Political Economy Update: US Mid-Term Elections.

Highlights:

- ✓ ***The clean sweep of Democrats in the House of Representatives and the Senate mark a change in the trajectory of US politics for the next 2 years till the next presidential elections in 2028. The results of the mid-term election points to a sharp rejection of the incumbent US administration.***
- ✓ ***The win of the Democrats can lead to a reduction in uncertainty in global financial markets, even though the veto powers of the executive do not afford much space for any fundamental change in the direction of US polity.***
- ✓ ***For Asian countries, especially India, while the volatility caused due to tariffs might reduce, the downside risks owing to tariffs remain intact.***

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US Mid-Term Elections: An Analysis.

The US Mid-term election outcomes, where the Democrats have gained control of both the houses of US Congress i.e. the Senate and the House of Representatives signals a period of tension between the executive and legislative arms of the government, with a Republican White House endowed with veto powers and a Democrat led Congress without a veto-proof majority, i.e. 2/3rd majority in both houses.

For countries such as India, this means there may be no major shift in US foreign policy or its tariff policies since the US President as the head of the executive function can veto any decision that gets stuck in a Congressional fight between the Republicans and Democrats. While the initial reaction of financial markets has been very positive, like the Brent Crude oil prices moving southwards of USD 100 per barrel, once the limitations of the victory set in, markets should stabilize at USD 85-95 per barrel conditional on geopolitical events in the Middle East.

Initial reaction of global financial markets: The mid-term elections have given Democrats control of the US Congress for the remaining term of Donald Trump's presidency offering hope to financial markets around the world of a possible de-escalation of the US-Iran conflict, and a respite from the commodity inflation plaguing most economies. Also, specifically for India, the election outcome may bring in better news as far as trade relations with the US are considered in the current context.

Global commodity markets have witnessed strong reactions with Brent crude oil prices declining sharply from USD 104 per barrel to USD 93-94 levels per barrel while other safe haven assets such as gold have risen. US Treasuries have moderated from 4.96 per cent to 4.84 per cent, due to expectations of a drop in political uncertainty while the dollar has weakened by 0.4-0.6 per cent due to an expected gridlock and increased scrutiny on AI related tech investments such as data centers by the Democrats.

The Democratic Majority is not veto-proof: For a veto-proof majority a two-third supermajority (greater than a simple majority) is required, which translates into a 67-seat majority in the Senate and 290 in the House of Representatives, which is rare. The Democrat win in both the US Senate and the House of representatives wrests the control of the US Congress from the Republicans to the Democrats and effectively makes this a divided government, with a Republican White House and a Democrat-majority Congress. However, the power of veto rests with the US President, and statistics on vetoes is not very encouraging as US Presidents have issued a total of 2,599 vetoes throughout American legislative history, and Congress has overridden 112 of them (about 4.3 per cent of all vetoes)

War and Peace: On both the US-Iran and the Ukraine-Russia war, diminished presidential influence in the US Congress, can mean extremes on both sides as the US president may be more restrained as an effect of the diminished influence on the legislative or try to be extremely adventurist in defense and foreign policy creating increased uncertainty for global economies. Experts[1] believe that the next two years of the President's regime might be more focused on foreign policy than the previous two years as he might want to leave a legacy of ending the war in Ukraine before he steps down.

What happens to Tariffs? The presidential authority to impose tariffs is delegated by the US Congress to the President, and just change of control of the Congress will not automatically change the tariff policy per se. Any change to be made to override the veto requires a two-third majority or a supermajority in both chambers (House of Representatives and Senate), which is unlikely. Hence, the tariff policies might remain largely unchanged but with ensuing fights and legal challenges in addition to increased negotiations with the affected trading partners causing more delays in policy implementation.

What it means for India?

The Democratic win is likely a mixed bag for US-India relations:

- The biggest immediate positive for Indian markets has been the sharp decline in Brent Crude oil near month contract from USD 102 to USD 94 per barrel, calming fears of extremely adverse inflation views and a widening CAD going ahead. This has also resulted in market rallies in both the debt and equity markets, with the 10Y G-sec yields ebbing below the 7.10 per cent level and the Nifty 50 reaching an intraday high of 24,579.90 and closing 24,536.60 (+576) or 2.4 per cent higher than

[1] What does Asia make of Democrats taking control of Congress? Joshua Kurlantzick, Council of Foreign Relations.

its previous close. On equities market expectations of a surge in the so-called AI-hedge flows are expected, and to an extent validated as the ~10 per cent rebound in Indian equities has coincided with a ~7 per cent sell-off in tech heavy Asian markets.

- If there is relative calm on the global front, especially now with Iran allowing select country ships to transit through the strait of Hormuz and the US Congress being able to keep a check on the Iran war, Brent crude oil might stabilize in a zone of USD 85-95 per barrel, bringing much wanted relief to policy makers in India on the USD/INR which has stabilized to an extent after RBI's measures and even appreciated after the decline in crude oil was more pronounced. More importantly if the upside risks to inflation moderate, RBI might consider the overall hikes to be less than 100 bps in this cycle.

- The US-India trade deal will be affected by multiple factors as the Republicans in general and the US President in particular might want to fast track a trade deal with the intention of getting more wins abroad while domestic policy making is now restricted. In the current scenario, the US-India trade deal outcome seems uncertain, with a more restrictive demands put forth by the US administration leading to a possible deadlock in the trade deal.

Conclusion: Indian markets have rallied across the board, especially the fixed income markets, as the 10Y closed trading at 7.19 per cent on the day of election outcome and further fell to 7.07 per cent on November 5th, 2026, on falling crude oil prices. As the US turns its focus on the presidential primaries for 2028, the potential candidates will analyze the mid-term election results to hopefully forge a more non-interventionist path. Until then the tussle between Republican White House and a Democrat Congress will only lead to more delays in policy making by increased oversight and legal investigations but might not change the overall direction of US foreign policy or its usage of tariffs on trading partners. The worst outcomes of the US President choosing to become emboldened post the mid-term outcomes and implement policies that he seems fit, can be bracketed as a more outlying scenario, but one that has a non-zero probability. This will assume increased importance especially in the context of the ongoing US-India trade deal negotiations.

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