DomainMart

Domain Name Markets: Firm Commitment vs. Best Effort

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Introduction

I present the advantages of pushing the domain-name secondary markets toward a *firm commitment* regime—a regime where, before you sell or buy a domain name, you shop it among marketplaces that are willing to commit to a transaction value. Such a regime is value-adding for buyers, sellers, and marketplaces.

I first outline some of the drawbacks of the current domain-name secondary market and then highlight the advantages of firm commitment over the current *best effort* relationship.

Current State of Secondary Market: Best Effort

There are three types of publicly accessible listing venues: exchanges, forums, and newsletters. Each is essentially a conduit and most often provides no advice on identifying fair prices, finding buyers, or setting a timeframe for completing a transaction. They simply make public the fact that you intend to sell information. Further, when they actively seek to match buyers and sellers their incentive is to arrange a quick deal, not necessarily the best deal for you.

Disadvantages of Best Effort to Buyers and Sellers

1. High search cost:
    a. Sellers, in general, have limited time and expertise to find and analyze potential buyers.
    b. Corporate buyers have to develop internal expertise to determine the domain names that add value for branding, protection, and traffic, then contact and negotiate with each owner.

2. High cost of performing due diligence for buyers of parked domain names. The due diligence is needed to make sure click fraud does not inflate stated revenue.

3. No price revelation.[1] Domain name market prices are very noisy; without expertise or a rigorous appraisal, one side of the transaction is not getting a fair deal. This limitation results in limited liquidity, as buyers and sellers are hesitant to transact. A buyer would needlessly wait when the seller is unknowingly demanding an unjustifiably high price for her domain name; a seller can lose fair sales and a buyer

[1] In the domain name industry, the issue of price revelation is commonly summed up by this saying: "A domain name's price is what a buyer is willing to pay for it." This is a descriptive state of affairs compared to appraisals, which, in contrast, are value prediction models.

fair opportunities. If a domain owner does opt for a professional appraisal, the typical appraisal is simply a number and therefore ineffective[2] in providing useful actionable information.

4. For a domain name to generate a positive net value to a buyer, it has to be acquired at below fair-market price. Thus, even if a buyer and a seller agree on a price, they might disagree on how to split the buyer's net benefit.

How to improve marketplaces?
Instead of passively listing a domain name with one of the marketplaces, a seller is better off shopping the name for a firm commitment from one of the marketplaces. The seller can then commit the domain name to the best offered value. Thus, there is a need for cooperative intermediaries retained by a buyer and/or a seller. Such a regime creates competition for providing value-adding services instead of the current competition for listing views. The inefficient listing venue has some domainers advocating cold calling potential buyers.

Advantages of a firm-commitment approach:

1. Improved valuation for buyers and sellers, and thus more liquidity and fairness. This, in turn, improves industry image, increasing everyone's pie.

2. Better assessment of whether the buyer/seller should wait for more relevant information. This is because of the presence of a competent intermediary.

3. Better assistance for buyers in raising funds or assembling a syndicate of buyers. Again, this is because a competent intermediary is present. The borrowing involved in raising the funds does increase risk for the buyers and the industry, but it also improves liquidity.

4. Greater effectiveness of cold calling potential buyers/sellers. This is because of the intermediaries' cost and experience advantage.

5. An edge in negotiations if the buyer uses an experienced intermediary and the seller doesn't. Even when both sides agree on the value of the domain name, an intermediary agent may still split the buyer's net gains in favor of his client.

Benefits to Buyers

1. Decrease cost of:
    a. Searching for individual or a complementary corporate portfolio of domain names for branding, protection, and traffic. Nevertheless, developing such expertise internally may not be cost effective for some companies.
    b. Needless waiting for the seller and/or buyer to make up her mind with regard to a fair value.
    c. Negotiating a fair price due to the agent's expertise.

[2] See Alex Tajirian (2007), "Effective Domain Name Appraisals," DomainMart.

2. Decrease the risk of click fraud–infested parking revenue.

3. Increase in revenue due to increased liquidity as a result of enhanced trust in the exchange mechanism.

Benefits to Sellers

1. Increased sales due to the benefits, noted above, to buyers and the resulting increased trust in the exchange process.

2. Decreased cost of:
    a. Searches, as a result of the trust-based relationships of intermediaries with buyers and sellers.
    b. Waiting for a dream buyer to knock on your door.
3. Increased revenue due to better analytics. An intermediary is better equipped to perform market analytics, such as using Porter's "5 Forces."[3]

4. Decreased risk of undervaluation.

Benefits to intermediaries: new entrants and incumbents

Active intermediaries increase the pie and make transactions less risky through increased public and private information[4] and operating efficiency. Thus, their fees can be higher per transaction, combined with higher transaction volume.

Concluding Remarks

1. Moving to a firm-commitment regime benefits buyers and sellers. Accordingly, there is an incentive for providing such service, but agents must stay away from trademark-related names.

2. Improved image of the secondary market has positive spillover effects for the rest of the industry, thus increasing the industry pie.

3. Network effects can tip the secondary market to a single provider.[5] ■

[3] See Alex Tajirian (2005), "Porter's 5 Forces and Domain Name Value," DomainMart.
[4] See Alex Tajirian (2006), "Price Inefficiencies in Domain Name Markets: An Empirical Investigation," DomainMart.
[5] For an analysis of tipping forces in the current market, see Alex Tajirian (2005), "Multiple Viable Domain Name Marketplaces Can Co-exist," DomainMart.