IMEF's PMI surveys – A bump in the road

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- ***IMEF*** **Manufacturing PMI (October, sa): 46.7pts; Banorte: 47.7pts; consensus: 47.7pts; previous: 48.1pts**
- ***IMEF*** **Non-manufacturing PMI (October, sa): 48.1pts; Banorte: 48.4pts; consensus: 48.0pts; previous: 48.2pts**
- **Both indicators suggest that weakness in activity extended to the start of 4Q19, staying in contraction territory for six consecutive months**
- **In manufacturing, we highlight that all components were lower except for 'deliveries', with 'inventories' and 'employment' posting the largest contractions. Non-manufacturing registered a more mixed performance, with 'production' and 'deliveries' lower**
- **The report suggests that levels of activity remained modest at the start of 4Q19. Nevertheless, we are cautious of not reading too much into this print, particularly in manufacturing as it was likely skewed heavily to the downside due to GM's labor strike in the US, which impacted the auto sector**

IMEF's **PMI's worsen in October.** The Mexican Institute of Financial Executives (*IMEF)* published its PMI surveys for October. The manufacturing index stood at 46.7pts, below our estimate of 47.7pts and all other forecasts according to *Bloomberg*. The non-manufacturing index was also lower than the previous month and expectations by coming in at 48.1pts, with September's print revised an inch higher (0.1pt). As a result, both indicators now add six consecutive months in contraction, suggesting that muted activity levels extended to the start of 4Q19.

In our view, the most relevant detail is the 1.4pts fall in manufacturing, almost double the +0.8 observed in September, with the indicator at its lowest level in two and a half years. We think this is a clear sign of the temporary impact from the GM strike in the US. In this respect, in the 1st day of the month, the company informed that their plant in Silao, Guanajuato would be temporarily suspended –affecting 6,000 workers– as they did not have the necessary imported components to keep producing. A similar situation happened in Ramos Arizpe, Coahuila, affecting about 415 employees. Given the deep integration of supply chains between Mexico and the US, in our view today's report strengthens the case of a non-negligible impact in both manufacturing production and non-oil intermediate goods imports during the month.

Manufacturing impacted by autos. We stress that the most relevant decline was in the 'inventories' subcomponent, which plunged from 53.6pts to 46.0pts, lowest since mid-2017. This was followed by the 'employment' component from 48.6pts to 43.8pts. In our view, this performance is consistent with the news that the closing of the Silao plant was due to missing parts, resulting in the suspension of workers. Moreover, both 'production' and 'new orders' fell 1.3pts. We believe this decline to be temporary, with a possible rebound in November considering that manufacturing exports have been pretty resilient and the fact that the UAW reached an agreement with the company in October 25th.

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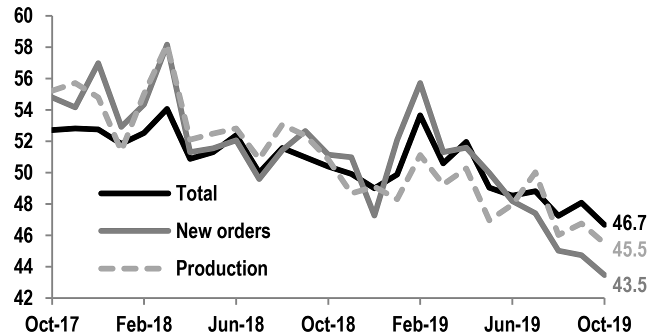
IMEF's PMI manufacturing index
Seasonally adjusted figures

	Oct-19	Sep-19	Difference
Manufacturing	**46.7**	**48.1**	**-1.4**
New orders	43.5	44.7	-1.3
Production	45.5	46.7	-1.3
Employment	43.8	48.6	-4.8
Deliveries	53.5	50.4	3.1
Inventories	46.0	53.6	-7.6

Source: Banorte, IMEF

IMEF's PMI manufacturing index
Seasonally adjusted figures



Source: Banorte, IMEF

The non-manufacturing index fails to gather pace. Contrary to our expectations of a slight improvement, the indicator inched lower (-0.1pts) to 48.1pts, suggesting that domestic demand has stabilized at lower levels. Taking a look at the breakdown, results were more mixed. 'Production' and 'deliveries' both fell by 0.7pts, with the former reaching a new low since April at 48.2pts. On the contrary, new orders rebounded by 0.9pts to 48.5pts, which coupled with the relative stabilization of the headline index may be suggesting some underlying improvement going forward. Nevertheless, it is our take that this is too early to call given its recent performance, which has been muted despite still strong fundamentals. In this respect, we remain somewhat worried by the recent behavior in terms of domestic demand.

Non-manufacturing PMI index
Seasonally adjusted figures

	Oct-19	Sep-19	Difference
Non-manufacturing	**48.1**	**48.2**	**-0.1**
New orders	48.5	47.5	0.9
Production	48.2	48.9	-0.7
Employment	47.8	47.4	0.4
Deliveries	49.7	50.4	-0.7

Source: IMEF

A weak start to activity in 4Q19, albeit aware of the possible skew to the downside due to the temporary impact from the auto sector. As mentioned above, we believe the adverse effect to the auto sector from GM's strike likely skewed the results to the downside significantly, a situation we expect to reverse in November. In this respect, we are cautious about reading too much into this print, particularly in manufacturing. In non-manufacturing, the trend downwards seems to be stabilizing at a more modest level. Overall, the report suggests that economic activity remained modest at the start of 4Q19.

Despite of the latter, we maintain a slightly more positive view on performance in coming months on the possibility of a potential reduction in high levels of uncertainty faced by economic agents, both in the domestic and external fronts. Among them, we highlight the possible trade deal between the US and China along an early ratification of the USMCA agreement in the US, both as soon as this month. In our view, business confidence could improve if these events materialize positively, which is our base-case scenario.

Domestically, we observed some rebound in formal job creation in September, helping to at least stop the downfall in the annual pace of advance, still positive at 1.8% yoy. Moreover, the unemployment rate and inflation remain low, while the Federal Government has stepped-up efforts to stimulate the economy by bringing forward some of the planned spending in infrastructure projects for 2020 –remembering that construction is within the non-manufacturing index–. Meanwhile, the central bank has adopted a more accommodative stance and we expect them to continue the easing cycle, cutting the reference rate towards 6.00% by year-end 2020. This situation may help credit growth and consumption. Overall, we maintain our view that private consumption will gradually improve, although we recognize that so far it has failed to strengthen as expected and that more definitive signals about this prospect are still missing, maintaining the downside risks to our outlook.

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