Industrial production – Positive start in 2020, but high short-term risks are looming

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Juan Carlos Alderete, CFA
Director of Economic Research
juan.alderete.macal@banorte.com

Francisco Flores
Senior Economist, Mexico
francisco.flores.serrano@banorte.com

- **Industrial production (January): -1.6% y/y; Banorte: -1.3%; consensus: -1.5% (range: -2.6% to 1.0%); previous: -1.0%**
- **In seasonally-adjusted terms, activity increased 0.3% m/m, with growth in three out of the four main sectors**
- **Mining keeps showing a strong performance, up 4.5% m/m and led by services related to mining (8.5%). On the other hand, oil output edged-up 0.8%**
- **Construction managed to increase for a third consecutive month, at 0.5%. Edification was stronger (1.2%), while civil engineering (-1.9%) dragged the sector, likely related to low public spending in infrastructure**
- **Manufacturing remained resilient, increasing 0.1%. Specifically, we highlight the 3.6% advance in transportation equipment**
- **Despite today's relatively favorable figures, we warn that disruptions caused by the Coronavirus, coupled with high market volatility in recent days, suggest risks for industrial activity are skewed to the downside**

Industrial activity fell 1.6% y/y in January. This was lower than consensus (-1.5%) and our slightly more upbeat estimate of -1.3%. The result was negatively influenced by an adverse base-effect in both construction and manufacturing. On the contrary and more favorable, mining exhibited its highest advance in annual terms since December 2005, standing at 5.8%. This sector remains supported by oil and gas (6.9%, see Table 1), with higher production by Pemex. Non-oil was more modest at 1.7%, while services were also strong at 6.5%. Construction declined strongly (-8.6%) exacerbating the -4.5% at the end of last year, with both edification and civil engineering in contraction. Manufacturing was also lower, partly still impacted by lingering shocks that took place in 4Q19 (Chart 2).

More positive start of the year in monthly terms. Using seasonally adjusted figures, industry advanced 0.3% m/m, with three out of the four main subsectors in positive territory (Chart 3). Nevertheless, overall activity levels remain low (Chart 4). Similar to annual figures, this was led by mining which increased 4.5%. Specifically, oil and gas edged-up 0.8%, albeit with services leading gains at 8.3% (Table 2). Construction decelerated to 0.5% from 0.6% in the previous month, dragged by civil engineering, which more than reversed gains in December. In this respect, we believe this performance pours some cold water to signals of a stronger footing into 2020. Edification stood at 1.2%, following the recent trend of outperformance relative to the rest of the sector. Manufacturing extended the advance of the previous month (0.1%), with 11 out of 21 sectors higher. We highlight that transportation bounced 3.6%, reverting the 1.7% drop observed in December. In other relevant subsectors, we also highlight the 1.1% expansion in the food industry. Nevertheless, computers and electronic equipment fell 2.1%. Overall, we believe that despite the relatively good performance, risks for the sector, not only due to the Coronavirus but due to the overall economic deceleration, prevail.

The external environment has worsened further. As warned in our previous report, the effect from the Coronavirus outbreak on global manufacturing represents an important headwind, at least for 1Q20 and increasingly likely also for the full first half. News on this front have turned for the worse, with diagnosed cases still increasing at a relatively high pace globally and several countries restricting activities further, including those related to supply chain disruptions. Given the extent of the problem, the initial supply-side shock has increasingly permeated to the demand-side, making it even more worrisome. Heightened financial market volatility only adds further to the significant spike in uncertainty, likely resulting in consumers and businesses holding back on spending.

Regarding mining, we believe the government will keep working heavily to increase production despite the steep fall of crude-oil prices at the start of the week, which challenges their profitability. In this sense, given that most oil and gas production is still done by the government, the immediate impact in mining might be relatively modest. The most important risk, in our view, is that the price adjustment results in a spending setback due to the expectation of lower oil-related income, with the government remaining committed with healthy public finances. Nevertheless, it should be reminded that some of this income was hedged last year, which along resources from the Stabilization Fund, ensures an average price for the Mexican mix of US$/bbl 49.00, according to the Ministry of Finance (MoF). On the other hand, both construction and manufacturing are more vulnerable given the likely hit to economic growth. In the former, business confidence is likely to keep falling beyond the decline already observed in most subsectors in February (with a slight rebound in commerce and services) as the outlook darkens. An eventual retracement of public spending, as already mentioned, could also have an additional effect, particularly in construction. In manufacturing, auto production in February picked up 4.5% y/y, while exports fell 1.9%, providing mixed signals. The US manufacturing index fell only modestly according to PMIs, with the ISM to 50.1pts from 50.9 in December and Markit's indicator at 50.7pts from 51.9pts, respectively. In Mexico, the IMEF manufacturing for the same period remained in contraction territory despite only inching lower sequentially. Although these may be cues about the sector's resiliency, we stay very cautious and see a negative bias ahead given the multiple challenges already observed in other countries.

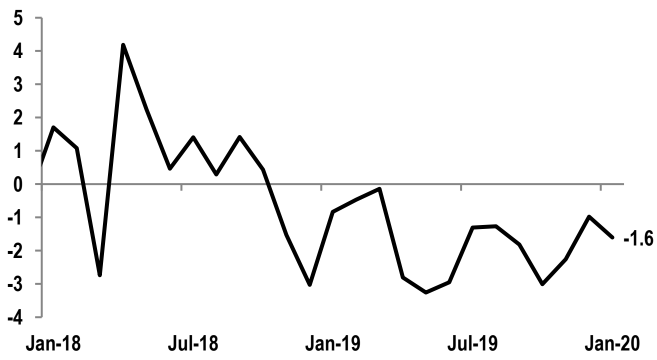
Going forward –assuming the Coronavirus eventually recedes– more upside is likely in the second half of the year given policy support. Locally, Arturo Herrera stated last week they will speed up already budgeted spending plans to help economic growth, including among them infrastructure outlays. Undersecretary Gabriel Yorio stated they are analyzing possible fiscal stimulus for impacted businesses, including those in tourism and some services, along other measures with development banks. We have more uncertainty about the next steps from Banxico, as inflation picked up in February and the exchange rate adds risks to the upside to prices despite the downside bias for growth. Globally, several countries are working to provide fiscal and monetary stimulus to their economies, with the possibility of a coordinated response to help economic growth, albeit yet with some limited visibility given the rapid evolution of events in recent weeks.

Table 1: Industrial production
% y/y nsa

	Jan-20	Jan-19	2019	2018
Industrial Production	**-1.6**	**-0.8**	**-1.8**	**0.5**
Mining	**5.8**	**-10.5**	**-5.1**	**-5.7**
Oil and gas	6.9	-14.3	-6.7	-6.8
Non-oil mining	1.7	-5.3	-2.2	-2.4
Services related to mining	6.5	3.0	2.6	-3.8
Utilities	**0.4**	**-0.6**	**2.3**	**7.5**
Electricity	0.1	-1.1	2.6	9.2
Water and gas distribution	1.3	1.2	1.2	1.9
Construction	**-8.6**	**1.7**	**-5.0**	**0.5**
Edification	-7.3	4.7	-3.0	1.2
Civil engineering	-17.7	-2.7	-6.1	-6.0
Specialized works for construction	-4.9	-7.7	-13.1	5.3
Manufacturing	**-0.9**	**1.3**	**0.2**	**1.8**
Food industry	2.4	0.7	1.7	3.0
Beverages and tobacco	1.1	4.3	2.4	5.5
Textiles - Raw materials	-16.3	7.0	-4.0	1.7
Textiles - Finished products ex clothing	-2.7	1.6	-4.0	6.4
Textiles - Clothing	-4.5	-3.1	-4.7	1.2
Leather and substitutes	-8.0	-1.4	-2.1	-1.4
Woodworking	-1.6	-5.5	0.3	-1.9
Paper	-2.9	2.6	-0.5	1.5
Printing and related products	-0.5	-11.6	-10.7	8.3
Oil- and carbon-related products	21.5	-17.5	-2.7	-16.9
Chemicals	-1.6	-4.7	-1.5	-2.7
Plastics and rubber	-2.5	-1.6	-2.1	2.6
Non-metallic mineral goods production	0.1	-5.4	-2.5	-1.9
Basic metal industries	2.4	-2.0	-1.7	-1.9
Metal-based goods production	-6.9	0.3	-5.6	1.0
Machinery and equipment	-12.8	5.9	-1.3	1.9
Computer, communications, electronic, and other hardware	-1.6	3.0	4.8	2.2
Electric hardware	2.3	2.5	-0.9	1.5
Transportation equipment	-1.7	7.0	1.3	4.5
Furniture, mattresses and blinds	-0.2	-1.2	-3.6	6.4
Other manufacturing industries	-3.4	3.2	0.2	2.3

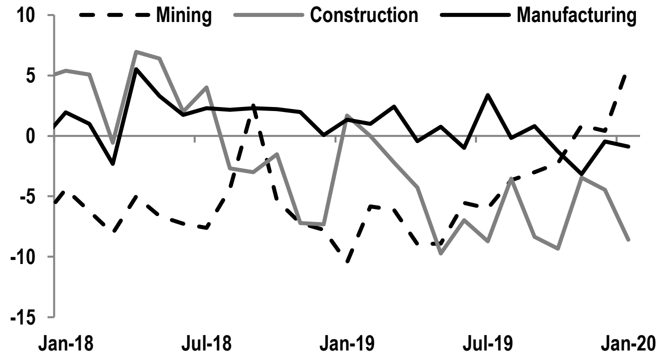
Source: INEGI

Chart 1: Industrial production
% y/y



Source: INEGI

Chart 2: Industrial production by sector
% y/y



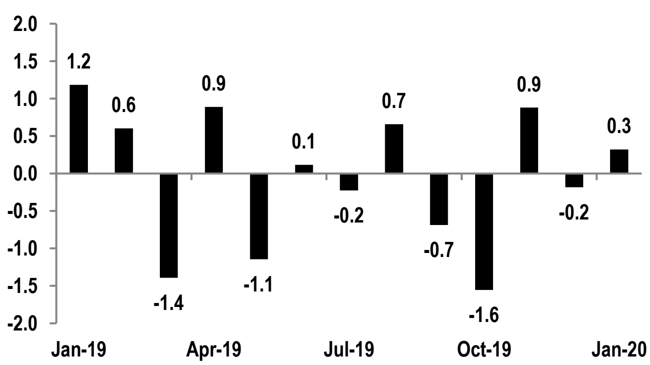
Source: INEGI

Table 2: Industrial production
% m/m sa; % 3m/3m sa

	% m/m			% 3m/3m	
	Jan-20	Dec-19	Nov-19	Jan'20-Nov'19	Dec-Oct'19
Industrial Production	**0.3**	**-0.2**	**0.9**	**-0.4**	**-1.3**
Mining	**4.5**	**-1.2**	**1.3**	**1.7**	**1.0**
Oil and gas	0.8	0.0	3.1	2.6	1.5
Non-oil mining	1.0	0.0	0.3	1.8	1.6
Services related to mining	8.3	-6.7	-5.5	-9.7	-4.9
Utilities	**-4.3**	**0.1**	**-0.3**	**-1.8**	**0.2**
Electricity	-5.7	0.5	-0.3	-2.1	0.4
Water and gas distribution	-0.3	0.1	0.3	0.5	0.6
Construction	**0.5**	**0.6**	**1.2**	**0.3**	**-1.1**
Edification	1.2	0.4	4.8	3.0	-0.3
Civil engineering	-1.9	1.4	-6.4	-8.6	-8.1
Specialized works for construction	1.3	2.9	-0.6	1.7	1.4
Manufacturing	**0.1**	**0.6**	**0.0**	**-1.0**	**-2.1**
Food industry	1.1	-1.2	-0.3	-0.6	-0.5
Beverages and tobacco	1.2	0.8	-2.1	-0.9	-0.4
Textiles - Raw materials	-1.4	-4.2	-1.2	-3.1	-1.7
Textiles - Finished products ex clothing	2.1	6.2	-10.4	-2.5	1.2
Textiles - Clothing	1.6	0.3	-3.1	-4.4	-4.3
Leather and substitutes	-1.7	-0.5	-3.4	-4.9	-3.4
Woodworking	-3.4	5.6	-0.9	0.8	0.7
Paper	0.2	-2.0	1.0	-0.7	-0.2
Printing and related products	6.5	-2.1	-1.3	-3.5	-5.1
Oil- and carbon-related products	2.5	-1.3	-0.6	-1.0	-1.5
Chemicals	-1.2	-1.8	0.4	-1.4	-0.5
Plastics and rubber	-6.9	6.1	2.7	3.7	3.2
Non-metallic mineral goods production	-0.2	0.1	3.4	0.9	-1.4
Basic metal industries	3.3	0.5	-2.1	-3.7	-4.4
Metal-based goods production	-1.6	-1.0	-0.1	-2.1	-1.3
Machinery and equipment	0.6	5.5	-9.5	-9.9	-11.7
Computer, communications, electronic, and other hardware	-2.1	2.5	-1.7	-0.5	-0.6
Electric hardware	2.3	-1.5	1.3	2.6	2.0
Transportation equipment	3.6	-1.7	7.1	-0.7	-7.1
Furniture, mattresses and blinds	-1.1	0.5	1.7	1.9	3.2
Other manufacturing industries	-0.98	0.0	-0.8	-2.0	-1.6

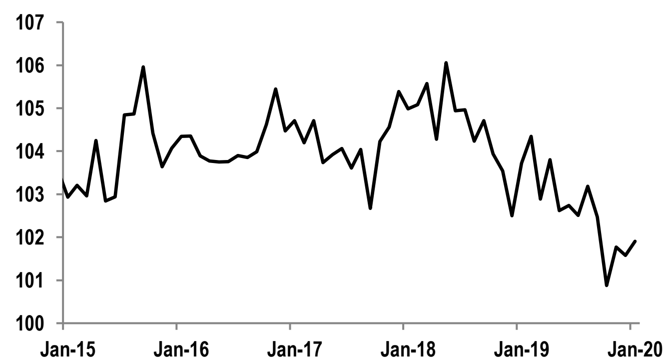
Source: INEGI

Chart 3: Industrial production
% m/m sa



Source: INEGI

Chart 4: Industrial production
Index sa



Source: INEGI

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GRUPO FINANCIERO BANORTE S.A.B. de C.V.

Research and Strategy			
Gabriel Casillas Olvera	IRO and Chief Economist	gabriel.casillas@banorte.com	(55) 4433 - 4695
Raquel Vázquez Godinez	Assistant	raquel.vazquez@banorte.com	(55) 1670 - 2967
Lourdes Calvo Fernández	Analyst (Edition)	lourdes.calvo@banorte.com	(55) 1103 - 4000 x 2611
Economic Research and Financial Market Strategy			
Alejandro Padilla Santana	Executive Director of Economic Research and Financial Markets Strategy	alejandro.padilla@banorte.com	(55) 1103 - 4043
Itzel Martínez Rojas	Analyst	itzel.martinez.rojas@banorte.com	(55) 1670 - 2251
Economic Research			
Juan Carlos Alderete Macal, CFA	Director of Economic Research	juan.alderete.macal@banorte.com	(55) 1103 - 4046
Francisco José Flores Serrano	Senior Economist, Mexico	francisco.flores.serrano@banorte.com	(55) 1670 - 2957
Katia Celina Goya Ostos	Senior Economist, Global	katia.goya@banorte.com	(55) 1670 - 1821
Luis Leopoldo López Salinas	Economist, Global	luis.lopez.salinas@banorte.com	(55) 1103 - 4000 x 2707
Market Strategy			
Manuel Jiménez Zaldívar	Director of Market Strategy	manuel.jimenez@banorte.com	(55) 5268 - 1671
Fixed income and FX Strategy			
Santiago Leal Singer	Senior Strategist, Fixed Income and FX	santiago.leal@banorte.com	(55) 1670 - 2144
Leslie Thalía Orozco Vélez	Strategist, Fixed Income and FX	leslie.orozco.velez@banorte.com	(55) 5268 - 1698
Equity Strategy			
Marissa Garza Ostos	Director of Equity Strategy	marissa.garza@banorte.com	(55) 1670 - 1719
José Itzamna Espitia Hernández	Senior Strategist, Equity	jose.espitia@banorte.com	(55) 1670 - 2249
Valentín III Mendoza Balderas	Senior Strategist, Equity	valentin.mendoza@banorte.com	(55) 1670 - 2250
Víctor Hugo Cortes Castro	Senior Strategist, Technical	victorh.cortes@banorte.com	(55) 1670 - 1800
Jorge Antonio Izquierdo Lobato	Analyst	jorge.izquierdo.lobato@banorte.com	(55) 1670 - 1746
Eridani Ruibal Ortega	Analyst	eridani.ruibal.ortega@banorte.com	(55) 1103 - 4000 x 2755
Corporate Debt			
Tania Abdul Massih Jacobo	Director of Corporate Debt	tania.abdul@banorte.com	(55) 5268 - 1672
Hugo Armando Gómez Solís	Senior Analyst, Corporate Debt	hugoa.gomez@banorte.com	(55) 1670 - 2247
Gerardo Daniel Valle Trujillo	Analyst, Corporate Debt	gerardo.valle.trujillo@banorte.com	(55) 1670 - 2248
Economic Studies			
Delia María Paredes Mier	Executive Director of Economic Studies	delia.paredes@banorte.com	(55) 5268 - 1694
Miguel Alejandro Calvo Domínguez	Senior Analyst, Economic Studies	miguel.calvo@banorte.com	(55) 1670 - 2220
Wholesale Banking			
Armando Rodal Espinosa	Head of Wholesale Banking	armando.rodal@banorte.com	(81) 8319 - 6895
Alejandro Eric Faesi Puente	Head of Global Markets and Institutional Sales	alejandro.faesi@banorte.com	(55) 5268 - 1640
Alejandro Aguilar Ceballos	Head of Asset Management	alejandro.aguilar.ceballos@banorte.com	(55) 5268 - 9996
Arturo Monroy Ballesteros	Head of Investment Banking and Structured Finance	arturo.monroy.ballesteros@banorte.com	(55) 5004 - 1002
Gerardo Zamora Nanez	Head of Transactional Banking, Leasing and Factoring	gerardo.zamora@banorte.com	(81) 8318 - 5071
Jorge de la Vega Grajales	Head of Government Banking	jorge.delavega@banorte.com	(55) 5004 - 5121
Luis Pietrini Sheridan	Head of Private Banking	luis.pietrini@banorte.com	(55) 5004 - 1453
René Gerardo Pimentel Ibarrola	Head of Corporate Banking	pimentelr@banorte.com	(55) 5268 - 9004
Ricardo Velázquez Rodríguez	Head of International Banking	rvelazquez@banorte.com	(55) 5004 - 5279
Víctor Antonio Roldan Ferrer	Head of Commercial Banking	victor.roldan.ferrer@banorte.com	(55) 5004 - 1454