



NOVEMBER 2015 | PRICE £250

THE BUDGET HOTEL SECTOR'S POSITION IN THE SHARING ECONOMY

Harry Douglass, MRICS
Senior Associate



Introduction

Overall, there are signs that hotel markets across Europe and elsewhere have been buoyed by increasing business confidence and movement within the jobs markets. Compared to strong markets like Germany and the UK, a backdrop of terrorism and political uncertainty has, however, led to larger variations in some regions, postponing any widespread celebrations by hotel operators.

In terms of tourism flows, London, Bangkok, Paris and Dubai lead the way by the number of overnight stays by international visitors whilst Istanbul, Hamburg, Copenhagen and Lisbon are the top four fastest-growing European destinations. More positive hotel performances have generally crystallised investment horizons and encouraged new budget entrants into the European hotel market and elsewhere, including the Middle East.

Underlying all of these development fundamentals is an increasingly competitive budget hotel sector that now encompasses a commercialised private rental market. In the three weeks it has taken to produce this paper, the subject has gained widespread prominence in the media and this accelerated movement warrants an expansive approach to marketing and online distribution channel exposure that embraces the principles of the emerging 'sharing economy'.

The Sharing Economy

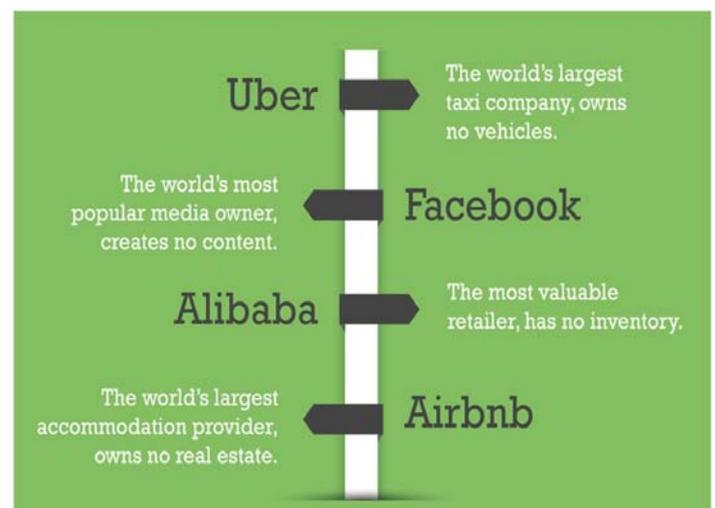
The sharing economy is acknowledged as being a product of the four mega trends affecting today's society. Around 30% of the world's population lived in urban areas following the Second World War. However, today's urbanisation rate is moving towards 60%, putting a strain on housing and resources. At the same time, western economies in particular are facing a profound demographic change as the over-65s is the fastest growing age bracket in many countries, leading to concerns about how a shrinking number of the economically active can support this group in the



long term. Globally, the balance of economic power is perceived to be shifting from the west to the east; China and India have six times more Fortune 500 companies than they did in 2000. This economic power shift is partly attributable to the proliferation of the Internet and the digital revolution, which has contributed to a five-fold increase in international trade and entrepreneurialism since 1980.

These factors have accentuated supply and demand pressures leading to an expanding section of society now familiar with decentralised 'peer-to-peer' technology platforms which increasingly prioritise 'access to' rather 'ownership of' goods and services.

SOMETHING INTERESTING IS HAPPENING



The now famous Tom Goodwin quote about Uber, Facebook, Alibaba and Airbnb concisely articulates how the Internet has enabled the sharing economy and brought in a new range of multi-sided technology-based contributors to the hotel market, such as Airbnb.

Airbnb's Impact in Austin, Texas

In May 2015, researchers from Boston University revised a study first published in 2013 that set out to estimate the impact of Airbnb on the hotel market¹. Focussing on Austin (Texas) and using a 'difference in differences' empirical strategy that exploited the significant spatio-temporal variation in the patterns of Airbnb adoption across city-level markets, the study made some important findings on matters that up to then were only largely anecdotally held.

AUSTIN, TEXAS



The peer-to-peer platform's exponential growth since its formation in 2008 has been aided by its ability to scale supply in a near frictionless manner using existing residential inventory, and marketing a personalised experiential hotel substitute. Overall, the study found that a 10% increase in Airbnb supply resulted in a 0.37% decrease in hotel room revenue; luxury and upscale hotels were least affected by new Airbnb supply because of their price segmentation and amenities.

Airbnb's impact was magnified going down the price scale, and branded hotels were more resilient than independent hotels because of their

¹ Byers D and Zervas G (Dec 2013 & May 2015) The Rise of the Sharing Economy: Estimating the Impact of Airbnb on the Hotel Industry

standardised products and services, larger marketing budgets and loyalty programmes.

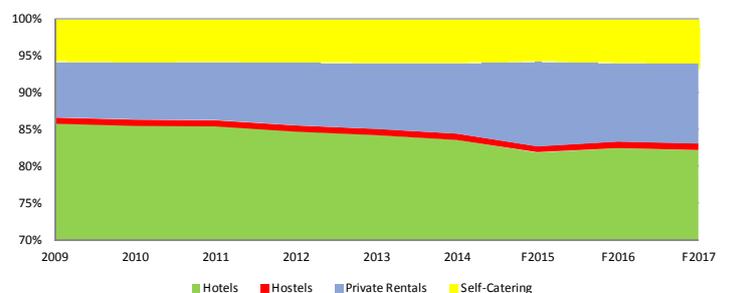
Looking back at the 2014 International Hotel Investment Forum (IHIF), attendance at the Airbnb seminar was negligible. These and other findings² suggest that future events discussing the impact of further commercialisation in this space may be a lot more popular when there is still room for the growth of smaller competing platforms.

The Wider Accommodation Market

With no equivalent to the Austin study having been undertaken in Europe that we are aware of, we looked into the implications of the convergence of the Internet and the private rental market on the hotel sector in a selection of countries. Selecting eight representative jurisdictions, we set out to understand trends affecting the sector across Croatia, France, Germany, Ireland, Italy, the Netherlands and the UK that may be of interest to conference delegates.

The following chart shows the percentage share of aggregate lodging sales by type: chain hotels, hostels, private rentals and self-catering. What is apparent is the expansion of the private rentals market, growing from about 8% of the market in 2008 to 10% in 2014, and this share is forecast to increase to around 12% by 2017.

FIGURE 1: PERCENTAGE SHARE OF AGGREGATE LODGING SALES BY TYPE (€)



Source: Euromonitor

² Clough R, HVS (October 2015) Airbnb and Impacts on the New York City Lodging Market and Economy

This expansion is shown to capture market share from the chain hotels; however, it is not yet at the expense of the hostel market (although we acknowledge this is a less transparent sector to accurately quantify).

Self-catering accommodation is shown to maintain its market share, although this represents mainly managed holiday lets in seasonal locations across France and Italy, which we expect to converge with the private rentals market in due course and which already contain some hostel type resort accommodation.

The Growth in Shared Accommodation

What or who is causing this growth in the private rentals market that facilitates the sharing of accommodation, typically through independent rooms within the same house? We tracked the same four component segments in the eight countries from 2009 to 2014, setting Euromonitor's forecast increases (or decreases) against these. The following chart shows the size of the private rentals markets by volume of annual sales on the y axis, and the compound annual growth rate (CAGR) in private rental sales between 2009 and 2014 in the size of the bubbles.

The chart shows that France, the UK and Italy have the highest volume of private rental sales of the eight markets, with Ireland having the smallest, and Germany appearing to have a surprisingly undeveloped market.

What is significant, however, is the CAGR in sales in Germany of 28% alongside the Netherlands with an overwhelming 89%; Spain with 18% growth is also noteworthy. The expansion of the Netherlands' market has been attributed to the transport connectivity between the gateway city of Amsterdam and its neighbours, Rotterdam, The Hague and Utrecht, all of which lie within proximity to one another. We forecast that a disproportionate share of this will be centred on Amsterdam, not least because of the reduction in luxury hotel development opportunities in the city centre following last year's moratorium. Only Ireland recorded a compound annual decline in private rental sales.

In terms of revenue driven from hostels, Croatia recorded the highest CAGR (+26%) over the period under review, principally as a result of the increasing propensity of young people to visit the country on both specific holidays and backpacking.

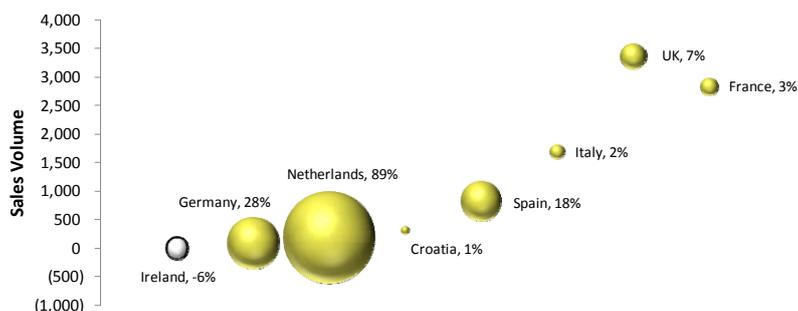
Direct v Online Sales

Hyatt Hotels recently purchased a stake in Lifealike Ltd (onefinestay.com and unhotel.com), demonstrating the hotel industry's increasing acceptance of the necessity to take a position in the peer-to-peer distribution market. Is this strictly necessary?

The following chart demonstrates that total lodging sales for the eight countries in the analysis has increased year on year, although

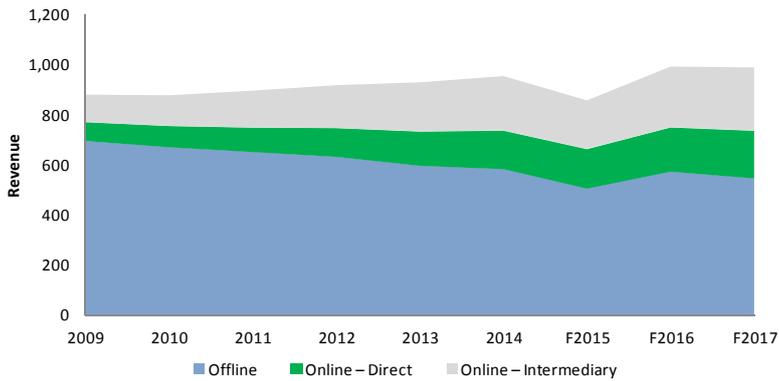
Euromonitor forecasts an overall decline in 2015, which we understand is due to weaker performance from continued economic volatility in the Eurozone. More importantly, offline sales as a percentage of total sales are forecast to continue to decrease as both direct online sales and sales generated through online intermediaries are forecast to rise; sales

FIGURE 2: PRIVATE RENTAL SALES VOLUMES BY COUNTRY 2014 & CAGR 2009-14 (€ 000s)



Source: Euromonitor

FIGURE 3: OFFLINE VS ONLINE SALES VOLUME (€ 000S)



Source: Euromonitor

through intermediaries are expected to capture a greater market share. This confirms the importance of an effective online presence.

The Now Generation

Consumers are spending more time online, with a growing share of lodging bookings made via smartphones; social media increasingly shapes consumer behaviour; OTAs are ever more effective at bridging the gap between guests and smaller independent hotels³; and millennials are said to value an experience more than a formal service. Collectively, these factors are telling the industry to embrace technology to make sales from the 'now generation', a consumer group that will make instant hotel decisions based purely on peer-to-peer reviews and what is 'hot'. This attitude is increasingly prevalent amongst older-aged service users who seek social environments through portals such as City Socializer.

In the past, we have forecast substantial consolidation in the industry, in which major hotel brands attempt to minimise the impact of online intermediaries by using their own distribution networks through a range of brands that capture the guest from the moment when they first make hotel purchasing decisions. Whilst the limited-service hotel investment market has

been relatively quiet, the pace of technological change has not.

We now view the commissions payable to OTAs as an unavoidable marketing expense for a service that is actually fragmenting the branded budget sector, and not marginalising sections of independent hotels as we previously thought. Larger hotel groups may in time have to accept the necessity of being in this mix.

Whilst brands have proven to be more resilient to changes in the hotel environment, we would argue that the strength of a hotel's online presence may in time offer hotel investors an alternative to the balance-sheet security the larger multinational brands currently provide, with the backing of some management vehicles coming from their ability to maximise the online profile through becoming less of a place to stay and more of a way to participate.

The Future

Multiple supply and demand imbalances are symptoms of globalisation. These factors have accentuated supply and demand pressures leading to an expanding section of society familiar with decentralised 'peer-to-peer' platforms and prioritising 'access to' rather 'ownership of' goods and services.

Online sales of hotel accommodation through intermediaries are forecast to continue to increase, and there are now signs that rather than consolidating the larger hotel groups' positions, this is fragmenting the market, which may benefit a larger section of the limited-service hotel market. With a higher number of hosts and participants now in the market and the main brands expanding outside Europe, the consumer should see even greater value in time.

³ Perrett S & Barthel J, HVS (July 2015) OTAs – A Hotel's Friend of Foe?



About HVS

HVS, the world's leading consulting and services organization focused on the hotel, mixed-use, shared ownership, gaming, and leisure industries, celebrates its 35th anniversary this year. Established in 1980, the company performs 4,500+ assignments each year for hotel and real estate owners, operators, and developers worldwide. HVS principals are regarded as the leading experts in their respective regions of the globe. Through a network of more than 35 offices and more than 500 professionals, HVS provides an unparalleled range of complementary services for the hospitality industry. HVS.com

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About the Author



Harry Douglass specialises in hotel consultancy and valuation. He holds an MSc in Real Estate Management and is a member of the Royal Institution of Chartered Surveyors (MRICS). Harry spent a year with Meininger Hotels in 2013/14 and now typically

provides development consultancy advice, transaction due diligence for ho[s]tel and hotel feasibility studies, and single asset and portfolio loan security valuations. Services also extend to hotel transaction and wider residential property investment services covering the student accommodation and branded private residential sector.

HVS London
7-10 Chandos Street
Cavendish Square
London W1G 9DQ

Tel: +44 (20) 7878 7700
hdouglass@hvs.com
www.hvs.com