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US Midterm Elections:

what to expect and what the market impact could be

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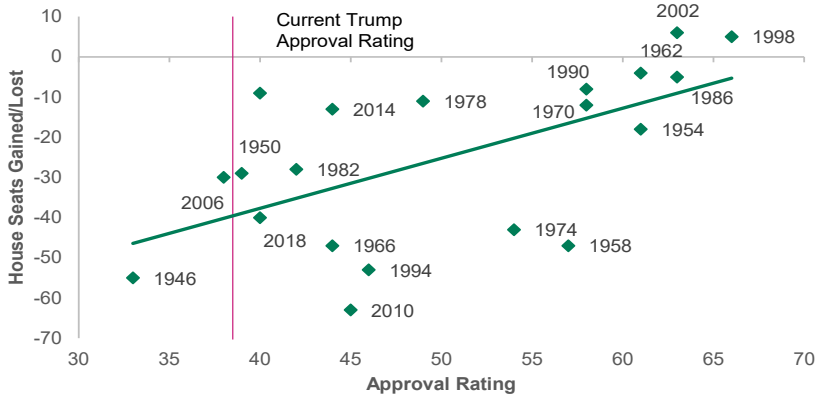
US Midterm Elections

LIKELY OUTCOMES AND POTENTIAL POLICY IMPACT

2026 midterms arrive under a tough backdrop for Republicans

- The incumbent President's party typically struggles in midterm elections, with only two instances since WWII when it has gained seats
- 2026 is unlikely to offer anything different, as the backdrop looks like a difficult one for Republicans given widespread concerns over affordability and discontent around President Donald Trump's handling of several key issues
- This is reflected in Trump's overall approval rating, which has now dipped below 40% to put him more than 20ppt underwater when compared to his disapproval rating
- In addition to his overall approval rating, Trump's approval on issues that used to be his bread and butter has deteriorated significantly as well, as he is further underwater with regards to the economy (-32.4ppt) and inflation (-43.8ppt), and is now underwater on immigration (-10.6ppt) as well
- This combines to make Democrats a strong favourite in the House and a favourite in the Senate as well, albeit to a more modest degree. We would handicap the odds as:
  - Democratic sweep: 65%
  - Democratic House/Republican Senate: 25%
  - Republican sweep: 10%
  - Republican House/Democratic Senate is a highly unlikely combination

President's party typically struggles in midterms



Trump's approval rating is well underwater



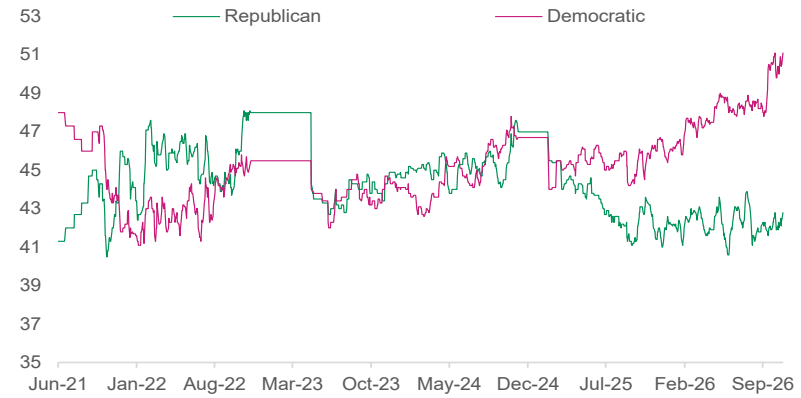
Source all charts: Gallup, RealClearPolitics, Bloomberg, Crédit Agricole CIB

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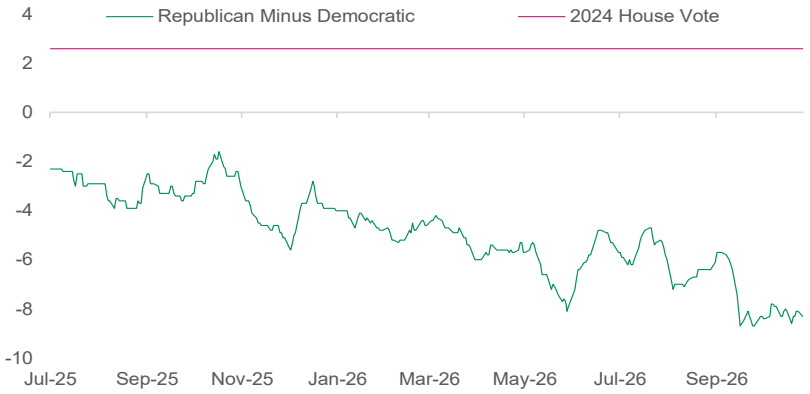
House polling suggests Democratic control a near certainty

- This backdrop is most evident in the House, where Democrats look a near certainty to re-take control
- Republicans currently hold a 220-215 edge (if the two vacancies are assigned to the party that previously held the seat), meaning that Democrats would need a net gain of at least three seats to take control
- Polling for the generic congressional ballot gives Democrats a clear edge, as they currently lead by a margin of more than 8ppt
- When compared to the 2024 cumulative House vote that Republicans won by 2.6ppt, this represents a swing of close to 11ppt towards Democrats over the past two years
- Admittedly, polling is not perfect, but the magnitude of the swing means that anything other than a Democratic victory would be a major surprise, with odds of around 90% that Democrats retake control
- One silver lining for Republicans is that redistricting efforts (eg gerrymandering) have limited the number of seats that are truly in play, which may now only be in the 20s
- That makes a wave-type election with gains of 40+ seats highly unlikely, though the net gain of three seats needed to re-take control is not too high a bar

Generic congressional ballot strongly favours Democrats



And represents a large shift since 2024



Source all charts: RealClearPolitics, Bloomberg, Crédit Agricole CIB

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Senate is a closer call with a modest lean towards Democrats

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- The Senate can be a different animal with roughly one-third of seats up for re-election each two-year cycle, compared to all 435 House seats, meaning the shifting map can play a role
- In 2026, Republicans have to defend substantially more seats than Democrats, and given the difficult backdrop a number of seats in decently red states seem in play
- With Republicans holding a 53-47 edge currently, Democrats need a net gain of at least four seats to regain control, as a 50-50 tie would be broken by Vice President JD Vance
- In looking at the list of key races to watch below, there is a clear path toward that net gain of four seats, though this is not a guarantee, and we would place Democrats odds at around 65% in this chamber

Key Senate races by Cook Political Report rating

State	Current Party Control	Cook Political Report Ranking	Presidential Vote 2024	Republican Candidate	Democratic Candidate	Latest RCP Average	RCP Average Two Weeks Ago
North Carolina	Rep	Likely D	Trump +1.9	Michael Whatley	Roy Cooper	Cooper +10.6	Cooper +9.0
New Hampshire	Dem	Lean D	Harris +2.8	John E. Sununu	Chris Pappas	Pappas +6.5	Pappas +6.7
Alaska	Rep	Toss-up	Trump +13.1	Dan Sullivan (I)	Mary Peltola	Peltola +1.2	Peltola +1.4
Iowa	Rep	Toss-up	Trump +13.2	Ashley Hinson	Josh Turek	Hinson +0.6	Turek +0.6
Kansas	Rep	Toss-up	Trump +16.1	Roger Marshall (I)	Adam Hamilton	Marshall + 0.3	Tie
Maine	Rep	Toss-up	Harris +6.9	Susan Collins (I)	Troy Jackson	Jackson +1.4	Jackson +1.2
Michigan	Dem	Toss-up	Trump +1.4	Mike Rogers	Abdul El-Sayed	El-Sayed +1.9	El-Sayed +2.7
Ohio	Rep	Toss-up	Trump +3.2	Jon Husted (I)	Sherrod Brown	Brown +3.3	Brown +3.1
Texas	Rep	Toss-up	Trump +13.7	Ken Paxton	James Talarico	Talarico +1.5	Talarico +2.8

Source all charts: RealClearPolitics, Cook Political Report, Crédit Agricole CIB

Midterm elections likely to lead to legislative gridlock

- As long as Democrats win the House, the likely outcome will involve legislative gridlock, regardless of the Senate result. This comes down to the fact that even if the Democrats capture the Senate, they would still face obstacles in the form of the filibuster and the Presidential veto, which we do not think Trump would hesitate to use
- This means that Senate control is not a game changer in many ways, though could still have some impact in several ways. We note a few issues below:
  - **Judges and other appointments:** while the President chooses nominees for judgeships and various other appointments, these must be confirmed by the Senate. Thus, if Democrats were to gain control of the Senate, they would be able to block Trump's choices for key vacancies that could open up later in his second term. This would likely be the most significant impact of the Senate outcome
  - **Oversight and investigations:** Democrats will most certainly open several investigations into Trump and/or members of his administration and winning the Senate would allow them to double down. The investigations themselves may not lead to any concrete outcomes, though at the very least they could be a thorn in the administration's side that take up time it would otherwise prefer to devote to other priorities. We see a good chance that some of these investigations could lead to another impeachment, though we would see any impeachment as noise, if we are being frank, as there is little chance that Democrats would be able to reach the two-thirds majority in the Senate that would be needed for removal from office
  - **Legislation:** as noted above, we expect that legislative gridlock will result regardless of the outcome in the Senate given the existence of the filibuster and Presidential veto. Admittedly, a veto can be overridden, but the two-thirds majority in both chambers necessary to do so would represent a high bar to achieve with Democrats likely to hold only narrow majorities even in the situation in which they sweep to control of both chambers of Congress
  - **Government shutdown:** this is an issue that could go either way. In theory having one party control both chambers could make it easier to reach agreement on funding the government, but there is always a chance Trump could choose to veto legislation coming out of a Democratic congress if he thought the blame would fall on Democrats as the party controlling Congress. Overall, there is a decent chance that we could face another government shutdown at some point next year
  - **Tariffs and trade:** we do not expect Congressional election outcomes to change much on this front, as Trump is relying on authority that Congress has previously delegated to the president in past legislation. The new Congress could in theory overturn past legislation, or implement some limitations on the President's trade powers, but the veto again looms large
  - **Foreign policy:** again, the President tends to have greater authority over foreign policy, so we would not expect any major shifts based on the election outcome

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US Rates Outlook

MIDTERMS' IMPACT ON RATES, CURVE, TERM PREMIUM

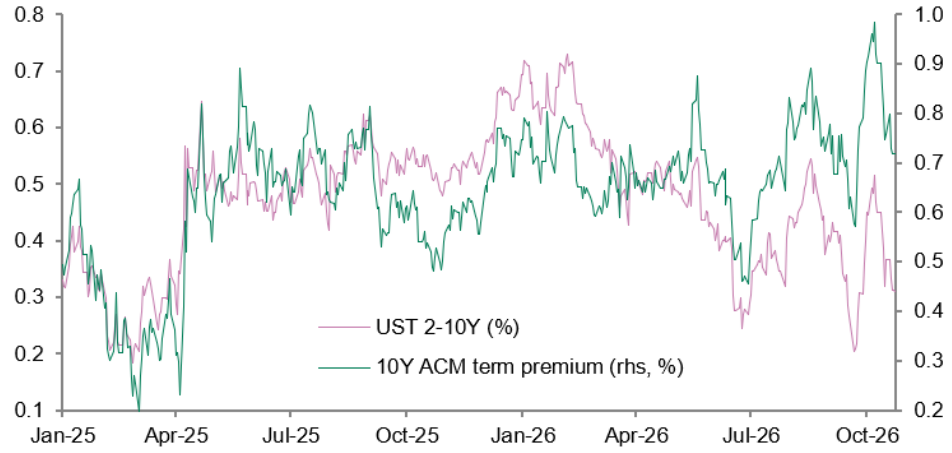
Midterm elections: rates, curve, term premium

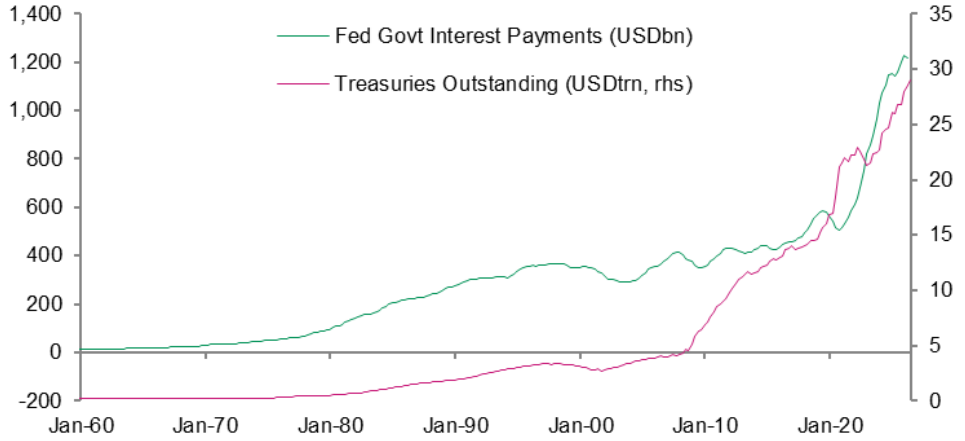
Midterm elections are approaching and could have important implications for the fiscal outlook and Treasury market. Our base case is that Democrats regain control of the House. Under this scenario, legislative gridlock is likely regardless of which party controls the Senate.

A divided government would reduce the likelihood of major spending programmes and tax cuts, easing upward pressure on Treasury term premium and long-term interest rates. All else equal, this would be supportive of lower long-end yields and a flatter yield curve. Front-end rates, however, are primarily driven by monetary policy expectations. With energy prices remaining elevated and the Fed likely to deliver additional rate hikes, front-end yields such as the 2Y Treasury yield, are likely to remain high.

The federal budget deficit surged to USD1.99trn in fiscal year 2026 (ended 30 September), driven by USD7.4trn in spending (up 6%) against USD5.4trn in revenue (up 3%). This represents a significant increase from the prior two years' deficits of USD1.775trn (FY2025) and USD1.817trn (FY2024). At roughly 6% of GDP, the deficit is exceptionally large for a period without recession or major economic crisis.

The Congressional Budget Office projects the debt-to-GDP ratio will climb from 100% currently to 120% within a decade. While economic growth could marginally improve the outlook, it cannot reverse the debt accumulation trajectory – achieving 6% real GDP growth with 5% interest rates would be required merely to stabilise debt levels.





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Debt level and to GDP ratio

Ownership of US Treasuries

Foreign Holders

Fed Holdings

Debt level and to GDP ratio

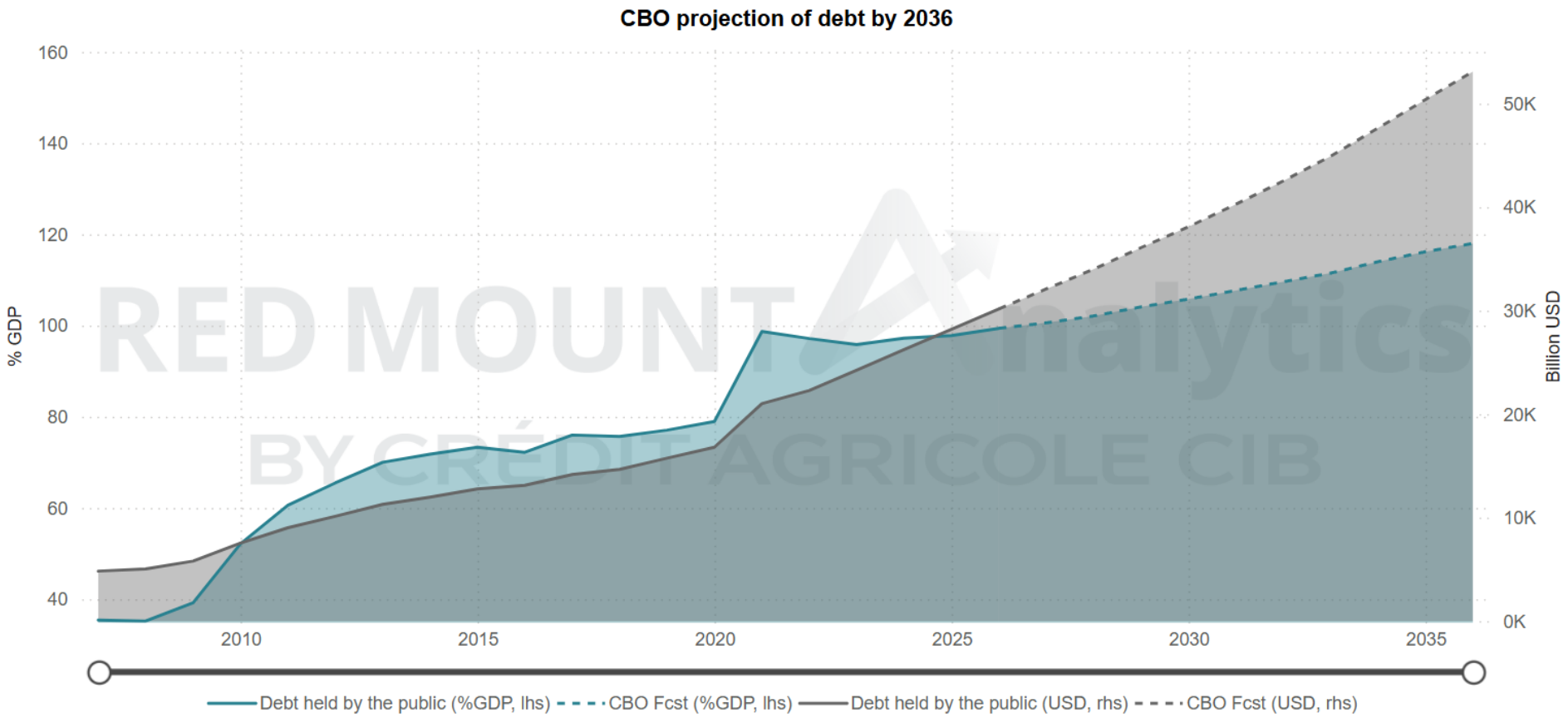
US debt and supply forecast

10Y yield and debt to GDP ratio

Evolution of US sovereign CDS

Short term yields vs FFrate

- The grey area represents the nominal amount of outstanding debt held by the public, with forecasts according to the CBO
- The blue area represents the ratio of outstanding debt held by the public to GDP, with forecasts according to the CBO



RED MOUNT Analytics
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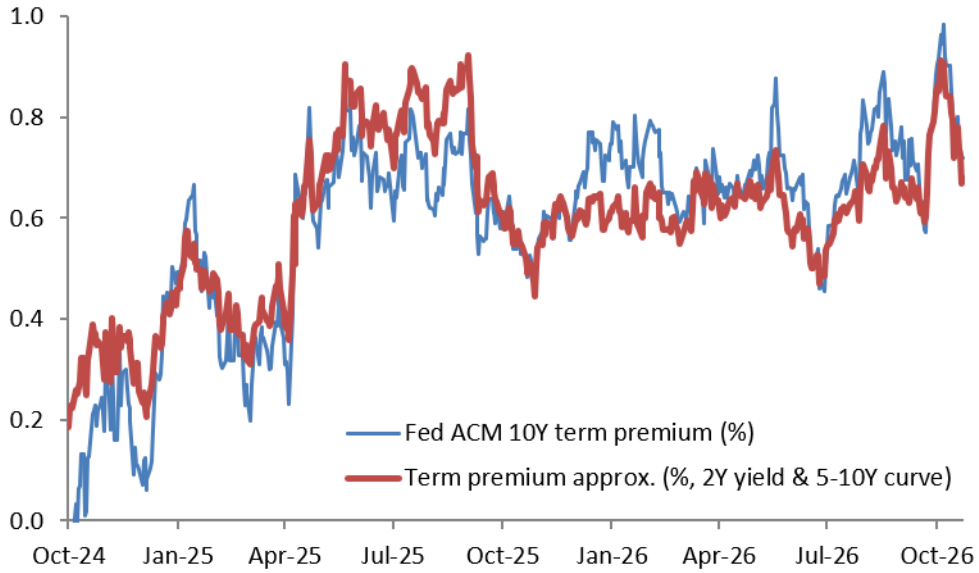
What drives term premium?

In economics, Treasury yields consist of two components:

1. Expectations of the future path of short-term Treasury yields, eg, 2Y yield
2. Treasury term premium, defined as the compensation that investors require for bearing the risk that interest rates may change over the life of a bond, eg, 5-10Y curve. Inflation expectations and the deficit trajectory have been primary factors lately in driving term premium.

Macro factors: growth, R*, inflation expectations, deficit/supply, foreign demand

	5-10Y	2Y yield	Constant
Coefficient	2.27	0.55	-2.32
Standard error	0.06	0.02	0.09
R^2	76%	0.08	
F statistic	811.1	499.0	
T stats	40.2	31.7	-27.3



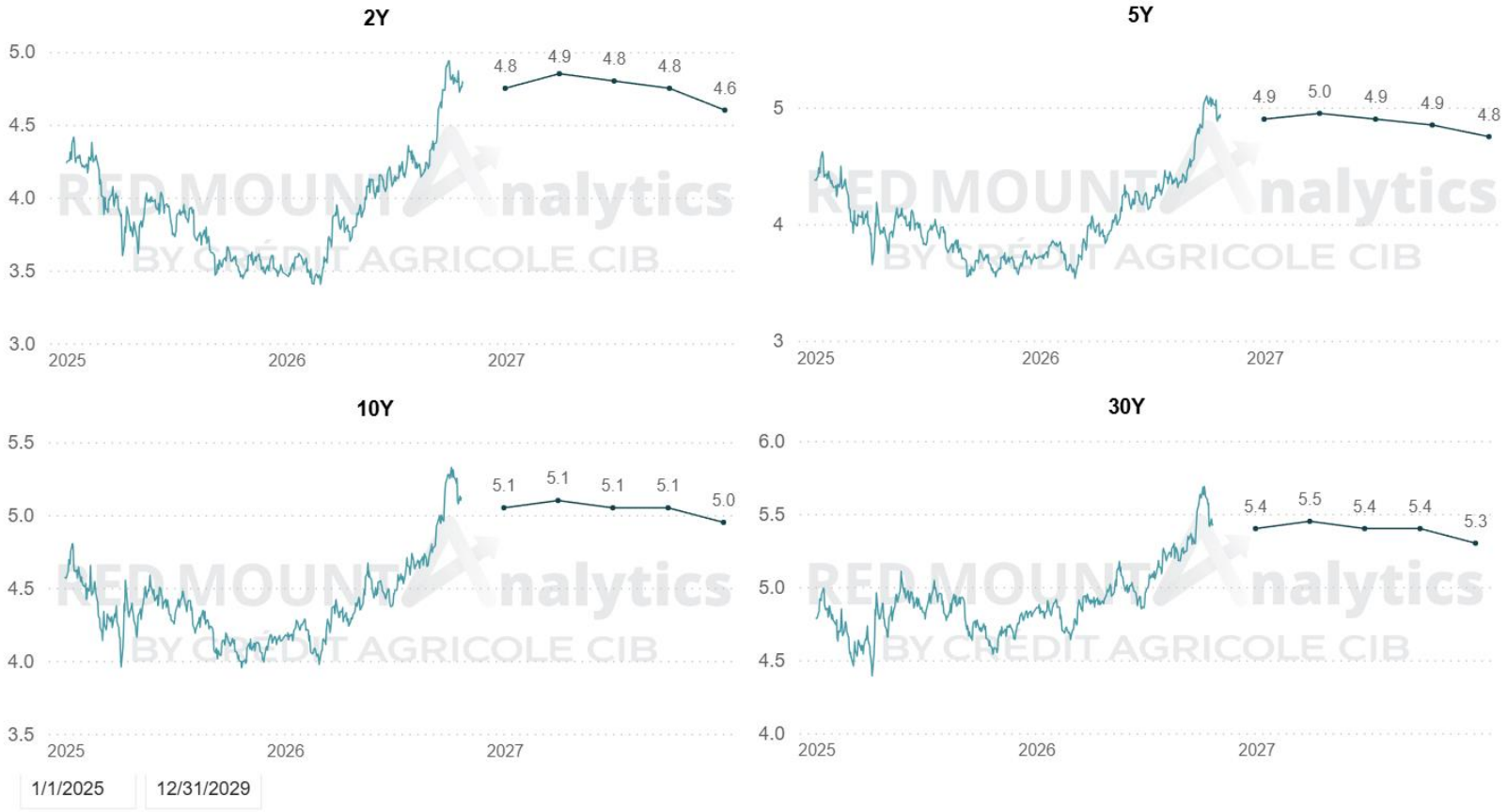
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US rate forecast

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- Forecasts Big Picture
- Money market
- Swaps
- Bonds
  - EGB big 4: yields
  - EGB big 4: spreads
  - EGB all: 10Y spreads
  - UST: yields
  - UST, EGB big 4, JGB: slopes and…
- Bonds vs Swaps
- EUR - US comparison
- Historical forecasts



	Dec-26	Mar-27	Jun-27	Sep-27	Dec-27
2Y	**4.75**	4.85	4.80	4.75	**4.60**
5Y	**4.90**	4.95	4.90	4.85	**4.75**
10Y	**5.05**	5.10	5.05	5.05	**4.95**
30Y	**5.40**	5.45	5.40	5.40	**5.30**

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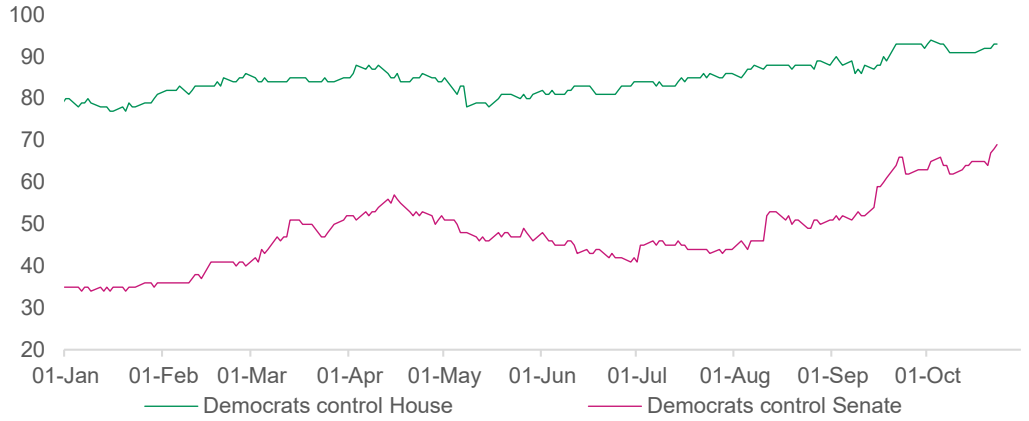
A midterm GOP loss to trigger a USD mid(life) crisis?

MIDTERMS' IMPACT ON THE USD AND THE FX MARKETS

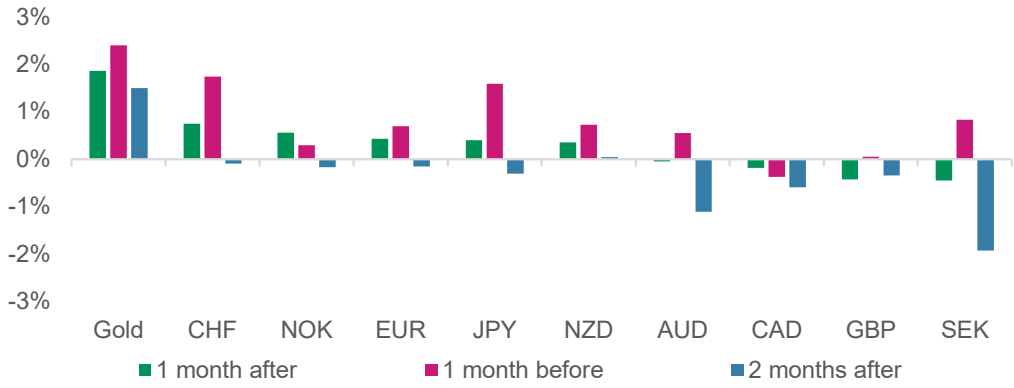
US midterms (1): legislative gridlock and the USD

- Ahead of the US midterm elections on 3 November, the market betting odds suggest that investors are expecting a Democratic sweep of US Congress.
- We agree that there is a strong chance of the House changing hands and that the risk of the GOP losing the Senate has increased considerably of late as well.
- Our US economist expects a return of legislative gridlock in DC after the midterms, with fiscal support for the economy giving way to more policy uncertainty and potential government shutdowns.
- Democratic control over the Senate could lead to more intense legislative oversight over the executive and frustrate President Donald Trump's foreign policy as well.
- Political gridlock and a continuation of Trump's foreign policy could pose downside risks to the US economic outlook and therefore the USD outlook.

Market betting odds ahead of the US midterms



Performance vs the USD around past government shutdowns



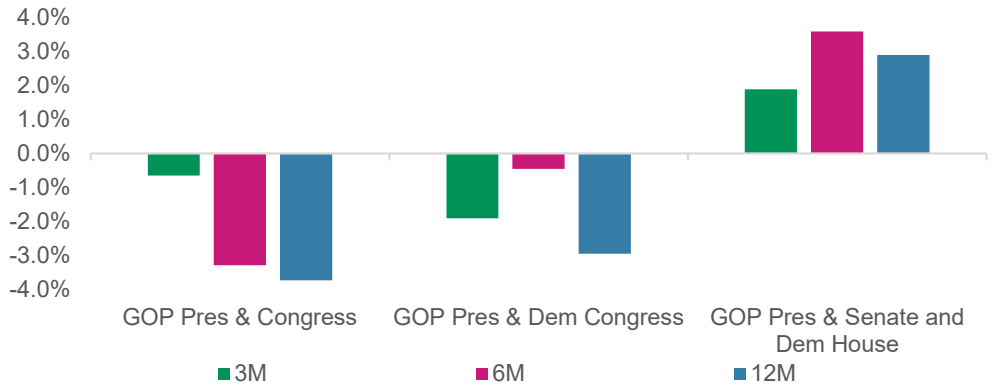
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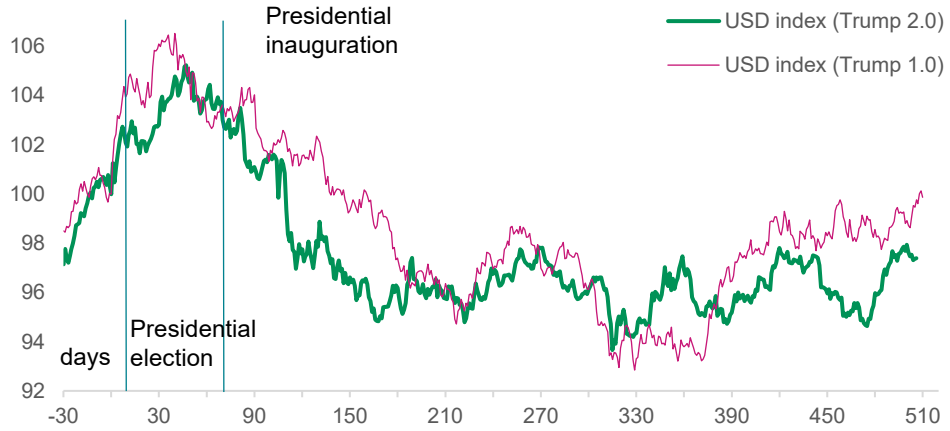
US midterms (2): analyzing the historic FX impact

- The experience since 1976 suggests that the two possible outcomes of the midterms could have very different FX impact:
- In cases of a Democratic Congress coupled with a GOP president, the USD weakened in the months after the vote.
- The results reflect the impact of the 1985 Plaza Accord but also the USD's weakness at the start of both George H W Bush's presidency and George W Bush's second term.
- The two episodes also featured a slowing economy, Fed rate cuts and a Middle Eastern conflict.
- During periods with a GOP President and Senate coupled with a Democrat House, the USD rallied across the board.
- The last such episode was during Trump's first presidential term, after the 2018 midterms. It coincided with a recovering US economy and a hawkish Fed.
- Earlier episodes from the 1980s were less USD-positive, however, partly due to weak economy and Fed easing.

USD performance after US elections since 1976



USD performance during Trump 1.0 and 2.0



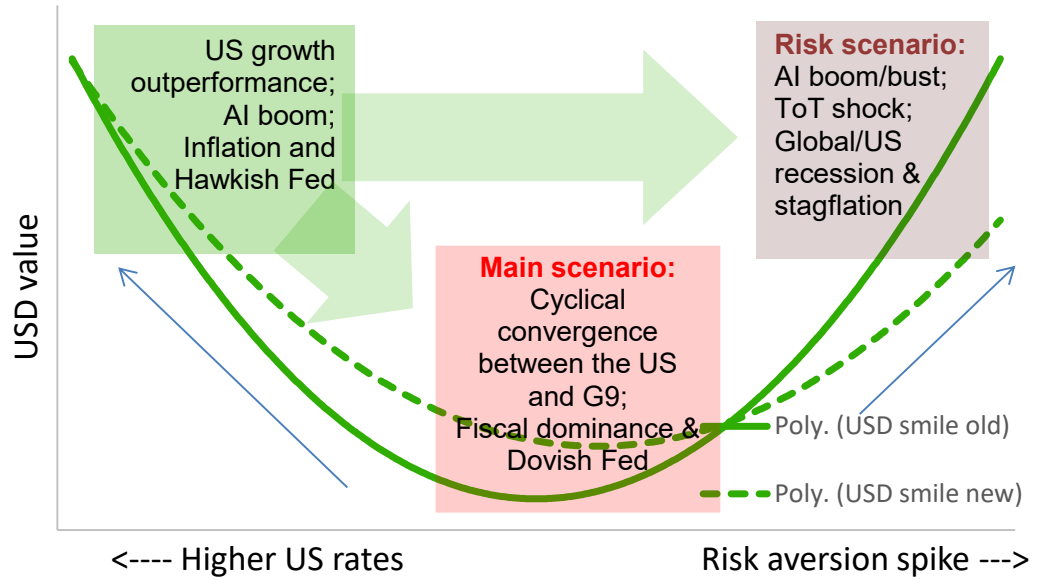
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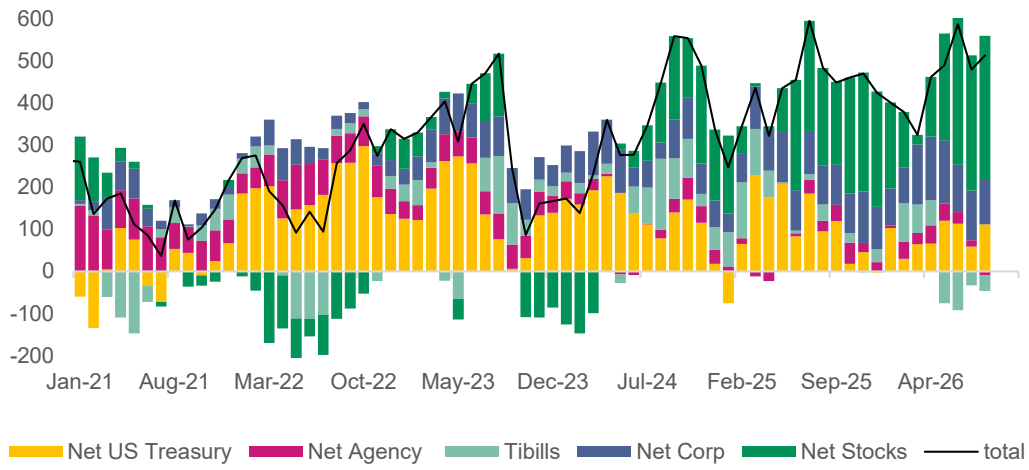
Looking beyond the midterms – the USD smirk

- **Main scenario:**
  - **Cyclical convergence between the US and the rest:**
    - Slowing US AI investment & AI stock market correction → rebalancing flows
    - Legislative gridlock in DC and fading fiscal support in the US after the midterms
    - Slowing real wage growth and lack of savings → weaker US private demand
    - Lower energy costs – a boon for economies of energy importers in Europe/ Asia
    - Fiscal support in parts of Europe & Japan → repatriation flows into EUR & JPY
    - Easing energy shock & ample household savings → more resilient domestic demand in Europe and Japan
  - **Global disinflation → central banks' policy convergence:**
    - Fiscal dominance in the US and Fed rate cuts in H227 → Fed policy rate convergence with the rest of G10
    - Tighter financial conditions in Europe to force the ECB to cut rates too
    - Economies with superior fiscal fundamentals require less CB support
- **Risk scenario:**
  - AI boom-bust cycle ends triggering a global market selloff
  - Negative energy shock persists and hurts global growth
  - Global and US slowdown – a potential recession and/or stagflation

The USD smile/ smirk and our FX market scenarios



Foreign investors buying US stocks but not USTs



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FX Forecasts

		Dec-26	Mar-27	Jun-27	Sep-27	Dec-27
USD Exchange rate						
Industrialised countries						
Euro	EUR/USD	1.13	1.13	1.14	1.16	1.17
Japan	USD/JPY	156	155	154	152	150
United Kingdom	GBP/USD	1.31	1.32	1.34	1.37	1.39
Switzerland	USD/CHF	0.84	0.84	0.83	0.81	0.80
Canada	USD/CAD	1.38	1.36	1.34	1.33	1.32
Australia	AUD/USD	0.69	0.70	0.72	0.74	0.74
New Zealand	NZD/USD	0.58	0.60	0.61	0.62	0.63
Sweden	USD/SEK	9.40	9.30	9.30	9.05	8.90
Norway	USD/NOK	9.45	9.30	9.10	8.90	8.70
Euro Cross rates						
Industrialised countries						
Australia	EUR/AUD	1.64	1.61	1.58	1.57	1.58
Canada	EUR/CAD	1.56	1.54	1.53	1.54	1.54
Japan	EUR/JPY	176	175	176	176	176
New Zealand	EUR/NZD	1.95	1.88	1.87	1.87	1.86
Norway	EUR/NOK	10.70	10.50	10.40	10.30	10.20
Sweden	EUR/SEK	10.60	10.50	10.60	10.50	10.40
Switzerland	EUR/CHF	0.95	0.95	0.95	0.94	0.94
United Kingdom	EUR/GBP	0.86	0.86	0.85	0.84	0.84
Precious metals						
Gold	USD/oz	5,000	5,200	5,300	5,400	5,500

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Emerging Markets

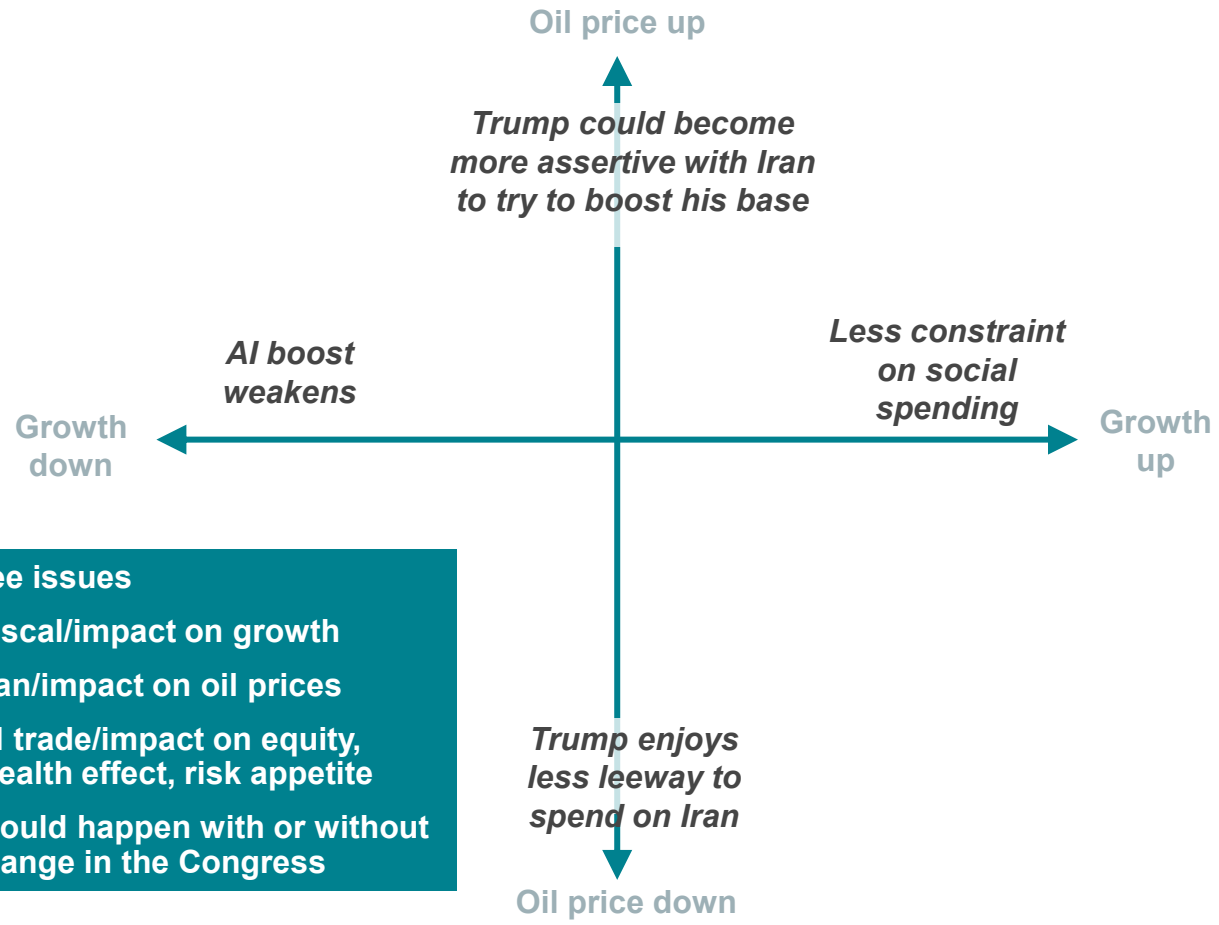
NOT A GAME CHANGER

US midterms: possible changes in backdrop for EMs

- On the paper: likely not a game-changer for EMs

	DEMOCRATIC SWEEP	***DIVIDED GOVERNMENT***	**Impact**
Likely outcome: More power to the Democrats. Possible changes:			
● Fiscal/Spending: less leeway.	Social spending (SNAP/Medicaid) cuts (OBBBA) could be delayed or limited (possibly vetoed by Trump?)	Slightly less leeway	Social spending could be growth supportive
● AI trade cooling down?	Possibly	To a lesser extent	AI trade adjustment could cap risk appetite
● Iran	Less leeway (funding constraints?) to be assertive	Slightly less leeway to be assertive	Less pressure on Iran = less upward pressure on oil prices?
Swing factor: President Trump's assertiveness. Less leeway could mean less assertiveness… or not… It could also lead to more assertiveness to offset the loss of leeway and galvanise potential political support.			More pressure on Iran = more upward pressure on oil prices?

Possible effects of a shift to the left: no clear-cut conclusions



Three issues

- **Fiscal/impact on growth**
- **Iran/impact on oil prices**
- **AI trade/impact on equity, wealth effect, risk appetite**

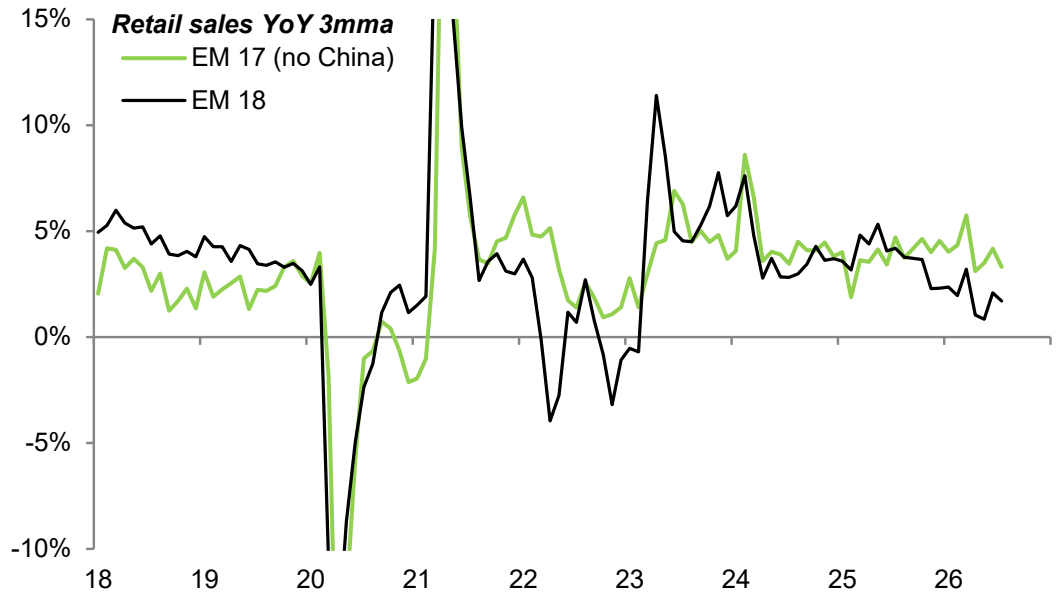
→ Could happen with or without a change in the Congress

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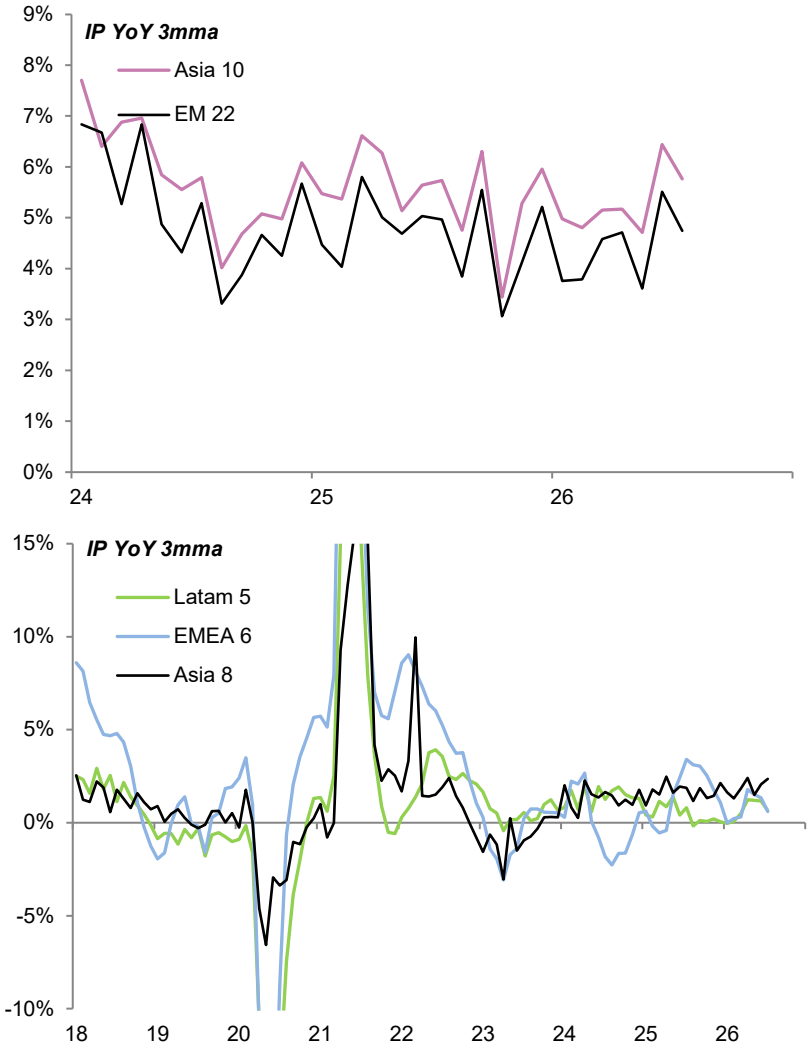
Domestic economic activity: resilient YTD

- Retail sales: resilient in EMs (China is a different story)
- Industrial production resilient and stable, thanks to Asia

EM retail sales: resilient



Industrial production



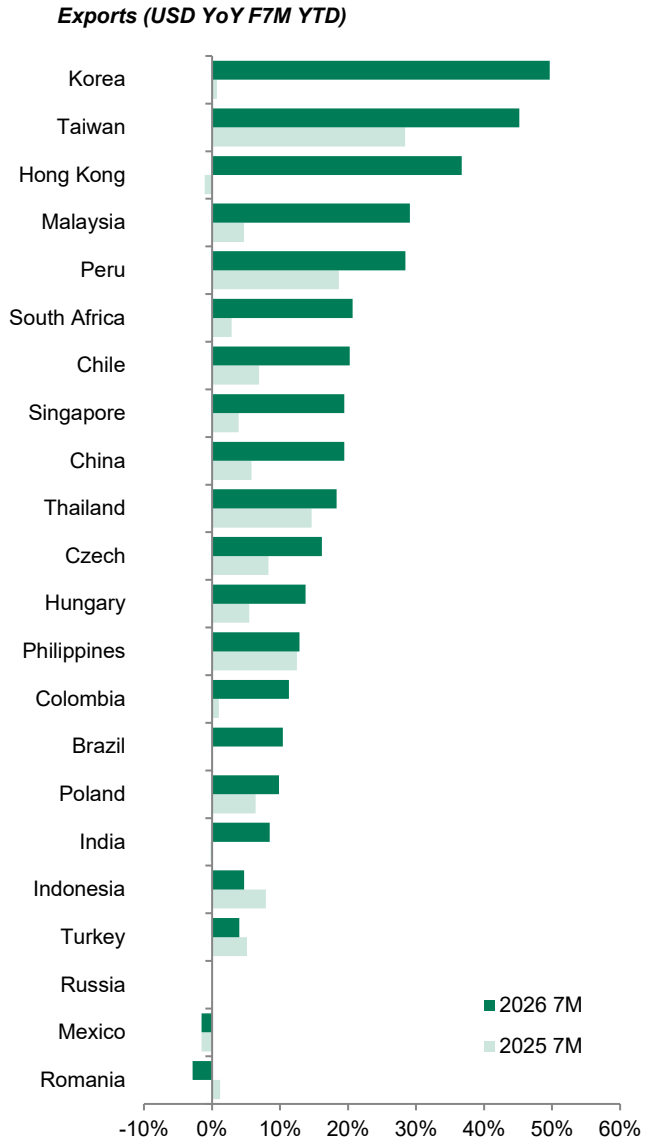
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EM exports: strong acceleration

- EM exports have been supported by different features: electronics/chips/AI (Asia), commodity prices (Latin America, Middle East), mid-tech components/German investment (Central Europe)
- Not only a volume effect, the price effect for both tech products & components and commodities has been significant. For electric cars (China): mostly a volume effect
- Asia benefits more, other countries also benefit from the tech push (eg, metals, incl Chile, Peru, South Africa)



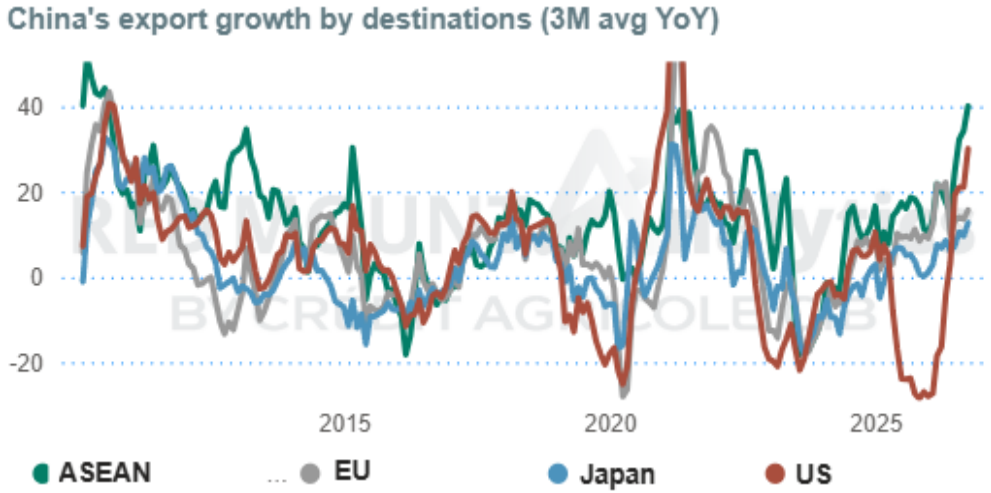


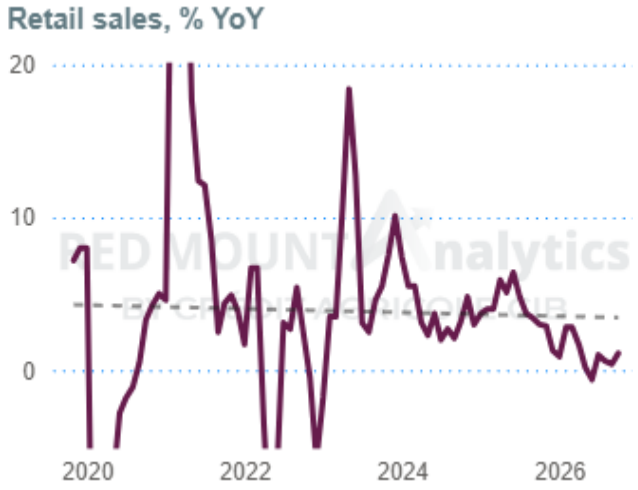
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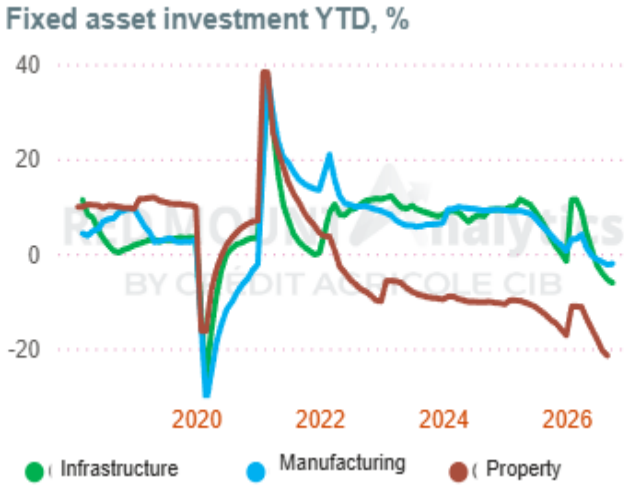
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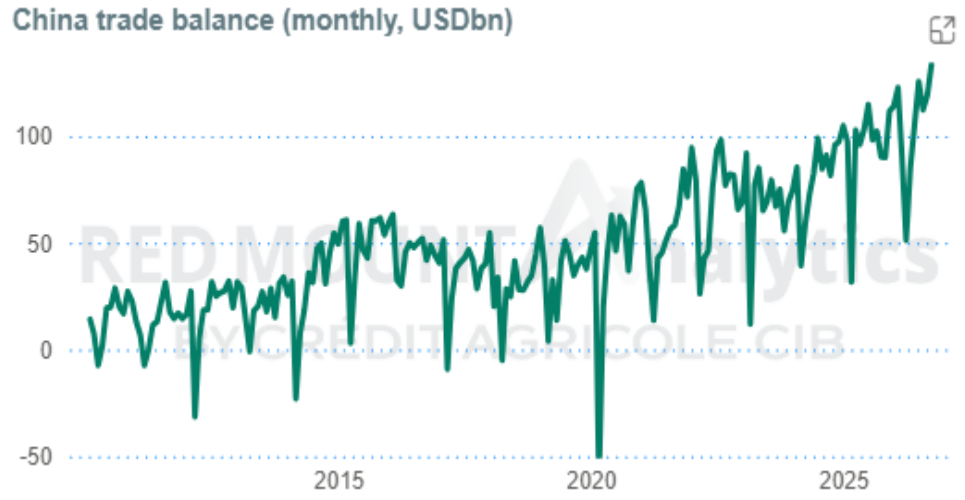
China: difficult growth equation… whatever the US election results

- Coping with difficult growth equation, but exports are helping
- GDP growth expected at 4.6% in 2026 (targeted stimulus measures on top of exports)
- US midterm elections: not a game changer (bi-partisan consensus on the need to cap China's geoeconomic ascent)









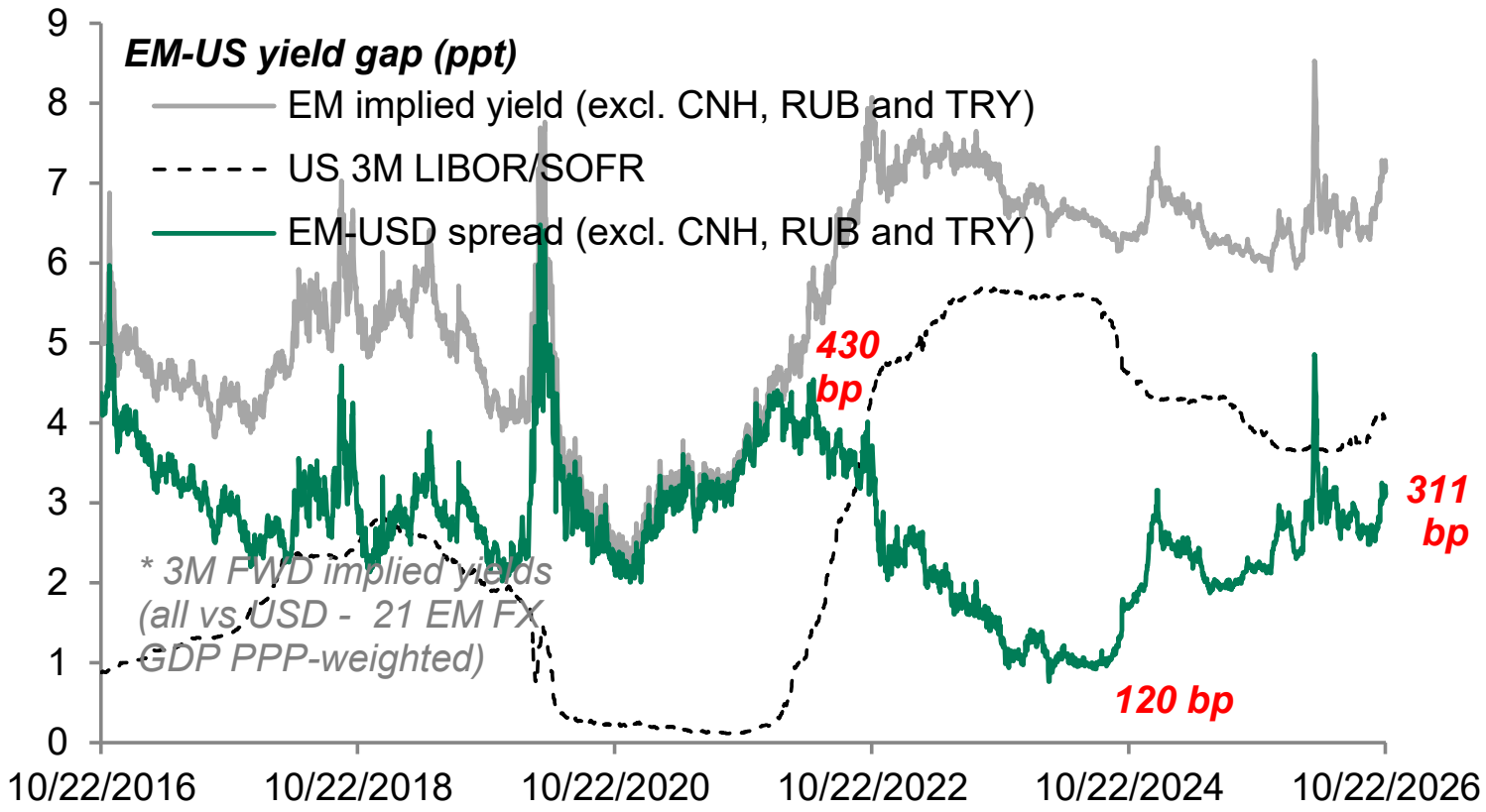
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EM carry attractiveness: decent

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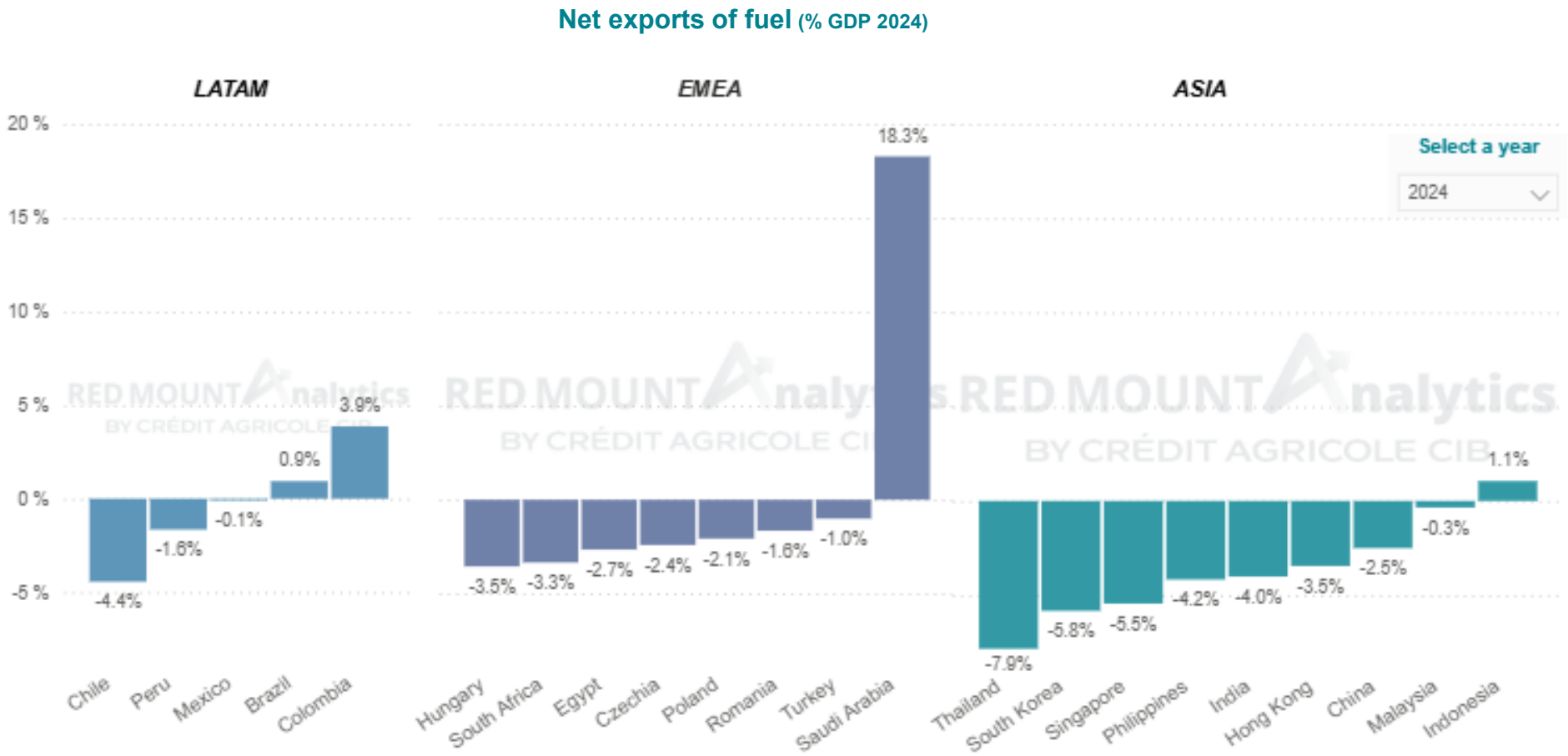
EM-DM carry gap: decently attractive



Source all charts: Bloomberg, Crédit Agricole CIB

Differentiated dependence on oil imports

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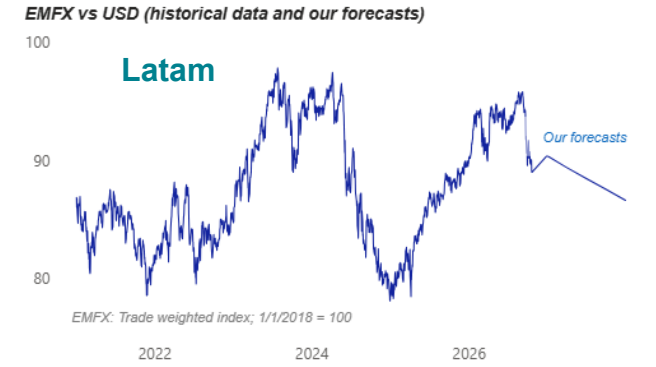


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Our forecasts









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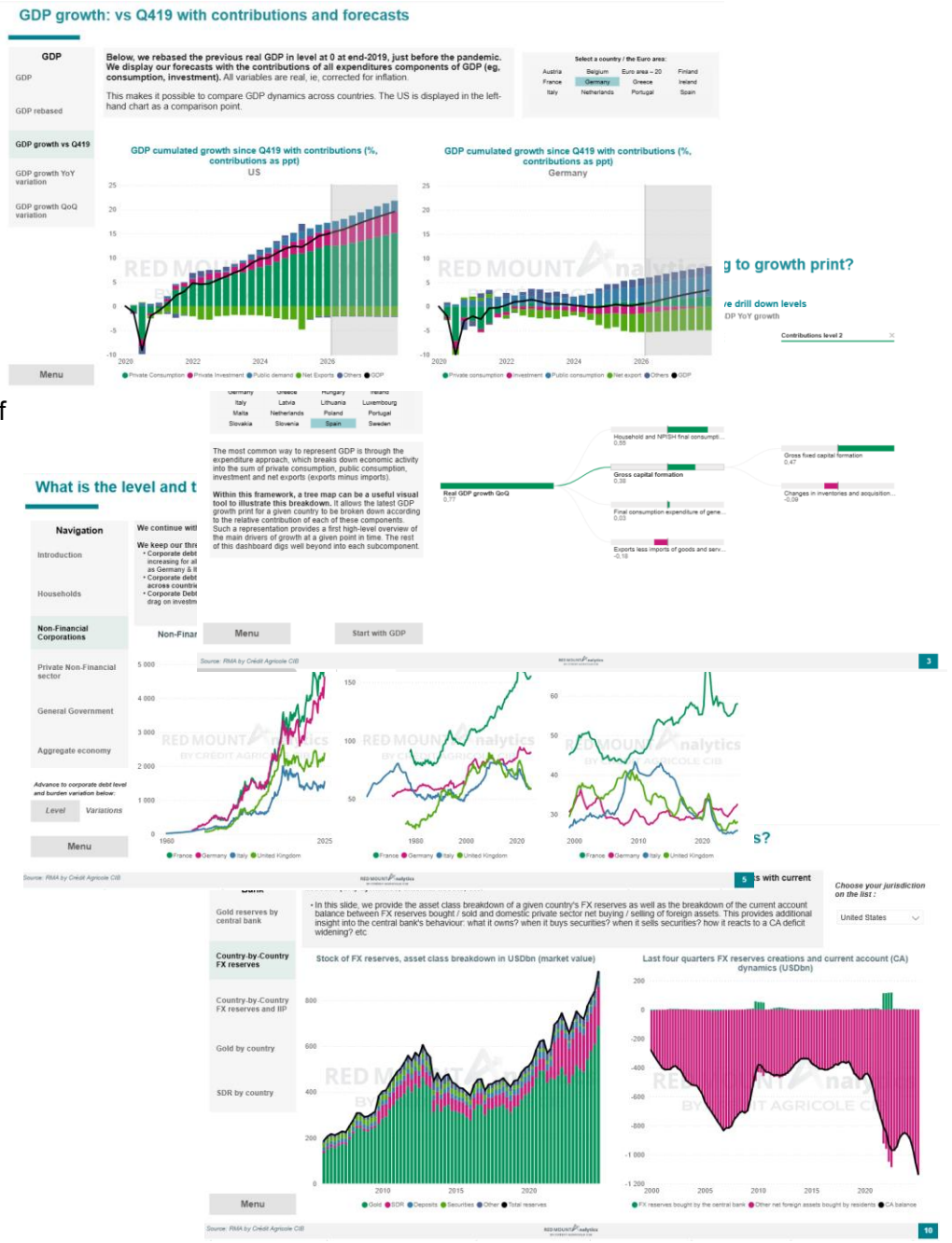
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