Industrial production – Growth in January, but with short-term risks looming large

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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): -4.9% y/y nsa; Banorte: -4.9%; consensus: -4.5% (range: -9.6% to -1.7%); previous: -2.1%**
- **This print was lower than the previous month, dragged by a negative calendar effect despite more dynamism in some sectors, especially construction**
- **In monthly terms, industry increased 0.2%, marking its eighth improvement in a row. With this, activity remains around 3.3% below pre-pandemic levels (vs. February 2020)**
- **By sectors, construction was the main driver at 1.5%, rebounding after last month's decline, with mining also positive at 0.2%. In contrast, manufacturing declined 0.5%, dragged by a weak performance in autos**
- **Short-term headwinds have increased on supply disruptions, especially for manufacturing. Nevertheless, the outlook remains positive in the medium-term as US growth is likely to outperform the rest of the world**

Industry declines in the annual comparison on a negative calendar effect. The headline came at -4.9% y/y (see Chart 1), slightly lower than consensus (-4.5%) but exactly at our estimate. We recall that the figures are skewed due to a negative calendar effect, with two fewer working days in the annual comparison (vs. two more in December). Correcting for this, activity fell 3.7% (previous:-3.2%), above the -4.1% in INEGI's *Timely Indicator of Economic Activity*. Back to original figures, manufacturing declined 3.4% after last month's outperformance (Chart 2). In our opinion, this was a result of both the calendar effect and a weak result in key industries, such as clothing (-28.6%), transportation (-12.3%) and food (-1.3%). On the contrary, we highlight strength in oil and carbon (15.5%), electric (9.8%) and electronic (7.8%) goods. Mining stood at -3.3%. Inside, both oil and gas and non-oil were broadly stable relative to December, even with a more complex base effect (Table 1). Construction was the only one stronger at -10.0%, with civil engineering surprising to the upside (-7.9%).

Activity continues its upward trend in monthly terms. Industry rose 0.2% m/m (Chart 3), adding eight consecutive months higher, since the reopening of the economy in June. This is positive as available data did not rule out a possible downturn given the deterioration of epidemiological conditions. However, and as we have mentioned before, we still thought industry might have fared better to a new round of lockdowns relative to more exposed sectors, such as services. As a result, industry is close to levels seen in mid-2011 (Chart 4) and about 3.3% lower than in February. Manufacturing declined for the first time since the recovery began at -0.5%. We think this is important as the sector is facing short-term challenges related to bottlenecks in raw materials, highlighting the 3.7% contraction in autos. Fourteen out of 21 categories were negative (Table 2), highlighting clothing (0.9%) and food (-0.4%) to the downside. On a more positive note, beverages surged 6.9%, with a strong performance also in electrical equipment (5.9%) and oil and carbon (5.4%).

Construction strengthened 1.5%, with a volatile performance lately. In contrast to dynamics established since the recovery started, the main driver was civil engineering at 13.7%. Despite this, we believe it is very likely that the sector will moderate strongly again, constrained by austerity measures by the Federal Government. In turn, edification was barely unchanged at 0.1%. Lastly, mining picked up 0.2%, boosted by a rebound in services related to the sector (6.8%) while oil and gas and non-oil were positive for a second month at 0.1% and 0.4%, respectively.

Signs of a steep deceleration in February, with other short-term risks. While today's result remained positive, especially considering a complex backdrop at the beginning of the year, the situation in February turned significantly worse. The evolution of COVID-19 infections was mixed, with a slight deterioration at the beginning of the month, but turning drastically better in the second fortnight, leaving only two states in 'red' according to the traffic light indicator.

However, and most important for industry, electricity blackouts and natural gas shortages were reported in the middle of the month due to extreme cold weather in the south of the US and northern states in our country. Detailing on the blackouts, electric centrals in some Northern Border states were shut down late on February 14th and the first hours of the 15th. From Monday through Wednesday (February 15th to 17th), several issues were reported in the northern and central region of the country, affecting a plethora of industries. Specifically, and to the best of our knowledge, as much as 26 of the 32 states were impacted. By the 18th, CENACE assured that 100% of electricity demand was reestablished. Nevertheless, we had reports that manufacturers were still having issues because of the undersupply of natural gas as late as February 22nd. While this will have a direct impact on utilities, the drag should be modest given its relatively low share within total output.

Nevertheless, the overall effect on activity is likely to be large, given ample disruptions also to construction and manufacturing. This was especially evident for the latter as warned by most automakers, which announced shutdowns until gas supply was reestablished. In this context, vehicle production declined sharply to -28.8% y/y, lowest since May 2020, when we were in the middle of nationwide lockdowns. We should mention that although this was skewed downwards because of the *leap year* effect –one more day in February 2020–, performance was nonetheless impacted meaningfully. There was another negative driver, which is the lack of semiconductors. This has plagued autos and other relevant manufacturing sectors. While problems in this front started impacting auto production in February, industry experts expect distortions to prevail at least until the summer. This is because they expect manufacturing plants in East Asia to resume production at higher capacity until then. Hence, it is likely that a vigorous recovery remains limited while supply is constrained, despite favorable prospects from external demand. Moreover, prices could rise to clear the market. Signals from this could be seen in the US ISM manufacturing, reaching its highest in three years at 60.8pts. Although part of this is due to prices, underlying trends keep supporting a healthy performance abroad that will likely continue helping the sector in Mexico. This is especially relevant given domestic demand weakness, as seen in domestic vehicle sales.

In construction, sentiment figures continue to improve –including business confidence and the aggregate trend indicator–. Nevertheless, we remain cautious as they have not captured some of the swings in recent prints. Some news was positive, including efforts from Mexico City's government to relaunch large-scale projects with the private sector, implementing measures such as expedite permits and other requirements. However, we still believe that activity will be subdued on prevailing weakness in domestic demand –which will probably stay until uncertainty drops sharply and the overall recovery is well underway– and limits on Federal government investment. On mining, weather conditions likely had a very limited impact on oil production, although we do not rule out other distortions. In this respect, we should mention that the main destination for our exports is Texas, which suffered the strongest impact from the bad weather conditions.

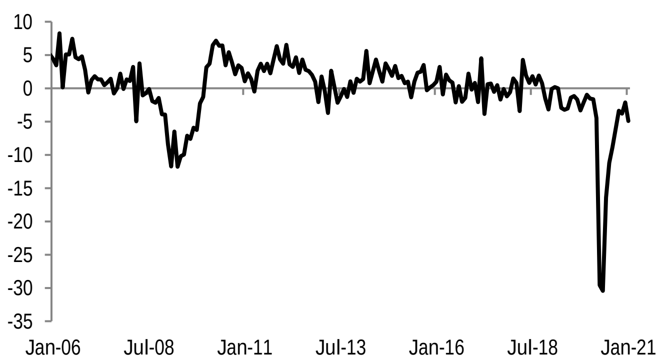
Turning to the medium-term, we still believe the outlook remains favorable. Externally, the US Congress approved this week the US$1.9 trillion stimulus package, which should kick the country's economy into overdrive. As a result, we revised our GDP forecast for Mexico higher for this year. Specifically, manufacturing remains the most leveraged sector to US dynamism. In addition, once the vaccination process gathers steam locally, we could see sentiment bounce back with renewed strength.

Table 1: Industrial production
% y/y nsa

	Jan-21	Jan-20	2020	2019
Industrial Production	-4.9	-1.5	-10.0	-1.7
Mining	-3.3	6.8	-1.1	-4.4
Oil and gas	-3.1	6.6	-0.1	-7.2
Non-oil mining	4.4	2.0	-4.6	-2.8
Services related to mining	-13.0	13.5	-1.1	17.5
Utilities	-4.9	-0.1	-5.3	-0.6
Electricity	-5.8	0.2	-6.0	0.0
Water and gas distribution	-2.0	-0.9	-2.4	-3.0
Construction	-10.0	-8.1	-17.2	-5.2
Edification	-12.3	-6.8	-16.6	-3.0
Civil engineering	-7.9	-18.8	-25.3	-9.7
Specialized works for construction	0.1	-2.5	-11.0	-10.5
Manufacturing	-3.4	-1.3	-10.0	0.6
Food industry	-1.3	0.8	-0.5	2.3
Beverages and tobacco	0.8	0.5	-8.1	3.3
Textiles - Raw materials	-5.2	-16.0	-30.5	-4.1
Textiles - Finished products ex clothing	-3.7	-5.1	-13.9	-3.7
Textiles - Clothing	-28.6	-3.7	-34.6	-3.2
Leather and substitutes	-18.6	-3.4	-34.4	-2.3
Woodworking	-14.4	-1.0	-14.1	0.5
Paper	-4.6	-3.0	-5.1	-0.1
Printing and related products	-14.8	2.9	-16.9	-9.0
Oil- and carbon-related products	15.5	7.3	-8.9	-2.6
Chemicals	-4.2	-1.9	-4.8	-2.2
Plastics and rubber	3.2	-4.2	-9.7	-2.6
Non-metallic mineral goods production	0.7	1.2	-7.7	-0.2
Basic metal industries	-1.1	2.9	-9.0	-2.4
Metal-based goods production	-1.4	-0.9	-10.2	2.8
Machinery and equipment	-1.9	-11.5	-16.8	-1.7
Computer, communications, electronic, and other hardware	7.8	-1.6	-6.1	5.1
Electric hardware	9.8	1.7	-0.9	-1.1
Transportation equipment	-12.3	-2.6	-20.9	1.3
Furniture, mattresses and blinds	-6.1	4.1	-17.5	-3.2
Other manufacturing industries	-7.2	-5.8	-10.1	-4.8

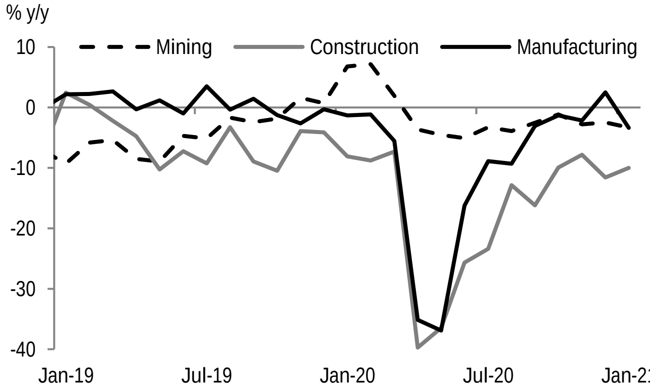
Source: INEGI

Chart 1: Industrial production
% y/y



Source: INEGI

Chart 2: Industrial production by sector
% y/y



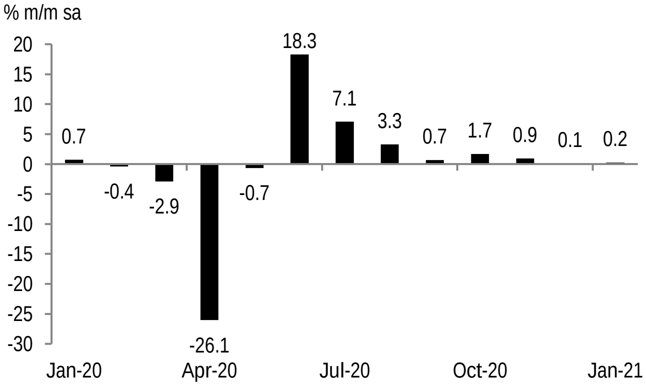
Source: INEGI

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

	% m/m			% 3m/3m	
	Jan-21	Dec-20	Nov-20	**Nov'20**-Jan'**2**1	Oct-Dec**'20**
Industrial Production	0.2	0.1	0.9	2.5	3.9
Mining	0.2	-0.2	-0.2	0.4	1.4
Oil and gas	0.1	0.2	-0.1	0.4	1.2
Non-oil mining	0.4	1.1	-0.5	2.5	4.1
Services related to mining	6.8	-6.6	1.2	-4.3	-7.4
Utilities	-1.7	1.6	-2.1	-1.9	0.1
Electricity	-1.8	1.9	-2.9	-2.6	-0.3
Water and gas distribution	-0.4	-0.3	0.5	0.7	1.4
Construction	1.5	-2.2	2.2	2.7	5.8
Edification	0.1	-5.3	5.2	3.3	7.2
Civil engineering	13.7	-3.5	0.2	3.0	1.0
Specialized works for construction	0.6	3.5	-1.1	4.1	8.1
Manufacturing	-0.5	1.0	0.4	2.6	3.8
Food industry	-0.4	0.5	-0.2	0.6	0.9
Beverages and tobacco	6.9	-7.1	1.1	-1.1	-0.7
Textiles - Raw materials	-2.2	7.9	1.4	8.9	14.3
Textiles - Finished products ex clothing	1.2	2.6	-0.6	2.9	3.8
Textiles - Clothing	-0.9	-4.5	7.6	5.8	11.4
Leather and substitutes	4.4	-0.3	-0.5	7.1	12.6
Woodworking	-6.7	-4.0	2.7	2.6	10.4
Paper	-2.0	-0.4	0.2	0.1	2.9
Printing and related products	-3.2	4.3	4.1	5.1	7.5
Oil- and carbon-related products	5.4	18.0	-14.9	2.6	12.0
Chemicals	-0.6	-0.4	-0.4	-0.1	1.7
Plastics and rubber	-2.9	7.7	-1.9	3.8	6.2
Non-metallic mineral goods production	-0.4	1.4	0.7	2.6	5.0
Basic metal industries	2.4	-0.1	0.5	5.5	10.8
Metal-based goods production	-1.3	1.7	-1.6	1.8	4.3
Machinery and equipment	-0.7	1.5	0.5	5.1	9.0
Computer, communications, electronic, and other hardware	-1.2	6.5	-1.9	3.1	2.0
Electric hardware	5.9	-2.4	1.5	3.7	4.6
Transportation equipment	-3.7	1.6	0.3	1.6	3.0
Furniture, mattresses and blinds	2.7	0.5	-2.5	0.6	2.2
Other manufacturing industries	-2.0	-1.1	2.2	0.9	3.7

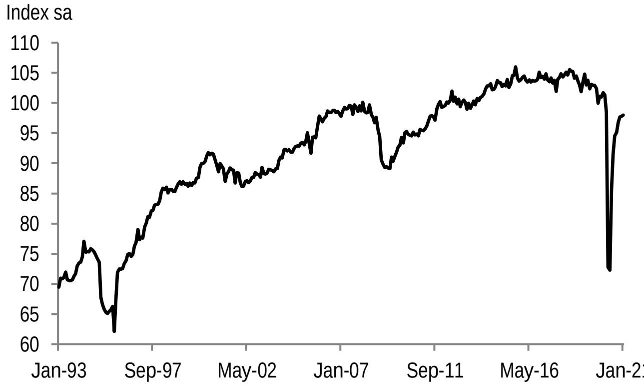
Source: INEGI

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
Eridani Ruibal Ortega	Analyst	eridani.ruibal.ortega@banorte.com	(55) 1103 - 4000 x 2755
Juan Barbier Arizmendi, CFA	Analyst	juan.barbier@banorte.com	(55) 1670 - 1746
Corporate Debt			
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 Aguilar Ceballos	Head of Asset Management	alejandro.aguilar.ceballos@banorte.com	(55) 5268 - 9996
Alejandro Eric Faesi Puente	Head of Global Markets and Institutional Sales	alejandro.faesi@banorte.com	(55) 5268 - 1640
Alejandro Frigolet Vázquez Vela	Head of Sólida Banorte	alejandro.frigolet.vazquezvela@banorte.com	(55) 5268 - 1656
Arturo Monroy Ballesteros	Head of Investment Banking and Structured Finance	arturo.monroy.ballesteros@banorte.com	(55) 5004 - 1002
Carlos Alberto Arciniega Navarro	Head of Treasury Services	carlos.arciniega@banorte.com	(81) 1103 - 4091
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
Lizza Velarde Torres	Executive Director of Wholesale Banking	lizza.velarde@banorte.com	(55) 4433 - 4676
Osvaldo Brondo Menchaca	Head of Specialized Banking Services	osvaldo.brondo@banorte.com	(55) 5004 - 1423
Raúl Alejandro Arauzo Romero	Head of Transactional Banking	alejandro.arauzo@banorte.com	(55) 5261 - 4910
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