

Airbnb In Virginia Beach



AIRBNB IN VIRGINIA BEACH

Airbnb is an international, internet-based firm that connects owners of rental properties (“hosts”) with prospective short-term renters (“guests”). Founded in 2008, Airbnb asserts that it is active in more than 65,000 cities and 191 countries and that it has hosted more than 150 million guests. Its market value exceeded \$30 billion last year.¹ Airbnb claimed to have more than 3 million rental listings worldwide in early 2017², and in January 2017, 454 of those listings (mostly involving residential homes) were in Virginia Beach.³

Virtually every new economic phenomenon that upends customary ways of doing business stimulates concerns and the rise of Airbnb is no exception. Conventional hotels and motels question whether Airbnb is “playing by the rules” and the city of Virginia Beach worries that it is not collecting all taxes due.

This chapter analyzes the development of Airbnb in our midst, but places this phenomenon in the broader context of the rise of the “gig economy” – a world in which occasional contractors, part-time workers and temporary economic arrangements increasingly hold sway. What we observe is Joseph Schumpeter’s “creative destruction” in action – yet another example of the never-ending churn in the economic system that drives out the old and brings in the new.⁴

Airbnb In Virginia Beach And Hampton Roads

To track Airbnb’s activities in Virginia Beach, one must rely upon data produced by Airdna, a separate and independent organization that generates numbers and analytics focusing on vacation rental entrepreneurs and investors. Per Airdna

¹ Matt Rossoff, “Airbnb Is Now Worth \$30 Billion,” *Business Insider* (Aug. 6, 2016), www.businessinsider.com.

² www.airbnb.com.

³ Airdna market reports.

⁴ Joseph Schumpeter (1883-1950) was an Austrian-born economist who spent much of his career at Harvard. His *Capitalism, Socialism and Democracy* (1942) is considered a classic in the literature of economic development.

(whose data we use throughout this report), “active” Airbnb listings in Virginia Beach grew from only one in 2011 to 392 in 2016, more than doubling each year since 2011. Airdna classifies a listing as active if it has a confirmed booking in a month, if it is currently live on Airbnb, if the host has updated the calendar for the listing or if the host actively responds to inquiries about the property. The number of available properties (active and inactive) listed at the end of each month increased steadily from 109 in January 2015 to 464 in December 2016.

From January 2015 to December 2016, even though December is a low point in the tourism season in Virginia Beach, the number of available Airbnb properties increased by 325 percent.⁵ Over the same period, according to Smith Travel Research, the supply of conventional hotel rooms increased by only 1.2 percent.

Airbnb frequently talks in term of “listings.” An Airbnb listing may consist of a shared room, a private room, studio apartment or several rooms within a house that are available for rent. The number of listings understates the number of rooms available through Airbnb. This is a very important point to consider when one attempts to estimate Airbnb’s share of the overall hotel market in Virginia Beach.

In January 2017, 358 of the 454 Airbnb listings in Virginia Beach were active and we estimate that these 358 listings offered 655 rooms for rent daily. Only

⁵ This is consistent with the reported national Airbnb growth rate in revenues in 2016 of 138 percent. During this time, Airbnb’s revenues grew from an estimated \$2.4 billion in 2015 to \$5.7 billion in 2016. Chris Kirkham and Greg Bensinger, “Hotel Group Assails Airbnb Model,” *The Wall Street Journal*, 269 (March 20, 2017), B4.

33 percent of these listings were for one room (which could be shared, private or studio). For each active listing, on average, there were 1.8 rooms on the Airbnb website (compared to an average of 1.6 for the entire United States in fourth quarter 2015).⁶ This means that many of the most active listings for Virginia Beach for the period in question were for multiple rooms, confirming that listings understate the number of rooms Airbnb offers for rent daily.

Our “more Airbnb rooms than listings” conclusion is consistent with a recent study performed for the American Hotel and Lodging Association by CBRE, a well-known national real estate firm. While the association is hardly a neutral party in terms of its attitudes toward Airbnb, its commissioned study concluded that one-third of Airbnb’s revenues now come from individuals and investors who own or control multiple units (see Graph 1).

The American Hotel and Lodging Association fervently argues (perhaps correctly) that the parties that function in this fashion in essence are hotels, albeit operating without having to comply with all the rules and regulations confronting standard hotels. Not surprisingly, the association advocates a legal and enforcement crackdown on Airbnb operators, who increasingly have become viable competitors to the association’s members. The association’s reaction in this regard is similar to that observed when any established industry is confronted with a new viable competitor that appears to be upending previously well-established rules. Witness the reactions of taxicab companies to Uber and Lyft, established commercial banks to internet competitors such as Synchrony and Quicken, some universities to online learning sites and, of course, dozens of competitors across many industries to Amazon, Facebook and Google.

DAILY ROOMS AVAILABLE

One can use end-of-month Airbnb data (which actually come from Airdna) to estimate the daily number of rooms available in Virginia Beach via Airbnb. In December 2016, for example, there were 464 properties listed for rent on Airbnb. This translates to an estimated $464 * 31 \text{ days} = 14,384$ Airbnb room nights available during the entire month of December 2016. **However, if**

⁶ Airdna and CBRE data quoted in Jason Clampet, “Airbnb’s Real Threat to U.S. Hotels Using Industry Metrics,” *Skift* (Feb. 13, 2016), <https://skift.com/2016/02/03/measuring-airbnbs-real-threat-to-u-s-hotels-using-industry-metrics>.

the typical listing really involved 1.8 rooms, then there were $14,384 * 1.8 = 25,891$ room nights potentially available through Airbnb in Virginia Beach in December 2016. This was approximately 4 percent of rooms available in the overall lodging market in Virginia Beach.⁷

One can quibble about the precise number of rooms actually available via Airbnb in Virginia Beach and one should remember that Airbnb is not the only such rental firm in operation. Even so, it is clear that Airbnb has grown steadily since 2014 and, while still relatively small, is becoming an increasingly important part of the lodging market in Virginia Beach. Interestingly, a 2015 analysis of Airbnb growth rates ranked neighboring Norfolk No. 2 in the United States in terms of its year-over-year growth rate in Airbnb listings as of third quarter 2015.

OCCUPANCY RATES

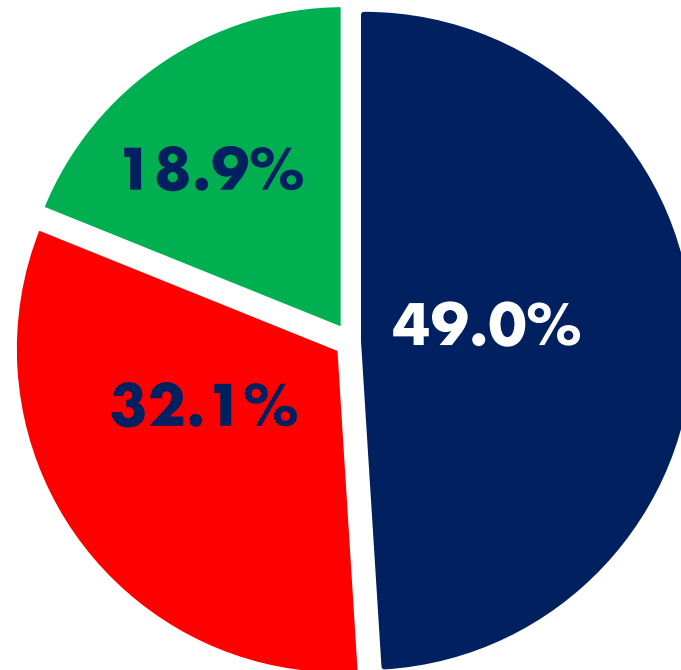
Occupancy data for traditional hotels, available from Smith Travel Research (STR), are not strictly comparable to the data supplied by Airdna for Airbnb because of the “listings not equal to rooms” situation previously noted.

Between February 2015 and December 2016, however, Airbnb’s occupancy rates per listing were below those of the traditional lodging sector every single month. On average, the traditional lodging sector recorded an occupancy rate of 61.7 percent for 2016 – significantly higher than Airbnb’s 43.7 percent (see Graph 2). Occupancy rates for both segments of the market are highly seasonal and predictably increase after New Year’s Day until peaking in the summer months. As the summer tourist season winds down, occupancy rates of both segments decline. In this regard, there is little difference in Airbnb’s behavior and that of the traditional sector: the simple correlation coefficient between the occupancy rates of the two is 0.93.

⁷ Compare this to an approximate 1.8 percent market share for Airbnb in New York, San Francisco and Los Angeles in September 2015, according to Airdna and CBRE (as cited in Jason Clampet, footnote 3).

GRAPH 1

AIRBNB REVENUE SOURCES: UNITED STATES, 2016

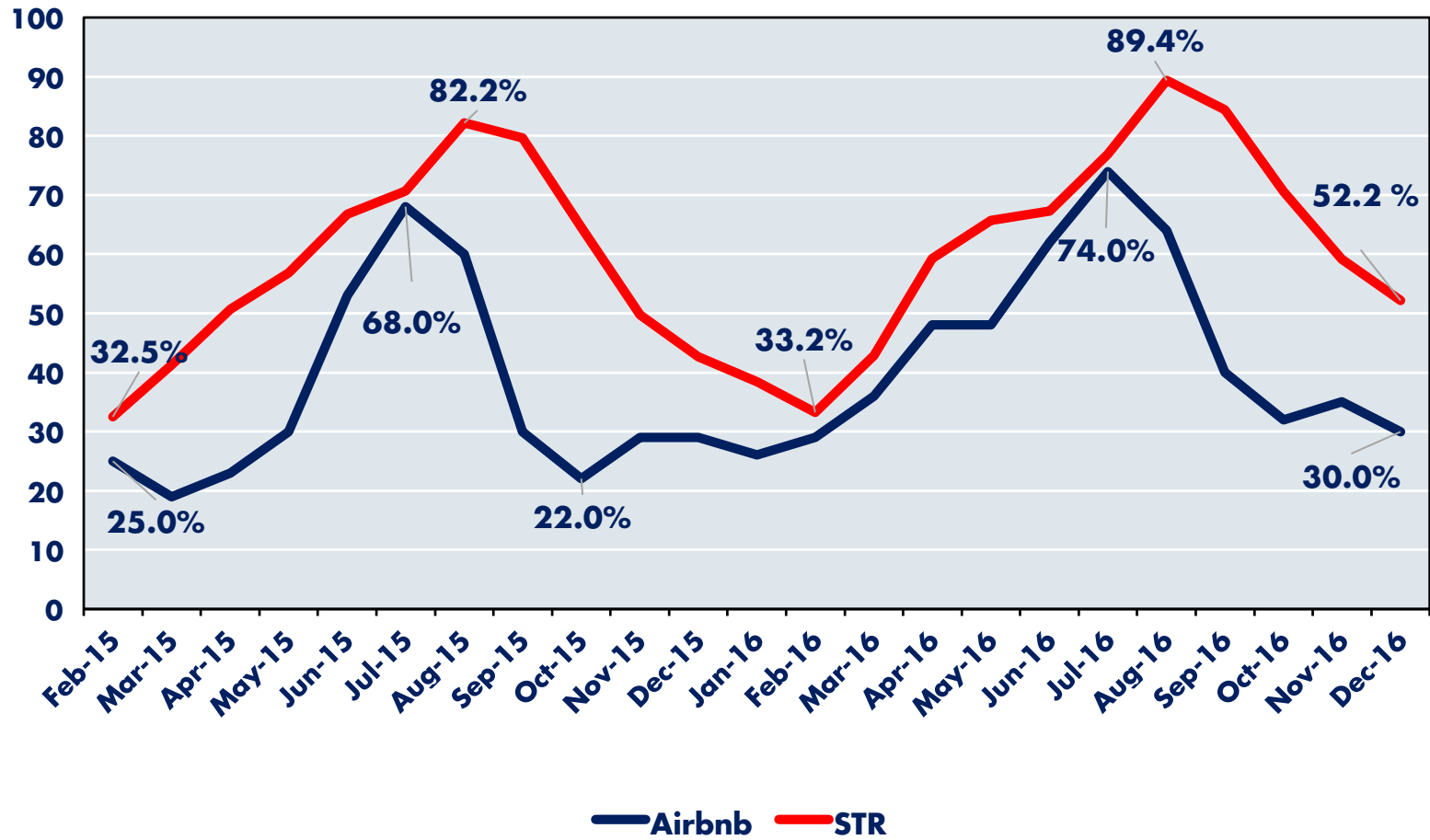


■ **One Entire Property** ■ **Two or More Properties** ■ **Others (Rooms)**

Source: Chris Kirkham and Greg Bensinger, "Hotel Group Assails Airbnb Model," The Wall Street Journal, 269 (March 20, 2017), B4

GRAPH 2

OCCUPANCY RATES FOR TRADITIONAL AND AIRBNB LODGING FOR VIRGINIA BEACH



Sources: Airdna market report and Smith Travel Research

AVERAGE DAILY RATE (ADR)

Average Daily Rate (ADR) is a standard metric used in the hotel industry because it captures the price guests actually pay as opposed to advertised prices. The Airbnb ADR for a four-plus room rental (around \$533) is nine times that of its ADR for a single private room (around \$60). Unless adjusted for such differences, comparing the ADRs of Airbnb versus the traditional lodging sector is not very useful.

Airbnb's ADR per listing consistently has been higher than that of traditional hotels and motels. However, if we deflate the Airbnb ADR by 1.8, which is our estimate of the ratio of rooms to listings for Airbnb in Virginia Beach, then the two series look rather similar. The dotted line in Graph 3 depicts the adjusted ADR value for Airbnb after we have accounted for the average number of rooms per listing. The prevailing wisdom is that Airbnb's rooms often are superior to typical conventional hotel rooms,⁸ but Airbnb does not appear to be earning more revenue per rented room than the traditional lodging sector. Hence, the hypothesis that Airbnb frequently skims demand for the most expensive rooms in the market may not always hold water.

REVENUE PER AVAILABLE ROOM (REVPAR)

Revenue per Available Room (REVPAR) is an important performance metric for the lodging industry because it incorporates both supply and demand influences. REVPAR gives the average revenue earned per available room, not the average revenue earned per room eventually rented, which is ADR. ADR can be deceptive if many rooms sit unrented.

REVPAR looks virtually the same for Airbnb and the traditional hotels (see Graph 4), but recall again that Airbnb's REVPAR is per listing, not per room. **After we again perform the 1.8 rooms per listing adjustment (the dotted line in Graph 4), it is immediately apparent that Airbnb hosts on average are reaping far less REVPAR than the conventional lodging-sector hotels.**

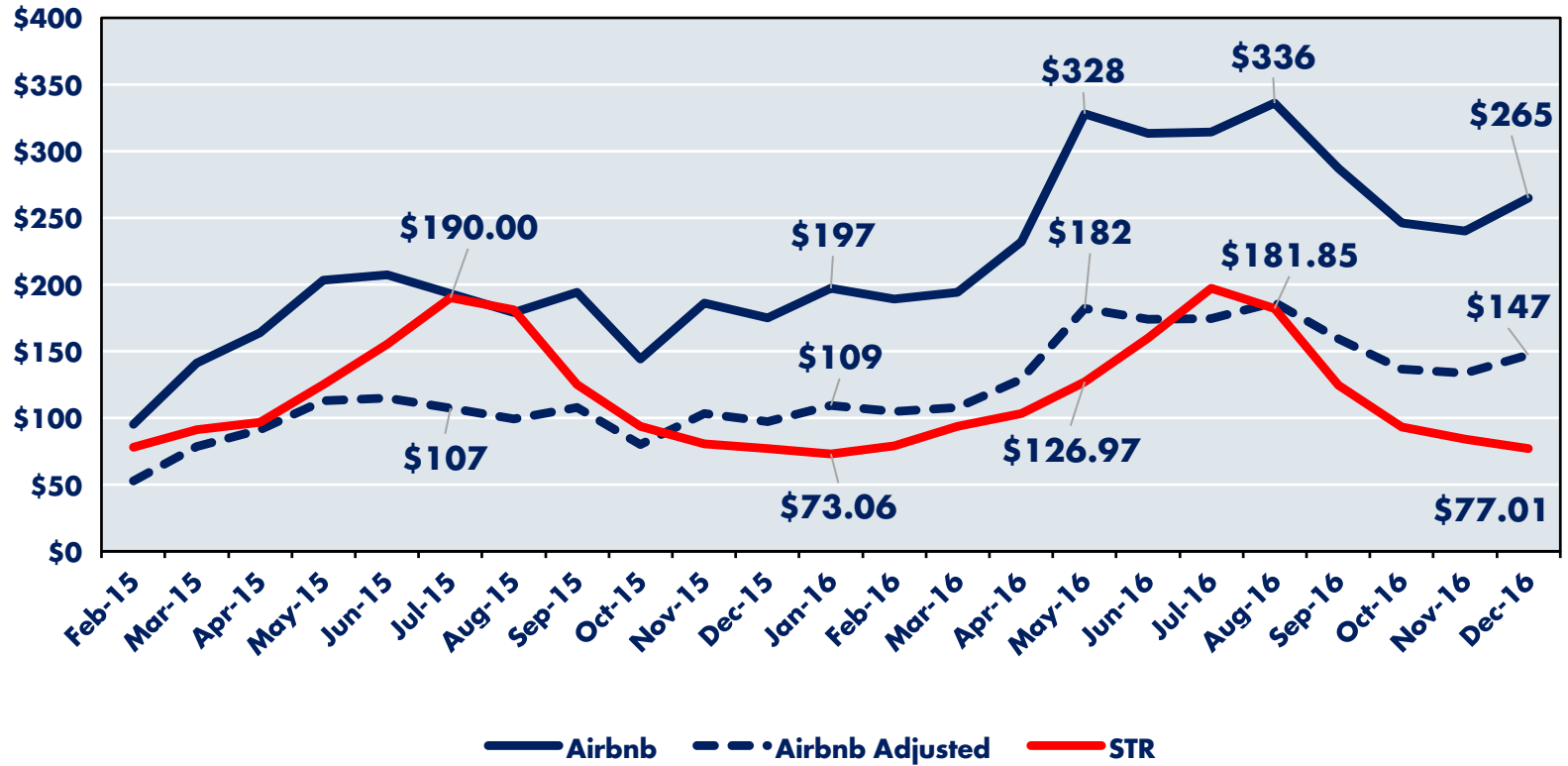
⁸ See among several, Jason Clampet (footnote 6), who assumes that Airbnb rooms typically "have more services and features than a hotel room, including kitchens, additional bedrooms, and parking..."

Does this mean that Airbnb is uneconomic? Far from it. The virtue of being an Airbnb host is that one can decide not to rent any rooms at any time, especially if the rooms are in one's own home. To the extent that Airbnb and similar competitors are merely an add-on activity that earns additional revenue for a family, this is an entirely tenable, even desirable, situation.

The traditional hotel sector does not enjoy the same luxury. Either hotels fill their rooms, or they suffer financially. At the limit, they go broke. The same might be said of Airbnb investors in multiple-room homes, some of which almost approach the size of small apartment houses. Such investors appear to be a more important part of the Airbnb world than Airbnb officials tend to admit. Nevertheless, the predominant Airbnb host remains someone who usually is not aggrieved if he/she does not rent a room on a specific day. Therefore, one would expect the average Airbnb host to earn lower REVPAR because the host is only a part-time supplier of rooms (perhaps during tourist season) and simply may not care too much when those rooms are not rented.

GRAPH 3

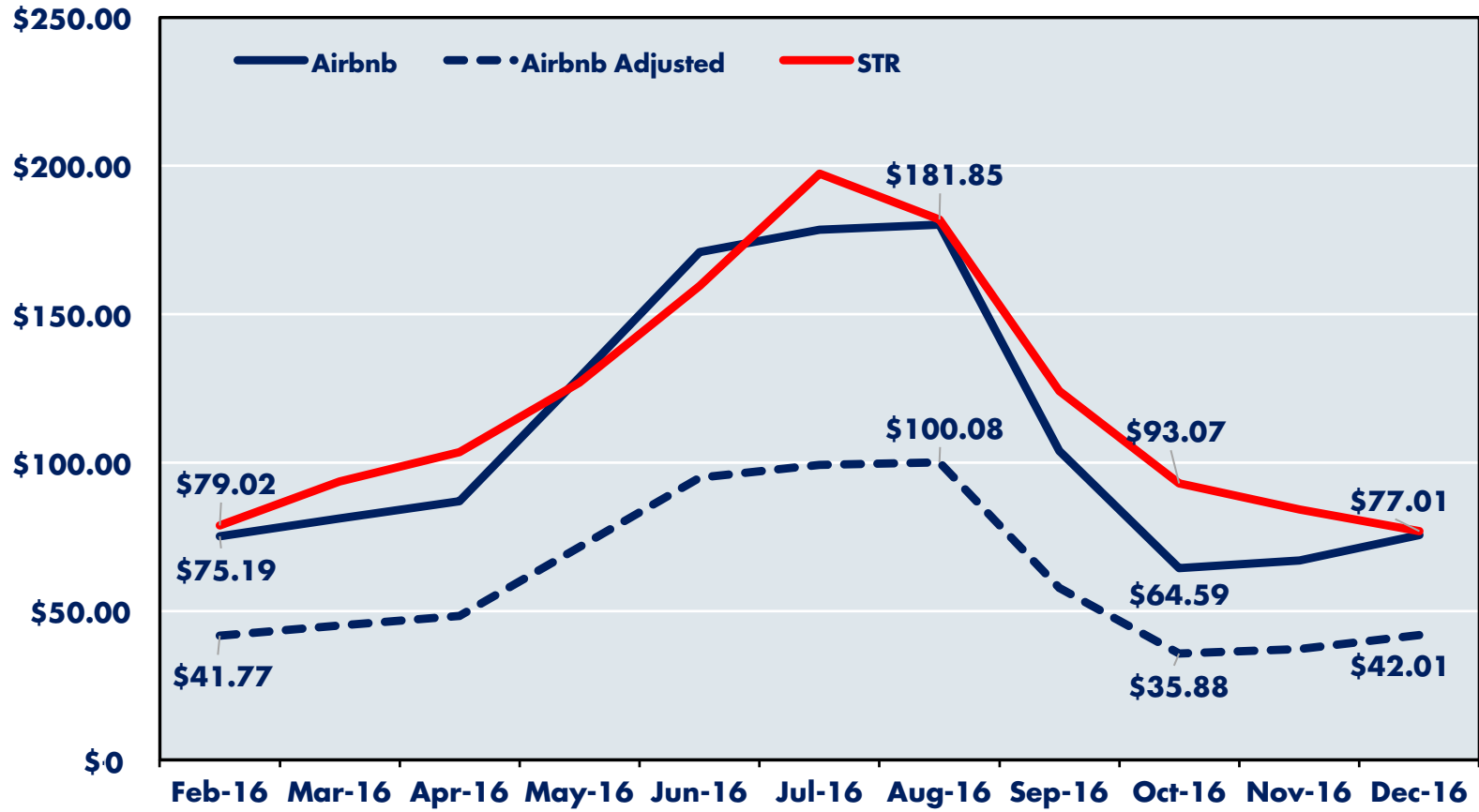
AVERAGE DAILY RATE PER AIRBNB LISTING AND STR TRADITIONAL LODGING SECTOR ROOMS: VIRGINIA BEACH, 2015-2016



Sources: Airdna market report and Smith Travel Research

GRAPH 4

REVPAR PER LISTING OR ROOM: VIRGINIA BEACH, 2016



Sources: Airdna market report and Smith Travel Research

COMPARING VIRGINIA BEACH TO OTHER MARKETS

How does Virginia Beach compare to other markets? We have selected 11 similar cities in the South and other mature Airbnb markets in the United States for comparison. In all these cities, Airbnb listings grew rapidly from 2011 through 2016 (see Table 1). While some of the rapid growth can be attributed to the initially small number of the overall listings, even those markets with relatively large Airbnb listing pools saw double- and triple-digit growth over this period. Compared to other markets of similar size, the Airbnb market segment in Virginia Beach grew the fastest from 2015 to 2016.

Virginia Beach is also markedly different with regard to the distribution of rentals. Using active listing data from March 2017, we can see in Table 2 that over one-quarter of listings in Virginia Beach were for four-plus bedroom listings, 10 percentage points higher than the next city, Nashville. This may

reflect what one local termed “The Sandbridge Effect,” whereby many large, four-plus bedroom buildings exist in Sandbridge and elsewhere along the oceanfront that are rented to large groups for weekends or entire weeks. Parenthetically, these also tend to be the Airbnb properties that generate the most complaints concerning unruly behavior, illegal parking, trash and the like.

With respect to occupancy, the seasonality of Airbnb occupancy in Virginia Beach is the predominant factor to consider. Data in Table 3 reveal that Airbnb occupancy in the first quarter of 2016 in Virginia Beach was the lowest among all but one of the selected cities. Occupancy rates increased across all but one of the sample cities in the second quarter and in half of the cities in the third quarter. While occupancy declined for all but one of the cities in the fourth quarter of 2016, the declines were steepest in Virginia Beach. This suggests a rather obvious conclusion: Airbnb in Virginia Beach (compared to a city such as Arlington) is tied closely to the ebb and flow of the tourism market.

TABLE 1

CURRENTLY ACTIVE AIRBNB LISTINGS: SELECTED CITIES, 2011-2016

	2011	2012	2013	2014	2015	2016	Growth 2015-2016
Arlington	30	53	94	178	448	982	119.20%
Charleston	10	28	74	156	395	906	129.37%
Jacksonville	4	8	18	45	132	311	135.61%
Lynchburg	5	14	74	172	132.43%
Nashville	18	50	147	525	1,600	3,400	112.50%
New Orleans	65	200	545	1,100	2,400	4,600	91.67%
Norfolk	2	6	8	14	63	153	142.86%
Portland	82	226	527	1,100	2,200	3,800	72.73%
Richmond	4	9	25	71	459	642	39.87%
Roanoke	..	1	3	9	38	90	136.84%
Savannah	17	35	106	166	283	619	118.73%
Virginia Beach	1	9	20	47	156	392	151.28%

Source: Airdna market reports

TABLE 2

DISTRIBUTION OF ACTIVE AIRBNB LISTINGS: SELECTED CITIES, MARCH 2017

	Studio	1 Bedroom	2 Bedroom	3 Bedroom	4+ Bedroom
Arlington	6.45%	45.66%	32.37%	9.83%	5.68%
Charleston	4.26%	28.61%	32.60%	23.52%	11.00%
Jacksonville	4.38%	32.50%	34.38%	19.38%	9.38%
Lynchburg	11.84%	28.95%	31.58%	15.79%	11.84%
Nashville	4.50%	22.44%	31.48%	25.80%	15.79%
New Orleans	6.51%	37.22%	34.57%	14.04%	7.66%
Norfolk	5.75%	25.29%	43.68%	14.94%	10.34%
Portland	15.42%	41.59%	27.66%	9.86%	5.48%
Richmond	6.19%	37.61%	28.76%	19.47%	7.96%
Roanoke	8.16%	34.69%	24.49%	24.49%	8.16%
Savannah	4.43%	35.82%	34.75%	15.60%	9.40%
Virginia Beach	6.86%	23.53%	27.45%	16.18%	25.98%

Source: Airdna market reports

While Airbnb rentals in Virginia Beach may have lower REVPAR in 2015 than comparable tourist destinations such as Charleston and New Orleans, the growth in Virginia Beach’s Airbnb REVPAR was higher than most of the surveyed cities (Table 4). Comparing similar months in 2015 and 2016, Virginia Beach’s Airbnb REVPAR grew almost 64 percent from May 2015 to May 2016 and about 50 percent from October 2015 to October 2016. The May 2015 to May 2016 increase for Virginia Beach was only behind that of Lynchburg, an Airbnb market that is one-quarter the size of Virginia Beach. Comparing October 2015 to October 2016, Virginia Beach’s Airbnb REVPAR was only behind Norfolk.

Turning next to Airbnb revenues, we examine total earnings of Airbnb hosts from various rentals in 2016. **Virginia Beach stands out from the other cities in this regard because it has the highest percentage of revenue earned through listings for four bedrooms or more (see Table 5).** Virginia Beach’s share of revenue from four bedrooms or more rentals (36.6 percent of revenue earned) eclipsed that of New Orleans (36.2 percent), Savannah (34.1 percent) and Charleston (30.2 percent).

If tax revenue collections are a major concern for the city of Virginia Beach, then the data in Table 6 strongly suggest that the city’s focus should be upon the multiple-bedroom Airbnb properties. Almost three-quarters of all revenue earned by Airbnb hosts in Virginia Beach is derived from multiple-bedroom properties.

TABLE 3

AVERAGE AIRBNB OCCUPANCY RATES: SELECTED CITIES, 2016

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
Arlington	57.67%	70.67%	66.33%	57.67%
Charleston	43.33%	63.67%	55.00%	44.67%
Jacksonville	64.00%	61.33%	58.33%	58.00%
Lynchburg	30.67%	39.00%	45.00%	44.33%
Nashville	44.00%	59.33%	55.67%	46.67%
New Orleans	47.33%	52.67%	38.00%	43.00%
Norfolk	34.00%	49.33%	53.33%	42.67%
Portland	56.00%	74.00%	84.67%	60.33%
Richmond	38.33%	51.00%	55.33%	51.67%
Roanoke	32.00%	53.67%	58.67%	47.67%
Savannah	48.33%	56.33%	51.67%	44.00%
Virginia Beach	30.33%	52.67%	59.33%	32.33%
Source: Airdna market reports				

Table 6 provides additional detail based upon our estimates of Airbnb activity in Virginia Beach between September 2014 and February 2017. We estimate that 79.9 percent of the lodging taxes for which Airbnb hosts are liable in Virginia Beach would be paid by hosts who rent full houses, apartments or condos. The same is true for the Commonwealth’s sales tax collections. The percentage paid by full houses, apartments or condos for the city’s occupancy tax is smaller, 55.9 percent, but it is far less lucrative to the city than the lodging tax.

TABLE 4

NOMINAL AIRBNB REVPAR PER LISTING: SELECTED CITIES, 2015 AND 2016

	May-15	Oct-15	May-16	Oct-16	Growth May-May	Growth Oct-Oct
Arlington	\$ 83.43	\$ 77.00	\$ 99.82	\$ 86.86	19.65%	12.80%
Charleston	\$ 97.71	\$ 92.29	\$ 134.11	\$ 111.86	37.24%	21.21%
Jacksonville	\$ 42.86	\$ 51.29	\$ 54.11	\$ 47.00	26.25%	-8.36%
Nashville	\$ 81.43	\$ 100.43	\$ 128.93	\$ 133.14	58.33%	32.57%
New Orleans	\$ 95.14	\$ 90.71	\$ 106.79	\$ 86.57	12.24%	-4.57%
Norfolk	\$ 58.29	\$ 35.86	\$ 69.82	\$ 54.57	19.79%	52.19%
Portland	\$ 70.71	\$ 79.14	\$ 84.11	\$ 77.43	18.94%	-2.17%
Richmond	\$ 54.14	\$ 52.71	\$ 67.32	\$ 70.00	24.34%	32.79%
Roanoke	\$ 56.86	\$ 50.57	\$ 48.75	\$ 54.14	-14.26%	7.06%
Savannah	\$ 81.57	\$ 74.57	\$ 114.11	\$ 111.00	39.89%	48.85%
Lynchburg	\$ 38.00	\$ 37.00	\$ 63.93	\$ 50.14	68.23%	35.52%
Virginia Beach	\$ 59.71	\$ 39.14	\$ 97.68	\$ 58.86	63.58%	50.36%

Source: Airdna market reports

TABLE 5

DISTRIBUTION OF AIRBNB EARNINGS BY RENTAL TYPE: SELECTED CITIES, 2016

	Shared Revenue	Private Revenue	Studio Revenue	1-Bedroom Revenue	2-Bedrooms Revenue	3-Bedrooms Revenue	4-Bedrooms Revenue
Arlington	3.06%	8.79%	9.78%	15.60%	19.90%	17.08%	25.80%
Charleston	1.09%	7.50%	10.93%	15.48%	16.37%	18.40%	30.22%
Jacksonville	2.41%	9.84%	12.11%	14.77%	17.23%	17.90%	25.73%
Lynchburg	0.00%	10.76%	12.57%	15.98%	20.45%	11.93%	28.30%
Nashville	2.60%	6.74%	11.90%	13.16%	14.17%	20.78%	30.66%
New Orleans	3.05%	6.31%	10.29%	11.18%	14.82%	18.14%	36.22%
Norfolk	0.56%	11.28%	11.62%	16.17%	20.96%	18.78%	20.62%
Portland	3.78%	7.23%	12.28%	12.65%	16.04%	21.03%	26.98%
Richmond	2.85%	6.95%	9.05%	14.49%	14.77%	19.49%	32.39%
Roanoke	0.00%	10.35%	15.09%	14.71%	17.80%	19.74%	22.30%
Savannah	1.76%	9.37%	11.42%	11.96%	15.72%	15.67%	34.11%
Virginia Beach	1.04%	9.66%	2.26%	12.12%	17.65%	20.67%	36.59%

Source: Airdna market reports

TABLE 6

ESTIMATED AIRBNB ACTIVITY IN VIRGINIA BEACH, SEPTEMBER 2014-FEBRUARY 2017

Dates	Estimated Virginia Beach Airbnb Revenues	Estimated Number of Nights	Estimated Revenue Per Night	Estimated Associated Lodging Taxes	Estimated Associated Occupancy Taxes	Estimated Associated Virginia Sales Tax Collections
Full House/Apt/Condo						
Sept. 2014 to Dec. 2014	\$65,834	528	\$124.68	\$5,267	\$528	\$3,950
Jan. 2015 to Dec. 2015	\$771,011	4,556	\$169.23	\$61,681	\$4,556	\$46,261
Jan. 2016 to Dec. 2016	\$4,831,689	18,840	\$256.46	\$386,535	\$18,840	\$289,901
Jan. 2017 to Feb. 2017	\$644,233	1,976	\$326.03	\$51,539	\$3,952	\$38,654
Totals	\$6,312,767	25,900	\$243.74	\$505,021	\$27,876	\$378,766
Private Rooms						
Sept. 2014 to Dec. 2014	\$19,041	224	\$85.01	\$1,523	\$224	\$1,142
Jan. 2015 to Dec. 2015	\$327,159	3,835	\$85.31	\$26,173	\$3,835	\$19,630
Jan. 2016 to Dec. 2016	\$1,143,958	14,637	\$78.16	\$91,517	\$14,637	\$68,637
Jan. 2017 to Feb. 2017	\$86,462	1,419	\$60.93	\$6,917	\$2,838	\$5,188
Totals	\$1,576,621	20,115	\$78.38	\$126,130	\$21,534	\$94,597
Shared Rooms						
Sept. 2014 to Dec. 2014	\$0	0	\$0	\$0	\$0	\$0
Jan. 2015 to Dec. 2015	\$1,240	34	\$36.47	\$99	\$34	\$74
Jan. 2016 to Dec. 2016	\$12,990	364	\$35.69	\$1,039	\$364	\$779
Jan. 2017 to Feb. 2017	\$974	32	\$30.42	\$78	\$64	\$58
Totals	\$15,203	430	\$35.36	\$1,216	\$462	\$912
Grand Totals	\$7,904,590	\$46,445	\$357	\$632,367	\$49,872	\$474,275
Assumptions: lodging tax 8%, occupancy tax = \$1 until December 2016, occupancy tax = \$2 thereafter, state sales tax = 6%						
Source: Airdna market reports						

The moral to the story told by the data in Tables 5 and 6 is that if the city were to devote many resources to forcing compliance from hosts renting studio rooms or single bedrooms, it seems likely that the costs of doing so would exceed the incremental revenues received. This is not where the revenue is. The hundreds of small Airbnb hosts who come and go from the market are difficult to track and would present significant challenges to enforcement personnel. **Further, we predict that specialized Airbnb imitators will rise in importance as they address the specific circumstances of populations ranging from gay people and Catholics to women and military veterans. The point is that the more of these hosting organizations there are, the more difficult it will be for the city of Virginia Beach to enforce any ordinances that putatively apply to such operations.**

There is another fundamental conclusion to be drawn from our analysis. Given the sometimes, almost casual nature of the Airbnb phenomenon, it is not an easy task for the city of Virginia Beach to collect taxes due from Airbnb hosts. **Any tax based upon revenues or sales will be challenged by problems connected to tracking and identifying both Airbnb hosts and their activities. This dictum applies both to the city's lodging and occupancy taxes and to the Commonwealth's sales tax.**

Identification and collection problems may diminish, however, if it is income rather than sales that is subject to taxation.

Airbnb and related hosts may believe they can thumb their noses at the city of Virginia Beach, but they are less likely to hold that attitude with respect to the federal government's Internal Revenue Service, which possesses a variety of digitized tools to identify scofflaws and some impressive penalties to inspire cooperation.

Perish the thought: a city income tax, perhaps piggybacked on the state or federal income taxes, may be the wave of the future for Virginia Beach – if it is serious about collecting taxes due from Airbnb hosts and the multitude of other gig-economy entrepreneurs who increasingly will inhabit the city's

economic environment. We make this observation not because we are advocates of income taxes, but rather as dispassionate observers of economic trends. Sales-related taxes may become increasingly difficult to collect.

IS THERE A CONNECTION BETWEEN ADR, REVPAR AND THE GROWTH OF AIRBNB IN VIRGINIA BEACH?

Costs and prices make a difference, or so at least academic economists tell their students. With this in mind, **it should not escape readers that Airbnb has grown more rapidly in Virginia Beach than in any of our 11 comparison cities and that this meteoric growth occurred when the price of a typical hotel room (measured by either ADR or REVPAR) was rising much more rapidly in Virginia Beach than either in Hampton Roads or Virginia. REVPAR in Virginia Beach, for example, rose 34.6 percent between 2011 and 2016, but only 25.6 percent in Virginia.**

Supply-side adjustments contributed to this. The absolute number of hotel rooms available in Hampton Roads declined almost 2,500 between 2009 and 2016, falling a little bit more than 300 rooms in Virginia Beach itself.

While a more rigorous analysis would be required to render a definitive judgment, *prima facie* it appears that the pricing behavior of Virginia Beach hotels is partially responsible for the rapid growth of Airbnb in the city. Alert consumers look for opportunities to substitute less-expensive goods for those that are more expensive, and rental rooms are no exception. Rising hotel room prices stimulate tourists and business travelers to contemplate alternatives, including Airbnb, which may result in hotels losing market share to competitors such as Airbnb.

Unless truly revolutionary action is taken by the Virginia Beach City Council, it is safe to say that Airbnb and similar rental contractors are not going to disappear. Nevertheless, traditional hotels in Virginia Beach have three major avenues

open to enable them to become more competitive with respect to Airbnb and similar hosts. First, they can be more modest in terms of future price increases and perhaps even adjust their current prices by means of special sales or offerings. Second, they can make their properties and offerings more enticing, such that accommodations at their properties are more personal, engaging and memorable (qualities many Airbnb customers say attract them to Airbnb accommodations). Third, the city can make the oceanfront more attractive by addressing issues such as traffic control, parking availability and cost, and perceived safety. If such developments do not occur, then simple, but straightforward economic analysis suggests that Airbnb's growth in Virginia Beach will continue apace.

Policy Alternatives

It is not blindingly obvious where the public interest resides in the debates concerning the activities of Airbnb and similar firms in Virginia Beach because there are competing points of view, each of which is supported by some favorable evidence. A rough definition of the public interest is that it coincides with activities that do the most good for the most people.

Nonetheless, if we adopt the "most good for the most people" view, then we can observe that it is not the job of government to protect existing firms and industries from new, more efficient or more attractive competitors that would serve consumers better and do so at lower prices. If it were, then horse-and-buggy manufacturers and producers of 8-track and cassette tapes still would be dominant because both would have been protected from new competition.

Enabling citizen consumers to spend their dollars where they wish is a welfare-maximizing stance for government to adopt, provided this consumption does not generate undesirable side effects such as pollution, noise, traffic congestion, crime, unsanitary conditions that impact public health, and the like.

As a general rule, challenging competing firms to meet "the market test" – that is, offer goods and services at prices and levels of quality that are attractive to consumers and do not generate the side effects just noted – not only is an equitable approach that treats all citizens and firms the same, but also generates the best overall results for the citizenry. "Best overall" here means presenting consumers with a larger selection of goods and services at lower prices.

An important question relating to Airbnb in Virginia Beach is whether all parties are being treated the same – literally, whether all participants (Airbnb and traditional hotels alike) have had to meet the same market test under the same rules. We believe the answer is no and that some Airbnb hosts have consciously evaded (and been able to avoid) city regulations and taxes.

This said, it is not clear to us that it would be wise for Virginia Beach to devote substantial resources to ensuring that every Airbnb-type host complies with all of the city's ordinances. By our calculations, Airbnb hosts who rent single or shared single rooms accounted for no more than about 1 percent of the total number of rooms available in Virginia Beach during the past year. Further, they account for only about one-fifth of the city's potential tax revenues from Airbnb-like activities. And, these hosts do not often appear to be the sources of behavioral problems (noise, trash, crime, etc.).

The city of Virginia Beach would be wise to devote its scarce enforcement resources to identifying and obtaining compliance from Airbnb hosts who rent a full house, apartment or condominium. Plainly speaking, this is where the revenue is and evidence suggests that any behavioral problems that Airbnb generates are concentrated among these properties as well. This is not the same as saying that the city should ignore ordinances that apply to the Airbnb small fry. Instead, it is a rational economic calculation that expending resources on such does not make much sense, just as members of

the city's police force do not issue citations to every motorist who is traveling 32 MPH in a 30 MPH zone.

At the limit, Virginia Beach might consider amending its ordinances so that they apply only partially, or not at all in some cases, to property owners who rent nothing more than single rooms. These Airbnb hosts have relatively little impact on traditional hotels or city revenues.

The city usefully could imitate San Francisco in terms of its relationship with Airbnb. San Francisco negotiated an agreement with Airbnb that, among other things, uses the Airbnb administrative structure to collect taxes due from Airbnb hosts. If Virginia Beach is able to replicate this, then the revenues it receives from small Airbnb-like hosts plausibly could exceed the costs required to collect them.

In any case, compliance with certain ordinances always presents challenges to cities. **If Virginia Beach is serious about its ordinances that relate to larger Airbnb-like hosts, then it must consider issuing citations to and prosecuting exemplary large Airbnb hosts who clearly have been flouting its ordinances. It should not be difficult to identify the most egregious violators. This would send a message to Airbnb hosts concerning their collective and individual obligations to obey the law, pay requisite taxes and monitor their properties.**

Finally, to return to a theme developed above, traditional hotel operators would be well advised to re-evaluate their pricing and quality strategies. Airbnb and similar rental hosting firms are not going to go away. In contrast to Uber, which is losing several billion dollars per year and has yet to demonstrate a viable business model, Airbnb is a profitable enterprise that already in August 2016 was valued at \$30 billion when it raised \$850 million in a private offering.⁹ To place this in perspective, this is about 25 percent higher than the value of the entire Hilton Hotel chain.

⁹ Matt Rosoff, "Airbnb Is Now Worth \$30 Billion," *Business Insider* (Aug. 6, 2016), www.businessinsider.com.

The notion that the meteoric growth of Airbnb and similar hosts could be choked off by punitive law enforcement is naive. Nor would this be a good idea. Airbnb and similar rental hosting firms appear to be meeting the market test, and traditional hotels need to ensure that they do so as well.

The Implications Of The Gig Economy For Virginia Beach

It would be short-sighted for anyone to view the Airbnb phenomenon as an isolated development. Instead, Airbnb is one part of a much larger socioeconomic trend that some have chosen to term the “gig economy.” In the gig world, employees are not permanent; rather, they are temporary contractors who accomplish a task and then move on to something else (or nothing at all) with another employer, or even the same employer, but for a different, delimited task.

More gig activity has occurred in 2017 than in years previous, and more occupations and tasks are being filled or satisfied by gig workers than ever before. Intuit, the software company that produces products such as Quicken and TurboTax, predicts that 40 percent of all workers will be gig employees by 2020.¹⁰ Graph 5 illustrates the dramatic growth in contract and temporary employees in the U.S. economy.

These are among the major implications for the city of Virginia Beach.

- The city will be dealing with many more workers (including Airbnb hosts) who don't fit traditional categories, are not accustomed to applying for things such as business licenses, may or may not be willing to pay established taxes (or even be aware they exist), can be difficult to track down, and who actually may be located thousands of miles away from Virginia Beach.
- The city itself, seeking to economize and do the best for its citizen taxpayers, likely will choose to hire more temporary workers. Does the city wish to place limits on its employment of contractual workers even if this turns out to cost more money?
- The city must decide what levels of fringe benefits (if any) it will provide contractual employees, particularly when their employment period is lengthy, or when the individual is employed repetitively. That is, how long or often

must someone be employed in order for the city's obligations to such employees change?

- The city will find that the gig economy workers who actually reside in Virginia Beach (though perhaps only for a period of time) will place larger demands upon the city's schools and social services, and perhaps on other agencies such as law enforcement and the judicial system. For better or worse, permanence of residence and permanence of employment are significant predictors of positive social behavior.
- Virginia Beach K-12 schools will find that increasing proportions of their students will come and go because their parents or guardians literally are footloose, or their financial circumstances have changed.
- The city may conclude that many conventional measures of achievement, such as college degrees, do not fit the gig world as well as certificates and certifications. Thus, being certified as a project manager, court reporter, EMT, internet network specialist, massage therapist or licensed nurse often is more important than having earned a baccalaureate degree.
- If we put aside seasonable agricultural work, then the gig economy currently is proportionately overrepresented with Caucasians, many of whom are well educated and even wealthy. To the extent that the city employs gig economy workers, it may find that these workers are not representative either of Virginia demographics or the population of Virginia Beach. The city must be proactive if it wishes a different outcome. Further, reputable recent evidence suggests that many Airbnb hosts engage in racial discrimination based upon the names of prospective renters.¹¹ Virginia Beach should be alert to the possibility that conventional means of enforcing nondiscrimination ordinances in housing and accommodations, as well as policies monitoring its short-term rental market and overall revenue sources, may have been rendered less effective by gig economy developments.

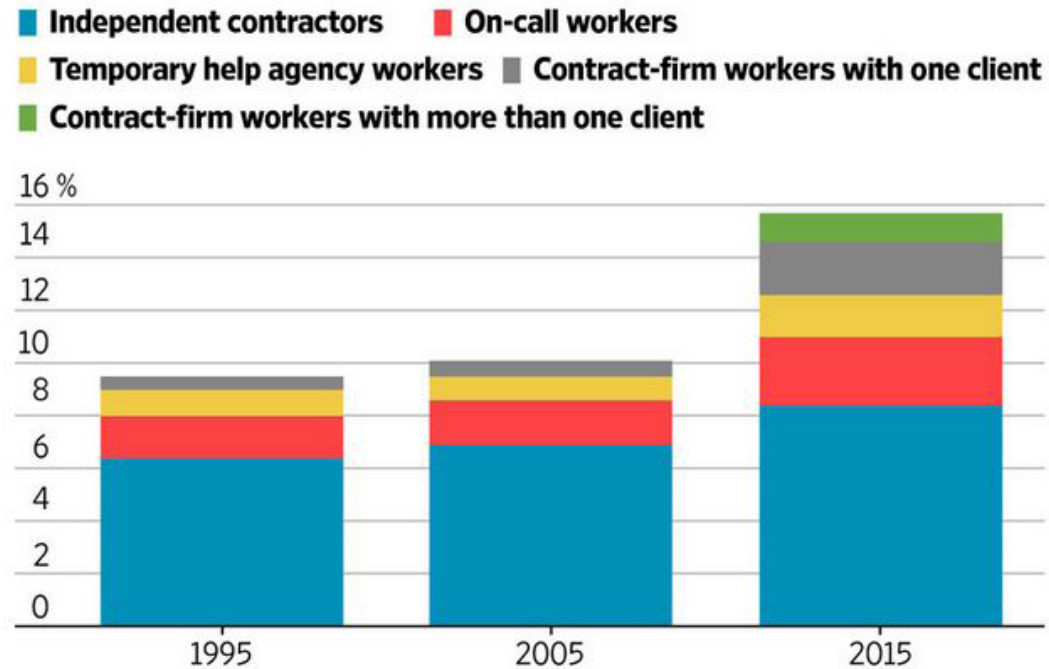
¹⁰ Intuit 2020 Report. *Ten Trends That Will Shape the Next Decade*. https://http-download.intuit.com/http.intuit/CMO/intuit/futureofsmallbusiness/intuit_2020_report.pdf.

¹¹ Benjamin Edelman, Michael Luca and Dan Svirsky, “Racial Discrimination in the Sharing Economy: Evidence from a Field Experiment,” *American Journal of Applied Economics*, 9 (April 2017), 1-22.

GRAPH 5

THE INCREASING NUMBER OF PART-TIME AND GIG EMPLOYEES IN THE UNITED STATES

Estimates suggest a sharp increase in the percentage of the U.S. workforce that isn't employed directly by the company where they work.



Note: A janitor who is employed by a contract firm and cleans five unrelated offices a week is counted as working for more than one client. Data for 1995 and 2005 don't include exact comparisons for that group.

Source: Lawrence Katz (Harvard University) and Alan Krueger (Princeton University)

Source: The Wall Street Journal, 269 (Feb. 3, 2017), A10

