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SEPT. 2013
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INDUSTRY REPORT

Retail Jewelry Industry in the U.S. 2013

A Current Portrait:

Price Trends
Landscape After Recession
Brick and Mortar vs. Online
Emerging Markets
Challenges & Opportunities

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THE RETAIL JEWELRY INDUSTRY IN THE U.S.

A CURRENT PORTRAIT

The U.S. retail jewelry industry has now surpassed pre-recession sales figures.

EXECUTIVE SUMMARY

2012 was a year of growth, innovation, and change for retail jewelers in America. Total revenues from fine jewelry and watch sales in the U.S. reached a record $71.3 billion in 2012, an increase of 5.9% over 2011 ($67.3 billion). While total industry growth in 2012 neared 6%, the rate of growth was slower than in 2011 when revenues increased 10.7% year-over-year. However, it is important to note that the majority of 2012 revenues were driven by unit sales as opposed to price inflation. In 2011, elevated prices of polished diamonds and precious metals were primarily responsible for double-digit growth.

In 2012, wholesale fine jewelry prices rose at a rate of 2.5% year-over-year, in line with historical pricing trends, while retail prices fell by 1.2%, further diminishing margins for commercial retailers. Opportunities for brick-and-mortar jewelry retailers to enter the fragmented mid-range U.S. market remain significant, as the retail landscape continues to recover following thousands of store closures during the 2008 – 2009 economic recession.

While the exact percentage of total jewelry sales that took place online in 2012 is not yet known, online sales made up 6% of total U.S. jewelry sales in 2011. Consumers are gradually becoming more comfortable with online shopping, and online jewelry sales are growing in tandem with other retail sectors. The long-term trend of increased online shopping by fine jewelry customers was compounded and complimented by double-digit growth of jewelry and watch sales during the 2012 edition of the 1-day nationwide online shopping promotion Cyber Monday. Emerging markets continued to experience growth in fine jewelry sales, consumption of precious metals and polished diamonds, albeit at a slower pace than in recent years. Importantly, India is the world’s largest consumer of gold, while China has become the world’s largest consumer of platinum.

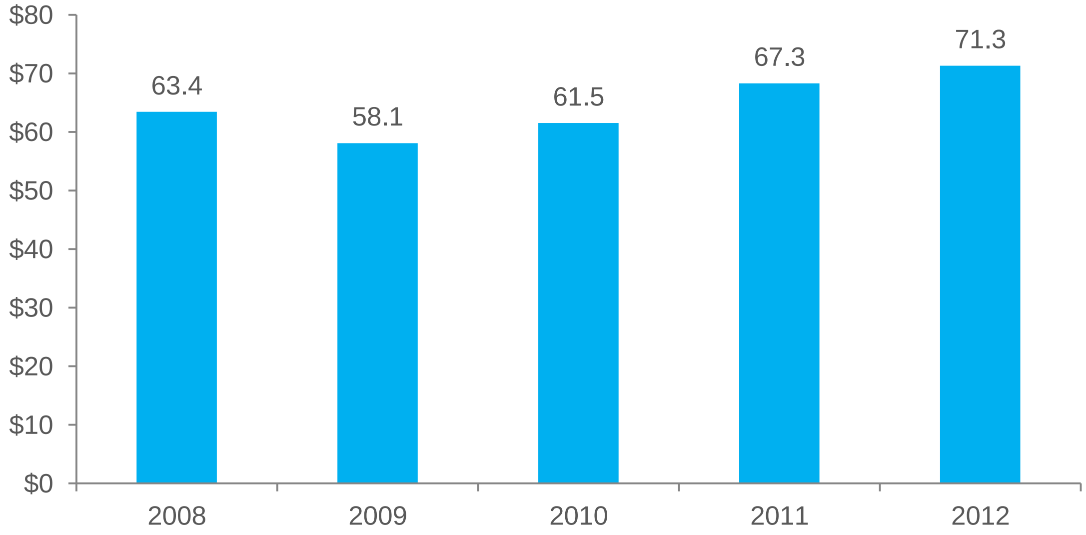
Fine jewelry and watch sales in the U.S. grew to a record $71.3 billion in 2012.

TOTAL U.S. FINE JEWELRY & WATCH SALES

The American retail jewelry industry has bounced back from a decline in revenues during the recessionary period of 2008-2009 to post record fine jewelry and watch sales in 2011 and 2012. Sales for both years far surpassed the previous yearly sales record of $65.3 billion set in 2007. U.S. fine jewelry sales increased 6% in 2012 to reach $61.9 billion, while revenue from fine watches grew 5.8% to $9.4 billion - a total sales figure of $71.3 billion. Both sectors experienced growth at near-identical rates month over month.

Data for the first quarter of 2013 shows growth continuing at an increased rate, with total jewelry sales in America up 17.7% year-over-year for April 2013, and retail jewelry sales up 10.6% between Q1 2012 and Q1 2013.

TOTAL U.S. FINE JEWELRY & WATCH SALES ($B)



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

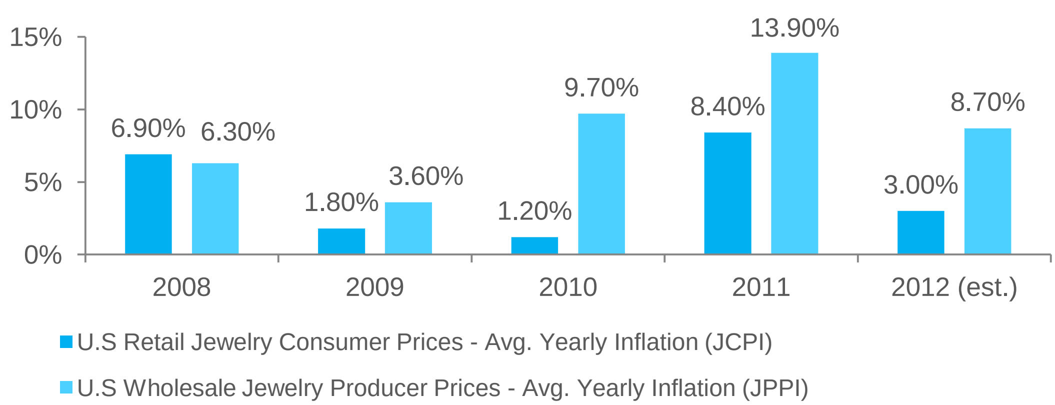
Retail jewelry price inflation can be attributed to declining retailer profit margins.

WHOLESALE VS. RETAIL JEWELRY PRICE TRENDS

Retail prices for fine jewelry were volatile in 2012, as commercial retailers fluctuated between raising prices in an attempt to increase shrinking margins, and lowering prices in an attempt to retain customers and generate new sales. Fluctuations in the market price of gold and silver further contributed to unstable retail pricing. Year-over-year, wholesale jewelry prices have historically increased between 2 – 3%, and 2012 continued this trend. Wholesale jewelry prices increased by 2.5% between March 2012 and March 2013, while retail jewelry prices decreased by 1.2% during the same period, demonstrating the continued reduction of retail profit margins. Between September 2011 and September 2012 wholesale jewelry prices rose 3.3%; during the same period, retail jewelry prices increased by only 2.8%, with nearly all inflation occurring in August and September after 8 months of flat prices.

While recent year-over-year figures provide some perspective, comparing Jewelry Producers Price Index (JPPI) and Jewelry Consumers Price Index (JCPI) inflation over the longer term illustrates the steep decline of retailer margins.

INFLATION: RETAIL VS. WHOLESALE JEWELRY PRICES



Source: U.S. Dept. of Commerce, Bureau of Labor Statistics, National Jeweler

During the 2008 – 2009 recession, approximately 3500 jewelry stores closed their doors permanently in the U.S.

THE RETAIL LANDSCAPE AFTER RECESSION:
INDEPENDENT, CHAIN AND DEPARTMENT STORES

During the recessionary period of the late 2000's, nearly 3500 retail jewelry stores closed their doors permanently in the United States. Three large national chains - Friedman Jewelers, Whitehall Jewelers, and Bailey Banks & Biddle - went out of business during this time, accounting for 857 store closings nationwide. The three chains once generated over $1 billion in yearly diamond sales combined, and their liquidation pushed customers back into the market, seeking new retailers to fill the gap.
Other major retailers also closed stores at the end of the decade, however were able to avoid insolvency through reorganization: Zale shut down 145 retail outlets, while Macy's, Cartier and Fred Meyer each closed several stores. In response to these opportunities, major discount retailers Costco, Target and Wal-Mart stepped in to the market with expanded lower-ticket offerings at their in-house jewelry counters. At the other end of the spectrum, luxury jeweler Tiffany and Co. opened eight new stores, and mid-range department store retailer Kohl's opened 69 new stores in a dramatic grab for market share.

Revenues generated through other retail jewelry distribution channels are also in flux. Jewelry TV, offering jewelry products to home-based shoppers, grew total 2011 sales to $400 million, a 21% increase since 2009. Fellow shopping channel and direct competitor QVC experienced a 30% drop in jewelry sales during the 2009 – 2011 period.

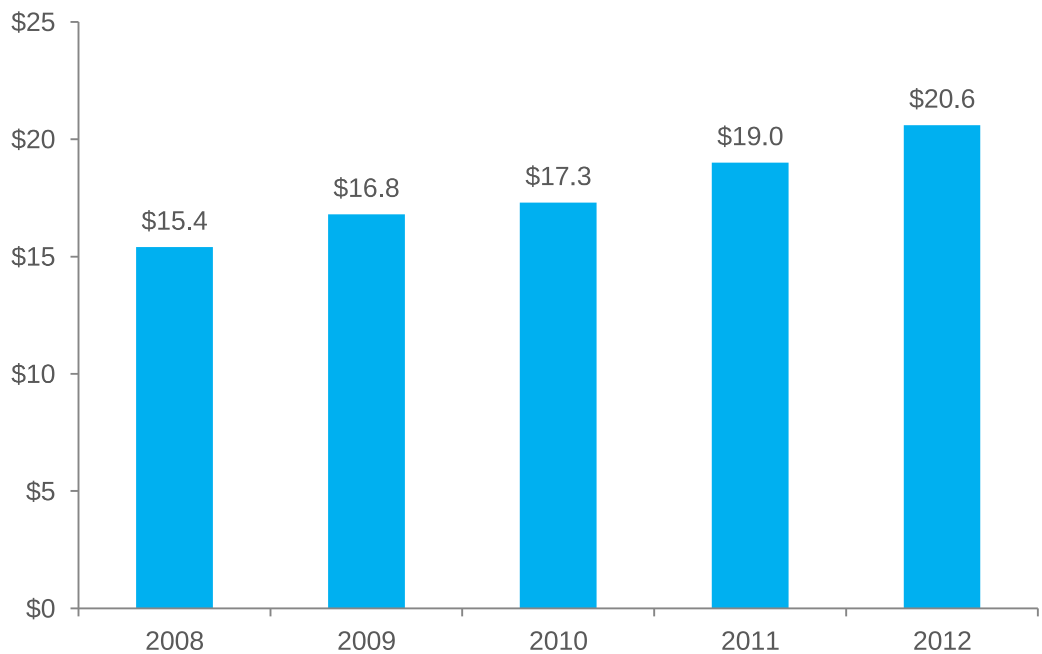
U.S. department stores experienced a 2.1% decrease in jewelry sales in May 2013 compared to May 2012, an indication that consumers may increasingly be looking to independent or online retailers for fine jewelry. In 2012, chain retailer Tiffany and Co., specializing in high-ticket bridal jewelry items, increased total sales by 4% year-over-year to $3.8 billion. The largest luxury retail jeweler in the U.S., Signet Jewelers, experienced an 11.8% increase in year-over-year sales during the fourth quarter of 2012, evidence that well-placed chain retailers with the advantage of significant market penetration and brand recognition can continue to grow and exceed projections. The continued success of Tiffany and Co., Signet and other specialty retailers can be attributed to effective global brand awareness campaigns, value perception, brand loyalty, and an expanded range of product offerings.

Holiday sales of fine jewelry and watches reached a record $20.6 billion in 2012.

HOLIDAY SALES

Total U.S. retail sales of fine jewelry and watches reached $20.6 billion during the 2012 holiday season, a year-over-year increase of 8.9%. This record-setting figure represents a 5.6% jump from the previous holiday retail jewelry sales record of $19.5 billion set in 2007, just ahead of a recessionary period beginning in 2008. After four years of below-peak sales, 2012 sales show that the retail jewelry industry has regained momentum and will continue to grow in 2013.

TOTAL U.S. HOLIDAY FINE JEWELRY AND WATCH SALES ($B)



Source: U.S. Dept. of Commerce, U.S. Census, National Jeweler, Mastercard

Diamond jewelry continues to account for nearly 50% of U.S. retail jewelry sales.

WHAT ARE CUSTOMERS BUYING DURING THE HOLIDAYS

The United States remains unchallenged as the world's largest consumer of polished diamonds, with total revenue from diamond sales in the area of $27 billion annually, more than triple the revenues of the nearest competitor in diamond consumption, China. This position is supported by consistently strong retail diamond sales, which account for nearly 50% of total U.S. retail jewelry sales every year. Most retail diamond jewelry sales take place over the holiday season, and generate a significant portion of total yearly revenues for many fine jewelers.

According to a 2012 year-end survey of U.S. retail jewelers released by National Jeweler, 35% of respondents said that gold jewelry sales were "flat", with another 35% reporting that sales of gold jewelry had actually decreased year-over-year compared to 2011. On a more positive note, 22% indicated that sales of gold jewelry had increased during the 2012 holiday sales season. Some retailers said that the fluctuating price of gold was proving to be an obstacle for sales, making it difficult to accurately price their inventory. Since retail outlets price their items according to the market value of gold, when the price of gold drops retailer price points must be recalculated to avoid the perception that their jewelry is overpriced. Gold price fluctuations continue to prove challenging for retailers in 2013.

Traditional retail jewelry stores continue to generate 30% of total industry sales.

BRICK AND MORTAR RETAILERS VS. ONLINE SALES

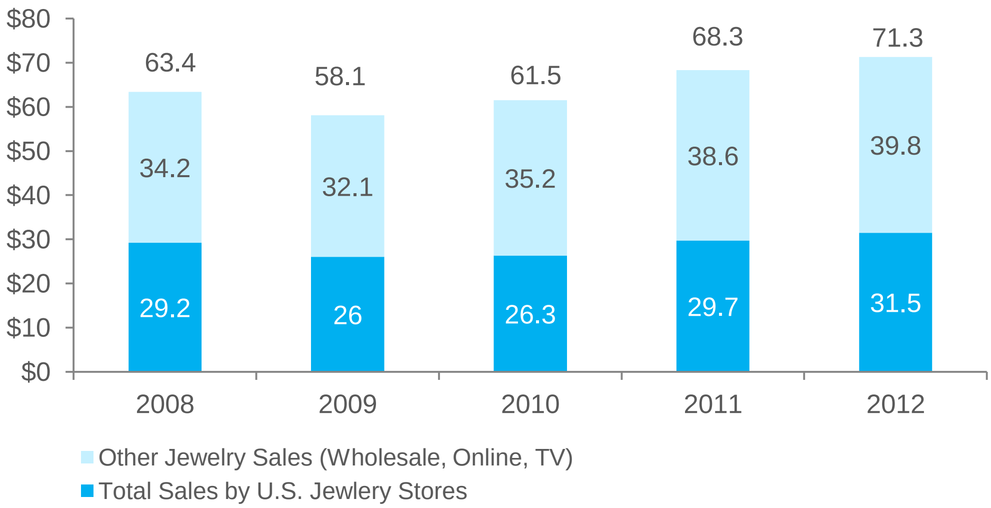
Since 2000, the percentage of U.S. jewelry sales generated by brick-and-mortar jewelry stores has declined from nearly 34% of total industry sales to 30%, with the rate of decline increasing during the recessionary period of 2008 to 2009. This decline continued in 2010 and 2011, however at a slower rate than during the peak years of recession.

Despite market share gains by online jewelry retailers and overall growth in online jewelry sales, customers shopping for bridal jewelry continue to prefer buying from physical retailers. Research indicates that a desire to interact personally with the retailer and the opportunity to handle and try on merchandise remain strong considerations among customers seeking high-ticket bridal items. Some retailers are reporting frustration with a process known as “Showrooming”, whereby potential customers visit physical retailers to try on items and enjoy personalized service, before leaving the retailer to go online and make their purchase at a lower price.

While the bridal market remains elusive for online retailers, sales figures show that U.S. consumers are becoming increasingly comfortable with shopping online for fine jewelry, including high-ticket items. Online-only jewelry retailer Bluenile.com generated sales of $400 million in 2012, increasing revenue by 14.9% over 2011 and netting profits of $75.1 million. The success of an online-only retailer with no brick and mortar stores is an important and ongoing development in the retail jewelry industry. For traditional retailers, the success of Blue Nile provides an opportunity to gain insight into what works for jewelers operating in the online marketplace.

Online sales of fine jewelry and watches continue to grow at a rapid rate.

TOTAL U.S. JEWELRY SALES VS. SALES BY JEWELRY STORES ($B)



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

ECOMMERCE

2012 was a year of significant developments in online retailing and ecommerce technology, some of which will have a direct impact on the retail jewelry industry. Two of the most notable events were the 2012 edition of Cyber Monday, which saw double-digit growth for online jewelry purchases, and the publication of a retail forecast by IBM (based on 22 years of historical data) that predicted large-scale growth for the retail jewelry industry in the 2nd quarter of 2013.

While the accuracy of the IBM study has yet to be evaluated, the adoption of “Big Data” technology to predict and analyze consumer behavior has become a common practice in many industries. For retail jewelers, data analysis will likely become an essential part of sales and marketing, customer retention and promotional initiatives, with further applications in supply chain, quality control, and sustainability efforts.

Jewelry and watches are two of the fastest-growing categories in online retailing.

CYBER MONDAY: TRENDING THE FUTURE

Cyber Monday is one of the few sales events that can provide retailers with valuable, actionable information regarding online shopping trends. These insights allow commercial retailers to make informed decisions when considering how to engage with customers in the digital world.

Total sales for jewelry and watches on Cyber Monday 2012 jumped 17% from 2011, with 25% of online shoppers visiting retailer websites using mobile devices. This figure doubles the 13% of 2011 Cyber Monday shoppers who used mobile devices (smart phones or tablets) to make their purchases.
Shoppers using mobile devices were nearly evenly split in their choice of device, with tablets accounting for 13% of total visits, and smart phones making up 12%. Of shoppers using tablet devices, 91% used the Apple iPad to visit retailer sites, with these users generating 7% of total Cyber Monday sales.

Looking at total visits to online retailers on Cyber Monday, including those that did not result in a purchase, fully 18% of visitors came from mobile devices. This figure represents a 70% year-over-year increase from 2011. Total Cyber Monday sales attributed to mobile users jumped to 13% in 2012, representing growth of 96% over 2011 figures. Social media traffic – which refers to visitors from Facebook, Twitter and other social media platforms - to online retailers drove less than 1% of sales revenue on Cyber Monday 2012, a decrease of 26% compared to 2011. This significant decline illustrates the ever-changing nature of social traffic, as social media users migrate to new platforms, adopt new technologies, and shop online in different ways.

Jewelry consumption in emerging markets has slowed, but remains on the rise.

EMERGING MARKETS

China experienced significantly slower growth of fine jewelry sales in 2012 compared to 2011, dropping from 40.7% in 2011 to 19% in 2012. Growth of total gold consumption in China also decreased, from 27.88% growth in 2011 to 10.09% in 2012. Currently, China is the world's second-largest consumer of gold behind India, and the second-largest consumer of polished diamonds behind the United States. China has also risen to become the world's top consumer of platinum, accounting for 68.3% of global platinum consumption.

India remains the world's largest consumer of gold, with growth poised to increase substantially in both precious metal and polished gem consumption. Some retail surveys indicate a desire by Indian retailers to shift their product focus from gold to diamond jewelry, increasingly so in the face of unstable gold prices. Diamond jewelry sales generally provide a higher margin for retailers than precious metals, even with a much lower sales volume.

Synthetic stones and ethical sourcing are pressing concerns in the industry.

SOCIAL, POLITICAL AND ENVIRONMENTAL FACTORS

Negative public opinion regarding the mining and sale of 'conflict diamonds' and other precious minerals continues to trend upward, becoming a factor for retailers to consider as a new generation of socially and environmentally conscious retail customers enter the fine jewelry market. In 2010, the issue was thrust into the media spotlight after diplomatic cables released by WikiLeaks suggested that World Federation of Diamond Bourses vice-president Ernest Blom was involved in the illegal Zimbabwean diamond trade. This highly-publicized event, combined with an unrelated large-scale synthetic diamond distribution scandal uncovered in 2012, has contributed to political and economic concerns about the integrity and quality of jewelry being sold to the public. The 2012 scandal was uncovered when a laboratory owned by IGI in Antwerp, Belgium tested a sample of polished stones marked and priced as natural only to discover that 60% of the stones were in fact lab created diamonds of very high quality. IGI went on to state that the stones had false 'flaws' introduced during the creation process to create a natural appearance, and that the stones were made with the intent of defrauding buyers. As a result, both the value perception and quality of fine jewelry products should be reinforced and confirmed by retailers and wholesalers at every opportunity. Today's fine jewelry customer tends to be more savvy and more willing to look elsewhere, including online, to find fine jewelry items that meet their high expectations of quality and sustainability. Some buyers seek out Canadian diamonds exclusively when seeking ethically sourced stones, in an attempt to grow supplier support for non-exploitative mining practices.

The retail market for fine jewelry and watches in the U.S. continues to grow.

CHALLENGES AND OPPORTUNITIES FOR RETAILERS

In 2013, slim margins for fine jewelry retailers pose a challenge to the retail jewelry industry as a whole. Erratic pricing can undermine value perception, leading to confusion and dissuading potential customers. Wholesale suppliers find themselves in a dominant position as prices for their goods continue to rise year-over-year.

In an annual report on the global luxury goods industry, titled the Altagamma Consensus, Fondazione Altagamma forecast 8% worldwide growth in the retail Jewelry and Watches industry in 2013. U.S. monthly retail jewelry sales for Q1 and Q2 2013 suggest that sales are exceeding this target, with total U.S. retail jewelry sales increasing by 10.8% in the first quarter of 2013 compared to the same period in 2012. Online retail platforms offer significant growth opportunities for independent retailers and chain stores alike. While overall market share attributed to online jewelry purchases remains comparatively small at 6%, it continues to grow at a steady pace, punctuated by instances of explosive growth driven by technological innovation.

As the post-recession retail landscape continues to evolve, there remain significant opportunities for both independent and chain store jewelers to enter the brick-and-mortar retail marketplace. While discount stores and high-end specialty retailers focus on their respective niche markets, there is still room for growth within the fractured mid-range market. Retailers who adapt to the current landscape and engage potential customers by offering products and service that exceed expectations will be positioned to build a loyal customer base in the long-term.

There remain significant opportunities for growth in the U.S. retail jewelry market.

CONCLUSION

The U.S. retail jewelry industry enjoyed a year of record sales in 2012, however these gains were tempered by slimmer profit margins for retailers. Emerging markets continued to grow, as evidenced by increased consumption of precious metals and polished stones, keeping India as the world's top consumer of gold and China as the world's largest consumer of platinum.

Innovation in data analysis and customer engagement via online sales platforms opened the door to new possibilities for retailers, while challenging traditional business models. Trusted luxury brands continue to enjoy modest year-over-year growth, as department stores experienced a decline in revenues from fine jewelry sales. In the wake of nationwide store closures during the late-2000's recession, currently there is room for growth within the U.S. retail landscape for chain retailers and independents alike. One of the most important revelations of 2012 was the significant increase in the number of customers using mobile devices to buy fine jewelry and watches online. Coupled with documented long-term growth of total online jewelry sales, these trends make a compelling case for the continued growth of the jewelry industry in both the physical and digital realm.

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