IGAE – The recovery extended through July as the country adjusts to the 'new normal'

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- ***Global Economic Activity Indicator* (Jul): -9.8% y/y; Banorte: -9.7%; consensus: -10.1% (range: -12.0% to -8.5%); previous: -13.3%**
- **This figure is higher for a second consecutive time, in our view benefitted by stronger external demand and additional efforts to reopen the economy**
- **Inside and as already known, industry contracted 11.3% y/y, with construction lagging at -23.5%. On the other hand, services improved to -10.1%. Primary activities have been more resilient and surprised considerably to the upside this time around, at +11.0%**
- **In monthly terms, the economy strengthened 5.7%, with all sectors advancing. Industry picked up 6.9%, while services were slightly more muted at +4.6%, with only two subsectors lower**
- **Today's report helps confirm that the lowest point for activity was observed in May, although with timely indicators more mixed in terms of the likely trend for activity during the rest of 3Q20. We believe the recovery will continue, although at a more modest pace**

Economic activity declined 9.8% y/y in July. This was higher than consensus (-10.1%) but practically in line with our -9.7%. The figure was stronger for a second month in a row, more positive when considering a challenging base effect and less working days in the annual comparison when compared to June. In this respect, and using seasonally adjusted figures, activity fell 9.8% vs. -14.6% in the previous month. As a result, and back to original data, the economy accumulated a 9.9% contraction so far in 2020 (see Chart 1), very close to our -9.8% full-year forecast. In our view, two main factors drove the recovery: (1) Strong external demand, mainly benefitting industry, but also some externally driven sectors in services; and (2) an additional reopening of domestic activities, helping services more extensively. In this respect and taking a look at the breakdown –using non-seasonally adjusted figures–, industrial production stood at -11.3% y/y, with manufacturing outperforming (-9.0%), particularly transportation, hand in hand with the relative recovery in trade volumes. In our view, this sector has been more successful in adjusting to the 'new normal', partly because of the possibility of producing without direct contact with clients, but also as demand for their goods has not been as affected, particularly for export-oriented sectors –in turn, likely supported by strong stimulus measures, particularly in the US. Services were broadly in line with expectations, standing at -10.1% (Chart 2). We point that the categories that have been mostly affected since the pandemic broke, such as lodging, transportation, and recreational services, remain among the weakest (Table 1) but were also higher than in the previous month. Finally, agriculture has been resilient given its essential status, reaching +11.0%, surprising significantly to the upside.

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Monthly figures confirm that the bottom in activity has already passed. The economy strengthened 5.7% m/m (Banorte: 5.7%), extending the 8.8% observed in June (Table 2). The latter helps reaffirm that the lowest point for activity was likely in May, when lockdowns remained very stringent. Nevertheless, we should mention that the absolute level of the index is 8.5% lower than in February, before the full effect of COVID-19 was felt domestically (Chart 4). This is consistent with most other indicators for the period, which improved broadly. IP was quite strong at 6.9%, considering it popped +17.9% in June. All four sectors exhibited gains. Mining was more stable (0.8%) as it depends mostly on Pemex production which had been declining recently, followed by construction (0.9%) which has been quite modest. As mentioned above, manufacturing (11.0%) has been the most dynamic, and which in our view will also prove more resilient in coming months.

Services came in at 4.6% (Chart 3), with only two of nine subsectors down. Broadly speaking, we see these results as positive, thinking that fatigue about social-distancing measures may have helped, despite modest advances in terms of the local evolution of the pandemic. In this sense, non-essential sectors remain the weakest despite improving strongly at the margin, such as recreational (+11.4%), lodging (+22.6%), and transportation (+3.5%), also aided by higher mobility. We highlight that retail increased 17.6%, considerably stronger than the report published a couple of days ago. Meanwhile, professional services bounced back 9.9% after plunging 8.1% in June. More importantly, education and healthcare declined for a third consecutive month (-1.5%), which may be related to a modest fall in hospitalization rates related to COVID-19, along less need to use services such as childcare and summer camps, among others. Lastly, we highlight that government services picked up 3%, highest since February.

Mixed signals about the extension of the recovery going forward. Following the rebound of the previous two months, more timely indicators of activity have been mixed in terms of signaling the likely trend during the rest of 3Q20. Among them, we highlight IMEF indicators for August, with both lower relative to the previous month and staying in contraction, including declines in the 'production' and 'new orders' components and a sizable downward surprise in manufacturing, which has been the main support of the recovery so far. The latter may be related to some mismatch in inventories, as the sector in the US keeps growing according to the ISM –reaching 56.0pts, highest since early 2019– and industrial production, among others. Regarding local industry, auto production in said month was modestly lower in absolute terms relative to July, with domestic sales also muted as they declined -28.7% y/y. In this respect, business confidence indicators were broadly lower across all sectors, which in our view may be a signal that growth is stalling after the recent rebound.

On a more positive note, we highlight: (1) The relative improvement in the domestic evolution of the pandemic, as judged by the 'traffic light' indicator; and (2) continued efforts to reopen activities by the local and federal government. As an example of the former, by the end of August only one state was in 'red' (Colima), 21 in 'orange' and 10 in 'yellow'. Big metropolitan areas such as in Mexico City, State of Mexico, Jalisco and Nuevo Leon were all in 'orange'.

This is much better than at the end of July, in which the 32 states were evenly divided between 'orange' and 'red´. In this respect, it should be reminded that allowed activities depend on where they are in terms of risks according to this system. Therefore, additional benefits could have materialized, suggested also by the aggregate trend indicator in non-financial services, manufacturing and construction, which were all better at the margin. Regarding the second point and without been exhaustive, Mexico City permitted since early August the restricted reopening of bars, cinemas and museums. There were similar announcements in other states, which have extended through September (such as the case of public beaches, archeological sites, etc.). Nonetheless, mobility indicators –such as those compiled by *Apple*– show much more modest gains since August, remaining below the baseline. Moreover, ANTAD's same-store sales registered a more a modest contraction, in our view driven by improved availability of physical stores. In particular, they stood at -6.8% y/y in real terms vs. -12.3% in July, with the most sizable pickup in departmental stores.

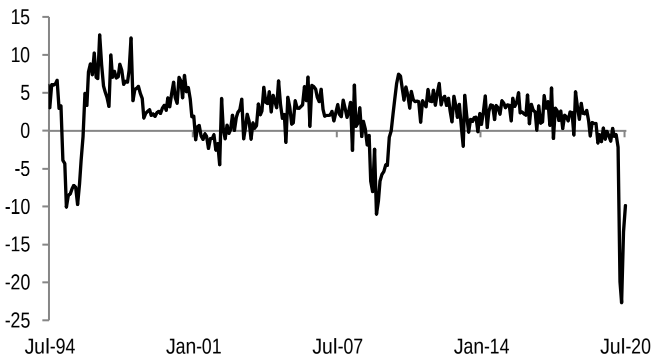
Judging by data released so far, it is our take that activity in August likely kept recovering in sequential terms, although at a more modest pace relative to the previous two months, not only because of a more difficult base effect but also as most activities have already reopened. In this respect, –banning some very specific sectors unusually hit by the pandemic, such as massive events– limits for a stronger rebound ahead will probably be due to dampened demand as opposed to their availability, which could be argued had a more immediate effect in terms of supply when the lockdowns were at full steam.

Table 1: Global economic activity indicator
% y/y nsa, % y/y sa

	y/y nsa				y/y sa	
	Jul-20	Jul-19	Jan-Jul'**20**	Jan-Jul'**19**	Jul-20	Jul-19
Total	-9.8	0.4	-9.9	0.0	-9.8	-0.6
Agriculture	11.0	2.5	2.3	0.7	10.6	2.2
Industrial production	-11.3	-1.3	-13.7	-1.6	-11.6	-2.4
Mining	-3.1	-5.9	-0.4	-7.5	-3.0	-5.7
Utilities	-8.9	0.2	-5.7	0.9	-8.8	0.3
Construction	-23.5	-8.8	-21.2	-4.4	-23.7	-9.3
Manufacturing	-9.0	3.3	-15.1	1.2	-9.5	1.2
Services	-10.1	1.1	-8.7	0.7	-10.0	0.1
Wholesale	-14.1	1.1	-13.4	-2.4	-14.0	-1.9
Retail	-8.1	4.2	-13.4	2.9	-7.2	2.5
Transport	-21.9	1.3	-15.4	0.2	-22.0	0.4
Financial services	-1.1	0.2	-0.8	1.7	-1.2	0.1
Professional services	0.8	3.2	-2.5	4.6	0.1	2.4
Education and healthcare services	-4.5	0.0	-1.8	0.1	-4.1	-0.1
Recreational services	-19.5	0.1	-17.3	0.4	-19.6	0.4
Lodging services	-61.4	0.4	-43.0	0.0	-61.4	0.4
Government services	4.4	-3.5	3.8	-3.9	4.3	-3.5

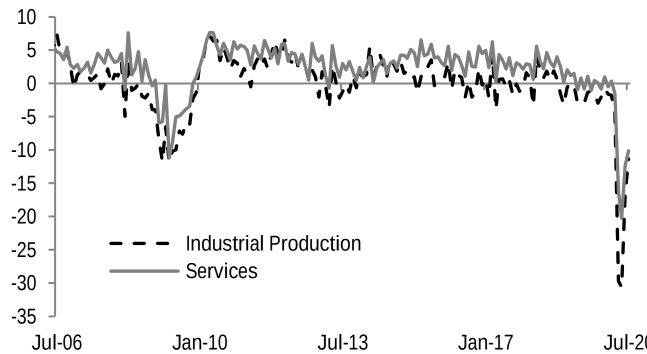
Source: INEGI

Chart 1: Global economic activity indicator
% y/y nsa



Source: INEGI

Chart 2: Global economic indicator by component
% y/y nsa



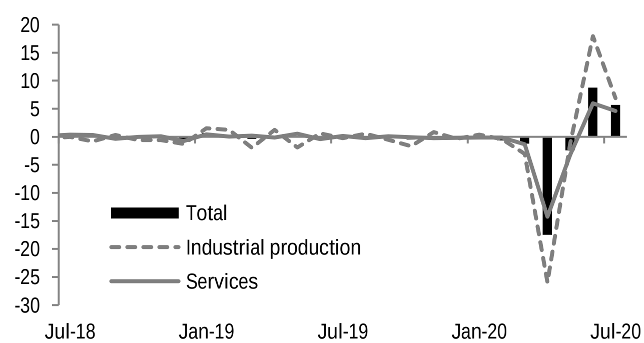
Source: INEGI

Table 2: Global economic activity indicator
% m/m sa, % 3m/3m sa

	% m/m, sa			% 3m/3m sa	
	Jul-20	Jun-20	Difference	May-Jul'20	Apr-Jun'**20**
Total	5.7	8.8	-3.1	-8.1	-17.3
Agriculture	13.9	-5.1	19.0	1.3	-2.3
Industrial production	6.9	17.9	-11.0	-9.2	-23.9
Services	4.6	6.0	-1.4	-8.4	-15.2

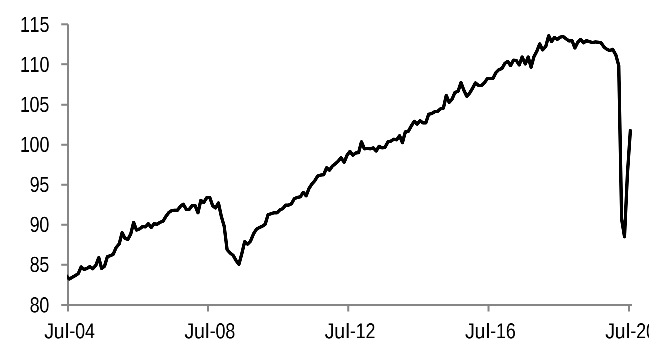
Source: INEGI

Chart 3: Global economic activity indicator
% m/m sa



Source: INEGI

Chart 4: Global economic activity indicator
Index sa



Source: INEGI

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