

This was essentially the setting for the President's proposals last September to moderate the capital goods boom.

While the suspension of the investment tax credit and the use of accelerated depreciation on structures were elements in the subsequent cooling down of the capital goods expansion, there were other factors working in the same direction. I shall cite two important ones:

One, some of the major sources of private demand have been less buoyant since mid-1966. Retail sales have been on a virtual plateau since June a year ago; auto sales, in particular, have continued at lower rates than in the early months of 1966. Housing starts, which had declined to exceptionally low rates last October and November, have continued to be weak compared with the first half of 1966, although preliminary figures for May show a good rise over April.

Two, corporate profits after taxes, which had risen in the fourth quarter of 1965 and in the first quarter of 1966, weakened during the second half of the year, and then turned down sharply in the first quarter of 1967. The trend of profits is an important consideration by corporations in making their investment decisions concerning the period ahead.

As capacity expanded and the intensity of many sources of demand waned, the rate of manufacturing operation declined—from 19 percent of capacity in the third quarter of 1966 to 87 percent in the first quarter of this year (FRB basis). This was also a basic development which influenced businessmen to revise downward their earlier investment programs and to scale down sharply their projected increases in capital outlays for 1967. In view of the swift cooling off of the investment boom, an early restoration of the investment tax incentives to help bolster such demand was indicated.

This is, briefly, the background for considering the outlook for fixed nonresidential investment in the near term.

According to a report issued earlier this month, based on the survey of plant and equipment expenditure programs conducted in late April and May by the Department of Commerce and the Securities and Exchange Commission, businessmen anticipate only a 3-percent rise in their 1967 capital outlays over 1966; this compares with a 16½-percent increase last year.

The pattern of anticipations during the quarters of 1967 is shaped saucerlike; i.e., the actual decline of almost \$1¼ billion (at annual rate, seasonally adjusted) in the first quarter of 1967 is expected to be followed by a further small drop in the current quarter, an increase of \$1¼ billion in the third quarter, and another rise of \$¾ billion in the fourth quarter. All major industries are anticipating smaller increases in 1967 than in 1966 with the exception of railroad companies, which report a sizable decline. (See chart 4.)

(Chart 4 follows:)