slightly above the 2013 average of 34%. This data shows that retail jewelry stores remain in an advantageous position when it comes to attracting customers during the holiday season.

According to comScore, which tracks purchases made from desktop computers, online retail platforms selling jewelry, luxury goods and accessories were among the top 10 most visited web properties in November 2013 when ranked by month-to-month percentage change in number of visits. Online jewelry retailers had nearly 23 million unique visitors in November 2013 compared with about 18 million in October, an increase of 23%. An end of year report released by MasterCard Advisors, which tracks consumer spending on electronics, apparel, home furnishings and luxury items during the Christmas season, reported jewelry as being the “best-performing” retail category during the holidays.

U.S. JEWELRY STORE SALES IN DECEMBER (BILLIONS)



Source: U.S. Census

17% of all Cyber Monday sales in 2013 were made using a mobile device.

HOLIDAY SEASON SALES (CONT.)

Retail jewelers cited in the report said their best-selling items included diamond stud earrings, Pandora charms, simple diamond jewelry, silver, and watches.

A survey conducted by Deloitte before the 2013 holiday shopping season found that 47% of shoppers planned to shop online, compared to 44% who planned to visit discount department stores, showing the growing reach of online shopping as it took the top spot in the survey for the first time since being added as a category in 1998. The top reasons cited by survey respondents for moving to online shopping were convenience, at over 75%, and price, at 63%.

The Deloitte survey provides many insights into the mind of the contemporary retail customer. When asked for the top reasons they would still consider shopping at a physical store, 54% of respondents stated a “knowledgeable sales associate” would entice them to visit a brick-and-mortar retailer. For jewelry retailers, this would indicate that the retaining of informed and engaging sales staff should remain a priority.

In a dramatic demonstration of growth, total Cyber Monday sales grew to $2.29 billion in 2013 from $1.46 billion in 2012, with data indicating that mobile continues to be a fast-growing sector of online shopping: 17% of all Cyber Monday sales in 2013 were made using mobile devices, an increase of 55.4% over 2012.

Several new technologies to identify gem fraud were developed in 2013.

GRADING

2013 brought several developments in the grading and appraisal industry. Early in 2014, the Gemological Institute of America introduced an internally-designed device able to identify synthetic and treated diamonds, available for sale to retailers and currently deployed in partnership with several major international diamond bourses.

The DiamondCheck device retails for $23,900. GIA has been involved in the design and manufacture of grading equipment, including professional-grade microscopes, since the 1930’s.

DeBeers has also announced that they now employ a technology they are confident can detect individual synthetic stones within mass shipments of diamonds, following in the tradition of the DiamondView/DiamondSure devices that the company marketed in the 1990’s.

According to a study published in the science journal PLoS ONE, the Swiss Gemmological Institute SSEF has developed a method to determine the true origin of pearls using advanced DNA testing. The techniques employed in the test do not devalue or damage the pearls, and have proven to be highly accurate.

China imported 33% more gold in 2013 than in 2012, a total of 1108 metric tons.

EMERGING MARKETS

In 2013, China displaced India as the world's largest consumer of gold. Chinese gold consumption reached a record 1066 tonnes in 2013, surpassing the previous world record for amount of gold consumed in a year - 1007 tonnes - set by India in 2010.

This major development distinguishes China in more ways than one. The country is also the world's most prolific producer of gold, having mined an estimated 437 tonnes of the metal in 2013, a year-on-year increase of 6% that continued a dominance of the sector that began when China surpassed South Africa as the world's top producer of gold in 2007.

In another example of their prominence in the global gold industry, China also imported 1108 metric tons of gold in 2013, up 33% from 2012, further distinguishing China as the world's largest importer of gold.

The increase in Chinese demand for gold products is at least partially attributable to falling gold prices, which in 2013 dropped to significant lows during the months of April and June. Overall, gold prices fell 28% in 2013.

The Letseng diamond mine, located in the landlocked African country of Lesotho, continues to produce the most dramatic finds of diamonds in the world. The mine has produced several iconic diamonds in recent years, including the 550-carat Letseng Star, and early in 2014 two 160-carat rough stones in excellent condition were extracted from the mine.

Americans aged 26 to 35 are more likely to buy jewelry than any other group.

SOCIAL, POLITICAL AND ENVIRONMENTAL FACTORS

I. THE JEWELRY CUSTOMER IN 2014

One of the most important factors often overlooked by retailers is the changing nature of the modern jewelry customer. According to a report published by the U.S. Bureau of Labor Statistics, Americans between the ages of 26 and 35 are more likely to purchase jewelry than any other segment of the population. They also spend more than twice the average amount when purchasing jewelry as a gift.

These young people are tech-savvy, informed, wary of making large purchases, and significantly more likely to take what used to be considered outlying factors – social and political concerns, the environment – into account very seriously when considering a jewelry purchase. A poll conducted by KPMG indicated that nearly 70% of consumers under the age of 30 “consider social issues” before making large-ticket purchases, such as automobiles, electronics and jewelry.

The poll also indicated that while only 16% of the general U.S. population has heard of the term “conflict minerals”, consumers under the age of 30 were 75% more likely to be aware of conflict minerals and the issues surrounding them.

The most effective way to reach these customers is to carry inventory that speaks to their wants while addressing their concerns. Ethical sourcing, certifications of product value, and community-oriented promotional events are all strategies that resonate with young customers.

For these individuals, the internet is not a new tool. It is a fundamental part of their life experience, and as such is intimately intertwined with the physical world in every aspect of their lives. Younger customers are also starting to participate in the economy at a time when good jobs are scarce, personal levels of debt are sky-high, and career stability and retirement are uncertain.

In the mid-to-long term, precious metal mines face multiple business challenges.

SOCIAL, POLITICAL AND ENVIRONMENTAL FACTORS (CONT.)

With this in mind, instead of begrudging the "showroomer" – the client who browses in person, then shops online for a lower price - consider that the person is simply using the tools available to them to make the most informed, economical decision they can within a highly competitive retail market.

Remember too that this new generation of jewelry customers have as much to learn from traditional retailers – namely, the art and pleasure of personal interactions, shopping at a relaxed pace, the subtlety of an inviting atmosphere, the importance of community – as retailers do from them.

II. GLOBAL FACTORS

Worldwide, precious metal and gem mining operations are under increased scrutiny from government regulators, and in many countries face opposition from communities affected by mining development.

While currently, precious metal and gem production worldwide is robust, putting downward pressure on prices, regional factors will likely contribute to higher operating costs for mining companies in the mid-to-long term as governments demand higher royalty rates for resource extraction and communities push for better compensation and inclusion during the negotiation process.

Examples of this burgeoning trend include the closure, sale or reduced production goals at 12 of 27 mines owned by Barrick Gold, citing low gold prices and development delays at several mine sites, the closure of the New Dawn gold mine in Zimbabwe, and the temporary shutdown of the world's largest gold mine by reserves, the Freeport Grasberg mine in Indonesia, due to a structural collapse which resulted in the deaths of 28 miners.

All areas of jewelry retailing have been deeply affected by the internet.

CONCLUSION

In 2014, retail jewelers operate within several paradoxes at once. The jewelry industry is rooted in tradition and built on personal interactions, yet in 2014 the industry is enduring technological change that is forcing brick-and-mortar store owners into new, digital realms at every step of the business process.

Sourcing, selling, marketing, and customer service have all been deeply affected by the internet, which has led to transparency of the global supply chain and the rise of mobile technology. Jewelers must adapt to these new realities without sacrificing core business principles in order to thrive.

There are opportunities for investment and expansion in practically all areas of jewelry retailing, yet threats remain pronounced in the post-recession climate. The merging of the largest retail jewelry chains presents enormous challenges as well as strategic opportunities for independent retailers of all sizes. The continued profitability and growth of major online-only retailers leaves a smaller market share for other players, yet their successes provide competitive insights that quick-moving independents can capitalize upon.

Flexibility and adaptability should be the guiding principles of the jewelry retailer's strategy for success in the short term. Diversifying product offerings and sourcing options by using online services can help to keep costs low, expand inventory without spending, and widen your customer base.

Online engagement will continue to play an important role in branding and marketing, and community partnerships will play a greater role in developing loyal, local clients in 2014.

SOURCES

U.S. Dept. of Commerce

U.S. Census

U.S. Bureau of Labor Statistics

ComScore.com

Mastercard Advisors

KPMG

Deloitte

PLoS ONE

IB Times

Signet Jewelers

Bloomberg.com

The Motley Fool