

Special Commentary — May 9, 2025

Soft-Landing, or No Soft-Landing, That is the Question Q1 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 Q1 data.
- In the first quarter, the soft-landing probability decreased from 44% to 40%. Meanwhile, the recession and stagflation probabilities increased to 27% and 28%, respectively.
- The probabilities of each growth scenario saw a reversal in direction during the first quarter. While the change in the trend of probabilities is not a concern yet, it is something to be watched over the next few quarters, especially if the upticks in the stagflation and recession probabilities start to solidify.

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

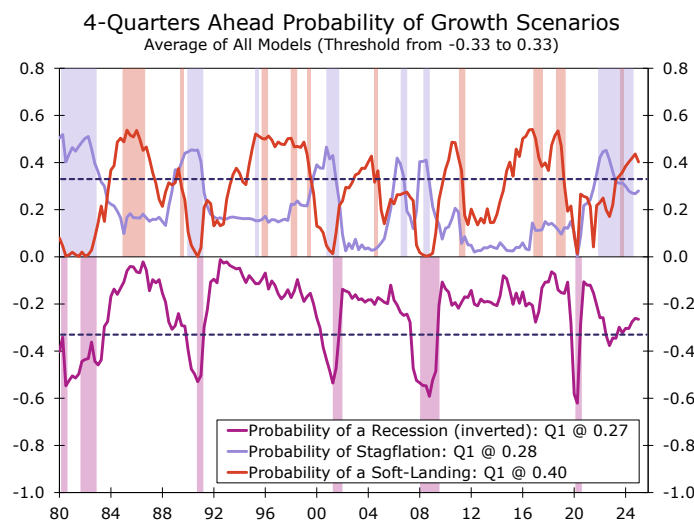
A Switch-Up in Q1

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 Q1 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.

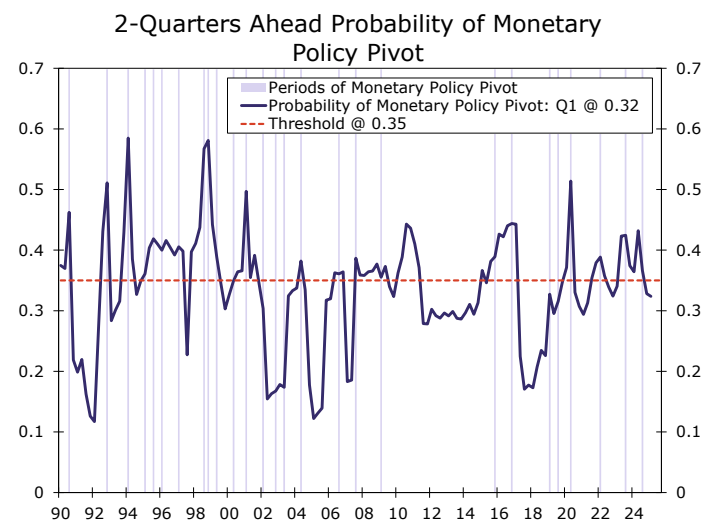
In the first quarter, the soft-landing probability decreased from 44% to 40%. Meanwhile, both the recession and stagflation probabilities increased to 27% and 28%, respectively. The soft-landing probability is the highest, which indicates that the chances of a soft-landing (trend-like growth) are higher during the next four quarters. However, elevated probabilities for all three scenarios should caution analysts to consider more than one scenario occurring.

The probabilities of each growth scenario saw a reversal in direction during the first quarter. The soft-landing probability fell for the first time since 2022, while both the stagflation and recession probabilities increased. While the change in the trend of probabilities is not a concern yet, it is something to be watched over the next few quarters, especially if the upticks in the stagflation and recession probabilities start to solidify.

Meantime, the probability of a monetary policy pivot occurring in the next two quarters fell further to 32% from 33% last quarter. While the declining trend in the probability is consistent with the Federal Open Market Committee's (FOMC) most recent policy decisions, a further rise in the stagflation and/or recession probabilities may increase policy uncertainty. As a result, the monetary policy pivot probability should be carefully watched in the next few quarters.



Source: Wells Fargo Economics



Source: Federal Reserve Board and Wells Fargo Economics

We readily acknowledge the outlook for the growth probabilities is cloudier than normal due to uncertainty surrounding U.S. trade policy. We have maintained it would be a bit extreme to assume tariff rates remain at current levels, as the Trump Administration could reduce tariffs, at least partially, through deals with other countries. We thus assume the effective tariff rate will recede to about 15% and remain there through the end of 2026, imparting a modest stagflationary shock to the economy. As written in our [monthly economic outlook report](#), we anticipate a bumpy ride for GDP growth this year as consumer and business spending dips in the wake of the pre-tariff spending surge that occurred during Q1 and likely carried into early Q2. Additionally, if hiked tariffs are sustained, we look for a push higher in consumer prices. If realized, both the stagflation and recession growth probabilities may increase in the near quarters. As such, we will be closely watching the growth probabilities for any red flags. Stay tuned.

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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
Azhin Abdulkarim	Economic Analyst	212-214-5154	Azhin.Abdulkarim@wellsfargo.com
Coren Miller	Administrative Assistant	704-410-6010	Coren.Miller@wellsfargo.com

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