

Allianz Global Investors

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Democrats take Congress, but sweeping change looks unlikely

The 2026 US midterm elections have delivered Democratic control of both the House and the Senate. In our view, the outcome points to more political friction than policy transformation. But greater congressional oversight and constraints on the administration could make the policy backdrop more predictable for investors, while shifting the relative appeal of sectors, asset classes and regions.



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What happened?

The US midterm elections have handed Democrats control of both the House of Representatives and the Senate, a reversal from current Republican majorities. Democrats have outperformed most pundits' expectations, winning seats in many staunchly Republican states which President Trump won by large margins in 2024. Moreover, Democratic candidates also won key governorships in Ohio, Texas and Georgia.

The result reflected voter concerns about affordability and the economy, unease over the conflict with Iran, and broader dissatisfaction with the administration. Key races in South Carolina and Texas helped to shape the final outcome. While some ballots are still being counted and a small number of races may remain too close to call, the overall shape of Congress is now clear.

Initial market reaction

The initial market reaction was pronounced; Treasury yields fell, the US dollar weakened and equity futures declined[1] as investors assessed the implications for fiscal policy and economic growth.

While it is too early to draw firm conclusions from the initial moves, investors appear to be focusing on what a Democratic sweep could mean for policy, including greater constraints on defence spending and a reduced risk of contentious debt-ceiling negotiation. Greater support for AI and data centre regulation could also have implications for markets.

What does it mean for policy?

While the result reshapes Congress, it does not fundamentally alter the balance of power in Washington. Democrats have won a majority in the Senate, but this remains well below the three-fifths of senators needed to break a filibuster and two-thirds of both chambers necessary to override a presidential veto. With President Trump retaining veto authority, major Democratic legislation will face a high hurdle. Investors may therefore focus less on sweeping legislative change and more on where the new Congress can constrain the administration through oversight, appointments, funding and bipartisan legislation.

That influence is likely to be felt in several areas. Democratic lawmakers are expected to challenge parts of the president's agenda, with varying levels of success. They are likely to push back against further increases in defence spending, while using congressional hearings and appointment processes to scrutinise other parts of the administration's agenda. Impeachment proceedings against the president remain a wildcard.

Meanwhile, Congress has little sway over trade policy and limited ability to curb immigration enforcement, and Democrats will have to build a bipartisan coalition to successfully pass a war powers resolution to restrict the conflict with Iran.

In our opinion, despite the election outcome, the macroeconomic backdrop may change less than the headlines suggest. Fiscal tightening remains unlikely, deficits are expected to remain elevated, and the broad direction of economic policy remains constrained by divided political authority. Treasury markets could face a modest risk-off reaction.

Our view: implications for investors

- Beyond the initial reaction, the size of the Democratic majorities and the balance of power within the party will be the main drivers for equities and the dollar. Investors will look closely at the composition of the incoming Congress for clues about the direction of policy on taxation, regulation, healthcare and spending.

- A more moderate agenda, such as limiting cuts to US healthcare and food assistance programmes, could support sectors like healthcare and consumer staples, although it would add to deficit pressures. Efforts to check executive power could improve policy predictability, while more progressive proposals on regulation and taxation could raise market concern.

- AI is one area where the new balance of power could matter. Democrats may push for clearer frameworks around AI deployment and governance, and greater uncertainty over regulation, capital expenditure plans or returns on investment could challenge market assumptions, including the aggressive pricing of some AI stocks. At the same time, the scale of AI investment means traditional political playbooks may prove less reliable than in past cycles.

- Defence and financial sectors could underperform as Democrats push back against the ongoing US-Iran conflict and block a rapid expansion in the defence budget, while the deregulatory agenda of the administration is likely to see some scrutiny. In addition to any risk-off tone, Treasuries face a more supportive environment: with both chambers unified, the risk of a contentious debt ceiling debate has declined and supply risks from an expanded defence budget have been curtailed.

1. Source: Bloomberg, 4 November 2026.

- That said, in our view the longer-run fiscal implications are cloudy, and the deficit implications depend on which priorities Democrats pursue.

- If investors respond by seeking diversification away from US equities, Europe and parts of Asia could benefit, with a shift between regions more likely than a change in overall market direction. While a somewhat weaker dollar may be anticipated in the short term, over the long run increased oversight over the executive and greater institutional credibility would be supportive.



What happens next?

With the 11 December government funding deadline approaching, shutdown risk remains high unless spending bills pass soon. Republican leaders will need to use the election defeat to persuade fiscal hawks to support a reconciliation bill during the post-election session of the outgoing Congress. The bill would likely raise the debt ceiling and increase defence spending. Democrats, meanwhile, may prefer to delay budget talks until next year, when the new Congress takes office in which they regain control. These conflicting priorities and the short time available for talks increase the risk of a shutdown.

We believe Democrats could address affordability concerns through raising the minimum wage, investigating corporate price-setting techniques, and extending healthcare subsidies, but are likely to face Republican opposition.

We think a Democratic sweep ultimately brings greater political tension than fundamental policy change. Signalling ahead of the 2028 presidential elections will be a top priority. While the election outcome may increase scrutiny of the administration, investors could conclude that Washington remains structurally constrained, limiting the prospects for dramatic shifts in the economic outlook.

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