The Intersection of Hotels and Vacation Rentals:

Competition and Merging in the COVID-19 Pandemic

Introduction

It's no secret that hotels and vacation rentals are natural points of comparison, but their many differences mean they rarely compete directly. This is evidenced by the fact that both industries have seen unique trends during the COVID-19 era—which are also reminders of the evolving nature of travel behavior. And future trends will likely only further accentuate these differences.

In this report, we examine aggregate data on short-term rentals (STR) from AirDNA and traditional hotel data from STR/CoStar from 2018 to 2022. Both data sources represent the industry's best efforts at a comprehensive, if not exhaustive, assessment of their categories. More on our methodology at the end.

Perhaps unsurprisingly, COVID-19 greatly accelerated the growth of the rental market's share of the lodging space. However, the gradual recovery of conventional hotel demand in 2021 and 2022 has reclaimed some of the rental share and slowed rentals' growth rate to below pre-COVID-19 levels.

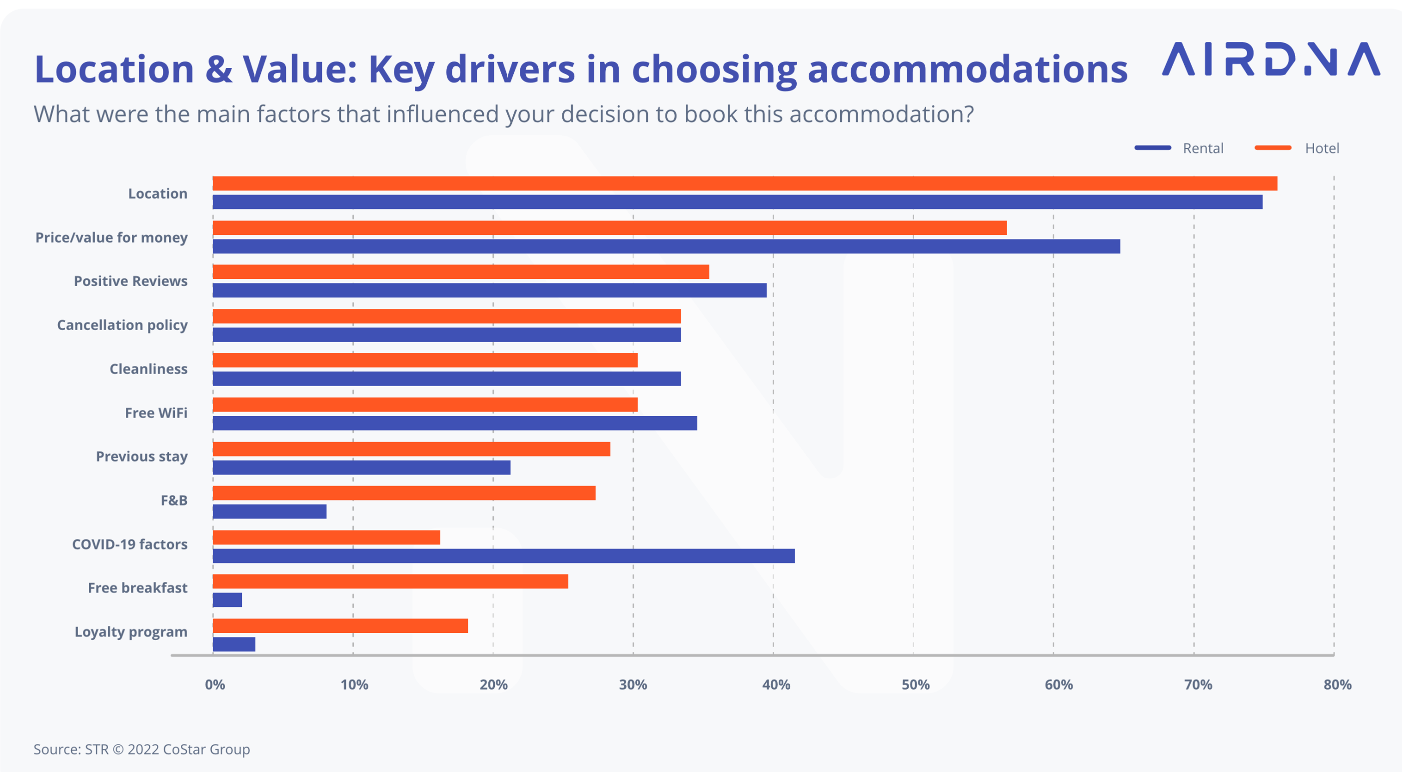
There is a considerable overlap between hotels and rentals: different situations or destinations might make us choose one or the other for different trips. These changing consumer preferences go a long way in explaining the dynamics that have played out since 2020. In a recent survey of more than 1,000 travelers, STR/CoStar asked guests of both hotels and rentals to rate the factors most important to their booking decisions.

Location, Location, Location

Location was most consistently rated as important for both hotels and rentals. This creates value for rentals in desirable locations with proportionately fewer hotel rooms, such as mountain and coastal resorts. In locations with a high supply of conventional hotel rooms, such as urban and suburban destinations, rentals need to compete on other criteria.

The two types of lodging differed most in a preference for food, beverage, and free breakfast in hotel guests and COVID-19 factors, which pushed rental guests towards a preference for private space. Concerns about COVID-19 help to make the decision between hotels and rentals for consumers, as rentals have an advantage in consumer perception when it comes to COVID-19 safety.

Value for money is also more important for rental guests, though it remains important for hotel guests too. Rental prices in urban locations are considerably lower than hotels, which can factor into the decisions of guests in these locations opting for rental properties.



Methodology

In a collaborative effort between AirDNA and STR/CoStar, we examined aggregate data on rentals and traditional hotel rooms from January 2018 to June 2022. The data was broken out along several dimensions to better characterize the changes in the performance and relationship between the two markets. Hotel demand data was contributed by STR/CoStar, and AirDNA contributed data on rentals. Both data sources represent the industry's best efforts at a comprehensive, if not exhaustive, assessment of their respective product categories. STR/CoStar collects data directly from hotel operators from most hotels in the United States and estimates the performance of non-contributing properties. AirDNA sources the totality of public listings from both Airbnb and Vrbo, representing a large majority of the U.S. rental markets.

Hotel demand is defined as the total number of room nights occupied in hotels over a given time period, while rental demand is the total number of nights occupied in a rental listing. This means that a single listing that contains multiple rooms would account for only one occupied night. The sum of hotel and rental demand is total accommodation.

Supply of units for both hotels and rentals is the number of individual units available to rent, whether or not they were rented. This number is significantly more stable in hotels, where the supply corresponds closely with the number of extant rooms. Rental supply is more flexible, as rooms are frequently brought in and out of the supply depending on market conditions. Supply can surge during major events, like the Super Bowl, and contract during the winter in markets like Cape Cod, Massachusetts. The supply in this case is the sum of the occupied listings nights and the nights noted as being advertised as available to rent in the month.

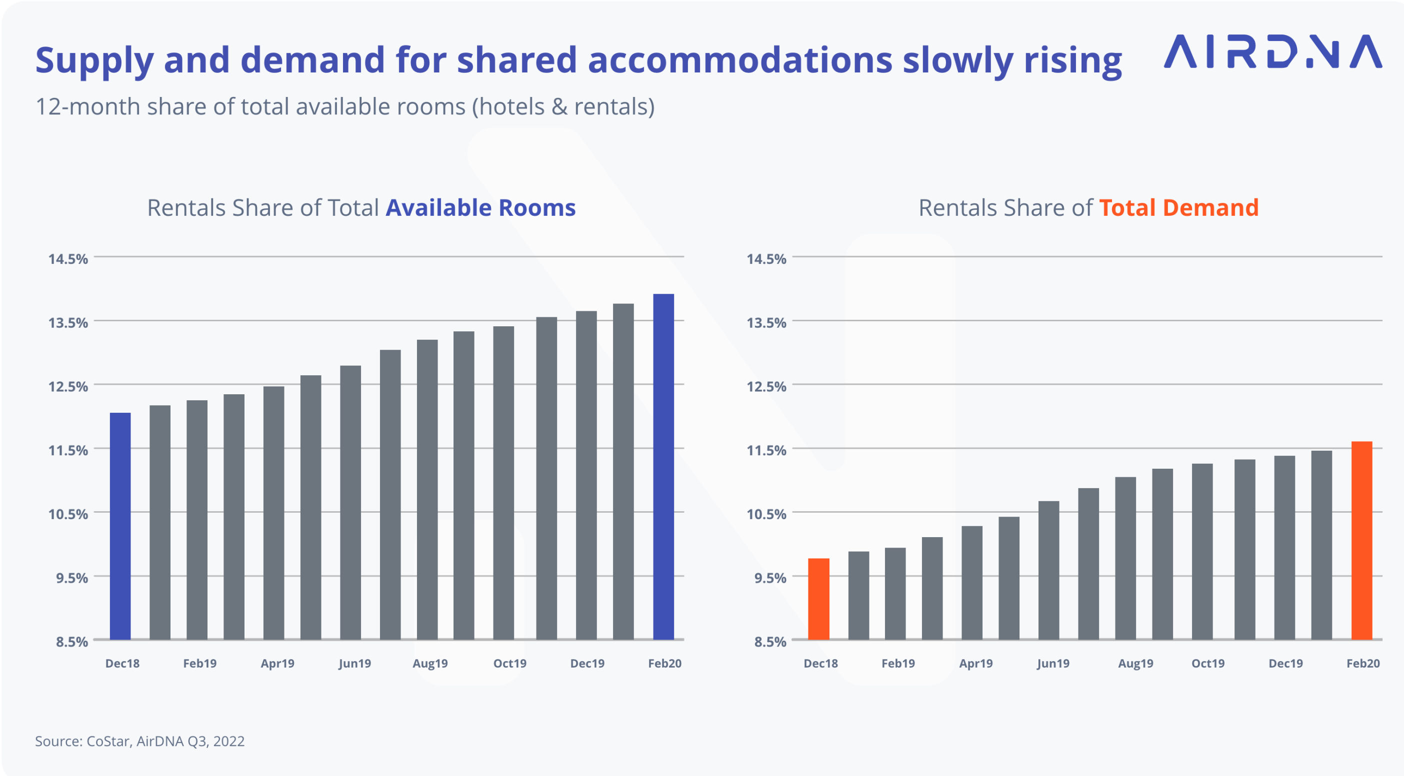
Additionally, revenue information is gathered by these firms. Average daily rate (ADR) is the total revenue generated by a property or market divided by the number of nights occupied over the same time period.

Rental share of the accommodation market is examined as a way of gauging the relative prevalence of rentals compared to hotels. It is calculated by taking the ratio of the total number of occupied nights in rentals, or rental demand, to total accommodation.

Supply and Demand Pre-COVID-19

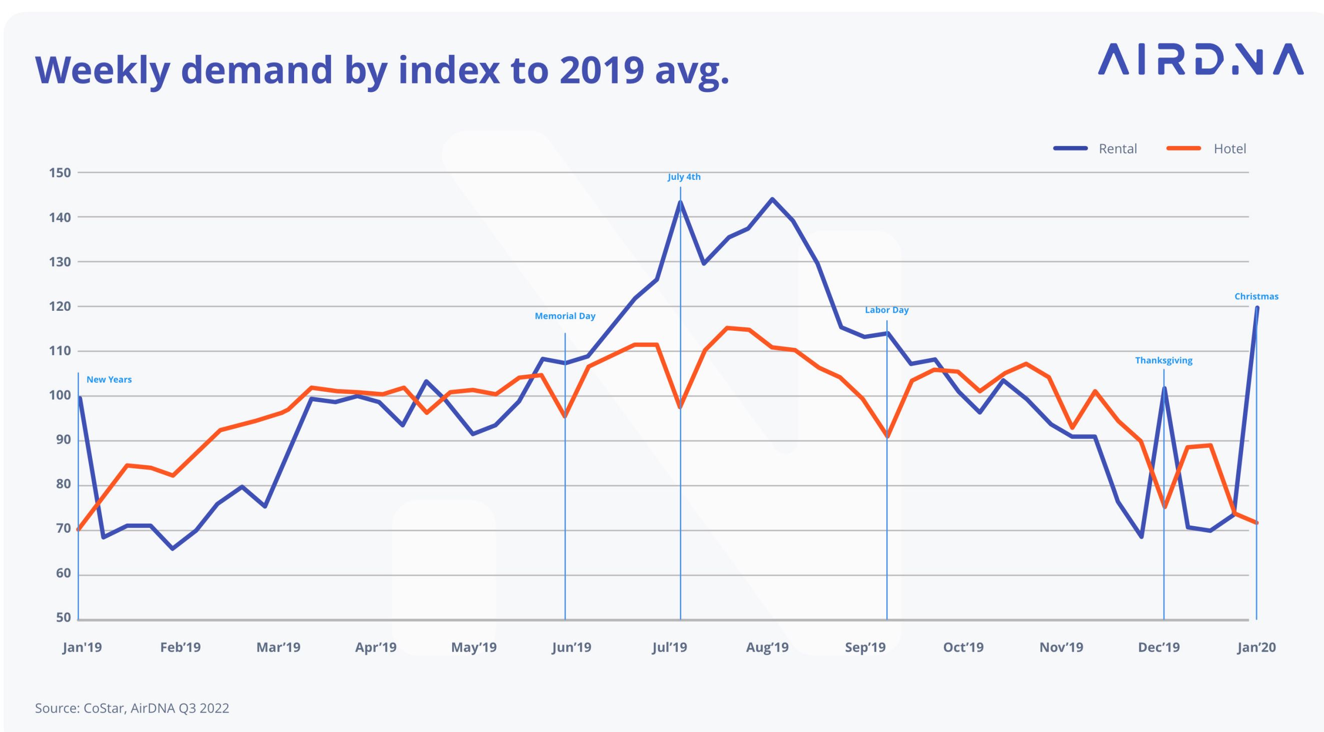
Before the U.S. imposed large-scale COVID-19 restrictions in March 2020, rentals made impressive, steady gains in market share of both supply and demand of accommodations. Looking at the period from January 2018 to February 2020, rentals' share of total supply increased by between 10 to 14 basis points each month, and demand grew slightly faster. Rental supply is closely linked with rental demand, and supply usually follows behind demand. However, rentals on the whole see lower occupancy than traditional hotels, so the share of rental supply is higher, with demand spread across more properties. The progression of market share of rental properties as a trailing 12-month average is illustrated below.

Exhibit 1: Trailing Twelve Months Market Share of Rentals Increased Steadily Prior to COVID-19



Seasonality differences between hotels and rentals illustrate the different use patterns among consumers. The chart below shows the demand for hotels and rentals in each week of 2019 as a percentage of the average weekly demand for that lodging type. This means we can see the relative differences in seasonality, even though in absolute numbers, hotel demand is much larger than rental demand. Although both hotel and vacation rentals share a strong summer season, hotels had an approximate 10% demand premium over the year average in summer 2019, while rentals saw a huge 45% premium.

Exhibit 2: Rentals' Summer Seasonality Stronger than Hotels'

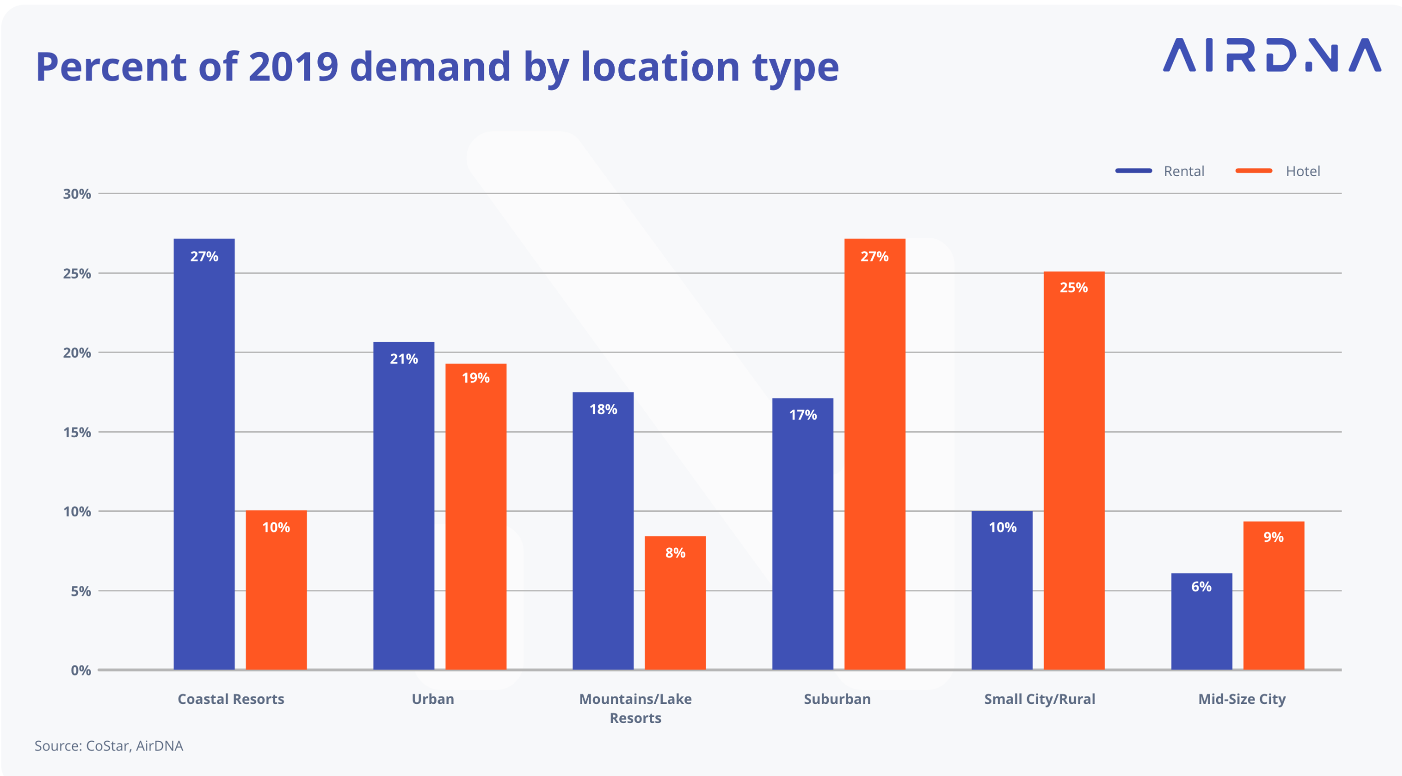


Additionally, hotels saw noticeable downturns on several important holidays, including Memorial Day, July 4th, and Thanksgiving, while rental demand spiked during those same holidays. As demand moves in opposite directions, the correlation between the two lodging types is dampened, so that only about 60% of the demand in one sector can be predicted from the other's on an average week.

This difference in seasonal demand can be explained in large part by looking at the types of travelers choosing rentals or hotels. The rental sector sees a high proportion of leisure travelers who prefer to travel during the warmer months. Hotels, on the other hand, have a larger business travel contingent that pads out the cold-weather "shoulder season."

Looking at location types confirms this relationship, as you can see in the chart below. Nearly half of rental demand in 2019 was realized in resort locations, with beach resorts taking the lead in the warmer months. This can also explain the downturn on holidays in hotels. Those business travelers who stay in hotels ordinarily can become rental leisure travelers during the holidays.

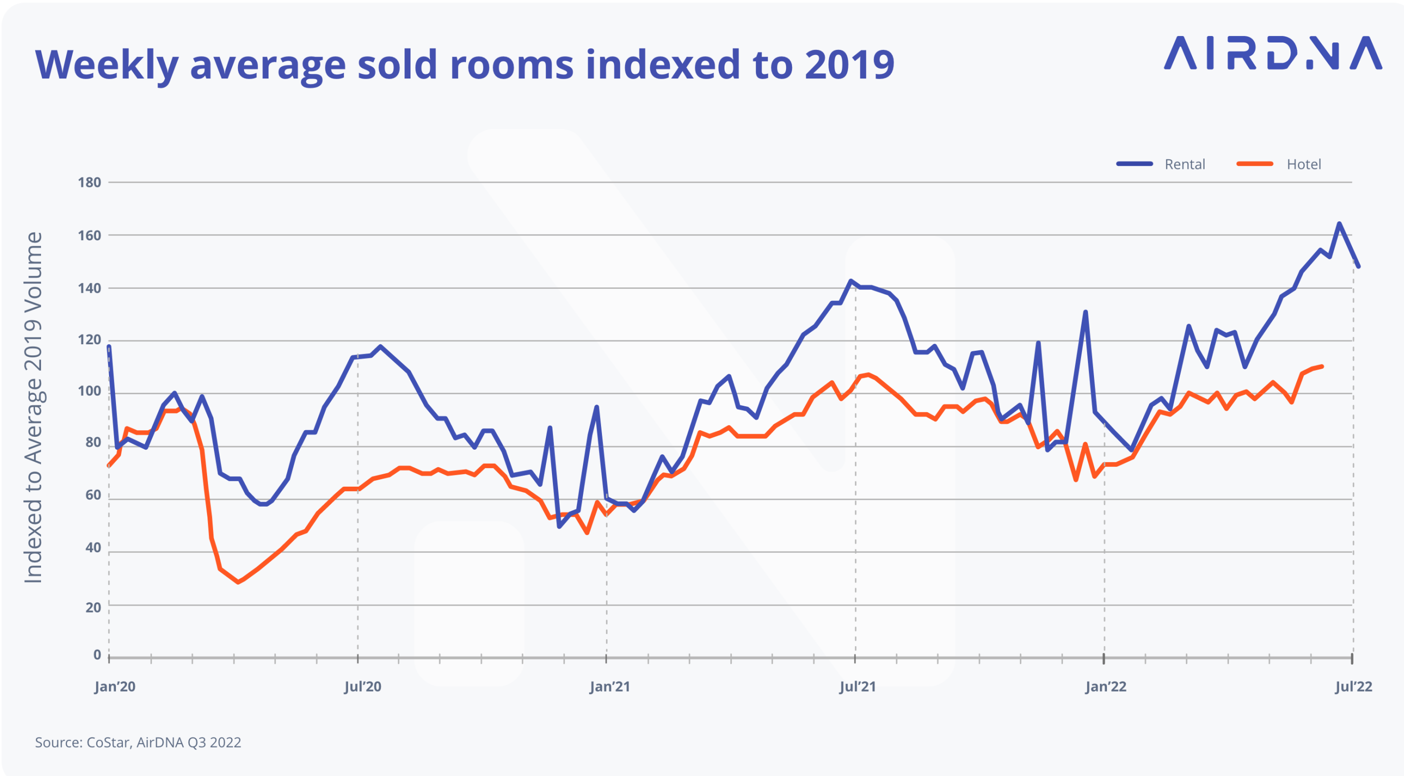
Exhibit 3: Rental Demand Concentrated in Resorts and Urban Locations



Recovery Changes

When COVID-19 struck the U.S., the immediate effect of social distancing, restrictions, and increased fear of infection on both the rental market and hotels was to drastically lower demand. Demand levels relative to 2019 sank abruptly in March 2020, as illustrated below.

Exhibit 4: Leisure Recovery Buoys Both Rentals and Hotels in 2021

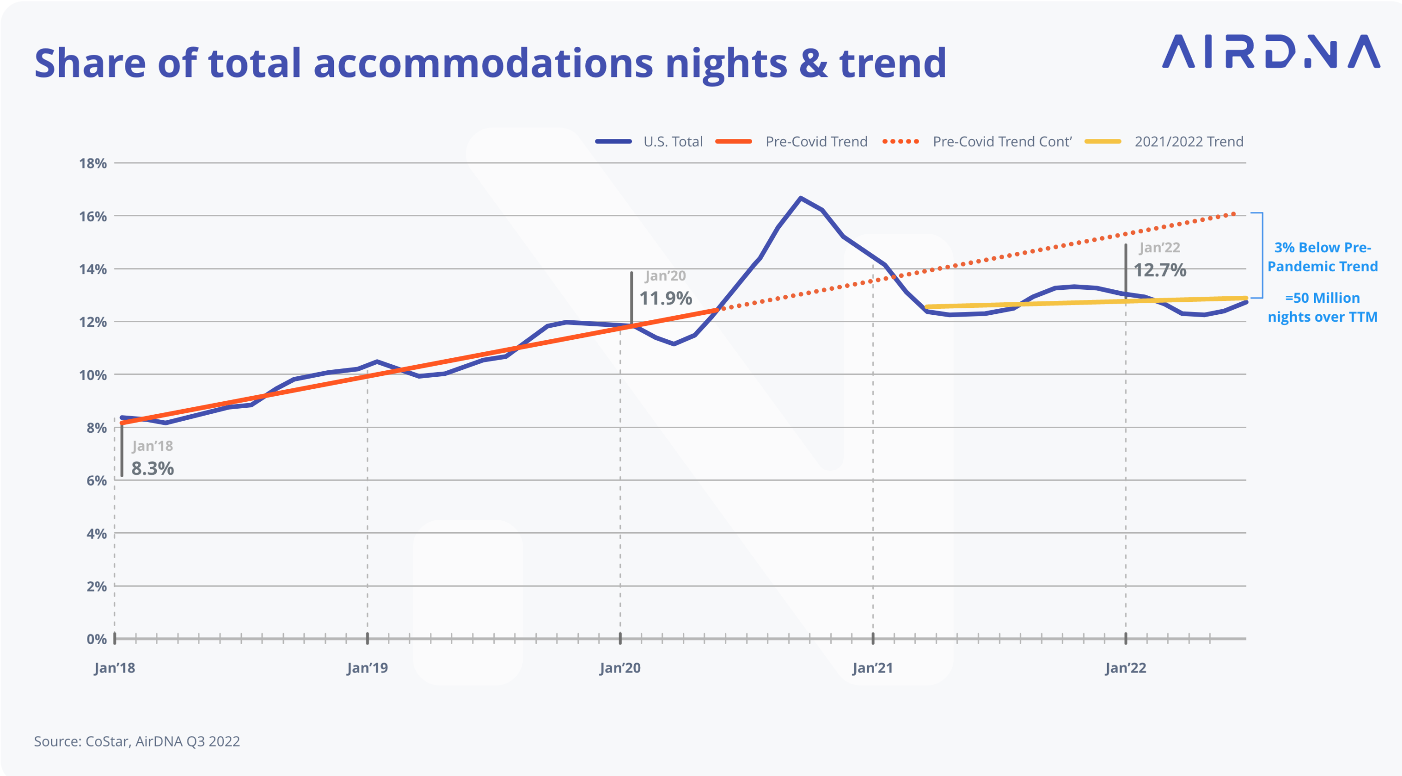


Business travel was especially affected as companies sought to minimize liability, protect workers, and make efficient use of new remote work technologies. This led to a greater initial downturn in hotels than rentals. Rental properties, already catering to the now-predominant leisure traveler and naturally allowing for social distancing, recovered swiftly and exceeded 2019 average demand levels by June of 2020.

By 2021, both sectors were making steady gains as hotels began to focus more on attracting the leisure guest. Although rental demand still had an exaggerated seasonal effect in 2021 compared to hotels, there are no longer the large dips in hotel volume surrounding holidays. Moreover, as the two sectors began to compete more closely with one another, the statistical relationship between the two series strengthened as well. The predictability of one sector's demand from the other increased 27 points from 2019 to 87% in 2021.

The interplay between the two recovery patterns has had implications for the growth of the share that rentals have over the total accommodations market. As illustrated below, the initial impact of the pandemic created a spike in rental market share to its highest level yet recorded—nearly 17% of all accommodation demand. As the hotel sector recovered by taking more leisure demand in the subsequent years, this drove down rental market share. Moreover, had the market share followed the linear growth trend before the pandemic, illustrated by the dotted line, rentals would have approximately three percentage points higher share than now. The current linear growth trend from 2021 to present has a slope significantly flatter than that of the pre-pandemic trend.

Exhibit 5: Rental Share Spikes in 2020, Stagnates in 2021, 2022



Supply on the Move

So, we know that one reason for this change in trajectory is that hotels are now competing more closely with rentals for the same leisure guests. But has supply also played a role in this? Rental supply is able to shift in response to demand trends, growing to meet spikes in demand and leaving the market when demand drops off. In response to the COVID-19 pandemic, rental supply was able to contract quickly, particularly in urban markets. On the other hand, aggressive fiscal stimuli directed at businesses affected by the pandemic prevented large-scale permanent closures of hotels. As demand trends reversed and guests returned to cities, hotel supply was already able to accommodate new travelers whereas urban rental supply has yet to regain pre-pandemic levels. As you can see in the chart below, urban supply in May 2022 was still more than 17% lower than in 2019.

Exhibit 6: Flexible Supply Helps Rentals Grow in All Locations But Urban

Despite the demand incentive for urban rental property managers, these urban locations often discourage quick supply regrowth due to a difficult market situation. Many large urban metro areas have significant regulation that complicates or discourages re-entry. Existing rules in New York City saw reinvigorated enforcement during the pandemic recovery. From March 2020 to 2021, total listings in New York fell by about 16,000, more than a quarter of pre-pandemic supply. A similar story unfolded in San Francisco, where total listings dropped by about 4,000 rooms, a quarter of supply. In both cases, supply in these urban metros has not recovered. More recent rules in places such as Boston, San Diego, and Los Angeles have made supply recovery difficult.

The usual financial incentives that motivate new rental supply are also experiencing headwinds in urban locations. Prior to the pandemic, hotel rooms and comparable rentals had similar pricing—with the notable exception of urban locations, as shown below.

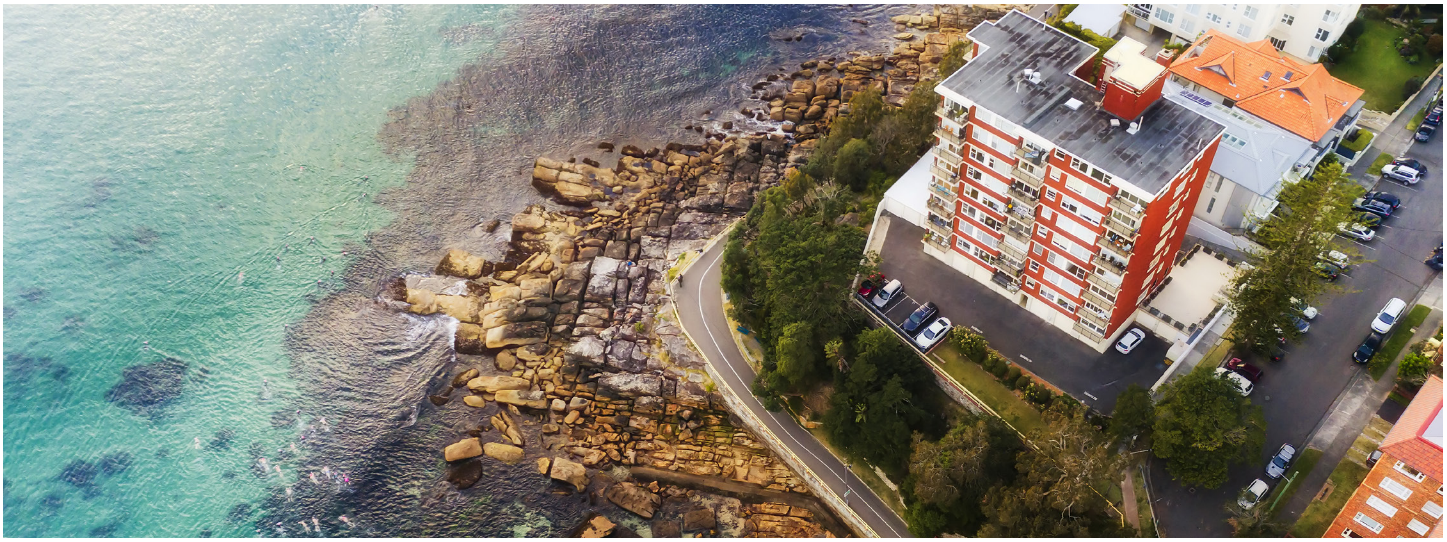
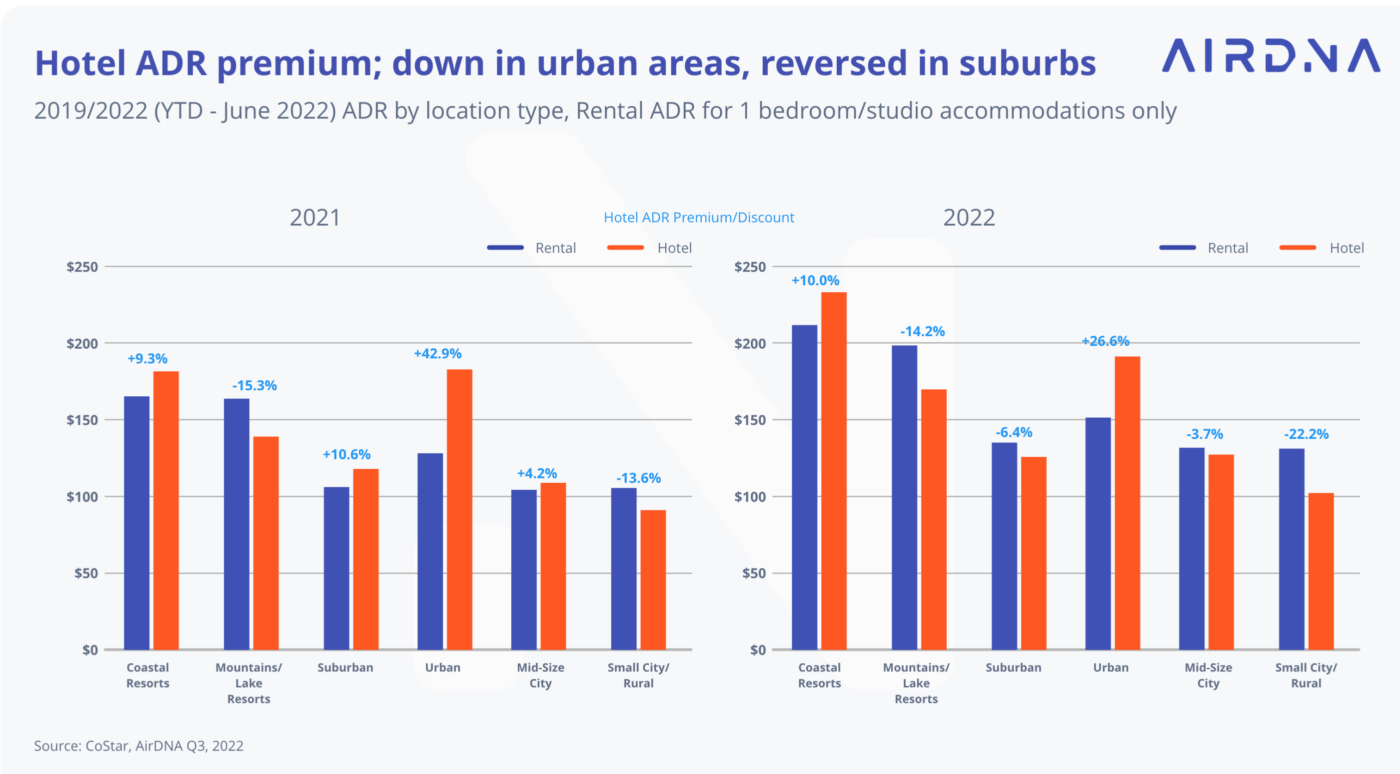


Exhibit 7: ADR Similar Except In Urban Locations

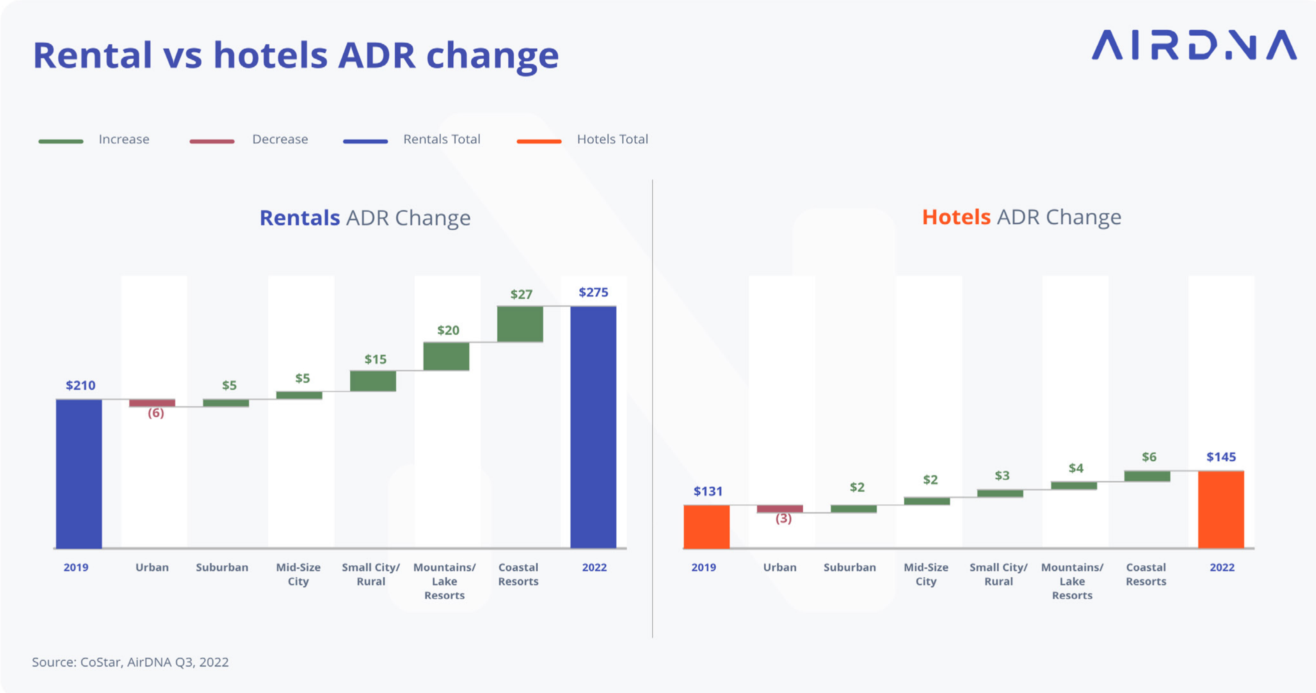


Given that urban locations are well-stocked with conventional hotel rooms in desirable places, rental operators face additional pressure to compete based on price. This situation was exacerbated by the dynamics of the pandemic, as conventional hotels in urban locations found themselves with a glut of rooms and decreased their rates in response.

While our guest survey noted that value was the second-highest reason for choosing a rental accommodation, the relative value of rentals has shrunk since 2019, especially in the largest U.S. cities. In urban areas, hotel ADR was 42.9% higher than a comparable studio/one-bedroom rental during the first half of 2019. During the same period in 2022, that premium reduced to only 26.6%. In suburban areas of the same cities, hotels were 4.2% more expensive in 2019, while in 2022, rentals are actually now achieving higher ADRs. These changes have greatly reduced the relative value of rentals.

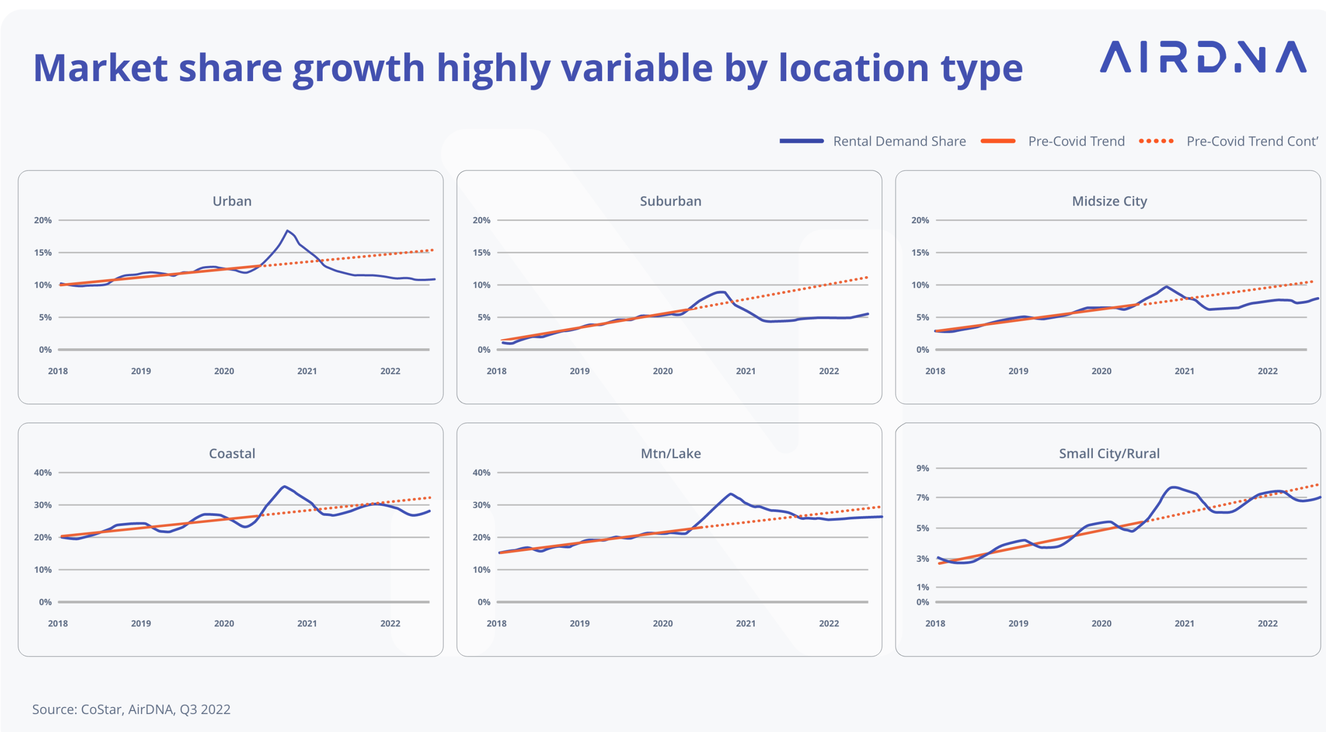
Meanwhile, leisure destinations and resorts had considerable power to increase rates. You can see below the ADR changes seen since 2019 for hotels and rentals broken down by location. Attractive gains were produced in resort markets and small city or rural rentals, while declines were conspicuous in urban locations for both rentals and hotels.

Exhibit 8: Urban ADR Declines, Resorts and Small City Rentals Post Large Gains



Different market types present a more nuanced picture than illustrated by overall rental market share. Although rental market share has, in aggregate, stagnated or greatly slowed its growth in the past two years, significant gains continue to be made in some locations—in some cases close to projected linear trends pre-pandemic. Meanwhile, urban and suburban locations' share has flattened, and in the case of urban areas, has begun to decline. Until demand in these locations can begin to create compression and push rates up more swiftly, it will be difficult to foster the aggressive growth trends these locations previously enjoyed before the pandemic. Below, we break out the change in market share by location, with a linear extrapolation of pre-pandemic trends.

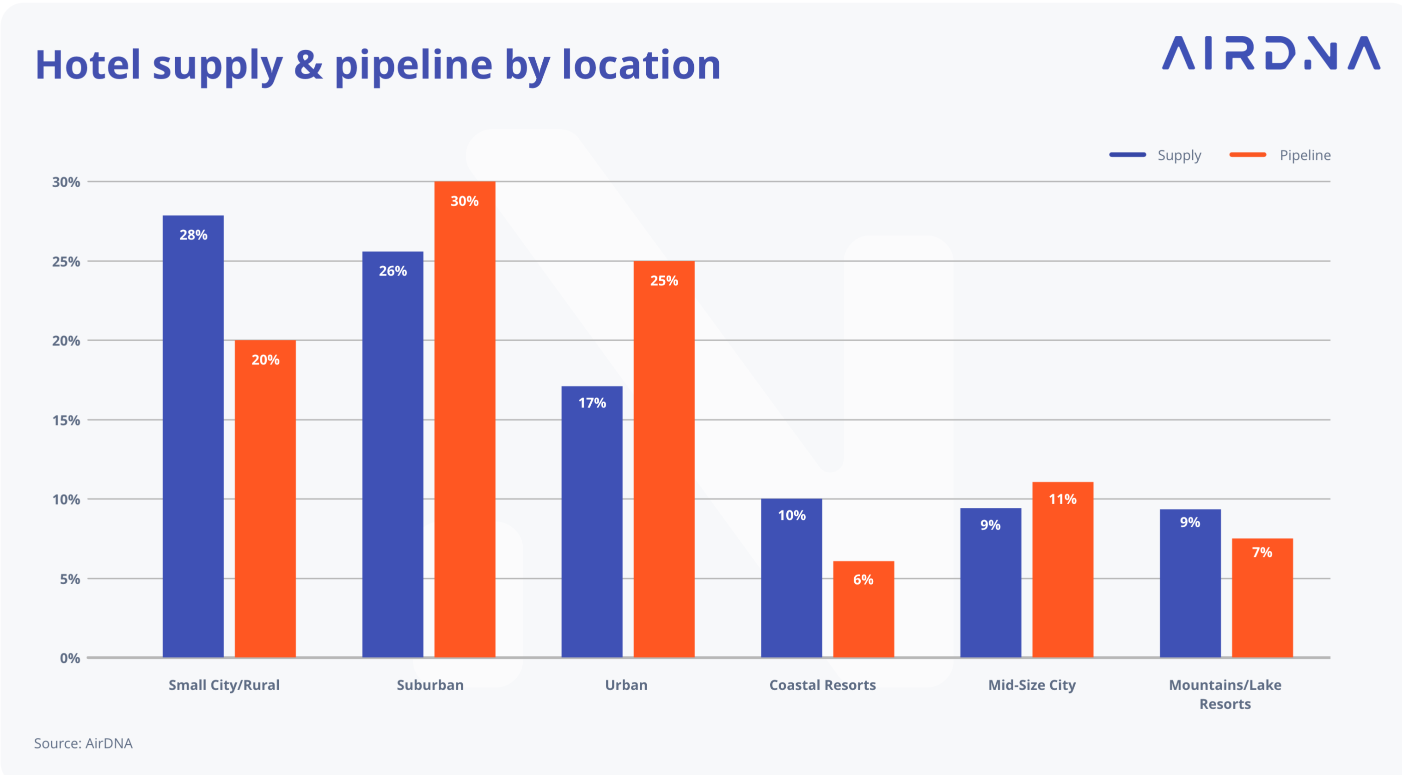
Exhibit 9: Market Share Growth Highly Variable by Location Type



Implications for the Future of the Rental Market

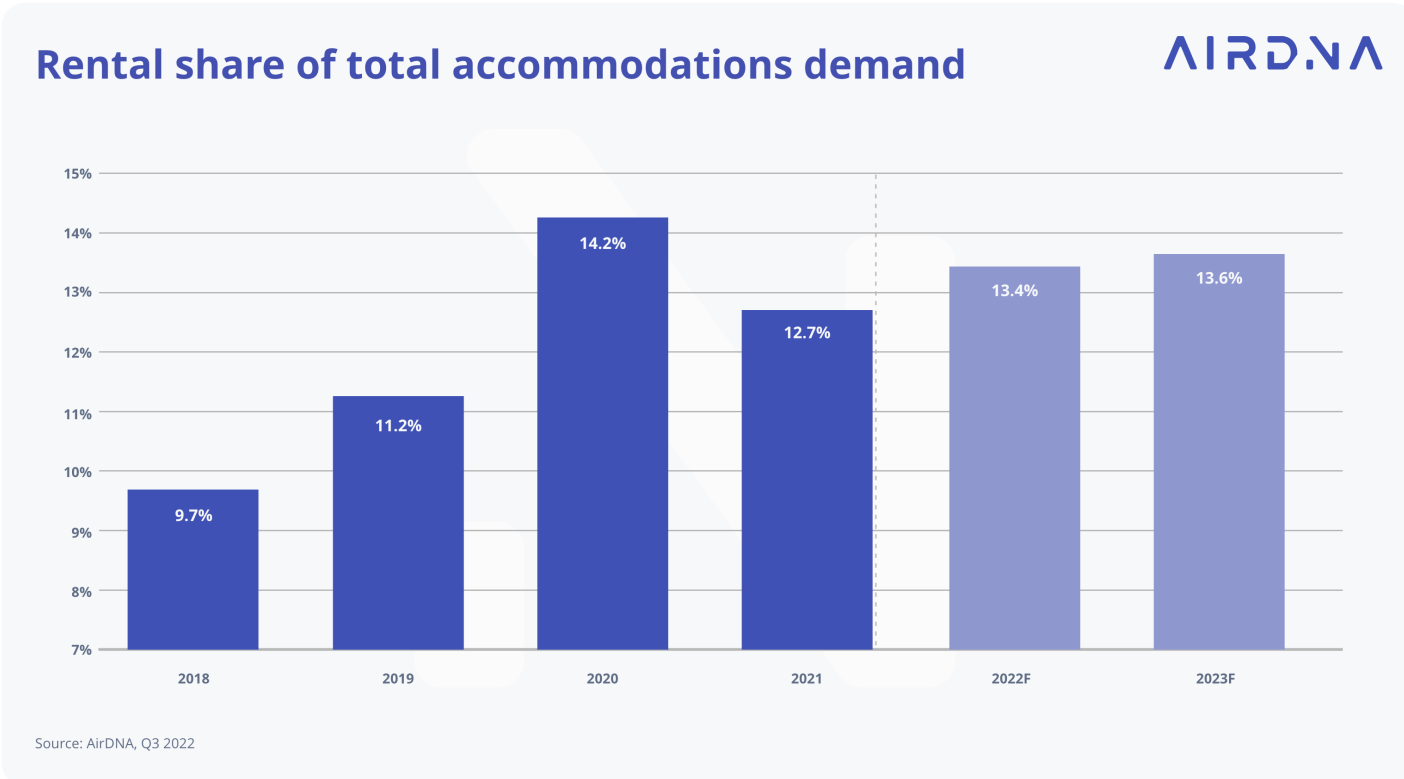
Those hosts hoping for an increase in rentals' supply share in urban and suburban locations to push up ADRs may be disappointed, looking at the hotel pipeline. Below we compare the pipeline of new hotel development to the current stock of rooms by location type. The highest ratios of new development to existing rooms are found in urban and suburban locations. Disproportionately low development is found in coastal resorts and small town/rural locations.

Exhibit 10: Pipeline will Continue Current Trends



Current forecasts, in aggregate, have rentals continuing to grow their market share, albeit at a slower pace than before the pandemic, led by continuing expansion in resorts and small towns less well-served by conventional hotel supply. With hotels expanding in urban location areas, rental growth in urban areas will be a continued drag. This tale of two markets will allow for slight gains in rentals' market share over the coming years.

Exhibit 11: Rental Share Growth Grows, But More Slowly

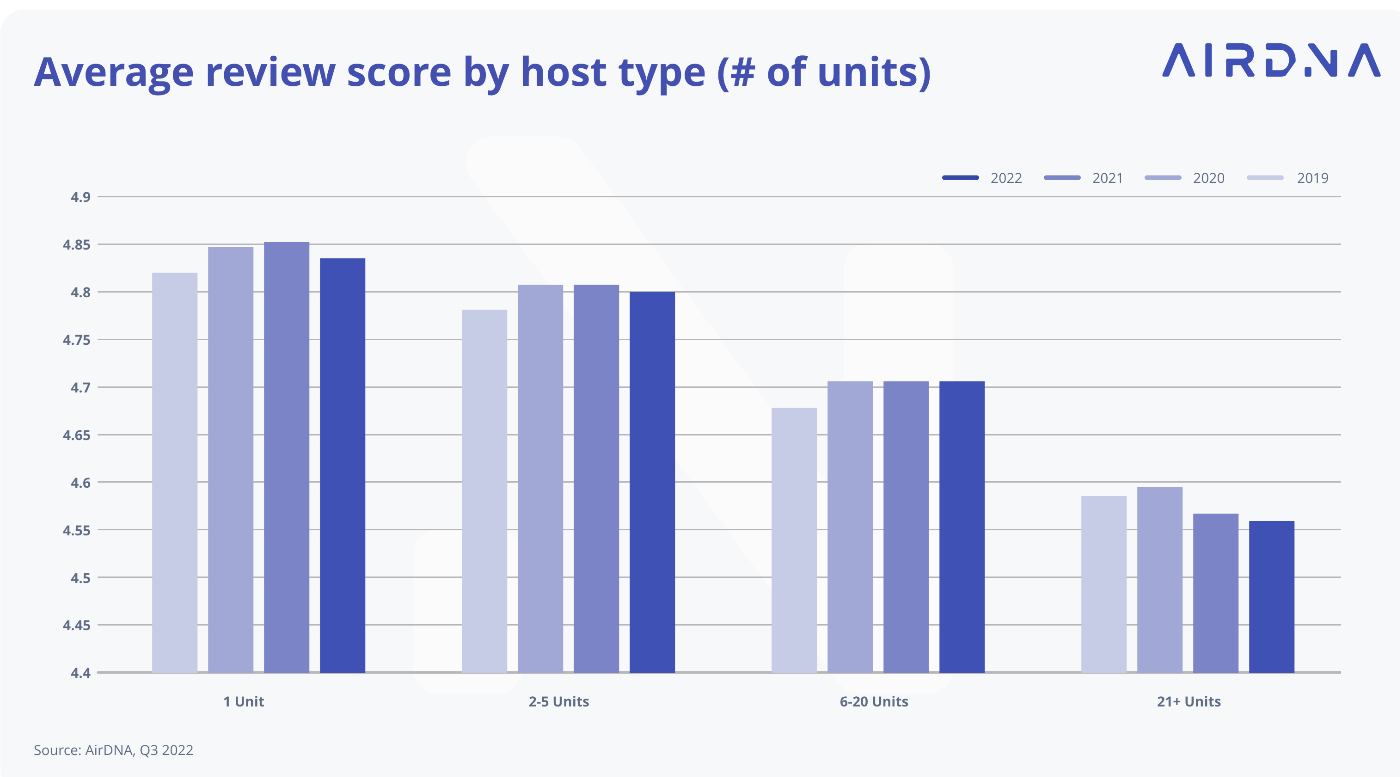


Finally, as rentals continue expanding into new and existing leisure markets, guest experience may be a key differentiator between rental properties and the more commodified hotel space. While individual hosts (those with five or fewer listings) still manage the vast majority of rental supply, those larger managers with 20 or more listings have seen the fastest growth over the past few years, and it remains to be seen how they professionalize without losing the individuality which makes the rental guest experience special.

The initial boom in the rental market in the early stages of the pandemic helped to boost outreach and exposed many new clients to the rental space. Importantly, this provided many high-quality experiences for guests, as evidenced by increases in review scores, shown below. This was also the first exposure for many guests to the rental sector—in 2020 and 2021, over 40% of guests were first-time Airbnb users, compared with just 25% in a typical year prior to the pandemic.

This boost has so far produced durable and lasting gains to guest satisfaction except, curiously, in the case of professional hosts—that is, hosts that manage more than 20 listings. This type of host reaches a lot more guests, so the guest experience they provide may be essential to continue differentiating rental experiences from conventional hotel stays.

Exhibit 12: Durable Review Score Gains Except in Pro Hosts



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