A Single Price Index for Domain Names Is Misleading

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Having a single price index for the domain name industry would be worse than useless. Such an index is presented in a recent study by Thies Lindenthal. The index is intended to be a benchmark for domain owners and investors. But it's out of line with other studies and the common sense of how a market operates. A much better barometer to follow is average prices for groups of domain names with similar characteristics.

Remember that the Dow, the S&P500, and NASDAQ sometimes move in opposite directions. A single index for stocks couldn't contain that movement, and a single index for domain names couldn't contain the differences in the amount and direction of price fluctuations among various domain name groups with common characteristics

Using a single index would have dire consequences. Basing transactions on such values would cause some owners to overpay, others to underpay. The resulting prices would be worse than imprecise, they'd be wrong — contrary to fair market value. Inflated prices can cause owners to resist selling and thus, forego lucrative deals. In the early days of the domain industry, wild price predictions by some owners not only put the industry on the map but created so much interest that investment returns rocketed above those of other industries. However, it is hard to determine if on average the sales have been over- or undervalued.

Other problems with Lindenthal's single price index:

1. It's based on information taken from just one market, Sedo. But other studies reveal that sale prices for similar names vary across marketplaces. Moreover, Lindenthal's model ignores the ask prices of listed domain names. That's relevant data if the aim is more precise estimates.

2. The reported index-price correlation with the NASDAQ 100 is grossly misleading. Why would prices of domain names of large companies move in synch with those of small and backdoor domains! One would expect that different groups of domain names would be correlated with different indexes depending on their risk characteristics.

3. The methodology is not robust to the presence of outliers in domain name price data.

4. The model does not identify risk factors driving domain name prices, such as the number of a domain's key word searches, the cost per click (CPC) of the key word, the popularity of the key word as shown by uses of it on Web sites, etc.

5. The model ignores evidence of a nonlinear relationship between prices and the explanatory variables.

Yes, there are domain name pundits who dismiss quantitative modeling and listen to the predictions of high-flying "experts." This approach all but guarantees more misses than hits. Studies confirm that "people who make wild bets but successful are remembered for those hits — but on average are the worst predictors." (See Jerker Denrell's *"Experts" Who Beat the Odds Are Probably Just Lucky*.) Tom Cruise could use sheer instinct to fly a jet in *Top Gun,* but in real life smart pilots use their instruments.

We need models based on rigorous analytics if we want to track the price movements of domain names. Of the models available, the single price index doesn't measure up. ■