

Unemployment rate surprises lower in May, but labor market conditions are still weak

- **Unemployment rate (May; nsa): 4.2%; previous: 4.7%**
- **Part-time workers: 29.9% (previous: 25.4%); Participation rate: 47.4 % (previous: 47.5%)**
- **As in the previous month, these figures were obtained through a phone survey instead of the usual face-to-face method. Therefore, they are not strictly comparable to the historical series despite being quite useful as a reference**
- **Surprisingly, the unemployment rate declined, explained by a higher number of employed people and a relatively stable participation rate. The latter was contrary to our expectations of a stronger rebound in the number of people in the labor force, likely remaining discouraged due to the pandemic**
- **Informal sector data suggests that the increase in employment was focused in this sector, with the informality rate up to 51.8% from 47.7% in April**
- **Despite today's results, we believe the unemployment rate is likely to deteriorate in coming months and will increase above its long-term historical average, as the reopening of the economy remains very gradual and the rate of contagion of COVID-19 stays elevated**

The unemployment rate surprisingly falls in May. According to INEGI's report, the rate stood at 4.2% (non-seasonally adjusted figures, see chart below to the left), 48bps below April's data. As in the previous month, the statistics agency reaffirmed this is not strictly comparable with the historical series (more details in the section below). This result was contrary to our expectations, driven by two main factors: (1) A reduction of 216,039 in the number of unemployed and an increase of 283,985 in total employed people; and (2) a relatively stable labor force, with the participation rate standing at 47.4% from 47.5% (chart below, right), still depressed after last month's considerable decline.

In particular, the labor force went up by only 67.9 thousand people after plunging by 12 million in April. On the contrary, within those not in the labor force, the share of people available for work remained high at 38.4%. We think that, given economic conditions and the pandemic, most of them remain discouraged as they believe they will not be able to find a new job. Specifically, this latter group within those available to work stands at 18.9 million, meaningfully above pre-pandemic levels. If they were accounted for as part of the labor force, the unemployment rate could be much higher. In this sense, it is our take that, in coming months, this metric will keep failing to tell the whole story about the country's labor market conditions, so added focus should be placed in complementary indicators to gauge more clearly what is actually happening.

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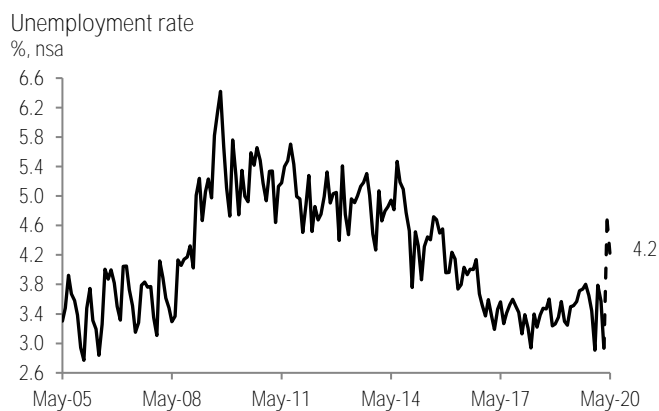
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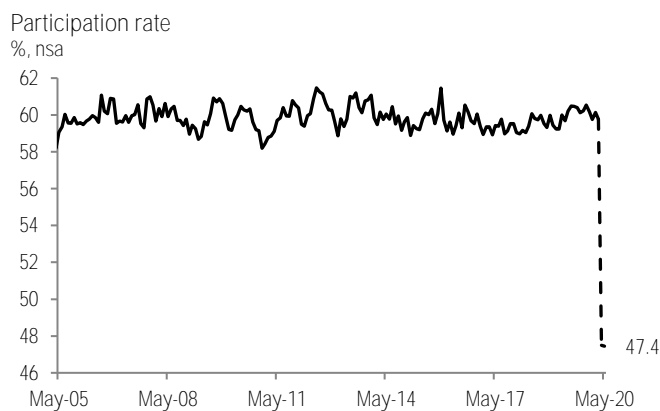
Winners of the award for best economic forecasters for Mexico in 2019, granted by *Refinitiv*



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Note: Dotted lines correspond to data obtained through the alternative methodology
Source: Banorte with data from INEGI



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On the other hand, we believe quality in employment has deteriorated, driven by two factors. First, the important increase in part-time workers to a new historical high of 29.9% from 25.4% in the previous month. In our view, this is mostly because of reduced operations in most businesses as stringent measures to contain the spread of the virus stayed in place. Second, informality rebounded to 51.8% from 47.7%. The latter, in conjunction with the highest increase being in those considered as purely informal, supports the hypothesis that most new jobs were in this category, compensating for [formal job losses according to IMSS figures](#). Broadly speaking, these two results are negative as they point to a hit in terms of job quality despite of the absolute improvement in total employment relative to the previous month.

INEGI's employment report

Non-seasonally adjusted figures

%	May-20	Apr-20	Difference
Unemployment rate	4.2	4.7	-0.5
Participation rate	47.4	47.5	0.0
Part-time workers rate	29.9	25.4	4.5
Formal employment	48.2	52.3	-4.1
Informal employment ¹	51.8	47.7	4.1
Working in the informal economy	23.6	20.7	2.9
Working in the formal economy	28.2	27.0	1.2

Source: INEGI

Methodological considerations. The press release reaffirmed the warning, first included in April, that data presented today are not strictly comparable to the historical series from the employment survey, given that there are significant differences between them. The main one is the sampling method, as today's figures were obtained through a telephone survey, while the usual survey is carried out face-to-face. This is explained by measures taken by the agency to maintain social distancing as well as other public health recommendations. In addition, other important differences include a different sample size and rate of non-response, among others, although the conceptual design is very similar. We should mention that INEGI originally said this would apply for April and May figures, while as far as we know they have not stated yet if they will switch back for June, given the start of the plan to reopen the economy.

¹ Informal employment considers workers not affiliated to the Social Security Institutes (IMSS and ISSSTE) and the armed forces. However, workers in the formal economy do pay some form of income tax

We expect the unemployment rate to increase as economic activity reopens.

Although this seems counterintuitive at first glance, we believe April and May data are significantly distorted by the pandemic, especially as it has led to a very strong decline in the labor force. In this respect, it is our take that, with the gradual reopening of the economy starting in June, its recent fall will start to reverse. If this is coupled with a higher proportion of people back into the labor force being catalogued as unemployed –as we think will be the case–, then the unemployment rate would increase. Apart from this, our base-case is that the recovery of activity will be very gradual, with new cases of COVID-19 in Mexico still not showing signs of decelerating and higher risks of a second wave around the world. Moreover, and even in the case of eventually observing a more meaningful reopening, some industries will be affected for longer (*e.g.* tourism, lodging, entertainment services) and consumers more cautious, with lower total payrolls impacting aggregate demand. All in all, and according to our calculations, these will pressure the unemployment rate and show the true shock of the pandemic to the labor market with a lagged effect. Considering these potential dynamics, along [our recent downgrade of 2020 GDP to -9.8% y/y](#), we also adjusted our unemployment rate estimate by the end of the year to 8.0% (previous: 7.2%). Moreover, we believe it could reach a new high somewhere in the third quarter, with our forecast for the end of that period at 8.6%.

Nevertheless, after the report we recognize the deterioration in the unemployment rate could be more modest relative to our expectations. In this respect, key highlights today include: (1) That the informal sector may be acting as a relief valve for people affected by the pandemic, given that its share of total employment surged –driven particularly by those categorized as purely informal–; and (2) that the latter was observed in tandem with a sizable increase in part-time workers, in our view possibly related to disruptions to the economy, including to mobility patterns, which may linger around at least for the rest of the year. Lastly, we think that accurate readings of the state of the labor market have become more challenging, driven by higher uncertainty about these dynamics along those of the evolution of the economy, the pandemic itself, and measures to fight against it.

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