US MIDTERMS:

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why a DIVIDED WASHINGTON *could suit* MARKETS

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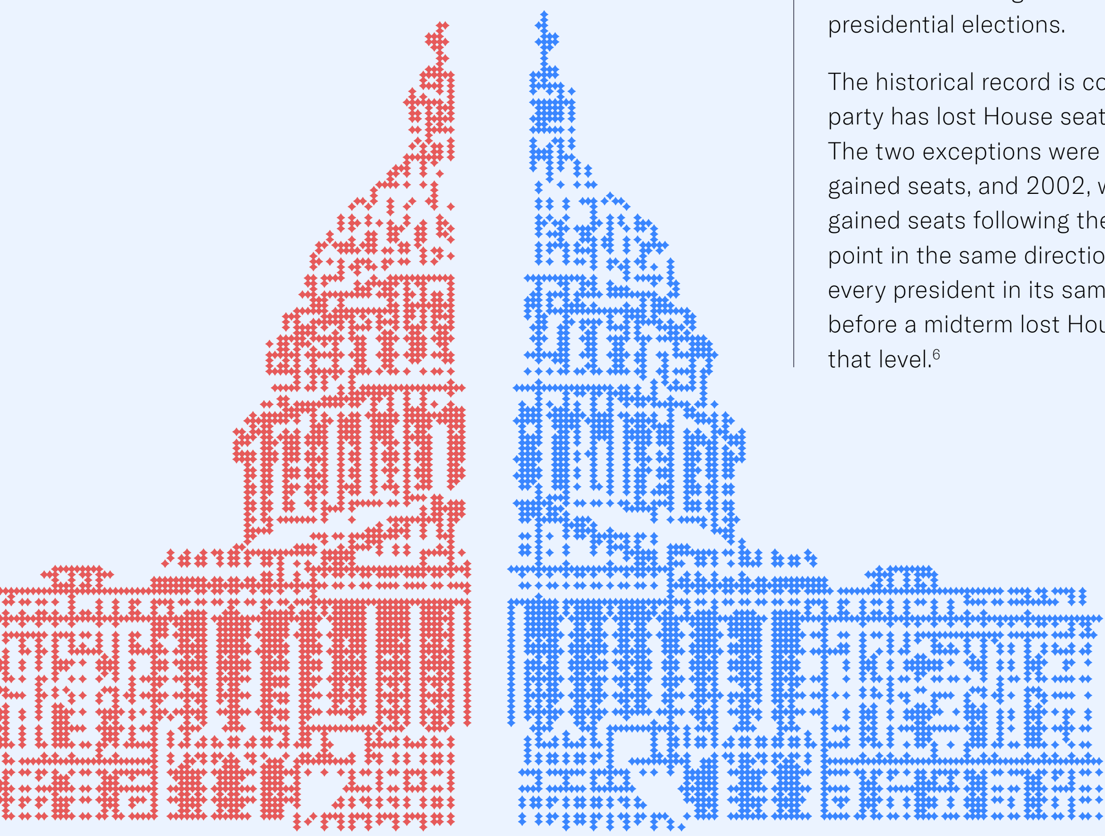
Markets can become more volatile ahead of the midterms, but increased certainty after the vote could provide support for equities.

With two months to go until the US midterm elections, Republicans, led by President Donald Trump, face a difficult fight to retain control of Congress. Trump's approval rating remains below 50%[1], Democrats are favoured to regain the House and the Senate race is on a knife edge.[2]

Markets often become less settled as midterms approach, as investors assess the possible policy consequences while the result remains uncertain. Once the vote is over, uncertainty begins to fall. Equities have historically tended to rally in the months after midterm elections, although the wider economic and earnings backdrop remains more important over time.



A difficult election for Republicans

Our recent article examined why November's elections could become a major test of Donald Trump's presidency. Since then, the campaign has drawn closer and the political backdrop has become more complex. Several states have redrawn congressional districts, making some House seats[3] safer for one party or the other.[4] That makes the eventual number of seats won by each party harder to predict from national polling alone.

Midterms usually work against the incumbent party in the White House. The president is not on the ballot, but the administration's policies are. Voters who are unhappy with the direction of the country can use the election to provide a check on the government, while opposition supporters often turn out in greater numbers than they do during presidential elections.

The historical record is consistent. Since 1946, the president's party has lost House seats in 18 of 20 midterm elections.[5] The two exceptions were 1998, when Bill Clinton's Democrats gained seats, and 2002, when George W. Bush's Republicans gained seats following the 9/11 attacks. Approval ratings point in the same direction. Gallup's analysis found that every president in its sample with approval below 50% shortly before a midterm lost House seats. Trump is currently below that level.[6]

US midterms: House results outliers

Year	President	Approval rating	Midterm US House results
1946	Truman	33%	-45 seats
1950	Truman	39%	-29 seats
1954	Eisenhower	61%	-18 seats
1958	Eisenhower	57%	-48 seats
1962	JFK	61%	-4 seats
1966	LBJ	44%	-47 seats
1970	Nixon	58%	-12 seats
1974	Ford	54%	-48 seats
1978	Carter	49%	-15 seats
1982	Reagan	42%	-26 seats
1986	Reagan	63%	-5 seats
1990	GHW Bush	58%	-8 seats
1994	Clinton	46%	-52 seats
1998	Clinton	66%	5 seats
2002	GW Bush	63%	8 seats
2006	GW Bush	38%	-30 seats
2010	Obama	45%	-63 seats
2014	Obama	40%	-13 seats
2018	Trump	38%	-40 seats
2022	Biden	40%	-9 seats

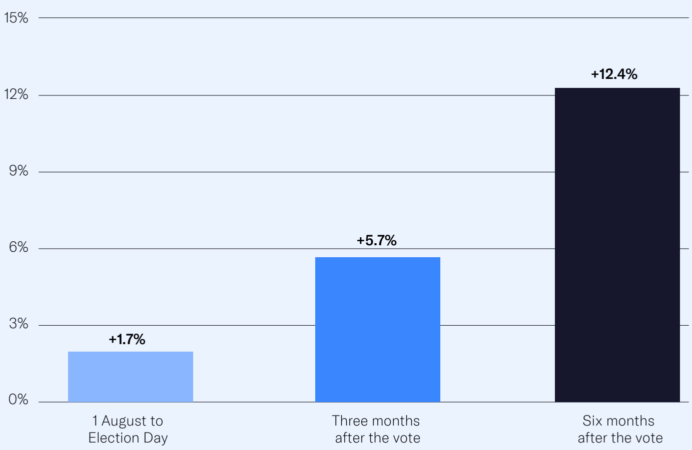
Source: Presidential approval data from Gallup; Midterm US House results from The American Presidency Project at UCSS

Trump is unlikely to leave the campaign to Republican candidates. He has already endorsed candidates, campaigned on their behalf and urged supporters to treat the election as a vote for his agenda. His involvement may increase as November approaches, particularly if turnout becomes a concern. A Republican defeat could be presented as a rejection of Trump's presidency, while a Republican victory would strengthen his influence over the second half of his term.

What history tells us about the markets during the midterms

The historical market pattern is more reassuring than the political one. Since 1974, the S&P 500 has delivered an average return of just 1.7% between 1 August and Election Day, a period when volatility has often risen as political uncertainty builds. Returns have historically been stronger once the vote is over: the average gain was 5.7% in the following three months and 12.4% over six months. In every midterm election in this 13-election sample, the S&P 500 was higher six months after the vote.[7]

S&P 500 returns around US midterm elections: average price returns since 1974 (%)



Source: Schwab Center for Financial Research, based on S&P 500 price returns from Yahoo Finance, as at 14 August 2026

Past performance is not a guide to future returns. Price returns exclude dividends.

This does not mean that elections cause markets to rise. Investors often become more comfortable once the result is known and the likely policy environment is clearer. Some uncertainty is removed, allowing attention to return to economic conditions and company earnings.

The pattern is not guaranteed. In 2022, high inflation and rapid interest-rate rises had a much greater influence on markets than the election itself.[8] However, going into the 2026 midterms, the fundamental backdrop has been broadly supportive, with strong corporate earnings and resilient economic growth outweighing uncertainty from geopolitics and changing expectations around inflation and monetary policy.

What could the result mean for markets this time around?

Markets are likely to focus less on the result itself than on whether it matches what investors already expect. A surprise outcome would be more likely to move markets than one already reflected in prices. A Democratic House and Republican Senate is the outcome markets broadly expect. If confirmed, it would mean a divided government, reducing the scope for major new legislation while increasing scrutiny of the administration and the potential for difficult negotiations over spending and the debt ceiling.

However, a Republican sweep could prompt investors to revisit the outlook for tax, spending and tariff policy. A stronger-than-expected Democratic performance could place greater constraints on the current administration's agenda and lead to more forceful oversight. In either case, the market response would depend on the implications for inflation, interest rates and company profits, as well as how investors were positioned going into the vote.

The impact could be clearest at sector level. Defence and infrastructure companies are sensitive to government spending, energy companies to tariffs and permitting, and healthcare companies to drug-pricing and regulatory policy. Technology and other growth companies have often performed well during rallies post-midterm, particularly when divided government reduces the likelihood of sweeping policy changes. Their performance will still rest on whether they can deliver on earnings expectations and on the direction of interest rates.

The result may matter more for which parts of the market lead than for the direction of the market as a whole.

The takeaway

Midterm uncertainty may unsettle markets before November. Once the result is known, this certainty could give equities room to rally. However, that historical tendency is not a reason to trade around the election. With economic growth and earnings broadly supportive so far, staying invested in a diversified portfolio keeps investors exposed to potential market gains. Ultimately, the lasting direction of markets will depend on the economy and company profits rather than on which party controls Congress.

Sources:

1 Reuters/Ipsos Core Political Data: Presidential Approval Tracker, Ipsos, 26 August 2026.

2 Thirteen House Rating Changes Toward Democrats as Seat-by-Seat Assessment Better Aligns with Our November Expectations, Sabato's Crystal Ball, University of Virginia Center for Politics, August 2026.

3 The House of Representatives is the lower chamber of the US Congress. It has 435 elected members, each representing a local district, and all seats are contested every two years. Along with the Senate, it passes laws and approves federal spending.

4 Redistricting Ahead of the 2026 Elections, Ballotpedia, accessed 27 August 2026.

5 For 80 Years, the President's Party Has Almost Always Lost House Seats in Midterm Elections, a Pattern That Makes the 2026 Congressional Outlook Clear, The Conversation, 19 January 2026.

6 Midterm Seat Loss Averages 37 for Unpopular Presidents, Gallup, 12 September 2018.

7 What the 2026 Midterms Could Mean for the Markets, Charles Schwab Center for Financial Research, 18 August 2026. S&P 500 price returns; dividends excluded; data from Yahoo Finance, as at 14 August 2026.

8 The Consumer Price Index, November 2022, US Bureau of Labor Statistics, 13 December 2022; Federal Reserve Issues FOMC Statement, Federal Reserve, 14 December 2022.

9 Balance of Power: 2026 Midterms, Polymarket, accessed 27 August 2026.

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