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# A DYNAMIC NETWORK MODEL OF THE UNSECURED INTERBANK LENDING MARKET\*

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## ABSTRACT

We introduce a dynamic network model of interbank lending and estimate the parameters by indirect inference using network statistics of the Dutch interbank market from February 2008 to April 2011. We find that credit-risk uncertainty and peer monitoring are significant factors in explaining the sparse core-periphery structure of the market and the presence of relationship lending. Shocks to credit-risk uncertainty lead to extended periods of low market activity, intensified by reduced peer monitoring. Moreover, changes in the central bank's interest rate corridor have both a direct effect on the market as well as an indirect effect by changing banks' monitoring efforts.

**KEYWORDS:** Interbank liquidity, financial networks, credit-risk uncertainty, peer monitoring, monetary policy, trading relationships, indirect parameter estimation

**JEL CLASSIFICATION CODES:** C33, C51, E52, G01, G21

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