Special Commentary — November 15, 2024

Soft-Landing, or No Soft-Landing, That is the Question

Q3 Update

Summary

- In September, we wrote a five-part series of reports that introduced a new toolkit to predict the probability of soft-landing, stagflation and recessionary episodes. The toolkit also predicts the probability of a monetary policy pivot occurring in the next two quarters. In this report, we update our framework with Q3 data.
- In the third quarter, the soft-landing probability increased from 40% to 42%. Meanwhile, the recession probability declined to 28% from 30%, and the stagflation probability declined to 27% from 28%. The soft-landing probability is the highest, which indicates that the chances of a soft-landing (trend-like growth) are higher during the next four quarters.
- Though the growth scenario probabilities were little changed from last quarter, the aftermath of the election has created uncertainty for the economic outlook, which may create volatility for the probabilities moving forward.

Economist(s)

Azhar Iqbal
Econometrician | Wells Fargo Economics
Azhar.Iqbal@wellsfargo.com | 212-214-2029

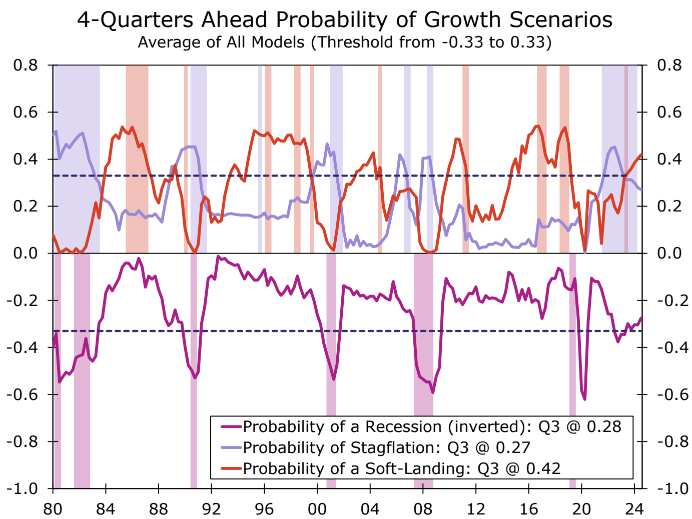
Delaney Conner
Economic Analyst | Wells Fargo Economics
Delaney.Conner@wellsfargo.com | 704-374-2150

Is a Soft-Landing Still in the Cards?

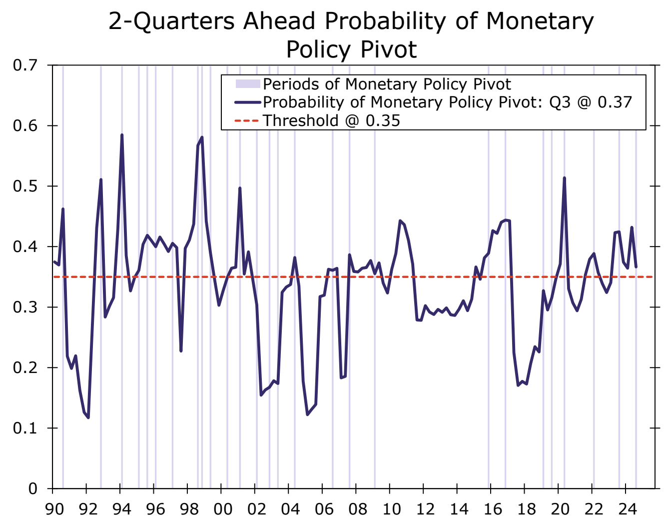
In September, we wrote a five-part series of reports that introduced a new toolkit to predict the probability of soft-landing, stagflation and recessionary episodes. The series details our methodology, but on a basic level, our framework effectively predicted periods of soft-landing, stagflation and recession using a threshold of 33% in the post-1950 era. It also accurately predicted episodes of policy pivots in the post-1990 era using a threshold of 35%. In this report, we update our framework with Q3 data to predict the probabilities of the three scenarios occurring during the next four quarters. We also predict the probability of a monetary policy pivot occurring in the next two quarters.

In the third quarter, the soft-landing probability increased from 40% to 42%. Meanwhile, the recession probability declined to 28% from 30%, and the stagflation probability declined to 27% from 28%. The soft-landing probability is the highest, which indicates that the chances of a soft-landing (trend-like growth) are higher during the next four quarters. However, elevated probabilities for all three scenarios should caution analysts to consider more than one scenario occurring. Additionally, new policies administered by the newly-elected Trump administration may affect the probabilities of each growth scenario in the near future.

While the probabilities of each growth scenario were little changed from last quarter, the probability of a monetary policy pivot occurring in the next two quarters saw a bit more movement, dropping to 37% in Q3 from 43% in Q2. Though still above the threshold of 35%, the declining trend in the probability is consistent with the Fed's most recent policy decisions. The Fed kicked off its easing cycle at its September meeting with a 50 bps cut, and it continued to ease at its November meeting with a 25 bps cut. Historically, once the FOMC adopts a policy stance, it keeps it for at least several meetings. We therefore expect the probability of a monetary policy pivot in the next two quarters to remain depressed, which is consistent with our framework.



Source: Wells Fargo Economics



Source: Federal Reserve Board and Wells Fargo Economics

In short, the growth scenario probabilities are little changed from last quarter, with the chances of a soft-landing the highest. However, the aftermath of the election has created uncertainty for the economic outlook, which may create volatility for the probabilities moving forward. As we wrote in our post-election report, President-elect Donald Trump expressed support for a variety of policy changes that will impact our economic outlook. More specifically, he vowed to impose a 10% across-the-board tariff on America's trading partners with a 60% tariff levied on China. These tariff increases, if implemented shortly after Inauguration Day, would impart a modest stagflationary shock to the U.S. economy, boosting our inflation forecasts in the near term, but also dampening our economic growth outlook.[1] Should this occur, the probability of a stagflation scenario in our growth model would likely increase. That said, there is tremendous uncertainty about future potential policies. Our framework may help eliminate some of that uncertainty by predicting potential risks to the economic outlook and utilizing those probabilities to forecast policy pivots. This would help decision makers create effective policy moving forward.

Endnotes

1 – Bryson, Jay H. and Azhar Iqbal, "Stagflation from Higher Tariffs: 1970s Redux?", Wells Fargo Economics, 18 July 2024. (Return)

Subscription Information

To subscribe please visit: www.wellsfargo.com/economicsemail

Via The Bloomberg Professional Services at WFRE

Economics Group

Jay H. Bryson, Ph.D.	Chief Economist	704-410-3274	Jay.Bryson@wellsfargo.com
Sam Bullard	Senior Economist	704-410-3280	Sam.Bullard@wellsfargo.com
Nick Bennenbroek	International Economist	212-214-5636	Nicholas.Bennenbroek@wellsfargo.com
Tim Quinlan	Senior Economist	704-410-3283	Tim.Quinlan@wellsfargo.com
Sarah House	Senior Economist	704-410-3282	Sarah.House@wellsfargo.com
Azhar Iqbal	Econometrician	212-214-2029	Azhar.Iqbal@wellsfargo.com
Charlie Dougherty	Senior Economist	212-214-8984	Charles.Dougherty@wellsfargo.com
Michael Pugliese	Senior Economist	212-214-5058	Michael.D.Pugliese@wellsfargo.com
Brendan McKenna	International Economist	212-214-5637	Brendan.Mckenna@wellsfargo.com
Jackie Benson	Economist	704-410-4468	Jackie.Benson@wellsfargo.com
Shannon Grein	Economist	704-410-0369	Shannon.Grein@wellsfargo.com
Nicole Cervi	Economist	704-410-3059	Nicole.Cervi@wellsfargo.com
Jeremiah Kohl	Economic Analyst	212-214-1164	Jeremiah.J.Kohl@wellsfargo.com
Aubrey Woessner	Economic Analyst	704-410-2911	Aubrey.B.Woessner@wellsfargo.com
Delaney Conner	Economic Analyst	704-374-2150	Delaney.Conner@wellsfargo.com
Anna Stein	Economic Analyst	212-214-1063	Anna.H.Stein@wellsfargo.com
Ali Hajibeigi	Economic Analyst	212-214-8253	Ali.Hajibeigi@wellsfargo.com
Coren Miller	Administrative Assistant	704-410-6010	Coren.Miller@wellsfargo.com

Required Disclosures

This report is produced by the Economics Group of Wells Fargo Bank, N.A. (“WFBNA”). This report is not a product of Wells Fargo Global Research and the information contained in this report is not financial research. This report should not be copied, distributed, published or reproduced, in whole or in part. WFBNA distributes this report directly and through affiliates including, but not limited to, Wells Fargo Securities, LLC, Wells Fargo & Company, Wells Fargo Clearing Services, LLC, Wells Fargo Securities International Limited, Wells Fargo Securities Europe S.A., and Wells Fargo Securities Canada, Ltd. Wells Fargo Securities, LLC is registered with the Commodity Futures Trading Commission as a futures commission merchant and is a member in good standing of the National Futures Association. WFBNA is registered with the Commodity Futures Trading Commission as a swap dealer and is a member in good standing of the National Futures Association. Wells Fargo Securities, LLC and WFBNA are generally engaged in the trading of futures and derivative products, any of which may be discussed within this report.

This publication has been prepared for informational purposes only and is not intended as a recommendation, offer or solicitation with respect to the purchase or sale of any security or other financial product, nor does it constitute professional advice. The information in this report has been obtained or derived from sources believed by WFBNA to be reliable, but has not been independently verified by WFBNA, may not be current, and WFBNA has no obligation to provide any updates or changes. All price references and market forecasts are as of the date of the report or such earlier date as may be indicated for a particular price or forecast. The views and opinions expressed in this report are those of its named author(s) or, where no author is indicated, the Economics Group; such views and opinions are not necessarily those of WFBNA and may differ from the views and opinions of other departments or divisions of WFBNA and its affiliates. WFBNA is not providing any financial, economic, legal, accounting, or tax advice or recommendations in this report, neither WFBNA nor any of its affiliates makes any representation or warranty, express or implied, as to the accuracy or completeness of the statements or any information contained in this report, and any liability therefore (including in respect of direct, indirect or consequential loss or damage) is expressly disclaimed. WFBNA is a separate legal entity and distinct from affiliated banks, and is a wholly-owned subsidiary of Wells Fargo & Company.

Important Information for Non-U.S. Recipients
For recipients in the United Kingdom, this report is distributed by Wells Fargo Securities International Limited ("WFSIL"). WFSIL is a U.K. incorporated investment firm authorized and regulated by the Financial Conduct Authority (“FCA”). For the purposes of Section 21 of the UK Financial Services and Markets Act 2000 (the “Act”), the content of this report has been approved by WFSIL, an authorized person under the Act. WFSIL does not deal with retail clients as defined in the Directive 2014/65/EU (“MiFID2”). The FCA rules made under the Act for the protection of retail clients will therefore not apply, nor will the Financial Services Compensation Scheme be available. For recipients in the EFTA, this report is distributed by WFSIL. For recipients in the EU, it is distributed by Wells Fargo Securities Europe S.A. (“WFSE”). WFSE is a French incorporated investment firm authorized and regulated by the Autorité de contrôle prudentiel et de résolution and the Autorité des marchés financiers. WFSE does not deal with retail clients as defined in MiFID2. This report is not intended for, and should not be relied upon by, retail clients.

SECURITIES: NOT FDIC-INSURED - MAY LOSE VALUE - NO BANK GUARANTEE