Industrial production – A slight bump in the road to recovery in April

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- **Industrial production (April): 36.6% y/y nsa; Banorte: 38.1%; consensus: 37.6% (range: 34.0% to 44.5%); previous: 1.7%**
- **This is a new historical high, significantly skewed to the upside due to a very favorable base effect, recalling that the same period of 2020 was the first month of strict lockdowns. With seasonally adjusted data, activity grew 35.7% y/y**
- **In sequential terms, industry fell 0.2% m/m, breaking with 10 positive months. This was a result of declines in manufacturing (-0.5%) and construction (-0.3%). With this, activity stands 2.7% below February 2020, closer to pre-pandemic levels**
- **In our view, industrial activity is facing a complicated balance between a plethora of supply chains issues but compensated by vigorous demand levels. All in all, we believe industry remains fundamentally robust**
- **Despite the contraction, today's print adds some upside risks to our call of 23.1% y/y growth for this sector in 2Q21, in line with the view of higher dynamism despite lingering risks**

Industry increases strongly in April given distortions from base effects. The indicator reached 36.6% y/y (see Chart 1), below both consensus (37.6%) and our forecast (38.1%). This is a new historical high, significantly skewed to the upside due to a very favorable base effect, recalling that the same period of 2020 was the first month of strict lockdowns. This effect will likely be even greater in May, remembering that construction and manufacturing (*e.g.* autos) were not catalogued as 'essential' until June. In this respect, these sectors surged to 45.1% and 52.0%, in the same order (see Chart 2). On the other hand, mining (5.5%) and utilities (-3.1%) were more modest, recalling that in the first case, the oil sector kept operating without restrictions. We should also consider distortions from the *Holy Week* holiday, which happened during the first days of the period. Correcting for the latter with seasonally adjusted data, activity grew 35.7% y/y, stronger relative to the 34.5% estimated by INEGI in its *Timely Indicator of Economic Activity*. For more details, please refer to Table 1.

Modest sequential decline after a sizable pickup in March. Abstracting from the abovementioned distortions, industry fell modestly, at -0.2% m/m (Chart 3). With this, activity broke 10 consecutive months of gains and stands 2.7% lower than in February 2020, before the pandemic (Chart 4). In our view, performance may have been negatively impacted by the previous month's strength (+0.7%), considering that overall conditions remained positive. Among them, we highlight better COVID-19 dynamics, helping both directly –*e.g.* with job creation in all main sectors–, as well as due to its positive effect on consumer and business confidence. By sectors, we highlight manufacturing (-0.5%), which apart from its previous uptick, is still facing some growth limitations (scarcity of some raw materials, delays in goods' deliveries.

Specifically, the auto sector declined 2.2%, with weakness also in textiles excluding clothing (-13.2%) and furniture (-23.2%), all of them vulnerable to the lack of raw materials. Moreover, oil and carbon fell strongly (-23.2%), recalling that the Minatitlan refinery caught fire at the beginning of the month. On the contrary, among those growing we saw electrical equipment (3.8%), chemicals (1.3%) and food (0.4%), as shown in Table 2.

Construction also contracted at the margin (-0.3%), albeit with an upward revision for March. Civil engineering backtracked (-4.1%), albeit only after increasing 6.0% in the previous month, partially signaled by the federal government's physical investment data. Nevertheless, we are cautious on the latter, as its correlation with activity is low due to different accounting methods. We believe it could have improved ahead of the midterm election. On the other hand, edification was more modest (-0.6%), reinforcing some signals of greater caution.

Lastly, mining rebounded 1.0%) after the 3.0% fall of the previous period. Despite Pemex data on oil and gas production decelerated modestly, the oil sector was up at the margin (0.4%). On the other hand, non-oil was stronger (1.8%), with a relatively modest acceleration given accumulated gains. Moreover, related services were stronger, at 6.1%.

A positive outlook remains despite prevailing risks. In our view, today's figures were not that negative despite the month's sequential contraction, Even accounting for this. we see some upside risks to our forecast of 23.1% y/y growth industry for 2Q21. In this respect, the IMEF manufacturing indicator improved to 52.3pts in May, with a good pickup in 'new orders' and 'production'. Nevertheless, we are cautious as *Markit's* PMI for the sector showed less orders and exports, with: (1) Affected margins due to a steep increase in various input costs, with little room to pass them on to consumers; and (2) a strong deterioration in supplier's delivery times. This contrasts with other indicators, such as the ISM manufacturing in the US which suggests that external demand remains strong, with export and import orders gaining ground. We maintain our forecasts given somewhat mixed signals, believing that the sectors most integrated with North American trade remain supported and will keep showing good dynamics.

In this backdrop, we are still seeing reports about issues in the auto sector. Among them, at least Ford and Nissan were added to the list of automakers with technical stoppages in May (along VW in June) due to the scarcity of chips. On the contrary, General Motors said they will resume operations in their Coahuila and San Luis Potosí plants. Alberto Bustamante, foreign trade director for the *National Auto parts Industry* (INA, in Spanish), stated that between January and May this year around 212,874 vehicles were not produced in our country due to this problem, of which 77,029 correspond to the latter month. He also said that disruptions will probably be observed at least until June, hoping that, starting in July, these issues will gradually start to be resolved for a full normalization by December.

Given this situation, the US administration announced plans this week to alleviate supply chain bottlenecks. Among other measures, a special task force has been created to find solutions at least for semiconductors, 'high capacity' batteries for electric cars, pharmaceuticals and 'rare earth' metals, among others.

Moreover, the *Mexican Association of Vehicle Distributors* (AMDA, in Spanish) increased their vehicle sales forecast to 1.07 million units this year (12.7% y/y from 10.6% previously) on the back of more economic dynamism. Although these are positive news, the problems are quite complex, and in our view, could continue limiting a stronger rebound of the auto sector.

On the other hand, a faster pace of vaccinations, along plans to accelerate their application at the country's northern border, are favorable as they diminish the risk of new restrictions due to a higher number of cases. Import substitution from China (with trade tensions with the US still in place) and greater certainty because of the USMCA are also helping, particularly the export-oriented and *maquiladora* industries. In oil and carbon, we've had some marginally positive developments. Among them, the government of the state of Veracruz informed at the beginning of May that the Minatitlán refinery would soon be operating normally, following a fire at the beginning of April. This would be before expectations, with President López-Obrador saying that gasoline production was back online in said month.

Progress on fighting the virus will likely induce greater dynamism in other sectors, such as construction. In this sense, business confidence and the aggregate trend indicators for this sector remain on the upside. Francisco Solares, President of the *Mexican Construction Industry Chamber* (CMIC, in Spanish) signed an agreement with Cemex to support SMEs through preferential conditions for the purchase of materials, among other measures. An additional factor that could be positive for the rest of the year is the possibility of more dynamism after the midterm elections. On this, President López-Obrador stated that they will 'hurry up' in the construction of key government projects (*e.g.* the Dos Bocas refinery, the Felipe Angeles international airport, the Mayan Train, to name some of them). We will keep watching this sector closely given its potential indirect effect on other domestic sectors.

In mining, the oil sector remains limited. Apart from lingering uncertainty, we will watch closely the upcoming hurricane season given very challenging weather conditions so far this year. In this respect, Pemex has started to kickstart procedures designed to face potential problems due to this factor. In non-oil, commodity prices' strength has continued, which could keep supporting this subsector.

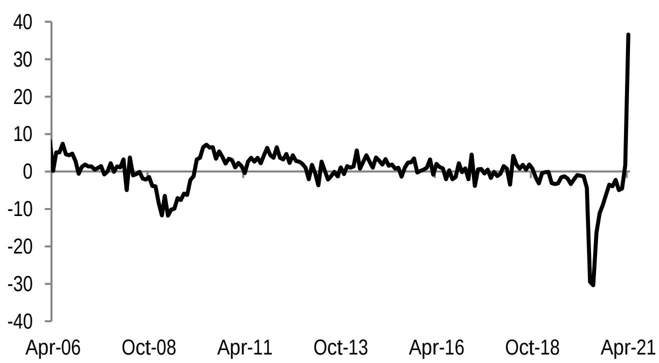
All in all, we reiterate our positive view despite some risks. We believe the latter could mean some headwinds to the pace of the recovery but will not result in a renewed decline. Specifically, because of good demand levels –mainly from the US– and stronger confidence on steps forward in the fight against COVID-19.

Table 1: Industrial production
% y/y nsa

	Apr-21	Apr-20	Jan-Apr'**21**	Jan-Apr'**20**
Industrial Production	36.6	-29.5	4.8	-9.0
Mining	5.5	-3.7	-0.9	3.0
Oil and gas	-1.4	3.0	-2.4	4.5
Non-oil mining	43.7	-31.6	10.5	-7.2
Services related to mining	-1.0	13.8	-9.2	12.8
Utilities	-3.1	-2.9	-5.3	-0.6
Electricity	-5.4	-2.4	-7.0	-0.1
Water and gas distribution	5.6	-4.8	0.6	-2.3
Construction	45.1	-39.8	2.1	-15.7
Edification	59.0	-46.2	1.2	-16.2
Civil engineering	-0.1	-18.4	-2.6	-16.6
Specialized works for construction	49.8	-32.4	11.2	-12.0
Manufacturing	52.0	-35.0	8.8	-10.3
Food industry	2.9	-0.4	0.2	1.2
Beverages and tobacco	57.4	-38.3	12.3	-11.7
Textiles - Raw materials	298.3	-76.1	19.1	-28.4
Textiles - Finished products ex clothing	124.0	-61.1	14.6	-16.0
Textiles - Clothing	229.2	-76.6	-1.3	-24.2
Leather and substitutes	439.2	-85.7	6.5	-27.3
Woodworking	51.8	-38.0	6.5	-13.0
Paper	20.1	-7.6	2.0	-3.0
Printing and related products	46.1	-47.2	3.3	-11.0
Oil- and carbon-related products	3.6	-5.0	21.9	-5.3
Chemicals	2.0	-6.3	-4.3	-1.3
Plastics and rubber	63.4	-35.3	16.1	-11.1
Non-metallic mineral goods production	70.4	-39.1	13.2	-8.6
Basic metal industries	29.7	-22.2	7.3	-7.7
Metal-based goods production	69.5	-39.3	15.8	-10.2
Machinery and equipment	66.4	-41.8	14.6	-18.4
Computer, communications, electronic, and other hardware	40.6	-26.6	14.2	-9.1
Electric hardware	43.9	-10.6	18.6	-1.3
Transportation equipment	584.6	-86.4	20.0	-25.0
Furniture, mattresses and blinds	118.5	-64.7	17.9	-19.6
Other manufacturing industries	34.1	-31.5	4.1	-11.3

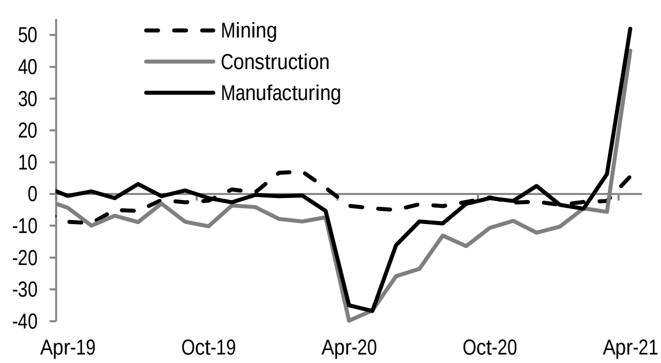
Source: INEGI

Chart 1: Industrial production
% y/y



Source: INEGI

Chart 2: Industrial production by sector
% y/y



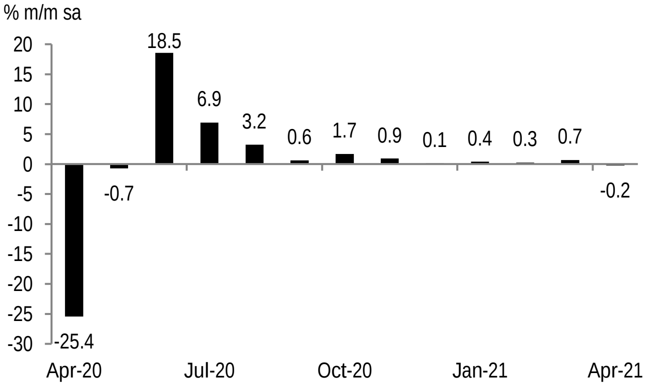
Source: INEGI

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

	% m/m			% 3m/3m	
	Apr-21	Mar-21	Feb-21	Feb-Apr'**21**	Jan-**Mar'21**
Industrial Production	-0.2	0.7	0.3	1.0	1.2
Mining	1.0	-3.0	3.0	1.7	1.6
Oil and gas	0.4	-2.0	3.0	2.0	1.7
Non-oil mining	1.8	-7.2	2.1	-1.9	-0.5
Services related to mining	6.1	-4.4	6.0	7.6	5.7
Utilities	-1.0	5.0	-4.2	-2.0	-2.5
Electricity	-1.9	6.3	-5.4	-2.8	-3.3
Water and gas distribution	1.7	0.6	0.1	0.8	0.1
Construction	-0.3	0.0	2.6	3.4	3.5
Edification	-0.6	-1.6	3.7	1.4	1.6
Civil engineering	-4.1	6.0	1.3	7.7	5.5
Specialized works for construction	2.8	0.6	-0.7	3.0	3.9
Manufacturing	-0.5	3.0	-2.2	-0.5	-0.3
Food industry	0.4	0.5	0.1	0.5	0.2
Beverages and tobacco	0.2	-0.9	-2.1	-0.7	0.4
Textiles - Raw materials	1.2	5.3	-2.7	2.8	4.0
Textiles - Finished products ex clothing	-13.2	3.2	2.7	1.3	4.5
Textiles - Clothing	-1.3	8.9	0.4	4.0	2.3
Leather and substitutes	-3.4	3.0	-3.4	0.1	2.4
Woodworking	-2.1	-1.8	10.2	0.6	-4.4
Paper	9.1	0.6	0.2	2.3	-1.6
Printing and related products	-17.8	1.0	6.7	0.6	6.4
Oil- and carbon-related products	-23.2	14.7	-2.2	7.7	15.2
Chemicals	1.3	0.2	-2.7	-2.7	-2.8
Plastics and rubber	-0.2	4.1	-2.6	1.0	1.5
Non-metallic mineral goods production	-1.2	3.7	-1.5	0.7	1.0
Basic metal industries	0.5	3.0	-3.1	0.5	1.4
Metal-based goods production	-3.7	4.6	1.0	2.7	1.9
Machinery and equipment	-6.3	8.9	-1.0	3.2	3.8
Computer, communications, electronic, and other hardware	-0.1	0.3	-0.1	1.5	3.1
Electric hardware	3.8	4.5	-0.7	6.7	5.9
Transportation equipment	-2.2	10.8	-9.5	-5.6	-5.5
Furniture, mattresses and blinds	-11.7	-1.1	3.1	0.5	4.3
Other manufacturing industries	-0.4	-1.6	2.9	-0.1	-0.7

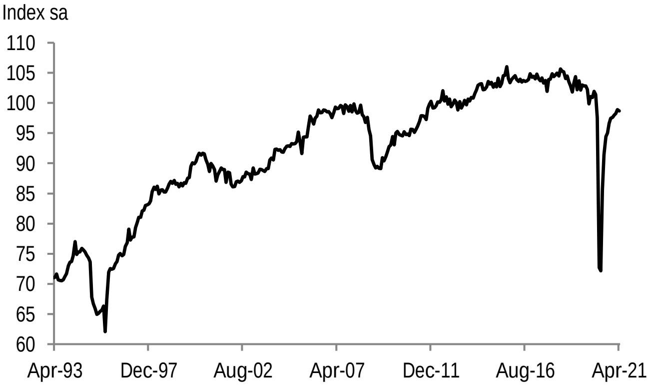
Source: INEGI

Chart 3: Industrial production
% m/m sa



Source: INEGI

Chart 4: Industrial production
Index sa



Source: INEGI

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