Rarity is in the Eye of the Beholder: Impact of Rarity Tools on NFT Marketplaces

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Abstract. Non-fungible Tokens (NFTs), which have recently exploded in popularity, represent a fusion of technology, art, and commerce that challenges traditional notions of ownership and value. Given their significant financial influence and unique nature, understanding the trade dynamics of NFTs is essential for market sustainability. Recent tools have started providing rarity ranking for NFTs within a collection. As rarity is a key driver of an NFT's value, we investigate the impact of displaying these rankings on collections. We find that even though this information is crucial for NFT trading, its disclosure can negatively impact a collection's sales and revenue. Interestingly, when a ranking is shown on a third-party website, the subsequent information disclosure creates an information asymmetry between sellers and buyers, resulting in an adverse selection that hurts the rarest NFTs. When the ranking is displayed on the marketplace itself, we find that this transparency makes less rare NFTs even less attractive. Both of these effects harm collections and marketplaces. Our findings offer insights for collection owners in assessing whether they benefit from these rankings, for marketplaces in choosing whether to display these rankings, and for traders in deciding which NFTs to buy contingent upon whether and where ranking is displayed.

Key words: NFT, Marketplace, Adverse Selection, Information Disclosure

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