NAB ECONOMIC INSIGHTS

OFFICE DEMAND HIT BY INCREASED WORK FROM HOME

NAB Group Economics

Office demand hit by increased work from home, not job losses

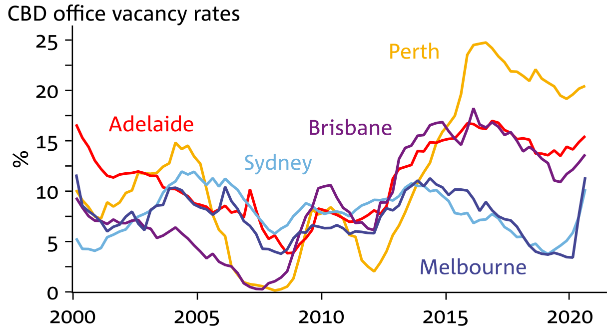
- The pandemic has prompted a considerable fall in activity, which has seen office vacancy rates rise. This comes at a time of rising supply, particularly in NSW and Victoria. As such, it is unsurprising that sentiment in the office market has slumped, as reported in NAB's commercial property survey.
- We use detailed employment data to show that nearly all job losses to date are in non-office roles. As such, the bigger hit to office work is likely to come from increased working from home, where a sixth of large firms expect more than a quarter of their staff to keep working from home in future.

The pandemic has been a major blow to demand for office space

The pandemic has prompted widespread job losses, considerable business closures and unprecedented changes to the way we live and work. At its peak, around 0.9 million jobs were lost in April and May. Business surveys from the same period reported around 10% of firms stopped trading. Further, around 30% of SMEs and 45% of large firms have more than a quarter of their staff working from home.

The collapse in activity has seen CBD office vacancies rise sharply, most notably in Sydney and Melbourne. Data from JLL Research shows the Melbourne vacancy rate jumped 8.0pp to 11.3% and the Sydney vacancy rate rose 4.3pp to 10.2%. In other capital cities, the increase has been between 0.8 to 1.5pp.

Chart 1: Vacancy rates have spiked in Sydney and Melbourne

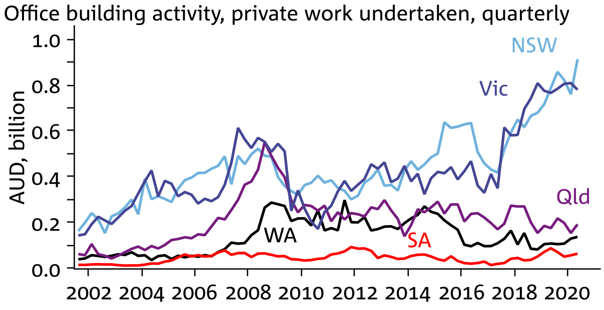


Source: JLL Research

The collapse in demand has occurred at a time of rising office supply

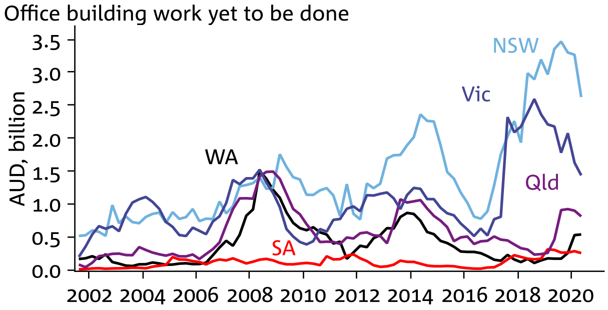
Prior to the pandemic office supply was on the rise, notably in NSW and Victoria. Office building activity in these two states was at close to record levels. The pipeline of office building work is also elevated in NSW and Victoria, although Queensland also has a sizable pipeline of work.

Chart 2: Office construction had been ramping up in NSW and Victoria



Note: Seasonally adjusted by NAB
Source: National Australia Bank, Australian Bureau of Statistics

Chart 3: The office construction pipeline is large

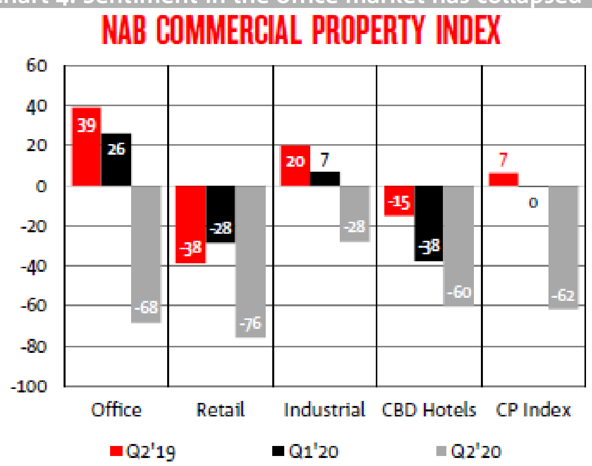


Note: Seasonally adjusted by NAB
Source: National Australia Bank, Australian Bureau of Statistics

Commercial property sentiment has deteriorated

Given the rise in vacancies and the outlook for a drawn out economic recovery, it's no surprise that commercial property sentiment towards office real estate has deteriorated. NAB's Q2 Commercial Property Survey shows that office market sentiment has slumped, to fall from the best performing commercial property market to the second worst, after retail.

Chart 4: Sentiment in the office market has collapsed



Note, the Q3 Commercial Property Survey will be released Thursday 26 November.

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But office jobs have seen little impact from the pandemic

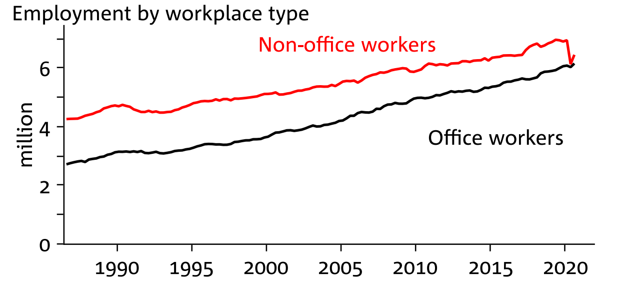
At the peak of the pandemic, a large 0.9 million jobs were lost. Almost half of these jobs have since been recovered, according to the official monthly figures from the ABS.

However, the ABS also publishes detailed quarterly labour data that splits workers into role types. We used these data to split employment into office and non-office workers. On our simple split:

- Office workers were those working as professionals, admin. staff, sales people and managers. Managers and sales people in farming, retail and hospitality were not included.
- Non-office workers included trade workers, personal service workers, machinery operators, labourers and managers/sales people in retail, hospitality and farming.

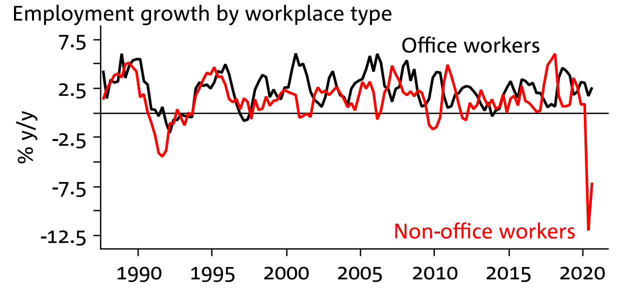
These data show that nearly all the jobs lost were non-office jobs. Even after a rebound in Q3, there are 7.1% fewer non-office workers than a year ago. In stark contrast, the number of office workers is up 2.6% from a year ago and, to-date, shows little impact from the pandemic.

Chart 5: Nearly all the job losses to date have been non-office workers



Note: Office workers are professionals, administrative workers, sales agents and managers (excl. farm, hospitality and retail). Seasonally adjusted by NAB.
Source: National Australia Bank, ABS

Chart 6: There are 2.6% more office workers than a year ago, despite the pandemic



Note: Office workers are professionals, administrative workers, sales agents and managers (excl. farm, hospitality and retail)
Source: National Australia Bank, ABS

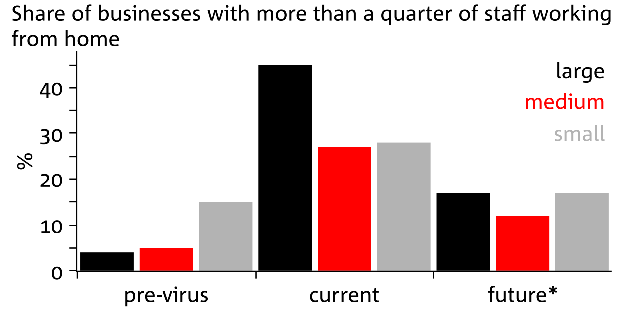
The divergence may partly reflect reports that professionals, who are just over half (53%) of office workers, had a large pipeline of work in place that supported employment through the peak of the pandemic and it is likely that office jobs growth will slow as the pipeline of work shrinks. Nevertheless, it seems the pandemic has not dealt a large blow to office employment.

Even without a fall in office jobs, the switch to work from home suggests a large fall in office demand

One of the key shifts in office work to emerge from the pandemic has been the take-up of working from home arrangements. The ABS business impacts survey shows that in September almost three-tenths (28%) of businesses had more than a quarter of staff working remotely. In contrast, pre-virus just 14% of firms had a considerable share of staff working from home. The increase in remote working was particularly stark for large businesses.

To understand the shift in work habits going forward we looked at businesses' expectations for remote work. Overall, just 16% of businesses expected more than a quarter of staff to continue working remotely once restrictions ease, similar to pre-virus levels.

Chart 7: Working from home is expected to be more common in the future



* Expectations once restrictions are lifted and conditions stabilise
Source: National Australia Bank, ABS

However, the level of working from home was expected to be much greater for large and medium firms, compared to pre-virus. Our analysis focuses on large firms, who employ 200 or more employees. These businesses are likely the key drivers of office demand.

For large businesses, 17% expected to have more than a quarter of their workforce working remotely in the future. This is 13pp more than the 4% of firms that had a sizable remote workforce pre-virus. Breaking this down, there was a:

- 9pp increase in firms with 25 to 50% of the workforce remote working,
- 3pp increase in firms with 50 to 75% of the workforce remote working, and;
- 1pp increase in firms with more than 75% of the workforce remote working.

Partially offsetting this is a 3pp decrease in firms with some but less than 25% of employees remote working.

We make the key assumption that a large firm's likelihood of working from home is unrelated to its workforce size. In other words, the large companies reporting they expect >75% of their workforce to work from home should have, on average, the same number of people as the large firms reporting they expect 25 to 50% of their staff to work remotely.

With this assumption, these figures imply an increase in working from home of between 4.5 and 7% of large company employees. This suggests a huge hit to demand for office space, much larger than the impact of limited office job losses.

Going forward, the shift to increased working from home means office demand faces a new COVID-normal

Our analysis shows little impact on office employment to date from the pandemic and containment restrictions, suggesting office work has been relatively insulated from jobs losses. Going forward, we expect office jobs growth to slow a little, reflecting softer economic demand, but with the virus contained and the recovery underway this impact should be minimal.

Our analysis shows the much bigger impact on office demand comes from the shift towards working from home. We estimate an additional 4.5 to 7% of staff at large firms will be working from home in future, once most restrictions are eased.

This suggests there will be significant adjustment in the office market, due to the near-term fall in demand. Further, after workplaces adjust to their new COVID-normal levels of office and remote working, the outlook for office demand growth will have weakened. Given the shift towards working from home, it is likely that office demand will be less responsive to growth in the office workforce.

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