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Stimulus talks weigh on JPY

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- **JPY testing 108 on stimulus talks**
- **Sell JPY on rumour; buy JPY on fact?**

JPY testing 108 on stimulus talks

Overnight Kyodo News reported that Japan is considering JPY 20 trillion fiscal stimulus package to help the domestic economy emerge from deflation and fend off possible adverse effects of Brexit. This is more than an initial plan of just over JPY 10 trillion yen. The stimulus package will include projects for fiscal year 2017 and beyond and increase 'zaito' low interest government loans by JPY 6 trillion. The government is reported to seek Cabinet approval in early August. The Japanese yen was sold off with stops being triggered above 107 against the US dollar early this morning. Firmer equity markets and improving risk sentiment (VIX declined to below 12, lowest level since August 2014) also weighed on the yen.

Sell JPY on rumour; buy JPY on fact?

In our previous note, we had mentioned that the yen is expected to find strong support around 107-108 region. We expect domestic life insurers and exporters to increase their hedging activities as the yen weakens. Given that market expectations of more powerful fiscal and monetary stimulus are high, there is also a risk that the yen may recover if such expectations are not exceeded. Technical indicators in the yen hourly chart also imply that the yen is in oversold territory and hence some recovery in the yen is likely. Having said that, ahead of the BoJ monetary policy meeting on 29 July, we expect unwinding of speculative long yen positions to cap yen strength around 106. Looking ahead, we think that there are limits to yen weakness in the absence of Fed raising interest rates.

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