

**Financial crisis and the interbank market:
Japan's banking crisis in 1997-98**

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Abstract

We examine the interbank market in Japan during the 1997-98 banking crisis. We find almost no relationships between borrower risk and borrowing terms in the pre-crisis period. In contrast, we find that riskier banks borrowed less from the interbank market during the crisis period. These results suggest that lenders became highly sensitive to borrower risk, and thus, counterparty risk played a key role in disrupting the interbank market during the crisis.