IGAE – The recovery gathered pace in May, especially in services

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- ***Global Economic Activity Indicator*** **(May): 25.1% y/y; Banorte: 23.2%; consensus: 23.9% (range: 21.9% to 25.7%); previous: 22.3%**
- **As in April, the annual rate is heavily skewed upwards on base effects due to the pandemic, with very high restrictions during this period in 2020. With seasonally adjusted figures it grew 25.3% y/y, above INEGI's *Timely Indicator of Economic Activity***
- **By sector, industry stood at 36.4% y/y, services picked up 21.5% and primary activities increased 10.3%**
- **In monthly terms, the economy grew 0.6%, accelerating at the margin. All sectors advanced, with industry up 0.1% and services at 0.8%. Primary activities rebounded 8.4%, more than compensating for the -3.2% in April**
- **We expect Friday's 2Q21 preliminary GDP to have accelerated to 1.6% q/q, with risks skewed to the upside after today's results. We maintain our full-year forecast at 6.2% despite some headwinds to industry and the new wave of COVID-19 cases worldwide**

Economic activity up 25.1% y/y in May. This was higher than consensus (23.9%) and our forecast (23.2%). As in April, the annual rate is heavily skewed upwards on base effects due to the pandemic, with very high restrictions during this period in 2020. With seasonally adjusted figures, it grew 25.3% y/y, above the mid-point in INEGI's *Timely Indicator of Economic Activity*. Back to original figures, industry stood at 36.4% y/y, services picked up 21.5% and primary activities increased 10.3%, as shown in (Chart 2). Within services, the wide differences observed in April remain in place (Table 1), with lodging (183.9%) and transportation (38.2%) among the highest, coupled with retail (52.4%) and wholesales (41.7%). Given last year's lockdowns, all categories were positive, albeit less so for essential ones such as financial (2.9%), government (3.3%), and education and healthcare (5.8%). The primary sector surprised us to the upside even as difficult weather conditions likely kept challenging volumes.

The recovery consolidated in May. The economy grew 0.6% m/m, accelerating relative to April, which in turn was revised to +0.2% from -0.2% previously. In this respect, all major sectors grew (see Table 2). Therefore, results suggest that the recovery consolidated, with overall activity stronger for a third month in a row. By sector, services (0.8%) outperformed industry (0.1%). In our view, this is consistent with better COVID-19 conditions, also reflected in mobility data and the 'traffic light' indicator, among other figures. Specifically, more socially-intensive sectors such as lodging (5.4%) and transportation (2.2%) advanced even after relatively strong gains in April. In turn, this is consistent with stronger hotel occupancy rates and air passenger traffic, which went up despite adverse seasonality. In contrast, recreational fell 2.4% despite the 2.5% contraction of the previous month.

Retail sales were stable, which was lower than the +0.6% in the sector's stand-alone report. We also highlight strength in financial (1.7%) and government (0.9%), possibly signaling also some strength in domestic demand.

Industry advanced 0.1% (Chart 3), with construction (2.0%), mining (1.0%) and utilities (1.3%) helping compensate for the -0.7% in manufacturing. As stated before, we think goods' producers remain in a tough position, with supply chain issues impacting key subsectors such as transportation (*e.g.* autos), appliances and other electric and electronic goods, despite elevated demand.

Lastly, the primary sector grew 8.4% m/m, more than compensating for the -3.2% seen in April. Apart from the usually elevated volatility in these figures, it is our take that production growth has been affected by harsh weather conditions and higher input prices (*e.g.* food, energy) for livestock, among other factors. Although the former seems to have lessened since late June and could also help moderate the increase in grain prices (as flagged by *Bloomberg's* BCOMGR subindex, comprised of corn, soybeans and wheat), the overall situation remains difficult.

All in all, activity is close to levels seen in October 2017 (Chart 4), showing that there is still ample room left to recover despite a rebound that has been stronger than anticipated at the beginning of the year.

A better than expected report, posing upside risks to our 2Q21 GDP estimate of 19.8% y/y (+1.6% q/q). This week's highlight in the economic agenda will be the 2Q21 preliminary GDP, to be released on Friday. Our forecast stands at 19.8% y/y, up 1.6% q/q which would be stronger than the 0.8% seen in the first quarter. After today's IGAE, we see risks to our call as skewed upwards. We are also factoring in: (1) Trade balance data for June published at the same time of this release, in which total exports grew 0.2% m/m and imports 0.3%, albeit with mixed results in the non-oil sector; and (2) a better than expected unemployment rate, favorable despite some signs of difficulties for the labor market ahead. Moreover, our analysis of other data for the month suggests growth continued, although with sector differences prevailing. Industry is poised to a sequential fall, mainly because of manufacturing (especially auto production), as well as a setback in construction. On the other hand, services would have recovered further despite a more difficult backdrop in terms of new COVID-19 cases. Regarding this, we highlight that mobility has been resilient so far. This is key as it is likely more correlated with actual dynamism relative to new cases. Considering broader indicators, IMEF's PMIs signaled a moderation in both manufacturing and non-manufacturing, albeit with both still in expansion.

Looking ahead, the acceleration in cases due to virus' variants –both locally and abroad– is the most important risk to keep monitoring. It is our take that, even if strict lockdowns are not imposed again, as suggested by federal authorities, some added precautions are likely if the trend keeps going up. Moreover, we cannot rule out higher uncertainty that affects consumer and business confidence, which in turn may moderate demand. Although the 'traffic light' indicator has been modified to avoid strict lockdowns, vaccinations have continued, and people's fatigue is high, we cannot rule out an impact.

Specifically, our main concern is that incipient growth in sectors such as tourism (related to lodging, recreational and transportation, among others) is halted prematurely.

The other main issue is the scarcity of raw materials, as well as some trade disputes. This is especially the case for manufacturing. On the former, recent news signal some progress, but the fact is that there is still a long way for a complete normalization. Among them, CEOs of automakers such as GM and Ford have recently stated that ongoing work by the US administration in this regard is lessening the squeeze from the undersupply of semiconductors. On the second factor, labor and regional content disputes in the framework of USMCA may be increasing uncertainty to production and investment plans despite the regional advantage that the treaty provides, particularly given persistent tensions between the US and China.

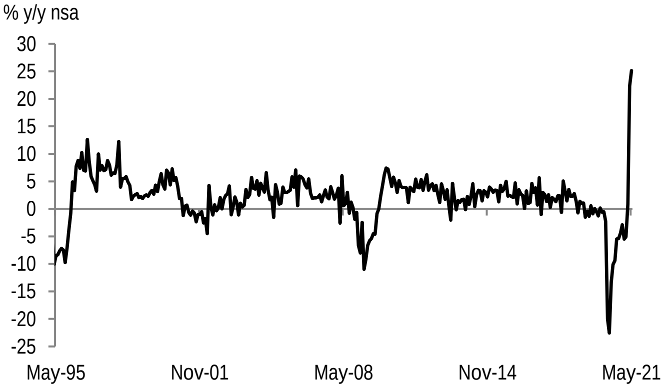
Overall, we maintain our call of full-year GDP at 6.2% in 2021 and 3.0% in 2022. It is our take that the Mexican economy is poised to keep benefiting from stimulus measures, mainly in the US, although risks remain high and could affect performance if they keep building up.

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

	y/y nsa				y/y sa	
	May-21	May-20	Jan-May'21	Jan-May'20	May-21	May-20
Total	25.1	-22.6	6.2	-9.3	25.3	-21.5
Agriculture	10.3	-1.0	4.1	-2.0	10.0	-1.3
Industrial production	36.4	-30.4	9.9	-13.3	36.6	-29.3
Mining	8.9	-4.5	0.9	3.2	9.2	-4.3
Utilities	8.7	-12.3	-2.5	-3.8	8.8	-12.1
Construction	45.0	-36.6	8.5	-18.7	45.9	-36.2
Manufacturing	48.0	-36.8	15.0	-16.0	48.3	-35.2
Services	21.5	-20.0	4.6	-7.7	21.6	-18.9
Wholesale	41.7	-35.1	12.9	-13.4	41.7	-31.9
Retail	52.4	-36.2	13.3	-14.5	52.1	-34.1
Transport	38.2	-30.6	3.9	-11.9	38.2	-29.7
Financial services	2.9	-0.6	0.0	0.1	2.7	-0.8
Professional services	7.7	-9.3	5.0	-4.0	7.2	-8.6
Education and healthcare services	5.8	-2.6	3.0	-1.7	5.8	-2.2
Recreational services	17.5	-34.0	-4.7	-14.8	18.0	-33.6
Lodging services	183.9	-72.0	2.6	-34.9	179.8	-72.5
Government services	3.3	0.9	-1.3	4.1	3.3	1.0

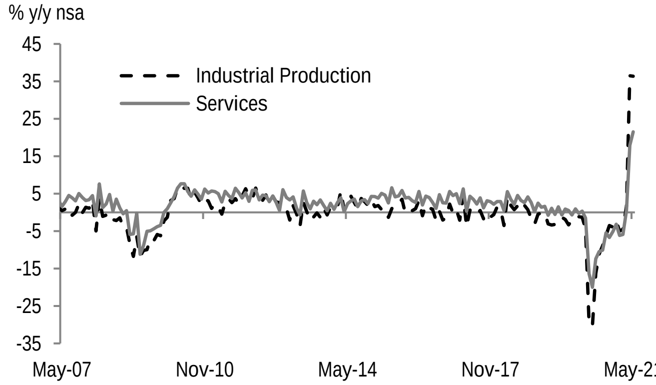
Source: INEGI

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



Source: INEGI

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



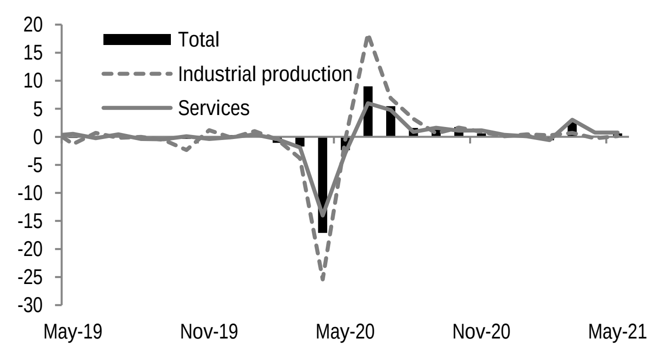
Source: INEGI

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

	% m/m, sa			% 3m/3m sa	
	May-21	Apr-21	Mar-21	Mar-May'21	Feb-Apr'21
Total	0.6	0.2	2.7	2.7	1.6
Agriculture	8.4	-3.2	0.8	3.2	1.2
Industrial production	0.1	-0.3	0.7	0.9	1.0
Services	0.8	0.8	3.0	3.4	1.9

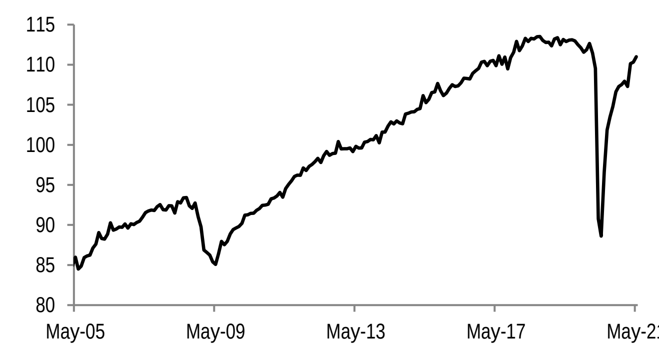
Source: INEGI

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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