REPORT | MAY 8, 2017

Short-term rentals , hotels, and growing the hospitality pie

1. Executive summary

The rise in popularity of home sharing platforms like Airbnb, VRBO and others has opened the door to important questions around the impact of short-term rentals on the traditional hospitality industry. Unfortunately, groups representing the hotel industry have continued to issue misleading reports about the impact of short-term rentals on the traditional hospitality industry. As a result, we decided it was a valuable exercise to do our own research to evaluate the health of the hotel industry in specific U.S. cities. Currently, Los Angeles is considering short-term rental rules and so we decided to perform our first analysis here.

Our analysis of the health of the hotel industry in Los Angeles shows it continues to experience strong, sustained growth despite the rise in home sharing.

By virtually every measurable metric, the hospitality industry in Los Angeles exceeded expectations in 2016.

In fact, Los Angeles County's average hotel occupancy rate surpassed 80% for the first time in County history. A record 29.2 million hotel room nights were sold countywide, with average daily rates (ADR) reaching a new high of $171.95. This type of record-breaking success resulted in Travel Weekly declaring the Los Angeles hotel market its "Big Winner" in 2016.

Beyond hotel performance, Los Angeles shattered tourism records this past year, welcoming 47.3 million visitors and setting a new record for the sixth consecutive year. As a result, Mayor Garcetti announced his goal of welcoming 50 million tourists to Los Angeles by 2020. To accommodate this influx in travel, hotel developers are pursuing tax incentives and are expected to add 6,000 additional hotel rooms in 2017, including a 900-room InterContinental downtown and a 216-room Kimpton in Hollywood." With 31.1% more hotel rooms under construction in 2017 than in 2016, the industry remains keen on increasing available supply in order to meet the needs of Los Angeles's flourishing travel industry.

Mayor Garcetti said it best when he stated:

> "Not only did 2016's tourism figures exceed expectations, we crushed it.

LA's tourism industry has been lucrative for the hotel industry. Since 2005, roughly $660 million in tax breaks, fee waivers, and loans to hotel developers have been approved to incentivize development. In 2005, for example, the J.W. Marriott development group was able to keep $270 million of the tax revenue generated by their project until 2035. Several similar deals have benefited hotel companies, including a recent $60.8 million in tax incentives for the new Wilshire Grand Hotel.

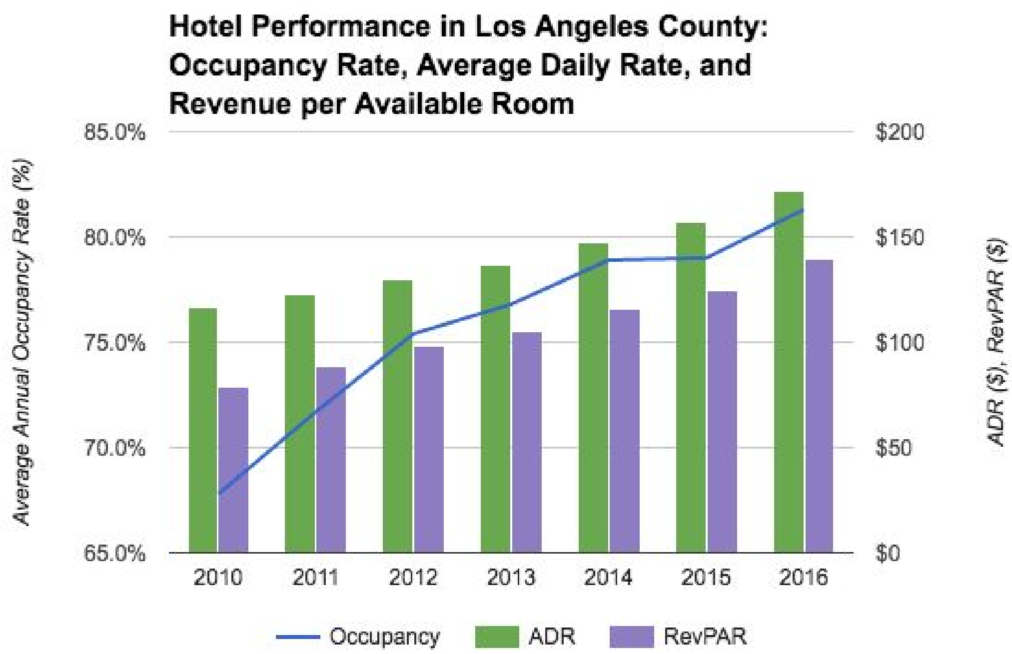
As the hotel industry has seen record performance, home sharing has also continued to thrive. In 2016, more than 1 million guests stayed with Airbnb hosts in Los Angeles. This helped generate over $1.1 billion in economic activity for the City, including over $263 million in host earnings and over $800 million in guest spending. By dispersing guest spending across neighborhoods and households throughout the City, Airbnb helps support local business in many neighborhoods that don't typically see tourism activity. The company also pays its fair share in taxes. From August 2016-December 2016, Airbnb collected and remitted $13 million on behalf of hosts and it is projected that this tax revenue to the City will more than double in 2017.

There is room for both hotels and home sharing in the hospitality industry. In fact, we believe home sharing is actually growing the "hospitality pie." One-third of Airbnb travelers would not have traveled or would not have stayed as long at their destination if not for Airbnb. In Los Angeles, 51% of Airbnb room-nights come from 7+ day stays, vs average stays of ~2 days for hotel travelers. And finally, Airbnb serves "overflow" travelers during times when hotels are booked (e.g. during events) -- travel that physically would not have been able to happen without supply from home sharing platforms like Airbnb.

The billion dollar hotel industry, and everyday Angelenos who earn an average of $7,200 a year sharing their homes on Airbnb, can exist together in today's booming tourism economy. When policymakers see the facts, it becomes clear why hundreds of municipalities around the world have developed fair home sharing rules that benefit hosts and protect and strengthen communities -- and why doing the same in Los Angeles is a win-win for residents and the city.

Hotel Performance Nationally and in Los Angeles

- **Another record year.** For all of 2016, U.S. hotel industry occupancy, ADR and RevPAR all increased over 2015 to the highest absolute values STR has ever benchmarked (Hotel News Now, January 23, 2017).
- **83 consecutive months of growth.** In January 2017, U.S. hotel industry revenue per available room (RevPAR) grew 3.8% to $65.33, the 83rd consecutive month of growth (Hotel News Now, February 21, 2017).
- **LA the big winner.** The Los Angeles hotel market was dubbed the "Big Winner" of 2016 by Travel Weekly. (Travel Weekly, January 25, 2017)
- **Hotel industry ADR record broken in LA County.** Los Angeles County's average hotel occupancy rate reached 81.3% in 2016, surpassing 80% for the first time in County history. A record 29.2 million hotel room nights were sold countywide with the average daily rate (ADR) reaching a new high of $171.95, an 8.6% increase over 2015. (Los Angeles Tourism & Convention Board press release, January 11, 2017; Hotel News Now, January 23, 2017).
- **Double-digit growth.** The Los Angeles/Long Beach market was the only U.S. market to reach double-digit revenue per available room (RevPAR) growth at nearly 11%. The increase in ADR was the largest of any of Smith Travel Research's top 25 markets. (Hotel News Now, January 23, 2017)
- **Record occupancy, room nights sold and ADR in 2016.** Los Angeles County's average hotel occupancy rate reached 81.3% in 2016, surpassing 80% for the first time in County history. A record 29.2 million hotel room nights were sold countywide with ADR reaching a new high of $171.95, an 8.6% increase over 2015. Los Angeles County was the only U.S. market to reach double-digit RevPAR growth at nearly 11% (Los Angeles Tourism & Convention Board press release, January 11, 2017; (Hotel News Now, January 23, 2017).
- **Hotels near LAX among most unavailable, Santa Monica, Venice and Hollywood most expensive.** Hotels near LAX and in the Hollywood/Beverly Hills/Westside L.A., South Bay, Santa Monica/Marina del Rey/Venice and Pasadena/Glendale/Burbank areas were particularly expensive and unavailable, with occupancy rates north of 83% in all of the areas in 2016 and the ADR in Hollywood/Beverly Hills/Westside L.A. and Santa Monica/Marina del Rey/Venice at nearly $300. (Los Angeles Tourism & Convention Board, February 15, 2017).



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Tourism Growth Nationally and in Los Angeles

- **Over 200 million visited by air in 2016, a six percent increase over 2015.** International air traffic to or from the U.S. totaled 220.8 million passengers in 2016, a six percent increase over 2015 (National Travel and Tourism Office, February 16, 2017).

- **Travel expenditures nearly $1 trillion in 2015, generating $148 billion in tax receipts.** Domestic and international travel expenditures in the U.S. totaled $947 billion in 2015. The expenditures generated $148 billion in total tax receipts in 2015, a 4.5% increase over 2014. (U.S. Travel Association, "The Economic Review of Travel in America, 2016 Edition.").

- **$1.47 trillion contribution to GDP in 2015.** The total contribution of travel and tourism to GDP in the U.S. was $1.5 trillion in 2016 and was forecasted to rise 2.3% in 2017. (World Travel & Tourism Council, United States Economic Impact 2017).

- **Record Number of Travelers to Los Angeles.** A record 47.3 million people visited Los Angeles County in 2016, up 3.8% from 2015. The amount surpassed mid-year forecasts and broke visitation records for the sixth consecutive year (Los Angeles Tourism &

[1] Source: Discover Los Angeles and Los Angeles Tourism & Convention Board (spreadsheet)

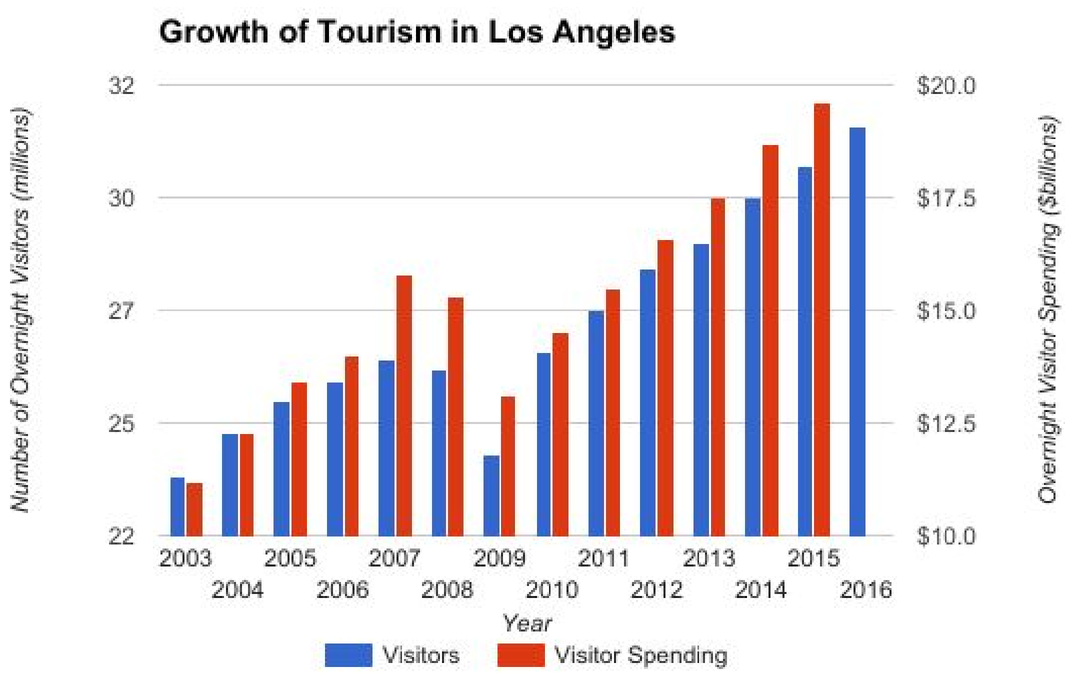
Convention Board, January 11, 2017).

- **Chinese tourists flock to L.A.** Los Angeles became the first U.S. city to attract more than 1 million tourists from China in a single year (Fox 11, January 11, 2017).

- **Booming tourism driving L.A.'s economy.** "Tourism is booming in Los Angeles, and it's helping to drive our whole city's economy forward," said LA Mayor Eric Garcetti. (Los Angeles Tourism & Convention Board, January 11, 2017)

- **Tourism numbers exceeded expectations in L.A.** Not only did 2016's tourism figures exceed expectations, "we crushed it," Garcetti said (Los Angeles Business Journal, January 11, 2017).

- **Goal to welcome 50 million by 2020.** Mayor Garcetti's goal is to welcome 50 million tourists to Los Angeles by 2020 (Los Angeles Tourism & Convention Board, January 11, 2017).



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Hotel Tax Subsidies in LA and Hotel Growth Continue

[2] Source: Discover Los Angeles (spreadsheet)

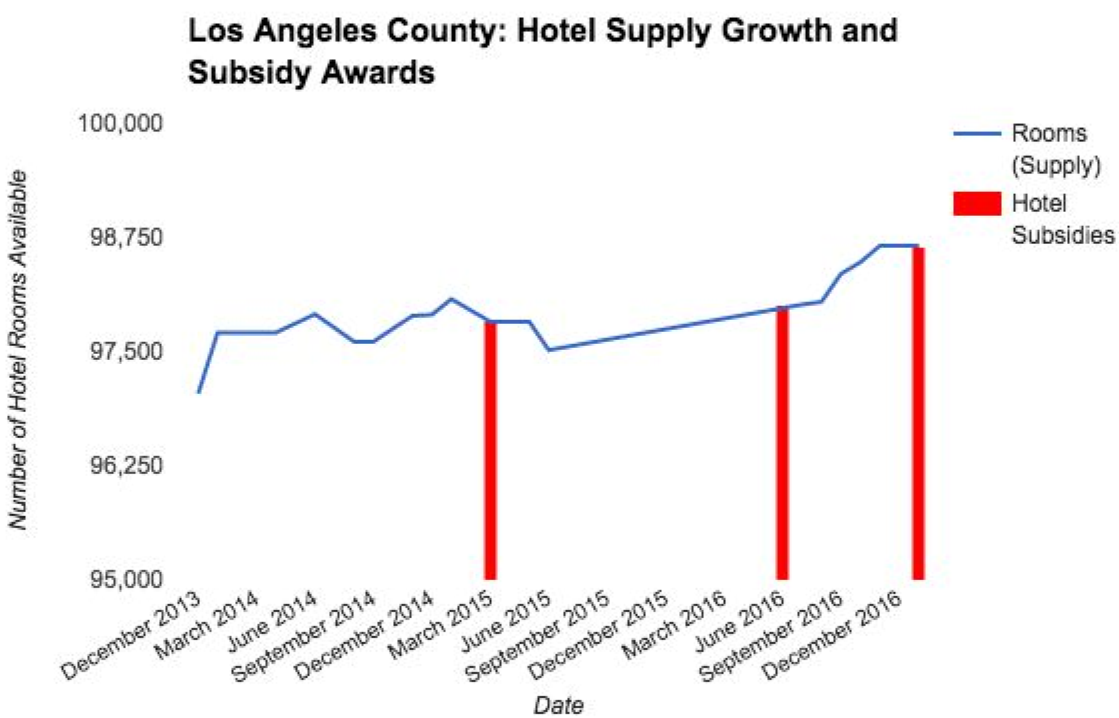
- Between 2005 and 2017, the City of Los Angeles has approved up to $660 million in tax breaks, fee waivers and loans to hotel developers. The City Council's strategy for attracting new hotels has been to offer substantive tax breaks to developers..
- A 2014 Los Angeles Times report detailed four hotel projects that received tax breaks worth half a billion dollars over twenty years.
- The first of the large tax deals in the city's strategy occurred in 2005, when a developer group was allowed to keep $270 million of the tax revenue generated by their J.W. Marriott project until 2035. But when the project opened in 2010, Los Angeles was "cash-strapped" and struggling to pay for city services such as firefighters or police, and the city would end up losing needed revenue due to tax breaks.
- "Despite a sizzling hot real estate market in down Los Angeles," a developer was given a $49 million hotel subsidy to build a luxury hotel on the long-stalled Grand Avenue project. As part of the deal, the developer was allowed to keep half of the sales tax revenue generated by the project over the next 25 years, diverting tens of millions of dollars from the city's general fund that pays for police, street maintenance and other services.

Recent subsidies awarded to hotels include:

- **February 2017:** $60.8 million to Hanjin International (Real Deal, February 28, 2017)
- **June 2016:** $198.5 million to Frank Gehry Designed Hotel Project (Real Deal, February 28, 2017; Los Angeles Times, June 3, 2016; City of Los Angeles Economic Development Subsidy Report, "Grand Avenue Mixed-Use Development," October 27, 2016)
- **March 2015:** $18.7 million to Greenland LA Metropolis Hotel Development LLC (Los Angeles Daily News, March 17, 2015)

Supply growth in LA is accelerating:

- **6,000 more hotel rooms expected in 2017, including massive DTLA project and 216 room Kimpton in Hollywood.** Los Angeles County expects to add almost 6,000 new hotel rooms in 2017, including a 900 room InterContinental in downtown Los Angeles and a 216 room Kimpton in Hollywood (Los Angeles Times, January 19, 2017).
- **31.1% more rooms under construction in 2017 than 2016, 6.2% of preexisting supply currently being built.** The construction represents 6.2% of preexisting supply and is 31.1% more rooms than the County had in construction in 2016. As of February 2017 only two other U.S. markets had more hotel rooms in construction than Los Angeles: New York and Dallas (Hospitality Net, February 14, 2017).



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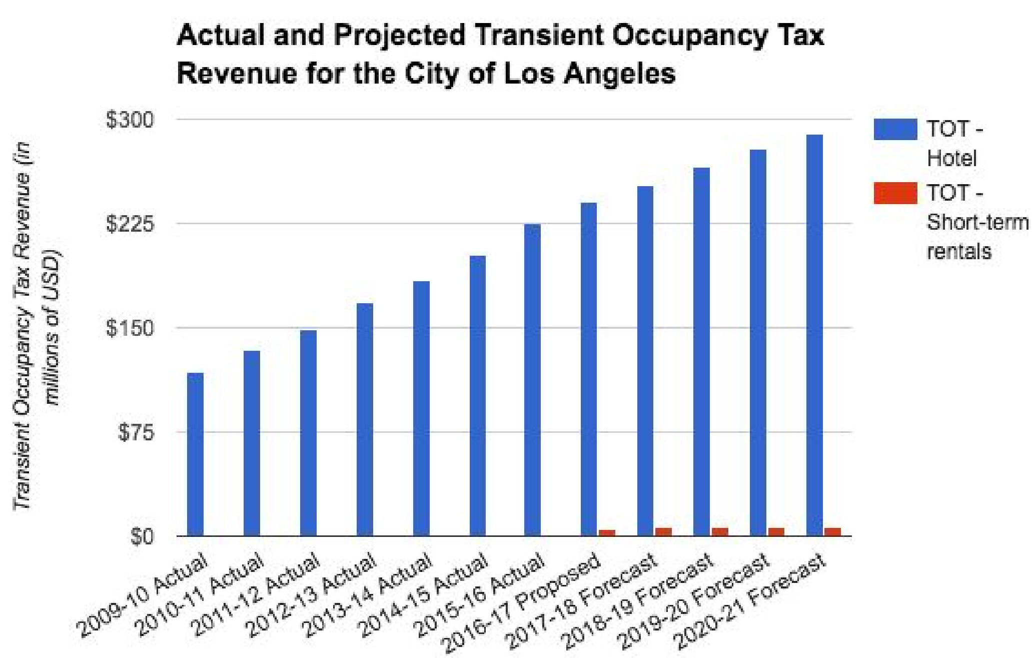
[3] Source: [Discover Los Angeles]

Transient Occupancy Tax Revenue

- Hotel TOT generated $225.1 million in last fiscal year. According to the most recent budget documents, the City of Los Angeles received $225.1 million in Transient Occupancy Tax (TOT) revenue in FY 2015-16 (City of Los Angeles FY 2016-17 Budget Revenue Outlook Supplement, pg. 3).
- Growth of 20.4% to $289.1 million forecasted for 2020-21. Excluding any amounts from Airbnb and other short-term rental platforms, the city has forecasted TOT revenue to increase from $240.1 million in FY 2016-17 to $289.1 million in 2020-21, an increase of 20.4% (City of Los Angeles FY 2016-17 Budget Revenue Outlook Supplement, pg. 12).
- Airbnb generated $13 million in TOT for Los Angeles in just five months despite projections of less than half that amount for a full year. The City of Los Angeles forecasts negotiated TOT collections from Airbnb and other short-term rental platforms to rise from $5.8 million in 2016-17 to $6.9 million in 2020-21. Crushing their projections, Airbnb generated $13 million in TOT revenue for Los Angeles, or nearly 6% of the amount generated by hotels in all of FY 2015-16, in just five months of 2016. (City of Los Angeles FY 2016-17 Budget Revenue Outlook Supplement, pg. 12; Southern California Public Radio, January 20, 2017).



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[4] Source: City of Los Angeles Fiscal Year 2016-17 Budget, 2012-13 Budget Supplement, and 2013-14 Budget Supplement

Comparing Airbnb to Hotels

According to a Smith Travel Research comparison of performance between hotels and Airbnb units in Los Angeles, hotels experience much higher occupancy and achieve much greater revenue.

- Hotel occupancy outperforms Airbnb occupancy in Los Angeles by an enormous margin (81% to 53% in 2016).
- Despite growth, Airbnb's overall market share still pales in comparison to the hotel industry; Airbnb only has 4.1% share of overall revenue in Los Angeles.
- Hotel demand still outpaces hotel supply in Los Angeles.

Moreover, Airbnb attracts a different profile of traveler, according to STR:

- Airbnb guests stay longer. 46.5% of all Airbnb room-nights sold were part of a "long-term stay" across seven U.S. markets. By contrast, only 9% of all hotel room-nights sold in the same seven markets were attributed to extended-stay brands[5].
- In Los Angeles, more than half of all Airbnb room-nights sold (50.9%) were part of trips lasting more than seven days.
- Airbnb's low weekday demand (4.7% in 2016) shows that Airbnb diverts little business travel from hotels in Los Angeles. Furthermore, Airbnb captured only 6.3% of demand in Los Angeles' central business district.

[5] STR does not track length of stay in hotels. This figure does not account for guests who stay for extended periods in non-extended stay hotels.