IMEF's PMI surveys – Both indices remained in contraction in August

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- ***IMEF* Manufacturing PMI (August, sa): 47.4pts; Banorte: 49.0pts; consensus: 49.2pts; previous: 48.9pts**
- ***IMEF* Non-manufacturing PMI (August, sa): 47.7pts; Banorte: 47.8pts; consensus: 47.7; previous: 47.0pts**
- **Both Indices again diverged in terms of performance, with manufacturing falling to a low not seen in more than two years, while non-manufacturing improved relative to July. Nevertheless, both now add four consecutive months in contraction territory**
- **Performance in manufacturing was weak in both the 'production' and 'new orders' components. Services improved broadly, albeit with all subcomponents still below the 50pts threshold**
- **In our view, the report suggests that weakness in economic activity extended to 3Q19, with concerns about external demand in a context where global trade tensions prevail**

***IMEF's* PMI's remain weak in August.** The Mexican Institute of Financial Executives (*IMEF)* published its PMI surveys. The manufacturing index stood at 47.4pts, below consensus and the previous month, with the latter figure revised down by 0.7pts. The non-manufacturing index recovered to 47.7pts, virtually in line with our forecast. After four consecutive months in which both indices stood in contraction territory, today's report suggests that economic activity remained weak in 3Q19, with an average level for the former so far at 48.1 vs 49.9pts in the previous quarter, with the latter at 47.4pts against 49.0pts, in the same order. In this respect, these figures seem to validate our argument in July's report that the decline in the 'new orders' component for both indices heralded weakness in coming months. In this respect, we highlight the additional 2.4pts fall of this subcomponent in the manufacturing index to 45.0pts, low since April 2017, likely impacted by global trade tensions.

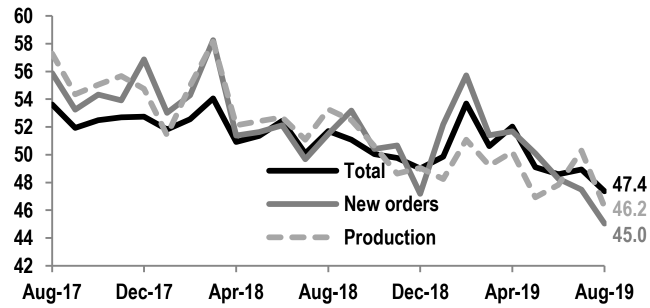
Manufacturing weakness is likely reflecting global headwinds. We should stress that the index was revised significantly lower for previous months, with -0.7pts in July –and which initially had improved– and an accumulated fall of 0.5pts in the January-June period. By component, we highlight the steep decline of 6.1pts in deliveries, which had stood until now above the 50pts threshold since January. Moreover, production was the second hardest hit, to 46.2pts from 50.3pts, followed by new orders to 45.0pts from 47.5pts. In contrast, employment picked-up 1.6pts to 46.3pts, albeit in contraction since March, while inventories increased to 53.3pts. Broadly speaking, the report is still consistent with a challenging environment for the sector going forward.

IMEF's PMI manufacturing index
Seasonally adjusted figures

	Aug-19	Jul-19	Difference
Manufacturing	**47.4**	**48.9**	**-1.6**
New orders	45.0	47.5	-2.4
Production	46.2	50.3	-4.0
Employment	46.3	44.8	1.6
Deliveries	47.8	53.9	-6.1
Inventories	53.3	52.0	1.3

Source: Banorte, IMEF

IMEF's PMI manufacturing index
Seasonally adjusted figures



Source: Banorte, IMEF

The non-manufacturing index improved after four months in decline. The indicator went up 0.7pts, from 47.0pts to 47.7pts. Nevertheless, this was observed only after four consecutive months pressured, which took it to a minimum in almost two years and a half. In this context, all subindices improved with the exception of deliveries, with the strongest increase in production (+5.4pts, to 49.4pts) and new orders (+3.9pts, to 48.1pts). On the other hand, the employment component was modestly up, in our view consistent with the deceleration observed in formal job creation figures. We believe that the peso's depreciation during the period and lower inflation may have provided some support to services, suggesting a possible stabilization in domestic demand at more modest absolute levels.

Non-manufacturing PMI index
Seasonally adjusted figures

	Aug-19	Jul-19	Difference
Non-manufacturing	**47.7**	**47.0**	**0.7**
New orders	48.1	44.2	3.9
Production	49.4	43.9	5.4
Employment	47.8	47.8	0.1
Deliveries	49.1	50.8	-1.7

Source: IMEF

In our view, the report suggests that activity remained weak in 3Q19. Regarding manufacturing, the signal provided is consistent in terms of direction with the US PMI, which dipped to contraction (49.9pts) for the first time since September 2009. According to *IHS Markit*, weakness in the US mainly reflected a weaker contribution from new orders, falling for the second time in the past four months, while also signaling a steep reduction in export sales, which is negative for our country due to the integration of supply chains. This seems to confirm the signal provided by the ISM report for July, in which business imports were also contained and in contraction at 47.0pts, a new minimum in three years. Overall, the sector looks to be extending its soft patch despite the stronger performance of exports in July's trade balance, in a context in which US businesses' expectations for the year ahead have deteriorated further.

In this respect, the report also supports our view that trade tensions will probably be net negative in spite of possible gains for our country. The latter could come at least from two main factors: (1) The recent depreciation of the MXN, helping the relative competitiveness of Mexican exports; and (2) US tariffs to Chinese imports, helping our country to gain market share in the former country. It should also be mentioned that a new round of US tariffs started since yesterday, for which China also imposed countervailing measures. After today's results, we remain cautious about the sector's performance and the impact of these measures on Mexico's industry.

On services, the improved performance is welcome news although it came only after a series of declines that had resulted in very low levels in absolute terms. Among the factors that could help in upcoming months, we highlight the strong moderation of inflation and the accumulated advance in real wages. In economic policy, the possibility of lower interest rates in the near future (expecting accumulated cuts of 50bps by Banxico during the rest of the year) and the Federal Government's plan to increase infrastructure and consumption spending (with resources that total around 2% of GDP). Last but not least, our expectation that the peso will depreciate towards 20.30 per dollar by the end of the year could help induce more consumption of domestically-produced goods relative to imports, while averting strong inflation pressures. In spite of the latter, business confidence remains low, which coupled with more modest formal job growth, will continue to be relevant headwinds for a stronger rebound in domestic demand.

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