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02/04/2016 09:00 AM GMT, Q4 2015 ING Groep NV Earnings Call

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PRESENTATION

Operator

Good morning. This is Cecelia welcoming you to ING's 4Q 2015 conference call.

Before handing this conference over to Ralph Hamers, Chief Executive Officer of ING Group, let me first say that today's comments may include forward-looking statements, such statements regarding future developments in our business, expectations for our future financial performance, and any statement not involving a historical fact.

Actual results may differ materially from those projected in any forward-looking statement.

A 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 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, Ralph. Over to you.

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

Good morning. Welcome, everyone, to ING's full-year 2015 results. I will take you through today's presentation as an introduction, and then for questions we have Patrick Flynn, our CFO; Wilfred Nagel, our CRO, here with me from Executive Board.

Turning to page 2. I'm very pleased with our achievements in 2015, as we have delivered consistent results against our Think Forward strategy. We really work hard and we concentrate on it every day to improve our customer experience, so it is very rewarding to report that we added another 1.4 million new customers in 2015. We have also been able to grow our customer lending by over EUR21 billion during the year.

This has clearly contributed to our strong financial results for the year. The underlying net result banking increased by 23.2% from 2014 to

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EUR4.2 billion, and the return on equity was up to 10.8% for the year.

Our capital position continued to strengthen as well, and on a fully-loaded core equity ratio of ING Group and Bank were respectively 12.7% and 11.6% at yearend.

Given the good results and given the strong capital position, we are very pleased to propose a full-year dividend of EUR2.5 billion, or EUR0.65 per share.

We're committed to maintaining a healthy Group core equity Tier 1 ratio in excess of the prevailing fully-loaded requirements, which currently stand at 12.5%; and also, to returning capital to our shareholders. As such, we aim to pay a progressive dividend over time.

If we turn to slide 3. Basically, you see that when we launched our strategy two years ago, we had one clear purpose: empowering people to stay a step ahead in life and in business; and in order to empower people, innovation and constant improvements of service concepts are important.

In the third quarter -- or in the fourth quarter in Poland we launched Moje ING which is a new omni-channel banking platform, which gives customers insight in their personal finances in an easy and intuitive way, so they can do their banking more and more themselves.

Now, in Spain and The Netherlands we launched a new product as well. it's called Twyp. It's an acronym for the way you pay, and it's a peer-to-peer payments app, which allows consumers to pay small amounts to contacts on their mobile devices, using their mobile phone numbers only, and you can do it in a few seconds. After seven weeks we already have more than 200,000 users on this app.

Clearly, we're also looking at fintech innovations outside of ING that can help us strengthen our capabilities, and specifically on the lending capabilities we are looking at fintechs in the area of consumer lending and SME lending.

We recently announced an investment in a fintech called WeLab, which provides consumer loans in China and Hong Kong in a fully automated process, and it only takes minutes from application to approval.

I'm happy to say, if you turn to the next slide, that we welcomed another 1.4 million new customers. More importantly, as part of our strategy, we established 550,000 new primary banking relationships, with particularly strong growth in the challenger and growth countries, as it is in line with our strategy. If we continue to make progress on our strategic initiatives, and I'm sure we will, I'm confident we will reach our goal of at least 10 million primary customers by 2017.

All of this, clearly, leads to growth in a commercial sense. So on slide 5, you see that our deposits are growing by 4% to EUR509 billion, and our customer lending has increased to EUR533 billion, despite further reductions in our run-off portfolios.

If we zoom in on the core lending franchises, on slide 6 you can see that they grew by EUR21.7 billion, or 4.2%, during 2015. Wholesale bank increased by EUR13 billion, driven by growth in industry lending and general lending and transaction services. Retail banking increased by EUR9 billion, mainly in retail Belgium, Germany and the other challengers and growth markets.

All of that, the focus on clients, increasing number of clients, increasing your client's business both on the deposit side as well as the lending side, in the end, leads to better results, which is on page 7.

Moving to the P&L, we posted strong results in 2015. The underlying net result bank increased 23% from 2014 and the return on equity increased to 10.8%.

If we were to exclude CVA and DVA, which was positive in 2015, the underlying result increased by 11.9%; still a strong growth. That was explained by a couple of factors which are on page 8.

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So the strong results were supported by a healthy income growth and lower risk costs. The net interest income, excluding financial markets, was increased 4.5% from 2014, and that was clearly supported by the strong volume growth that we have shown.

Our risk cost of EUR1.3 billion, or 44 basis points of risk-weighted assets, are now in line with our long-term average of 40 basis points to 45 basis points of risk-weighted assets through the cycle.

If we then look at the underlying businesses, on page 9, we see that the improved results are both in retail banking and wholesale banking this year.

We see the relatively strong growth in retail banking driven by retail Netherlands, where the risk costs have come down sharply and retail Germany. I think it's worth highlighting the performance in Germany in a bit more detail, if we turn to slide 10.

Now as you can see in slide 10 ING Germany continued its strong performance in 2015 reaching a pre-tax profit of EUR1.152 million -- EUR1.1 billion. For the first time they are above the EUR1 billion mark, which is an enormous accomplishment.

The strong performance of Germany is mainly due to the customer-centric focus, resulting in achieving the award of preferred consumer bank for the ninth consecutive year. Focusing on customer services, improving customer services every day, making things easy simple and empower your customers does work.

Our customer base and number of primary customers continue to increase, while we are also diversifying our product offering to customers in order to increase the cross-buy. As customers see us increasingly as their primary bank, they don't only want to do savings and mortgages with us; they want to do the whole product spectrum in a direct, Internet-driven and digital way.

Consumer loans in Germany increased by 20% to EUR5.7 billion in 2015. But we are also seeing an increase in the purchase of investment products, as set by our clients.

Also, the wholesale banking operations in Germany are growing fast. Wholesale banking also has increased further to [EUR13.5] billion at yearend as we continue to grow the franchise and optimize the balance sheet.

I think one of the specific parts that shows how we work at managing cost income is also shown here. Here we have a franchise in which it is okay to have cost increase, given the fact that it's growing so fast and the efficiency is only growing with the growth, that the cost income ratio is rapidly going down, whereas the cost line is increasing.

Now those strong results across the Group have further strengthened our capital position. The Bank Core Equity capital increased to 11.6%, due to the positive net profit, 26 basis points, in the fourth quarter; and an increase in the revaluation results, which was partly offset by an increase in the risk-weighted assets.

The Group core equity Tier 1 capital increased to 12.7%. That's largely mirroring the developments of the Bank, but also including a EUR600 million release from interim profits that had not been included in capital in the first nine months of 2015.

Now, in January 2016 we've further reduced our stake in NN Group to 14.1%. That results in an uplift of 30 basis points in the Group core equity Tier 1 ratio pro forma to 13%. And if we would allow for the full investment of NN Group the pro forma Group core equity Tier 1 ratio would be at 13.4%.

As far as the capital levels are concerned, for 2016 the Group has a minimum core equity Tier 1 capital level of 10.25%, which is composed of the 9.5% core equity Tier 1 SREP requirement and a 75 basis points phase in of the Dutch systemic risk buffer.

The systemic risk buffer is scheduled to phase in by 75 percentage points5 -- by 75 points -- 0.75 percentage points, sorry, per annum to 3% from January 1 2019, so our fully-loaded requirement is currently 12.5%.

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Now, as these capital levels are requirements for the Group, rather than for the Bank, we have introduced a new target for the Group core equity Tier 1 ratio.

Firstly, we want to remain above the fully-loaded core equity Tier 1 requirements, currently 12.5%. Secondly, we intend to grow over time into a management buffer over the fully-loaded core equity Tier 1 requirements.

Now, taking into account these new capital requirements, including the 3% CP buffer on top of the SREP, we have decided to propose at the AGM to pay a dividend of EUR2,515 million or EUR0.65 per share. Going forward, we aim to pay a progressive dividend over time.

Now, on slide 13, you basically see an additional table, which is the Core Equity Tier 1 requirement on Group level versus the Bank. That's a change from the past. So you see in ambition 2017 now on the Group level and you see the other ambitions on the Bank level still being the same.

Coming to those ambitions -- actually, in 2015 we already reached most of our ambitions 2017 targets. I'm pleased with the progress we are making on each and every of these metrics.

Now turning to the fourth quarter results, I'm now turning to slide 15.

In a seasonally weak fourth quarter ING's underlying pre-tax result was solid at EUR1,202 million, despite a significantly higher regulatory cost.

Net interest income excluding financial markets has remained steady in the past year, supported by an ongoing volume growth.

Turning to the NIM, the net interest margin was up from the third quarter by 1 basis points, and that's due to net interest results in financial markets; they're a bit higher versus the third quarter.

The commercial interest margins have been rather stable over the past year. A large part of the 6 basis points reduction from one year ago is as a result of the lower interest result in the financial markets.

We have touched upon this previously, where you see the composition of the income in financial markets changing from a non-interest income to interest income, and also changing it back. You see also in this table how it moves, whereas the financial markets division is actually performing very well and in a stable manner. It's just that the composition of income changes now and then, and that does affect our NIM. That's why we keep it explaining it.

Looking at the NIM, we see lower margin in current accounts. They have been offset by higher margins on savings as a result of lower client savings rates. In line with market developments, we have further reduced these rates in several countries in December 2015, and January 2016.

Focusing on the lending growth in the fourth quarter then, you can see on slide 17, I guess we are, in our core lending businesses, they all increased, or most of them increased from the third quarter 2015, with most growth actually in the wholesale bank.

As shown at the beginning of the presentation, our core lending franchises grew by 4.2% in 2015, and that's fully in line with our guidance. So, in 2016, we expect this positive momentum to continue.

Moving to expenses. Our expense base is more and more impacted by regulatory costs, and you can that in these tables as well. There seems to be no limit here in terms of what some of the countries are thinking about.

We are confronted with a new bank tax in Poland as you know. Now you see the increase here for 2015. Here we were trying to manage that,

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and we are managing it, also in terms of further improvement of efficiency.

But this is the picture. So if you look at your expense base and you see it's more and more impacted by the regulatory costs.

We also took a number of smaller redundancy provisions in retail Benelux and also banking this quarter, an aggregated amount of EUR120 million. These are expected to deliver annual savings of EUR65 million by 2017.

Adjusted for the redundancy costs and regulatory costs, expenses increased by 6.2% from fourth quarter 2014, and were flat from the third quarter in 2015.

Now, the risk costs. We have seen a small increase from the third quarter, but the trend remains positive year on year, for sure, 2014, 2015. Total risk costs were 38 basis points of average risk-weighted assets this quarter, below our through-the-cycle average.

The NPL ratio also decreased to 2.5%. That's an improvement for the third consecutive quarter, both in retail banking and wholesale banking.

Then zooming in on wholesale banking risk cost on slide 20. Risk costs in wholesale banking continued their downward trends. They amount 33 basis points in 2015 as a whole; 26 basis points in the fourth quarter, and that's clearly below the long-term average.

However, there are some uncertainties out there. The most obvious ones being the very low oil prices.

The NPL ratio and our lending to the broader oil and gas industry is still low. It's at 1.8% and hasn't deteriorated in the fourth quarter. That's despite a further weakening of oil prices to around $30 a barrel. But we cannot rule out that we will be hit in a future by incidents affecting our wholesale banking loan book. For that I go to the next slide.

The slide gives you the overview on oil and gas exposure; it's the slide that is familiar to you. We have included -- we started to include it last year in most of our presentations.

The slide shows that 85% of our lending to oil and gas is not directly exposed to oil price risk, and that hasn't changed. The remaining 15% is exposed to oil price risk to some degree, although it is important to note that there are many different mitigants in place.

Nevertheless, given the further decline of oil prices in the fourth quarter, the oil price risk in certain segments of our oil sector has increased.

Overall, we expect the risk costs for 2016 to be at, or slightly above, the level of 2015. But if oil prices were to stay at around $30 or below, and remain there for an extended period of time, 2016 risk costs may increase. In such a scenario we estimate overall risk cost for the total Bank could end up somewhere between the 2014 and 2015 levels, i.e., potentially between EUR1.4 billion and EUR1.6 billion. That's overall risk cost; overall on a total portfolio.

Now to wrap up, if you take one step back and you look at the results for this year, we actually have been able to deliver on three counts: growth in customer numbers, growth in lending, and growth in savings; results, strong results; and the third one being strong capital and an attractive, handsome dividend that we started paying.

I'm confident that our story's on track. I'm confident that we can continue our strategy across our network, benefiting the shareholders as well as the customers.

I would like to open the call to questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Anton Kryachok, UBS.

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Anton Kryachok ***UBS - Analyst***

Just two questions, please. Firstly, on the capital target for the Group, now that you have a clear capitalization level in mind for the overall Group, would you be able to guide us on the target return on equity that you would like to achieve in the Group. We have a target for the Bank. But given that the focus is now shifting more towards the Group, it would be helpful to know your ambition on ROE for the ING Group rather than just ING Bank.

And the second question, please, what proportion of your oil book is exposed to clients in the US? And have you seen an increased provisioning on your US energy book? Thank you.

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

Thank you, Anton. The first question will go to Patrick, and the second question I will give to Wilfred to answer. Patrick, go ahead.

Patrick Flynn ***ING Group - CFO***

As a consequence of the SREP, and having the [D-SRB] come on top, we have to update our targets with respect of capital ratios.

We have not done a full review of all our ambition levels. That will come in the next Investor Day we will have, which hopefully will be some time towards the end of this year, maybe early next.

So in terms of ROE we're still staying at the underlying results of the capital in the Bank as the target. We'll have to factor in thoughts around the Group in due course. It means the Bank, as you know, is above the 10%, nearly 11%. But I think the Group average for 2015 was just around 9%.

But in terms of targets, that's something -- for ROE for the Group is something we'll update with our next full strategy day.

Anton Kryachok ***UBS - Analyst***

Thank you.

Wilfred Nagel ***ING Group - Chief Risk Officer***

On US oil exposure, the main component of that is what sits in our reserve-based lending business in the US, which is about [1.8] billion. There is beyond that a bit of exposure to some of the US global oil majors. But I wouldn't really call that US exposure in the terms you mean.

Anton Kryachok ***UBS - Analyst***

Thank you. So it's [1.8] billion?

Wilfred Nagel ***ING Group - Chief Risk Officer***

That's correct.

Anton Kryachok ***UBS - Analyst***

Perfect. Thank you so much.

Operator

David Lock, Deutsche Bank.

David Lock ***Deutsche Bank - Analyst***

Just a couple from me, the first one just to ask a little bit more on the management buffer, that you point to in the presentation; it's growing in to a comfortable management buffer over time. When we wind back to the Investor Day you gave a 10% target for the Bank, but with an 11% in mind, including that buffer. Should we be thinking about a similar 100 basis point buffer for the Group obviously building in to that over time?

And then the second question I had was really around oil, but also thinking more on the impact potentially for your loan growth. Are you still

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confident you can hit 4% loan growth going forward, given where oil is? And are there any other additional sensitivities you can give us around that. I appreciate the sensitivities on the risk cost, but just on the growth aspect. That would be really helpful. Thank you.

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

Patrick?

Patrick Flynn ***ING Group - CFO***

Yes, I think the first thing to say is where we currently are, the phased-in, as Ralph reported, was 10.25%; pro forma was 13.4%. So it's more than comfortable over 300 basis points today.

That phased-in will happen over the next four years. So that, if nothing else happens, just mechanically that buffer would diminish a bit, as the phase-in continues.

That said, there's a number of moving regulatory parts here that we have to just see how they play out. I think there's a growing recognition that the way the SREP process and the [D-SRB] buffers is played out in terms of how that translates into MDA is perhaps not the intended result.

There may well be a revision to MDA levels, we're hearing talk of that. That may take some time, but I expect that to come to fruition in the course of that period.

Also in terms of domestic buffers and harmonization thereof, the EC is repeatedly saying it wants a level playing field in capital. We are hopeful that will happen. Again, over that three-year period there's ample time to see that flow through.

So, sorry, it's a bit of a longwinded answer but there are a couple of important regulation moving parts that will determine what we might need in terms of a buffer.

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

Okay, David, yes, on loan growth there's two ways to go about your question as to what will it mean for growth.

Honestly, in 2015 the growth in our book did not necessarily come from the oil and gas sector, given the lower oil price. Actually, certainly on the short-term side it actually decreased. So, that was not leading the growth in our book.

Then on the contrary, I actually think that we should all look at the positives of a low oil and gas price, leading to further domestic demands, disposable income in most of the economies in which we're active. As a consequence of which, a larger part of our loan book and a larger part of our clients will actually benefit from it. Therefore, it does not necessarily alter our confidence in being able to grow our loan book the way we have guided up to now.

Thanks a lot.

David Lock ***Deutsche Bank - Analyst***

Thank you.

Operator

Ashik Musaddi, JPMorgan.

Ashik Musaddi ***JPMorgan - Analyst***

So, first of all, can I have a bit more color on risk cost? I think you have clearly mentioned that this year's risk cost, if all remains here, would be a bit higher, give or take 45 to 55 basis points.

But let's say if all remain here for the next three, four years, how should we think about your risk cost, i.e., will you be taking a one-off hit

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from oil in 2017/2018 or will it be staggered in the risk cost? How does the accounting work on that would be great to hear?

Secondly is on your NIM outlook. Clearly, your guidance is 150 to 155 basis points. Are you still sticking with that guidance, given that you are still a way away from that guidance at the moment? It's still, I think, at 146 at the moment. So, are you still comfortable with that guidance? Thank you.

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

On risk cost I'll give the word to Wilfred.

Wilfred Nagel ***ING Group - Chief Risk Officer***

Yes. Ashik, I think what you're going to see, if, indeed, oil prices were to stay low for a longer period, is a gradual development of the risk cost, for a couple of reasons. One is different parts of the portfolio will have different timing in when they will be hit.

If you take a large part of a reserve-based lending, that is likely to come somewhat early. This is a high OpEx/low CapEx business, where the margin of profitability is very sensitive to oil prices. These are the wells that are going to be shut down first, as we are already seeing at this point.

A large part of our book, however, is more exposed to the conventional development and exploitation, which means that this is a much longer cycle where even development projects that had already been started before the oil price drop hit, are still continuing and these fields will come on stream, will require servicing, will require rigs.

If you look at our book, typically what we do is collateralized and cash flow-based, i.e., in that segment of the business what we look at in terms of thinking about provisioning in the end is going to be the NPV of the cash flow from the contracts that we have these rigs on versus the outstandings.

In many of these cases you're talking about modern new rigs with contracts of five to seven years where, by definition, the problems, if they arise, will start showing up quite a bit later than, for example, in the reserve-based lending.

So, you would expect a gradual increase of provisions there over a prolonged period. We're certainly not, at this point, seeing a big shock coming.

Ashik Musaddi ***JPMorgan - Analyst***

Okay, that's very clear. Thank you.

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

Okay, Ashik, it's Ralph on your question as to the NIM guidance.

The 150/155 guidance that we gave was for 2017. We're touching it, honestly. I think it's 147. It's not that far away from the lower end of the range of 150. We're 98% there, to be quite honest. We have explained to you as to how the financial markets results influenced this a little bit as well. We have been into the range; we're just out of the range.

Then one more remark to be made: yes, we do feel comfortable we can get there. We feel we can manage the NIM in the current circumstances, because, in the end, when we guided the NIM range to go up to 150/155 by 2017, we also indicated that that was dependent on the change in asset composition where we would grow more in higher margin assets in industry lending; in some of the commercial banking activities; in SME lending and consumer lending, away from a concentration on mortgages.

So, basically, we are showing that every quarter, that the asset composition is changing, and that will also help us to move towards, and maybe close into, the range that we guided for 2017.

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Ashik Musaddi *JPMorgan - Analyst*

So, is it fair to say that your high margin shift -- high margin asset shift as well as some more deposit rate cuts is still -- will still be able to absorb the risk you are seeing on the asset side?

Because, clearly, after the Bank of Japan start, basically the market is really worried about negative rates here as well. So, you are still comfortable. Okay.

Ralph Hamers *ING Group - CEO & Chairman of the Executive Board*

Yes. So, for 2016 we feel comfortable.

Ashik Musaddi *JPMorgan - Analyst*

Okay, great, thank you.

Operator

Bruce Hamilton, Morgan Stanley.

Bruce Hamilton *Morgan Stanley - Analyst*

Just going back again to the energy, and metal and mining's exposure, could you give us what your undrawn committed line exposure would be? Because obviously it's only in the metal and mining space there's a risk, I guess, that those lines could be drawn down.

And then, secondly, in terms of the Dutch market, obviously you've got further scope to take deposit cost down or savings deposits down, but where do you think the limit is on that? And, are you still seeing any benefit in terms of mortgage front book pricing or is that all now played out just in terms of the NIM for the Netherlands specifically?

Ralph Hamers *ING Group - CEO & Chairman of the Executive Board*

Okay. Wilfred.

Wilfred Nagel *ING Group - Chief Risk Officer*

Yes. Bruce, on undrawn commitments, the vast majority of that really sits in our trading commodity finance environment in the segments that you're talking about.

On the actual project and pre-export finance deals, it is very limited. It's not a big percentage of the total book undrawn committed there.

Ralph Hamers *ING Group - CEO & Chairman of the Executive Board*

Then, Bruce, specifically on the Dutch market, we see the current mortgage market and the pricing there is higher than the average of the back book. So, that should improve the picture slightly. That's one.

On the other side, we also know that our total exposure on mortgages now is decreasing with the transfer of the US and Utrecht book to NN. So, from an NII basis the development may be different than from a margin basis.

Now, in terms on managing our savings rates versus managing on the asset side, there are two different sides here. It's about how the market develops, how the customer relationships develop as to how we can go about pricing. I can't really comment on how we will move there, but there is scope.

If you compare to other markets outside of the Netherlands, you'd see that savings rates are much lower already. But it depends on how the market develops as well.

Bruce Hamilton *Morgan Stanley - Analyst*

Thank you.

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Operator

Mr. Murray, Autonomous Research.

Farquhar Murray *Autonomous Research - Analyst*

Just two questions, if I may. Firstly, with regard to the EUR0.65 full-year dividend, should we just regard that as the base dividend on a going concern basis or is there any excess capital distribution component within that?

And over what timeframe might ING be able to address any potential excess capital that it sees? Are we really looking at a three-year timeframe to try and settle down regulations from here?

And then, finally, just on a point of detail, what approach will ING take to the dividend accrual against capital for full-year 2016. Obviously, last year you stopped accruing profit to capital in the second quarter. I just wondered what approach you'll take this year. Thanks.

Patrick Flynn *ING Group - CFO*

Okay, thank you. In terms of how we thought about setting this, in the past we've just -- just a bit of a retour about what we said we would do.

We said we'd pay a minimum capital -- a minimum dividend of 40%. We've done that and we've topped it up, come up with EUR0.65 per share and we're aiming for that to be a progressive dividend through time.

Now, in terms of surplus capital, did that play a role? Yes, it did, albeit, given the SREP requirements, that quantum is a lot lower now; mechanically, you can see it's just under EUR3 billion.

But in terms of setting the base dividend for go forward, that was part of how we're able to set it at this level.

Prospectively, the aim is to have a progressive dividend policy through time. So ideally we can try to grow this through time and that would absorb capital generation from the Bank and the reduced surplus out of the Group as well.

In terms of accounting, yes, mechanics are -- stay the same. To pay a dividend, profits will have to be earmarked for dividend rather than for capital; that mechanic is the same: we can't count them twice, as it were.

Precisely what we do every quarter in terms of how much we put into each of the two buckets, the capital or the dividend bucket, it's something we'll work out in Q1.

Farquhar Murray *Autonomous Research - Analyst*

Okay, thanks.

Operator

Robin Van Den Broek, Mediobanca.

Robin Van Den Broek *Mediobanca - Analyst*

I was wondering if you could share your thoughts on the discussion with the Dutch Central Bank regarding the lack of level playing field on capital? Do you feel that, if there's more clarity on Basel 4, for example, that the Dutch Central Bank might be more lenient to reduce [D-SRB] requirements? That's question one.

And secondly, I saw in your slide pack, you also give some disclosure on your oil book about the maturity of the loan exposure. Could you maybe share some comments on your willingness to reduce exposure, especially the less than one-year maturity part of the book, and what potential margin impact that could have? Thank you.

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Ralph Hamers *ING Group - CEO & Chairman of the Executive Board*

Okay, thank you, Robin. I will take the first question, and Wilfred will take the second one.

Clearly, I think the Dutch Central Bank knows that they have created an unlevel playing field with this high buffer that they put on the Dutch banks. They also know that there is some more regulatory change coming, and that maybe impactful for many banks as well.

We are in constant discussion with the ECB, with the DNB, on each and every measure that we can see coming, whether it's from Basel; whether it is from the FSB; whether it is from different approaches that the central banks themselves take in terms of modeling and all of that, in order to show what the effects are.

The only thing I can say is that this is a very open and constructive discussion. But, yes, we are dealing with an unlevel playing field here.

Robin Van Den Broek *Mediobanca - Analyst*

Okay.

Wilfred Nagel *ING Group - Chief Risk Officer*

Okay. On the exposure oil and gas shorter maturities and the development of the exposure, the short maturities that we have in the book consists of two things.

One is, of course, the trade and commodities finance business which, by definition, most of that is shorter than one year. And then there is the maturities on the longer facilities.

Now, the underlying dynamic here is that the music, in terms of new development, basically stopped 18 months ago. So what we still have coming, and that also goes back to the earlier question about undrawn commitments, is really mainly those facilities that we committed to before the CapEx largely stopped and that are being gradually drawn down. Obviously, being that now almost two years behind us, a lot of that has been drawn.

On the other hand, a lot of these facilities, particularly the ones that are, for example, on the drilling side with rigs on contracts, are paying back; and there is not a lot of new business coming. So our view is that, net/net, the exposure will gradually come down. But we may well, and there is no intention to stop that at this point at all, simply continue with the shorter-term trade and commodities finance business.

So I think what you're going to see is gradual translation of longer exposures into shorter and then maturing ones. A continuation of the short revolving-type facilities.

Robin Van Den Broek *Mediobanca - Analyst*

And your impact on margins, can you comment on that?

Wilfred Nagel *ING Group - Chief Risk Officer*

Well, given the fact that there's not a lot of new business, what you're going to see is project finance-type margins continuing as the majority of the book for a while. On the PCF side, it is more a volume than a margin change that we're going to see. So I wouldn't expect a massive impact on margins from this development, net/net.

Robin Van Den Broek *Mediobanca - Analyst*

Okay. Thank you very much.

Operator

Guillaume Tiberghien, Exane.

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Guillaume Tiberghien ***Exane BNP Paribas - Analyst***

It's a follow-up question on the net interest margin. Could you maybe help us quantify how negative the impact might be in the ECB announces new measure to put rates into more negative territory before any mitigation that you might be able to implement?

Patrick Flynn ***ING Group - CFO***

Maybe the way to think about this is, we have a stable core deposit base that is -- not getting too technical, it's replicated over a reasonably long timeframe. So our results are, to some degree, resilient to immediate impacts. We're not a trading shop, so there isn't a mark to market -- daily mark to market in our banking book.

So it's more a question of prolonged low rates will have a negative impact through time. A quantitative easing impact tomorrow would not show any immediate impact in results. Longer term, of course, the lower the rates are for longer it, clearly, is a negative.

But as Ralph said, for 2016, we think the outlook is broadly similar to where we currently are, stable-ish, and the three levers apply. We look very carefully at the pricing of all our products, including deposits. We are very much focused on trying to grow our lending and improve the composition of our balance sheet.

So balance sheet optimization and loan growth, play a major part too. We have been able to deliver that, are delivering that, and will hope to continue to deliver that so. Hopefully, stable-ish margins, which is what we achieved in 2015, if you exclude FM. Same thing, hopefully, for the coming quarters of 2016.

Guillaume Tiberghien ***Exane BNP Paribas - Analyst***

Thank you. A very small follow-up; did you highlight whether you would think you're able to still grow volume at around 3% or 4% this year and next?

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

Well, we did indicate so, given the fact that the oil and gas price also has a positive effect on an even larger part of our portfolio, that, in the end, that will support domestic demand and, therefore, GDP and, therefore, a large part of our portfolio will benefit from it. Certainly, it should also lead to growth on that side.

So where we saw this year with some uncertainties surrounding the global markets and specific markets, I'm sure -- well, this year 2015, I'm sure there will be uncertainties surrounding specific markets in 2016 as well.

But you know we have a good core franchise in Europe and we have a very good global franchise from a commercial wholesale banking perspective that gives us ample opportunity to grow.

Operator

Alex Koagne, Natixis.

Alex Koagne ***Natixis - Analyst***

Just two follow-up questions from my side. The first one is on the capital. I was just wondering whether you can share the potential impact of the IFRS 9 on your capital.

And secondly, it's more on the cost side. I was wondering whether we can expect any new initiative to compensate the potential impact of the regulatory cost? Thank you.

Patrick Flynn ***ING Group - CFO***

On IFRS 9, it's a bit too early really to be definitive on the impact. A couple of -- we'll be working out -- very much focused on this now, this year.

Big picture is that I think the broad view is that this will increase the quantum of provisions. If that happens, they would be taken through

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equity on transition, as IFRS requires. But also, we've got this expected loss reduction in capital today, that should be released.

So the net impact on capital is difficult to judge whether it'll be a net increase or not. But we're working on trying to develop the models to compute this, and that will be something we're doing this year.

And your second question was?

Alex Koagne *Natixis - Analyst*

Was on cost initiative. We should expect a new cost reduction program to compensate the impact of the regulatory cost?

Patrick Flynn *ING Group - CFO*

Yes, we -- this is -- it's something we're working on. We've done it in big numbers in 2014. We've done another one in the course of -- there have been smaller ones in the course of 2015; and also, the [EUR120 million] we've announced this quarter.

And cost discipline, cost focus, cost savings, it's just a constant theme, and something we're going to be doing a lot; working very hard on; something we want to improve on, so watch this space. But there's a lot more work we have to do here and will do.

Alex Koagne *Natixis - Analyst*

Okay. Thank you.

Operator

[Kiris Vijayarajah], Barclays.

Kiris Vijayarajah *Barclays - Analyst*

I've got a couple of questions on your RWA development. Could you give us more color on the model adjustments you flag at the back? Specifically, what are the methodology changes; what's driving that? And are there more changes we've got to factor into our models for 2016?

And then, separately, on the more positive side. You've had some positive ratings migration as well. So which books are showing the improvement? And again, what's your outlook for ratings migration into 2016, please? Thanks.

Wilfred Nagel *ING Group - Chief Risk Officer*

Yes. I think, generally speaking, we're still seeing improvements in most of the books around the globe. Certainly, the ones that were giving us some heartburn over the past few years are all improving. NPLs are generally coming down. We see, certainly on the mortgage book, for example, here in the Netherlands, also the improvement in property prices having a positive impact on [pure] rates, and on LGDs.

So generally speaking, that migration, we think, maybe at a slightly less rapid pace, will continue into 2016.

We talked already about the oil and gas exposure. So obviously, that is going to show a slightly different development.

Then, looking at the models, there is a constant review of models going on. We're upgrading. We're also complying with new guidelines around these models. It won't be a surprise that models that present an increase in risk-weighted assets tend to go through the whole approval system a little bit faster, also with the regulators, than the ones that reduce RWAs.

Kiris Vijayarajah *Barclays - Analyst*

Okay. Thank you.

Operator

Tarik Mejjad, Bank of America.

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Tarik El Mejjad ***BofA Merrill Lynch - Analyst***

A couple of questions. First, a follow up on the discussions of SREP plus [D-SRB]. Thanks, Ralph, for your input on that. But can you specify what's the speed of these discussions? Would we -- would you hear more from the Dutch Central Bank around this year? Or when you will be discussing the dividend next year again? Or what's the timeframe on that?

And secondly, what's your thoughts on the AQR or even the SREP for the next year? Because we understand this 9.5% can -- may be moving up or down. Do you think they might include part of the stress on the commodities book this year, or is it not really on the table? Thank you very much.

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

Thanks, Tarik. Well, on the discussions with the regulators. Well, first, the [D-SRB] is phased in, right. So let's not -- it's phased in over the next four years. We do fulfil the fully loaded already, so we've fulfilled that requirement already. But it's a phased in, so that in itself already shows the DNB taking into account that these things may take time. That's one thing.

On the other side, the Basel discussions, we hear many different things coming back out of Basel. On one side, we have a consultancy -- a consultation round, not leading to many changes. On the other side, we hear that there is quite some opposition to floors, not only from the industry, but specifically, also, from regulators.

Honestly, we don't know where this is going to end up, and when it's going to end up somewhere, because timelines are being shifted as well.

So I think we have to deal with what we have. This is what we know right now, which is this 3% phased in until 2019. We feel comfortable at these levels; we work with these levels. Based on that, we've also set our dividend. So -- and it shows as well as to how we feel about it.

In terms of next year's SREP, I'm looking at my colleagues. DCF volatility, I'm not sure that leads to a lot of risk also in itself, because that's all collateralized, and it goes up and down in our book as a volume -- from a volume perspective. But it doesn't show any difference in risk experience. So I'm looking at Wilfred.

Wilfred Nagel ***ING Group - Chief Risk Officer***

No, that is right. Certainly, the commodities -- the DCF side of the commodities business is not showing any particular stress at this point.

To the extent that the overall environment deteriorates, it will translate into higher risk weights through our models; and, as such, find our way into the capital. I don't think there's going to be any particular reason for that to become a SREP topic in itself.

Tarik El Mejjad ***BofA Merrill Lynch - Analyst***

Okay. Thank you. Just a quick follow-up, please, on your previous comments on the MDA. You mentioned that MDA levels could set some [unmeasurable] consequences. Do you think the MDA level could change in here? EBA is requested to be Pillar 1 and 2; some Nordics have only Pillar 1. So what's your thinking on that?

Patrick Flynn ***ING Group - CFO***

Well, as I said, the -- what we saw was, in the course of last year, when the SREP first came out, there was quite a lot of confusion about how to interpret MDA in terms of SREP. Should it be based on a -- there was an 8% number talked about; should it be based on the SREP number, including buffers? So there's quite a bit of confusion on that.

And then, there was clarification given earlier that it would be set based on the total, including SREP.

I'm also hearing a number of regulators indicating that was not necessarily an intended outcome. That could be -- it's not where they necessarily wanted this to be.

So I think there's scope for this to be reviewed. Revisions that change lower capital requirements in whatever form are not easy to get

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through. But there is discussion that the outcome of having MDA based on the fully loaded requirements is perhaps not what was intended at the beginning.

So again this may take time, but that is something that I do hear on the regulatory change agenda.

Tarik El Mejjad ***BofA Merrill Lynch - Analyst***

Okay, thank you.

Operator

Robin Down, HSBC.

Robin Down ***HSBC - Analyst***

Apologies about coming back to the energy book again, but obviously this is a big issue for the market.

What I find kind of interesting is that we've seen growth in a number of your sub-components in that energy book. I appreciate with a trade in finance that's probably some element of drawdown of previous facilities.

If I look at the reserve-base lending that also seems to have grown by quite a high percentage in the fourth quarter. Obviously, you guys are the experts and we're not, so I'm just wondering what is it that gives you confidence, given everything you're saying about higher credit losses there, to go out and grow that book.

And are there any sort of metrics you could share with us in terms of maybe a loan-to-value type equivalent, with a $30 oil barrel? Can you tell us roughly what sort of percentage of the reserves you're actually lending against? Thank you.

Wilfred Nagel ***ING Group - Chief Risk Officer***

Okay. On the actual movements, there is a couple of things going on here. One is a currency effect. Two is there's always a little bit of undrawn commitment that gets drawn.

What is important to keep in mind also is that the reserve-base lending is not just oil, there's a pretty big component, it's about 50/50, is gas. And whilst that is not totally uncorrelated, the market dynamic is different. We have seen one particular transaction in that area.

I think your question was typically what kind of loan-to-value should you be thinking of in terms of reserve-base lending. Obviously, they vary a bit, but typically this is around 55%, 60% or so. It's important to keep in mind that our business in this particular area is purely senior and almost always secured.

I know there's a lot of talk in the market about high-yield exposure to the energy sector. I don't completely recognize the concern around that, because, as I say, whatever we do, certainly in the normal investment rate domain, is secured lending against cash flows and assets.

Robin Down ***HSBC - Analyst***

So if you're putting on a new facility today with oil at -- well, I guess we're just over $30, are we effectively saying that you almost need to see that dropping down into sort of mid-teens level before you'd think that you might be at risk?

Wilfred Nagel ***ING Group - Chief Risk Officer***

If you're looking at a 60% loan to value, then you can see that there is a 40% cushion. Are we doing -- are we actively pursuing new deals at this point? The answer is no.

If there is a particularly compelling situation with a very strong capital structure and a good loan-to-value, we might still do something, but it's -- we're not actively hunting for deals at the moment.

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Robin Down ***HSBC - Analyst***

Okay, great. Thank you.

Operator

JP Lambert, KBW.

JP Lambert ***KBW - Analyst***

I would like to come back to the fintech involvement in Kabbage and WeLab and the question is how you see the implementation within your own operations in terms of timing, pilots; what kinds of reserves you can share with us?

The second question is again on oil and gas, more specifically on timing. You indicated you expect a gradual increase. The question is can we expect a gradual increase in that scenario also on a quarterly basis next year -- I mean this year, 2016? Thank you.

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

Okay. Jean-Pierre, thanks, it's Ralph. On the fintech question, first, I want to go back to innovation as a whole. Clearly, we innovate a lot ourselves, as we have launched many different products ourselves in the payments area, in the customer loyalty area and all of that.

That's a promise we need -- that we made when we said okay, we will want to deliver differentiating experience for our customers and it fits with what we're strong at, and why we are so successful, because if you go back 10 years ago we were probably seen as the fintech in the world, although it was not referred to as a fintech.

You see also with the successes that we have in countries like Spain and Germany and Australia that you can build a completely different model.

Now what we have also indicated in our strategy is that we are in need of developing new lending capabilities and particularly in the area of SME, financing and consumer financing.

When we launched this strategy two years ago we also indicated that we didn't want to go about, for example, SME lending by building a branch next to every church in every village, because that's a very expensive way to build a platform to do SME lending. So we had to look at alternative ways to do so.

Now clearly, if we can't develop those ourselves or if we see a good practice out there, and we've seen one called Kabbage in the US, then we want to engage with this practice.

That's what we did with Kabbage. So we took an equity investment as a more strategic player, not as a venture capital firm, because that's not how we play, it has to fit our strategy. And then we look at how do these algorithms work? Can it fit our client proposition, etc.?

So with Kabbage we have a joint venture in Spain, as we speak. We started to do SME lending about five, six weeks ago. It's too early now to indicate to the market as to how we go about it; how the book is developing; how fast we're growing; and all of that. So we'll have to see how it develops, but we are looking at it.

With WeLab, that's on the other side. So it's a Hong Kong, China-based consumer finance fintech. Also, instant lending and we think their algorithms and their time to service their clients is one that fits our promise to our clients as well.

Therefore, we took a participation there. We're looking at it, we are working with them and taking a close look as to whether we can use some of their experience and their algorithms back into the franchise that we already have.

So this is not for opening new markets, this is really to look at how can we build the franchises that are already so successful in a broader client franchise.

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JP Lambert ***KBW - Analyst***

Thank you.

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

Then I refer to Wilfred for the second question.

Wilfred Nagel ***ING Group - Chief Risk Officer***

Yes, that was on timing on a quarterly basis of our provisions, which is quite an ambitious question frankly. Let me give it a try though.

If you peel the onion of the exposures that are sensitive to oil price, if I think about our services and drilling activities, most of these clients have contracts that will last them into 2017. There will be a bit of expiry in 2016; frankly, we're not expecting very big issues there.

So the part that could still have a bit of impact on the 2016 provisions Is largely going to be the reserve-base lending. There, we'll see the semi-annual reset in Q2. So this is when we will start seeing -- if there is going to be more stress, we'll probably start seeing that show up then in the Q3 provisioning discussion.

So I can't tell you whether, at this point, we believe there are going to be problems. If we did, we would be taking provisions. But we'll see what happens after the Q2.

So that's, I guess, the best I can say about what the timing of these things might be.

JP Lambert ***KBW - Analyst***

Thank you very much.

Operator

Andrew Coombs, Citi.

Andrew Coombs ***Citi - Analyst***

I think all the questions on capital and energy have been exhausted, so perhaps I could have one on costs and one on loan growth.

Firstly, on costs, if I look at the regulatory costs, you've actually come in slightly lower than expectation for the full-year 2015; EUR620 million versus the EUR650 million guidance. And yet, you're increasing your guidance for next year from EUR800 million to EUR850 million. So just trying to tie those two things together. What's led to the increase in expected regulatory costs for 2016?

And the second question would be on the core loan growth. Two aspects to that. The first is when I look at the Dutch retail lending, you've seen a EUR1.6 billion contraction. That's accelerated Q on Q and I think you identify lower business lending as the reason. That seems slightly surprising when you look at the DNB statistic, which shows that SME loan demand is increasing. So perhaps you could elaborate there.

And then on the flipside, industry lending, very strong loan growth this quarter; quite a bit increase from Q3. What drove that please? Thank you.

Patrick Flynn ***ING Group - CFO***

On costs at least, so what happened was that there was a legislative hiccup in the Netherlands and the DGS, which we expected to be implemented, actually, we thought it was coming in in the midyear, then it got delayed to the fourth quarter and then it turned out there was a flaw in the legislation and it's got pushed back.

So that was a deferral. It's about EUR40 million a quarter. That's all it is, is a deferral; so it all comes in, it's EUR133 million comes in in 2016 as the full-year impact.

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And then the other thing that came in new was the Poles gave us a nice surprise of EUR70-odd-million on top, which had increased the 2016 estimate to EUR840 million.

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

Then on lending growth, the growth for the quarter, actually, we're looking at the specifics, so there's a couple of people now going through some of the pieces of material that we have in front of us is if you want to know it exactly.

So on real estate, there was certainly some growth and in the structured finance area as well. It's actually spread across the different sectors that we have. So there's not one sector that comes out here and we see that growth continuing.

We have the teams in place. We actually see some of our competitors withdrawing from some of these markets. So it's a combination of growth or growing our teams and seeing that competitor withdrawing; so we have real momentum there across the different activities that we have. Thanks.

Andrew Coombs ***Citi - Analyst***

And on the Dutch retail side?

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

So the Dutch retail, yes, so whatever the DNB statistics, we don't see the demand increasing. So there is demand in the SME sector. It is stable. We haven't seen it increase over the fourth quarter, whereas we had expected so, so its hasn't come in as an increase. Approval rates are stable or improving even. So that should show some pickup.

But in the end, the book runs off more quickly than the new production comes in and that's -- it's a combination of the two that makes that the book has shrunk by EUR400 million in the fourth quarter.

Andrew Coombs ***Citi - Analyst***

Okay, thank you.

Operator

Pawel Dziedzic, Goldman Sachs.

Pawel Dziedzic ***Goldman Sachs & Co. - Analyst***

I have two follow-up questions on growth and on the regulatory costs as well.

On your volume growth, you increased your core lending by EUR22 billion in 2015, which corresponds to around 4% growth rate. But if we look at this on a quarterly basis, it's nearly 70% of that came in the first half of the year.

So is it fair to assume that although maybe the growth rates remain solid overall, the growth rate going forward will be somewhere below that 4%?

On regulatory costs, a follow-up question as well. So you increased your costs to EUR850 million, but can you give us a little bit better idea what are the sensitivities around this number? So, for instance, in Poland, there are further talks about Swiss franc scheme that could push regulatory costs higher.

And also, I was hoping if you can comment on any talks about potential elimination of overlap between the fees you pay on Dutch bank levy and the resolution fund in Europe. Thank you.

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

Okay, thanks. So, on the growth, honestly you can't -- I would not look at a quarter-by-quarter picture, nor even a half year-by-half year picture here. It really varies. Certainly, in the commercial banking book, these are sometimes larger deals and, therefore, in one quarter, we

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have a higher growth than others.

Even on the mortgage side in some of the countries, depending on where the customer demand is and also the tenors, we grow a little bit faster and sometimes a little bit slower.

So the guidance, not specifically is a target, but the guidance that we have given when we launched the strategy of growth of 3% to 4%, we still feel comfortable there across the different franchises that we have.

Now, on the regulatory cost outlook, Patrick is going to give you some more information there.

Patrick Flynn ***ING Group - CFO***

I hesitate to predict what this would be. What we can be clear about is we can compute what business growth will give us in terms of insurance schemes and deposits. But what we're not able to predict necessarily is which countries decide to introduce a much bigger amount.

As I said, I think the Polish piece that was a surprise [element] was EUR70 million. Right now, that's all we know and hence, we think the total is around the EUR840 million, which is -- the increase is due to, as I said, the Dutch DGS, which is implemented in full in 2016 rather than partially in 2015, so that's EUR133 million; and the Polish bank tax of EUR70 million is the bulk of it; and the remaining smaller increase is just due to business growth. So business growth is small.

Now, what would cause it to go up significantly is another element -- another new tax.

In terms of the foreign currency mortgages, I don't think that's in a bank tax sphere, that -- and by the way, we've a very, very small exposure there. Our Polish businesses, I think, it's about EUR300 million or EUR400 million, tiny; so that's not a big issue for us.

I think that's been translated more into minimum capital requirements for dividends for the entities in Poland rather than bank tax. There, given again, we have a very small requirement, it's something we can manage around.

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

Wilfred?

Wilfred Nagel ***ING Group - Chief Risk Officer***

Just briefly coming back to the question on the long growth in the commercial banking. As Ralph said, it's split pretty much across the board, the segments that stand out a bit as growing faster, are transportation infrastructure, working capital solutions, export finance and real estate.

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

[Across the board].

Pawel Dziedzic ***Goldman Sachs & Co. - Analyst***

Thank you.

Operator

Anke Reingen, Royal Bank of Canada.

Anke Reingen ***Royal Bank of Canada - Analyst***

Firstly, on your risk cost guidance of flat 2016 versus 2015, I was just wondering if you can give us a bit more of an indication of where -- of the different sub segments, looking at the second half? So basically, you're saying retail Netherlands/Belgium more like flat and the growth increase is coming then from the wholesale banking area. If you could just give a bit of indication of the sub segment?

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And then secondly, on the dividend, obviously in the past you've talked about the payout ratio of at least 40% of net profit. Just going forward, should we be thinking about like 60% of net profit in 2015? Is that sort of like a formula we could apply going forward, or should we just basically look at the -- really, just at the absolute level? Thank you very much.

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

Wilfred?

Wilfred Nagel ***ING Group - Chief Risk Officer***

Like we said on risk cost, generally in most business, we see improvement certainly on the retail side continuing maybe, as I said, not as quickly as it did over the past two years, but certainly will continue a positive trend.

Then what would be adding to provisions potentially, is as we discussed, the energy sector. Generally speaking, of course, also banking tends to be lumpy and could cause here and there through some bigger files also on uptick.

In terms of sub-segments, I think you've seen the development on business lending in the Netherlands. I think it's fair to assume that that will continue for a while.

The mortgage book in the Netherlands will certainly also continue to improve as far as we can see.

I think rest of the world, generally, is at healthy levels, might improve a bit; I'm not expecting a massive change there.

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

Then, Anke, on your question on dividends, yes, we are moving away from a payout ratio, that's the way we've guided over the last two years, as to what, at that moment, thought was the best way to kind of communicate it.

I think there's more clarity now around capital levels; more clarity about the underlying performance for us as well. Therefore, we have changed this to an absolute level of dividends, and the statement is that we aim to strive -- that we aim to grow the dividend over time.

Anke Reingen ***Royal Bank of Canada - Analyst***

Okay, thank you.

Operator

(Operator Instructions). Matthew Clark, Nomura.

Matthew Clark ***Nomura - Analyst***

Another question on costs please. Just wondering what you think your gross cost inflation is underlying? So if you strip out the regulatory costs, the redundancy costs, and the benefits from your legacy cost saving programs, it looks like you were very high in 2015, at 4% or 5%, is that a figure that you recognize? Why was it that high and what do you see it being going forwards? Thanks.

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

If you look at, and try to strip it down to the essence and look at what we see, things like inflation and labor schemes, which should mandate the pay increases, it's much lower than the 4%; it's maybe 1%/1.5% is maybe you might see a push factor and costs that come against us from those regulatory requirements as to indexing labor costs.

Matthew Clark ***Nomura - Analyst***

Okay, so why was it that much higher in 2015 then?

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

I don't think the inflation on the underlying salary costs have increased. It's just that, as we have announced, just over a year ago we decided to invest in the Dutch franchise, which is EUR100 million. We have indicated that we were investing in the industry-lending franchise; that

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we don't mind investing in the challenger and growth markets, if it is improving the cost income ratios, as we have shown you with the German picture, where costs are certainly increasing, but the cost income is rapidly coming down.

So the costs going up is not necessarily a bad thing. Those are the three areas that we specifically have decided to allow some cost growth. There's many areas where we don't allow it at all, and where we're actually decreasing cost.

But -- so the underlying cost growth in terms of inflation and all of that, salaries, we more or less take into account that for 1% to 1.5% of these last year. But then you have, as I said, EUR100 million in the Netherlands; EUR50 million in Germany; EUR50 million industry lending; EUR50 million in foreign exchange, on a cost, so it's a dollar cost and in euro costs its increased. So it's a combination of many factors there.

Matthew Clark ***Nomura - Analyst***

So, do you expect that same level of cost increase driven by rising investments, 2016 versus 2015, as you saw 2015 versus 2014? Or should the growth cost increase just reflect more the inflation you talked about, the 1.5% or so?

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

So the cost we don't want to necessarily grow is the inflation -- is the one with inflation and that's where basically indicated -- Patrick indicated we would allow for 1%/1.5%.

However, we really managed cost income. We really managed efficiency and we see much more volume coming through and it's the efficiency that we manage.

Again, in certain areas we don't mind costs growing. If, in the end, we feel that it is positive from a cost income perspective and, hence, positive also from a return on equity perspective. That's the way we look at costs, at this moment in time.

Matthew Clark ***Nomura - Analyst***

Okay, thank you.

Operator

Bart Jooris, Petercam.

Bart Jooris ***Degroof Petercam - Analyst***

Just one small follow-up question. Do you have any exposure towards the troubled Italian banking?

Wilfred Nagel ***ING Group - Chief Risk Officer***

We don't have any exposures to Italian banks that we worry about. We concentrate very much on the top end there and most of it is short-term interbank placements. But we don't really do a lot in the Italian market.

Bart Jooris ***Degroof Petercam - Analyst***

That's clear, thank you.

Operator

Robin Van Den Broek, Mediobanca.

Robin Van Den Broek ***Mediobanca - Analyst***

One follow-up question on your dividend versus capital framework. I was just wondering, if you look at your return on equity and your loan growth, you could calculate that your -- you need to retain 30% to 35% of your capital generation to support your capital targets. If you then look at consensus expectations for 2016, your pay-out ratio to be progressive is around 60%.

So I was wondering, what implications that may have for potential M&A and fintech investments? If you see sizeable opportunities, how will

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you deal with that? Could that go at the expense of dividends or how should we look at that?

Secondly, a more detailed question on the Netherlands. I believe that people that will refinance their mortgages and that are still on an interest-only framework, they cannot switch providers. Is that correct? So how do you look at that from a pricing perspective? It seems that you have flexibility to lift up the prices. But, again, that could also lead to some political pressure on that behavior. Thank you.

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

Okay, Robin. On the first one, this is the balancing act that we have. At the end of each year we have a capital generation. Out of that capital, and whatever capital requirement you, at that moment, have, you can make a decision between how do you firm up your capital even further; what do you want to reserve for further growth in your business; what is there for dividend.?

Now, on the dividend side, I think we have indicated where we are going, so we aim to pay a progressive dividend over time. So that should give you an indication as to the dividend components of it.

Now, when it comes to M&A, I've indicated previously as well, the core of our strategy is an organic strategy. Where we are looking at fintechs, these are very small amounts; they are not huge acquisitions that use a lot of capital. These are small, tactical amounts in order to get new abilities in through which we can grow organically ourselves. It may be teams and some asset portfolios which come with specific skills as well, but there's not, we're not earmarking a lot of capital from that perspective.

In the Netherlands on your mortgage situation, it is the case that if you stay with the same provider and you refinance on interest-only, then you do that within the same contract. As a consequence of which, you don't have to -- you're not ruled by the new law in which you have to adhere to annuity under your mortgage from a tax deductibility perspective.

Now, if you switch providers, clearly you have to enter into a new contract, because it's a different legal contract, because you're taking it out with a different bank. At that moment a new law applies and that law prescribes that you have to repay your mortgages, at least on an annuity basis, at least from a tax deductibility perspective. So it's what the law prescribes.

Robin Van Den Broek ***Mediobanca - Analyst***

And can you put a margin incremental on that? I guess so, because the annual -- the monthly payments for a client will be lower if they stay interest-only, so.

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

No, we don't.

Robin Van Den Broek ***Mediobanca - Analyst***

Okay.

Operator

That was our final question. Thank you.

Ralph Hamers ***ING Group - CEO & Chairman of the Executive Board***

Okay, thanks. Thanks for attending this call and for preparing these questions. It's always good to have these discussions around our set of numbers. I want to wrap it up very quickly.

I think 2015 has been a particularly successful for ING. We've really made progress on our Think Forward strategy and we're hitting the three bases that you need to hit.

The first one is growth: growth in customer numbers; growth in lending; growth in savings. The second one is profitability, and we're showing good profitability with good return on equity. The third one is capital levels and dividend policy.

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We're very happy that in 2015 we performed well on all three.

Thanks for your questions and talk to you soon. Thank you. Bye.

Operator

This concludes today's conference call. Thank you for your participation, ladies and gentlemen. You may now disconnect.

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