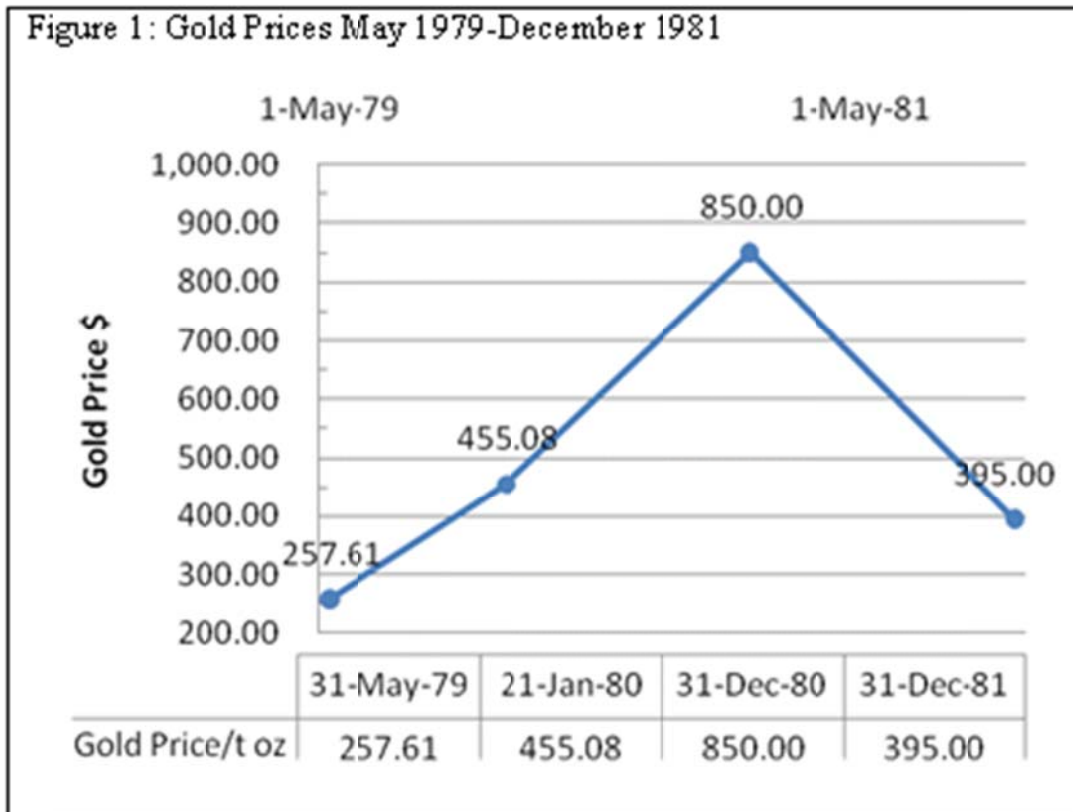


Gold Buybacks Mark Uncertain Times

“A bird in the hand is worth two in the bush”, a 15th century proverb meaning, “it is preferable to have a small but certain advantage than [the] mere potential of a greater one”, may well describe specialty jeweler’s current gold buyback practices. Certainly, since 2008, thousands of independent jewelers have been buying back consumer’s old gold jewelry at an increasing rate. Anecdotal information suggests that a third or more of jewelry companies have made up to 50% of their profits in recent years from buying back consumer’s old gold jewelry. If true, these windfall profits are certainly one example of ‘a bird in hand’ marketing. However, one has to wonder about the “two in the bush”... did they get away? This issue of RJI is about whether buying back old gold costs jewelry companies core jewelry product sales, while making the future more uncertain.

History Is Unclear

Has buying back old gold cost jewelry companies core jewelry product sales, while making the future more uncertain? The answer is unclear, if history is the measure. Some writers have recently suggested jewelers successfully bought back consumer’s old gold when gold prices first ballooned in the 1980’s. That may be partially correct, but if true, the trend was short-lived, lasting only about nine months. Figure 1 illustrates gold price trends from May 1979 to December 31, 1980. More significantly, the era was uniquely different from today when gold was near the height in popularity as an accessory. As such, the period was accentuated by a gold buying frenzy rather than a gold selling craze, when consumers were strongly motivated to buy because they believed gold jewelry prices would be higher tomorrow. Indeed, many jewelers could not keep up with demand, when higher priced gold actually increased both unit sales and turnover. Moreover, because gold prices more than tripled in a short period of time, many jewelers and manufacturers melted old, unproductive, and “toxic” inventory, often recovering more than book value.



Specialty jewelers also witnessed “Silver Mania”, another commodity bubble in 1980. The product

of the Hunt brothers' attempt to manipulate silver prices for much of the 1970's, silver reached a historic high price of \$50/ T oz on January 17, 1980, only to collapse in value on March 26, 1980, "Silver Thursday", declining to \$10.50/ T oz. Nonetheless, when silver hit \$50/ T oz, the event triggered another consumer buying frenzy where about 18 Morgan silver dollars could buy a new refrigerator with change left over for lunch. While some coin collectors and dealers may have melted coins, most bought durables like appliances and jewelry with their old silver coins. Just how wide spread was "Silver Mania", is not clear. However, what is clear, the process was viewed more like a currency exchange versus a silver buyback.

A Half Century of Trust at Risk

Unlike 1980 when the gold price spiked only to immediately decline, today's record price is the result of a decade of continuous increases. Now, with gold prices exceeding \$1,500/ T oz, the combination of high unemployment and escalating food and fuel prices, likely means more consumers are likely to be drawn to gold buying parties, pawnshops, internet gold jewelry buyers, and local specialty jewelry stores to sell the gold in their jewelry. Simultaneously, the cash for gold business has suffered from notoriety for sharp practices and dishonesty as state AG's publicly investigated suspect businesses for alleged criminal conduct, while other firms have been scrutinized by consumer organizations for unfair gold buyback methods. Despite the public scrutiny, the gold jewelry buyback business remains strictly "caveat emptor" or let the buyer (seller) beware. That is not the professional image most specialty jewelers and industry organizations like the Jewelers of America (JA), Jewelers Vigilance Committee (JVC), and the American Gem Society (AGS) have sought to cultivate over the last 50 years.

Gold Buyback Tactics Influence Perceptions

While jewelers frequently offer higher prices for old gold than non-jewelry competitors, that does not mean businesses offering half or less for a commodity that trades daily for at least twice as much on the Chicago Mercantile Exchange (CME) are perceived that to be honest, trustworthy, and professional by consumers, as much as, shrewd, savvy, and street smart. Add specialty jewelers also face a broad range of challenges to their image. For example, social cause marketing raised consumers' awareness of conflict diamonds and gold, intentionally tying, in part, the plight of millions of third world workers to developed nation's demand for fine jewelry products and the jewelry companies that sell them.

Taken together, these issues may be part of an underlying cause for specialty jewelers' loss of market share to non-jewelers selling fine jewelry since 2005. Clearly, there are indirect evidence consumers' view alternative sellers of fine jewelry as having better value. That is especially true for gold products, where value may be defined by today's consumer in terms of a number of factors including 1) fairness, 2) trust, 3) quality, and 4) price.

This suggests, those that believe specialty retail jewelers are actually building their business by taking gold buyback business from historically, less reputable gold-buying outlets, may find they are also losing core jewelry business to non-jewelry retailers selling fine jewelry as an unanticipated consequence. For instance, jewelry stores' market share was calculated to be about 47% at the end of calendar year 2010, a new low and is continuing to decline.

While specialty jewelers' image continues under threat from many sources, including association with other firm's gold buyback practices, jewelry storeowners can differentiate themselves from competitors and reduce the potential negative impact of gold buyback marketing on their business. For instance, jewelry storeowners can position gold buyback programs as a service that includes a range of components including 1) a clear explanation of how gold value is determined, 2) gold price and date, 3) costs of assay and refining, 4) under karating and gold loss, 5) gemstone removal services and cost, and 6) trade-in alternatives. While consumers may not want to know all the details, knowledge of the process, along with related costs and risk means consumers are likely to view jewelers as offering a professional service in contrast to seeing jewelers as traders, looking to make big profits at the expense of the seller. In addition, a

clear understanding of the entire process increases a jeweler's credibility and further establishes fine jewelers as specialists and experts in the gold business versus less skilled competitors.

Managing Ambiguity

The fact some gold buyback tactics are, in effect, about how little one can pay for customers' gold should concern decision-makers in light of continuing and escalating market share losses since 2005. Clearly, consumers have changed their perception of specialty jewelry stores' historic position for expertise, value, and trustworthiness for a variety of reasons, not the least of which may be gold buyback programs and tactics. However, it is also true, cash flow from gold buyback transactions has been a lifeline for many jewelry company owners, struggling to prosper or just survive in this volatile economy.

In the real world, successfully managing ambiguity is essential for survival. It is all about understanding risk and choosing ways to mitigate it. Thousands of gold buyback transactions over several months may do little to change consumers' insight about jewelry stores. However, millions of gold deals over three or four years, in the face of harmful national publicity, has and will continue to change the consumer's perception of the specialty jeweler for good and bad. What is essential is decision-makers recognize these risks and adjust the marketing mix to minimize any erosion of confidence and value that would place the firm in jeopardy.

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