The unemployment rate reacts to worse COVID-19 dynamics at the start of the year

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- **Unemployment rate (January; nsa): 4.73%; Banorte: 4.61%; consensus: 4.37% (range: 3.80% to 4.61%); previous: 3.80%**
- **Part-time workers: 14.9% (previous: 14.2%); Participation rate: 56.1% (previous: 56.4%)**
- **We should recall that the month's seasonality is very adverse, with the rate typically increasing by a significant amount and reversing gradually in both February and March**
- **A total of 883.8 thousand positions were lost in the month. This happened in an environment of renewed lockdowns due to worse pandemic dynamics, in our view affecting once again more in services. In this context, about 3.8 million jobs are yet to be recovered from the level in February 2020, before COVID-19**
- **The participation rate declined further, in line with its seasonal trend, with 391.0 thousand workers less in the labor force. Most keep being reclassified as 'not available for work', which is unusual relative to previous years but may have been affected again by the pandemic**
- **The part time rate increased to 14.9%, which helps confirm that the overall results for the labor market were weak**
- **Job losses in the informal sector stood at 597.5 thousand (67.6% of the total), with the informality rate fell to 55.6% from 55.8% in December**
- **Total workers earning up to one minimum wage (MW) surged by 1.0 million, while those between one and two increased by 384.7 thousand. This was likely driven by the 15% upward adjustment in the benchmark measure**
- **Short-term risks for the labor market have increased due to shocks affecting activity at the start of the year, albeit likely still recovering gradually for the rest of 2021**

The unemployment rate increases above expectations. Specifically, it stood at 4.73% (non-seasonally adjusted figures, see chart below to the left), above consensus (4.37%) but closer to our 4.61% forecast. Nevertheless, the period's seasonality is quite adverse, typically more than reversing the decline observed in December and correcting downwards along February and March. Several factors are likely at play behind these dynamics, including: (1) The specific answers of unemployed workers, depending on whether they are or not looking for a job; (2) distortions due to the renewal of labor contracts; and (3) temporary hiring in some sectors during the holidays, such as tourism and entertainment –albeit with possible layouts in others, such as industry. In this sense, using seasonally adjusted figures, the unemployment rate increased by 9bps relative to December, at 4.47%. This suggests that the recovery of the labor market stalled, which may be related to a more difficult dynamic in terms of the evolution of the pandemic. Regarding the latter point, available high frequency data indeed suggests that economic activity was affected by this factor.

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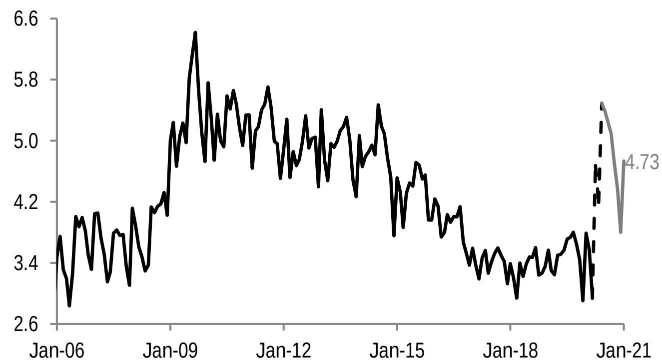
In the period, net employment decreased by 883.8 thousand positions, of which 286.3 and 597.5 thousand were in the formal and informal sectors, respectively. Total employees stood at 52.0 million, also lower than in December and about 3.8 less than in February 2020, before the pandemic started.

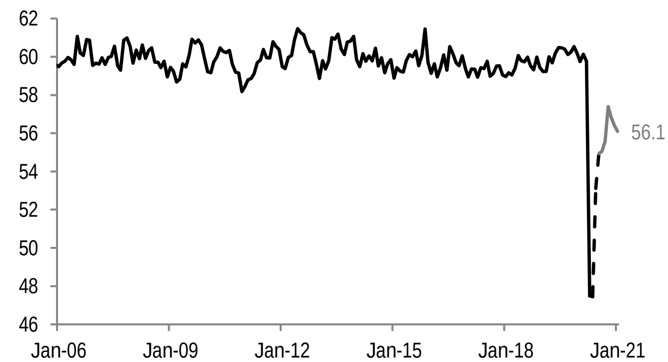
The labor force fell by 391.0 thousand, resulting in a decline of the participation rate to 56.1% from 56.4% in the previous month (see chart below on the right). People outside of the labor force increased by 230.2 thousand, with most of them (152.1 thousand) catalogued as 'not available for work'. Those 'available for work' picked up by 78.1 thousand, which remains high relative to the long-term historical series. Apart from the period's strong seasonality –which makes it more difficult to read underlying dynamics–, we still believe that data is distorted by the pandemic. To reflect labor market conditions more accurately, if we sum the latter group to the total unemployed and add them back into the labor force, the 'expanded' unemployment rate would have reached 18.9% (previous: 17.9%), above the 12.4% seen in December 2019.

Unemployment rate
%, nsa



Note: Dotted lines correspond to data obtained through the phone-only survey. The grey line indicates the hybrid survey
Source: Banorte with data from INEGI

Participation rate
%, nsa



Note: Dotted lines correspond to data obtained through the phone-only survey. The grey line indicates the hybrid survey
Source: Banorte with data from INEGI

Job losses remain mostly in the informal sector. As mentioned above, 597.5 thousand jobs were shed here. Similar to the most difficult moments of the pandemic, it is likely that new restrictions affected them the most, particularly in services as they are more sensible to mobility levels. In turn, formal employees fell by 286.3 thousand. This was much weaker than the signal provided by the report of affiliated workers to IMSS, which showed a net creation of 47,919 posts. This suggests that other formal positions (*e.g.* government, Defense Ministry and Pemex) were eliminated in the period. The informality rate declined to 55.6% from 55.8% in December. Meanwhile, the part-time rate stood at 14.9% from 14.2%. In broad terms, we believe results weak, albeit not severely considering the restrictions, with both employers and employees acquiring some experience to adjust to the conditions imposed by COVID-19. On the other hand, average wages per hour increased by MXN 2.6 sequentially, reaching 46.94 pesos. In this context, we recall the [15% minimum wage hike] starting on January 1st. In our view, this was likely an additional driver against employment dynamics. When looking at employment changes by income level, workers earning up to one MW surged by 1.0 million, while those between one and two MW increased by 384.7 thousand.

Meanwhile, the remaining categories fell by around 1.4 million. In our view, this is due to the change in the benchmark measure, which also increased, as opposed to pay cuts to existing workers. On a sector basis, and consistent with what we already said about the pandemic, losses were mostly in services with -468.8 posts, followed by industry (-249.4 thousand) and agriculture (-186.4 thousand).

INEGI's employment report
Non-seasonally adjusted figures

%	Jan-21	Dec-20	Difference
Unemployment rate	4.73	3.80	0.93
Participation rate	56.1	56.4	-0.3
Part-time workers rate	14.9	14.2	0.8
Formal employment	44.4	44.2	-0.2
Informal employment[1]	55.6	55.8	0.2
Working in the informal economy	28.2	27.8	0.5
Working in the formal economy	27.4	28.1	-0.7

Source: INEGI

The labor market is still many months away from a full recovery. As warned in our previous report, short term risks for employment had been on the rise after a series of positive surprises in labor market statistics throughout 2H20. In this respect, this is the first setback (with seasonally adjusted figures) since the recovery began after the pandemic shock, back in June. As the unemployment rate usually lags activity, we do not rule out a modest upward adjustment in the short term, based on the cue from the moderation to 0.1% m/m in the economy in December, according to the monthly GDP proxy (IGAE). Nevertheless, the latter surprised positively and avoided a contraction. Furthermore, we are cautious because of other short-term shocks that may induce some upward pressures. Among them, we highlight the stoppage of several activities some days ago due to electricity and natural gas shortages. According to news reports and the *National Center of Energy Control* (CENACE, in Spanish), 26 out of the 32 states of the country were affected. It is our take that industry was more affected than services. Although the impact was temporary and energy supply has been mostly reestablished, there may well be secondary effects into other sectors. In this respect, we will look closely to the 'employment' components within IMEF indicators and business confidence measures for February. To the latter, we add reports that companies in the auto industry had to diminish production due to the shortage of key raw materials (*e.g.* semiconductors). This may well be an additional and more persistent headwind, not only for them, but also for other manufacturing activities such as home appliances or TVs. All in all, it is our take that heightened risks for the recovery of the labor market remain in place.

We maintain that the medium-term outlook is more favorable, with more optimism due to the start of vaccinations as well as increased fiscal stimulus in the US, prompting us to revise upwards our 2021 GDP estimate for said country to 5.4% from 3.9%. Hence: (1) Externally-driven sectors could have even more gains left despite the recovery being well underway; and (2) the unemployment rate could accelerate further to the downside once we see more vigorous activity, particularly on sectors which have been affected most by the pandemic.

[1] Informal employment considers workers not affiliated to the Social Security Institutes (IMSS and ISSSTE) and the armed forces. However, those in the formal economy do pay some form of income tax

Nevertheless, the abovementioned increase in the minimum wage may limit the overall speed, with the unemployment rate still some way to reach levels like those before COVID-19, at around 3.5%. Ample slack conditions are likely to keep upward adjustments in average wages at bay but would translate into less job posts created. We also reaffirm our view that the part-time rate will probably remain high, acting as shock-absorber to avoid additional employment losses. All in all, we still think that a full recovery of the labor market is many months away, dampening prospects for a faster rebound in domestic demand, which remains muted.

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