IMEF's PMI surveys – Signals of headwinds into the third quarter

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- ***IMEF* Manufacturing PMI (Jul, sa): 52.2pts; Banorte: 51.9pts; consensus: 51.9pts; previous: 52.2pts**
- ***IMEF* Non-manufacturing PMI (Jul, sa): 52.9pts; Banorte: 53.0pts; consensus: 53.0pts; previous: 54.0pts**
- **The effects of worsening epidemiological conditions seem evident in both indicators, especially in 'new orders' and 'production'. Despite of this, all subcomponents remain in expansion territory**
- **'Inventories' and 'deliveries' increased again in manufacturing, in our view providing signals of a gradual normalization in the sector**
- **In non-manufacturing we saw a mixed performance in the rest of the components, with 'employment' confirming the adverse impact of the pandemic**
- **These indicators are consistent with our view of a moderation in GDP growth into 3Q21, albeit still in recovery**

***IMEF's* PMIs more modest at the margin in July.** The manufacturing indicator reached 52.2pts, unchanged relative to the previous month, although with the latter revised marginally down, from 52.4pts. Non-manufacturing stood at 52.9pts, with a stronger correction lower from June (-1.1pts). In our view, part of this is "natural", in the sense that a slowdown in growth is more likely as the recovery matures. Nevertheless, we think higher uncertainty driven by the acceleration of COVID-19 cases may have made businesses and consumers more cautious at the margin. The latter would be particularly relevant for non-manufacturing. Moreover, we believe this was mostly reflected in both components, primarily in 'production' and 'new orders'. Nevertheless, the indicators and all their subcomponents stayed in expansion (above the 50pts threshold), suggesting that the recovery continued.

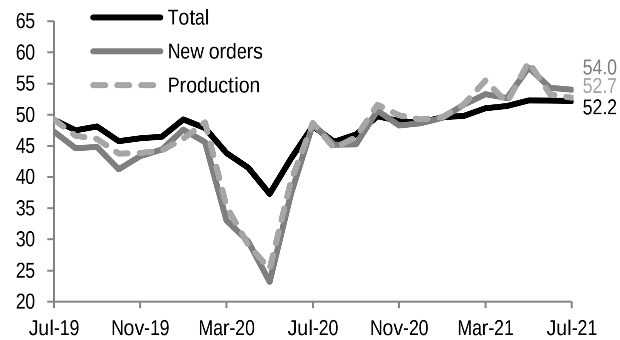
Signals of a gradual normalization in manufacturing. As already mentioned, this indicator reached 52.2pts, unchanged relative to revised figures for June. Performance was somewhat mixed, albeit with slight moves in most components. Specifically, the only one that accelerated meaningfully was 'inventories', up 2.8pts. Nevertheless, it is important to recall that the interpretation could be difficult as it is based on a ratio of sales to inventories. Considering the slight uptick in 'deliveries' (+0.3pts), this signal could be positive at the margin and could even point to the incipient start of a normalization in the sector, which has been highly affected by the scarcity of raw materials. In this backdrop, President Biden's advisors said they expect the undersupply of semiconductors to ease gradually during 3Q21 as chip manufacturers have compromised on this. Nevertheless, it is still soon to evaluate this, so we will focus on the dynamics of these two categories in coming months. In 'employment', its modest 0.1pts uptick is relatively favorable, probably as workers have not been furloughed despite technical stoppages due to supply chain issues –such as in factories by Audi, VW and Nissan among automakers.

IMEF's manufacturing indicator
Seasonally adjusted figures

	Jul-21	Jun-21	Difference
Manufacturing	52.2	52.2	0.0
New orders	54.0	54.3	-0.3
Production	52.7	53.3	-0.5
Employment	51.9	51.8	0.1
Deliveries	51.3	51.0	0.3
Inventories	54.2	51.4	2.8

Source: IMEF

IMEF's PMI manufacturing indicator
Seasonally adjusted figures



Source: Banorte, IMEF

Non-manufacturing showed a relevant decline. This indicator stood at 52.9pts from 54.0 in June –revised marginally upwards, by 0.2pts. Both 'new orders' (-1.5pts) and 'production' (-4.3pts) fell. Nevertheless, the latter's adjustment was strong as it was the most sizable since the start of the pandemic (April 2020). On the other hand, 'employment' also deteriorated slightly, down 1.1pts. In this backdrop, the main driver behind the deceleration seems to have been worsening epidemiological conditions. Cases rose meaningfully as part of the 'third wave'. This happened despite: (1) Mobility levels stayed broadly unchanged relative to June; and (2) the 'traffic light' indicator was modified to allow for more activities to stay opened at every stage. Regarding the latter, we do not rule out that people are still modifying their behavior based on previous guidelines, which are indeed reflecting a more difficult environment. In addition, we could have had an adverse effect from persistent price increases within services such as in restaurants, in turn inducing some people not to visit these places.

IMEF's non-manufacturing indicator
Seasonally adjusted figures

	Jul-21	Jun-21	Difference
Non-manufacturing	52.9	54.0	-1.1
New orders	56.3	57.7	-1.5
Production	52.3	56.5	-4.3
Employment	50.2	51.3	-1.1
Deliveries	51.4	49.2	2.2

Source: IMEF

These indicators are consistent with our view of a moderation in GDP growth into 3Q21, albeit still in recovery. Today's results are consistent with our view that the recovery will keep going, albeit at a more modest pace. Specifically, we think uncertainty about the outlook may be on the rise. This is not only because of COVID-19, but also on a myriad of factors –both domestically and abroad– that may dampen optimism about the short-term path of the recovery. Despite of the latter, we continue seeing growth of 0.7% and 0.4% q/q in the third and fourth quarters of this year, respectively.

As mentioned last month, we are watchful of the possibility of a renewed slowdown in socially intensive sectors such as tourism (also related to lodging, transportation, and entertainment, among others). This would be very negative news as an incipient recovery has taken hold in the last few months, mostly because of a renewed inflow of foreign tourists.

On a more positive note, the pace of vaccinations has gathered steam again recently, which in our view may help support confidence levels. These are only a few of the challenges still posed by the pandemic. Although services have surprised us to the upside since the beginning of the year –in part because of a stronger performance in fundamentals for consumption, such as employment and remittances–, we should mention that lingering risks are still present.

In manufacturing, we also see potential issues that could keep limiting growth. Apart from worldwide problems in supply chains and higher commodities prices, tensions between the US and Mexico regarding USMCA have risen. It is our take that these may delay, but not cancel completely, future growth. In this respect, one key aspect is that demand remains very vigorous, especially from the US. Moreover, it is our take that some of the problems about the implementation of USCMA will be resolved through the instances established for this purpose. Meanwhile, tensions with China are on the rise on several fronts, a situation that maintains Mexico as more attractive in relative terms.

All in all, we think GDP is still facing a difficult and uncertain environment ahead, albeit not high enough to mean a new decline in activity, which would reverse some of the accumulated gains since the reopening started, back in June 2020.

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