

# **Logs and Precious Stones**

## **The Role of Divergent Corporate Strategies in Creating Commodity Tracking Regimes**

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ABSTRACT – Illegal trade with natural resources has become a severe policy problem for resource-rich countries. At present only one international certification scheme exists which was set up in a multistakeholder initiative. The Kimberley Process Certification Scheme (KPCS) regulates trade with diamonds. Whereas in the case of diamonds, the Kimberley Process was able to set up an international certification scheme very swiftly, currently no international attempt can be perceived to devise a similar regime in the case of timber. While acknowledging that various factors account for this variance the paper focuses on the divergent roles corporate actors have played in the different policy outcomes. Although both industry sectors were confronted with the same policy issue, the corporate strategies to counter the problem differed to a great extent. Whereas the diamond industry took an active stance and called for the creation of a commodity tracking regime, the logging industry has stayed very passive for a long time. The aim of the paper is first to analyze how divergent corporate strategies impact on the international regulatory framework and second to explain why these different strategies came about in the first place. The paper thus demonstrates the importance of the specific properties of the different extractive industry sectors when explaining why different regulatory initiatives are set up. More specifically, the paper argues that a specific industry structure, a certain business culture, and corporate leadership are crucial for setting up strong multistakeholder initiatives.

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## **Introduction**

Illegal trade with natural resources has become a severe policy problem for resource-rich countries. Illegal trade contributes to conflict, corruption, the loss of government revenues and environmental degradation. One effective policy tool to fight these illegal activities are commodity tracking regimes which aim at keeping illegal goods out of the legal supply chain.

At present only one international certification scheme exists. The Kimberley Process Certification Scheme (KPCS) regulates trade with diamonds. Whereas in the case of diamonds, the Kimberley Process was able to set up an international certification scheme time in comparatively short time, currently no international attempt can be perceived to devise a similar regime in the case of timber. While acknowledging that various factors account for this variance the paper focuses on the divergent roles corporate actors have played in the different policy outcomes. Although both industry sectors were confronted with the same policy issue (i.e. illegal trade), the corporate strategies to counter the problem differed to a great extent. Whereas the diamond industry took an active stance and called for the creation of a commodity tracking regime, the logging industry has stayed very passive for a long time. The aim of the paper is first to analyze how divergent corporate strategies impact on the international regulatory framework and second to explain why these different strategies came about in the first place. The paper thus demonstrates the importance of the specific properties of the different extractive industry sectors when explaining why different regulatory initiatives are set up. More specifically, the paper argues that a specific industry structure, a certain business culture, and corporate leadership are crucial for setting up strong multistakeholder initiatives.

The remainder of the paper is structured as follows: The following section will briefly introduce the policy field of illegal trade with natural resources and the role of the extractive industries sector. Then, the international initiatives aiming at combating illegal trade will be analysed. The fourth section will analyse how corporate behaviour influences the creation of the specific regulatory frameworks and explains why different corporate strategies were formulated. The concluding section sums up the findings.

## **Natural Resources, Illegal Trade, and the Extractive Industries**

Since the mid-nineties the impact of illegal trade with natural resources has gained both academic and policy attention. In academia the main focus has been the link between the illegal exploitation of lucrative natural resources, such as timber, precious minerals, and gemstones, and armed conflict (see e.g. Berdal and Malone 2000; Collier 2000). However, even if the illegal extraction or trade of the commodities do not fuel civil conflicts social, environmental, and human impacts can be severe as it leads to the loss of government revenues, corruption or environmental degradation.

The paper singles out the markets of two natural resources, timber and diamonds, which attract illegal trade. In the case of diamonds, trade with illegal goods (so-called 'conflict diamonds') has fuelled civil wars in Angola, Sierra Leone and the Democratic Republic of Congo (DRC). Conflict diamonds are defined as rough diamonds stemming from regions controlled by rebel groups. The goods serve as a financial resource to wage war against the legitimate governments (United Nations Security Council 2000). Before the KPCS was in place around 4% of the global diamond output stemmed from illegal sources (Bone 2004). Illegal trade with timber is even more widespread. At present, the international community has not yet agreed on a definition of illegal logging. Gulbrandsen and Humphreys (2006: 3) define it as logging practices and activities violating national law. It is very difficult to give an estimate of the size of the illegal trade worldwide, but a study of Global Witness and the World Bank in Cambodia suggests that the illegal exploitation is at least ten times the size of the legal harvest, valued at US\$0.5-1 billion (Global Witness 1999). Conflict timber has financed rebel groups in armed conflicts in Cambodia, Liberia, Burma, and Indonesia (Global Witness 2002). Apart from fuelling conflicts, the phenomenon of illegal logging has also severe impacts on local communities and the industry. It causes environmental problems as well as economic, developmental and social problems.

The extractive industries play a key role in resource-rich countries. They are the main agents – often in joint venture with host-state state-owned companies – that exploit, trade, and transport the resources. Furthermore, they contribute to a great extent to the GDP of their host-countries. Thus, their relational power in these countries is very high. Although most MNCs claim to adopt a politically neutral position in host countries many of these companies knowingly or unknowingly contribute to conflict or political tensions (Zandvliet 2005). There are a number of ways how international business or small-scale companies can impact in a negative way the political order of resource-rich countries (see Banfield, Haufler, and Lilly

2003). The core problem of the extractive industries in resource-rich countries is the opacity of their business operations which derives partly from their powerful position in the countries. In this regard, regulating trade with diamonds or timber is a difficult task as the trade in both commodities does not follow simple export-import routes (Brack, Gray, and Hayman 2002; GAO 2002). Traders often change trade routes, and the commodities are processed in different countries. Much of the trade is not reported officially. Trafficking is further complicated since the goods are mixed numerous times. The end product, jewellery or pieces of furniture usually consist of different types of timber or diamonds. The producing and processing companies have long ignored the issue by not inquiring to deeply the commodity's origins.

### **The Growth of International Initiatives Addressing Illegal Trade**

The growing concerns of the negative impact of illegal trade with natural resources have led to a flourishing of international initiatives since the turn of the millennium. Given the key role and the powerful position of the extractive industry a prominent policy response are multistakeholder initiatives. They are supposed to address the issue more effectively by including NGOs and MNCs into the negotiations of international agreements. Policy tools to regulate trade are very diverse ranging from intergovernmental commodity tracking regimes to private sector initiatives, such as Codes of Conduct.

### **The Kimberley Process to Curb Trade in Conflict Diamonds**

In May 2000 diamond producing and importing countries along with the diamond industry and NGOs initiated the Kimberley Process which aimed a finding an international solution to the issue of conflict diamonds. After two informal meetings the stakeholders agreed on devising an international certification scheme on a ministerial meeting in Pretoria in September 2000.

The Kimberley Process combines two types of regulation. The KPCS, an intergovernmental certification scheme, was launched after two years of negotiation on January 1, 2003.<sup>1</sup> The scheme is complemented by a self-regulatory agreement of the

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<sup>1</sup> For the following see the Interlaken Declaration of November 2002 on the Kimberley Process Certification Scheme for Rough Diamonds (KPCS), available at [http://www.kimberleyprocess.com:8080/site/www\\_docs/plenary\\_meetings9/interlaken\\_declaration.pdf](http://www.kimberleyprocess.com:8080/site/www_docs/plenary_meetings9/interlaken_declaration.pdf), last accessed September 2, 2005.

diamond industry, the System of Warranties (SoW). The Kimberley Process can be considered as the first serious attempt to regulate trade with a natural resource. It therefore serves as a role model for other natural resources such as timber, oil, or coltan. On top of that, the KPCS is a very strict trade regime in comparison to other commodity tracking regimes (CITES, Basel Convention, Montreal Protocol). The remainder of the subsection will briefly analyse the institutional design of the KPCS. The KPCS will be analysed on the basis of the literature on institutional design (Abbott and Snidal 2000; Koremenos, Lipson, and Snidal 2001).

*Membership* – Despite the fact that the KPCS is a tool of soft law and membership is voluntary, the scheme developed into a global trade regime. Although initially only a small number of diamond producing and importing countries initiated the Process, a large number of countries were attracted to join the negotiations in the later stages. As of October 2006, 46 countries and the European Community participate in the process. Thus, the KPCS includes the diamonds producer countries (e.g. South Africa, Namibia, Canada), countries that engage in diamond sorting and transshipment (e.g. Belgium and Switzerland), and countries with cutting and polishing centres (e.g. Israel, China, India). Furthermore, countries with special interest in retail are members as well (e.g. US and Japan).

With regards to the non-state actors, during the negotiations, the NGOs and the diamond industry were participants with rights equal to the states. In the KPCS they have an observer status but fulfil various crucial functions. Therefore they are now indispensable stakeholders (see section below on control and obligation).

*Scope* – The Kimberley Process does not attempt to totally eliminate trade with illegally mined diamonds. But the KPCS aims at creating a clear distinction between legal and illegal markets. Thus, it is more difficult for illegally mined diamonds to enter the legal market which increases the costs and risks for traders dealing with illegal goods.

The KPCS refers to trade in rough diamonds and requires that import and export of the goods requires a Kimberley Process Certificate. Member-states have to ensure that the goods are traded in tamper resistant containers. Domestic trade of rough diamonds does not require certification.

Since the KPCS only regulates international trade with rough diamonds the industry set up a self-regulatory System of Warranties (SoW) which extends to cut and polished stones. Although not being part of the KPCS, the trade regime explicitly refers to and

endorses the SoW. The SoW certifies on all invoices that cut and polished diamonds as well as jewellery containing diamonds have been purchased from legitimate sources.

*Control* – This indicator refers to the way collective decisions are made. The Kimberley Process is a consensual regime. The KPCS was launched in consensus by the participating states, NGOs and the industry bodies. Theoretically, NGOs and the diamond industry only have an observer status. But since they fulfil crucial functions, all decisions are taken in consensus with the non-state actors.

*Flexibility* – The Kimberley Process allows for a significant amount of flexibility. Essentially due to the hortatory language of the KPCS and the structure of the Process one can consider the regime as a ‘learning network’ (Ruggie 2001). Since participants meet on a regular basis after the launch of the scheme and exchange their experiences three requirements could strengthened or adapted since January 2003. Firstly, monitoring was significantly enhanced in the first ten months of operation of the KPCS (see below on obligation). Secondly, diamond producing countries were very reluctant to agree on the disclosure of trade statistics as this data was considered as both commercial and security sensitive. However, without reliable data on production, imports and export commodity tracking cannot be efficient. As cooperation and consultation continues after launching the KPCS more and more countries are willing to provide this data. Finally, also the SoW could be strengthened as industrial self-regulation is now audited by the companies’ independent auditors.

*Obligation* – The KPCS as well as the SoW are tools of soft law, hence only politically binding. However, the specific set up of the KPCS is based on performance obligation which renders the regime into a *de facto* mandatory (though not legally binding) trade regime. In comparison to other politically binding agreements, the KPCS has strict enforcement measures. KPCS participants are only allowed to trade diamonds with other KPCS participants. Based on human security considerations the regime was exempted from the WTO requirements in 2002. Non-compliant participants can be expelled from the KPCS. For the countries this has serious consequences since it cannot trade in diamonds legally anymore. In comparison to other commodity tracking regimes such as CITES the KPCS monitoring provisions are specifically strict. It is based on a peer review mechanism. The participants have to submit annual reports on their implementation of the certification scheme. Moreover, the Kimberley Process Plenary organises voluntary review visits in order to inspect

implementation of the scheme. Finally, review missions are deployed in cases of credible indications of non-compliance. According to government officials, the peer review mechanism can be considered as a major breakthrough. Although being voluntary, in practice no member can avoid them. Moreover, representatives from industry and the civil society participate in these review missions. In sum, the monitoring provisions are exceptionally strict especially because the non-state actors fulfil an official watchdog function.

### **Combating Trade in Illegal Timber**

Global regulation of trade with timber is still in its infancy. As of October 2006 there has not yet been made any serious attempt to create a coherent global trade regime.<sup>2</sup> Numerous voluntary initiatives of product labelling and certification have flourished in the last decade. Most of the schemes intend to certify that the products derive from sustainably managed forests complying with social and environment standards (e.g. Forest Stewardship Council, FSC, ISO 14000 series). Brack, Gray and Hayman (2002) point out that over forty schemes exist in this category. However, most of these schemes do not explicitly certify that the product derives from legally produced timber. Only the FSC incorporates a chain of custody component.

Since the turn of the millennium the issue of illegal logging is addressed more specifically. The G8 Action Programme on Forests of 1998-2000 reinforced by the 2002 World Summit on Sustainable Development in Johannesburg contributed to increasing awareness of the global problem of illegal logging. Due to pressure of civil society a global response is gaining momentum albeit only in the form of regional or sectoral initiatives (Fripp 2006).<sup>3</sup>

At the regional level the most important policy responses are the Forest Law Enforcement and Governance (FLEG) conferences in East Asia (Bali, September 2001), Africa (Yaoundé, 2003) and North Asia (ENA FLEG, St. Petersburg, November 2005). The FLEG processes foster policy frameworks for political and legislative actions. They are based on a supply-side approach, i.e. they aim at reducing illegal logging at the source in producer countries. However, they have not yielded policy output yet.

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<sup>2</sup> An attempt to create a global agreement on forestry failed at the Rio Earth Summit in 1992 (Brack 2005).

<sup>3</sup> The issue is also discussed in international organizations and regimes such as the UN Forum on Forests (UNFF), the Food and Agriculture Organization (FAO), the International Tropical Timber Organization (ITTO), the Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES), and the World Trade Organization's (WTO) Committee on Trade and Environment. However, these discussions are less advanced than the FLEG processes (Brack 2005; Gulbrandsen and Humphreys 2006).

The European Union complements these processes and launched an action plan (Forest Law Enforcement, Governance and Trade Initiative, FLEGT) focussing on demand-side measures in October 2003 (Gulbrandsen and Humphreys 2006). The action plan consists of voluntary partnership agreements (VPAs) between producer countries and the EU on timber licensing, the adoption by member states of procurement policies stipulating the purchase of timber from legal sources, and promoting private sector initiatives, which include codes of conduct). The VPAs aim at assisting the producer countries in improving their governance and forest management, and implementing a licensing system EU. As of March 2006 negotiations for VPAs still continue. Informal discussions about possible VPAs have been initiated in Ghana, Cameroon, Gabon, the Republic of Congo, Malaysia and Indonesia (Fripp 2006).

As the FLEGT focuses on excluding illegal products from entering the EU market, the heart of the initiative is a new licensing timber system similar to the KPCS (Brack 2006). The European Commission adopted a proposal for a regulation to implement the timber import licensing scheme in July 2004.<sup>4</sup> The EC Council approved the legislation required for the implementation of the VPAs and the licensing system in October 2005. However, the major difference to the KPCS will be that there will be no international agreement which could serve as a framework for the new timber licensing scheme. Hence, the EU has to create one through a series of bilateral agreements with major producer and exporter countries (Brack 2005).

Although the system is not yet implemented there are already some potential problems related to the FLEGT licensing scheme. Most of the issues described in the following paragraph concern the other FLEG processes as well. The major shortcoming of the processes relate to the fact that no global scheme is in place but only regional initiatives. The agreements will only apply to the countries that are participating. In contrast to the Kimberley Process, countries that do not participate in any of the processes cannot be excluded from the international trade in timber. For instance, with regards to the VPAs of FLEGT some countries could simply choose not to enter in an agreement with the European Union in order to avoid regulation. Since the global timber market is bigger than the diamond market exporters from producing countries can afford to avoid regulated markets such as the EU and divert their products to alternative markets, for instance to China (Brack and Saunders 2006). Furthermore, the scheme could be evaded easily by VPA countries as well since the goods can be imported via an intermediary (i.e. non VPA) country. EU customs will not require licensing from non VPA countries.

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<sup>4</sup> [http://ec.europa.eu/comm/development/body/theme/forest/initiative/index\\_en.htm](http://ec.europa.eu/comm/development/body/theme/forest/initiative/index_en.htm)

Five EU member states, Denmark, France, Germany, the Netherlands and the UK, have launched governmental timber procurement policies which are considered as a promising route to building markets for legal timber (Brack 2005). The procurement policy requires all Government departments and their agencies to buy timber and forestry related products from legal and sustainable sources.

Alongside regional processes, a number of bilateral initiatives have developed since 2001. For instance, a UK-Indonesian initiative came into existence as a follow-up of the East Asia FLEG process in 2001. In April 2002 the Governments of the UK and Indonesia agreed on a Memorandum of Understanding (MoU) whereby they committed to reforming legislation and developing systems to prevent actions related to illegal logging. However, the agreement could not be extended to trade measures since such an agreement would only be possible on the EU level (Forest Trends 2006). Although bilateral agreements have certain advantages, for instance they are relatively easy to negotiate, they share the main disadvantage with regional agreements since they are very easy to evade.

The processes and initiatives discussed above stimulated the private sector to respond to the new needs of the demand side. Especially the FLEGT and the introduction Government procurement policies had a significant impact on the corporate sector. For instance, UK's main timber trade association, the Timber Trade Federation, adopted a Code of Conduct which obliges its members to only trade with legal timber products (Forest Trends 2006). However, compliance and enforcement measures are very weak. Individual retail companies with a high public profile launched own policies and Codes of Conduct. Yet, although some self-regulatory measures exist, it is too early to assess their effectiveness.

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International regulation of trade with diamonds differs very much to the one of timber. In the diamonds case an overarching strong international agreement could be set up in relatively short time. In comparison to that, the international community so far only has attempted to regulate trade in timber while not envisaging a global commodity tracking regime. In fact, there is the danger that multiplicity and complexity of processes and Codes of Conduct may prove to be counterproductive in combating illegal trade.

## **The Role of Corporate Strategies in Creating Global Regimes**

International Relations (IR) has long researched the way corporate behaviour influences international politics (e.g. Keohane and Nye 1972; Levy and Newell 2005). MNCs can both enforce and hamper the creation of international regimes (e.g. Sell 2003).

At first sight one might assume that business tends to prefer less international regulation. However, as research on private international regime finds, corporations may think the effective regulation can serve their interests (Haufler 2001). Especially in industry sectors where the power of business is very strong, regulation (whether public, private or public-private) only arises when it corresponds to business interests. The influence of corporate actors on the creation of regulation is reinforced by the flourishing of multistakeholder initiatives (Fuchs 2005). Corporate actors prefer self-regulatory governance or multistakeholder initiatives since these modes of governance enable them to directly influence policy-making while restoring consumer confidence at the same time. MNCs have always tried to influence politics, yet most of the time they were dependent on institutional pathways, like lobbying on the domestic level or international organizations. Multistakeholder initiatives allow corporate actors to speak and vote of their own right at negotiations. They have a direct leverage on the design of norms, their implementation and how they shall be enforced. One should therefore expect that MNCs take an active stance in international politics and try to initiate governance beyond the public-private divide so as to ensure regulation corresponds to own needs.

While the research programme on the influence of corporate behaviour has produced a very good understanding of the political role of MNCs in international relations, the research question how divergent corporate strategies arise in response to the same policy issue is still in its infancy (see e.g. Pegg 2006; Rowlands 2000). The remainder of the section will analyse more profoundly first to what extent divergent corporate strategies account for different regulatory approaches in dealing with illegal trade and second why divergent corporate strategies were formulated in the first place.

### **Divergent Corporate Strategies in the Diamond and Timber Trade**

Although the policy issue is the same corporate strategies evolved very differently in dealing with the issue of illegal trade. As it will be demonstrated below, the diamond industry very quickly called for government action and fully supported the creation of a global certification scheme. This concerted effort is mainly due to the leadership of the key players in the

industry, De Beers and the Antwerp-based High Diamond Council (HRD). In contrast to that the timber industry did not engage in the public debate about illegal logging which had significant impacts on the evolving forestry regime.

*The Role of the Diamond Industry in the Kimberley Process* – Before the governments took action and initiated the Kimberley Process, NGO-industry engagement actually led to increasing awareness of the issue of illegal trade with diamonds and the need for a regulatory trade device.

The diamond industry took leadership in the issue of illegal trade very early on. At the end of the nineties a transnational advocacy network had launched an international campaign against conflict diamonds and specifically targeted the leading corporate actors, De Beers and the HRD in Antwerp. While most of the NGOs aimed at establishing a dialogue with the diamond industry in order to find a solution to the issue jointly, other NGOs like Amnesty International had mobilised their members in order to put the industry under severe pressure. Realising the importance of the key actors De Beers and the HRD, the campaign concentrated on the giants while ignoring small scale companies, individual *diamantaires* or cutting and polishing centres to a large extent.<sup>5</sup>

The diamond sector, especially De Beers, used to be a specifically opaque and reclusive industry (GAO 2002). Although De Beers as a South African company always tried to maintain good relationships to the communities in Africa, the campaign against conflict diamonds was the first time it was attacked publicly by NGOs. The initial stance of De Beers' executives was that the best strategy to counter the campaign was to ignore it. However, as the campaign persisted the executives had to re-evaluate their strategy and concluded that they needed to engage with the leading NGOs. This change of attitude resulted in numerous meetings of the leading NGOs, Global Witness and Partnership Africa Canada, and De Beers which were sometimes very constructive and sometimes very confrontational.

The meetings resulted in De Beers' turn to international leadership in the issue. Firstly, the company called for government action. The NGOs had concentrated on campaigning against the industry and several countries avoiding strong regulation such as Angola, Sierra Leone, Switzerland and Belgium. According to the industry an effective solution to curb trade with conflict diamonds necessitated proper legislation not only industrial self-regulation. Therefore, De Beers mobilised the government of South Africa to take action together with other leading diamond producing and importing countries (Smillie 2005). As a major diamond

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<sup>5</sup> Apart from De Beers and the HRD the retail sector, especially high-profile jewellery shops like Tiffany, were in focus of the campaign (Tamm 2002).

producer, South Africa got very quickly interested in the issue and networked with Botswana, Namibia, Canada and the UK as well as the NGOs Global Witness and Partnership Africa Canada. This marked the beginning of the Kimberley Process.

Secondly, De Beers was crucial in promoting collective action within the diamond industry. Enforcing cooperation and mobilising the diamond dealers was very significant for the Kimberley Process as De Beers could reach the disparate industry players which were almost inaccessible for NGOs and governments. By the time governments, industry representatives and NGOs started the negotiations not all actors in the industry had accepted the need for an international certification scheme. However, so that the KPCS could come into force, full industry support was crucial. De Beers and the HRD in Antwerp took up the lead role in the industry.

As soon as the industry could reach a consensus, the various industry associations created a new body that should represent the whole industry from mining to retail. This was crucial as various industry representatives were present in the first technical meetings of the Kimberley Process but had not coordinated each other. The new World Diamond Council (WDC) bundled industry influence and corporate actors could increase their leverage in the negotiations by speaking with a single voice (Bone 2004). During the negotiations of the Kimberley Process the industry took up a key role as well. A Belgian industry representative became the chair of the Working Group Diamond Experts and Technical Issues. Governments relied heavily on the industry's expertise when devising the scheme.

*The Role of the Timber Industry in the Evolving Global Forestry Regime* – Like the diamond industry the forestry sector was hit by a global NGO campaign. Whereas the diamond industry very quickly took lead action and called for international action, the forestry sector has been long very passive. In fact, with the exception of some companies, most of the firms have been waiting for the governments to take lead action and then respond accordingly. Only recently, after the EU launched FLEGT and several EU member-states issues procurement policies, companies saw a new need to respond to a new business environment. Governments, on the other hand, have realised very quickly that the issue necessitates multistakeholder action. The divergent perceptions of the private and the public sector created a deadlock. Only few companies, especially those with a high public profile, have reacted to the issue early on. Some, like B&Q, a UK company owned by Kingfishers plc., recognized in the mid-nineties the dangers of not knowing exactly the origin of their timber (Toyne 2003). However, none of these companies began to take leadership and find a common strategy to combat the issue.

The divergent corporate strategies can account to some extent to the formation of different institutional frameworks dealing with illegal trade in natural resources. The diamond industry very quickly supported, actually called, for the creation of an international certification scheme. Together with the NGOs they lobbied like-minded governments and even put pressure on the governments while negotiating the trade regime. The logging industry on the other hand did not support the creation of a trade regime but took an attendant position. While there are also other important reasons why no global timber trade regime could be set up, one important explanatory factor is the passive position of the industry.

### **Explaining Divergent Corporate Strategies**

Both the logging and the diamond industry could take advantage of the illegal trade for a long time. But since the policy issue has gained public awareness, the incentive to create an international regulatory framework which eliminates illegal trade is in the interest of both sectors. In fact, the diamond industry and more recently the timber industry have expressed the need for effective commodity tracking regimes to regulate the trade. One should assume that both industries would take up a leadership role in order to ensure that the international regimes correspond to the needs and interests of business. As elaborated in the section above, only the diamond industry took up this role. The paper now turns to the analysis why the diamond and the logging industry pursued different strategies. The discussion will focus on arguments related to the different nature of the products, the industry structure, and the distinctive properties of natural resource extraction.

The first aspect that explains the differences in the corporate strategies in the diamond and logging industry are related to the nature of the product they deal with. The diamond industry trades a product particularly sensitive to reputation and morals and is therefore especially vulnerable to activists' pressure. Diamonds have acquired a high value because they are considered as scarce and as tokens for love and purity. Gems that are tainted with crime, aggression and suffering do not represent a romantic gift. Other than being a pure luxury good diamonds do not have any material use in the economy. Industrial diamonds, which had some material use, are more and more replaced by artificial diamonds.<sup>6</sup> Despite their limited use to

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<sup>6</sup> Industrial diamonds and gem quality diamonds are found in the same kimberlite pipes. As a result all diamond mining and distribution companies, including De Beers, trade both categories of diamonds. In contrast to industrial diamonds, gem quality diamonds are very rare and only account for about 15-17% of the total production. But the gems yield more than 80% of the value of the global diamond market (Yakovleva 2005). Economically speaking, industrial diamonds have always been insignificant for the industry sector.

man diamonds create significant wealth foremost in diamond producing and processing countries. The diamond industry is relatively small. From mining to retail, around 2 million people are working in the industry worldwide. On the upstream side the global diamond production is worth US\$7.5 billion. Further downstream, the diamond jewellery retail is valued at US\$13.7 billion (Even-Zohar 2002).

In contrast to the global diamond market, the forestry industry is a major global sector. In 1998 the gross production accounted for US\$160 billion world-wide (of which US\$105 billion in OECD countries). Thus, it represents 0.4% of value-added in the global economy. Southern companies, particularly those based in South-east and East Asia are becoming important market participants (Brack, Gray, and Hayman 2002; OECD 2001). Forestry products are important commodities of international trade. Their economic importance has repercussions on corporate behaviour. Whereas the diamond industry is dependent on a morally unimpinged reputation, the timber industry is not as vulnerable to consumer pressure. Thus, although the global pressure campaign against illegal trade with timber was launched before the campaign against conflict diamonds, the latter could yield more public awareness and political change. Or, as one activist in an interview with the author has put it: “Diamonds are sexy, logs aren’t”.

Another important reason for different corporate strategies lies in the variance of the industry structure of the logging and the diamond sector. In comparison to other industries, the diamond industry is structured in a considerable hierarchical way. Although the sector has changed since 2001,<sup>7</sup> the most important and influential actors were De Beers and the “narrow funnel” of the diamond entrepôt in Antwerp represented by the HRD (Smillie 2005).

In order to get the industry into line, De Beers used its discursive and structural power. The power of De Beers has two facets.<sup>8</sup> On the one hand, De Beers controlled supply and demand of diamonds which translated into an enormous financial capacity and the ability to cut off dealers from the supply chain. On the other hand, however, De Beers only rarely needed to exert (or threaten) with their instrumental power as the company also has a lot of discursive power. This discursive power stems from the fact that every diamond dealer knows that no other actor had put so much effort and money into preserving the industry and constructing the value of diamonds as De Beers (Even-Zohar 2002). Thus, De Beers can be a

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<sup>7</sup> Since then, the diamond industry has changed significantly. Due to new diamond explorations in Canada diversification has taken place and new companies such as BHP Billiton or Rio Tinto have become important taking significant power from De Beers. Furthermore, in 2003, De Beers switched from a custodial role to a ‘supplier of choice’ and only controls up to 40 % of the diamond supply (Shor 2005).

<sup>8</sup> On the three facets of business power see Fuchs 2005.

leader of the industry. To a lesser extent the HRD which represents the diamond industry of Antwerp has leading functions as well.

The two leading actors, De Beers and the HRD devised a strategy how to react to both, the activists' campaign and the issue of illegal trade. A certification scheme would re-install consumer confidence and curb illegal activities. They favoured a light, cost-effective trade regime. Fearing burdensome public regulation, the corporate actors realised they had to be part of the solution if not be a leader.

De Beers, and to a lesser degree the HRD, diffused a common business strategy in two ways. After the first technical meeting of what later became the Kimberley Process, De Beers realised at last that the issue would not disappear from the global agenda anymore. One month later, the company sent letters, signed by Nicky Oppenheimer, chairman of De Beers, and Gary Ralfe, Managing Director, to the Presidents of the World Federation of Diamond Bourses (WFDB), the International Diamond Manufacturers' Association (IDMA), and other industry bodies and diamond bourses worldwide. In these letters they not only called for a collective response to the issue of conflict diamonds but also urged the diamond bourses to expel any member caught trading with such goods (De Beers 2000; Hart 2003). This demonstrated that De Beers was taking the situation very serious and, thus, served as a 'wake up' call within the industry. Some weeks later, the Antwerp Diamond Bourse addressed the issue as well and started to call for united efforts (Antwerp Diamond Bourse 2000).

De Beers diffused the new strategy not only in letters and public speeches but also directly approached corporate actors and confronted them with the issue. Through its system of 'sightholders',<sup>9</sup> De Beers was the only body that had personal contacts with every disparate part of the industry. The company used its influence in order to arrange several meetings with diamond dealers in order to discuss the issue. In these cases, De Beers also acted as a facilitator for NGOs helping them to get into contact with traders.

In contrast to that the logging industry lacks a key player that has both significant market power and legitimacy to promote collective action in support for a global trade regime. Although the logging industry shares the interests of the diamond industry (the creation of a light, cost-effective certification scheme to re-install consumer confidence) no common strategy was devised. Rather, leading MNCs were hesitant to devise their own Codes of Conduct since a global regulatory framework was missing and being a first mover was considered to be a comparative disadvantage. Whereas the diamond industry could establish very quickly a consensus on the issue and possible strategies, many issues remain contested

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<sup>9</sup> The clients of De Beers are called 'sightholder'.

within the logging industry. For instance, one problem related to the effectiveness of private sector initiatives is that there is only little consensus within the logging industry about issues such as a workable definition of legality or credible auditing frequencies (Brack and Saunders 2006). These issues also arose during the Kimberley Process with regards to the intergovernmental scheme KPCS as well as the self-regulatory scheme SoW. Yet the industry could find a consensus very quickly.

Another aspect needs to be taken into account in order to explain differences in the corporate strategies between the diamond and the forestry sector. Historically, extractive industries like mining have built up long-term relations with the communities they work with. This is mainly due to the specific properties of the extraction. Mining tends to employ a large workforce and its operations are usually long term. As all mining, diamond (kimberlite)<sup>10</sup> mining is a capital-intensive business. It often takes several years to advance from discovery to extraction and costs amount to US\$80 million or more (Voss 1998). Among the extractive industries, the mining sector therefore has taken lead in establishing good company-community relations in order to address the social, environmental and human challenges related with mining operations (see e.g. Yakovleva 2005). Corporate social responsibility is a long accepted norm within the mining industry. In contrast to that, logging companies usually operate in one area only for a period of several months before moving to another one. Logging companies do not see the need of establishing good community relationships (Zandvliet 2005). The difference in attitudes is an important explanatory variable in order to account for different corporate strategies addressing the issue of illegal trade as it demonstrates that logging companies tend to focus on short-term solutions.

## **Conclusion**

The paper has analysed the formation of different regimes in the diamond and the logging sector to combat illegal trade with natural commodities. It suggested that divergent corporate strategies account for the creation of different regulatory frameworks. The diamond industry very quickly called for an overarching international commodity tracking regime and made its expertise available in order to create a light, efficient but cost-effective scheme. Such leadership did not develop in the timber industry. The outcome is a very fragmented

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<sup>10</sup> Kimberlite mining is industrial mining. In contrast to that alluvial mining are small-scale operation using rudimentary tools.

regulatory framework which is still in its infancy. Although both industry sectors should have had the same interest in setting up a certification scheme, only the diamond industry was able to devise a common strategy because of its hierarchical industry structure. Also, due to the nature of the product, diamonds, forced the industry to act. Finally, different business attitudes seem to account for divergent corporate strategies as well. The paper, thus, could demonstrate that corporate leadership can be an important factor when setting up multistakeholder initiatives.

Corporate behaviour and different corporate strategies are one important aspect in explaining why no overall timber trade regime is created. However, also other factors, which were largely ignored for the purpose of this paper, have to be taken into account. Two aspects seem to be of special significance which facilitated regulation in the diamonds case. Firstly, illegal activity was confined to Africa. In contrast to that, illegal logging although concentrated in certain regions in Africa and East Asia, is a global phenomenon. Therefore, the set of problems that are related to the illegal trade are more diverse. Secondly, the KPCS is specifically effective because diamonds are easy to certify. They are small goods and can be put into tamper-proof containers accompanied with forgery proof certificates. Setting up a licensing scheme for timber comes with some challenges as most wood products, such as logs are bulky. These factors should be researched more profoundly in order to be able to explain the different frameworks of regulating trade with diamonds and timber.

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