Industrial production – Renewed dynamism in October, despite worsening conditions

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- **Industrial production (October): -3.3% y/y nsa; Banorte: -5.6%; consensus: -5.5% (range: -7.0% to -3.6%); previous: -6.1%**
- **This figure was higher for a fifth consecutive month, benefited by a positive base effect after General Motors's strike last year driving a positive impact on manufacturing. On a year-to-date basis, industry has declined 11.3% y/y**
- **In monthly terms, industry accelerated to +2.0% after the slowdown to+0.6% in the previous month. With this, total activity is about 4.5% lower than in February, before the pandemic hit**
- **Mining stood at 1.0%, with oil inching higher 0.3% despite some challenges in the period. Non-oil rose 3.1%, largely driving the increase**
- **Construction rebounded 3.6% after the -5.1% shown in the previous month. This was due to a 6.0% expansion in edification, more closely related to the private sector. Civil engineering was also better, at 1.0%**
- **Manufacturing remained quite positive at 1.8% (previous: 0.8%). By industry, 16 out of 21 sectors improved, highlighting machinery and equipment (8.1%) and metallic goods (3.9%) to the upside. Meanwhile, transportation pared back some gains (-0.1%) along oil and carbon (-1.5%)**
- **Despite a positive start to 4Q20, the deterioration in epidemiological conditions, both locally and globally, has heightened risks for activity towards the end of the year**

Industrial activity keeps rising in October. The headline figure came in at -3.3% y/y (see Chart 1), above consensus (-5.5%), which practically matched our -5.6% forecast. In this sense, the annual comparison was stronger for a fifth consecutive month, benefited by a more favorable base effect relative to the previous month and despite a negative calendar effect due to one less working day (vs. September, with one more). Adjusting for this (using seasonally adjusted data), activity fell 3.1% y/y (previous -7.2%). Going back to original data, construction regained some momentum at -10.1% (Chart 2), with a correction higher in two out of three subcomponents. Moreover, mining stood at -1.1%, with the oil sector (-0.6%) resilient despite several hurricanes in the period. Manufacturing was considerably better, standing at -1.3%, with 9 out of 21 categories back in positive territory (Table 1). Among them, we highlight the auto sector at +2.3%, strongly benefited by the base effect stemming from General Motors's strike last year, which impacted the provision of raw materials. With these figures, industrial activity accumulates an 11.3% y/y decline in the first ten months of the year.

Momentum regained in sequential terms. Industry rose 2.0% m/m (Chart 3), adding five consecutive months advancing, following the reopening of the economy. We note that figures from the previous month were revised to the upside, now at +0.6% from 0.0% previously. Although a pickup was expected due to a more favorable effect, it was more sizeable than expected. In absolute terms, it remains similar to levels seen in early 2011 (Chart 4). Moreover, total activity is now around 4.5% lower than in February, before the pandemic hit.

The upward surprise was mainly due to the rebound in construction, standing at +3.6% after the -5.1% in September. Edification picked up 6.0%, with civil engineering also slightly higher at 1.0% (Table 2). Despite of this increase, the sector remains as the weakest relative to pre-pandemic levels, almost 12.4% below February, albeit remembering that it was already weak beforehand. Going into mining (1.0%), oil posted a slight increase (0.3%) despite some possible disruptions due to two hurricanes in the period. We believe overall prospects for the sector remain limited by CAPEX and other operational constraints in Pemex. The non-oil sector was much stronger (3.1%), in our view benefited by a recovery in commodities' prices. More positively, manufacturing maintained an upbeat pace, growing 1.8% after the 2.1% in September. By industry, 16 out of 21 sectors improved, highlighting machinery and equipment (8.1%) and metallic goods (3.9%). Meanwhile, transportation pared back some gains (-0.1%) along oil and carbon (-1.5%)

Despite this favorable result, risks towards the end of 4Q20 are high. In our view, the most important one is that epidemiological conditions started worsening in October and have kept trending negatively in both November and December. In this context, ten additional states transitioned from 'yellow' to 'orange' according to the latest 'traffic light' indicator. Considering this, we believe risks for activity have increased despite the government's aim to maintain activities open given the impact from nationwide closures experienced in April and May.

In manufacturing, this has started to show in forward-looking data, such as November's IMEF's PMI, falling 1.1pts to 48.5pts, with strong declines in 'new orders', 'inventories' and 'production'. Moreover, railway blockades continued in Michoacán during the month, also dampening activity. It should be noted that these ended exactly until the 30th. As mentioned in the previous report, these have mostly affected the flow of goods in the port of Lázaro Cárdenas, disrupting supply chains in the auto, oil and steel industries, among others. According to Kansas City Southern de México, losses amounted to about $120 million daily, although the cost was likely higher as several other industries were impacted. Data from the auto sector also showed a moderation, with vehicle output at 312,184, which implies an increase of only 1.4% y/y vs. +8.8% in October (albeit with the base effect mentioned above). Signals in the external front are somewhat mixed. In the US, the ISM manufacturing for November slowed down to 57.5pts from 59.3pts in the previous month, still positive despite its marginal decline. On the other hand, Markit's PMI for the same period picked up to 56.7pts. In the latter, producers saw a large expansion in output driven by stronger demand, although skewed mainly towards domestic buyers.

Another relevant driver for higher optimism was lower uncertainty because of the development of a vaccine and the results of the US election. Nevertheless, and probably reflected more clearly in the ISM, we will need to look for the impact from the lack of additional fiscal stimulus. This is relevant as information suggests that this will materialize ate least until we know the final composition of the Senate and the new administration takes office. Coupled with the surge in COVID-19 cases, we believe the most immediate outlook is at least uncertain if not more negative, with the possibility of a comeback much clearer only in the medium term.

In mining, climate conditions improved slightly after two hurricanes passed in October across the Gulf of Mexico. Following the impact of hurricane Eta in Central America, strong rains associated to it extended to the southern part of the country, mainly impacting Tabasco. Therefore, we do not rule out some impact to onshore fields in this oil-producing state. Nonetheless, the country's crude oil exports stood at a seven-month high in November, according to *Bloomberg*. We take this news with some caution though, as several Pemex terminals were closed for a while in October, which might explain part of this rise. In non-oil we expect dynamism to continue, with commodities prices pushed higher by expectations of a vaccine and the subsequent recovery.

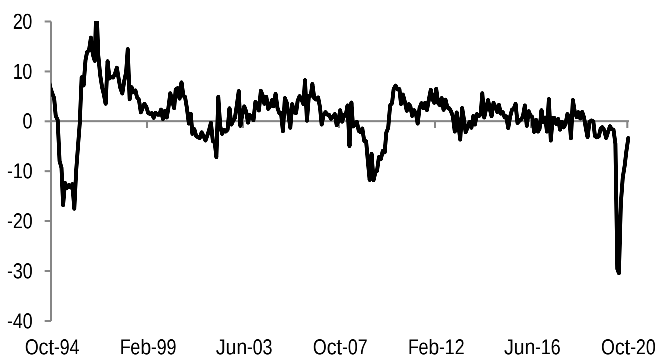
Finally, indicators for construction keep improving, including both business confidence and the aggregate trend indicator, albeit both at a more moderate pace. In contrast, banking credit to the sector has shown a double-digit decline from July to October, although with mortgage loans strong relative to other sectors. In addition, there are favorable news from the public-private infrastructure partnership. According to the Ministry of Finance, investment under this program has amounted to $43.6 billion since announced and until late November. In this context, eight new projects were slated to begin between November and December. Nevertheless, we still believe this sector is facing the strongest headwinds, with uncertainty from the pandemic but also because of other idiosyncratic factors that keep weighing.

Table 1: Industrial production
% y/y nsa

	Oct-20	Oct-19	Jan-Oct'20	Jan-Oct'19
Industrial Production	-3.3	-3.3	-11.3	-1.7
Mining	-1.1	-1.8	-0.8	-5.4
Oil and gas	-0.6	-4.6	0.5	-8.6
Non-oil mining	5.7	-2.5	-6.2	-3.3
Services related to mining	-19.4	26.9	1.1	17.8
Utilities	-4.2	2.1	-5.1	-1.0
Electricity	-5.0	3.4	-5.7	-0.5
Water and gas distribution	-1.1	-3.1	-2.9	-3.1
Construction	-10.1	-10.5	-18.7	-5.4
Edification	-8.6	-10.2	-18.2	-3.4
Civil engineering	-23.1	-9.5	-26.0	-8.9
Specialized works for construction	-2.1	-12.6	-12.8	-10.7
Manufacturing	-1.3	-1.3	-11.9	1.0
Food industry	-0.8	3.9	-0.6	2.3
Beverages and tobacco	0.0	5.9	-9.9	3.6
Textiles - Raw materials	-18.1	-4.1	-34.1	-3.2
Textiles - Finished products ex clothing	-5.4	-1.8	-16.3	-2.2
Textiles - Clothing	-30.5	-3.3	-36.9	-2.5
Leather and substitutes	-23.4	0.7	-37.0	-1.9
Woodworking	-1.9	0.2	-16.7	-0.1
Paper	-1.2	-1.4	-6.0	0.2
Printing and related products	-17.6	-7.8	-19.3	-9.1
Oil- and carbon-related products	2.0	7.9	-8.3	-4.6
Chemicals	-3.8	-0.3	-5.1	-2.8
Plastics and rubber	1.6	-4.4	-12.2	-2.5
Non-metallic mineral goods production	1.9	-0.9	-9.6	-0.5
Basic metal industries	-1.0	1.0	-10.9	-2.3
Metal-based goods production	0.4	3.5	-12.8	3.1
Machinery and equipment	-4.6	-5.5	-20.2	0.2
Computer, communications, electronic, and other hardware	0.1	3.7	-8.0	5.5
Electric hardware	7.2	-0.8	-2.7	-1.4
Transportation equipment	2.3	-9.4	-24.6	2.8
Furniture, mattresses and blinds	-5.5	-3.3	-19.7	-4.2
Other manufacturing industries	-5.6	-10.4	-12.0	-4.2

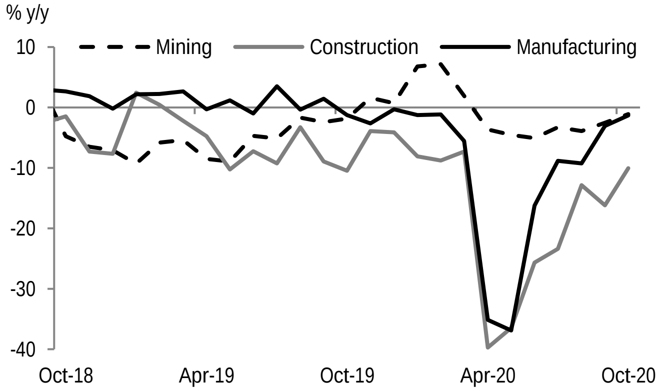
Source: INEGI

Chart 1: Industrial production
% y/y



Source: INEGI

Chart 2: Industrial production by sector
% y/y



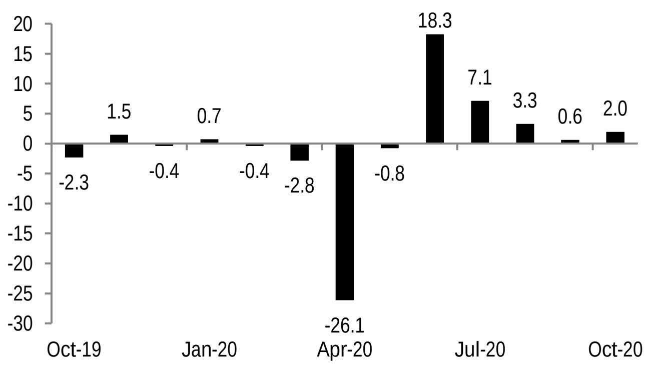
Source: INEGI

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

	% m/m			% 3m/3m	
	Oct-20	Sep-20	Aug-20	Aug-Oct'**20**	Jul-**Sep'20**
Industrial Production	2.0	0.6	3.3	15.0	22.0
Mining	1.0	0.3	1.6	3.4	2.7
Oil and gas	0.3	0.2	1.9	1.4	-1.4
Non-oil mining	3.1	1.8	2.1	19.4	31.1
Services related to mining	-3.9	-0.7	-4.7	-7.6	-5.7
Utilities	1.8	-2.6	5.6	8.3	5.4
Electricity	2.1	-3.3	6.8	10.1	6.3
Water and gas distribution	0.5	0.7	1.1	2.5	1.9
Construction	3.6	-5.1	12.1	15.8	19.7
Edification	6.0	-9.7	16.2	17.8	24.3
Civil engineering	1.0	-0.5	2.9	3.1	1.7
Specialized works for construction	0.0	7.9	7.1	20.4	18.7
Manufacturing	1.8	2.1	0.7	18.6	31.7
Food industry	0.3	1.3	-0.9	0.8	0.5
Beverages and tobacco	1.9	-2.2	1.8	24.1	46.4
Textiles - Raw materials	0.3	7.3	15.9	66.4	114.9
Textiles - Finished products ex clothing	0.7	2.0	2.6	30.1	65.3
Textiles - Clothing	-0.4	5.8	13.5	65.7	115.2
Leather and substitutes	8.0	3.1	7.9	73.2	169.8
Woodworking	8.8	-0.4	7.1	27.7	34.2
Paper	0.7	1.3	4.1	12.8	10.3
Printing and related products	-0.9	-1.3	14.3	20.5	30.1
Oil- and carbon-related products	-1.5	21.7	15.3	12.2	-4.6
Chemicals	1.2	0.2	2.9	6.9	5.6
Plastics and rubber	1.7	1.2	6.8	27.9	39.9
Non-metallic mineral goods production	1.0	0.9	6.6	22.6	36.8
Basic metal industries	0.9	11.7	5.5	17.5	12.6
Metal-based goods production	3.9	0.9	1.8	32.1	52.3
Machinery and equipment	8.1	-0.4	6.9	23.1	30.1
Computer, communications, electronic, and other hardware	0.1	3.5	-4.0	10.8	22.3
Electric hardware	0.2	4.3	3.4	21.4	22.9
Transportation equipment	-0.1	5.5	-3.1	49.1	155.8
Furniture, mattresses and blinds	2.3	1.0	2.2	37.8	81.7
Other manufacturing industries	-0.2	1.0	6.7	16.4	21.8

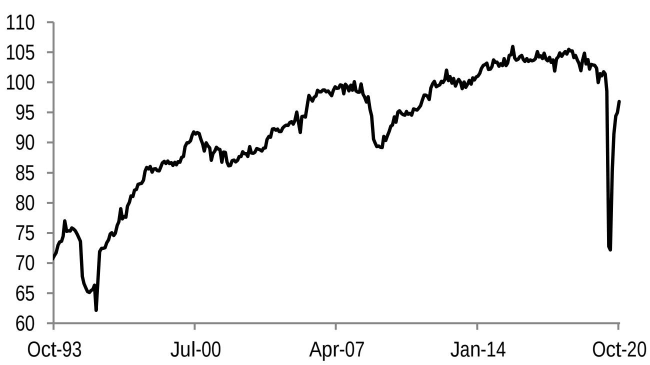
Source: INEGI

Chart 3: Industrial production
% m/m sa



Source: INEGI

Chart 4: Industrial production
Index sa



Source: INEGI

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