

Business unit overview continued



Above: Namdeb vessel *Ya Toivo* mines for diamonds off the coast of Namibia. Today, about half of Namdeb's production comes from its marine operations

Namaqualand Mines into a new, stand-alone diamond mining company has been announced. The Koffiefontein mine in South Africa was sold to Petra Diamonds Limited in July 2007. Petra also reached agreement with De Beers to purchase the Kimberley underground mines in September 2007, with this transaction expected to be concluded in early 2008. The Cullinan mine has also been sold as a going concern to Petra in a BEE consortium for approximately R1 billion.

The sale of Cullinan, consistent with the company's strategy to operate mines best suited to the future plans of De Beers in South Africa, completes the restructuring of DBCM's portfolio and will lead to improved returns on capital as new projects are commissioned in 2008.

De Beers is fully committed to implementing agreements with government partners that will lead to greater beneficiation in producer countries. Both NDTC and DTCB were established during 2006 to sort and value local diamond output as well as to perform local sales and marketing activities. The new joint ventures with the respective government partners will work towards the development of sustainable downstream diamond industries in Namibia and Botswana.

DTCB is expected to be fully operational in early 2008 and all 16 of the country's licence holders have been approved as sightholders, with contracts concluded for the years 2008 to 2011. In total, approximately \$360 million of rough diamonds are expected to be sold by DTCB to sightholders in 2008.

NDTC announced its client list consisting of 11 sightholders on 3 October 2007. On 29 October, those companies with operational factories as of 18 July received their first supplies for cutting and polishing in Namibia and the remainder will receive supply from 31 March 2008.

With the establishment of the State Diamond Trader (SDT) in South Africa, De Beers and the Department of Minerals and Energy (DME) of the Republic of South Africa have agreed that De Beers will make its management and technical expertise available to the DME for the next three years to facilitate the start up of the SDT. De Beers, like all other South African diamond producers, will be selling up to 10% of its production to the SDT.

Following a review of the DTCL operations, a decision was taken to maximise downstream effectiveness by establishing two separate divisions. The new De Beers Group Marketing (DBGM) unit will now be responsible for the marketing activity previously undertaken by DTCL, while DTCL will concentrate on purchasing, sorting and selling rough diamonds.

Downstream, DBGM continues to drive consumer demand and stimulate growth in the industry through its own marketing initiatives and an increase in advertising programmes by the DTC's clients, its downstream trade partners.

In exploration, De Beers is concentrating on projects in Angola, the Democratic Republic of Congo (DRC), Botswana, South Africa, Namibia, Canada and India. Exploration in the DRC and Angola, in conjunction with partners, is beginning to yield results as projects move from early to advanced stages. Advanced stage evaluation in Botswana has resulted in the potential development of AK06, a kimberlite mine in the Orapa region of Botswana. De Beers is conducting both early and advanced stage exploration activities in Canada focusing on the Slave and Superior craton target areas. In collaboration with Namdeb and DBCM and their associated partners, prioritised early stage exploration is being undertaken in northern Namibia and South Africa, respectively.

Financial overview

The Group's share of operating profit from De Beers increased by 5% to \$484 million. Earnings from joint ventures were higher than in 2006 and there was a modest rise in diamond prices in 2007, although the weakening of the dollar in the second half of the year had an impact on costs and margins. Diamond sales were lower than in 2006, resulting from diminishing supplies of rough diamonds to DTCL from the Russian state producer Alrosa. Underlying earnings at De Beers were higher than the prior year, principally reflecting an increased share of earnings from joint ventures and a tax refund to DBCM, which offset lower preference share income arising as a result of the June 2006 redemptions and higher minorities due to the Ponahalo BEE transaction which was completed in April 2006.

\$ million (unless otherwise stated)	2007	2006
Share of associate's operating profit	484	463
EBITDA	587	541
Group's aggregate investment in De Beers	1,802	2,062
Share of Group operating profit	5%	5%

In the US, preliminary agreement was reached in March 2006 with all of the plaintiffs, which resolved all outstanding class actions in the US and settlements were paid into an escrow account pending conclusion of the settlement process. The matter is proceeding according to the timetable of the Court and De Beers anticipates that a Fairness Hearing will occur in the first half of 2008.

The Court of First Instance in Luxembourg announced in July 2007 that it had annulled the European Commission's decision to accept commitments offered by De Beers to cease all purchase of rough diamonds from Alrosa from 1 January 2009. De Beers will continue to purchase goods from Alrosa, up to the agreed levels and within the proposed timeframe set out in the prior commitments.

In South Africa, De Beers was informed by the DME on 4 February 2008 that it has granted a new order mining right in respect of the Venetia mine, to be executed in March. De Beers has already been granted new order mining rights for Voorspoed and Cullinan and conversions for Namaqualand, Kimberley and Finsch mines are being processed by the DME.

De Beers has made an impairment charge of \$965 million (\$434 million attributable) against its Canadian assets. This non-cash valuation adjustment has been brought about by the strengthening of the Canadian dollar against the US dollar, revised long term crude oil prices, labour cost pressures and the effect of capital expenditure overruns at Snap Lake.

Markets

Early estimates indicate that the all important period from Thanksgiving to Christmas in the US saw sales of jewellery, including diamond jewellery, underperform against analysts' and retailers' expectations – despite a surge in the week before Christmas – with the result that sales are likely to have declined in comparison with prior years. Retail experts point to the 2007 holiday season having started well, but consumers reduced spending amid financial concerns in the worsening economic environment, resulting in soft retail sales across the board, particularly for diamond jewellery. The majority of chains also reported lacklustre sales, with Tiffany, a benchmark for higher end branded jewellers, reporting negative sales growth in the US for November and December. Notwithstanding this, diamond jewellery sales growth was positive in the US for the first three quarters of 2007 and it is likely that full year results will show positive growth, though in low single digits.

Operating performance

In 2007, De Beers' production was 51.1 million carats, maintaining the record production achieved in 2006. Output from the South African operations increased by 3% to 15.0 million carats, mainly due to improvements made to the diamond recovering process at Venetia mine which increased carat recovery by 9%. Output in Namibia rose by 4% to 2.2 million carats reflecting increased production from offshore operations. This offset a 2% decline in production from Debswana to 33.6 million carats. The industrial diamond arm, Element Six, continued to expand and recorded sales growth of 18% and organic growth of 10%.

Projects

Snap Lake in the Northwest Territories of Canada was brought into production in the fourth quarter of 2007. The mine is currently being commissioned and full production of 1.6 million carats per year is expected to be achieved during 2008. By mid-2008, the Victor mine in Ontario is scheduled to enter production and is expected to produce 0.6 million carats of high quality diamonds per year.

In Botswana, Debswana is reviewing expansion opportunities, the most significant of which is for a continuation of open pit operations at Jwaneng until 2022, when a transition to underground mining is planned. In mid-2007, the *mv Peace in Africa*, De Beers' latest marine mining vessel, started operations off South Africa's Atlantic coastline. It is expected to yield approximately 0.2 million carats per annum. Also in South Africa, the Voorspoed mine in the Free State is scheduled to commence production in the fourth quarter of 2008, reaching full production in 2009. Voorspoed is expected to produce 0.7 million carats per annum.

Outlook

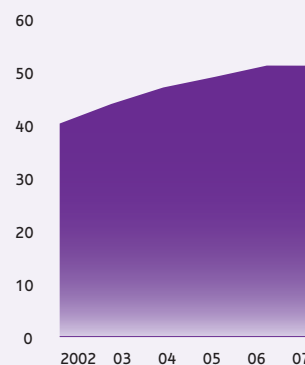
The outlook for 2008 is tempered by uncertainty over global economic growth.

The economic conditions in the US could continue to impact consumer diamond jewellery sales through the first half, particularly at the lower end. Nevertheless, strong demand from China, India and the Middle East is expected, sustaining pricing for larger and better quality diamonds.

Looking beyond 2008, De Beers is confident about the diamond market fundamentals. With strong growth in the emerging markets of China, India and Russia, demand should exceed new supply, with the opportunity for future price growth. In this environment, De Beers continues to focus on transforming itself to ensure it remains the leading company in an increasingly competitive diamond industry.

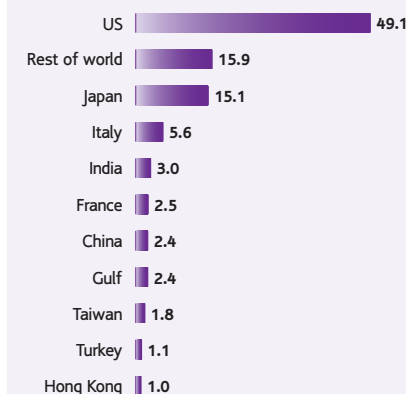
“In 2007, De Beers' production was 51.1 million carats, maintaining the record output achieved in 2006”

DE BEERS PRODUCTION*
Carats recovered (million)



*DBCM, Debswana, Namdeb, Williamson and Canada

2006 SPLIT OF DIAMOND JEWELLERY RETAIL MARKET BY SALES
%



Source: De Beers