DomainMart

Assessing Your Domain Name Investment

Alex Tajirian
May 26, 2009

You, not unlike a large segment of domain name investors, have accumulated your holdings in a different world than today's, a world of low competition and the lack of any compelling reason to use quantitative techniques. Now is the time to take a forward-looking view and shuffle your portfolio. As hockey great Wayne Gretzky said, "Skate to where the puck is going, not to where it is."

The current recession provides a great time and an added incentive to make necessary changes to the composition your domain names. The risk of not taking action is underperformance of your portfolio and a lost opportunity to capitalize on developing sites with the key words you want, ones tied to the businesses you know best.

It is not easy to sell domain names you have owned for a long time. Buy something and often enough you want to keep it. Second, you are facing groupthink about the general direction of domain name prices, not to mention a vast collection of biases in personal decision-making and in publicly available opinions. Like the fortunate few who weathered the subprime mortgage crisis without severe harm, you must ask yourself the hard questions, chief among them being "What happens to the value of my portfolio if I am wrong about …?" Also, keep in mind that there is empirical evidence that not all groups of comparable domain names move in the same direction.

If you are inclined to rely on quantitative tools or use them to complement your experience, you can approach the problem this way:

1. From your total list of domain names, remove the ones that have key words you really know about, the key words of which you have intimate knowledge about superior or inferior future potential.

2. Separate the resulting list of domain names into two groups: names with key words that are best suited to traffic generation, and names with key words best suited to branding/development. Which names go on which list can be up to your personal intuition and knowledge or a look at the domain name's branding-to-traffic ratio (B/T).

For generic traffic domain names,

a. Rank them by their return-to-risk ratio. If you don't care much about volatility, rank them by return. Return can be estimated by taking the average of monthly returns from monetization, or you can apply time-series forecasting techniques. Risk can be measured by the common measures of volatility (the variance of returns) or by the average of the absolute value of deviations), which is more robust to outliers.

b. Order the ranked domain names by their return-to-risk ratio into groups of equal size—say, four or five for large portfolios. Compare the performance of the lowest group to comparable-value domain names with higher return-to-risk for potential acquisitions, and compare the ratios to those of other investment opportunities, such as stock or money-market mutual funds. Consider selling domain names and investing in funds yielding higher return-to-risk ratios.

For development and/or generic branding, parking revenue is not a good barometer of value. An ideal valuation methodology of these domain names would be to use real option models (ROM)—option models were originally developed to price financial puts and calls. ROM explicitly incorporate strategic options of development and branding opportunities into the price and risk estimates. At the same time, you should investigate the potential acquisition of domain names with key words that you are interested in developing, whether you plan to do the development yourself or outsource them. ■

Related Essays

- Thoughts on Hedging Domain Name Price Risk
- To Renew or Not to Renew Your Domain Name?
- Value Synergies from Domain Name Portfolios