THE HOTEL INDUSTRY IN THE COMMONWEALTH

Do not forget to show hospitality to strangers.

– Hebrews 12:2

This chapter presents a long-term, 25-year look at the economic performance of the hotel industry in Virginia.[1] How important is the hotel industry to us? The candid answer: not as important as it used to be. **Table 1 reports hotel room revenue as a percentage of total personal income in the United States and Virginia in selected years. It is evident that hotel room revenue as a share of personal income generally declined in these geographic areas between 1991 and 2015.** However, the share of hotel room revenue to personal income bottomed out in the United States in 2009, but continued to fall in Virginia until 2013, when modest recovery began.

Is Airbnb responsible for some of this deterioration? Almost certainly (though data to demonstrate this are scarce). A July 2, 2016, examination of Airbnb's offerings in Virginia Beach revealed that more than 300 properties were available for rent.[2] However, Table 1 also reveals that the relative decline in importance of the hotel industry began well before Airbnb was founded in 2008. Therefore, current hotel and motel owners are off target when they blame all of their ills on Airbnb.

1 Not included in our analysis are travelers staying in nonhotel accommodations such as campgrounds, time-shares and private vacation rentals, or those who stay with friends and relatives. Also not included are expenditures that travelers make at businesses, restaurants and places of entertainment.
2 www.airbnb.com/s/Virginia-Beach--VA?s_tag=ZclJyHG2.

Why has the hotel industry fared so poorly in Virginia? The short answer is that the Great Recession of 2008 reduced the financial ability of people to travel and stay in hotels. This was compounded several years later by the federal government spending limits that were imposed by the Congressional sequestration agreement (versions of which are still in effect). Both Northern Virginia and Hampton Roads are notably dependent upon federal spending, especially defense spending, and this has had a visibly negative influence on the hotel industry.

TABLE 1

HOTEL REVENUE AS A PROPORTION OF TOTAL PERSONAL INCOME IN THE UNITED STATES AND VIRGINIA, 1991 TO 2015

	U.S.	Virginia
1991	0.887	0.918
2001	0.871	0.881
2007	0.896	0.902
2009	0.765	0.819
2010	0.795	0.820
2013	0.867	0.762
2014	0.904	0.784
2015	0.930	0.807

Sources: Smith Travel Research Trend Report, May 2, 2016; Bureau of Economic Analysis; and the Center for Economic Analysis and Policy at Old Dominion University

Where did we obtain our data? We have three primary sources. Smith Travel Research (STR) data are used for hotel lodging revenue, demand and supply of hotel rooms, as well as associated measures of hotel industry performance. Data on personal income come from the Bureau of Economic Analysis of the U.S. Department of Commerce. Consumer price index (CPI) data come from the Bureau of Labor Statistics of the U.S. Department of Labor. When we convert nominal dollars to "real" dollars, we use 1982-84 as our base.

How Has The Hotel Industry Been Performing Nationally?

We will measure performance using three metrics: (1) total hotel revenue; (2) revenue per available room (REVPAR); and (3) occupancy rates.

(1) Total Hotel Room Revenues in the United States

- Hotel room revenues, unadjusted for inflation, more than tripled from \$44.9 billion in 1991 to \$142.5 billion in 2015, or 217 percent (see Graph 1). However, in real terms, adjusting for inflation, hotel revenues increased by only 82.5 percent during the 25 years.

- Nominal room revenue increased by an average of 4.7 percent per year during this time period, but real room revenue increased by only 2.4 percent per year; prices during this time period increased by an average of 2.2 percent per year.

- **The hotel industry in the United States was severely affected by the Great Recession. Real hotel revenue declined from a peak of \$51.85 billion in 2007 to \$43.09 billion in 2009. It took the industry another four years to recover these revenue losses.** Since then, things have improved noticeably: real, inflation-adjusted hotel room revenues increased from \$52.34 billion in 2013 to \$60.15 billion in 2015, a 14.9 percent increase between 2013 and 2015.

(2) Revenue Per Available Room (REVPAR) in the United States

- Profitability is the best measure of the prosperity of a particular hotel or the hotel industry, but profitability data are not available for the market segments in which we are interested. Next best is the revenue earned by hotels per available room (REVPAR) because it is a measure that incorporates both supply and demand influences.

- REVPAR nationally increased from \$36.10 in 1991 to \$78.62 in 2015 – 117.8 percent. How much of this increase was due to general price inflation? All but 25.1 percent, which is what remains after deflating REVPAR by the Consumer Price Index. This translates to a rather small increase of only 0.9 percent annually. During the Great Recession, real, inflation-adjusted REVPAR declined from $31.61 in 2007 to a low of $24.96 in 2009. It was not until 2015 that real REVPAR had risen to $33.17 and surpassed its previous 2007 peak (see Graph 2).

(3) Hotel Occupancy Rates in the United States

- The average occupancy rate for hotels in the United States approximated 62 percent between 1991 and 2015. However, occupancy rates declined substantially during the Great Recession – the occupancy rate fell from 63.2 percent in 2006 to only 54.6 percent in 2009. It was not until 2014 that occupancy rates exceeded their 2006 level. The good news for the hotel industry is that the 2015 occupancy rate reached an all-time high – 65.5 percent (see Graph 3).

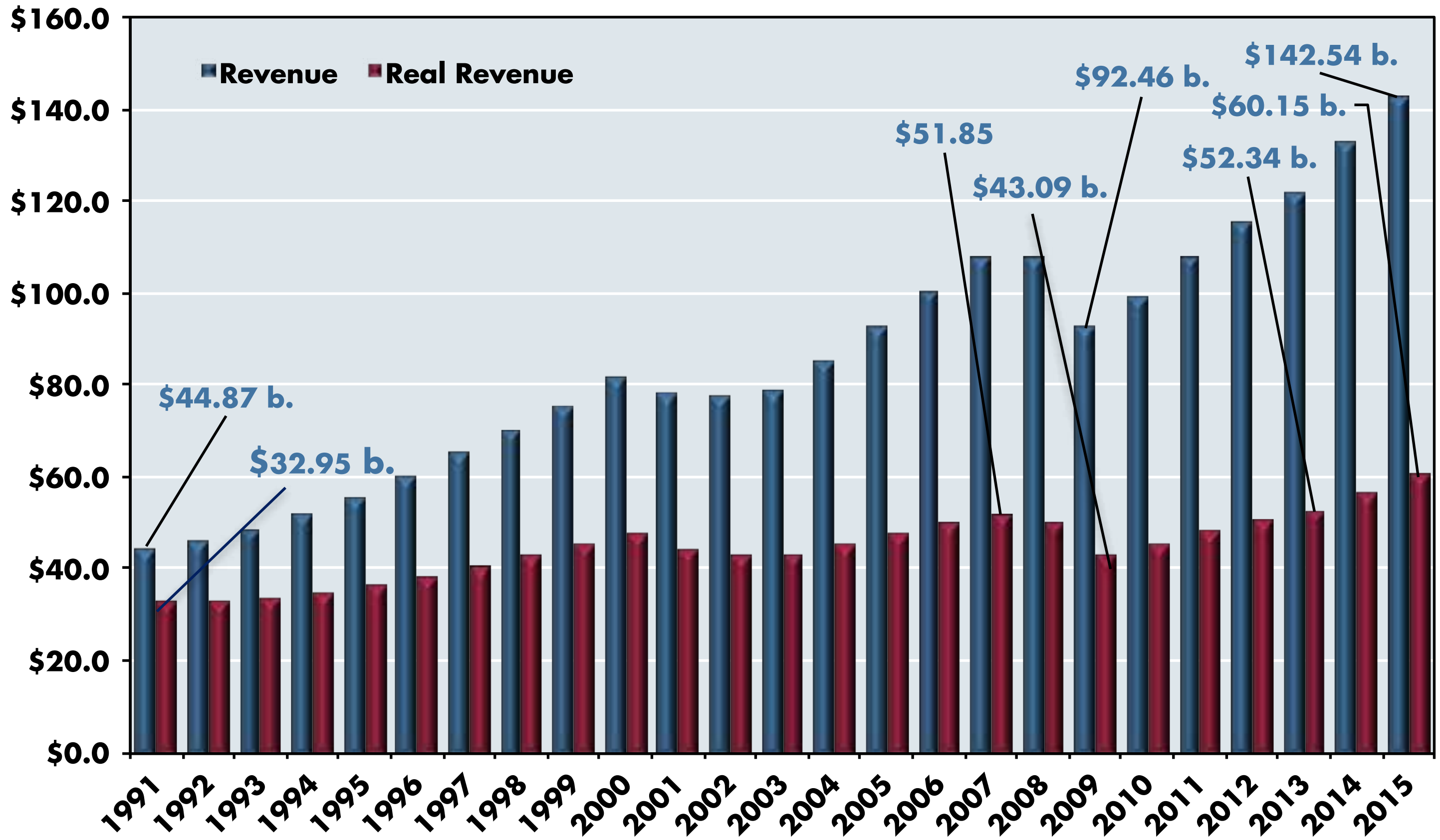
NATIONAL HOTEL INDUSTRY DYNAMICS

- The Great Recession is the major reason why the industry's performance declined between 2007 and 2009. The demand for hotel rooms began to recover in 2010 and has continued to increase steadily since then.

- The slackening of demand during the Great Recession was compounded by a substantial increase in the supply of hotel rooms. Between 2006 and 2010, the supply of hotel rooms nationally increased by 8.4 percent. Since then, the supply has been fairly stable, increasing by less than 1 percent each year between 2010 and 2014 and by only 1.1 percent in 2015 (see Graph 4).

GRAPH 1

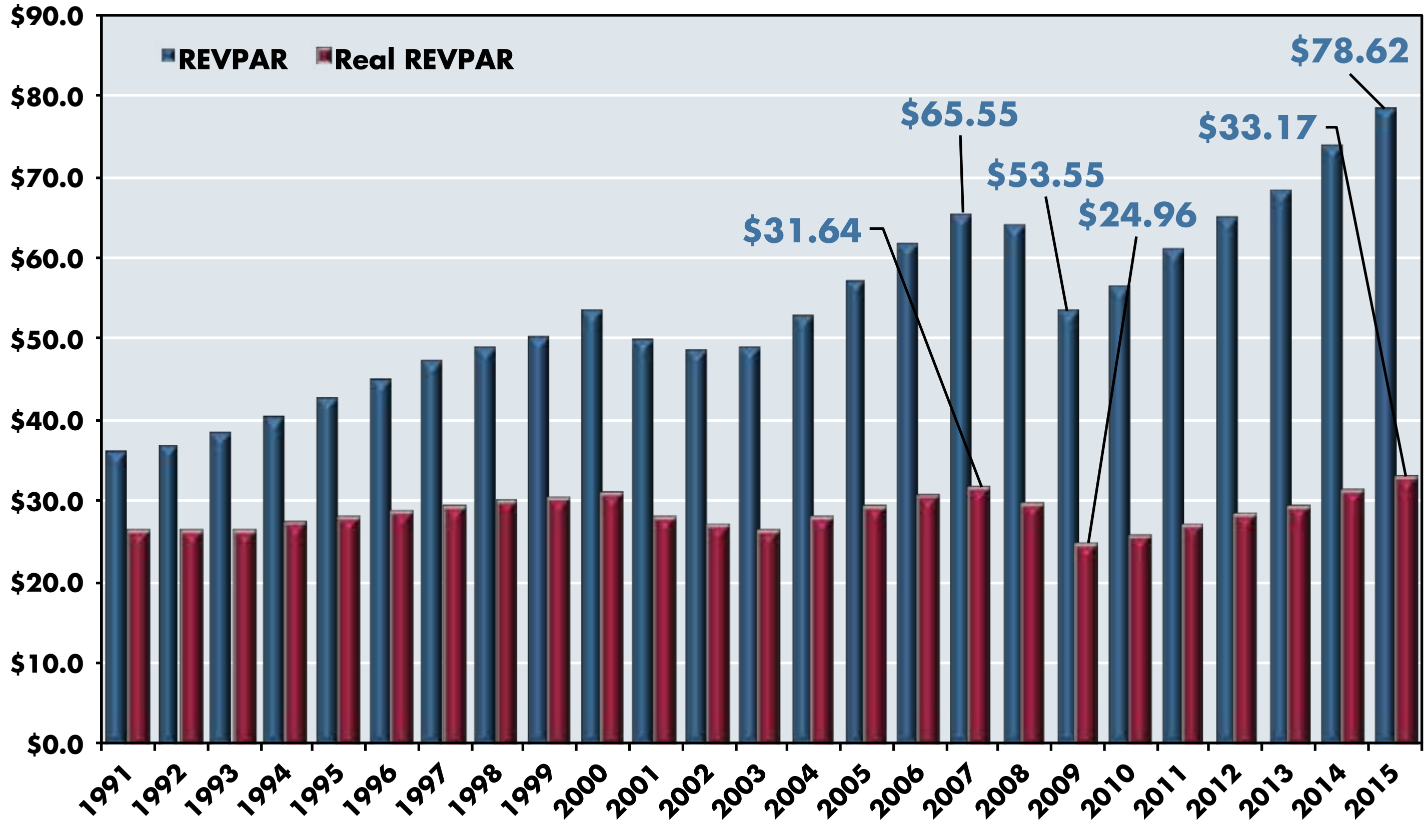
HOTEL REVENUE IN THE UNITED STATES, 1991-2015 (BILLIONS OF $)



Sources: Smith Travel Research Trend Report, May 2, 2016; Bureau of Labor Statistics; and the Center for Economic Analysis and Policy at Old Dominion University

GRAPH 2

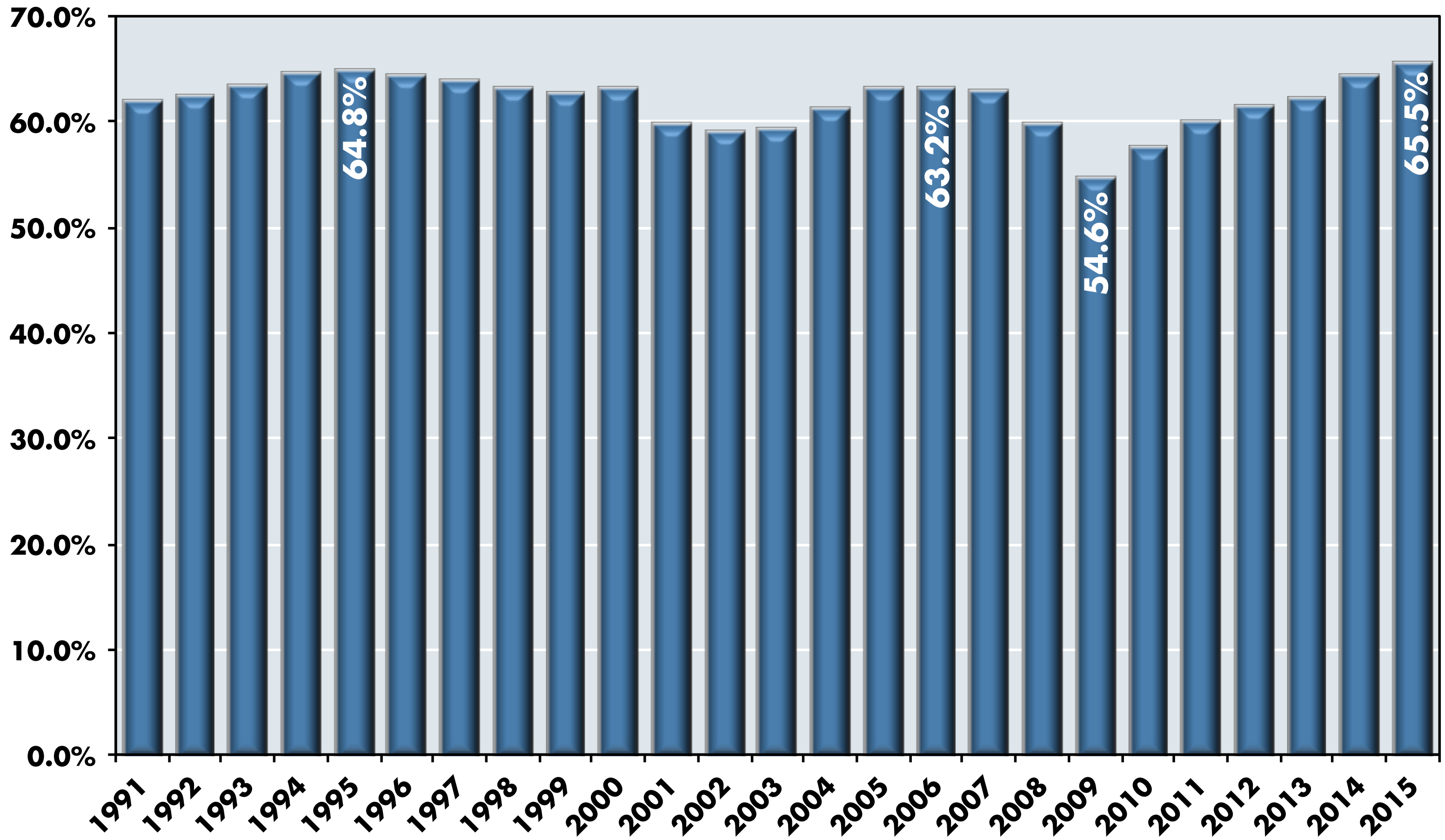
REVENUE PER AVAILABLE ROOM (REVPAR): UNITED STATES, 1991-2015



Sources: Smith Travel Research Trend Report, May 2, 2016; Bureau of Labor Statistics; and the Center for Economic Analysis and Policy at Old Dominion University

GRAPH 3

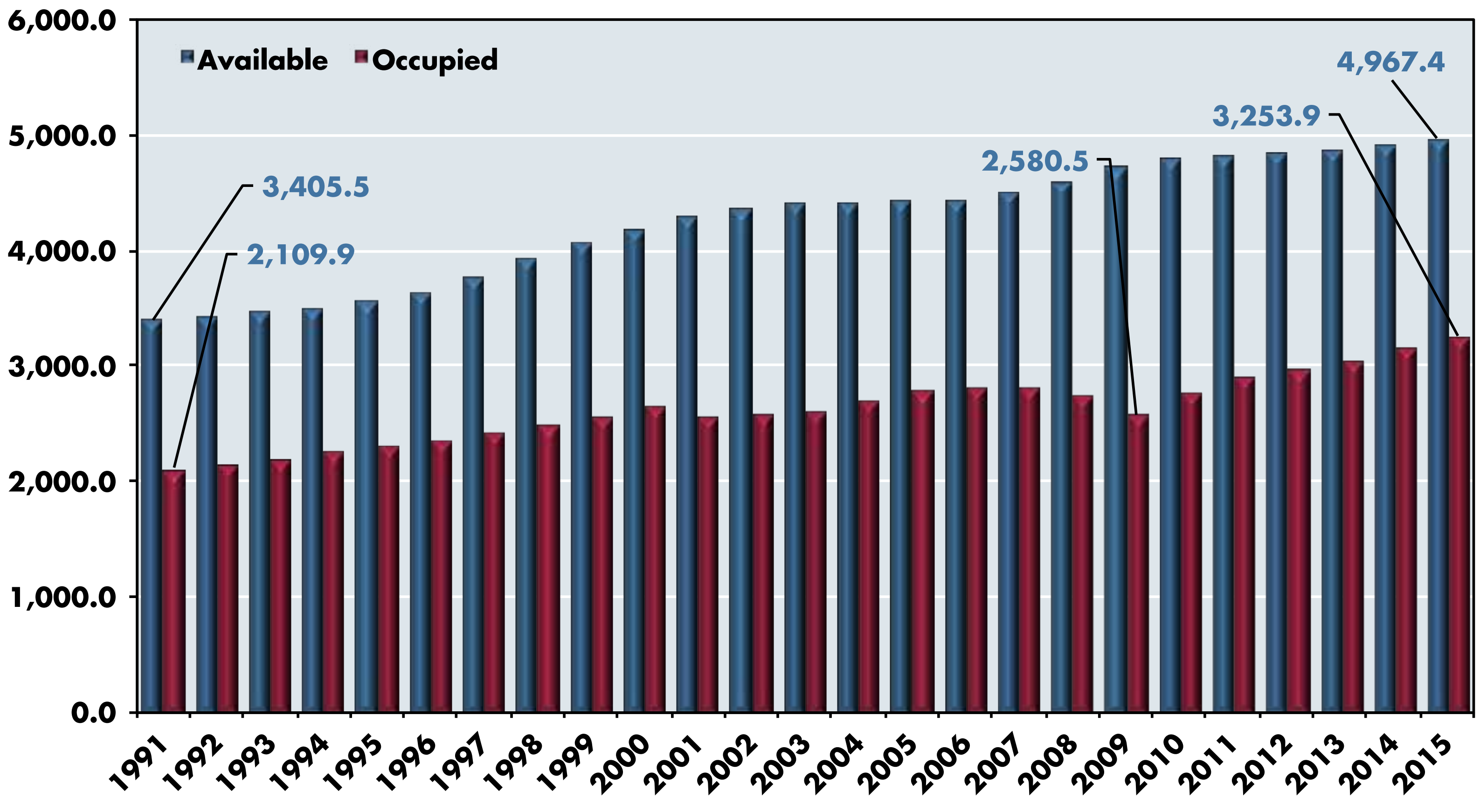
HOTEL OCCUPANCY RATES IN THE UNITED STATES, 1991-2015



Sources: Smith Travel Research Trend Report, May 2, 2016, and the Center for Economic Analysis and Policy at Old Dominion University

GRAPH 4

AVAILABLE HOTEL ROOMS AND ROOMS OCCUPIED IN THE UNITED STATES, 1991-2015



Sources: Smith Travel Research Trend Report, May 2, 2016, and the Center for Economic Analysis and Policy at Old Dominion University

How Has The Hotel Industry Been Performing In Virginia?

(1) Total Hotel Room Revenues in Virginia

- **If total hotel room revenue is the criterion, then over the past 25 years, the performance of the hotel industry in the Commonwealth has been poor compared to the nation as a whole.** Total hotel room revenue in Virginia increased by 185 percent between 1991 and 2015, but this easily trailed the national increase of 217 percent. When adjusted for inflation, hotel room revenues statewide increased by only 63.7 percent during the same time period, once again trailing the national average of 82.5 percent.

- Even though real hotel room revenues increased from $1.32 billion in 2013 to $1.49 billion in 2015 (a 12.87 percent gain), they remain slightly lower than the $1.50 billion peak in 2007 (see Graph 5).

(2) Revenue Per Available Room (REVPAR) in Virginia

- Over the last 25 years, nominal REVPAR in the Commonwealth increased from $32.18 in 1991 to $63.99 in 2015, or 98.9 percent. However, real, inflation-adjusted REVPAR increased by only 14.3 percent during the same time period, or only 0.5 percent annually. Further, real REVPAR began to decline in 2007 and continued to fall through 2013. Real REVPAR did increase in 2014 and 2015, but remains well below its 2007 peak of $29.86 (see Graph 6).

(3) Occupancy Rates in Virginia

- **The occupancy rate of hotels in Virginia averaged approximately 61 percent between 1991 and 2015 – slightly below that of the nation. The Great Recession hammered Virginia hotels and by 2009 their average occupancy rate had fallen to only 54.5 percent. Since then, occupancy rates generally have trended upward. The 2015 rate was 61.6 percent – still below the highs of 62.61 percent in 2005 and 63.51 percent in 1994 (see Graph 7).**

VIRGINIA HOTEL INDUSTRY DYNAMICS

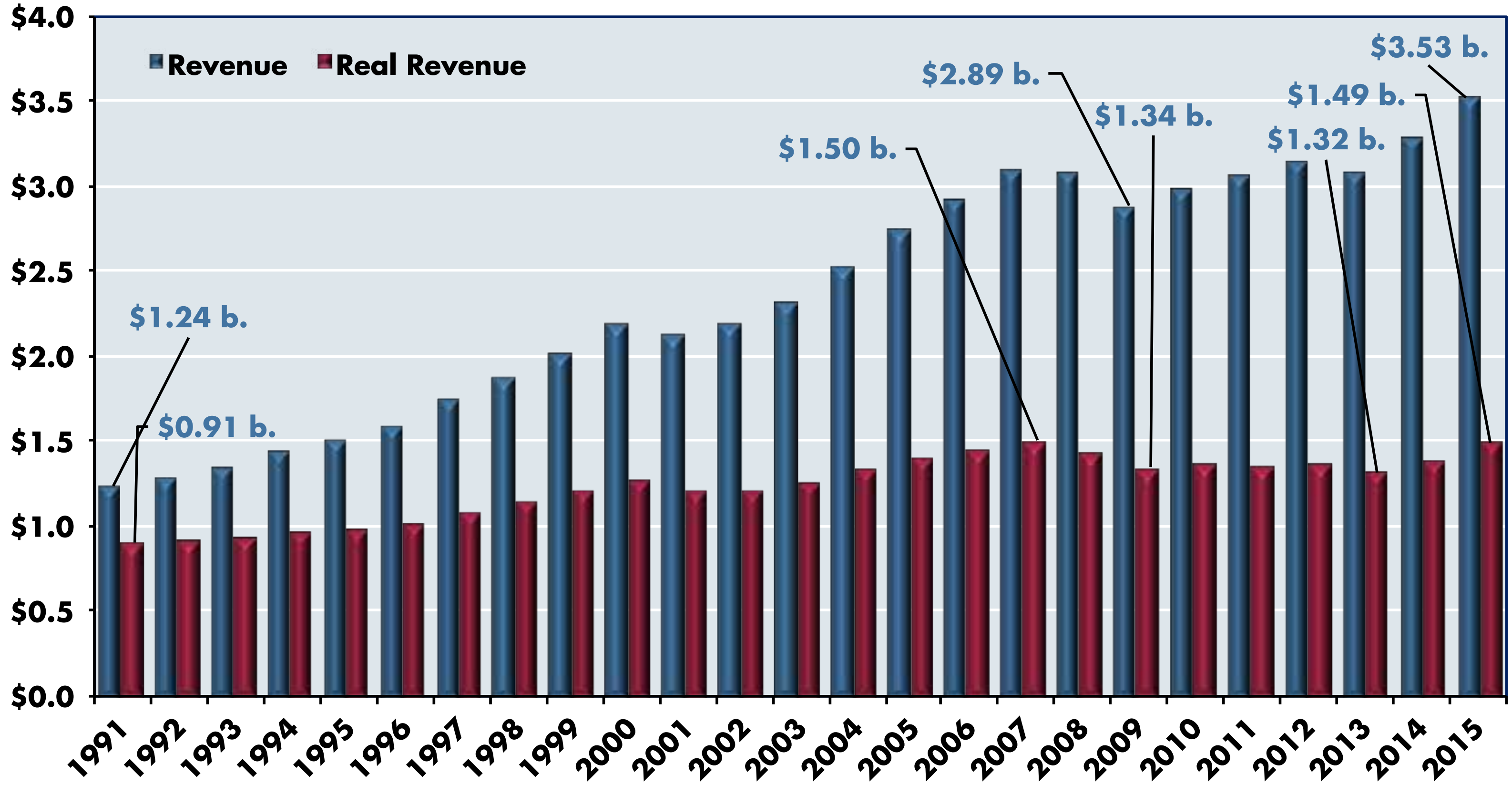
- **There is little mystery attached to the causes of the underperformance of the hotel industry in Virginia in recent years. The combination of the Great Recession plus federal government budget sequestration constituted powerful blows from which the industry has yet to recover.**

- Further, as was true for the United States, a substantial increase in the supply of hotel rooms in Virginia put an additional damper on industry performance. Even while the demand for hotel rooms was declining between 2006 and 2010, the supply of hotel rooms was increasing by 11.4 percent in Virginia. Since then, that supply has held fairly constant. By the end of 2015, the total supply of hotel rooms in Virginia actually was 0.05 percent below its 2010 level.

- The good news going forward for the Virginia hotel industry is that the hotel room supply/demand imbalance appears to be diminishing (see Graph 8). Nonetheless, happy days are not likely to return until federal spending in the Commonwealth, especially for defense, revives.

GRAPH 5

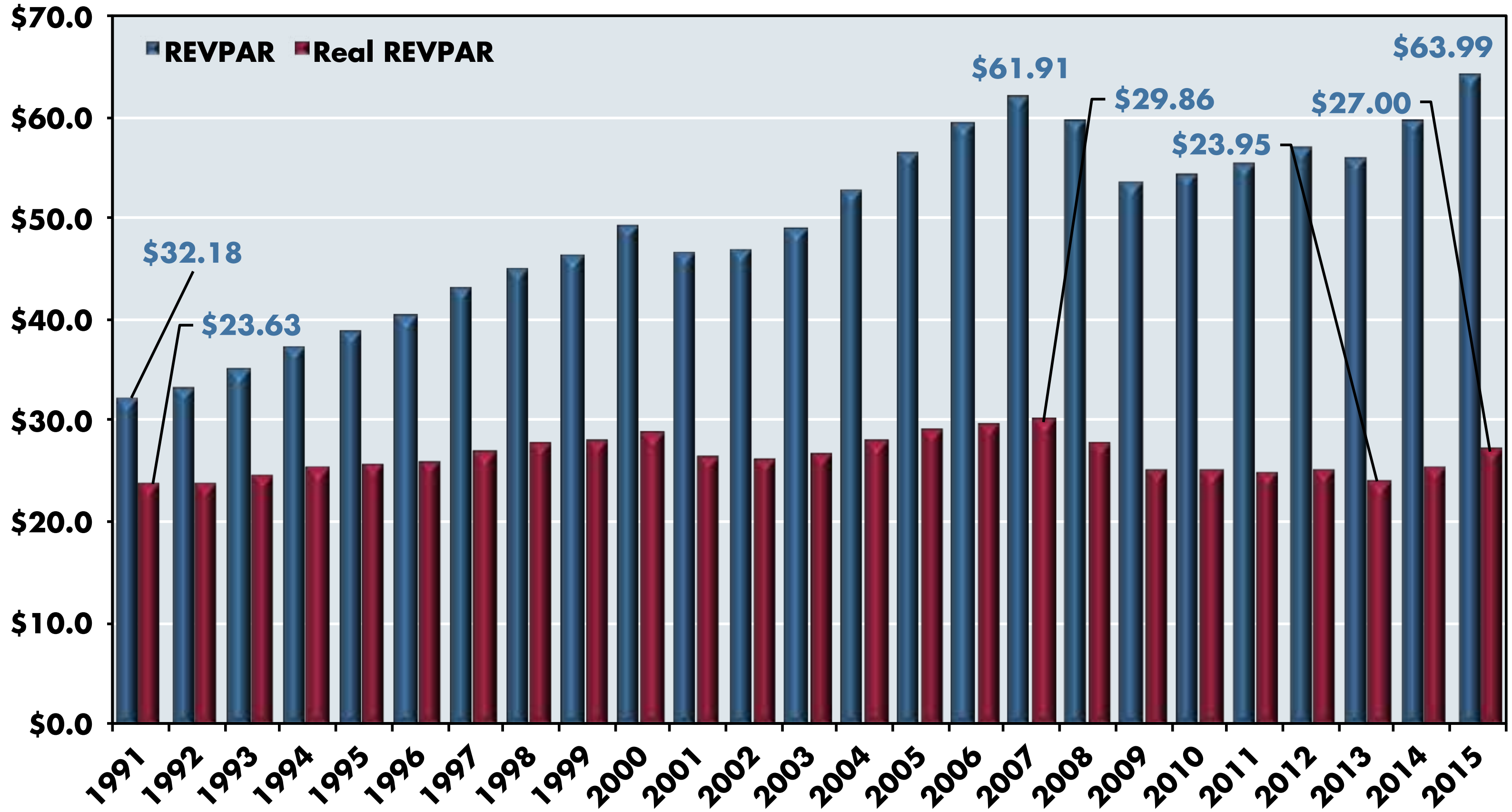
HOTEL REVENUE IN VIRGINIA, 1991-2015 (BILLIONS OF $)



Sources: Smith Travel Research Trend Report, May 2, 2016; Bureau of Labor Statistics; and the Center for Economic Analysis and Policy at Old Dominion University

GRAPH 6

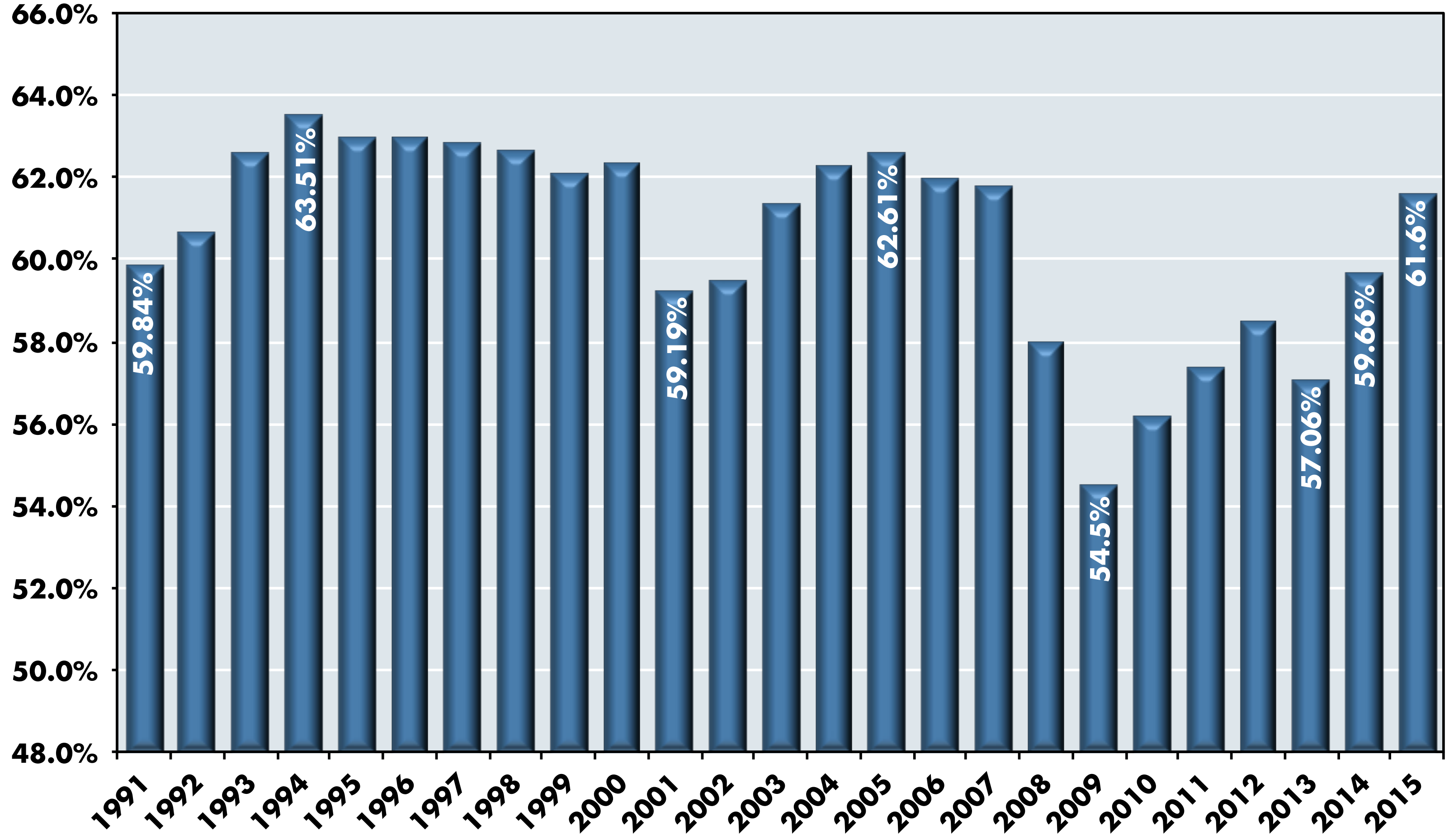
REVENUE PER AVAILABLE ROOM (REVPAR) IN VIRGINIA, 1991-2015



Sources: Smith Travel Research Trend Report, May 2, 2016; Bureau of Labor Statistics; and the Center for Economic Analysis and Policy at Old Dominion University

GRAPH 7

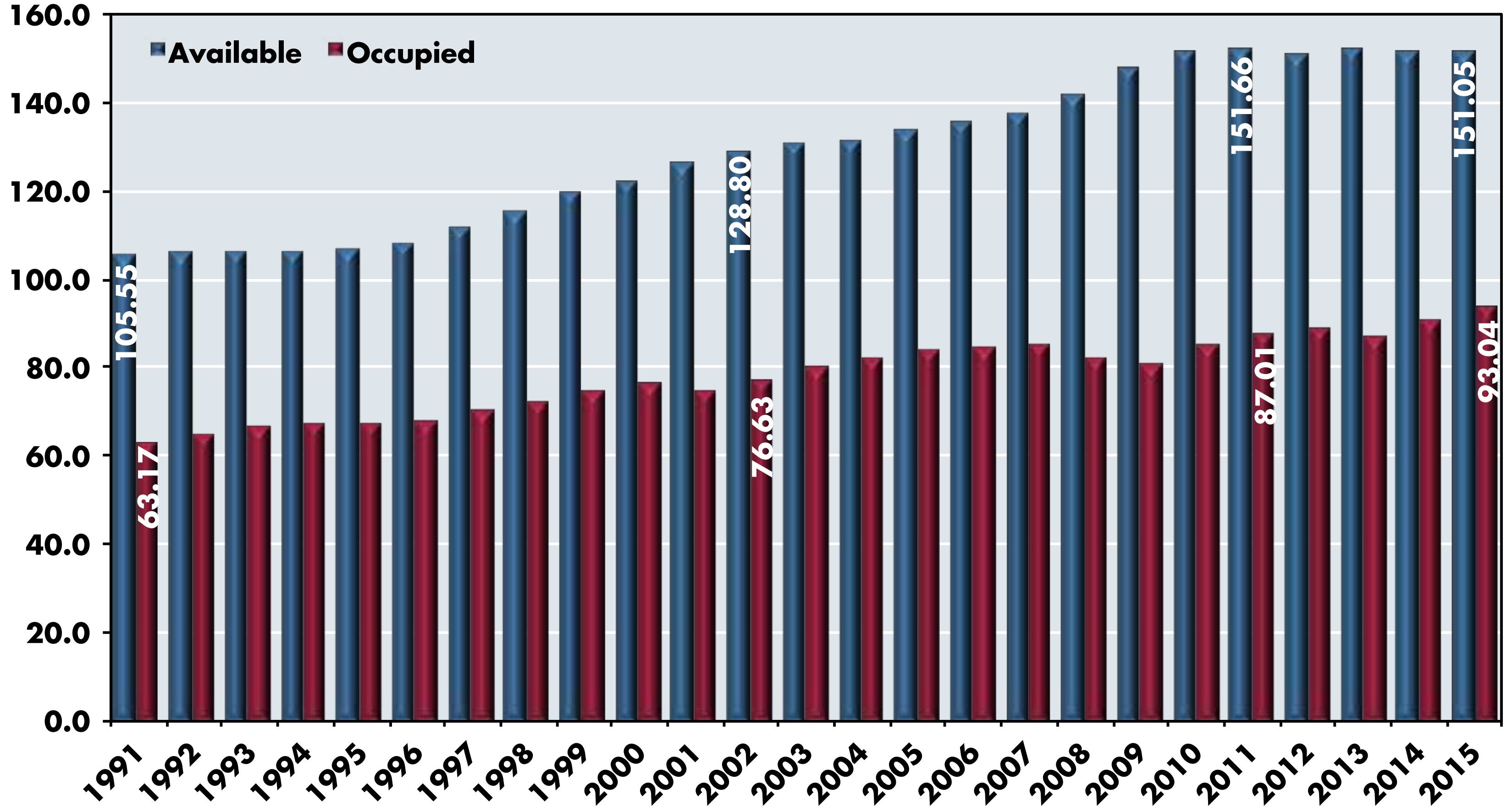
HOTEL OCCUPANCY RATES IN VIRGINIA, 1991-2015



Sources: Smith Travel Research Trend Report, May 2, 2016, and the Center for Economic Analysis and Policy at Old Dominion University

GRAPH 8

AVAILABLE HOTEL ROOMS AND ROOMS OCCUPIED IN VIRGINIA (000S), 1991-2015



Sources: Smith Travel Research Trend Report, May 2, 2016, and the Center for Economic Analysis and Policy at Old Dominion University

How Has The Hotel Industry Been Performing In Selected Virginia Metropolitan Areas?

(1) Total Hotel Room Revenue in Virginia Beach and the Virginia Portion of the Washington, D.C., Metropolitan Region

- If we once again use total hotel room revenue as our criterion, then the performance of the hotel industry in Virginia Beach has roughly matched the performance of the entire state over the past 25 years (see Graph 9). True, nominal total hotel revenue increased from $120.17 million in 1991 to $293.43 million in 2015 (144.2 percent). Nevertheless, in real terms, total hotel room revenue declined by a little less than 1 percent during the 25 years. Compare this to the nation's 82.5 percent increase and Virginia's 63.7 percent increase.

- Meanwhile, in the Virginia portion of the Washington, D.C., metropolitan region, nominal hotel revenue rose 235.9 percent to $1.63 billion in 2015 and real hotel revenues rose 93 percent to $687.8 million (see Graph 10).

(2) Revenue Per Available Room (REVPAR) in Roanoke and Bristol

- Where REVPAR is concerned, the Roanoke and Bristol/Kingsport metropolitan areas performed better than Virginia Beach, but not as well as Northern Virginia. Graph 11 reveals that real REVPAR in Roanoke increased by 6.1 percent between 1991 and 2015, while Graph 12 tells us that real REVPAR in the Bristol/Kingsport region increased by 2.3 percent during the intervening 24 years.

- Since REVPAR may be the single best measure of the health of a hotel or motel, the very modest increases in REVPAR that were spread over almost a quarter-century in these two regions underline the reality that, in general, these have not been boom times for hotels in Virginia.

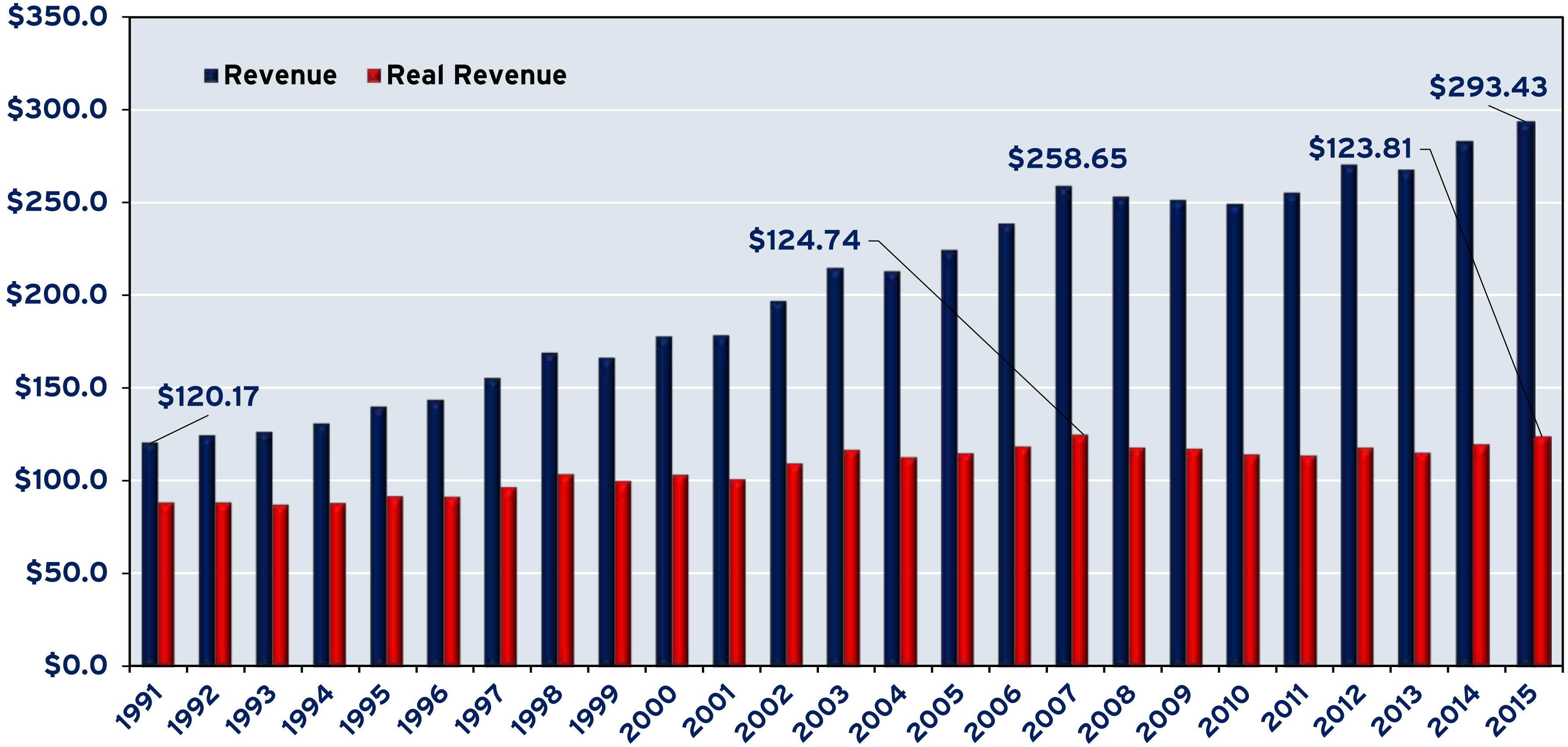
(3) Occupancy Rates in Richmond/Petersburg and Williamsburg

- The occupancy rate for hotels in the Richmond/Petersburg area peaked in 1996 at 63.64 percent, reached a low of 48.23 percent in 2009 and then recovered nicely to 61.94 percent in 2015 (see Graph 13). This occupancy rate roughly matches Virginia's 61.6 percent, but trails the national rate of 65.5 percent. This is further evidence that all is not well in the hotel industry in the Commonwealth.

- The story is even less attractive in the case of Williamsburg where, despite recent recovery, occupancy rates still are about 9 percent below what they were in the mid-1990s. The Historic Triangle (Williamsburg, Jamestown, Yorktown) currently is in the process of repositioning itself and the messages it sends to prospective visitors (see Graph 14).

GRAPH 9

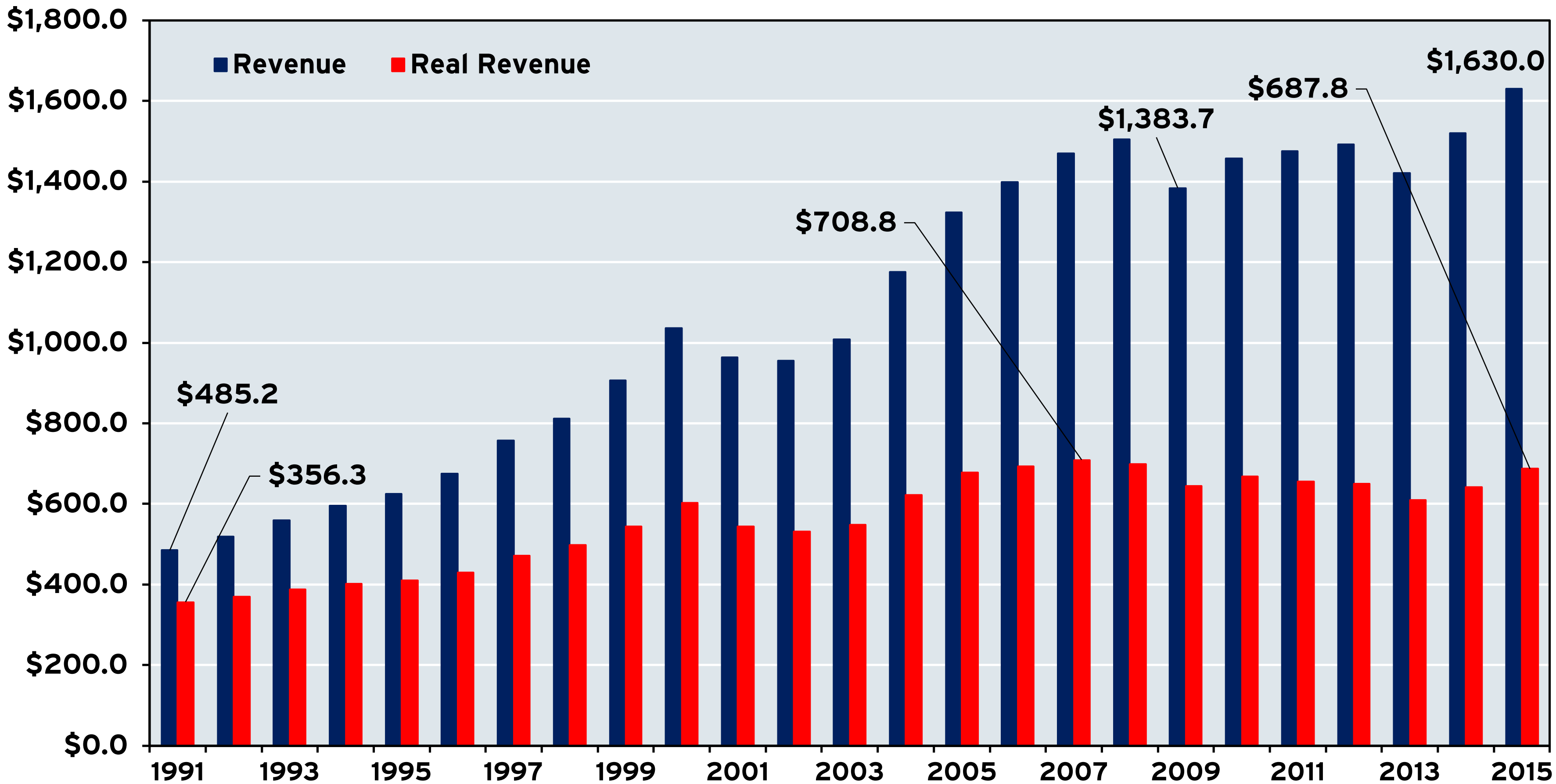
HOTEL REVENUE IN VIRGINIA BEACH, 1991-2015 (MILLIONS OF $)



Sources: Smith Travel Research Trend Report; Bureau of Labor Statistics; and the Center for Economic Analysis and Policy at Old Dominion University

GRAPH 10

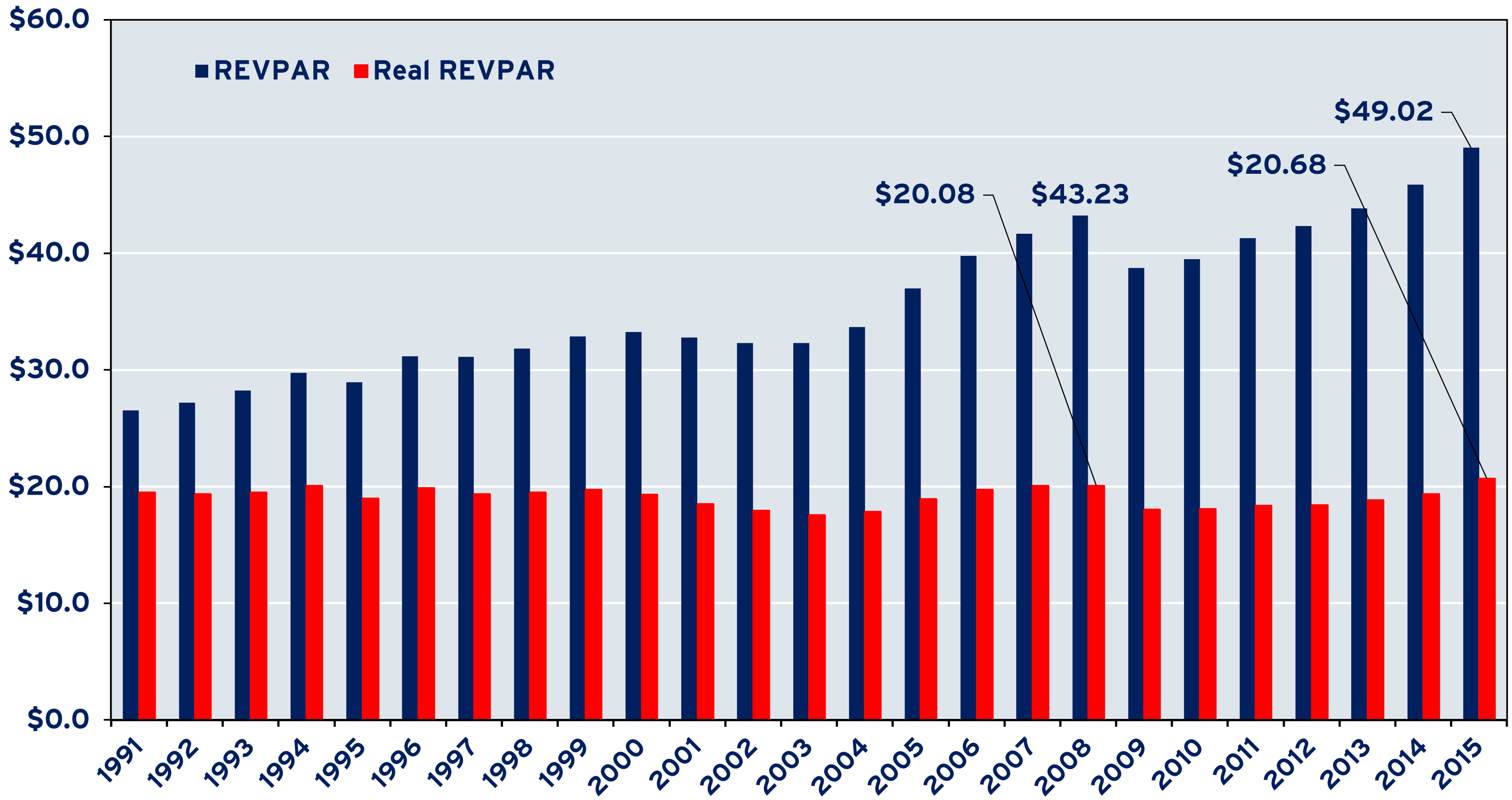
HOTEL REVENUE IN THE VIRGINIA PORTION OF THE WASHINGTON, D.C., METROPOLITAN REGION, 1991-2015 (MILLIONS OF $)



Sources: Smith Travel Research Trend Report; Bureau of Labor Statistics; and the Center for Economic Analysis and Policy at Old Dominion University

GRAPH 11

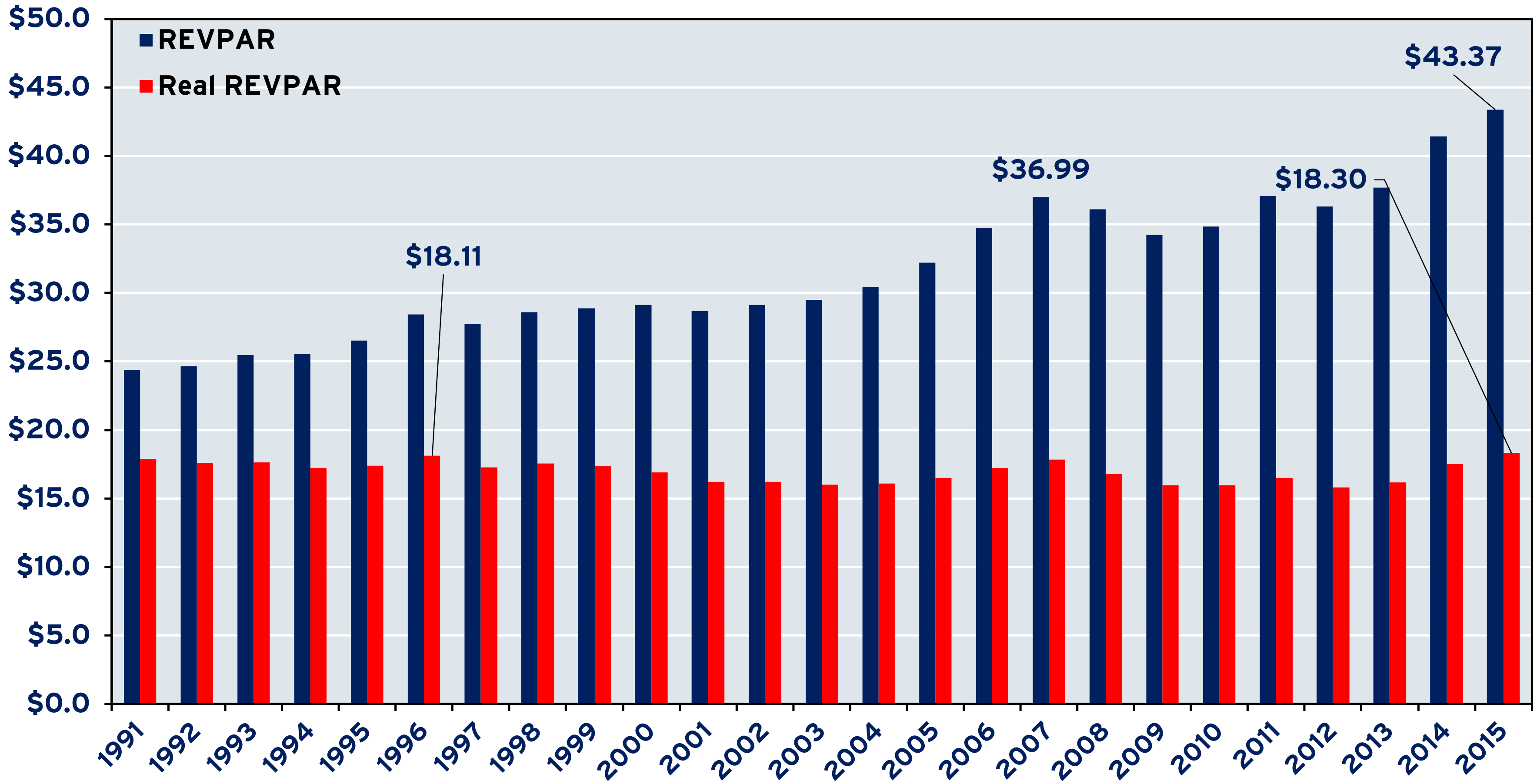
NOMINAL AND REAL REVPAR IN ROANOKE, 1991-2015 (MILLIONS OF $)



Sources: Smith Travel Research Trend Report; Bureau of Labor Statistics; and the Center for Economic Analysis and Policy at Old Dominion University

GRAPH 12

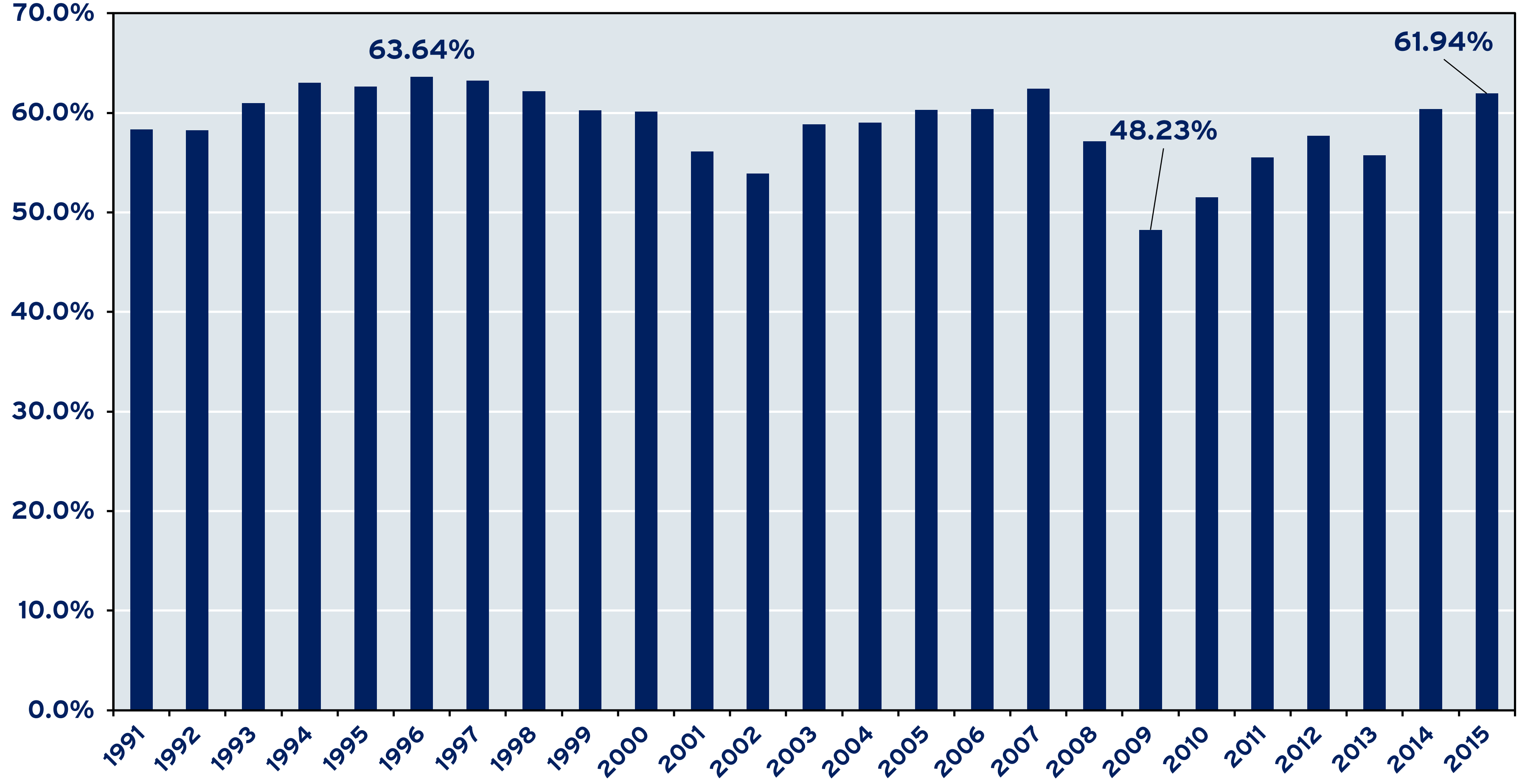
NOMINAL AND REAL REVPAR IN BRISTOL/KINGSPORT, 1991-2015 (MILLIONS OF $)



Sources: Smith Travel Research Trend Report; Bureau of Labor Statistics; and the Center for Economic Analysis and Policy at Old Dominion University

GRAPH 13

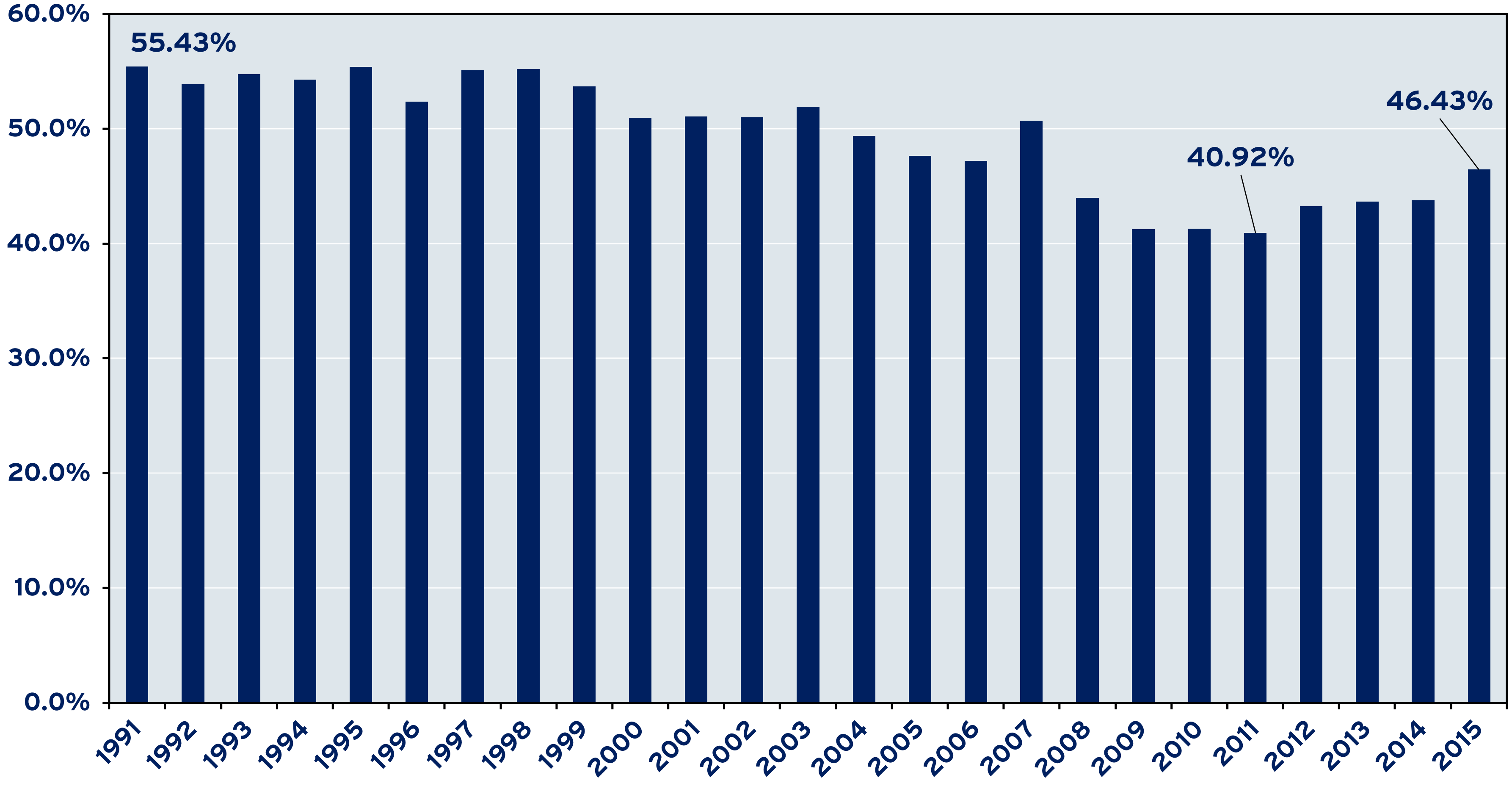
HOTEL OCCUPANCY RATES IN RICHMOND/PETERSBURG, 1991-2015



Sources: Smith Travel Research Trend Report; Bureau of Labor Statistics; and the Center for Economic Analysis and Policy at Old Dominion University

GRAPH 14

HOTEL OCCUPANCY RATES IN WILLIAMSBURG, 1991-2015



Sources: Smith Travel Research Trend Report; Bureau of Labor Statistics; and the Center for Economic Analysis and Policy at Old Dominion University

HOTEL INDUSTRY DYNAMICS IN THE METROPOLITAN REGIONS

- **Each metropolitan area in many ways is a microcosm of the Commonwealth in terms of the causes of its hotel industry distress. The Great Recession and torpid defense spending are the major culprits.** Alas, recent economic growth numbers for Virginia have not been encouraging, and Congressional spending sequestration is likely to continue. This does not bode well for Virginia. However, the Commonwealth does appear to be working its way out of the supply/demand imbalance for hotel rooms that reached its peak in the state in 2009 and 2010. If this trend continues, then it will improve both REVPAR and occupancy rates for hotel rooms throughout the state.

- The overall prosperity of Virginia's hotel industry is demonstrably sensitive to federal spending levels. Sequestration has had a significant negative impact upon the number of rooms demanded by federal employees and active-duty military personnel. The average daily rate charged by hotels in the Washington, D.C., hotel market in 2015 ($149.61) was below the comparable 2007 level ($153.13), and the real average daily rate in 2015 in the Capitol Region remained 14.3 percent below its 2007 level.

- Further, stagnant or contracting travel budgets have caused many federal agencies to substitute remote meetings powered by software such as Skype, Jitsi and Goober instead of face-to-face meetings that require out-of-town travel. In military-intensive Hampton Roads, every single submarket in that region experienced negative real REVPAR between 2007 and 2015. **As a general rule, the greater the distance a metropolitan hotel market is from Washington, D.C., the greater the probability that market did not experience a decline in REVPAR over the 2007-2015 time period.** Bristol, Lynchburg, Roanoke and Staunton all experienced increases in real REVPAR during the same years.

- An interesting trend in some of Virginia's hotel markets involves a gradual upscale movement in the quality of rooms being supplied and occupied. In brief, more upscale hotel rooms that typically operate under the aegis of national franchises and are able to command higher prices[3] gradually are replacing older, less impressive hotels and motels that have no national connections. In Virginia Beach, total hotel room revenue increased nicely (9.7 percent between 2013 and 2015) even though the city actually supplied fewer hotel rooms. A recent study performed for the city of Virginia Beach, based upon Smith Travel Research data, found that franchised, upscale hotels in the resort city not only charged higher rates, but also had higher occupancy rates than economy hotels. Table 2 presents some of those study results.

TABLE 2

HOTEL PERFORMANCE BY HOTEL CATEGORY: VIRGINIA BEACH, 2006 AND 2014

	2006	2014	Percentage Change
Supply of Upscale Rooms	2,365	3,019	+27.7%
Supply of Economy Rooms	2,698	2,661	-1.4%
Demand for Upscale Rooms	1,590	1,942	+22.1%
Demand for Economy Rooms	1,601	1,531	-4.4%
REVPAR at Upscale Hotels	$83.5	$93.0	+11.4%

Source: 2014 Virginia Beach Hotel Supply & Demand Analysis, February 2016, and the Center for Economic Analysis and Policy at Old Dominion University

3 Smith Travel Research data show that the supply of hotel rooms designated as "upscale" (measured by high average daily rates) increased 27.7 percent between 2006 and 2014, while "economy" hotel rooms decreased in number by 1.4 percent. Further, the average occupancy rate at the upscale hotels was 65.1 percent, compared to only 57.2 percent at economy hotels.

Final Thoughts

Can the hotel industry and the overall tourism sector recover their mojo and reverse their decline in relative economic importance in Virginia? This does not seem likely to occur as long as federal financial sequestration restricts federal expenditures overall and defense expenditures in particular.

Once again, it is apparent that the Commonwealth's economic dependence on federal spending is a two-edged sword. Ideally, the Virginia economy of the future will be more diversified and current federal contractors increasingly will find private-sector and international customers for their goods and services. There are encouraging signs that some of this evolution is occurring now in Northern Virginia.

It is easy to editorialize that Virginia's economic base should be more diversified than it is currently. Accomplishing this, however, is hardly an easy task and it is fair to say that no consensus exists among either elected officials or academics as to how to go about this. In the context of this chapter dealing with the hotel industry, it is an issue in need of further study.