Transcript Analyst Call 3Q2022

ING

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Presentation

Operator
Good morning. This is Mark, your operator, welcoming you to the ING's 3Q 2022 Conference Call. Before handing this conference over to Steven van Rijswijk, Chief Executive Officer of ING Group, let me first say that today's comments may include forward-looking statements, such as statements regarding future developments in our business, expectations for our future financial performance, and any statement not involving historical facts.

Actual results may differ materially from those projected in any forward-looking statement. The discussion of factors that may cause actual results to differ from those in any forward-looking statements is contained in our public filings, including our most recent annual report on Form 20-F filed with the United States Securities and Exchange Commission, and our own earnings press release as posted on our website today. Furthermore, nothing in today's comments constitutes an offer to sell, or a solicitation of an offer to buy any securities.

Good morning, Steven. Over to you.

Steven van Rijswijk
Thank you, Operator. Good morning and welcome to our third quarter '22 results call. I hope you're all well. As usual, I'm joined by our CFO, Tanate Phutrakul, and our CRO, Ljiljana Čortan. I'm pleased to take you through today's presentation. After that, we will take your questions.

It has become a recurring theme that we operate in a challenging environment and also recurring is that we perform well under these circumstances, and with our strong positioning and strategy I'm confident that we will continue to do so.

That conference applies to a successful execution of our strategy as well as delivering healthy financial results, and I am proud to see our people making an effort every day to create a superior experience for our customers and to support the transition to a more sustainable society. The results of these efforts were again visible this quarter: more primary customers, a leading NPS position in more countries, as well as more sustainable deals and volumes mobilised.

On our financial results, the accelerating NII momentum is a clear tailwind, while fee income proved to be resilient. Expenses were well-contained, despite the increasing inflationary pressure from indexation and contained investments to realise our strategy.

Loan growth continues, with good growth in wholesale banking and a slightly slower pace in retail. Risk costs reflect our prudent approach of taking management actions to incorporate the uncertainty posed by the economic environments, and we continue to operate with the low stage 3 ratio and with confidence in the quality of our loan book.

Finally, our capital position remains strong, which allows us to take another step in returning capital to our shareholders as we announced today a distribution of €1.5 billion.

Separately, although not a third-quarter event, I would like to address the ECB decision to change the TLTRO programme. As a result of changed conditions, we have had to unwind our TLTRO-related derivative position. The impact of this action adjusted for TLTRO benefit until November 23rd 2022, will lead to a negative impact on pre-tax profits of around €315 million in the fourth quarter.

Now, before we go into the quarterly figures, I will spend some time on our strategic priorities, our outlook in the current environment and the return of capital.

Slide three clearly shows how the world around us has continued to change since our investor update in June, fuelled by growing geopolitical instability and high energy prices. Interest rates are forecasted to remain at a much higher level, while inflationary expectations for 2022 and 2023 have increased significantly, before being expected to taper off in 2024.

Not surprisingly, this impacts the GDP outlook, which now includes a recession, although the expected economic contraction is still relatively modest. Overall, the impact of the energy shock is cushioned by two main factors.
First, labour markets have been tight following the pandemic. Employers can be reluctant to lay off workers, while those losing their jobs can quickly find a new one. Overall, this lowers the risk of high unemployment.

Secondly, while consumer confidence has been impacted, governments have been quick to offer large support packages in this cost-of-living crisis and to help both customers and companies cope with higher energy prices. Although bankruptcies can be expected to go up from the low level seen during the pandemic, the impact of difficult external conditions on corporate sentiment is still relatively mild.

For the near term, uncertainty remains high and it is hard to predict how things will evolve. We will manage through these times while we will also keep our eye on the longer term, on executing our strategy, which brings me to the next slide.

Slide four shows a selection of actions we have taken and the results for our two strategic priorities, a superior customer experience and sustainability. In Retail, we introduced new products and solutions with a focus on digital-only, mobile-first, to offer that superior experience that we strive for. For example with a new account in Spain, co-created with customers and offering instant digital onboarding. On the business side, we co-created an app that can be used in stores for easy access to contactless payments, to be piloted by a large retail chain in the Netherlands.

The hard work of our people on improving the experience for our customers has yielded good results. The share of customers using only mobile, went up by four percentage points, now reaching 57%. In 7 out of our 10 retail countries we had a leading NPS position, a step towards our ambition to have the highest NPS score in all 10 retail countries. This supported further growth of our primary customer base because we added 139,000 primary customers this quarter, bringing the total to 14.4 million.

On sustainability. In Retail, we introduced the eco-mortgage in two more countries, Germany and Italy, supporting our customers' transition to more sustainable homes. We will continue to expand our green product offering, in line with our target to have a green alternative for all our key retail products by 2025.

In September we published our 2022 climate report. We have now updated the intermediate 2030 targets for the sectors covered by our Terra approach. In Wholesale Banking, our colleagues' efforts on financing the transition have paid off with both volume mobilised and the number of sustainability deals growing compared to last year.

As we continue to focus on executing our long-term strategy, our near-term financial results are affected by the changing world around us. To start with the rate environment on Slide 5, that shows the positive development for ING.

We have mentioned before we will benefit from high-interest rates, with the benefits coming in over time as our replicating book gets reinvested against higher rates and also depending on the speed of pass-through.

During our investor update we gave you an estimate based on the sensitivity of our retail Eurozone book with an illustrative instant 50% pass-through scenario, which already gave insight in the potential upside. As we've seen the curve steepening since then, the upside has gone up. The updated sensitivity includes an illustrative gradual pass-through scenario to reflect the increased asymmetry with the replicating results in an environment with such rapidly rising interest rates.

The sensitive analysis clearly shows the increased NII tailwind for coming years. And already now, after years of downward pressure from negative rates, the boost in liability NII is visible in our results.

Then on to Slide 6, first on how the outside world affects our cost base. The impact of the increasing inflation rates actually doesn't need much explanation. We've talked about it before, that it impacts our staff costs, this quarter mainly through indexation. As an example, the legally required bi-monthly indexation in Belgium has so far driven up staff cost there by more than 7%. That's a number you can't fully offset anymore with all the good actions taken in Belgium to restructure the service model and change the footprint.

Next to indexation, in several countries we announced voluntary compensation to help our people cope with the rising energy prices. These one-off amounts will be booked in the coming quarters. As mentioned, we also continue to invest in our long-term performance, in digitising customer journeys and also marketing campaigns, to ensure we keep increasing the number of primary customers as the base of future success. Going forward, we steer to keep cost growth below the inflation rate.

Then to asset quality. Why I'm addressing the topic here, is because we generally see thematic concerns from the outside world increasing as the economic environment becomes more challenging. And I want to emphasise that we don't always

share these concerns. We are confident in our asset quality and our conviction is underpinned by our solid risk management framework and proven by our strong track record.

To highlight some characteristics of our loan book that support our confidence, our retail lending is primarily mortgages, with only a small consumer lending book. We operate at low LTVs, though our main focus is on affordability of the loan.

To illustrate, our largest mortgage book is in the Netherlands where 94% of the book has an LTV below 75% and in general home ownership is concentrated on higher income groups. The same group which is more likely to have savings and less likely to be affected by layoffs. During the global financial crisis we did not have material losses in this book and with a better risk profile now, we have no reason to believe it will be different in the current situation.

On our loan book to companies, the majority is to large companies, with a focus on investment grade. These companies are not immune to economic challenges. However, they generally do have larger buffers to withstand economic headwinds.

Then moving to slide seven. Over the past years, we have built a strong track record of delivering attractive yield to our shareholders. Going forward, ING continues to be a good investment case with consistent strategy execution, income growth, well-contained expenses and strong asset quality.

Combined with our strong capital position, we are in a position to return capital to our shareholders. And I'm pleased that today we have announced another step in converging to our targeted CET1 ratio of around 12.5%, with a €1.5 billion distribution. We aim to execute as much as possible in 2022 via share buyback, with any remainder to be distributed in cash on January 16th, 2023.

So, now let me take you through our third quarter results starting on slide nine. Our pre-provision profit was up almost 19% year on year and 9% quarter on quarter. I'm happy we realised another very good quarter in today's markets.

As mentioned, in NII we see the impact from the improved yield curve. The drag on liability margins from negative rates from the past years turned into an increasing tailwinds. And we also continue to benefit from higher rates in non-Eurozone countries.

On lending NII the picture was slightly different, as client rates generally track higher funding rates with some delay and prepayment penalty income continue to level off to more normal levels, although quarter on quarter we see that effect is bottoming out.

Looking at the P&L lines, fees in daily banking continue to grow, while uncertainty impacted fees on investment products and lending. Overall, with 4% fee growth realized year to date, we continue to target an average of 5% to 10% annual growth.

Operating expenses reflected inflationary pressure, mainly in staff costs. Overall, with measures taken to control expenses, we contained the upward pressure and kept cost growth well below inflation rates.

We did see some volatile items this quarter, including the previously announced expected impact from the Polish moratorium. In Belgium, we had an exceptional €-288 million hedge accounting impact, with a mirroring positive impact to be recognised over the coming years. We also added €75 million to the compensation for customers on certain Dutch consumer credit products.

Then we move to slide 10. Year on year NII was up 8.5%, excluding the expected impact from the Polish moratorium, mainly due to the accelerated recovery of liability margins I mentioned earlier, combined with a higher FX ratio hedging results. We continue to see some pressure on lending margins in the third quarter, reflecting a delay in tracking higher funding rates and lower prepayment levels on mortgages, although we see this bottoming out.

Quarter-on-quarter NII was up 6.1% excluding the Polish moratorium, again supported by improved liability margins offsetting some remaining pressure on mortgage margins due to the reasons I just cited. Excluding the Polish moratorium, our net interest margin for the quarter was up at 142 basis points, mainly reflecting the higher NII on liabilities.

Slide 11 shows net core lending growth. In Retail, mortgages continue to grow, mainly in Germany and the Netherlands, although at a lower pace, reflecting an overall slowdown of demand driven by uncertainty. Lower net core lending in business lending was mainly visible in Belgium. In Wholesale Banking, loan growth was mainly visible in lending, partly offset by trade & commodity finance, reflecting lower commodity prices.

Going forward, with increased macroeconomic uncertainty, we expect loan demand to be subdued.
Net customer deposits growth was €10.5 billion, mainly driven by Retail, with a continued inflow especially in Germany. Wholesale Banking also recorded an inflow, mainly visible in our cash management business and financial markets.

Then turning to fees on page 12, which show resilience despite growing uncertainty that affected the appetite for both investments and lending.

Year on year, fee income was stable. Daily banking fees continued to grow, this quarter by an impressive 26% compared to a year ago. This reflected growth in primary customers, the increase in payment package fees and new service fees.

Lending fees were down slightly, while in investment products fees we continue to see the effect of lower stock markets and less trading activity. Sequentially we saw the same development, with 8% higher daily banking fees, while investment products and lending were lower driven by uncertainty.

Then on slide 13, excluding regulatory costs and incidental items, operating expenses were up on both comparable quarters. And as I explained, this is mainly the effect of high inflation rates coming in through salary indexation and CLA increases, while we also keep investing for future growth.

Regulatory costs were down on both prior periods. Year on year this was due to a lower deposit guarantee scheme contribution in Germany. Quarter-on-quarter this mainly reflected a one-off contribution in Poland to a new institutional protection scheme in the previous quarter.

Incidental items this quarter included a €75 million addition of the interest-on-interest effect to the compensation for consumers on certain Dutch consumer credit products and €10 million for hyperinflation accounting in Turkey. Overall, in light of the current operating environment and especially when looking at the high inflation rates, I'm pleased with how well operating expenses were contained.

Then on to risk costs on the next slide, which were €403 million this quarter, or 25 basis points of average customer lending. We booked €116 million reflecting updated macroeconomic indicators and recorded a net addition of €89 million to management overlays for the potential impact of secondary risks of the current macroeconomic environment. In total we built up €520 million in management overlays.

Risk costs also included the release of €77 million in Stage 2, reflecting a further reduction of our Russia exposure.

The increase in the Stage 2 ratio is mainly the result of a methodology change following IFRS accounting, rather than a deterioration in the risk profile of our loan book. This change impacted primarily investment grade exposure, with a very small impact on risk costs. The stage 3 ratio improved to a low 1.3%.

The next slide shows our CET1 ratio, which remains stable at 14.7%. CET1 capital was €0.5 billion higher, mainly due to the inclusion of net profit for the quarter. RWA were up by €2.7 billion, including €3.1 billion of FX impacts. Credit RWA were up slightly when excluding FX impacts, reflecting some model impacts while the overall profile of our loan book improved.

Market RWA were lower, reflecting a decrease in the capital multiplier for trading book positions. Furthermore, higher operational RWA reflected the update of the AMA model.

Concerning our distribution plans: today we have announced we will distribute an additional €1.5 billion via share buyback in 2022. Any amount remaining after the 31st of December 2022 will be paid in cash on January 16, 2023.

Slide 16 shows our financial targets as we presented them to you during our investor update. CET1 ratio remains well above our target of around 12.5%, also when including the €1.5 billion additional distribution we announced today. The cost/income ratio remains an important input for our ROE, and we continue to work on our ambition of 50% to 52%. This will be supported by the acceleration of liability NII and continued customer growth. We keep our expenses contained and continue to invest in our scalable tech and operation foundation, that will enable us to grow at a lower marginal cost.

ROE came in at 6.8% including some exceptional items over the past quarters and based on a high capital position. On a 12.5% CET1 ratio the pro-forma ROE was 8.9%. We maintain our ambition to provide an attractive total return and are well-positioned to do so with continued growth of customers and income, focus on managing expenses and asset quality, while we optimise our capital position.

To wrap up with the highlights of the quarter, our people make an effort every day to build a superior experience for our customers and to support the transition to a more sustainable society. We see these efforts positively reflected in primary customer numbers, NPS, as well as sustainable deals and volumes mobilised.

Our financial results showed that accelerating NII momentum is a clear tailwind, while fee income has proven to be resilient. Expenses were well-contained this quarter, despite the inflationary pressure of indexation in some markets and continued investments to realise our strategy.

Our capital position remained strong, which also allows us to take another step in returning capital to our shareholders as today we announced a distribution of €1.5 billion.

Overall, in a challenging environment we have delivered another good quarter and with our positioning and strategy, I'm confident that we will continue to deliver healthy financial results as well as a successful execution of our strategy. And with that, I hand over for questions.

Q&A

Operator
Thank you. If you wish to ask a question, please dial 01 on your telephone keypad now to enter the queue. If you find your question is answered before it's your turn to speak, you can dial 02 to cancel. In the interest of time, we kindly ask each analyst to limit yourselves to two questions only.

Our first question comes from the line of Giulia Aurora Miotto of Morgan Stanley. Please go ahead, your line is open.

Giulia Aurora Miotto (Morgan Stanley)
Yes, hi, good morning. Two questions for me. The first one I will start with is capital. I think the €1.5 billion distribution with the clear commitment by the 16th of January was very nice. Can I just double check that nothing has changed in terms of your commitment to ultimately get to 12.5% and therefore we should expect potentially another one with the full-year results. And the reason I ask is just because we keep seeing these headlines from the DNB for example, that banks should keep as much capital as possible, etc. So just a confirmation of that would be helpful.

And then my second question is on costs. So, cost came in a little bit worse than what the market was expecting, and inflation is above what probably you were expecting last time you gave guidance. So, can you tell us what do you expect for costs for this year, but most importantly next? Thank you.

Steven van Rijswijk
Yeah, hi, Giulia. Thank you very much. I'll take the question on capital and Tanate will take the question on cost.

On capital we have said also at the investor presentation in June that we would gradually move to around 12.5% in approximately equal steps. We've also said that we are in constructive dialogues with our supervisors. And, as you can see, that constructive dialogue has now led to the €1.5 billion that we announced today. We still have our target capital level that is significantly above the requirements of our supervisors. And to that extent, we will continue to be in constructive dialogue with the supervisors for also our next steps, but we will only announce them when we will announce them.

And with regards to your remark of the DNB, I think that the DNB made a generic remark about banks remaining prudent, and therefore also mindful of keeping adequate capital levels. Which is exactly what we do, because we have a capital level that is significantly above the target capital level that we have, and significantly above the capital levels that supervisors require from us.

Tanate Phutrakul
Hi, Giulia. Then on costs, we recognise that cost pressures are higher because of inflation, and we see that in markets where there's indexation of salaries like in Belgium and in Central and Eastern Europe. And I think a trend like that we see more and more during the course of 2022. Besides this, is the fact that particularly currencies in dollars or Asian currency are appreciating due to the weakening of the euro, and that has reflected also in the translated cost increase that we see.

Of the year-on-year results, which I think is a good trend line for you to analyse, our costs are up around €117 million, at about half of that is due to the aforementioned FX results and some higher than usual legal expenses. So, the underlying wage and procured expense increase, it's around 2.2%. That's maybe the underlying increase year on year. And then to reiterate the

point, we continue to make sure that next year our guidance is still that we will keep costs below inflation.

Giulia Aurora Miotto (Morgan Stanley)
Thank you.

Operator
Thank you. Our next question comes from the line of Raul Sinha at JP Morgan. Please go ahead. Your line is open.

Raul Sinha (JP Morgan)
Good morning, everybody. Thank you very much for taking my questions. Can I have two please on NII? I guess the first one is just going to your new disclosure around NII sensitivity for this gradual pass-through scenario which is very helpful. When I look at that and I take your underlying NII run rate which is sort of around €14 billion, it looks like the delta into 2023 and 2024 is obviously very significant and probably ahead of consensus. Just based on your Eurozone replicating results sort of €2.9 billion, the uplift over 2022 is €0.6 billion. So essentially looks like your NII is going to be up €2.3 billion on a net basis.

So, I guess the first question is, can you give us a little bit more holistic picture around what are the other factors that might be offsetting this when we consider the NII moving parts over the next years? Any more colour on that would be helpful. Or should we take this as sort of the main driver?

And then secondly, I guess related to the NII and just to understand this TLTRO hedging, can I ask what type of risk were you hedging with your derivative position, and your repayment profile versus what you had previously assumed? Thank you very much.

Steven van Rijswijk
Okay, thanks, Raul. I'll take the question on the NII and Tanate takes the question on the TLTRO hedging. On NII I think your question is what are factors that could impact the growth in NII income and also in the replication? I think in the replication as such, it is of course the level of pass-through, i.e. the tracking of the rates. And as you have seen, because the rates are moving so quickly, we have a gradual pass-through scenario assumed for now, but it's just a little illustrative.

Two, of course is, what will the lending NIM do, or lending margin do? And we are seeing some contraction in lending margin also, mainly in mortgages because of lower prepayment penalties coming in by means of the rising of the interest rates, and that is currently stabilising.

So, we don't see contraction anymore in that book. For the same token, of course, the mortgage duration is also increasing. As the most mortgage duration is lengthening, that can have an impact. And last but not least, we have loan growth, yet there we do expect a more subdued environment. We still see good loan growth this quarter in mortgages, and we also see it in wholesale banking, but it's lower than compared to some of the previous quarters, and for the next quarters, we see that loan demand a bit more subdued than we've seen so far.

Tanate Phutrakul
And then, Raul, on your question on TLTRO. We were clearly disappointed by this change of terms that we see from the ECB so close to the end of the programme. But in fact, if you look at the TLTRO before the change, it was a fixed interest rate instrument. And in terms of our asset liability management, we always manage the volatility of our interest rate margin. And what we did was actually hedge our interest rate risk, and what we have seen because of this announcement as of the 23rd of November, that fixed instrument has become floating. So, that means that we need to close our interest rate position, which we have done so during the course of the last few days.

Raul Sinha (JP Morgan)
Thank you. If I can just follow up on the first one, Steven. What has been your actual pass-through so far? Just trying to think about the 30% you assumed in 2023. I know it's early days, but can you give us an indication of where your pass-through has been overall?

Steven van Rijswijk
Well, if you look at what we see - what we know so far, in Germany we announced 30 basis points. Spain, I think we announced 30 basis points. Netherlands, we announced 25 basis points. Those are the biggest announcement that we've made so far.

Raul Sinha (JP Morgan)
All right. Thank you.

Operator
Thank you. Now next question comes from the line of Farquhar Murray, Autonomous. Please go ahead. Your line is open.

Farquhar Murray (Autonomous)
Morning all. Just two questions, both actually on the capital return point. Firstly, on the €1.5 billion, last quarter you kind of indicated it didn't need to come with results, and there were incentives to perhaps moving earlier. So, I just wondered if you could explain why this ultimately did come with results, and in particular is the regulator in the Netherlands maybe a little bit go-slow?

And then looking forward, you're still talking towards converting to the 12.5% in roughly equal steps. Could you give us a sense of the likely frequency of those steps, and might there be any chance of aligning it with the full year reporting from here? Thanks.

Steven van Rijswijk
Thanks Farquhar. Yes, there is not a story behind doing it not during the quarterly results and equally there is also not a story doing it during the journey quarterly results. So, there is no story behind that. We just are in dialogues. We look at the forecast, we do our stress testing, we submit the stress testing, we get feedback, and then we make a proposal that we discuss internally with the board, with the supervisory boards and then we get approved for it, those are the procedural steps. But there is nothing particular or there's no particular agenda behind doing it now or doing it before, but that process in this case coincidentally led to us being close to the publication of the quarterly results. So, that was the reason why we announced today.

And like I said, we remain in contact and good dialogue with our supervisors. We continue to do our stress testing. We continue to build up capital and profitability, and then we will go through similar process steps to look at further decreasing our capital towards 12.5% in the future. But again, taking that same process in mind, and whenever there is a step to announce, we will announce that step. There's nothing to report on that at this point in time.

Farquhar Murray (Autonomous)
Just as a follow on, I mean that process still sounds quite clunky. Does that mean it probably takes six months to really do each step?

Steven van Rijswijk
No, that's not the case. Maybe I explained it quite clunky, but its not as clunky as I explained it, so I apologise.

Farquhar Murray (Autonomous)
There's nothing to apologise for. That's really helpful. Thanks.

Steven van Rijswijk
Thank you.

Operator
Our next question comes from the line of Benoit Petrarque, Kepler Cheuvreux. Please go ahead. Your line is open.

Benoit Petrarque (Kepler Cheuvreux)
Yes, good morning. So, yeah, just to come back on the cost guidance of less than inflation. I think back to June, your own macroeconomist were going for roughly 3% for 2023. Now they are expecting 5.6% for 2023. Obviously, this is a quite large gap. So, for next year when you say below inflation is that below 5.6 or could that be below 3, below 4? Where are you for 2023? I guess you have a good idea now about the wage inflation in the pipeline. Could you update us also on the CLA negotiations in the Netherlands please?

Just wanted to come back on the asset margins. So, the lending margin actually, where you do see some pressure. Is that purely a timing issue that should be resolved in 2023, or are we going to see the same type of behaviour we've seen in previous cycles which is that you know lending margins under pressure when rates are just higher that's just normal and natural effect. Try to understand because it's quite clear to us that the NII benefit will be quite significant from the replicating part for your next year. But any indication about more potential negatives you expect will be useful. And that's it actually, that's two.

Steven van Rijswijk
Okay. That is clear. I will pick the question of lending margins and Tanate will take the question of cost guidance. On the lending margin pressure that comes in - as you know approximately half of our book is mortgages, and what you do see with

increasing interest rates are two things in a book. The prepayments are lower. People will not prepay their mortgages as quickly as they used to do. And that also means that our prepayment penalty income is lower, and that prepayment penalty income is added to the interest income. So, because that is decreasing, that causes one element of margin compression. That element is now largely gone.

So, you now see stabilisation of prepayment levels in our book, but over the last number of years when the interest rates became lower and lower, the prepayment numbers went up and now they went down again, I would say to before negative interest rate levels. So, they are normalising. The second element is that we need to refund. When we fund ourselves, those funding rates are only passed through gradually in our lending books. So, therefore, if funding increases, the margin of our total book contracts - because we fund ourselves at higher rates without having been able to pass these rates through, that takes time and is also dependent on the competitive environment.

So, now the rates are stabilising, then also the margin contraction will be stabilising and what we already see is that prepayment penalties are not contracting anymore. And currently, we also see margins greatly normalising. So, we do expect that margin contraction on the lending side for lending NII to taper off.

Tanate Phutrakul
Thank you very much. I will give a bit more insight on inflation and cost evolution. I think we're watching clearly carefully these revisions in inflation to be higher next year compared to this year. And not only are we watching it, also our labour counterparts are also watching it. So, we are in discussions with respect to our various different collective labour agreements and that we'll let you know once those things are agreed, okay? But having said that, we continue to be disciplined on our various different programmes. We continue to make efficiencies, and one thing that I can assure you is that cost discipline, revenue trajectory, means that we will continue to converge on our target for cost income ratio of 50 to 52%. And we don't see anything in the environment despite the increased inflation that we will not make progress next year on our cost income ratio.

Benoit Petrarque (Kepler Cheuvreux)
Great. Thank you, Tanate.

Operator
Thank you. Our next question comes from the line of Andreas from Goldman Sachs. Please go ahead. Your line is open.

Andreas Scheriau (Goldman Sachs)
Hello. Thank you very much for taking my questions. On deposit margins and the outlook for it please, if I may. Given where market rates and your euro savings rates are. Would you say that you could re-establish the historical deposit margin that you had achieved before the 0 lower bound kicked in, later this year potentially and beyond that? Can you help me think about what the new normal for deposit margins could look like? Is there anything structural that you see which would give you reason to believe in higher deposit margins than the one you have achieved several years ago? And to what extent then could that be offset by a lower asset margin?

And my second question on that topic is more to downside risks. The policy rate in the Eurozone is now well above your replication yield, I believe, something we haven't seen for many, many years. Are you worried about retail customers or the public more broadly looking at 2% plus policy rates soon and pressure building for you to raise retail rates beyond what the replication yield suggests, leaving you in a way over hedged? Thank you very much.

Tanate Phutrakul
If you look at historical margins on deposits, back ten years ago, I think the margin for ING was around 1%, right? But that 1%, has a very different composition from a customer basis. As Steven mentioned, we have made a key focus on improving primary customers. And as you know, primary customers bring with it a lot of current account deposits and that is a fundamental shift in what we've seen back in 2011 today. That a significant part of our deposit base today is in current account which attracts no interest payments for the time being.

So, with that in mind, I don't really see any reason why we can't get back to those historical margins, because even back ten years ago, interest rate were barely zero as well. So, it's not as if something has changed from that perspective. And I think your second question is around tracking. And again, you know we're giving you a simulation of where things would go, but how that would evolve in actuality really depends on market forces. So, that remains to be seen, but I think we give you an indication of how tracking may or may not happen based on the current curve.

Andreas Scheriau (Goldman Sachs)
Perfect. Very clear. Thank you very much.

Operator
Thank you. Our next question comes from the line of Kiri Vijayarajah of HSBC. Please go ahead. Your line is open.

Kiri Vijayarajah (HSBC)
Yes, good morning everyone. Just one question really from my side. So, if you look at the extra NII, you're going to get from the euro replicating book, clearly some big numbers there. My question is do you regret exiting France and Austria? They were predominantly deposit led franchises, and would the current rate environment have been enough for those businesses that you've exited to maybe have cleared their cost of equity? I know clearly cost/income was a problem there, but with this rate environment, would those businesses actually have been more attractive please? So, just your thoughts on those business exits you did when you first became CEO. Thank you.

Steven van Rijswijk
Yes, thank you. The short answer is no. In the end, you have to have businesses that are sufficient in size to be able to provide the right and superior services to your customers at a good cost/income level, with a diversified profile with right profitability, and also with these interest levels or even higher, that would not have been the case. So, we of course have made analysis of difference scenarios, but in the end, what you need to be successful in the markets is to be of sufficient scale with a sufficiently diversified business. And if that's not the case, then you need to see whether you're able in the context of that particular market to get to that point. And for those markets, we have concluded that that was not the case, but if you would ask me the question today, we would come to the same conclusion.

Kiri Vijayarajah (HSBC)
Okay. That's very definitive. Thank you.

Operator
Thank you. Our next question comes from the line of Tarik El Mejjad of Bank of America. Please go ahead. Your line is open.

Tarik El Mejjad (Bank of America)
Hi, good morning. Thank you for taking my questions. The first one is on the TLTRO. I know it's a one-off small number in the scheme of things, but are you - do you have the intention to take any actions against, or discuss with the ECB? Because that could set the precedent on revising any retrospectively, any agreements, or contracts in funding or whatever? I would ask the same question to other larger banks benefitting from TLTRO, but I would be interested to have your view on that.

And the second question is on the costs. I understand you'll be watching carefully the inflation for next year, but definitely will be higher than your early estimate of 2.3%. Can you give me some elements of potential extra savings that would be able to offset that and keep you on track for your guidance, or are you just hoping that the top line faster growth will more than offset that uptick on costs? Thank you.

Steven van Rijswijk
Hey, thanks, Tarik. I will answer the question. I'll happily answer the question on TLTRO and then Tanate will talk about growth. And why do I say happily? There's a bit of cynicism in there. We are very disappointed with the way that the ECB - how the ECB made that announcement. And if you look in the broader light of economic circumstances and the interest rate movements, we, of course, understand at some points you say, well that TLTRO programme is not needed anymore. But then we would have expected that to be done, at the point that such programme would lapse and not mid-stream. Also, after banks put their hedges on to cater for interest movements on that support. So, unhappy with that, disappointed with that. And I would like to leave it at that. So, I will also not comment on whether or not we're going to take actions. That is not for this call.

Tanate Phutrakul
Tarik, just on expenses, you talk about levels that are visible next year. I think it's the same as the ones we have disclosed before. We still have the impact of closure of some business units flowing through our financials next year. That will have a reduction in cost, for example due to the closure of our business in France. And we continue to be more efficient in our operations, continue to be more efficient with savings in IT.

Particularly, you see our focus on straight through processes that allow us to grow our business scalably, without adding any additional expenses to grow our business, and you see that operating leverage coming through as well. And of course, we have continued our programme to move the gravity of our operational staff from our home markets to our hubs, whether in Eastern Europe or in some markets in Asia, and those programmes will continue to be the case. And then there’s just the basics of negotiating our various different contracts to mitigate as much. The suppliers are asking for increases, but given the scale of our business, we believe we still have that negotiating benefit.

Tarik El Mejjad (Bank of America)
Thank you.

Operator
Thank you. Our next question comes from the line of Benjamin Goy at Deutsche Bank. Please go ahead. Your line is open.

Benjamin Goy (Deutsche Bank)
Yes, good morning. Two questions please. First, you're clear on loan growth, but actually I'm more interested these days in deposit growth. Was good in the quarter, but in particular driven by Germany and daily banking. So, wondering was that somewhat of a one-off effect given the stop of negative rate charging, or how do you generally view the outlook for the positive growth from here? And then secondly, wondering about your views or how you see the risks of bank levies, or anything like that in your three biggest markets, Netherlands, Belgium and Germany. Thank you.

Steven van Rijswijk
Thank you very much. If you look at the deposit growth driver, it was that when we stopped negative charging, deposits that previously left the bank came back. So, that has increased deposits quite a bit. And we will continue to work on growing our base and our primary customer base, and in Germany we're doing very well. If you talk about the bank levies in our markets, there was nothing to report on. There was nothing new that we are aware of, and if there would be something coming then we will let you know.

Benjamin Goy (Deutsche Bank)
Okay. Thank you.

Operator
Thank you. Our next question comes from the line of Anke Reingen of RBC. Please go ahead. Your line is open.

Anke Reingen (RBC)
Yeah, thank you very much. My first question is on your 2025 targets and the ROE targets. Obviously, now the NII expectations in absolute terms are higher than when you presented the plan. So, you think there's upside to our ROE target, or is this offset by higher costs? Or do you think you could potentially reach your target faster than previously expected?

And then secondly, coming back on the buyback. Your comment about the roughly equal steps. Just to confirm, I guess, should we look at the €1.5 plus the €300 million or is one step the €1.5 billion you just announced? And are you able to request a new buyback from the ECB while you're still executing your buyback? Thank you very much.

Steven van Rijswijk
Sorry, the third question Anke. So, you had one on the upside of ROE. The second one was on the roughly equal steps, and then the third one?

Anke Reingen (RBC)
Are you able to request a new buyback programme from the ECB, while you're still executing the €1.5 billion plan?

Steven van Rijswijk
Oh, okay. Okay, good. So, on the buyback and on the roughly equal steps, what we mean with roughly equal steps is roughly equal steps in terms of our CET1 decrease. That's how we define roughly equal steps, and then we therefore gradually move to around 12.5%. And how we then do it in terms of the number of share buybacks or capital distributions, we will see. That we will just work out over the next quarters and years how to do that. But you are now seeing that we tried to do that by decreasing our capital ratio in approximately equal steps, that's what we mean with that. And then the question are you able to do that while you're still executing this one? Well, look we're in continuous dialogue with the ECB on a full range of topics. And of course, also on our capital, and also our capital is reviewed on a regular basis. So, we have been in dialogue, will continue to be in dialogue. And when there's something new to report on the next step, then we will do so. When we talk about our ROE targets, it's good, I like her ambition. Let's first get to the 12% and then we start talking further.

Anke Reingen (RBC)
Okay. Thank you. Thank you.

Operator
Thank you. Our next question comes from the line of Amit Goel, Barclays. Please go ahead. Your line is open.

Amit Goel (Barclays)
Hi, thank you. So, my first question is a little bit along the lines of what Anke just asked, but just thinking with the better NII outlook. Just on the cost/income ratio target for 2025, 50-52%. Is that something that you think you can do better or to a large extent is the NII offset by potentially higher costs? And then the second question or related, I appreciate it was asked a bit earlier on, but in terms of the NII for 2023, do you mind just remind me what the potential offsets to some or partial offsets to some of the tailwinds are likely to be? Thank you.

Steven van Rijswijk
All right. Thanks Amit. So, on the offsets, there are the prepayment penalties, but like I said, prepayment penalties have come down because the people are holding on to their mortgages longer. It is the longer duration of the mortgages, because the people holding on longer, it also means that we need to hedge our funding at higher levels, so that could be an offset.

Loan growth, that is not necessarily on the replicating portfolio, but that is on NII and that was good this quarter. But we expect at least for next quarter a more subdued environment giving the economic circumstance. And the last one is of course, I think there was also I think a question asked by one of your colleagues, think was Goldman, about how much of the replicating portfolio will be tracked, and what are your views on that and that's what Tanate gave. Those would be the main factors that would influence that.

With regards to the, can you do better on your cost/income targets? Again, you're in Anke's camp, which is let's do better. Which we always want to do better. This is our target. We are confident about our targets, and by the way, we pull on all levers, and we pull on higher income, more diversification of income that I've talked about previously. We talked about our scalable tech and operational foundations, our end-to-end digitalisation programmes, our moving of our skill sets, and all of the ways that we work on capital velocity in wholesale banking. And all of them will work towards these targets, it's not that we just work on one lever. We also continue to work on our cost level, bearing in mind that we also want to make investments there where we can make good return, and so we also need to balance that.

Amit Goel (Barclays)
Thank you.

Operator
Thank you. Our next question comes from the line of Flora Bocahut, Jefferies. Please go ahead. Your line is open.

Flora Bocahut (Jefferies)
Yeah. Thank you. The first question I wanted to ask you is on the NII again. Just the clarification on the negative deposit charging. Out of the €300 million run rate for the full year, I wanted to understand how much was already gone in Q3 and how much of a decline we could therefore see again in Q4, if any? And then the second question is on the regulatory cost. I'm not sure if this was answered before, I'm sorry if it was, but you had guided at the Investor Day, I think for a €0.4 billion decline in bank taxes in 2025 versus 2021. So, I wanted to check if that still holds from today's standpoint.

Just one quick clarification, if I may. The one-off €315 million euro that you're going to have in Q4, is this going to be in NII? Because you only mentioned pre-tax profits? Just to be sure. Thank you.

Steven van Rijswijk
Okay. So, the €315 million is pre-tax, and where it falls, that's accounting, we're not going to disclose that yet. In terms of regulatory costs, are they still going down with €400 million? That's currently our assumption indeed, that has not changed. And on NII, how much was already going into Q3 and further downside? That I will give to Tanate.

Tanate Phutrakul
The NII impact this quarter is around €66 million and they will be gone next quarter. So, it's getting very minor in fact. Most of the benefits with negative interest charging are gone after Q3.

Flora Bocahut (Jefferies)
Thank you.

Operator
Thank you. Our next question comes from Adam Terelak, Mediobanca. Please go ahead. Your line is open.

Adam Terelak (Mediobanca)
Morning. I just had one follow up on the NII guidance. You've given €600 million for 2022. How much of that is in the current run

rate and how much is going to come through in Q4? So, I'm just trying to think what the uplift in NII could look like 4Q versus 3Q versus that guidance. And then clearly, quite important for the year over year, that €2.3 billion versus €0.6 billion this year, to get the run rate NII for 2023 on the basis of that guidance. So, how much of that €600 million has been booked year to date in terms of replication benefit? Thank you.

Tanate Phutrakul
First of all Adam, thanks for the question. But again, we want to say we don't give forward guidance. We give you a simulation based on what the yield curve would look like, right? So, I think that's what we see and what you see really in terms of replication is that 40% of our replication is within one year. So, you see that impact already tracking and I think what is the best thing that you can look at, is look at the pick-up, in a single quarter alone, right? From Q2 to Q3, it's up 6% in a single quarter, which basically informs you of how fast the tracking is taking place. But again, I don't want to repeat the answer that Steven gave, which is that replication, it depends on many factors, deposit growth, tracking speed and all that. So, that will be what we will see next year.

Adam Terelak (Mediobanca)
So, you can't comment on replication benefit booked year to date?

Tanate Phutrakul
Maybe I would like to let you talk with our Investor Relations team after the call. Okay?

Adam Terelak (Mediobanca)
Okay. Thank you.

Operator
Thank you. And I think that was the final question on the line. I'll hand back to Steven for the closing comments.

Steven van Rijswijk
Yes, thank you very much everybody for dialling in, for your time, for your good questions and I wish you a fantastic day. Thank you very much.

Operator
This now concludes the conference. Thank you all very much for attending. You may now disconnect your lines.