Japan has been in recession or growth recession for most of the 1990s and does not look promising as an engine of growth for the world economy. The ongoing problems in the Japanese financial system have been exacerbated by the Asian crisis, and the government's attempts to reflate either through fiscal or monetary policy have so far not had lasting success. Japan is different from the other Asian economies in that its debt problem is a domestic one and that the Japanese government has the means to address the problem using its own resources rather than relying on foreign financing. However, the willingness of the government to take swift remedial action, which would in effect mean the failure of more financial institutions, remains highly questionable.

The absence of an obvious engine of growth for the world economy led many participants to be doubtful about a rapid export-led recovery for the Asian economies.

Debt vs Equity in the Evolving Crisis

The financial dimensions of the crisis are moving into the next phase, which will be dominated by questions of debt moratoria, nationalisation of debt, and debt restructuring / rescheduling negotiations. With it will come a new set of issues such as bankruptcy legislation (some of the affected economies have very poorly developed laws), competition policy, debt-equity swaps, and securitization of debt, which could lead to the deepening of Asian bond markets.

On the side of the most severely-affected banks and their national regulatory agencies, the emerging issue will be that of write-downs -- not a question of if, but when and how much. Tables 2 and 3 summarise the debt profile of the major affected Asian economies and the exposure of international lenders, including Canadian banks. Unlike the Latin debt crisis of the 1980s, American banks are much less exposed to Asian debt and so far, there has been virtually no talk of systemic risk to the global financial system. While bank lending is not likely to rush back to Asia, equity investors, having already "written down" their losses, will be looking for the best time to return to Asian markets.

It was suggested that this return of funds to Asia could be massive and rapid for two reasons: i) the very high level of liquidity held by fund managers who are scouring the