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The flow of information shows that the economy is in the early stage of recovery from the deep economic shrinkage of 2008 when the only idea agreeable to the majority was to throw money at it. It helped get us to here.

The stories of epic financial misdeeds pock marked by big time swindlers and predators marked the end of the destruction phase. Now we are gleaning from the wreckage the wisdom to repair institutions and guide policy. New revelations about Fred and Fannie are revealing what must be the grossest manifestation of bad policy and rapacious politics in modern times. The logic of rules shaped by the new Congress will be informed by the excesses now visible to all who will see.

Other signs of vitality are: good demand for discounted assets, a flattening of the downtrend in real estate prices with a recent uptick, a large increase in labor output per hour which will enable profit margins to pop right away, a workforce so lean that orders to restock sold out inventories will be followed by a surge in hours worked followed by a surge in new hires. We are in for a period of economic-business news surprises, mostly good. That's the upside.

Can you imagine what would happen if the youth in Iran unseated the ancient ones to gain freedom from oppression and revise the balance of power in the region? Perhaps it would inspire a revaluation of American freedoms and whether they are being respected and protected. That can happen in 2010.

Political forces are in motion which look strong enough to change profoundly the allocation of Congressional power this year. Investment implications are ill defined because government policy is transitory and could stay that way until new forces impose themselves. However, early thoughts focus on policy reversals that would be obvious: economic policy and taxation, the appropriate limits of government power, the affordability of domestic entitlements, and an assessment of international relationships and strategies, a subject recently rich in absurdity.

Taking the easy ones first, the acceleration of inflation would be moderated by policy reversals, but not eliminated. Until America is seen as being willing, politically, to get back on budget, the need for investors to cope with inflation will persist, but with a diminished priority.

Tax revulsion should be the next stimulant in the political buildup. When the stress of tax extraction rises, the energy of the revulsion will rise. By election time the intensity should be palpable. The probability of positive political surprise is high here too. As I was writing this, news broke that Senators Dodd and Dorgan announced they would not stand for reelection… and that's just among the Ds.

Investment implications of the political currents are healthy with respect to the improving likelihood that US politics will work toward a sustainable balance aimed at economic stability, a rising quality of life, and social support programs designed to be sustainable beyond the lifetimes of those given to empty promises.

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A turn toward normalcy in risk aversion is underway as money flows rise and world commerce keeps on growing. Political remedies for economic maladies are often clumsy but we learn as we go. The next change in public money flow will be for less, not more, on the expectation that natural economic vitality will take it from there. So, allocations among domestic and foreign equities should be maintained, and the same is true for conservatively financed real estate which seems at or near a price bottom. Audible worry about the ability to refinance the forthcoming maturity of commercial real estate is still out there, but here I feel not sufficiently competent to contribute. On the debt side, inflation protected US bonds and short term corporate bonds are good. Long term dollar price trends of energy materials, commodities and gold are likely to continue a gradual rise, reflecting cyclical demand trends and inflation. It is not a good time to buy long term bonds.

American energy security is improving very well and will be seen as a source of competitive strength, not vulnerability, for these reasons:

1) We are beginning to grasp the immensity of North American natural gas potential owing to recent advances in drilling technology.

2) Political resistance to generating electricity from radioactive energy is dissipating as fearful memories fade.

3) An open door to offshore drilling is a no-brainer.

4) Remember Y2K? The current version centers on carbon dioxide, CO_2, which by government proclamation now has the legal status of "pollutant" especially the CO_2 stimulated by human activities. The whole concept, including planetary temperatures, polar bears and Al Gore, is imploding as the light of ethics and scientific logic illuminates the data at hand and gave us a good informative look at third world leaders telling what they want from the developed world.

May it always be so that science can be suppressed and bullied only temporarily. Carbon will regain its benign reputation, "Cap and Trade" will fade and prices will guide the way to a rational succession of energy sources, assuming free market prices. Legitimate concerns with man made toxins will persist, of course.

One national security risk factor relates to the degree to which basic US economic functioning is supported by oil flows, the consequences of interruption, and the extent to which US policy ought to respect that exposure. Given the discernible attitudes of current government decision makers and the labor and civic organizations with which key government figures are allied, the chance of doing economic harm is worrisome.

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It is uneasy to be an investor in troubled times, but prices are marked down so as to make it worth the while. The economic machinery, with technology, inflation and human nature in the mix, is fluid enough to be interesting and logical enough to permit us to enjoy the rewards.

The past year has been engrossing by virtue of the drama and portent of world class developments. The new year seems likely to be similarly intense and decidedly more positive.

Best wishes,

John May