THE CHAIRMAN OF THE
COUNCIL OF ECONOMIC ADVISERS
WASHINGTON

June 30, 1966

MEMORANDUM FOR THE PRESIDENT

Subject: The Stock Market Decline

1. The stock market declined sharply this week.

   - The Dow Jones industrial average closed yesterday at 872. This was 26 points -- about 3% -- below the close last Friday.

   - The average was still 1% above the 1966 low reached on May 17.

2. The market has been generally declining since early February -- though there have been periodic recoveries.

   - The Dow Jones average reached its high 995 on February 9.

   - Stock prices then declined sharply until mid-March, after which they moved generally upward until the end of April.

   - There was a sharp slump in early May, then a recovery through last week.

3. The decline of 13.2% from February 9 to May 17 compares with a drop of 10.5% from the May 1965 peak to the low last June.

4. We have found no specific cause for this week's drop.

   - There are no indications that selling is dominated by institutions or other special groups.

   - This year's good earnings prospects were reflected in stock prices early in the year.

   - Since then, investors have become worried about

     -- the effects of tight money,

     -- the recent slowdown in the economic advance,

     -- the possibility of higher taxes or controls, and, more generally,

- -- the war in Vietnam and what it may portend.

- In short, they are <u>uncertain about the economy</u> and can get <u>good returns by buying bonds</u>.

5. A market decline in an expanding economy is not as bad as it appears -- indeed it is <u>probably a healthy sign</u>.

- We would have much more to worry about if the market were booming.

- That would indicate a general belief in uncontrolled inflation and leave us exposed to the risk of a real crash.

Gardner Ackley