How to Choose the Right Market to Invest in Short-Term Rentals

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Experience
Avery bought her first investment at the age of 26 on a $37,000 salary, and through strategically investing in mature vacation rental markets, scaled her portfolio to 30 doors (a mix of both vacation rentals and traditional long-term rentals) and achieved financial freedom by age 30. The Short Term Shop helps investors acquire short-term rental properties in the most recession-resistant markets and mentors them using the methods that led her out of the corporate rat race and into financial freedom.

Summary:]

1. [Three Types of STR Markets](https://www.biggerpockets.com/blog/how-to-choose-the-right-market-to-invest-in-short-term-rentals#three-types-of-str-markets)
2. [Metro Markets](https://www.biggerpockets.com/blog/how-to-choose-the-right-market-to-invest-in-short-term-rentals#metro-markets)
3. [National Vacation Markets](https://www.biggerpockets.com/blog/how-to-choose-the-right-market-to-invest-in-short-term-rentals#national-vacation-markets)
4. [Regional Vacation Markets](https://www.biggerpockets.com/blog/how-to-choose-the-right-market-to-invest-in-short-term-rentals#regional-vacation-markets)
5. [Tourism and Recession Resistance](https://www.biggerpockets.com/blog/how-to-choose-the-right-market-to-invest-in-short-term-rentals#tourism-and-recession-resistance)

Short-term rentals, or vacation rentals, are a relatively new strategy when it comes to real estate investing. Although vacation rentals have been around for decades, it wasn’t until the inception of Vrbo and Airbnb that traditional real estate investors began to invest more widely in them. If you’re reading this, chances are you want to explore the ins and outs of this strategy, but you aren’t sure where to start.

The first thing you’ll need to do is choose the type of market in which you want to invest. You’ll begin by researching and analyzing factors like the average occupancy rate, price per night, and cost of properties in the area you’re evaluating to determine whether an investment makes sense.

You’ve probably heard an anecdote or two from a friend who bought a house in the downtown area of their city and “is making a killing” on renting to conference-goers, traveling sports fans, and business travelers. “We’re getting $500 a night,” they might say. However, when probed, they cannot answer questions about things like occupancy rate, gross annual income, and expenses. A rate of $500 per night sounds great, but how many nights a year is the property booked? What is the monthly mortgage payment? How much do electricity and internet cost? Are there HOA fees? Does the $500 a night cover all expenses?

A random strategy yields random results. As a serious investor, you must do the proper research to choose the best market in which to invest based on data and historical information. Don’t just buy a place close to Wrigley Field that will “pay for itself” because you’re a giant Cubs fan.

Three Types of STR Markets

There are three core types of STR markets: metro markets, national fly-to vacation markets, and regional drive-to vacation and leisure markets. There is no right or wrong type of market for investing in STRs. However, all markets come with varying degrees of stability or volatility, based on a number of attributes. Each type has its pros and cons, which I will detail in this chapter.

Your choice of market will depend on what your goals are and how comfortable you are with risk. For example, I prefer the income and regulatory stability of the regional, drivable vacation rental market, although I know plenty of people who earn great returns from investing in metro markets, which are much riskier and have trickier STR regulations. Whichever type of market you choose, make sure you do the research before diving in.

Metro Markets

Metro markets are major metropolitan areas that attract many visitors but are not financially dependent on tourism. They have jobs and industries that support their local economies, and usually have large and dense permanent-resident populations. Examples include New York, Los Angeles, Austin, and Nashville.

In metro markets, short-term rentals are a relatively new choice for renters who historically would have stayed in a hotel, such as professionals on business trips, traveling medical professionals, and locals taking “staycations.” A significant pro of metro markets is this diverse pool of guests, a broad spectrum from which to obtain renters.

The inception of Vrbo and Airbnb presented quite the opportunity for early adopters of STRs in major metro markets, like my friend in Brooklyn. Their product was new and provided more space and comfort than standard hotel accommodations. Plus, at the time, such accommodations were scarce in their markets.

While metro markets have extremely high rewards in terms of cash flow, they are arguably the riskiest type of STR market, based on several factors. The historical renting of hotels rather than privately owned homes, coupled with a dense permanent-resident population, has proven troublesome for many metro markets over the past decade. Additionally, metro markets have a far more volatile STR regulation structure than other types of markets. I know many metro-market STR investors who were shut down after a few short years of operation.

There are three main economic drivers of anti-STR regulations in major metropolitan areas:

1. Hotel lobbyists: Lobbying funded by major hotel chains is the largest source of anti-STR regulations in metro markets across the country. As hundreds of STRs have flooded the hospitality market and gained significant market share, hotels have made no small effort to eradicate them. By having lobbyists work to get bills introduced at the local level, the hotel chains have successfully curtailed the growth of the industry. This has resulted in cities’ limiting the zones in which STRs are allowed, revoking permits, and, in some cases, banning them altogether.
2. Disgruntled neighbors: As STR investing has become more popular in many cities, properties on previously quiet residential streets have been converted into “mini hotels” and “party houses.” Their permanent-resident neighbors have taken to city councils to voice their contempt for the perceived negative effects that STR investors have had on their neighborhoods. Negative local media coverage of these grievances and the few incidents that have caused them have created an adversarial relationship between STR owners and non-investor permanent residents.
3. Lack of affordable housing due to Airbnb investors: As long-term rental or primary-home properties have been acquired, renovated, and converted into STRs, property values in many metro markets have skyrocketed. Since it can be difficult to acquire these properties in major cities, they are often sold at a premium, and those premium-priced sales have caused rapid appreciation in the surrounding areas. While this sounds like a positive to investors, it has caused a severe affordable-housing issue for permanent residents in some markets, once again sending advocacy groups and locals to city councils with their complaints.

Another key consideration when investing in metro-market STRs is market saturation. In the rare metro market where STRs are largely unregulated, this is a very real possibility. When a market has gone from very few of these rentals to many over the course of a few years, and additional properties are being converted into STRs almost daily, market saturation is on the horizon. Of course, you always have the option of converting the property into a long- or medium-term rental if needed.

National Vacation Markets

National vacation markets are tourism-dependent. Think big, popular vacation markets that most travelers access by plane, such as Hawaii; Aspen, Colorado; and Disney World/Orlando, Florida.

These markets are stable in terms of rental regulations because STRs have been part of the economic fabric for decades. Still, affluent permanent residents and large resort chains have pushed for STRs to be allowed only in certain areas. For example, Hawaii and Jackson Hole, Wyoming, have strict regulations to keep their permanent residents happy. In fact, there are fewer than ten neighborhoods in Jackson Hole where short-term renting is allowed. This makes it difficult to find properties that are properly zoned to allow short-term renting and self-management of STRs.

While national vacation rental markets are quite lucrative during economic booms, they are the first to see a downward trend in a recession. As travelers tighten their purse strings, lavish fly-to vacations are traded for more affordable, closer-to-home destinations.

Regional Vacation Markets

In regional vacations markets, the majority of tourists arrive by car. Examples include Gatlinburg, Tennessee; Panama City Beach, Florida; Big Bear Lake, California; and Branson, Missouri.

Regional leisure destinations are 100 percent financially dependent on tourism and have been for decades, just like the national vacation markets mentioned previously. There is little or no industry outside of tourism in these areas. However, one major difference from the national markets is that regional markets are much more affordable and easier to get to.

Since these markets are often smaller towns, real estate prices tend to be cheaper than in their national vacation rental market counterparts (though not always). Additionally, many of these markets are home to more vacation renters than permanent residents, many of whom have been renting privately owned cabins, condos, and single-family homes rather than hotels since well before the inception of sites like Airbnb.

STR regulations are very accommodating in these markets, where local governments determined how to monetize STR income decades ago, so city council clashes are nonexistent. As a matter of fact, the small occupancy tax collected by these governments is so lucrative that it would be far too fiscally detrimental for them to regulate against STRs.

On the surface, it would seem that metro markets are the best for STRs, given their diverse pool of travelers. However, because of regulation issues in most metro areas, it’s actually the regional, drivable vacation rental market that is the most stable investment. Regional markets are the most recession-resistant due to affordability and accessibility, which we will address in later pages.

*To learn more about analyzing, buying, and managing vacation properties, check out* [Short-Term Rental, Long-Term Wealth](https://store.biggerpockets.com/products/short-term-rental-long-term-wealth?utm_source=blog&utm_campaign=str)*by Avery Carl!*

Tourism and Recession Resistance

STRs are dependent on the tourism and travel industry, so it is important to ensure that there will be enough travelers for an STR to be profitable, even during economic downturns. Several factors contribute to market resilience.

First, we will take a look at the drivers of the past two economic downturns: the housing/financial crisis of 2008 and the COVID-19 pandemic of 2020–2021. During both of these economic downturns, the regional vacation market performed better than metro and national vacation markets. That was thanks to its two pillars of recession resistance: affordability and accessibility.

Affordability: In the Great Recession of 2008, the disposable income of the average American family dropped dramatically. Many potential STR investors mistakenly assume that, with less disposable income, everyone stops going on vacation. This is simply not the case. Travelers may no longer take a trip to Aspen, Disney World, or Hawaii, but they will still go on vacation—albeit to a more affordable vacation destination that does not require flights, or expensive ski lift and theme park tickets. In other words, families go on local weekend getaways in a recession.

Accessibility: At the beginning of the COVID-19 pandemic in 2020, all STR markets took a forceful hit, but as reopenings started across the country, regional leisure markets outperformed both metro and national vacation markets. This time, while affordability was most definitely a factor, accessibility was the main driver of success.

After months of lockdowns, the entire population was bursting at the seams to get out of their homes. However, most Americans were not comfortable traveling to big metro areas with large concentrations of people, and they were even less comfortable with boarding flights and being confined with strangers for even a short period of time. Due to the fear of contracting the virus, travelers drove to their nearest vacation destination, in the comfort of their own vehicles, to rent single-family residences where they could be outside and enjoy themselves at a safe distance from other people.

When you have found an STR market that interests you, the first thing you need to do is examine the STR regulations in that market. (You would be surprised at how many investors do not look into this before shopping for a property.) The second item to evaluate when choosing a market is its maturity. How long have STRs been the norm for travelers rather than hotels? How long have STRs been around? The earlier that STRs began to prosper in the market, the more mature the market is. The less mature a market is, the greater the chance of unfavorable STR regulations.