Transcript Analyst Call 4Q2022

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Presentation

Operator
Good morning. This is Priscilla welcoming you to ING's Q4 2022 conference call. Please note today's conference is being recorded. Before handing this conference call 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 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 statement is contained in our public filings, including our most recent annual report on Form 10-K filed with the United States Securities and Exchange Commission, and in 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. Steven, over to you.

Steven van Rijswijk
Thank you very much. Good morning and welcome to our full year 2022 results call. I hope you're all well. As usual, I'm joined by our CFO, Tanate Phutrakul, and our CRO, Ljiljana Čortan, and I'm pleased to take you through today's presentation. After that, we will take your questions.

After two years in which the pandemic dominated headlines, 2022 was another turbulent year. The war in Ukraine, an energy crisis, soaring inflation, and for the first time in over eight years, central bank rates turned positive. In this exceptional year, we continue to deliver value and I'm proud of our ability to adapt and to manage the company through challenging times. To manage the impact of negative rates, we diversified our income. To manage through the pandemic, we smoothly switched to working virtual. And most recently, with the war in Ukraine, we helped to keep our employees in Ukraine safe, and we de-risked our Russian book.

Let me reiterate that we focus on being the best universal bank in Europe and we focus on organic growth, which we again delivered in 2022 by adding 585,000 primary customers. Now over 47% of active customers are primary customers, and I am pleased to see that our focus on offering a superior customer experience is paying off. This is supported by our digital-only, mobile-first strategy in retail, as visible in the growing share of mobile-only customers, while also a larger part of customer journeys in retail are now end-to-end digital as measured through our Digi index.

Another achievement was the growing volume mobilized to help our wholesale clients transition to a more sustainable business model. In 2022, this volume was up by about 15%, exceeding €100 billion. In our P&L we saw the benefits of the rising rate environment, with clean NII up by €1.1 billion in 2022, and this is on top of the structurally higher fee base resulting from our efforts to diversify income. We expect this strong performance on income to continue, reflected in an improved total income growth target, which we'll come to later. All of this has enabled us to return €4.8 billion to our shareholders in 2022.

Now, before we go into the financial results, I want to spend some time on the progress of our strategy and related targets.

On to slide three, showing our purpose and strategic priorities. One priority is to deliver a superior customer experience. As banking products are commoditised, customer experience is a key differentiator for customer growth. This delivers value by increasing diversified income while serving a larger base will lower the cost to serve per customer. A superior customer experience means easy, relevant, personal and instant across all channels, leading to a growing number of customers who promote ING. In retail, we have the highest net promoter score in six out of ten countries, which includes some of the biggest markets like the Netherlands and Germany. In markets where we are not there yet, we are working hard to improve. Also in Wholesale banking, we have seen NPS improving from 59 at year end 2021 to 67 at the end of 2022.

More promoters lead to more customers, more cross-sell, and in the end, more primary customers. Growing our primary customers is a key target as the base for future value creation. With investments in our businesses and also with savings again becoming a profitable product, we will continue on our path to grow this base.

Our other priority is sustainability, where an important aim is to support our clients in their transition to a sustainable business model. Our efforts to do so have paid off, reflected in a growing volume mobilised for our wholesale banking clients and we have momentum to reach €125 billion per annum by 2025. To support our efforts to steer our loan portfolio to net zero, we have updated the intermediate 2030 targets for the sectors covered by our Terra approach, aligning with net zero pathways.

Then on to the strategic enablers on slide four, as also shared during our investor update. A seamless digital experience, a scalable tech and operations foundation, a safe and secure bank, and of course, our people. We continue to invest in these areas, and I would like to highlight the progress on some of these enablers. We mentioned progress on the digi index on the first slide as a 2022 highlight. This index measures the average straight-through-processing rate of 341 retail customer journeys and is a good proxy for how digital we are. At yearend, the average STP rate reached 64%, up from 60% end of 2021. Not reflected yet in this measurement is wholesale banking, however, we are working also to digitise the processes in wholesale banking and will take that into scope as well.

We made good progress on centralising services and capabilities in our hubs, which helps us to streamline processes and improve quality and productivity. For our people, we promote diversity at ING and it's essential for delivering on our strategy. We believe that diverse teams bring a healthy mix of contrasting perspectives and are more innovative, creative and therefore bring better outcomes. When looking at diversity and inclusion, we apply the 70%-principle, striving for teams to comprise no more than 70% of the same gender, nationality or age group. And we have set a target to grow the representation of women in senior management, which is at 29% now, already very close to our 2025 target.

Slide five shows the outcome of our strategy execution in 2022 and our financial targets for 2025. On fee growth, in daily banking we see further room to increase or introduce fees. In investment products, the continued growth of accounts is a strong base for growth when market confidence improves. This confidence will also support growth of lending fees. Higher fees will support total income growth, though for 2023 the main driver will continue to be liability NII. And while there are some uncertainties, such as further central bank rate increases, deposit tracking and customer behaviour, the tailwind from liabilities will continue. For 2023, we expect total income growth of over 10%, which also leads to an improvement of our target for the coming years, up from a 3% CAGR to a 4-5% CAGR. This income growth will support an improvement of our cost-income ratio to 55-56% in 2023. On the cost side, we expect to see some pressure from the full year effect of inflation, and we continue to invest in our business and to execute our strategy, which should bring benefits in the longer term.

On our CET1 ratio, we intend to move to our target CET1 ratio of around 12.5% through a 50% payout of resilient net profit combined with additional distributions, in roughly equal steps. We will update the market on the distribution plans with the announcement of our first quarter 2023 results.

On return on equity, with the targeted development of the cost-income ratio, our low through-the-cycle risk costs, and the CET1 ratio target of around 12.5%, we have confidence we will reach our target of 12% RoE by 2025.

Now let me take you through our full year 2022 results, starting on slide seven. The return of positive interest rates in 2022 clearly demonstrated the benefit of our funding profile, with a high share of retail deposits and limited dependence on more volatile wholesale banking funding. After years of being a drag on income, rate increases have turned our large retail deposit base back into a driver of income growth, and the effect is clearly visible in the improvement of our deposit margin over the past year.

At the same time, the quick pace of rate hikes impacted lending margins, as client rates generally track the higher cost of funds with a delay. Combined with lower prepayments on mortgages, lending margins have come down over 2022, stabilising at the end of the year. Lending demand was subdued, reflecting increased uncertainties and lower affordability in the case of mortgages, due to high inflation rates and energy prices.

These developments are visible when we look at total income. In 2022, liability NII was the clear driver of growth, while known liability NII declined slightly. Fees came in at a higher level, reflecting our focus on income diversification. Taking this all together, total income corrected for the net TLTRO impact and the Polish mortgage moratorium, grew by €1 billion in 2022.

The next slide zooms in on the main components of total income. As mentioned, liability NII was a clear growth driver, up 53% compared to 2021. Due to the aforementioned reasons, lending NII was subdued and came in 8% lower. Turning to fees. Fee income was resilient, despite uncertainty that has affected the appetite for both investments and lending. The full year increase was driven by impressive growth in daily banking, reflecting growth in primary customers, the increase in payment package fees and new service fees.

Then expenses on slide nine. Regulatory costs were slightly lower, mainly reflecting a 50% add-on to the Dutch bank tax in 2021. Furthermore, 2022 expenses for the full year included €325 million in incidental items, mainly reflecting restructuring provisions. Excluding these incidental items, operating expenses were impacted by high inflation, and this was mainly visible in staff costs, where increases were largely driven by indexation. As an example, the legally required bi-monthly indexation in Belgium drove up annual staff cost by 9%. This impact could not entirely be offset by the benefits from management actions taken to restructure the service model and change the footprint.

Next to indexation, in several countries, we have provided voluntary compensation to help our people cope with the rising energy prices. As mentioned, we also continue to invest in our businesses in digitalising customer journeys and also in marketing campaigns, to ensure we keep increasing the number of primary customers, thereby expanding the base for future growth. Combining these investments with the full year impact of inflationary pressure, we expect to see some cost pressure in 2023 and we will continue to focus on cost control.

Slide ten shows the risk cost development, with the full year 2022 risk costs coming in at €1.86 billion. This was largely driven by actions taken related to our Russia book and the impact of deteriorated macroeconomic indicators. Management overlays for risks from second order effects of the deteriorated environment were largely offset by releases of COVID-related overlays. The total amount of overlays remaining at year-end was €453 million. Our stage 3 ratio remained low at 1.4% and although the current environment is not without challenges, we feel confident about the quality of our loan book, supported by the fact that we are well diversified and avoid concentration risk. Our loan book is senior-only and well collateralized, and in wholesale banking, we mainly work with investment grade companies. And finally, historically, our provisioning has been prudent, and without surprises when we do move into the recovery phase.

Then we move to return on equity on slide 11. 2022 return on equity was affected by the higher level of risk costs, as well as incidental costs and high capital levels. When adjusting for the incidental costs, our through-the-cycle risk costs and our targeted around 12.5% CET1 ratio, the RoE was 9.6%. Going forward, reaching our 12% RoE target will be supported by several factors, such as further growth of primary customers, our 4-5% CAGR on total income, as well as higher fees combined with continued discipline on controllable expenses and maintaining high asset quality. And at the same time, we intend to reduce the equity level over time and we take management actions to control risk weighted assets and to improve capital allocation.

Then I move to slide 12. Over the past years, we have built a strong track record of delivering an attractive return for our shareholders. ING continues to be a strong investment case as the best European universal bank with consistent strategy execution, income growth, well contained expenses and strong asset quality. Combined with our strong capital position, we are in a good position to return capital to shareholders. for the amount we distributed over 2022 represented an attractive shareholder return of 12.5%.

I move to the fourth quarter results on slide 14, and I will take you through those a bit more quickly as the trends are known and we would like to have sufficient time for Q&A.

Fourth quarter results of 2022 showed a strong performance on our pre-provision profit. When excluding volatile items and regulatory costs, pre-provision profit was up almost 28% year on year and 4% higher quarter on quarter, and we will address underlying P&L lines in the following slides.

Slide 15 shows the strong development of NII. This was driven by liability NII, reflecting rate increases, limited deposit tracking and a continued deposit inflow. In lending NII we saw pressure on mortgage margins due to rising interest rates, as client rates generally track higher funding costs with a delay, as well as declining income from prepayment penalties. Quarter on quarter, this effect stabilised. Excluding the net TLTRO impact and the Polish mortgage moratorium, our net interest margin for the fourth quarter increased to 148 basis points, mainly reflecting the higher NII on liabilities.

Slide 16 shows net core lending growth. In retail mortgages continued to grow, although at a lower pace, reflecting an overall slowdown of demand driven by uncertainty and higher interest rates. Higher net core lending in business lending was mainly visible in Belgium. In Wholesale banking, loan growth was mainly visible in Lending and Working Capital Solutions, which was partly offset by trade & commodity finance, reflecting lower commodity prices. Going forward, with still heightened macroeconomic uncertainty, we expect loan demand to remain subdued. Net customer deposits growth was €7.2 billion, fully due to retail, mainly reflecting inflows in Germany, the Netherlands and Spain. Wholesale banking recorded a seasonal year-end outflow.

Then we move on to fees on page 17, which showed resilience despite uncertainty affecting the appetite for both investments and lending. Year-on-year fee income was down. Daily banking fees continued to grow, this quarter by 11% compared to the same quarter last year, and this reflected growth in primary customers, the increase in payment package fees and new service fees. Lending fees were up year-on-year thanks to strong fee income in wholesale banking. In investment products, we continue to see the effect of lower stock markets and less trading activity, although the opening of investment accounts continues. Sequentially, fees were up, reflecting growth in both investment products and lending. Daily banking fees were lower due to seasonally lower travel-related fees in retail banking.

Then we move to slide 18. Excluding regulatory costs and incidental items, operating expenses were well contained, with growth well below inflation. As I explained, this as mainly the effect of high inflation rates coming in via salary indexation and CLA increases, while we also keep investing for future growth. Regulatory costs were down year-on-year as the fourth quarter of 2021 included a 50% add-on to the annual bank tax. Quarter on quarter, higher regulatory costs reflected the payment of the annual Dutch bank tax, which is always paid in the fourth quarter. Incidental items this quarter included €43 million of restructuring costs, €30 million of allowances to employees to offer support for increased energy costs and €9 million for hyperinflation accounting in Turkey. Overall, in light of the current operating environment, and especially when looking at the high inflation rates, I am pleased with how well operating expenses were contained, especially in Belgium and the Netherlands.

Then to risk costs on the next slide, that's slide 19, which were €260 million this quarter or 17 basis points over average customer lending. This included a further release of €112 million in stage 2 for Russian exposure and a €46 million release of management overlays for the potential impact of secondary risks in the current macroeconomic environment. In total, we have built up €453 million in management overlays at the end of 2022.

In stage 3, we saw some collective provisioning in retail banking, mainly on consumer lending and business banking. In wholesale banking, we took stage 3 provisions mainly for some new files. The slight increase in the stage 2 ratio was mainly driven by wholesale banking. The increase reflected lower total credit outstandings, partially due to €30 billion repayments of TLTRO funds, rather than a deterioration in the risk profile. Our stage 2 outstandings actually went down. The stage 3 ratio remained low at 1.4%.

Slide 20 shows our CET1 ratio, which remained strong at 14.5%. It was actually up compared to our third quarter of 2022 pro forma CET1 ratio of 14.3%, which included the buyback we announced with the previous quarter's results. This buyback was also the main driver for a €2 billion reduction in CET1 capital, which also includes FX impacts. Risk weighted assets were €7 billion lower, largely due to €-5.7 billion of FX impacts. Credit RWA were down when excluding these impacts, reflecting an improvement of the overall profile of our loan book and model updates. Our operational RWA reflected the update of the AMA model. Finally, market RWA were marginally lower. Concerning our distribution, we propose a final 2022 dividend of 38.9 cents per share, subject to AGM approval on 24th of April.

Let me wrap up with the highlights. Overall, in a challenging environment, we have delivered strong results in 2022 and in the fourth 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. To see these efforts positively reflected in primary customer numbers, NPS and volume mobilised in transition finance. Our financial results show that accelerating NII momentum is a key tailwind, while fee income has proven to be resilient. Expenses were well contained, despite the inflationary pressure of indexation in some markets and continued investments to realise our strategy. Our capital position remains strong, and going forward, I am confident that we will continue to deliver robust financial results and successfully execute our strategy. And with that, I now go over to Q&A. Thank you.

Q&A

Operator
Thank you, Steven. Ladies and gentlemen, if you would like to ask a question, please press star one on your telephone keypad. In the interest of time, we kindly ask each analyst to limit yourself to two questions only. Thank you. We will take our first question from Benoît Pétrarque from Kepler Cheuvreux. Please go ahead. Your line is open.

Benoît Pétrarque (Kepler Cheuvreux)
Yes. Good morning. Benoît Pétrarque from Kepler Cheuvreux. So two questions. One, on the >10% income growth and the second one on the cost-income. So, first, on the >10% income growth, could you maybe be a bit more specific in terms of what you expect potentially, because that implies quite a large potential range. So what could be kind of the upper end of this guidance in the favorable scenario around pass-through and markets? And just to make sure, do you still have in mind in that guidance, the 30% pass through rate for 2023, or based on the current market developments, things probably change, and you have a different assumption. Could you maybe Specify that a bit? What are your thoughts around pass through as well the pass through rate embedded in this guidance?

The second one is on cost. I think you said in the past that you wanted to maintain costs below inflation. I think the 55-56% implies potentially a 6-7% cost growth for 2023, which will put you slightly above the inflation headline. So just wanted to check with you if that's the current view, if it's a proper way of thinking about cost growth. And also, maybe on the 55-56%, can we assume it's going to be more the 56% on the 10% income growth and potentially 55% on a 12-13% income growth scenario? Just wanted to clarify that. Thank you.

Steven van Rijswijk
Well, thank you very much. I think the questions are linked to some extent, so I'll hand over to Tanate.

Tanate Phutrakul
Thanks, Benoit. I think in terms of context of how we come up with the guidance, I think we want to remind you that we are operating in an environment of significant uncertainty and quite bearishness in terms of macroeconomic outlook. So we are prudent in terms of our financial planning in that context. Then in terms of income growth of more than 10%, what's driving that is really a few items, whether it's on the high or on the low side, as you mention it. One is loan growth. You see that loan growth in Q4 has been slowing and that will be one determinant, and lending margin.

The second is the tracking speed, we have given you at Q3 results a certain simulation of our tracking speeds. And we had assumed, if I can refresh your memory, around 30%, 40% and 50%. The tracking speed that we see so far in Q4 has been more like 15%, which in our opinion is on the low side. So, from that perspective, I think we see that the catch up in terms of deposit tracking should be more prevalent in 2023 compared to Q4 2022. Okay. Then in terms of linkages, yes, indeed, if we are operating at over 10% you would imagine the cost-income ratio to be on the high end of our guidance and if we go higher, then obviously it comes to the low end or beyond.

Benoît Pétrarque (Kepler Cheuvreux)
And maybe just on 2023, because growth implicitly, based on your cost-income, is in the range of 6-7%, slightly higher than the headline eurozone inflation for 2023. Is that correct?

Tanate Phutrakul
Well, that's why we give you guidance with respect to cost-income ratio, to give you variability in terms of income and cost trajectory. I think we have clearly more pressure in terms of salaries from the high inflation you see in the back end of 2022. But we also have targeted certain investments we will make in terms of, for example, client acquisition. So one of our primary targets for next year is to increase primary customer growth. So within that context, we do expect to operate at between 55-56% cost-income ratio.

Benoît Pétrarque (Kepler Cheuvreux)
Great. Thank you so much.

Operator
Thank you. We'll now move on to our next participant, Raul Sinha from JP Morgan. Please go ahead, sir. Your line is open.

Raul Sinha (JP Morgan)
Hi. Good morning. Thanks very much for taking my questions. A couple of questions from my side. The first one really just for Steven, what gives you the confidence to reiterate the 50-52% long term cost-income ratio guidance, given obviously the inflationary pressure that you're seeing in 2023? Could you talk to us about how you're able to manage the efficiency lever back to what you were thinking about at the Investor Day, given the environment for costs has changed quite dramatically since then. So what gives you the confidence that you can hit 50-52%? And also related to that, I guess your income guidance is higher than expected. Cost-income ratio is same, but the ROTE has not gone up in terms of what you think you can make. So is there some new negatives relative to what you saw at Investor Day or you're just being conservative?

The second question is around the buyback phasing for 2023. Could you remind us, please, of the withholding tax threshold for this year? And I'm surprised that there is some surprise in the market that there was no buyback today. So I just think it would be helpful for us to get a little bit more clear message in terms of the timing of any potential buybacks later this year. Thank you. Okay.

Steven van Rijswijk
I'll leave the question on the tax and the buybacks to Tanate, and I'll focus on the guidance that we have for 2025. Clearly, also compared to the rates that we saw during the Investor Day, the rates went further up. That goes for income, and it also goes for inflation. In that setting, what you continue to see is that first of all, we have been able to grow our interest income on the back of higher interest rates, and that was 17% compared to the same quarter last year. We have been able to actually still grow our fee income this year with 2%, but that was on the back of, let's say, more stability, more annuity in our payment business while our investment business was going was going down based on the fact that stock markets were lower and also

to some extent a bit subdued lending activity. And we start therefore from a better structural base of fee income than we did last year. We have grown our primary customers, with 600,000, and we are confident to continue to be able to do it. And these customers are people that we can do more with and therefore we continue to be confident to grow our fee base with 5 to 10% per annum.

And in that setting, we on the one hand benefit from higher interest income, but that has also to do with the tracking of interest rates which is currently still lower than the 30% that we gave as an example in the presentation we showed you in November. And of course, pressure on inflation that we are seeing in salaries in different countries, that we need to continue to manage with digitalisation through our scalable technology foundation as well as our seamless digital services that we do on a continuous basis. We're very strict on cost management, and that gives me the confidence that we'll move to these returns that we talked about, the 12% RoE and the 50-52% cost/income ratio in 2025.

Tanate Phutrakul
So just to answer your question, on the level of cash distribution to make the hurdle for share buyback in 2023, it's approximately €2.8 billion. And as mentioned, we are going to give you an update on our capital management at the Q1 results.

Raul Sinha (JP Morgan)
Thank you.

Operator
Thank you. We'll now move on to our next question from Flora Bocahut from Jefferies. Please go ahead. Your line is open.

Flora Bocahut (Jefferies)
Yes. Thank you and good morning. The first question I had is regarding the provisions. Obviously, you didn't provide any guidance for 2023 for that P&L line. You've been making positive comments regarding the strength of your loan book in the slide pack. So could you maybe elaborate a bit on the trends that you're seeing there, whether you are seeing first signs of a degradation in the asset quality, and therefore what we should expect maybe for the 2023 provision outlook compared to the through-the-cycle guidance? And then the second question is just coming back to the, sorry, the 10% income growth. I just wanted to check to what number that implies. Is that to the reported 2022 number or is that to the adjusted 2022 income for the Polish one off and the TLTRO impact? Thank you.

Steven van Rijswijk
I will answer that on income growth and Ljiljana will answer on provisions. So, the larger than 10%. So I should maybe emphasize that the larger than 10% forecast is based compared to the reported 2000 total income level. Sorry, 2022 income level. Ljiljana?

Ljiljana Cortan
Good morning. Yeah, with respect to provisions, as you recall, we usually do not guide. However, if you remember what we talked about in June, we feel quite confident with the portfolio structure and quality as it is, and as well with the risk management framework around it, which will, we are confident, ensure that in the next few years we remain within our through the cycle average. Additional to that, I would say the recent results of the fourth quarter give us additional confidence that we are doing the right things. That means that we do not see in our portfolios any increase of NPLs in the fourth quarter.

And secondly, we do not see any structural delinquencies either on payments or on the, I would say, deterioration of quality in any of the asset classes. Let me also remind you on the structure of our portfolio, which is very much collateralized, very much in residential real estate with low LTVs and quite, I would say, a subdued part of the consumer lending and business lending, which are usually the first deterioration part of the portfolio. So having said that, having seen the good development in 2022, specifically also the fourth quarter, having seen the structure of our portfolio going forward and having the risk management techniques in place that we do have, we feel confident to remain in that range. Thank you.

Operator
Thank you. We'll now move on to our next question from Farquhar Murray from Autonomous. Please go ahead, sir. Your line is open.

Farquhar Murray (Autonomous)
Morning, all. To come back to slide seven where you're showing the liability margin. I think at the last call you kind of indicated the scope for that to maybe go over 100 basis points. I just wondered if you could give us a sense, particularly looking forward through to full year 2025, what kind of liability margin you're kind of expecting to normalize back to? And then just coming

to the cost side of things. If I look at the 50-52% for full year 2025, it seems to be almost suggesting costs at a headline level are basically flat between full year 2023 and 2025. And I just wondered if you could give us a bit of a sense of the bridging elements within that. I think regulatory costs are expected to come down. I kind of now wonder if investment costs also come down and presumably there's some degree of background cost drift within that kind of assumption as well. So just run that some detail around that, if that's possible. Thanks.

Tanate Phutrakul
So the first one is on deposit margin, and as I mentioned before, the tracking speed has been slow given the sharp rise in the ECB rates that we see now. But what we've seen historically in more normal times is that deposit margin seems to range around 1%. So, we are at around 94 basis points as of the end of Q4. So, there is a bit more room in a normal situation for that. But I have to remind you that the yield curve is having this massively sharp rise and then plateaus after a while, so you have to take that into account.

In terms of cost target for 2025, I think you have to think about two things that we expect to moderate. Number one clearly is regulatory expenses. DGS contribution and taxes, we expect that to decline, particularly starting in 2024 they expect to normalise. As inflation comes down, the salary increases we expect to normalize as well, while continuing to maintain our efficiency programs to mitigate much of the cost increase, which we have done historically.

Farquhar Murray (Autonomous)
And just to follow up on that, I mean, should we expect an overshoot versus the 100 early in this year in terms of the liability margin?

Tanate Phutrakul
So it just depends on the competitive situation. When we do our planning, we had some observations where the system deposit level would go, decline or not. But as you noticed, deposits actually grew by €10 billion. So there is continued build-up of deposits, which bodes well for deposit margin.

Farquhar Murray (Autonomous)
Okay. Thanks a lot.

Operator
Thank you. We will now move on to our next question from Kiri Vijarayarajah from HSBC. Please go ahead, sir. Your line is open.

Kiri Vijarayarajah (HSBC)
Yes. Good morning, everyone. I've got a couple of questions on the fee side. So firstly, on the retail side, when interest rates were negative and you were actually pretty successful in pushing through some quite meaningful fee increases, I think that's more kind of to 2021 rather than last year. But my question is more as interest rates normalise and the deposit margin also normalises, do you think it gets progressively harder to push through kind of that next leg of retail fee increases that you're kind of assuming in your 2023 and 2025 targets?

And then secondly, still on fees, but more on the wholesale bank side, the fees there always sort of jump around a little bit quarter to quarter. But I wondered what your pipeline on the larger deals looks like in the wholesale bank. And I guess for the industry as a whole that's weakening at the moment. And then on the fee side, on the flow, businesses trading, commodity finance, does that also look like it's going to be subdued in the short term for the first quarter, first half of this year? So really just some color on the wholesale fee outlook, please. Thank you.

Steven van Rijswijk
Thank you very much. Clearly, we are entering a different environment than we did before. At the same time, we have said that, like we said before, there are a number of levers that we can pull to grow our business. First of all, it's growing our primary customer base. Very simply, that's what we grew by 600,000 this year with over 200,000 this quarter, and we work on growing that base. That's also why we continue to work on improving our experience and put marketing to work, because when we have these primary customers, they do more with us. That's step one.

Step two is we continue to focus on extending our services to more customers. And also in the fourth quarter, even though the stock market levels are still subdued, for example, in Germany, again, the number of new customers coming, or the net new number of customers coming on to the investment app was around 50,000. So we continue to grow the number of people that work with us on our fee business products.

Thirdly, we extend the number of services. So what we have done in Germany with investment, we also extend to other markets where we introduce new payment products. And for market leaders, the topic that you mentioned, we also reprice there where we can when we provide the adequate service. For example, this year we already announced that as per the first quarter of this year we will increase our payment packages in the Netherlands for retail customers and we will increase the payment packages for business customers in Belgium. So we also continue to do that, and all those elements give us confidence that we will continue to make 5 to 10% growth over the next years.

When it comes to wholesale banking, yes, the pipelines are good and we saw in the fourth quarter when there was, of course, a lot of uncertainty in the first part of the year and of course there are still uncertainties. But at some point, companies do need to invest. And that's why you see a number of the larger syndicated loan deals coming back. And that's what we've also seen in the third quarter, but also in the fourth quarter of this year. And on the flip side, we saw the lower energy prices that have an impact on the trade in the commodity finance financing. So the trade financing that's quite dependent on price. And therefore, also the fees on that part. So that the latter part is more volatile because it really depends on the pricing of, let's say, the barges of oil and gas.

And in terms of the deal volume in wholesale banking, we're cautiously optimistic that levels also continue in 2023, given the fact that inflation numbers are coming down a bit as GDP levels for Europe are a bit above zero, the activity in China is resuming after the lockdown has expired. Decrease in political tensions between China and the US, with, of course, a big overhang being the war in Ukraine, but cautiously optimistic also in that sense on fees for 2023.

Kiri Vijarayarajah (HSBC)
Great. Thank you.

Operator
Thank you. We'll now move on to our next participant, Benjamin Goy From Deutsche Bank. Please go ahead, sir. Your line is open.

Benjamin Goy (Deutsche Bank)
Hi, good morning. I have just two questions and maybe in light of some news, maybe surprising news last month, that you could update us on your capital allocation policy, dividends, share buyback, organic growth, but also M&A. And then secondly, obviously, that was a focus on primary customers. But I was wondering whether you have somewhat more appetite for also growing customers at large, given they're much more profitable these days and interest rate environment. So I think you're using some teaser rates in some markets. Just be interested in your thoughts here. Thank you.

Steven van Rijswijk
Okay. Thank you very much. I will answer the question on customers and Tanate on capital allocation. With regards to customers, we continue, on the one hand, to focus on growing our primary customers. Those are customers that have part of their salary account with us plus one additional product. And we do that by providing them with easy, instant, personal and relevant experience. And that's why we're also focusing so much on digitalisation of the journeys that I talked about, the Digi index, which we will also improve because that gives us the ability to grow. If you look at most of the markets, if not all the markets in the fourth quarter, we again were able to grow that number and we are able to do that because our experience generally is being perceived as better than that of our peers.

If you look at the net promoter score, in six out of the ten retail markets, we came in at number one, including large markets such as the Netherlands and Germany. So that's what we want to do on that end. And we know that primary customers do a multiple more of what non-primary customers will do. That's why in the target we have for 2025, we are focusing on the continuing growth of that number and it's in the KPIs of all of the country heads in all of the markets.

When we look at generically customer growth. If you look at, let's say, the still uncertain outlook that we have on the economic environment. Yes, cautiously optimistic, like I just said. Still uncertain. When we talk about the larger mid corporate wholesale banking clients, we largely focus on existing clients and try to help them try to focus also on their transition finance. Like I said, transition finance mobilized last year, increased at around 15% from €88 billion to €101 billion. So we want to be there for our existing clients and we're prudent with regards to onboarding new clients. Also, given the fact that currently the environment is still relatively uncertain and that's the way that we want to grow our client base. Tanate?

Tanate Phutrakul
So to answer your question, Benjamin, on capital allocation, we always look dynamically at our capital allocation, and that's why we decided to exit from subscale businesses like Czech, Austria and France, and that capital we deploy to businesses that make the hurdle. So that's one part of our strategy which continues. At the same time for 2023, you would see that our capital deployment in terms of lending will be less, right, given the fact that lending is slowing and that allocation of capital to that

aspect of our business will be more modest compared to previous year. But at the same time, we see more profitability coming from deposit gathering and that attracts relatively limited levels of capital required to increase that business. So overall, I think we can take whatever we need to do in terms of capital allocation but stick with our ambition in terms of capital distribution to get in roughly equal steps that to 12.5% by 2025.

Benjamin Goy
Thank you. You didn't mention M&A at all, so I assume this is a very low priority for you or maybe you can comment on that as well.

Steven van Rijswijk
Okay, so you were alluding to M&A. Well, look, I mean, our first focus is on organic growth. And we have been able, again, to grow over 600,000 customers. We were again able to grow our loan book with €18 billion, which is a bit lower than in the previous years because of the economic situation. We're able to grow last year our deposit franchise with €25 billion. We were able to diversify our income further. So we are being seen in a number of the markets as the best player and that also means that we're able to continue to grow our customer base there. Organic growth, that's the first focus area we have. In case in some of these markets we want to reiterate our position as a European universal banking leader, and in some of these markets there would be an opportunity for in-market consolidation under the right conditions, i.e. no big restructurings, a good digital platform, clients that we can put on our platform, broadening of the revenue base, ability to realise cost benefits, then we will look at it. If you ask me, do you focus on large scale European consolidation moves? The answer is no. I think it is very difficult. Also, not only in the light of the difficult integration we have to do there, but also because the benefits of cross-border mergers in banking are just limited given the compartmentalization that we see in liquidity, capital, data systems, product requirements, that makes it hard. And I'm not a firm believer in that at this point in time.

Benjamin Goy (Deutsche Bank)
Thank you very much.

Operator
Thank you. We'll now move on to Andreas Scheriau from Goldman Sachs. Please go ahead. Your line is open.

Andreas Scheriau (Goldman Sachs)
Good morning. Thank you for taking my questions. Can I come back to slide seven, please, and follow up on the Farquhar's question. If we're looking forward, the deposit margin will likely expand meaningfully again next quarter. What is your degree of confidence in sustaining the higher deposit margins that we will be seeing in the first and potentially second quarter? And what do you foresee for the development of asset margins from here in the fourth quarter as you showed on the slide or also in 2017, that was around 150 basis points versus 127 basis points in the fourth quarter. Should that pick up from here as repricing lags fade or stay around this level as this is a more structural issue in a higher rate environment?

And then the second one would be on deposit trends. If you could just speak to what you're seeing there, the mix within it and how this compares to expectations. And perhaps one specific question, if I can add, you've previously talked about migration from current into savings accounts. What is your expectation with regards to migration into time deposits? Thank you very much.

Steven van Rijswijk
Thanks very much. When we talk about the deposit margins, I'll leave that to Tanate. I will give you some answer on lending, on what we see in the lending market as such. What we have seen, especially in retail banking, is that lending margins have contracted over the last year. And the main reason for that was that on the one hand, the prepayment penalty fees came down and that was because less people start to prepay their mortgages because the interest rates were higher and most of our mortgages are fixed rate mortgages, therefore they don't feel a need to prepay so quickly. So those levels came off and that was included in that lending margin.

And secondly, you will see that the increase in the market rates always goes quicker than you can reprice to clients. So that has led to a contracting margin on the lending side, not so much in wholesale banking, where the margin remained pretty stable over the year, but largely in retail banking. In the fourth quarter, we now see that leveling off on the downside, I mean, what we now see is a sort of a stable level of prepayments. We now see that we were able to price in the higher market rates into the mortgages, and therefore we would expect that to also stabilize going forward and potentially, depending on demands, to have some risk on the upside, I would say, so there is maybe some benefit on the upside.

In wholesale banking, it largely depends. The margin will largely depend on the amount of liquidity that is coming onto the market. Clearly, there is now some monetary contraction by the ECB. That in itself could help. In terms of getting the margins at a higher level, whatever it will be, and we will need to remain prudent in that regard. We'll price all those deals to the applicable return. If the price is not making that return hurdle, that in the end leads us to the RoE levels that we also indicated in our investor update, then we will just not do the deal. So we need to stay prudent and very disciplined in that matter.

When it comes to savings and let's say the behavior of people, we've also seen that in the fourth quarter, again. Although we thought in Europe we would enter into a technical recession, that's still a question. All the central statistics bureaus are still calculating whether this is really the case or not, because the consumer spending actually in December and November went up quite a bit. So that remains a question. But I think more in general, one can say that the outlook seems to be a bit more positive than we thought let's say a quarter ago. It also shows, by the way, how volatile this outlook is. But in that setting, we do still see cautious behavior of customers. And in the fourth quarter, that meant that only for us already our savings increased in retail with €10 billion, which is quite significant, and we would expect that to continue also in 2023, because spending levels, given the current macroeconomic environment, are a bit lower.

When they're moving from current accounts to savings accounts, we haven't really seen a massive shift in that regard, so that remains to be seen. Most of the money that people use, they use for daily usage. In the past, by the way, when we talk about pre financial crisis or during the financial crisis, in many countries, we had only savings accounts because we started as a direct bank there. We brought our product also to current accounts and I haven't really seen in the last number of months a shift in that mix because people typically use their money on a daily basis.

Tanate Phutrakul
To address your question on deposit margin, just giving you our kind of views of where first ECB rates are to go. We do expect that the decision today would be for another rate hike and another two rate hikes into the month of May. So with rising ECB rates, then the tracking speed in Q1 and Q2 is likely to lag those ECB rate hikes. So that from that perspective, that would point to higher deposit margin. But then we do expect that tracking will increase and that margin would normalise over time to that kind of 90 to 100 basis points level on deposits. That's kind of our view at the current time. And the last really on tracking speed, it really depends on loan growth, right? The lower the loan growth, the less demand we have for additional funds. And that would mean that pressure on increasing deposit rates would be less.

Andreas Scheriau (Goldman Sachs)
Very clear. Thank you very much to both of you.

Operator
Thank you, Andreas. We will now move on to Sam Moran-Smyth from Barclays. Please go ahead, sir. Your line is open.

Sam Moran-Smyth (Barclays)
Hi. Good morning. Two questions, please. So the Dutch unions say the collective labour agreement negotiations have hit deadlock. So could you perhaps update us on the status there from your point of view, and perhaps you could give us a rough guide on how much salary inflation in the Netherlands is baked into your FY23 cost income guidance? And then secondly, on that cost income guidance of 55-56% and also on the 10% top line growth guidance, could you give us some clarity on which of those are adjusted for the FY22 exceptional, so namely TLTRO and the Polish mortgage moratoriums? Thanks very much.

Steven van Rijswijk
Tanate will answer the second question. I will do the first on CLA. Yes, we have been in conversations again with the unions in the past number of weeks. Those conversations in this country came to a halt. We believe that we offer a fair package for 2023 and 2024. The package also was made public. That is a clear increase for this year of 3%, the next year of 4%. That is not the total sum, because there also some in scale increases. Obviously, we have taken those all into our cost projections for 2023, and it remains to be seen what the unions will come back with. We are convinced that we have offered something which is completely fair, reasonable and we would expect the unions to come back and then would take it from there.

Tanate Phutrakul
Then, Sam, to answer your question, the 10% or greater guidance that we gave on revenue is based on our reported numbers, so unadjusted.

Sam Moran-Smyth (Barclays)
Brilliant. Thank you.

Operator
Thank you. We'll now move on to our next question from Tarik El Mejjad from Bank of America. Please go ahead. Your line is open.

Tarik El Mejjad (Bank of America)
Hi. Good morning. You sound today a bit cautiously optimistic and even say conservative in a number of P&L lines. Should we be concerned about you being conservative as well on the capital return announcements in Q1? I mean, the end goal is still 12.5%. You repeated that this could be done in equal steps, but if you are consistent with your cautious view on the environment in the short term, would that impact as well the phasing of the convergence towards 12.5%? And why would you not just instead of saying three steps, say we would like to pay €2.5-€3 billion excess capital split between buyback and some cash to avoid paying taxes on buyback would be a much clearer message and give confidence on your strategy on that front. Secondly, on M&A, I'll be slightly more explicit maybe in my question. There were some headlines that you should be bidding for an Indian bank. Could you deny that? Or is it something that you would consider in your earlier answer? You focused on Europe. Anything outside Europe would be, could be on the table? Thank you.

Steven van Rijswijk
Thank you, Tarik. Look, I think we have been quite clear and also consistent and also reliable on what we have said on our capital distribution and our ability to execute. And we stick to that guidance. So we have said we will move down in roughly equal to 2025. There is nothing in our guidance that would sway from that. As a matter of fact, we just increased our guidance on revenue quite significantly. We are in constructive dialogue with the ECB, and we've said that every time we take a step, we say we're in constructive dialogue. We also now said that we will let you know the outcome of that constructive dialogue by the first quarter of 2023.

And if I do the math, I know quite well that we need to pay out more than 100% of profit in the coming years to get to that level, given where we currently are. And I have not forgotten that. And that's what we will focus on. The same level maybe of preciseness on India. We have been saying a number of times that we focus to reiterate our leading universal banking position in Europe. Without being pedantic about it, the last time I looked India is not in Europe, and I'm actually a bit surprised that one article in an Indian newspaper on an Indian company in a country which we exited about six years ago, would then serve us again as something that we would focus on. So I will not go any further because otherwise I have to give comments on each of the 225 countries in the world, but I think that it is quite clear.

Tarik El Mejjad (Bank of America)
Okay. Thank you very much.

Operator
Thank you. It appears there is no further questions at this time. I'd like to turn the conference back to you, Mr. Steven, for any additional or closing remarks. Thank you.

Steven van Rijswijk
Great. Thank you very much. Great to talk to you again here. Well, not quite a start, but at least a month after the start of the new year. I hope you have started well, and I hope to talk to you again in the near future. Thank you very much and have a great day.

Operator
Thank you, everyone, for joining today's call. You may now disconnect.