

FINAL TRANSCRIPT

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HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

Event Date/Time: Dec. 11. 2008 / 9:00AM ET

Dec. 11. 2008 / 9:00AM, HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to Harry Winston Diamond Corporation fiscal year 2009 third quarter conference call. At this time, all participants are in a listen-only mode. We will conduct a question-and-answer session towards the end of today's conference. (OPERATOR INSTRUCTIONS) As a reminder, ladies and gentlemen, this conference is being recorded for replay purposes. I would like to turn the presentation over to your host for today's call, your Chairman and CEO, Robert Gannicott. Please proceed.

Robert Gannicott - *Harry Winston Diamond Corporation - Chairman of the Board, CEO*

Thanks. Well, good morning, ladies and gentlemen, and welcome to the Harry Winston Diamond Corporation earnings call for the third quarter of the financial year 2009. The third quarter has certainly been a challenge for us operationally on the mining side of our business and compounded by sharp and unpredictable changes in the rough diamond market as the industry struggles to comprehend the effects of credit constraint and general global economic conditions. Our sales in jewelry and watches improved during the quarter compared to the prior year and the prices for polished diamonds have only suffered modest declines compared to the more volatile rough diamond market.

Dec. 11. 2008 / 9:00AM, HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

Fortunately, mine production levels have returned to normal during October and November. At the grade in the A154 South kimberlite pipe will return to reserve grade levels and mining services became available in the A 418 open pit .

Subsequent to the quarter, we suffered an armed robbery in Paris where approximately \$30 million of inventory at cost was stolen. Our staff, although traumatized and physically assaulted in a few cases, are recovering well, I am very pleased to say. The loss is insured, and like all such claims, is subject to ongoing investigation. I will hand the call over to Alan Mayne, our Chief Financial Officer, to discuss the financial results in detail. Tom O'Neill, our President in charge of the jewelry and watch business will follow-- I am sorry will follow Alan with a review of that business. I will then return to discussing the mining and rough diamond

Alan Mayne - Harry Winston Diamond Corporation - VP, CFO

Thank you, Bob, and good morning. In the face of a challenging production environment at Diavik, a subdued rough diamond market, and a weakening global economy, consolidated sales decreased 16%, and earnings from operations were down 35% for the third quarter this year compared to the prior year. Our foreign currency exposure has material influence on our reported net earnings. During the third quarter ended October 31st of 2008, the Canadian dollar weakened against the US dollar. This resulted in a \$49 million net foreign exchange gain in the quarter compared to a \$40.6 million net foreign exchange loss in the same period last year. Taking into account this foreign exchange gain, our interest expenses, other income and income tax expense, we reported net earnings of \$71.9 million or \$1.17 per share, compared to a net loss of \$7.4 million or \$0.13 per share in the third quarter last year.

In the third quarter, cash flow from operations decreased 21% to \$48.3 million. However, our investment and capital assets decreased to \$39.7 million from \$60.5 million in the comparable period of the prior year. This decrease occurred in both the mining and retail segments and reflects a decision to incur only essential capital expenditures.

Net debt, excluding restricted cash balances as at October 31st, 2008, was \$278.5 million, compared with \$294.6 million as at January 31st, 2008.

Now, let me spend a few minutes on the financial review of the mining and retail segments. As highlighted in our results release yesterday, our share of production from Diavik was down 26% in the third calendar quarter. Mining sales were also down 26% as the Company reduced the size of its sale of rough diamonds in October to reflect the lower demand associated with the factory closures around Diwali, the Indian festival. The impact of the decrease in sales was reflected in a reduction in earnings from operations to \$47 million from \$70 million in the comparable period last year.

The retail segment recorded a 8% increase in the sales in the quarter. Sales for the third quarter started off strong, consistent with the second quarter of this year, but weakened as the global economy declined in the latter part of September. The gross margin rate, excluding the impact of sales of pre-acquisition inventory, was 48.6%, compared to 52.4% in the comparable period last year. This decrease in gross margin is the result of the product mix sold in the quarter, in particular, a lower proportion of higher margin sales in the Japanese market and the higher research and development cost to support the watch business. The retail segment recorded an increase in SG&A expenses of \$2.1 million in the quarter; however, the ratio of SG&A expenses as a percentage of sales remained consistent with the comparable quarter of the prior year at 53%.

I would like to now spend a few minutes discussing the Company's liquidity. The Company's mining and retail segments maintain separate financing arrangements, and management assesses liquidity on a segmented basis. The retail segment's cash requirements are for cash operating expenses, working capital, and capital expenditures. The Company believes that cash on hand, cash generated from operations, and access to credit facilities will be sufficient to meet anticipated cash requirements for the retail segment in the next fiscal year.

Dec. 11. 2008 / 9:00AM, HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

The Paris robbery does not effect our ability to borrow under the revolving credit facility. The stolen inventory will be replaced in the borrowing base by accounts receivable, and the available headroom is unchanged. Management expects to operate the retail business to ensure continued compliance with the covenants contained in the revolving credit facility.

The mining segment's cash requirements are for cash operating expenses, working capital, capital expenditures, and contractual debt repayments. The Company believes that cash on hand and cash generated from the sale of rough diamonds will be sufficient to meet anticipated cash requirements for the next fiscal year, excluding certain debt repayments.

The Company anticipates refinancing approximately \$50 million by June, 2009. However, the weakening of the global economy could reduce our ability to generate cash from operations, which could require us to refinance approximately \$75 million by March 2009. The Company is currently in discussions with a credit provider which, if successful, would provide debt financing in an amount sufficient to refinance the \$75 million of debt in the first quarter of next year. In the interim, the Company expects to continue to be in compliance with the covenants contained in the mining segment's credit facilities.

Now, let me turn the presentation over to Tom to discuss the retail business in more detail.

Tom O'Neill - Harry Winston Diamond Corporation - President

Thanks Alan. Good morning, everybody. After a very strong first half in our current fiscal year, while we were tracking at a year-on-year sales increase of about 23%, Harry Winston's retail and wholesale business experienced some impact from the global economic conditions in the third quarter. We experienced relatively strong performances in the US, in Asia, and in the Middle East, with mixed results in Europe, while we saw continued weakness in Japan. Overall, we continued to show solid results against the previous year but certainly less robust than in the first half of the year. Our global customer base insulated the core of our business during the third quarter, allowing us to record an 8% increase in sales over the same period last year.

The sales breakdown by country, that is to say, where the customer is from, rather than where the customer shops, continued to rebalance our sales more evenly throughout the world. For example, for third quarter fiscal 2008, our US clients comprised about 35% of our retail store business, while for the third quarter of this fiscal year, our US clients dropped eight points to 27% of total retail sales. Our Japanese clients dropped three points to 34% while the rest of Asia increased five points to 16%. And Europe, excluding Russia, increased two points to 12%. Russia increased six points to 7%, while the Middle East showed a very small decline.

Product sales mix continued to track at the high end through the quarter where we saw an increase of more than 20% in significant sales that we defined as greater than US dollars \$250,000. Our business is significantly skewed towards the high end where margin dollars are considerable while absolute profit percentages tend to be less than at the lower end of the product range. Our volume was off more in the middle rank of price points than in the lower price points. It indicates to us that while the customer base continued to buy in the third quarter, it was the middle of the product range that had been most effected by the economic environment, while products at the entry level price points and the significant sales at the high end showed comparative strength.

In terms of the Japanese business, which is largely conducted within Japan, exclusive of traveling tourists, any fluctuation in sales has a direct impact on our operating profit. Our business in Japan is much more of a volume business at more modest price points to carry larger gross margins than the lower volume high end of the sales mix. The weakening of our Japan business in the third quarter, where the sales mix is decidedly at lower price points but with higher margins and coupled with the increase in our high end lower margin business elsewhere in the world, have eroded operating margins for the third quarter.

On December 4th, we suffered an armed robbery in our Paris salon, which has been mentioned. As we have said, our employees are our first concern, and we are making every effort to care for our staff. I will tell you that we are working on reopening the salon as soon as possible, and we are appreciative of the work of the authorities and our insurance carrier in this very unfortunate

Dec. 11. 2008 / 9:00AM, HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

matter. Please note that we do have insurance; however, due to the ongoing investigation, we cannot comment any further than we have, nor can we provide any figures and information beyond what Alan and Bob have reviewed a few moments ago. We continue to cooperate with the authorities in their investigation over the incident.

The challenges that the global economy has presented to us have impacted our business in the third quarter. We don't see this changing in the fourth quarter and are managing it accordingly. The setback in Paris will certainly effect our holiday season to some extent, but the core business there is with wealthy international clients and can be readily shifted to other locations. We remain committed to our strategy of strengthening our retail segment through our own network of stores, through our wholesale jewelry business, and through our established watch business going forward.

Thanks, and now I will turn it back over to Bob.

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

Thanks, Tom. Production of the Diavik mine continued well below plan throughout the third quarter, as Alan referred to. The (inaudible) identified in the year continued, less than-- 26% less carats produced than during the prior third quarter. After reaching a zenith in August, rough diamond prices sort of stalled out September, and then declined sharply in October, bringing them eventually back to the levels of the prior year. Although painful, this decline is modest compared with other exchange traded commodities. Each mine produces each own unique mix of diamonds, and each producer has its own sales methodology. Our own system, focused on delivering on narrow assortments to long-term customers, has certainly moderated the effects of the market turmoil for us, which is being led by auction sale as the rough market struggles to find a new base. The price decline in polished diamonds varies according to size and qualities, but it is generally only in the single digits, suggesting that rough prices would recover promptly when liquidity reappears to a depleted pipeline.

At the Diavik mine, the grade of A-154 South is now fully returned to reserve grade levels, and the new A-418 pit now has reserve grade ore fully available for mining. Production in each of October and November exceeded one million carats, and it is reasonable to expect that we will end the year close to a 10 million carat forecast. Capital and operating budgets for the coming year are under review by Rio Tinto as all business throughout the world focus on operational and operational efficiency in challenging times.

To attempt a forward view of the diamond market would be pretty much pointless at this stage. Our key strength, though, is the Diavik ore (inaudible) are among the highest margined diamond resources in the world. The majority of the world's diamond production would become unprofitable well before Diavik would lose its cash operating margin. This kind of fundamental resilience is more important than ever in the conditions of the day. I don't really want to say anything more than that formally, but thanks for listening to us, and we are now happy to take your questions.

QUESTIONS AND ANSWERS

Operator

(OPERATOR INSTRUCTIONS) We will wait one moment while the question is compiled. First question comes from the line of Irene Nattel from RBC Capital Markets. Please proceed.

Irene Nattel - RBC Capital Markets - Analyst

Thanks and good morning, everyone. I was wondering if you could you just address what you are seeing in the market place as we have moved through Q4, both from the retail demand perspective as we've seen commodity prices continue to come

Dec. 11. 2008 / 9:00AM, HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

down, what you are seeing and you are experiencing from a rough diamond pricing perspective, and whether as we look into F '10, you would give any consideration to perhaps reducing the number of your rough diamond sales.

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

Well, I will start with rough diamonds since the question comes to me, and then I will let Tom have a go at the retail. I guess on the rough diamond side, the only bit of perhaps good news at the moment is there does seem to be a sense of some sort of stability returning to some extent. Some customers that have disappeared back in October that are now got their hands up again to come back in on the market and so on. I would stress that that-- one has to look pretty hard at the moment for signs of stability. Going forward from here, obviously, the process that is going on at the moment is classic deleveraging. There is a diamond supply chain known as the diamond pipe line, as you know, and that is being emptied out as the jewelers at one end don't replace sold inventory because of concern about looking forward. And that means they don't reorder jewelry. That means the jewelry manufacturers don't reorder polished. That means the people that are polishing rough diamonds don't need any rough diamonds in the meantime. The market is some what stuck at the moment, but perhaps a sign that it is opening again.

Would we consider reducing the number of sales? No, because a lot of our regular customers depend on regular supply to feed their factories, and many of these businesses are-- most of these business are still moving forward in a quite significant way.

Would we consider withholding back some material that's difficult to sell during this sort of period? Yes, we would. In fact, we do have some quite modest-- but we do have some stocks on hand at the moment.

So, Tom, would you like to address the retail side?

Tom O'Neill - Harry Winston Diamond Corporation - President

Sure. Hi, Irene. Alan talked a little bit about the third quarter in terms of our retail segment sales. August, actually, the first month of the quarter, was fairly strong. It was consistent with the first six months. Even the first two weeks of September were good for us. We hit a point in mid September where business became very difficult, but then in October, it went up again. So it was spotty for us through the third quarter. As we go into the fourth quarter, of course, we will recap the fourth quarter at the end of the quarter. But if we look at what happened in terms of the sales in the third quarter, where they are concentrated and where they are focused, we are seeing, strangely enough, at the high end of the market, there is still activity, and it is good activity for us. And at the lower price points, or the entry level price points, because it is the holiday season we would certainly see that that would be very similar to what it's been in the past.

Irene Nattel - RBC Capital Markets - Analyst

One of the things I was thinking about, Tom, this paradoxically could prove to be a bit of a demand boost to your watch business as people perhaps trade sideways, or, if you get a very beautiful Harry Winston watch, the price point is probably lower than a very beautiful Harry Winston piece of jewelry, but yet, it is still a beautiful gift. Are you seeing anything like that?

Tom O'Neill - Harry Winston Diamond Corporation - President

Not really, because the watch is probably less holiday gift driven but occasion driven and pretty much consistent through the year. Though, not so much. If it were to happen, of course, we would be very happy to accommodate the customers that want to move over from jewelry to watches. What we are seeing is at the higher end, the \$250,000 plus, there is activity there. And this year, like previous holiday seasons, we don't really get going until about now, around the 10th. And the better the retailers get at providing last minute shopping, the more accustomed our clients become in putting it off until later and later. Now with the globalization of our business, there is a much longer holiday selling period. Fifteen, twenty years ago, you could say by

Dec. 11. 2008 / 9:00AM, HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

December 24th, the business is going to do what it is going to do, and that's it. But we have now the Eastern European customers, so we have the Orthodox Christian New Year and Christmas. We have the Japanese gift giving opportunities around the first of the calendar year, and as we push towards the end of January, which is our last fiscal month of the year and of the quarter, we have the starting of Chinese gift giving around Chinese New Year. So it is a different landscape for global companies now, and while we certainly-- December is quite important for us, January becomes increasingly important for us.

Irene Nattel - RBC Capital Markets - Analyst

One final question, if I might. I know Tom said you weren't going to provide more color around the whole issue of the robbery, but can you tell us whether the insurance is at cost or at something more approaching retail value?

Tom O'Neill - Harry Winston Diamond Corporation - President

Perhaps Alan, are you in a better position to come men.

Alan Mayne - Harry Winston Diamond Corporation - VP, CFO

No, Irene. Sadly, we have a precedent for this type of incident. That's all I would say. I would guard to the precedent and leave it at that.

Irene Nattel - RBC Capital Markets - Analyst

That is very helpful, Alan. Thank you.

Operator

Next question, please. The next question comes from the line of Brian MacArthur from UBS. Please proceed.

Brian MacArthur - UBS - Analyst

Good morning. I was just wondering if we could flush out the near term refinancing a little bit more. Is this a-- if I look at this correctly, you've got \$25 million in debt repayments under the large loan you have to do in the next two quarters. You are going to obviously still generate pretty good cash from the mine as you said, from the point view, your margins, well maybe they're down, they are still very high. But is this just a-- I am surprised you have to refinance in the next little while and it would be as high as \$75 million. Is this just a working capital problem, getting everything up the road? Or can you just go through a little more, as much as you can, exactly what is happening there? I would have thought you'd still generate-- and I notice CapEx over the next-- you give as guidance over the next few years of \$180 million. Maybe it comes in the first two quarters. But I am just surprised. Is this a near term issue? I am surprised if you are looking on an annual basis that you are facing that.

Alan Mayne - Harry Winston Diamond Corporation - VP, CFO

Brian, there is a couple of things. Right now, we are sort of saying, the debt schedule is such that, by the end of the year on the mining side, we will have \$75 million due, \$25 million due in March roughly \$20 million in June, \$15 million in September, and \$15 million in December. The one thing that you may not have taken into account are the cash taxes. Which are, as you know, expected to be fairly significant next year, and they will happen certainly by the first half of the year. So, based on where we have modeled, and taking into account significant cash taxes, we would be looking at refinancing at least the \$50 million that would be remaining outstanding as at June 30th.

Dec. 11. 2008 / 9:00AM, HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

Brian MacArthur - UBS - Analyst

Right. So, it is the cash taxes that you are paying in the early part of next year for this year, effectively.

Alan Mayne - Harry Winston Diamond Corporation - VP, CFO

Essentially, yes.

Brian MacArthur - UBS - Analyst

So, it is the working-- as well as-- and I assume there is a bit of a working capital draw over the winter as you pull everything up to the mine as well. And it is those two things that really--

Alan Mayne - Harry Winston Diamond Corporation - VP, CFO

Yes, there is. But the cash tax is the plug in the model that is a significant cash outflow next year. And just to be clear, on the revised numbers we have given on CapEx, a lot of that is going to occur next year as the underground development is largely completed.

Brian MacArthur - UBS - Analyst

Right. So the majority of it, your share of (inaudible), there will be a hunk of it again next year.

Alan Mayne - Harry Winston Diamond Corporation - VP, CFO

Absolutely. Out of that, probably, depending on the exchange rate you use, about \$83 million for the underground and probably another \$20 million for sustaining. You have probably got \$100 million next year and then roughly \$20 million of sustaining thereafter. I think that's a good indication of the cash flow profile. But next year is big on CapEx and cash taxes.

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

Could I add a slight caution to that. The Rio Tinto's capital budget for next year is under constant review, and it's going to remain that way, frankly. Under the current circumstances of the markets of the day, Rio will continually look at the capital program and there may well be, in fact there almost inevitably will be changes as we go along, Brian. So you shouldn't regard it as something that's cast in stone for the year.

Brian MacArthur - UBS - Analyst

But to some extent, you have to keep the development of the underground going so you don't get behind in the future, right, like there's not--

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

Sure. There are things that are needed to actually keep the project intact, including its future intact, will be done, but there are other more elective things that could be deferred.

Dec. 11. 2008 / 9:00AM, HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

Brian MacArthur - UBS - Analyst

Great. Just to be very clear, the \$83 million and \$20 million you are talking about, Alan, was that US at a Canadian \$0.95 exchange rate again?

Alan Mayne - Harry Winston Diamond Corporation - VP, CFO

It is the \$83 is at \$0.98, and the \$20 million is at about \$0.98 as well.

Brian MacArthur - UBS - Analyst

Okay. Thank you very much. That helps clear it up a lot.

Operator

The next question comes from the line of David Christie, from Deutsche Capital. Please proceed.

David Christie - Scotia Capital - Analyst

I've changed shops. I am Scotia Capital, just so everyone knows. Anyway, just a couple of quick questions. First, the security at the Paris facility there, you guys had a robbery a couple of years ago. What did you do after that for security, and what will you be doing in the future?

Alan Mayne - Harry Winston Diamond Corporation - VP, CFO

Sorry, David, we can't discuss it at all. Obviously, we can't discuss what our security arrangements are. But during this police-- while we are in the period of the police and insurance investigation, we just can't say a thing. I don't want you to think we are being rude. We are just not allowed to.

David Christie - Scotia Capital - Analyst

Okay. Just sort of odd-- two robberies in two years. It's a little different. Okay. Next question. On the debt that you do have outstanding, could you give us an idea what the covenants are on the various debts?

Alan Mayne - Harry Winston Diamond Corporation - VP, CFO

I can give you a qualitative overview. Our mining credit facilities are filed on SEDAR. I think the thresholds on the covenants are probably unavailable. But we have certain covenants there that are related-- driven off net present value calculations of the value of the mine, which are confidential between ourselves and our banks. There are other more traditional coverage covenants there, and they are largely, those coverage covenants are largely historically looking, and as I mentioned in my comments, we are in compliance and expect to be in compliance with those covenants. On the retail side, the covenants are of a more traditional nature. There is a tangible net worth covenant, a leverage covenant, and a fixed charge covenant that has driven EBITDA and an interest expense. So, the thresholds remain confidential, but what I say is that we know where the covenants are. We have a number of scenarios at which we can manage the retail business to ensure that we continue to be in compliance with those covenants.

Dec. 11. 2008 / 9:00AM, HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

David Christie - Scotia Capital - Analyst

If you have like a 5% negative growth in retail sales in 2009, are you going to have a problem?

Alan Mayne - Harry Winston Diamond Corporation - VP, CFO

No, because the covenants aren't just driven-- sales obviously flows through the EBITDA, but there are other metrics in the mix that management has discretion over the amount of those metrics, and we can make adjustments there. And as I say, we have run our own models, and there are levers we can pull to ensure that we stay in compliance next year.

David Christie - Scotia Capital - Analyst

When are you going to know for sure whether you are refinancing those amounts? Are you are in negotiations now, or is that something you are waiting to do later?

Alan Mayne - Harry Winston Diamond Corporation - VP, CFO

No, we are in discussions right now. And we expect those discussions, if successful, to be concluded into the first quarter. If we get to a point where we are in the process where by it is either prudent or required for us to disclose the status of the discussions, then we will do so.

David Christie - Scotia Capital - Analyst

Okay. It is all over a debt repayment schedule, basically, you need to refinance them on.

Alan Mayne - Harry Winston Diamond Corporation - VP, CFO

Essentially what we are, in a nutshell, what we are aiming to do is shift \$75 million of principal payments that come due next year, out certainly beyond next year. That's the major objective of the refinancing exercise.

David Christie - Scotia Capital - Analyst

That will definitely save you there for sure.

Operator

The next question comes from the line of John Hayes from BMO Capital.

John Hayes - BMO Capital - Analyst

Hi, Bob. I have a question on the new mine plan. As I am reading through the commentary on the forecast going forward and the outlook. I notice that there is a section there saying that you are hoping you will reduce the CapEx and the operating costs, and I am just reading into this a bit, but I was wondering if you could help me out here. Does that mean there is going to be a greater reliance on open pit mining of 418 for the next period of time, and could we see a further push out of the under ground mining?

Dec. 11. 2008 / 9:00AM, HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

We don't actually have the plan in hand yet. We expect it right around the end of the year. You should also recognize that it is subject to change and if things get better, that more will be done. If the market for both diamonds and for debt, frankly, remains moribund as it is now, probably less will get done. But what I am expecting is yes, more reliance 418, but also, it seems that we probably can make more ore from 154 South available than was originally in the mine plan. This has to do with the basic stability of the pit walls being better than it being conservatively estimated, and therefore there's a couple more benches available there. And it does imply pushing the underground mining out probably toward-- certainly into the final quarter of the year-- third quarter towards the end of the year. And I will say there is the possibility of that even getting shifted right to the end of the year or perhaps into the following year. And that's about all the precision I can put on it.

John Hayes - BMO Capital - Analyst

I understand that. So, this goes back to your need for capital and refinancing. So even anticipating that some of this gets pushed out, you will still need this money.

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

We feel we don't wish to be in the risky position of being reliant on it getting pushed out. We are trying to put ourselves where we are comfortably funded to deal with a program, a capital program that we could possibly change the other way.

John Hayes - BMO Capital - Analyst

Now, fuel and FX are moving in your favor. There is a Canadian producer. What kind of impact do you see that having on your operating cost at the mine?

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

We haven't been able to measure it yet because a lot of the fuel is not yet purchased. So, it is a just-in-time thing. And you are right. It has been working in our favor. Also, there has been a significant cushion of fuel available at the site, on the order of 20 million liters that we will probably do without this year. We feel, or at least the operator feels that we don't really need to keep 20 million liters additional to probably pretty conservative estimates about consumption anyway. So, yes, there will be certainly some significant impact on the fuel consumption, fuel pricing, and you are right, FX. But I think you have to take your own view of what the FX ratio would be for the coming year. Alan, do you have any come minutes for that.

Alan Mayne - Harry Winston Diamond Corporation - VP, CFO

No. The only fine point I would put on it is that the cost of fuel that flows through the income statement isn't necessarily based on the price we will pay this year. We have an inventory at older, more historical prices, but certainly from a cash flow perspective, as we purchase fuel, that's going to have a significant positive impact on us.

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

It's probably a pretty good thing we don't have a winter road during the months when the oil price that goes through \$140.

Dec. 11. 2008 / 9:00AM, HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

John Hayes - *BMO Capital - Analyst*

Thanks very much.

Operator

The next question comes from the line of Matthew O'Keefe from Thomas Weisel Partners.

Matthew O'Keefe - *Thomas Weisel Partners - Analyst*

I have been reading a bit about the Indian diamond industry and there has been a one month moratorium imposed on diamond buying. Can you elaborate on that a bit and how it will impact your Q4 rough diamond sales?

Robert Gannicott - *Harry Winston Diamond Corporation - Chairman of the Board, CEO*

It was a moratorium that imposed by the sort of club of (inaudible) in India themselves. On other words, it wasn't a government imposed thing. And I am not sure I can formally answer for this being lifted, but certainly you can make exports of diamonds again to India now, and, in fact, we are doing that ourselves I think today. So, the idea was to try so that everybody-- what the Indian community was trying to do is keep everybody on a level playing field while they went through a prolonged Diwali holiday shut down. But of course, that can only go on for so long because these workers that are employed in these polishing factories eventually start to shift off to other industries or back to agriculture if they can't be employed. So the factories are now gearing up again, and there is a demand-- they've actually just shortened the period of this embargo as we understand it.

Matthew O'Keefe - *Thomas Weisel Partners - Analyst*

So you haven't had any drop? Like you haven't had any of your Indian customers say hold off on any shipments, and you don't expect to see that?

Robert Gannicott - *Harry Winston Diamond Corporation - Chairman of the Board, CEO*

We have had that. We have had that. We don't expect to see it going forward.

Matthew O'Keefe - *Thomas Weisel Partners - Analyst*

Can you remind us again how much of your production is moving in that direction or is going to the Indian clientele versus other parts of the world?

Alan Mayne - *Harry Winston Diamond Corporation - VP, CFO*

It's typically about 60% to 65%.

Matthew O'Keefe - *Thomas Weisel Partners - Analyst*

But you think it won't impact your-- you won't see a drop in the sales over the quarter?

Dec. 11. 2008 / 9:00AM, HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

Robert Gannicott - *Harry Winston Diamond Corporation - Chairman of the Board, CEO*

Well, it is two effects here. The production has picked up. In fact, the production has picked up to actually in front of the production levels that were anticipated for this quarter-- for this final quarter. So far. So, we are getting bigger deliveries of diamonds. The diamond market itself is very tight. We have been holding some stock. And I am not going to be predictive about the ability to sell it all going forward. I'm not that concerned about it because in a sense, I feel it is a good thing that the diamond pipeline sort of empties itself out to some extent. And so that all of these commodity games that have been happening over the last six months. There has been a lot of material being held within the supply pipelines because the prices were rising. This formed a kind of speculation. And I think it is a healthy thing that that empties out, but I will not be predictive about exactly when that's going to happen. My expectation is that the holiday sales, as it effects the broader diamond industry, will bring the reality-- the measurement of the sales, will actually bring a kind of base to the industry again, and it will march forward after that.

Matthew O'Keefe - *Thomas Weisel Partners - Analyst*

Fair enough. Thanks for that. Two other quick questions. This might be out there. We just, we heard Rio is selling a lot of assets, and not just common and risk specifically, but is there a right of first refusal for either of you on the sale of your portion of the Diavik mine?

Robert Gannicott - *Harry Winston Diamond Corporation - Chairman of the Board, CEO*

Yes, there is.

Matthew O'Keefe - *Thomas Weisel Partners - Analyst*

Does it go both ways?

Robert Gannicott - *Harry Winston Diamond Corporation - Chairman of the Board, CEO*

Yes, it does.

Matthew O'Keefe - *Thomas Weisel Partners - Analyst*

And just a final question. On the retail end, how many, can you remind us again how many you plan to open in calendar '09 and if you are still going to proceed with that?

Robert Gannicott - *Harry Winston Diamond Corporation - Chairman of the Board, CEO*

We are. We are opening one store. It is in Singapore. The reason we are doing it, of course, it was fully committed before the world turned pear shaped. But it's a good location, and we're not too worried about doing it. The expense of operating a store-- opening a store, really is almost 90% putting inventory in it. And so 10% is actually creating the store. So, what we will do, of course, is try to use the inventory from the rest of the network for awhile until the world gets back to rights again.

Matthew O'Keefe - *Thomas Weisel Partners - Analyst*

Thanks very much. That's it for me.

Dec. 11. 2008 / 9:00AM, HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

Operator

The next question comes from the line of Mr. Hammond from National Bank Financial.

Hammond - *National Bank Financial - Analyst*

Good morning. Most of my questions have been answered. Just a couple of quick ones though. In terms of the potential, let's say, like financing crush or financing short fall. Is there a potential to cut the remaining dividend to get another \$12 million, \$13 million dollars?

Robert Gannicott - *Harry Winston Diamond Corporation - Chairman of the Board, CEO*

Well, we've just sent out a dividend payment, as you know. I guess we sort of feel like at times like this, we have a kind of tool box of things that are available to us-- some of them less attractive than others. And cutting the dividend would be one of the less attractive ones. But, here again, in times like this, when you can't really see your way forward, one can't give guarantees about anything like that. But we have no formed intention to meddle with the dividend in the near future.

Hammond - *National Bank Financial - Analyst*

Okay. Thanks. In terms of-- in your press release, you mention that if acceptable terms for debt are not found that you will pursue alternatives, potentially the sale of assets. Could you give us more color on that?

Robert Gannicott - *Harry Winston Diamond Corporation - Chairman of the Board, CEO*

Not really. I think it is obvious what the assets are that we have, and here again, there isn't any-- we don't have any list together of what we will-- we are not looking to sell anything at the moment. If we felt we were getting close to that kind of pass, we would certainly start some more serious thought about it. But, no, we don't have that intention.

Hammond - *National Bank Financial - Analyst*

Okay. And finally, maybe, just on polished prices. From our own research, looking at a few other sources, we are seeing about a 5% decrease in polish prices over the last couple of months. Is that consistent with what you are seeing?

Robert Gannicott - *Harry Winston Diamond Corporation - Chairman of the Board, CEO*

The problem with this kind of conversation is that as you know, whether we are talking about rough diamonds or polished diamonds, there is this sort of huge spectrum of different things. But, yes, that is consistent with what you might call the bread-and-butter diamond supply that we see. Even for our own Harry Winston suppliers, of course, they're very much at the top end, but does go to a huge variety of (inaudible). We are buying very small diamonds to go into watch dials and dressing watches and so on, and we are also dealing with some of the very big ones and a whole range of things in between. And I think that would be about right. I think some of the really big things have got to very speculative levels that are more like (inaudible) really-- the art market. They've seen bigger falls than 5%. Specialty items-- if you want to buy engaged diamonds to go in watch dials or watch bands, they haven't gone down 5%. They are still the same price they were. Then there is sort of a range in between.

Dec. 11. 2008 / 9:00AM, HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

Hammond - *National Bank Financial - Analyst*

One last question, actually, and maybe we have to wait for Rio Tinto on this. In terms of cost. Looking at a cost structure next year. Would the deferral of underground mining, are we assuming that costs are coming down?

Robert Gannicott - *Harry Winston Diamond Corporation - Chairman of the Board, CEO*

Yes. And certainly costs-- capital costs and operating costs are targeted to be reduced by then. They have now announced that in a press release that they made yesterday evening. But, the extend of it is still in the process. I think you can understand why, as operator, they would want to have the flexibility going through the next six months. I completely understand that.

Hammond - *National Bank Financial - Analyst*

That's it for me.

Operator

The next question comes from the line of Irene Nattel from RBC Capital Markets.

Irene Nattel - *RBC Capital Markets - Analyst*

Hi, just a follow up question, if I might. In the press release, you address the issue of the good will around the retail acquisition. You say you did the test at the end of Q3. Everything is fine. Going to test at year end. Is that more of what I would think of as boilerplate in the press release, or is that something we really need to be concerned about?

Alan Mayne - *Harry Winston Diamond Corporation - VP, CFO*

No. It is not boilerplate, Irene. Under both Canadian and US GAAP, there are circumstances under which you need to do a goodwill impairment test other than at year end, and those circumstances were present in the form of the decline in the global economy and the impact that that was having on the retail business. So, no, it wasn't just boilerplate. We did conduct the exercise and concluded that the goodwill was not impaired. We would in the ordinary course do it in Q4 anyhow, and that's what we will be doing because, in this environment and the volatility we are dealing with, it is entirely possible that the conditions that were present to underpin the analysis in Q3 may be different in Q4. It is real work. It is real analysis, and it's not boilerplate.

Irene Nattel - *RBC Capital Markets - Analyst*

Thank you, Alan.

Operator

The next question comes from the line of Jacques Wortman from GMP Securities.

Jacques Wortman - *GMP Securities - Analyst*

Good morning, gentlemen. A question for more Bob. The diamond pipe line-- in the middle area of the pipe line, with the cutting and the polishing. This area is known to rely heavily on credit as I understand it. There is only a few institutions that actually lend to it. Bob, can you give any kind of color on the availability of credit to the pipeline right now, especially the middle.

Dec. 11. 2008 / 9:00AM, HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

The two principal diamond banks are ABN AMRO and then the Antwerp Diamond Bank. I have talked to the senior people in those very recently. They are committed to maintaining their credit availability to their customers. But they are not interested in extending it beyond the sort of normal levels. There are now more recently-- there are other players in the banking side of it. Some of the Indian banks, of course, play a role in this. But I believe everybody is taking a pretty conservative view. The way that they view it is-- their business is to finance somebody's ongoing business. In other words, the purchasing, the polishing, and the sale. And to finance that pipeline, what they are not interested in doing is financing any of their customers holding stocks. Which is a very reasonable position. Which is why I say that, as time progresses here, the pipeline is definitely being emptied, because nobody can use conventional banking facilities to fund stocks, and I doubt there is very little credit available to anyone.

Jacques Wortman - GMP Securities - Analyst

Yes, that's excellent. I mean, there has been a lot of commentary that that availability of credit even for ongoing businesses has dried up to a large extent, and that was having a limiting factor on the entire diamond pipeline and pushing down prices of polished and rough as the commentary had--

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

No, I think it is very interesting. That's a very interesting part of this business, because clearly, the people that are polishing are still selling through. There are several people that we deal with like specialty items. This one guy sticks in my mind that purchases triangular models of rough diamonds from us and he finds them ideal for making triangular trillion earrings, and it is a specialty business, and it's a niche. And he hasn't seen a decrease in his business at all, and he still buys exactly the same thing and, of course, is still paying the same price he was paying back in August, frankly.

Jacques Wortman - GMP Securities - Analyst

The last question, if you can provide the guidance. As it stands right now, I understand the mine plan is something to subject to change, but can you give us in rough terms what you see as being the mix of tons that you would take from 418, 154 South, and Underground, and would you just point us in the direction of the feasibility study grades from these three?

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

Jacques, no, not sitting in this room without significant number of documents in front of me. No, I can't. And I would still say it is variable, and A-154 South is definitely going to be a kind of suck it and see kind of project. In other words, it's going to be take out one lift and then stop for awhile and see whether the ground conditions are maintaining before going to the next lift, and if there is any problem with the ground conditions, stopping all together, switching more to over 418. It is going to be that kind of year. If you care to call me back in the office, probably tomorrow would be best. I'll see if I can do a bit better for you.

Jacques Wortman - GMP Securities - Analyst

The vast majority until, and again, the underground could be, you said it would be deferred until probably the second half of the fiscal year, so that means the vast majority in the first half will obviously come from 418 and a little bit of 154 South?

Dec. 11. 2008 / 9:00AM, HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

Yes.

Jacques Wortman - GMP Securities - Analyst

I may have missed it, but have you provided your overall guidance for calendar '09 in terms of care production.

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

No, we haven't because we don't have it yet.

Jacques Wortman - GMP Securities - Analyst

Thanks very much. I appreciate that.

Operator

The next question comes from the line of Brian MacArthur from UBS. Please proceed.

Brian MacArthur - UBS - Analyst

Just a quick follow up question. Going forward as you spend capital on the mine, should I just continue to assume that you are going to have no deferred tax benefit? Your split between current and deferred with continue to be a drawn deferred. Is that sort of the way it will work out the next year from a cash perspective.

Alan Mayne - Harry Winston Diamond Corporation - VP, CFO

No. Brian, as you know, certainly, deferred taxes are a complicated subject in what I call a traditional industrial manufacturing company. All I can tell you, it is that times 10 in the mining industry. It's not a straight forward don't assume that we don't have any deferred taxes. I think, as Bob mentioned earlier, I don't have the current mine model in front of me, but give me a shout, and I can give you with more color on that. It is very difficult with respect to current and deferred to make some very simplistic assumptions about it.

Brian MacArthur - UBS - Analyst

I realize that, and that's why I was trying to get you to do it for me, because I can't do it from the external, but obviously in the cash flow here at the moment, it's actually \$74 million payable at the moment. It is kind of critical that works out over to the next six or eight months.

Alan Mayne - Harry Winston Diamond Corporation - VP, CFO

What I can tell you is that a significant amount of that would be due and payable before the first half of next year.

Dec. 11. 2008 / 9:00AM, HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

Brian MacArthur - UBS - Analyst

Right. Okay. I will give you a call later then. Thank you.

Operator

The next question comes from the line of John Hughes from Desjardins Securities. Please proceed.

John Hughes - Desjardins Securities - Analyst

Thank you. One or two quick ones. Just in trying, everyone is struggling a little bit trying to come up with some type of production number for next year given the deferral of the underground and what will be filling what. Just in terms of starting at the top, tons moved. Is it reasonable to assume, at least from what you know today going forward, that you will move as many tons in next year that you did this year?

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

Oh, yes. I mean, the processing plant should run at about the same capacity. And I can see that you are struggling. And I don't want to give you a guidance number. But, if it, can I-- so point me towards. What we are looking at internally here, at the moment, absent further advice from Rio, and as I say, it is going to be changeable through the year. I think I would be using something more on the order of 8 million carats.

John Hughes - Desjardins Securities - Analyst

And last question. If Rio Tinto is indeed in the process of trying to sell their interest in Diavik, would you want to maintain your 40% direct interest in the event someone else is operating the mine?

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

If that were the case, and I would just stressing that I am not aware of that by the way, but if it is the case, we would seek actually to increase our interest.

John Hughes - Desjardins Securities - Analyst

Okay. Thank you very much.

Operator

The final question comes from the line of David Christie from Deutsche Capital. Please proceed.

David Christie - Scotia Capital - Analyst

David from Scotia Capital. Just a quick follow up on a couple of questions that were asked earlier. On the right of first refusal on your side, if someone makes an offer for Harry Winston, does-- is there some kind of underlying right of first refusal on the asset that supersedes the offer from the Company.

Dec. 11. 2008 / 9:00AM, HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

That is a difficult question to answer. There are parts of the joint venture agreement that, under some certain circumstances, that could well be the case.

David Christie - Scotia Capital - Analyst

I thought there was some kind of change of control thing. And that's good. On the purchase of fuel and steel for 2009, I know you have stock piles. Have you been filling them with fuel during the fall months?

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

There was some filling of some of the tanks during unpleasant fuel prices but not a whole lot. And for obvious reasons, when the fuel price looked as if it was going to moderately stop, and so that we thought, okay, let's do it just-in-a time basis. I can't tell you really what percentage of the fuel is already in Yellowknife. And at this point, it is probably close 1/2.

David Christie - Scotia Capital - Analyst

Okay. So I can assume some was probably bought at the lower end and some at the higher end?

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

That's right.

Operator

The next question comes from the line of Patrick Morton from RBC Capital Markets.

Patrick Morton - RBC Capital Markets - Analyst

That \$83 million in CapEx and \$20 million sustaining. Is that on a 100% basis?

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

No. That's our share.

Patrick Morton - RBC Capital Markets - Analyst

Great. Thanks.

Operator

We have no further questions for today. I would like to turn the call back over to management for closing remarks.

Dec. 11. 2008 / 9:00AM, HW.TO - Q3 2009 Harry Winston Diamond Corporation Earnings Conference Call

Robert Gannicott - Harry Winston Diamond Corporation - Chairman of the Board, CEO

Okay. Well, thanks very much for joining us today. If anybody thinks of anything subsequently, we are, both Alan and I, are around here in Toronto for the balance of this week. And Tom is more difficult to get hold of. He is in Paris at the moment for obvious reasons. Thanks again for joining us.

Operator

This concludes the presentation for today, ladies and gentlemen. You may now disconnect. Have a wonderful day.

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