Industrial production – Positive surprise in August, lifted by construction

October 12, 2021

www.banorte.com
@analisis_fundam

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 (August): 5.5% y/y nsa; Banorte: 3.9%; consensus: 4.1% (range: 2.5% to 6.0%); previous: 7.3%**
- **The period had a positive calendar effect, as there was one more working day in the annual comparison. With seasonally adjusted figures, industry grew 5.2% y/y**
- **In sequential terms, industry picked up 0.4% m/m after the 1.2% seen in July. Weakness was concentrated in mining, down 0.1% and in contraction for ah third month in a row. Meanwhile, construction (1.9%) and manufacturing (0.2%) surprised to the upside**
- **With this, activity stands 2.0% below February 2020, before the pandemic started. Industry remains affected by a series of factors that are limiting the recovery, even after considering US relative strength**
- **We still see downside risks due to both global and local headwinds that will likely keep limiting a more forceful rebound of the sector**

Industry above expectations in August. The indicator reached 5.5% y/y (see Chart 1), higher than consensus (4.1%) and our 3.9%. The base effect keeps becoming less favorable at the margin, which was partially compensated by a positive calendar effect as there was one more working day in the annual comparison. In this sense, growth was at 5.2% y/y with seasonally adjusted figures, also better than INEGI's *Timely Indicator of Economic Activity*. Differences prevail in annual terms across sectors, with construction (8.7%) and manufacturing (6.6%) still higher, as seen in Chart 2. Meanwhile, both mining (1.9%) and utilities (-4.8%) remain more modest. For further details, please refer to Table 1.

Relative strength considering a challenging backdrop. Industry grew 0.4% m/m, extending the +1.2% of the previous month (Chart 3). In our view, this was quite favorable considering that supply disruptions are still a very relevant headwind, as well as additional negative drivers such as: (1) Worsening pandemic conditions, both globally and locally; (2) increased raw materials' costs; and (3) domestic idiosyncratic factors. With today's result, activity stands 2.0% below February 2020, used as a pre-pandemic standard, but also -6.4% relative to the all-time high seen in September 2015 (Chart 4). Inside, two out of the four sectors were lower, highlighting mining at -0.1%. Weakness was centered in oil (-2.4%), impacted by a fire on August 22nd in a rig at the *Ku-Maloob-Zaap* complex which knocked production through the end of the month in around 125 fields (with progressive reopening in the last week of August). Meanwhile, the non-oil sector (1.1%) and services related (5.7%) were more resilient despite a challenging base effect in the previous month, still likely supported by high prices which in turn incentivize production.

Manufacturing were higher by 0.2% after July's +1.6%. Despite the possibility of higher dynamism due to booming demand, the sector remains affected by supply shortages. This is especially true in transportation equipment (-0.9%), which is at similar levels than those seen just in in the aftermath of the first pandemic lockdowns. Weakness was also observed in textiles excluding clothing (-10.2%) and machinery and equipment (-0.9%), as seen in Table 2. To the upside, we highlight electronic equipment (5.7%), textile inputs (1.8%) and chemicals (1.4%). All in all, 11 out of the 21 subsectors contracted in the period.

Construction came in at +1.9%, extending the +0.9% of the previous month and the most positive surprise among sectors. These two prints were strong enough to make up for the -1.9% in June. Edification gained 1.9%, with works related to the sector up by 1.1%, benefiting from a base effect. On the other hand, civil engineering was again the highest at 3.2%, which was very positive considering recent gains and the timing of the electoral period –which results in some restrictions to spending–.

The outlook for the remainder of the year and into 2022 remains clouded. Today's positive surprise is quite welcome, particularly in the midst of a persistently challenging backdrop according to most reports, with many of the headwinds likely to prevail more time than previously anticipated. From our assessment, the main issue continues to be the lack of raw materials for several producers. This is reflected by surveys like *Markit*'s PMIs, with businesses quoting this both in the US and Mexico. For example, research from the *Susquehanna Financial Group* (as reported by Bloomberg) affirms that wait times for semiconductors by automakers rose in September to an all-time high of 22 weeks. As if there were no issues before, the last deterioration came after power outages in China due to the scarcity and high prices of energy, mainly gas. This is also likely affecting a plethora of goods given the high integration of global supply chains and the important role that China plays in it. Signals of weakness prevail, such as those stemming from IMEF's manufacturing indicator which fell to contraction in September for the first time in six months. Confirming this, auto production totaled 208.1 thousand units, lowest since the April-May 2020 lockdown.

One of the few bright spots is the improvement in epidemiological conditions both locally and in the US. This could result in renewed activity in some sectors, boosting demand. However, COVID-19 remains a relevant risk, particularly given the approach by some countries –such as China– which impose harsh lockdowns at the first signs of an outbreak. This could induce even more disruptions if closures affect industrial centers or ports, as in recent months. At a domestic level, tensions on USMCA continue as the consultation process on the auto sector continue. Meanwhile, blockades in Michoacán have been more intermittent in past weeks, remembering that President López Obrador called for their end. However, we do not rule out further blockades later in the year and into 2022 as these remain a key bargaining tool.

In mining, Pemex stated that disruptions from the fire only affected operations in August, which should benefit figures sequentially in September. Nevertheless, we believe the sector keeps facing structural challenges. In addition, the situation on the *Zama* oilfield is still unclear after a dispute notice was introduced in early September by private producer *Talos Energy*. As such, uncertainty also prevails for these players. On a positive note, energy prices kept rising, which at the margin could give Pemex some breathing room in terms of its financial position. Meanwhile, we expect the non-oil sector to remain resilient, with more room to grow given booming demand for raw materials.

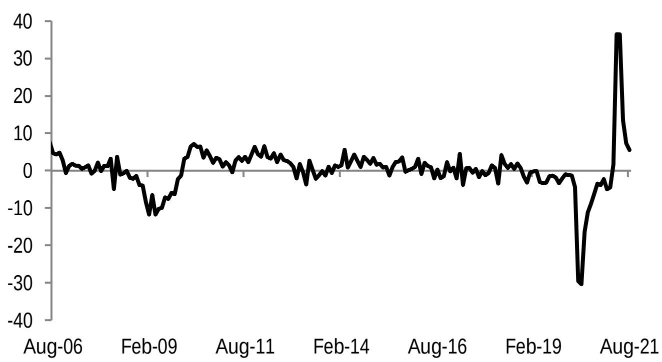
Lastly, in construction, there are some positive signals into 2022 from the *Fiscal Budget*, as the amount allocated to public investment is the largest since 2009. This mainly focuses on the administration's priority projects (*e.g.* Santa Lucía Airport, Mayan Train) and works surrounding it, possibly resulting in a limited spillover effect. However, on a shorter-term basis, we also believe risks have increased, mainly due to the rising cost of raw materials. According to several reports, in some cases works have had to stop as projects become unprofitable. As such, we will remain vigilant about price dynamics and other sector drivers.

Table 1: Industrial production
% y/y nsa, % y/y sa

	nsa				sa	
	Aug-21	Aug-20	Jan-Aug'**21**	Jan-Aug'**20**	Aug-21	Aug-20
Industrial Production	5.5	-8.9	9.4	-12.9	5.2	-8.1
Mining	1.9	-3.9	1.8	-0.6	1.7	-4.1
Oil and gas	-1.5	-2.3	-0.3	1.0	-1.5	-2.2
Non-oil mining	1.5	-0.9	11.5	-9.0	1.5	-1.1
Services related to mining	26.2	-18.1	-0.8	5.5	24.3	-20.5
Utilities	-4.8	-3.4	-0.8	-5.0	-4.9	-3.5
Electricity	-6.6	-3.7	-1.7	-5.5	-6.8	-3.9
Water and gas distribution	3.1	-2.2	2.4	-3.2	3.0	-2.2
Construction	8.7	-13.1	10.0	-20.1	7.6	-13.7
Edification	5.9	-11.8	9.8	-21.0	5.1	-12.6
Civil engineering	14.9	-17.2	2.4	-18.8	13.2	-18.3
Specialized works for construction	16.7	-15.0	19.1	-16.8	16.9	-13.2
Manufacturing	6.6	-9.3	12.8	-14.1	6.1	-7.3
Food industry	5.3	-3.5	2.4	-0.7	5.0	-2.1
Beverages and tobacco	2.0	1.1	13.8	-12.8	1.3	2.5
Textiles - Raw materials	33.5	-25.5	43.1	-38.4	30.9	-24.4
Textiles - Finished products ex clothing	-0.4	-10.9	19.5	-20.0	-0.9	-8.4
Textiles - Clothing	27.5	-35.3	28.1	-39.0	24.7	-33.9
Leather and substitutes	16.9	-33.3	29.1	-40.4	15.3	-31.6
Woodworking	25.4	-12.9	20.6	-19.3	22.8	-11.1
Paper	11.2	-5.7	10.0	-7.5	10.7	-4.3
Printing and related products	13.4	-22.8	18.5	-20.1	11.0	-22.4
Oil- and carbon-related products	22.2	-21.2	18.6	-11.9	22.2	-21.4
Chemicals	3.2	-5.6	-0.4	-5.3	2.1	-4.7
Plastics and rubber	14.1	-4.9	23.5	-15.2	12.1	-3.4
Non-metallic mineral goods production	4.2	-4.6	16.0	-12.2	3.8	-3.7
Basic metal industries	14.4	-16.6	14.6	-13.2	14.8	-16.2
Metal-based goods production	11.6	-5.3	22.6	-16.0	11.1	-4.3
Machinery and equipment	15.8	-17.0	21.6	-23.0	13.2	-15.8
Computer, communications, electronic, and other hardware	10.4	-5.9	13.2	-10.2	12.4	-4.3
Electric hardware	15.6	2.1	23.5	-5.5	15.1	4.3
Transportation equipment	-3.3	-15.3	22.0	-29.2	-4.4	-11.4
Furniture, mattresses and blinds	15.4	-12.6	31.8	-23.7	14.0	-11.3
Other manufacturing industries	10.3	-8.6	12.6	-13.5	8.7	-7.5

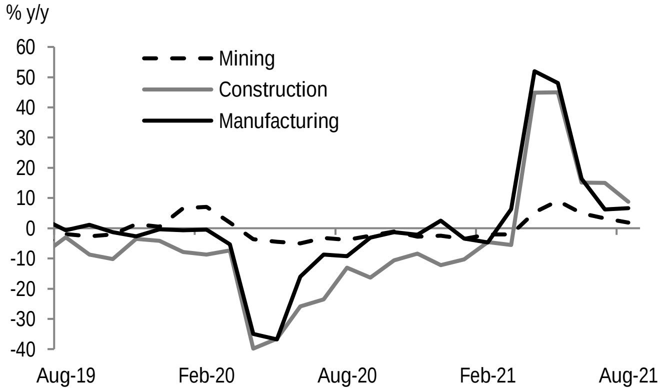
Source: INEGI

Chart 1: Industrial production
% y/y



Source: INEGI

Chart 2: Industrial production by sector
% y/y



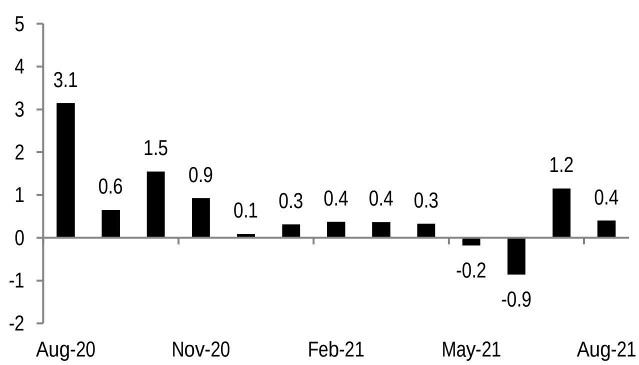
Source: INEGI

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

	% m/m			% 3m/3m	
	Aug-21	Jul-21	Jun-21	Jun-Aug'**21**	May-Jul'**21**
Industrial Production	0.4	1.2	-0.9	0.0	0.0
Mining	-0.1	-0.3	-0.9	-0.4	-0.6
Oil and gas	-2.4	-0.6	-0.9	-1.8	-1.0
Non-oil mining	1.1	1.1	-1.0	0.5	-2.4
Services related to mining	5.7	4.5	-1.8	7.8	6.9
Utilities	-2.5	1.7	-0.7	0.1	2.3
Electricity	-3.7	2.9	-0.8	0.3	2.9
Water and gas distribution	1.1	-1.2	-0.1	-0.3	0.4
Construction	1.9	0.9	-1.9	0.2	0.4
Edification	1.9	2.0	-3.6	0.2	0.5
Civil engineering	3.2	7.5	-2.5	2.0	0.0
Specialized works for construction	1.1	-3.4	2.8	1.0	1.6
Manufacturing	0.2	1.6	-0.2	0.3	0.4
Food industry	-0.2	0.3	1.2	1.9	2.0
Beverages and tobacco	1.3	4.4	-2.0	1.5	0.0
Textiles - Raw materials	1.8	1.5	1.3	2.8	3.7
Textiles - Finished products ex clothing	-10.2	8.8	-1.4	0.9	0.6
Textiles - Clothing	0.6	0.1	-0.7	2.3	6.8
Leather and substitutes	0.3	1.1	1.4	1.8	1.1
Woodworking	2.9	2.9	6.0	10.0	5.7
Paper	1.0	1.6	-1.8	1.1	3.5
Printing and related products	-0.8	-2.4	0.9	5.3	6.5
Oil- and carbon-related products	1.2	6.4	-6.9	-7.5	-9.3
Chemicals	1.4	2.1	1.1	2.6	1.0
Plastics and rubber	-0.3	2.4	-0.3	2.5	4.0
Non-metallic mineral goods production	0.4	0.4	-0.2	-1.2	-1.1
Basic metal industries	-0.6	1.5	-2.2	-1.0	0.8
Metal-based goods production	-0.2	3.4	2.0	2.3	0.6
Machinery and equipment	-0.9	0.0	3.1	0.7	0.7
Computer, communications, electronic, and other hardware	5.7	0.7	1.2	2.2	-1.1
Electric hardware	-0.7	6.0	-5.4	-2.3	-0.4
Transportation equipment	-0.9	0.5	-0.9	-4.1	-2.3
Furniture, mattresses and blinds	-3.0	2.0	0.0	7.5	9.3
Other manufacturing industries	-0.4	1.6	-4.6	1.8	5.8

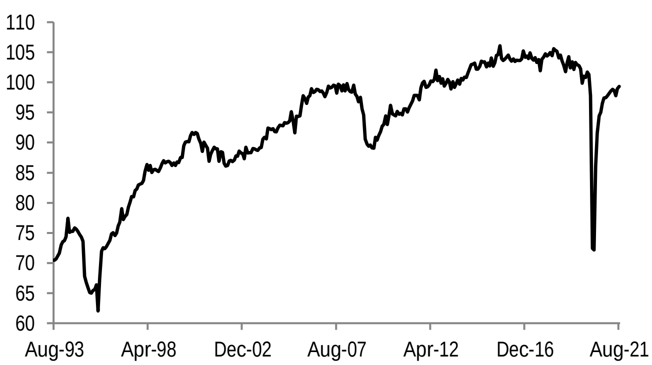
Source: INEGI

Chart 3: Industrial production
% m/m sa



Source: INEGI

Chart 4: Industrial production
Index sa



Source: INEGI

Analyst Certification

We, Alejandro Padilla Santana, Delia María Paredes Mier, Juan Carlos Alderete Macal, Manuel Jiménez Zaldívar, Marissa Garza Ostos, Francisco José Flores Serrano, Katia Celina Goya Ostos, Santiago Leal Singer, José Itzamna Espitia Hernández, Alik Daniel García Alvarez, Víctor Hugo Cortes Castro, Hugo Armando Gómez Solís, Miguel Alejandro Calvo Domínguez, Luis Leopoldo López Salinas, Leslie Thalía Orozco Vélez, Gerardo Daniel Valle Trujillo and Juan Barbier Arizmendi, certify that the points of view expressed in this document are a faithful reflection of our personal opinion on the company (s) or firm (s) within this report, along with its affiliates and/or securities issued. Moreover, we also state that we have not received, nor receive, or will receive compensation other than that of Grupo Financiero Banorte S.A.B. of C.V for the provision of our services.

Relevant statements.

In accordance with current laws and internal procedures manuals, analysts are allowed to hold long or short positions in shares or securities issued by companies that are listed on the Mexican Stock Exchange and may be the subject of this report; nonetheless, equity analysts have to adhere to certain rules that regulate their participation in the market in order to prevent, among other things, the use of private information for their benefit and to avoid conflicts of interest. Analysts shall refrain from investing and holding transactions with securities or derivative instruments directly or through an intermediary person, with Securities subject to research reports, from 30 calendar days prior to the issuance date of the report in question, and up to 10 calendar days after its distribution date.

Compensation of Analysts.

Analysts' compensation is based on activities and services that are aimed at benefiting the investment clients of Casa de Bolsa Banorte and its subsidiaries. Such compensation is determined based on the general profitability of the Brokerage House and the Financial Group and on the individual performance of each analyst. However, investors should note that analysts do not receive direct payment or compensation for any specific transaction in investment banking or in other business areas.

Last-twelve-month activities of the business areas.

Grupo Financiero Banorte S.A.B. de C.V., *through its business areas, provides services that include, among others, those corresponding to investment banking and corporate banking, to a large number of companies in Mexico and abroad. It may have provided, is providing or, in the future, will provide a service such as those mentioned to the companies or firms that are the subject of this report. Casa de Bolsa Banorte or its affiliates receive compensation from such corporations in consideration of the aforementioned services.*

Over the course of the last twelve months, Grupo Financiero Banorte S.A.B. C.V., has not obtained compensation for services rendered by the investment bank or by any of its other business areas of the following companies or their subsidiaries, some of which could be analyzed within this report.

Activities of the business areas during the next three months.

Casa de Bolsa Banorte, Grupo Financiero Banorte or its subsidiaries expect to receive or intend to obtain revenue from the services provided by investment banking or any other of its business areas, by issuers or their subsidiaries, some of which could be analyzed in this report.

Securities holdings and other disclosures.

As of the end of last quarter, Grupo Financiero Banorte S.A.B. of C.V. has not held investments, directly or indirectly, in securities or derivative financial instruments, whose underlying securities are the subject of recommendations, representing 1% or more of its investment portfolio of outstanding securities or 1 % of the issuance or underlying of the securities issued.

None of the members of the Board of Grupo Financiero Banorte and Casa de Bolsa Banorte, along general managers and executives of an immediately below level, have any charges in the issuers that may be analyzed in this document.

The Analysts of Grupo Financiero Banorte S.A.B. of C.V. do not maintain direct investments or through an intermediary person, in the securities or derivative instruments object of this analysis report.

Guide for investment recommendations.

	Reference
BUY	When the share expected performance is greater than the MEXBOL estimated performance.
HOLD	When the share expected performance is similar to the MEXBOL estimated performance.
SELL	When the share expected performance is lower than the MEXBOL estimated performance.

Even though this document offers a general criterion of investment, we urge readers to seek advice from their own Consultants or Financial Advisors, in order to consider whether any of the values mentioned in this report are in line with their investment goals, risk and financial position.

Determination of Target Prices

For the calculation of estimated target prices for securities, analysts use a combination of methodologies generally accepted among financial analysts, including, but not limited to, multiples analysis, discounted cash flows, sum-of-the-parts or any other method that could be applicable in each specific case according to the current regulation. No guarantee can be given that the target prices calculated for the securities will be achieved by the analysts of Grupo Financiero Banorte S.A.B. C.V, since this depends on a large number of various endogenous and exogenous factors that affect the performance of the issuing company, the environment in which it performs, along with the influence of trends of the stock market, in which it is listed. Moreover, the investor must consider that the price of the securities or instruments can fluctuate against their interest and cause the partial and even total loss of the invested capital.

GRUPO FINANCIERO BANORTE S.A.B. de C.V.

Research and Strategy			
Alejandro Padilla Santana	Chief Economist and Head of Research	alejandro.padilla@banorte.com	(55) 1103 - 4043
Raquel Vázquez Godinez	Assistant	raquel.vazquez@banorte.com	(55) 1670 - 2967
Itzel Martínez Rojas	Analyst	itzel.martinez.rojas@banorte.com	(55) 1670 - 2251
Lourdes Calvo Fernández	Analyst (Edition)	lourdes.calvo@banorte.com	(55) 1103 - 4000 x 2611
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
Alik Daniel García Alvarez	Senior Strategist, Equity	alik.garcia.alvarez@banorte.com	(55) 1670 – 2250
Víctor Hugo Cortes Castro	Senior Strategist, Technical	victorh.cortes@banorte.com	(55) 1670 - 1800
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	(55) 1670 - 1889
Alejandro Aguilar Ceballos	Head of Asset Management	alejandro.aguilar.ceballos@banorte.com	(55) 5004 - 1282
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 - 5140
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) 8173 - 9127
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) 5249 - 6423
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) 5004 - 1051
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) 1670 - 1899