US midterm elections – a setback for Trump?

The U.S. midterm elections will take place on November 3. The Republicans are likely to lose their majority in at least one of the two chambers of Congress. This would make things more difficult for President Trump on the domestic front. He might then focus more on foreign policy, since he is hardly dependent on Congress in that area.

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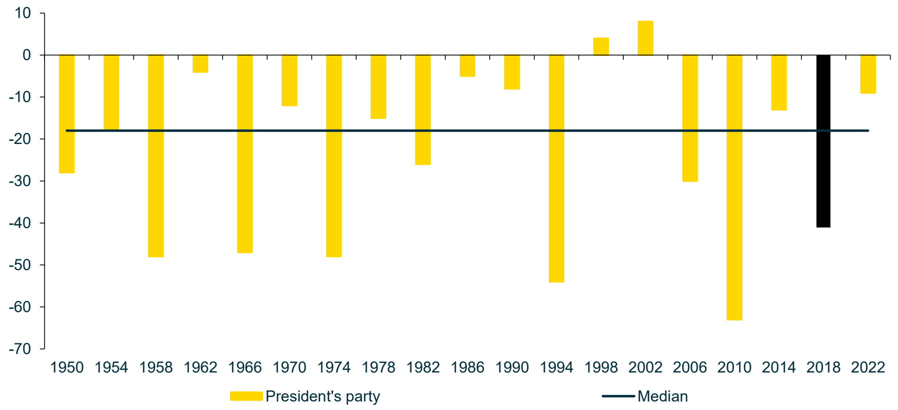
Will voters give a thumbs-down for Trump?

Americans are dissatisfied. According to polls, they are primarily concerned about high inflation, and the war against Iran is unpopular. President Trump's approval ratings are therefore very low; on average across various polls, about 55% disapprove of his performance in office. The Republican Party is therefore looking with concern toward the midterm elections on November 3. On that day, all 435 members of the House of Representatives will be up for reelection, and 35 of the 100 Senate seats will be up for election. So far, the Republicans have held majorities in both houses of Congress, which makes governing easier. This is likely to change with the elections.

Democrats are favored in the House of Representatives, ...

In the past, Americans have almost always used midterm elections to strengthen the opposition. Since 1950, the President's party has typically lost seats in the House of Representatives during midterm elections, averaging 18 seats. One of the few exceptions was the 2002 election, which was shaped by the extraordinary circumstances following the September 11, 2001, terrorist attacks (Chart 1). Since the Republicans currently hold only a slim majority of 218 seats to the Democrats' 212 (of the remaining 5 seats, 4 are vacant and 1 is held by an independent), it is very likely that the Democrats will take the majority in the House of Representatives away from the Republicans.

Chart 1 - President's party usually loses midterm elections
Midterm elections for the House of Representatives, seat changes of the President's party. Black column: midterms in Trump's first term of office



Source: Congress, Commerzbank Research

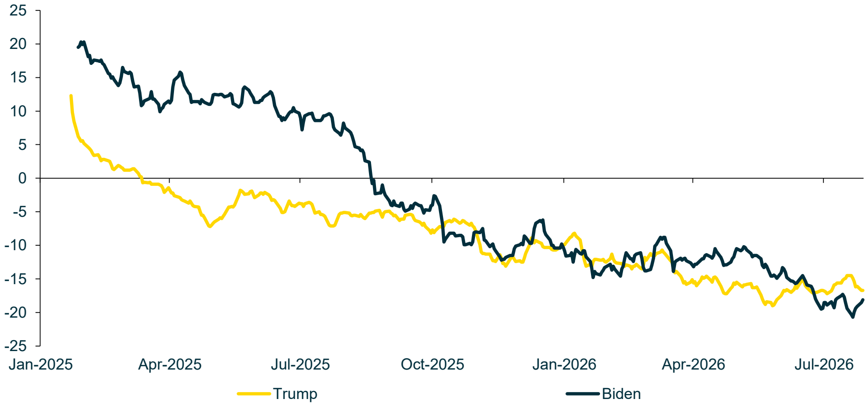
... but a landslide victory is unlikely

However, the Democrats are not expected to achieve a success like the one in 2018, when the Republicans lost 41 seats in the midterm elections during Trump's first term:

- In many "red" (i.e., Republican-governed) states, congressional districts have been redrawn, which is likely to give the Republicans additional seats. Efforts by the Democrats to counter this have not been enough to offset the impact.
- Trump's current very low approval ratings should not be overestimated. At the same point in his term, President Biden had similarly low approval ratings (Chart 2). Nevertheless, the Democrats' losses were limited to a net loss of 9 seats in the midterm elections.
- Furthermore, it is not only Trump who is unpopular, but also the Democratic Party. In polls assessing the parties, the Democrats actually fare even worse than the Republicans. Critics often point to the aging party leadership and its lack of fresh ideas. At the same time, the younger and more dynamic factions of the party are taking a distinctly left-leaning course, which also deters many voters.

Chart 2 - Americans are not happy with their Presidents

Net approval (percentage of survey respondents who approve minus percentage who disapprove) of President Trump since beginning of his second term and President Biden's corresponding figures at the same point in his Administration



Source: RealClearPolitics, Commerzbank Research

… and in the Senate, the Republicans could retain their majority

It will be significantly more difficult for the Democrats in the Senate than in the House of Representatives. They would have to take 4 seats away from the Republicans, who currently hold 53 seats, to secure a majority in that chamber (in the event of a tie—that is, 50-50—Vice President Vance has the deciding vote). Most of the senators up for election hold relatively safe seats; political analysts consider the outcome to be up in the air for only 8 seats. However, three of those are already held by Democrats. These would therefore have to be defended, and the Democrats would also have to take four of the five remaining seats from the Republicans. Current polls show the Republicans with 50 seats, which—taking into account the Vice President's tie-breaking vote—would allow them to narrowly defend their majority in the Senate.

What does this mean for the next two years? For politics…

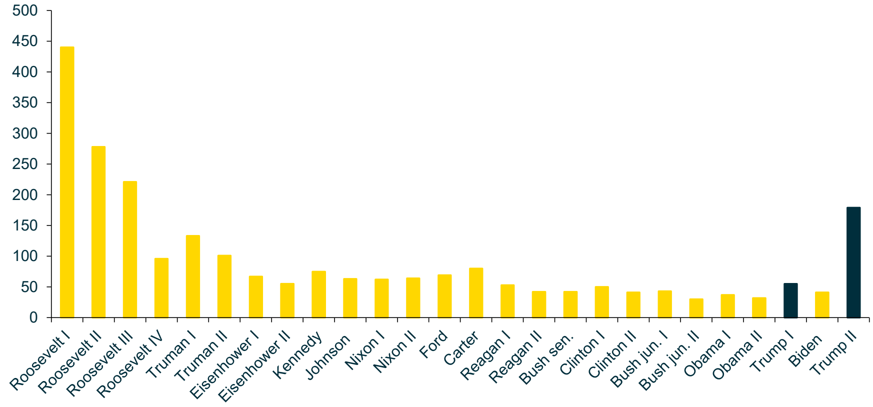
The likely outcome of a "divided government" (in U.S. politics, this term refers to a situation where the presidency and both houses of Congress are not controlled by the same party) would have implications for the second half of Trump's term. This is because if the Democrats win a majority in the House of Representatives, they will gain additional powers. They would then be able to appoint all committee chairs, initiate investigations and subpoenas—including, albeit a largely symbolic one, the impeachment of the President—and determine the legislative calendar (i.e., which bills are debated and voted on). Furthermore, under the U.S. Constitution, the House of Representatives holds budgetary authority, which means that all bills concerning federal revenue and spending must originate there.

This would allow the Democrats to make life politically difficult for President Trump. Trump would then likely rely even more heavily on executive orders than he has in the past (Chart 3). Furthermore, since Trump's election—not least due to decisions by the Supreme Court—the executive branch has been strengthened relative to Congress. For example, according to a recent Supreme Court ruling, the President can effectively dismiss the heads of the top federal agencies at will, with the exception of the Federal Reserve.

Furthermore, Trump is likely to focus more on foreign policy, where he can act more freely and independently of Congress. In terms of economic policy, he has already pushed through his agenda over the past year with the "One Big Beautiful Bill."

Chart 3 - Governing by executive orders: Trump follows Roosevelt

Executive orders, annual average in term of office, President Trump: black columns



Source: The American Presidency Project, Commerzbank Research

... and for the economy and the markets?

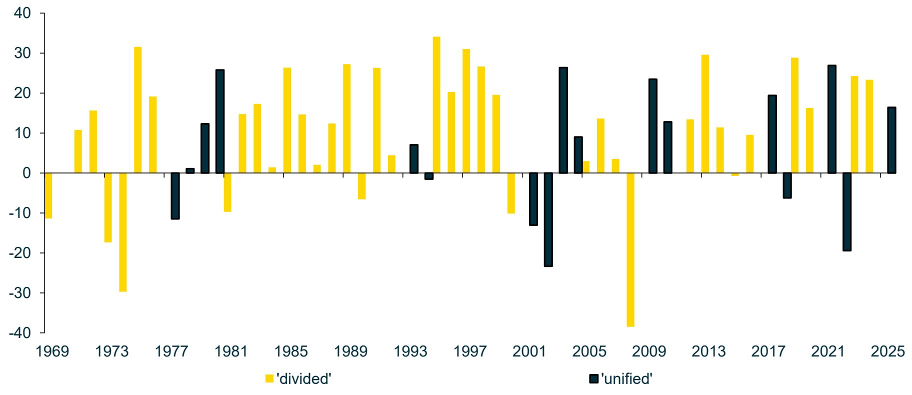
A “divided government” has been the rule rather than the exception over the past 50 years. Yet these were not necessarily bad times for the economy. For example, Presidents Reagan in the 1980s and Clinton in the 1990s had to contend with opposition majorities in Congress; this did not harm the country—in hindsight, these periods are considered nothing short of golden ages. Furthermore, since 1969, the S&P 500 Index has risen significantly faster on average under a “divided government”—at 9% per year—than under a “unified government”—at 5% (Chart 4).

However, if Trump focuses on policy areas where he has more leeway, his traditional unpredictability could lead to further disruptions:

- In **trade policy**, Trump is likely to continue relying on tariffs. No easing of tensions is expected here; rather, new rounds of tariffs loom. The U.S. Trade Representative will likely launch investigations in additional sectors to establish the legal grounds for additional tariffs by demonstrating alleged disadvantages faced by American companies.
- The same applies to **foreign policy**, where the president also has considerable leeway. These are also the biggest challenges of Trump’s second term, and the assessment of his presidency could hinge on them. At the same time, he no longer needs to worry about his own re-election prospects; after all, he will not be running in the next presidential election in 2028 (the 22nd Amendment limits the number of terms to two).

Chart 4 - "Divided government" is common - and not bad for equities

S&P 500, perfomance per calendar year in periods of divided and unified goverment ("divided government": President, House, Senate not in the hands of the same party)



Source: Bloomberg, Commerzbank Research

Implications for the 2028 Elections

Many observers will be scrutinizing the election results for implications regarding the next presidential election. For the Democrats, the question is whether the party’s left wing—which has recently been gaining momentum anyway—will continue to gain ground if the “progressive” candidates perform well. The same applies to the Republicans, where the dominance of MAGA candidates could be confirmed. This would further fuel political polarization—though it would leave open the big question of which side the growing number of independent voters will choose. The political focus is likely to shift increasingly toward the potential Democratic and Republican presidential candidates. How President Trump will cope with no longer being the sole center of attention is another interesting question. For the election outcome in two years, however, it will likely be more important how the economy develops between now and then and whether inflation eases noticeably.

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