

# Shareholder 03

Behind the figures

Quarterly Magazine ING Group

August 2008

Wholesale Banking  
shoots for the top

Customer focus in  
Poland

2Q: Solid business  
growth

The Asian Century



# Dear reader,

China is currently the centre of world attention with the recent staging of the Olympic Games in Beijing. As it has convincingly shown, Asian countries can match the world's best, particularly when it comes to sport and staging world class events. And it might not be too long before they do the same on the economic and business front. In a special feature on Asia, one leading academic argues that Asia will soon become a co-driver with the West in world political, economic and business matters.

The region is also seen as a beacon of economic hope as Europe and the US continue to be mired in the credit crunch crisis. Global financial services companies continue to be hard hit. While ING has not been immune from the global contagion, it has been relatively less affected due to prudent risk management and business diversification. As our feature on the second quarter results shows, ING's underlying business in terms of sales and value of new business remain robust, despite the market turbulence. Impairments remain limited. And despite the gloom surrounding global

banking, we look at two successful ING banking businesses. ING Bank Śląski in Poland is an excellent case study of ING's retail banking strategy at work. The bank has grown into Poland's third largest over a very short period of time. As we explain, the bank's formula for success has been a strong focus on execution, excellent customer service and attractive, simple, easy-to-understand products.

The second story in our banking theme features Wholesale Banking which accounts for about a fifth of ING's pre-tax profit. It plays a very important role as an asset originator for the group and after some restructuring several years ago, is now positioning itself to be the number one wholesale bank in the Benelux region. We explain how it plans to do this.

And finally, ING Gallery looks at a striking new sculpture in ING House, ING's headquarters in Amsterdam, which takes a very contemporary look at a very ancient theme.

*The editorial team*

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ING Bank Śląski has grown to be the third largest bank in Poland. Its rise towards the top has been largely built on a clear strategy that puts the customer first. Simplicity, transparency and good communication are all key elements.



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ING Wholesale Banking is on the move in a campaign designed to position it as the number one player in its core market of the Benelux.



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Brunon Bartkiewicz

# Customer focus yields solid growth

When the pioneers of ING's first banking foray into Poland set up business in 1989, they could little have imagined that their efforts then would lay the foundation for the country's third largest bank less than 20 years later.

**F**or the past two years, Poland has recorded its best economic performance since the late 1990s with growth exceeding 6%, according to the OECD. Equally impressive is the fact the country was the second-best performing economy among OECD countries during this period. It is this steady economic growth that is drawing foreign companies to the country. But back when the market opened up in the early nineties, ING's predecessor bank, NMB, one of the first Western banks to enter the country, faced significant uncertainties.

Today, Poland is one of ING's core markets in Central and Eastern Europe with high growth potential. ING Bank Śląski is a significant player in banking in the country with a rising share of the country's deposits and mortgages. Despite its success so far, ING Bank Śląski chief Brunon Bartkiewicz believes the best still lies ahead. "We have built a strong foundation for a fast growing bank. I strongly believe the real success is still in front of us."

## Restructuring for growth

Like most businesses expanding, it can often be a bumpy ride. ING Bank Śląski's current success was borne out of major restructuring four years ago, when the company faced major economic headwinds in 2003. In 2004, ING Bank Śląski introduced a new performance-oriented organisation structure. A programme rationalising the product portfolio and launching new products and marketing campaigns was started to re-establish its market presence and market position. Its ambition was to grow significantly, especially in the field of deposits, savings and mutual funds. On the asset side, in loans and mortgages, the bank aimed for selective growth.

"In the last four years, we have changed almost every piece of the bank: products, processes, attitudes of people, governance,

the way we organise ourselves, even the way staff talk to one another. We showed we could make changes in a very short period of time. Our aim was to be the bank of choice. If people were thinking about what to do with their money, we wanted them to be thinking about ING Bank Śląski," says Bartkiewicz.

## Customer acquisition via savings account

The bank built its strategy around the simple concept of acquiring customers through an attractive savings account and electronic banking. The Open Savings Account was changed in 2004 to be easily understood in terms of pricing, conditions and transparency and came with a relatively high interest rate. In 2008, the bank is recording major success with the strategy. In the four years since it began, the number of retail clients have grown 36% to 2.34 million at the end of the first quarter 2008 and retail funds entrusted have risen by 111% to EUR 10.85 billion. At mid 2008, ING Bank Śląski's network consisted of 430 branches, 250 of which have or are solely self service zones. Over this period, the bank had considerably strengthened its position in retail deposits, achieving 9.42% market share compared to 6.12% in 2004.

Bartkiewicz believes the bank's growth strategy has worked because it had been very clear in communicating it to both staff and customers. "We made it very clear we were going after an increasing number of customers through savings: savings first. We were able to offer a very attractive savings product to the market that showed the values that we wanted to stand for. No small print at the bottom of documents and no hidden charges or fees. We want the bank to be known for its openness and transparency. It was by far the best product for us to create the customer relationships and enabling us to deep-sell and cross-sell other products to customers."

In 2005, the bank's customer acquisition efforts were further strengthened with a major campaign to attract customers to internet banking and credit cards. The campaign was prompted by growing interest at the time in home-based banking. Only 9% of customers banked online then. Now the figure is close to 40%.

ING Bank Śląski also focused on expanding and modernising its branch distribution network. In 2007, Self'Bank franchise outlets were opened, which are self-service units where customers can carry out all their day-to-day banking. The model with its roots in the Self'Bank of ING Belgium and successfully introduced in Romania is based on teller-less branches, independent franchises and simple products on sale.

### Fierce competition

Competition in the Polish banking sector is fierce with more and more entrants attracted to the market by Poland's size, stability and growing economy. It means there is immense pressure to stay one step in front of the competition. Bartkiewicz believes the bank can do this by providing excellent service, the best in the market, and offering multi distribution channel banking services.

Bartkiewicz's ambition is to have in all ING Bank Śląski branches, terminals for access to the internet, telephones to contact call centres, financial advisers who can help people with more sophisticated investment products, ATMs and cash deposit machines.

Fast, good quality service is the name of the game. To reduce queues and waiting time, the bank has introduced so-called cash-in machines in many branches, especially for small-to-medium business who need to deposit cash. "There is a very high usage of cash in Poland. We are trying to attract small businesses and these people need the cash-in machines."

Bartkiewicz also believes being the best in internet banking gives the bank a very powerful competitive advantage in Poland. ING Bank Śląski customers are now able to secure a loan online without setting foot inside a branch. In January, the bank launched an internet-based Direct Account, a current account with internet, ATM, cash deposit machine and payment cards access which people can open completely online. "By introducing this new account, we want to be the most internet-oriented bank in Poland. ING is not only a large bank providing a full range of services, but it is also innovative and could well match that being offered by the pure e-banks," Bartkiewicz says.

ING Bank Śląski's customer centric approach has caught the eye of the media with Forbes magazine in Poland, the Polish version of *Newsweek* magazine and daily newspaper *Gazeta Wyborcza* all bestowing awards on the bank for service and promotion. "These awards are of course an honour, but they also mark a commitment. Clients now demand top quality standards."

### ING Group in Poland

ING Group has a very strong presence across many business lines in Poland. Apart from banking, ING is active in retirement services, insurance and investments. In retirement services, ING Pensions has 2.6 million clients and is ranked as the second largest player in the Pillar 2 (compulsory employer retirement savings funds) market with more than 20% market

share. ING Insurance is ranked the fifth largest in the life insurance market. In investments, ING Investment Management is the fourth largest fund management company in terms of assets under management. ING is also active in real estate through ING Real Estate Development and ING Real Estate Investment Management, which are market leaders in Poland.

### Future plans

ING Bank Śląski intends to continue attracting customers on the basis of its attractive savings account and electronic banking and also through self banking. "We aim to increase the number of savings accounts by 250,000 a year. At this growth rate, the deep selling process is more effective."

Bartkiewicz believes the bank has a key growth opportunity by cross and deep selling personal equity products such as mutual funds and structured products. This is because it has the backing of a global player with an extensive presence in financial services. "ING is very active in Poland across many fronts. We are the second largest player in pensions, the third largest asset manager, ING owns the largest stock exchange brokerage and we have a leasing company that is one of the largest in the country. When you look at it, we are pretty unique, we offer it all, often through the same channels. We have already achieved a scale that makes us an important player in each product category." He believes the ING brand plays an important role as brand recognition and financial strength are very important in the Polish market. "For the customers we concentrate on, the mass affluent and high net worth individuals, this trust in the brand is an enormously powerful tool. "ING Bank Śląski is the second most recognisable brand among the Polish banks."

While the bank is well known for its retail activities, wholesale banking is an important business for ING Bank Śląski. Almost 40% of the bank's profit is derived from its wholesale banking activities. According to Bartkiewicz, it also comes with many other benefits. It provides a steady source of leads for the retail side of the business, particularly in the mid-sized corporates and family business sectors. "We have a top five position in the wholesale banking market in Poland and plan to build strongly on this result." Bartkiewicz's formula for success in Poland is clear. "We have to be good on every front, provide a consistent message to the market and deliver a high quality service." ■

Eli Leenaars (right) with the first president of independent Ukraine, Leonid Kravchuk, at the opening of the first ING Bank branch in Kiev



## Up and running in Ukraine

With the formal opening of its first branch in Kiev in June, ING launched its retail banking operations in Ukraine – one of the fastest-growing economies in the region. By introducing the innovative self banking concept, customers will get convenience, transparency and fast service.

The rollout of the retail banking network in Ukraine is an example of ING's focus on growth. Eli Leenaars, member of the Executive Board of ING Group and responsible for retail banking said: "We have keenly followed the developments in Ukraine. Our decision to establish a retail banking operation reflects our confidence in the continued growth and development of the Ukrainian economy."

Ukraine is the largest country in Central and Eastern Europe. It is also the most populated country with more than 46 million inhabitants, a rapidly growing middle class and an estimated real GDP growth in 2008 of 6.2% (2007: 7.5%). The Ukraine greenfield operation capitalises on the successful self banking model that has previously been introduced in Romania, where more than a half million customers were gained since launching in 2004. Ukrainian customers will be offered a current card account that yields an 8% interest rate, combining the return of a savings account with a current account. The selfbank model is based on low-cost and teller-less offices, independent franchisees and straight through processing, allowing all transactions to be processed online.

"We're really setting a new standard," says Jef Van In, general manager of Retail Banking for ING Bank Ukraine. "This innovative concept combines internet banking with highly automated

offices with cash functions and access to personal advice. In the future, we plan to extend our product offering with mortgages, instalment loans, fixed-term deposits and credit card products. Our independent partners, who will manage the branches, are very committed to offer a high level of services to our customers." ING aims to become a top-5 retail bank in Ukraine within the next few years and has plans for quick expansion by rapidly growing to 250 branches in the largest Ukrainian cities (Kharkiv, Dnipropetrovsk, Odessa, Donetsk and Lviv), hiring more than 500 people.

"Our plans in Ukraine," Leenaars adds, "are in line with our retail strategy for growth in countries with significant potential, such as Poland, Romania and Turkey (acquisition of Oyak Bank)." The retail banking activities will further support the growth potential of the existing operations of ING in Ukraine. ING was one of the first western banks to start activities there in 1994, when it set up a wholesale banking office in Kiev. In January 2008, ING Lease commenced operations in the country. And in July, ING received a licence to begin life insurance operations and expects to launch these activities in the first half of 2009.

"We are confident that by building on the Romanian self banking concept, we will be able to rapidly build a successful retail bank in the emerging market of Ukraine," says Leenaars. ■

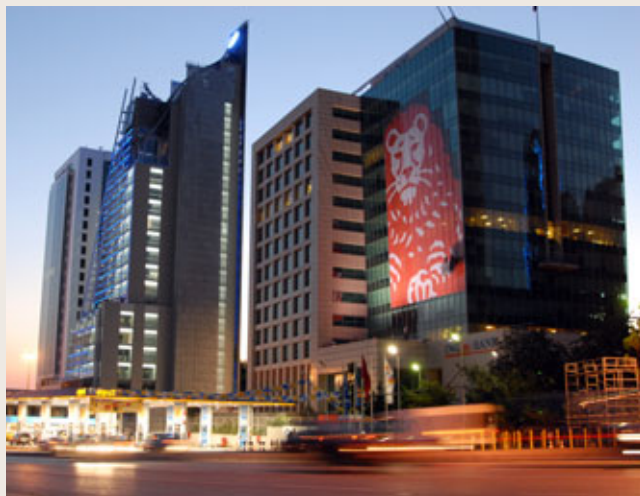


## Entering the Turkish pensions market

ING has reached agreement with Oyak Group in Turkey to acquire the voluntary pension fund, Oyak Emeklilik. The agreement follows the purchase of Oyak Bank last year, which was rebranded ING Bank Turkey in July.

Jacques de Vacleroy, member of the Executive Board of ING Group, said the transaction gave ING an excellent opportunity to tap into the fast growing Turkish pension market. "The acquisition is in line with ING's sharpened strategic focus on banking, investments, life insurance and retirement services." Under the terms of the agreement, ING will acquire Oyak Emeklilik for EUR 110 million which will be financed entirely from existing internal resources.

Tom Kliphuis, CEO of Insurance Central Europe said: "Oyak Emeklilik has strong management and its distribution is already well integrated in ING Bank Turkey. By combining our life insurance and pension expertise with Oyak Emeklilik's strong distribution and knowledge of the market, we will rapidly build a leading position in the Turkish retirement savings marketplace." Established in 2003, Oyak Emeklilik is the first and only voluntary private pension fund in Turkey. Oyak Emeklilik has more than 150,000 customers and 140 employees and distributes its products both through a network of independent agents and ING Bank Turkey.



ING Bank Turkey's head office in Istanbul, formerly Oyak Bank

## ING Direct and Interhyp: an attractive match

ING Direct has acquired a controlling stake in Interhyp, Germany's largest independent distributor of residential mortgages, valuing at EUR 416 million. It has a volume of mortgages distributed of EUR 5.7 billion, equalling a 3.1% market share. Since its foundation in 1999, Interhyp has offered residential mortgages from over 70 banks, building societies and insurance companies, mostly via the direct channel. As such it combines the benefits of the internet with the expertise of over 250 mortgage consultants.

"This acquisition," says Dick Harryvan, ING Group Executive Board member and CEO of ING Direct, "is in line with ING Direct's strategy to strengthen and expand our range of simple products in savings, mortgages, payment accounts and investment services. We believe that Interhyp's business model and sophisticated technology platform offer great potential for enhancing our distribution platforms in Europe. The acquisition of Interhyp will further strengthen our present position in the German

mortgage market and its commission income will help to diversify the profitability of the mortgage business. It's a next big step in achieving our vision to become the world's most preferred consumer bank."

Munich-based Interhyp will remain fully independent, keeping its identity, brand and management. It is a close and strong partner of ING-DiBa.



## ING appoints new head of Investor Relations

ING has appointed Dorothy Hillenius as the head of ING Group Investor Relations. Ms Hillenius replaces Jonathan Attack who was appointed chief financial and risk officer at ING Investment Management Europe. Ms Hillenius, a Canadian national, first joined ING in 1997 as a communications officer at ING Barings. She left the company in 1999 to pursue a role as a financial journalist with Bloomberg News, where she covered the Dutch financial services sector. She returned to ING in 2003 as a media spokesperson, handling

financial communications to the press. In 2007, she joined the Investor Relations team as senior manager. Speaking on Mr Attack's four years as the previous head of Investor Relations, Michel Tilmant, chairman of ING Group said: "Under Jonathan Attack's guidance, ING has made significant progress in upgrading the quality of our investor relations function. His many accomplishments include improving ING's financial disclosure and building a stronger relationship with analysts, investors and rating agencies."



Dorothy Hillenius

## Citistreet acquisition boosts US operations



ING has strengthened its leading position in a key segment of the US retirement services market, after closure of the CitiStreet LLC acquisition recently. ING is now the third-largest defined contribution business in the US based on approximately EUR 191 billion of combined assets under management (AUM) and assets under administration (AUA).

Based on the number of plan participants, ING is now the largest defined contribution business in the country.

ING acquired Citistreet for EUR 578 million, which was entirely financed from existing internal resources. Citistreet is one of the premier retirement plan, benefit service and

administration organisations in the US defined contribution marketplace. Defined contribution plans are retirement savings plans where the retirement benefit is largely based on the amount contributed to the account by the so-called plan participant.

Tom McNerney, ING Executive Board member and CEO for Insurance Americas said: "This acquisition significantly expands our existing footprint in retirement services in the US and will help drive long-term growth in the US retirement services marketplace."

The acquisition is in line with ING's focused strategy of supporting strong organic growth by making suitable add-on acquisitions which are aligned with its core banking, investments, life insurance and retirement services growth businesses.

Together, ING's total US retirement services and annuities business and Citistreet have more than EUR 259 billion in combined AUM and AUA and more than 16 million participants.



Eric Boyer (left) and  
Ralph Hamers

# Wholesale Banking aims for the top in the Benelux

ING Wholesale Banking has certainly chosen a good time to meet its ambition of becoming the number one Wholesale Bank in the Netherlands and Belgium.

Born out of a series of large mergers in the Netherlands and the acquisition of Banque Bruxelles Lambert, ING has long been the number two Wholesale Bank in its important home markets behind ABN AMRO in the Netherlands and Fortis in Belgium. ABN AMRO was acquired in late 2007 by a consortium of three banks including Fortis, which is now focused on splitting up the Dutch bank and making sure the integration goes smoothly. This has given ING a unique opportunity to gain market share, bring in new clients and recruit talented employees. "It's an historical opportunity. How often do you see such a dramatic change in your competitive landscape in your life?" asked Eric Boyer, the ING Executive Board member responsible for Wholesale Banking since 2004. "The institution understood that something important was happening and that we needed to react." A few months into its new strategy, Wholesale Banking can already point to early results in the Dutch market, including new clients, large deals and 40 new senior bankers. But as high-profile as the changes have already been in the Netherlands, Wholesale Banking is busy seeking out other leadership positions across the globe.

## Moving Forward

After years of improved capital efficiency, solid profit growth and expense reduction, Wholesale Banking is now embarking on its 'Fitter, Focused, Further' strategy for 2008-2010 with the aim of becoming a leader in a number of key markets and products. "In this business you can't be everything for everyone," said Boyer. "After first putting the house in order we are now focus-

ing on those areas where we can distinguish ourselves from the competition." By creating sustainable leadership positions in key areas, Wholesale Banking believes it will achieve returns beyond the sizeable amount of capital, knowledge and profit it already contributes to the Group. The business is now 'Fitter' after having transformed itself into a key profit centre within the Group. Over the last four years, Wholesale Banking's pretax profit has grown at an average annual rate of 11% – making up about 20% of the Group's profit – while reducing economic capital by around EUR 2.7 billion.

Wholesale Banking has done quite well in what has been a challenging business environment with financial markets experiencing significant turbulence. "There has been a big turnaround and the bottom line has grown very nicely thanks to efficiency levels," said Boyer. "Now the focus is on getting growth to a higher level."

The 'Focused' component of the strategy includes becoming the market leader in the Benelux, a top-5 Wholesale Bank in Central and Eastern Europe, as well as a global leader in a number of key product areas, including Real Estate (in which it is already number one) and Structured Finance, and a regional leader in Financial Markets, Payments and Cash Management (PCM) and Lease. 'Further' is all about accelerating growth while improving efficiency and investing capital into where it gets the best returns across the regions and product areas. Ultimately, Wholesale Banking aims to double economic profit by 2010.



### Wholesale Banking within Group

Wholesale Banking plays a fundamentally important role within ING Group. The essence of ING's business is to collect consumer deposits and redeploy them as investments in the economy. Wholesale Banking complements this in three ways: as a generator of profits, an important originator

of assets and as a source of skills and expertise. With many businesses and product offerings that are world-class, Wholesale Banking generates capital that can be redeployed efficiently by the Group to high-growth businesses or returned to shareholders. In 2007, Wholesale Banking earned the most underlying profit before tax of all six business lines, about 25%

of the Group's profit, making it a major contributor of profits to the Group.

Wholesale Banking also generates high-quality assets where ING can invest retail deposits. The current economic crisis has reinforced Wholesale Banking's role as a gatherer of attractive risk/reward high-yield assets. Developments in recent months

have again strengthened ING's belief that it is essential to be able to generate a good portion of its own assets in order to maintain a healthy company profile. Also, Wholesale Banking provides the Group with many relevant skills in financial markets, derivatives, risk and specialist finance, as well as access to financial markets around the world.



Ralph Hamers, member of the Wholesale Banking management team and responsible for coordination of the Wholesale Banking strategy by businesses spread out across 40 countries, says the new strategy allows the businesses to focus on the areas in which they excel.

"We chose areas where we already had a competitive advantage and where we think we can move faster," said Hamers. "We have skills on a world-class level in certain areas in which we can grow even further." Wholesale Banking decided it only wanted to be involved in activities on a global scale if it could be in the top-10, on a regional scale if it can be top-5, and in a local market if it can be in the top-3. "We had to set ambitious levels because in the end it's a scale business," said Hamers. "You strive to be among the best because otherwise you're not going to be competitive in the long-run."

### The Netherlands

Aiming to become number one in the Dutch market, Wholesale Banking launched several campaigns across the Netherlands to boost recruiting and visibility. A recruitment campaign was launched at the beginning of the year to hire new top talent and support ING's growth ambitions. An advertising campaign aimed at Dutch corporates was also launched to reiterate ING's position as a leading bank in the corporate market. The pictures of some of ING's most senior bankers were visible across billboards in a push to strengthen their visibility among the largest companies in the Netherlands. The 'right hand of Dutch corporates' cam-

paign aimed to help position Wholesale Banking as the financial partner of choice. "The very visible campaign was not very typical of Wholesale," said Hamers. "But it was very visible and everyone was talking about it. If the larger corporates now think about acquisitions, financing, advisories or PCM mandates, we are on top of their list."

It is still too early to judge the total success of the campaigns but early results include hiring 40 senior bankers and recruiting more than 20 new clients, including Hoogwegt Groep and Smit International. Wholesale Banking was promoted to 'lead bank' from 'core bank' by more than 20 clients, including Akzo Nobel and Randstad/Vedior. And it also included prominent media coverage for Wholesale Banking's new strategy.

In the last few months Wholesale Banking won some major business: a bond deal for Wolters Kluwer (EUR 645 mln) and financing for Unit 4 Agresso (EUR 230 mln). "The penetration and the recognition in the Wholesale market are now there and we also added a lot of quality to our team that will ultimately help us reach the goal of becoming number one," said Hamers. "I see the same potential for success in the Belgian market."

### Central and Eastern Europe

Another important market is Central and Eastern Europe, which Wholesale Banking entered in the early 1990s and now counts among its home markets. Wholesale Banking is currently the number four bank in the regional powerhouse Poland and



number seven in Romania. The aim is to be a top-5 leading full-service bank in the region on average. There are also plans to expand in Ukraine and Russia in the future.

As ING Retail Banking is also bolstering its presence in the region, there are good opportunities to work together and for Wholesale Banking to share its skills and expertise across the Group. As Retail Banking attracts savings from customers, Wholesale Banking plays a key role in generating high-quality assets where the deposits from retail clients can earn attractive returns. "The next piece of geographic expansion is one of growing further in Central and Eastern Europe where we already have a strong base but can grow even faster through the tie-up to Retail," said Hamers. "Our businesses go hand in hand. Our growth strategy in Central and Eastern Europe is very much aligned to the Retail strategy."

### Key Products

Beyond the geographical focus, there are a number of key products where Wholesale Banking counts itself among the global leaders and aims to build on these franchises. ING Real Estate, which falls under Wholesale Banking, is already the world's largest real estate investment company with a portfolio worth more than EUR 100 billion. ING wants to consolidate this position globally. Another important line of business

is Structured Finance, which helps companies finance large capital projects and transfer risk through various products. Key segments of expertise are Natural Resources, Telecom, Media, Finance and Utilities. Wholesale Banking is among the top-20 globally and seeks to be in the top-10. In Financial Markets ING seeks to be a top-3 player in the Benelux (from number four) and a top-5 in selected Emerging Markets (from number eight-ten).

PCM is a truly international business since the launch earlier this year of the Single Euro Payments Area (SEPA) where the distinction between national and intra-European cross-border payments has been removed. "Given our strong position already in PCM we want to take advantage of SEPA and become a consolidator," said Hamers. ING aims to be among the top-5 in Europe (from number six-seven.) ING Lease (currently number seven in Europe) seeks to build on its market leader position in the Netherlands through expansion in Italy, the UK and Central and Eastern Europe to become a top-5 player.

"It's all a matter of choosing your battlefields. This business is really competitive and you just can't fight on all fronts," said Boyer. "So you need to choose given your position and natural expertise in those areas that you can capitalise on." ■



### Wholesale Banking Explained

ING Wholesale Banking conducts global wholesale banking operations for corporations - from large corporates to major multinationals - as well as governments and financial institutions. Wholesale Banking also provides some product services for midcorporates, a client segment managed by ING

Retail Banking. Wholesale Banking's primary focus is on the Netherlands, Belgium, Poland and Romania where it offers a full range of products to companies and other financial institutions. Wholesale Banking has six business lines: General Lending & Payments and Cash Management, Structured Finance, Leasing & Factoring, Financial Markets, ING Real Estate and Other Wholesale Products.

Elsewhere it takes a more selective approach with regard to clients and products. Wholesale Banking also includes ING Real Estate, the world's largest real estate investment manager based on the value of its assets under management. In all, Wholesale Banking has about 18,000 employees in 40 countries. Wholesale Banking, after having successfully sharpened its strategic focus and improved

capital efficiency and returns, now has new initiatives for growth geared towards the Benelux and Central and Eastern Europe, and global franchises in Structured Finance and Real Estate.

# Results 2Q, 2008

## ING posts EUR 1.9 billion underlying net profit

On Wednesday 13 August, ING announced its second quarter 2008 results. ING recorded an underlying net profit of EUR 1,946 million, down 28.8% on the previous second quarter as a result of lower investment income. Michel Tilmant, chairman of ING said: "ING continues to weather the turmoil in credit markets well, as writedowns on pressurised assets remained limited in the second quarter. We are, of course, not immune to the challenging environment around us, and the sustained weakness across financial markets put pressure on earnings," he said. "We took advantage of the brief market rally in April to reduce our equity exposure. Nonetheless, equity gains net of impairments were significantly below the exceptional levels realised last year. Combined with lower real estate and private equity valuations, lower investment results accounted for the vast majority of the profit decline. Interest income in the banking business rose strongly, despite competition for deposits. Risk costs increased, but remained below over-the-cycle norms. Costs remained under control in mature markets, while we continued to invest to support growth.

"ING maintained its commercial growth in these challenging market circumstances. The net new production of client balances was EUR 29.6 billion in the quarter, bringing the total to EUR 1,482 billion. Growth was driven by a large increase in lending, particularly in Wholesale Banking. In Retail Banking and ING Direct we continued to grow savings despite strong competition for deposits. Sales of life insurance were up 8.8% excluding currency impacts as product innovation and expanded distribution helped compensate for lower demand for unit-linked products.

"All capital and leverage ratios are well within target. The Group has EUR 3.9 billion of spare leverage capacity after the completion of ING's EUR 5 billion share buyback and the payment of last year's final dividend in the second quarter. In line with our policy to pay an interim dividend equal to half of the previous year's total

### Key figures ING Group

In EUR million	Quarterly results		
	2Q2008	2Q2007	Change
<b>Underlying profit before tax<sup>1</sup></b>			
Insurance Europe	397	679	-41.5%
Insurance Americas	374	593	-36.9%
Insurance Asia/Pacific	124	153	-19.0%
Corporate line Insurance	250	531	
<b>Underlying profit before tax from Insurance</b>	<b>1,145</b>	<b>1,956</b>	<b>-41.5%</b>
Wholesale Banking	365	604	-39.6%
Retail Banking	558	619	-9.9%
ING Direct	179	171	4.7%
Corporate line Banking	-2	-65	
<b>Underlying profit before tax from Banking</b>	<b>1,101</b>	<b>1,329</b>	<b>-17.2%</b>
<b>Underlying profit before tax</b>	<b>2,246</b>	<b>3,285</b>	<b>-31.6%</b>
Taxation	324	472	-31.4%
Profit before minority interests	1,922	2,813	-31.7%
Minority interests	-23	77	
<b>Underlying net profit</b>	<b>1,946</b>	<b>2,735</b>	<b>-28.8%</b>
Net gains/losses on divestments	2		
Net profit from divested units		12	
Special items after tax	-28	-188	
<b>Net profit (attributable to shareholders)</b>	<b>1,920</b>	<b>2,559</b>	<b>-25.0%</b>
<b>Earnings per share (in EUR)</b>	<b>0.94</b>	<b>1.18</b>	<b>-20.3%</b>
Net return on equity <sup>2</sup>	19.0%	23.9%	
Assets under management (end of period)	614,100	636,700	-3.5%
Total staff (FTEs end of period)	130,988	119,097	10.0%

1 Underlying profit before tax and underlying net profit are non-GAAP measures for profit excluding divestments and special items  
2 Year to date

dividend, our interim dividend has been set at EUR 0.74 per share, to be paid fully in cash.

"Financial services companies are facing unprecedented market volatility, limited liquidity, and intensified competition for deposits, which we see continuing into 2009. We are executing our strategy in the context of this challenging environment by focussing on growing client balances, while keeping a close eye on margins and expenses. We continue to adapt our product range to meet our customers' changing needs, while investing to expand

our distribution in growth markets. In mature markets we are on track with the transformation projects at our Retail Banking businesses in the Benelux, and expense reductions at the Dutch insurance business are now evident. As markets remain volatile, we will continue to manage our risk and capital with discipline. While financial markets are expected to put pressure on results in the short term, we are confident that ING will continue to create profitable growth for our shareholders over the long term through the breadth of our business and the strength of our franchise."

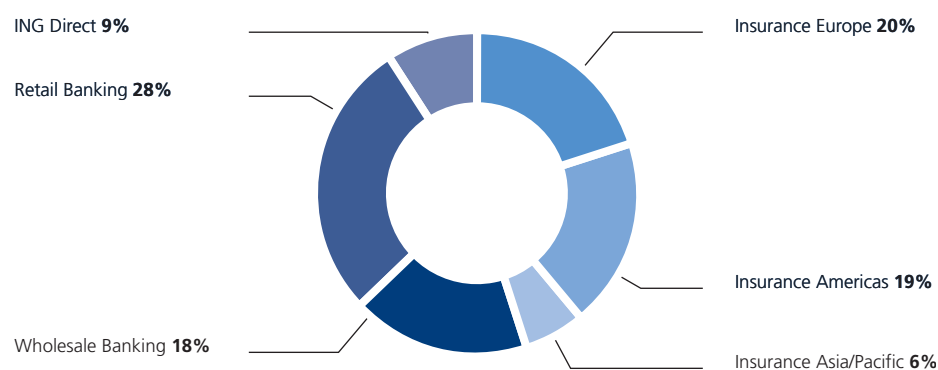
## Earnings analysis: Second quarter

ING continued to show solid commercial growth, while the sustained market turmoil impacted investment income. The direct impact from the credit and liquidity crisis remained limited in the quarter. Losses on ING's investments in pressurised asset classes were limited to EUR 44 million after tax (EUR 60 million before tax), reflecting the high structural credit protection of the securities in ING's subprime and Alt-A RMBS portfolios. The ongoing weakness of financial markets continued to put pressure on investment returns from real estate and equities.

ING realised EUR 727 million after tax in capital gains on equities in the second quarter, mainly at the insurance business, as we took advantage of the brief market rally in April to reduce our equity exposure. However, that was partially offset by EUR 291 million of impairments on equities as markets sustained their declines. On balance, gains net of impairments were EUR 436 million after tax, down from EUR 849 million in the second quarter last year, which included a gain of EUR 573 million on part of ING's stake in ABN Amro. Negative revaluations on real estate amounted to EUR 180 million after tax (EUR 285 million before tax) in the quarter. That was related mainly to Canada, where a full external appraisal of the Summit portfolio was completed in the second quarter. The year-earlier quarter included positive revaluations of EUR 117 million after tax.

Returns on private equity and alternative assets declined by EUR 128 million (EUR 138 million before tax) compared with a year earlier. Currency fluctuations had a negative impact of EUR 67 million, which were offset by a positive result on FX hedges of EUR 139 million. Combined, the impact of the market deterioration reduced results by EUR 754 million after tax (EUR 977 million before tax) compared with the second quarter last year. That drove the 28.8% decline in underlying net profit.

## Underlying profit before tax by business lines 2Q\*



\* excluding corporate line

Commercial growth remained solid, generating EUR 29.6 billion in total net production of client balances in the second quarter, bringing total client balances to EUR 1,482 billion. Bank lending grew by EUR 22.3 billion excluding currency impacts, driven by corporate lending and mortgages, as ING leveraged its strong balance sheet and solid liquidity position. Customer deposits of the banking business increased by EUR 7.0 billion excluding currency effects despite increased competition for savings as the ongoing liquidity crisis pushed up funding costs on wholesale markets. Life insurance generated a net production of EUR 3.1 billion. Sales of life insurance were up 8.8% and the value of new business rose 39.8% excluding currency effects to EUR 267 million.

Operating expenses were under control with expenses increasing in mature businesses only 0.9% from a year ago, while expenses at the growth businesses increased 14.4% to support expansion. The effective tax rate of 14.4% in the second quarter was in line with the rate in the same quarter last year, supported by tax-exempt gains on equities as well as some tax releases. For the full year, the effective tax rate for the Group is expected to be around 20%.

Net profit declined 25.0% to EUR 1,920 million. This includes EUR 2 million in currency results related to the sale of NRG and EUR 28 million restructuring costs for the Dutch retail bank. Net earnings per share were down 20.3% to EUR 0.94. Part of the decline in net profit was offset by the impact of the EUR 5 billion share buyback completed in May. The total number of shares outstanding declined by 8.9% from a year earlier to 2,026 million.

## Insurance

Total underlying profit before tax from insurance declined 41.5%, reflecting the impact of volatile equity, real estate and private equity markets.

The challenging investment and credit market environment put increasing pressure on profit as well as sales of investment-linked products in the second quarter.

Strong inflows at US Wealth Management and the pension funds in Central & Rest of Europe continued to drive growth. However, consumer appetite for investment-linked products was dampened in some markets due to faltering equity markets. In response to the challenging market environment, ING is focused on

leveraging its product expertise to adapt its product offering to meet customer demands for guarantees and capital protection.

Profit from Insurance Europe declined 41.5%, mainly driven by a 49.8% decline in the Netherlands due to lower investment income from private equity and real estate as well as the EUR 5.0 billion upstream of surplus capital from the Dutch business last year. Profit from Central & Rest of Europe declined 3.3% due to higher greenfield investments, mainly to support second and third-pillar pension funds in Romania.

Insurance Americas' profit before tax fell 36.9%, or 28.8% excluding currency effects, due to a EUR 107 million increase in interest- and credit-related losses (net of hedging and DAC) as well

as EUR 22 million lower investment income from alternative assets in the US. Profit in Canada fell 10.7% excluding currencies on higher claims associated with an active storm season, as well as lower investment results.

In Asia/Pacific, underlying profit before tax declined 19.0% but was flat at constant currency rates. Higher results in Japan were largely offset by Australia/New Zealand where market declines reduced asset values and fee income. In Korea, profits were affected by lower investment income and unfavourable claims experience.

The Corporate Line Insurance recorded a profit before tax of EUR 250 million, supported by EUR 473 million in realised capital gains net of impairments as well as EUR 99 million positive fair value changes on derivatives. The result declined from a year earlier due to lower capital gains on equities as well as higher interest on hybrids and core debt.

Total gross premium income from Insurance increased 6.7% excluding currency effects, reflecting strong sales in the US and Central Europe.

Operating expenses were up 4.2% excluding currency effects, reflecting business growth, investments in greenfields and acquisitions in growth markets. Expenses in the Dutch insurance businesses declined by 4.1%.

New life sales (APE) increased 8.8% excluding currency impacts, reflecting ING's increased distribution capacity and product expertise. The increase came from Europe and Americas, while Asia/Pacific was down 10.9%, mainly due to lower sales of investment-linked products. The value of new business increased 39.8% excluding currency impacts to EUR 267 million with notable increases in the US, Latin America and Central & Rest of Europe. Changes in the policy for expense allocation and group life contract renewals had a positive impact of EUR 31 million. Margins improved, with the internal rate of return up at 15.2% from 12.8%.

## Banking

Underlying profit before tax declined 17.2% to EUR 1,101 million mainly due to negative revaluations of real estate and an increase in risk costs. The interest margin improved to 1.05%, supported by the reduction of short-term interest rates in the US and Canada, which benefited ING Direct.

Underlying profit before tax from Wholesale Banking declined 39.6%, mainly due to negative revaluations of real estate and higher risk costs. This was partly offset by a record quarterly profit, for the second time in a row, from Financial Markets.

Underlying profit before tax from Retail Banking was down 9.9%, reflecting lower fees on assets under management and increased competition for savings, particularly in the Benelux. Income increased 4.4% supported by the inclusion of ING Bank Turkey and strong volume growth in Poland.

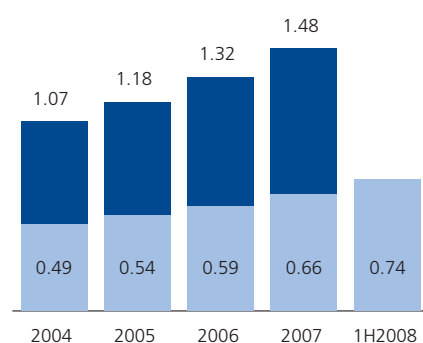
Profit before tax from ING Direct rose 4.7% from a year earlier and 15.5% from the first quarter, driven by the improved interest rate environment in the US and Canada. Losses in the UK narrowed to EUR 21 million.

Total underlying income from Banking rose 2.5% to EUR 3,765 million, driven by volume growth and an improved interest result. The interest margin increased 10 basis points compared with the same quarter last year, mainly due to a higher margin at ING Direct and the inclusion of ING Bank Turkey. Commission income rose 1.6% as lower fees from the securities business and asset management were more than offset by higher fees from brokerage & advisory and funds transfer fees.

Investment income declined from a positive EUR 265 million in the second quarter of 2007 to a negative EUR 185 million in the second quarter of 2008, reflecting lower realised results on bonds and equities as well as negative fair value changes on real estate.

## Recent dividends

Dividend per share (in EUR)



## Dividend

ING will pay an interim dividend of EUR 0.74 per (depository receipt for an) ordinary share, in line with ING's policy to set the interim dividend at half the total dividend of the previous year. ING's shares will be quoted ex-dividend as of 14 August 2008 and the dividend will be made payable on 21 August in Europe and 28 August in the US.



Underlying operating expenses increased 4.8%, reflecting the inclusion of ING Bank Turkey and investments to support the growth of the business at ING Direct, ING Real Estate and the retail banking activities in developing markets. The turmoil in the credit markets and further growth in lending led to an increase of net risk costs. ING Bank added EUR 234 million to the loan loss provisions, up from EUR 25 million a year earlier and EUR 98 million in the first quarter of 2008. Net additions amounted to an annualised 36 basis points of average credit-risk-weighted-assets, trending towards the normalised level of 40-45 basis points.

The underlying risk-adjusted return on capital (RAROC) after tax decreased to 15.7% from 26.2% a year earlier, reflecting lower real estate revaluations, higher tax charges and a strong increase in economic capital. Average economic capital rose due to the acquisition of Oyak Bank, the increased value of ING's stake in the Bank of Beijing and business growth as well as methodology refinements.

### Assets under Management

Despite the ongoing uncertainty in financial markets, ING achieved a net inflow of EUR 3.6 billion in assets under management in the second quarter. However, total AUM declined by EUR 6.7 billion as lower asset prices had a negative impact of EUR 6.0 billion and exchange rates reduced the total by EUR 2.5 billion. Acquisitions and divestments had a net negative impact of EUR 1.7 billion.

### Capital Management

All of ING's capital and leverage ratios remain well within target. Adjusted equity increased in the second quarter due to the issue of hybrid capital, profit generated in the quarter and a slight improvement in market conditions since March. That more than offset the payment of the final dividend to shareholders and the completion of the EUR 5 billion share buyback. ING's spare leverage capacity declined from EUR 6.2 billion at the end of the first quarter to EUR 3.9

## Risk Management

- The direct P&L impact from the ongoing credit and liquidity crisis remained limited with a pretax loss of EUR 60 million (EUR 44 million after tax). Negative revaluations of EUR 398 million before tax (EUR 260 million after tax) in the second quarter were reflected in shareholders' equity.
  - An impairment of EUR 7 million was booked on the US subprime RMBS portfolio at Insurance Americas. At the end of the second quarter, the subprime RMBS portfolio was valued at EUR 2.2 billion, or 79.7% of amortised cost value, down from 81.4% at the end of March. The decline resulted in a pretax revaluation of EUR -32 million in the quarter, bringing the total revaluation to EUR -560 million, which is reflected on an after-tax basis in shareholders' equity.
  - There were no impairments in ING Direct's Alt-A RMBS portfolio. The market value was reduced from EUR 22.8 billion at 31 March 2008 to EUR 22.0 billion at the end of the second quarter. Of the EUR 0.8 billion decline, EUR 341 million is due to negative revaluations and the remainder was due to redemptions and prepayments. The negative revaluation is mainly driven by higher interest rates. As of 30 June 2008, EUR 183 million of ING's Alt-A RMBS had been downgraded. A further EUR 1.4 billion was downgraded
- by rating agencies as of August 8. The total credit watch list increased to EUR 4.6 billion.
- ING's net exposure to CDO/CLO increased from EUR 2.1 billion at 31 March 2008 to EUR 4.3 billion at the end of the second quarter. Wholesale Banking increased its exposure by EUR 0.9 billion. Insurance Americas wrote credit protection on EUR 1.5 billion of super-senior tranches of investment grade corporate credit indices and custom corporate credit portfolios.
  - ING's CDO/CLO portfolio was valued at 94.6% at 30 June 2008. ING took a EUR 12 million loss on its CDO/CLO exposure in the second quarter, of which a EUR 4 million fair value loss was in Insurance Asia/Pacific, EUR 2 million in Insurance Americas, and EUR 6 million impairments at Wholesale Banking.
  - ING's direct exposure to monoline insurers is negligible. ING has some indirect exposure as it insured EUR 2.9 billion of assets with monoline insurers, either through financial guarantees (wraps) or credit derivatives. Exposure to monoline insurers resulted in a loss of EUR 5 million before tax in the second quarter as Wholesale Banking wrote off the value of credit derivatives bought from a downgraded monoline insurer.

billion at the end of the second quarter due to the buyback and the dividend to shareholders as well as the consumption of capital to support growth at the Bank. The Debt/Equity (D/E) ratio of ING Group improved from 9.7% to 9.5%, while the D/E ratio of Insurance improved from 12.3% to 9.2%. ING Bank's Tier-1 ratio declined

slightly from 8.3% to 8.2% due to strong growth of risk-weighted assets from EUR 309 billion to EUR 323 billion. The BIS Capital ratio improved from 11.5% to 11.9% because ING Bank issued approximately EUR 2 billion of lower Tier-2 capital in the second quarter. ■



Seoul, South Korea

# The Asian Century

As economic growth falters in the US and Europe, the international spotlight has intensified further on the Asia/Pacific region to carry world growth. In this feature, two leading academics give their thought-provoking views on the region's enormous potential and how it could be harnessed.

Asia is on the cusp of a golden economic renaissance, according to Professor Kishore Mahbubani. In the following interview, he explains why the West's domination of world economic affairs will end soon, but it has nothing to fear.

***Can you explain what you mean when you say we are experiencing one of the greatest shifts of power in human history?***

I would like to make two points in regard to this. The first is that it is the end of the era of Western domination of world history. However, I hasten to add that the end of this era is not

the end of the West. The West will remain the single strongest civilization for a century or more. But what's different – and this is the second point – is that we are going to see the return of Asia. The reason I call it the return of Asia is because up until the year 1820, as the British historian Angus Maddison has told us, the two biggest economies were China and India. So, in the 21st century, what you will see is a return to the norm. According to the Goldman Sachs BRICs projection, the four largest economies in the world in 2050 will be: China, India, the US and Japan. What's significant is that not a single European economy is among the top four, and this is a huge shift in world history compared to the last 200 years.





Professor Mahbubani speaking at ING's International Conference in May

***So if indeed, China and India were at the top for so long, why has it taken until now for them to remerge?***

The simplest explanation is that, finally, the Asian societies have understood and absorbed what it takes to secure long term, stable economic growth. They've cracked the seven pillars of Western wisdom which they need to absorb and implement in their societies. This explains the spectacular transformation of Asia, currently underway.

***What are these seven pillars?***

I believe successful societies are those which embrace the principle of free economics, have mastered science and technology, strive for a meritocratic society, are pragmatic, have developed the culture of peace, enforce the rule of law without fear or favour and place a strong emphasis on education.

***What in your opinion is the most important one?***

The first one, and the most important one, is free market economics. I can't think of a better example than China to illustrate this point. What's truly remarkable is that ever since China switched to free market economics thirty years ago, China has had the fastest-growing economy in the world for thirty years. Watching the world's most populous country having the fastest-growing economy is like watching the fattest boy in class win the 100-metre race. It's not supposed to happen, but that's what free market economics has done.

***What are some examples from history that illustrate why science and technology are so important?***

If you want to understand why the West succeeded in dominating the world, it's because they mastered science and technology. It explains how a small country like Portugal could go out and conquer a bit of Latin America (Brazil), conquer Angola and

Mozambique in Africa, take a bite of India, in Goa, and take a bite of China, in Macau. A small country of four million people conquered and colonised the world through its mastery of science and technology. And today, in a remarkable shift that many people still haven't understood, that mastery of science and technology is shifting to Asia. When I was doing research for my book *The New Asian Hemisphere*, I came across a remarkable statistic from an article in Time magazine entitled "Asia's Great Science Experiment". The article quoted a late Nobel prize-winner, Richard Smalley who said that by 2010, 90 per cent of all PhD holders in science and engineering would be Asians.

***How is meritocracy important?***

The best way I can answer this is by talking about soccer in Brazil. Why is Brazil consistently a soccer superpower but not yet an economic superpower? The simplest explanation is that, when it comes to looking for soccer talent, Brazil looks everywhere. They go to the upper class, middle class, lower class, and they go to the slums, the favelas, and if they find a young boy who can play football they say, come play for Brazil. They look for talent among all Brazilians. But when it comes to looking for economic talent, they look at the upper class, middle class, but they don't go much beyond that. So when you look for talent from a much smaller pool, you don't get the same results as you do when you look for talent from a bigger pool. Indeed, if you want the simplest explanation of why Asia is succeeding, it's remarkably simple: Asia always had the largest pool of brainpower, made up of hundreds of millions of brains. For two centuries, this pool was not used. Now it is being used and this is fuelling Asia's growth.

***How are Asian societies being pragmatic?***

The best definition of pragmatism is the one given by Deng Xiaoping (former Chinese leader). He once said it doesn't



matter whether a cat is black or white, if it catches mice, it is a good cat. That's a brilliant definition of pragmatism. But the key point to bear in mind here is that Deng Xiaoping was by no means the first pragmatist in Asia. The first pragmatists in Asia were the Japanese. After watching India being colonized and seeing China humiliated in the opium wars, the Japanese were convinced that this must not happen to them. So, during the Meiji Reformation in the 1860s, a group of young men from Japan went around the world to study best practices. They copied and implemented the American economy, the German military, the French legal code, and so on and so forth. This is an important point. Due to the legacy of what the Japanese did 150 years ago, the culture of copying best practices is now widely adopted in Asia. The success of one Asian country leads to the success of another one. It began with Japan. After World War Two, it spread to the four tigers, Korea, Taiwan, Hong Kong and Singapore. From these four, it went to South-east Asia, and from there to China, and from China to India. So the process of learning from each other is a powerful factor that is driving change.

#### ***What do you mean by the culture of peace?***

Europe has achieved the highest point in human civilization because in Europe you don't just have zero wars, you have zero prospect of war. This is what I call a true culture of peace. It's a huge achievement in Europe – Asia hasn't achieved that yet. But what's remarkable is that in East Asia, in the region where you've seen the three biggest wars since World War Two – the Korean War, the Vietnam War and the Sino-Vietnamese War – the guns are silent. That silence of the guns is not an accident, it's the result of the leaders deciding that they have to focus on their development.

#### ***What are you seeing in Asia that suggests education is a powerful driver of change?***

Education is very important to Asians. And this again is a powerful reason why Asia is succeeding because there's always been a deep hunger for education in Asia. In the city of Guangzhou, there are seven universities, and when these universities ran out of space, they had to look for a satellite campus. When I visited the satellite campus outside Guangzhou, I expected there to be about 30,000 students. But I was wrong! There were 150,000 students. That's the kind of hunger for education that you see happening in Asia. Hundreds of millions of minds in Asia have been opened to new possibilities. Indeed, if you want to meet the most optimistic generation of young people, you will find them in Asia. This optimism will be a massive driving force, which will ensure that the Asian century is real.

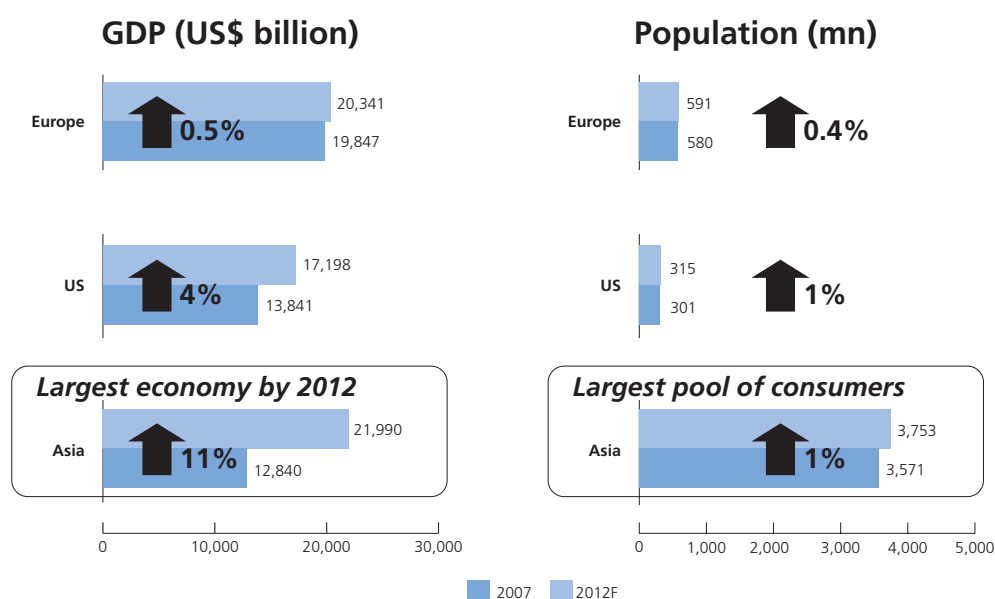
#### ***Many people fear the rise of Asia will lead to the domination of the West. What do you think?***

The most important point I want to emphasise is that the new Asian powers do not want to dominate the West. They want to replicate the West. Their dream of the future – and you can see this in the young people – is to achieve the same kind of comfortable, middle-class societies that we see in the West. Their dream is to have a nice home, a nice car, education for their children, stability at home. The new Asian states want to modernise and transform themselves.

#### ***In your opinion, does modernisation equate to westernisation in Asia?***

Whenever we use the term "modernisation", some switch turns on in Western minds that equates it to "Westernisation". ►

### **Asian economies poised to take the lead**



Source: Economist Intelligence Unit



These are two very distinct concepts. Asian societies want to modernise, but not Westernise. And indeed, the most exciting thing that is going to happen in Asia – and this is why it's so wonderful to be living at this time in history – is that just as the West went through a magical renaissance in the 16th and 17th centuries, when societies rediscovered their connections with the Greek and Roman civilizations and something magical happened in the Western mind that enabled it to succeed and flourish, that same magical occurrence will happen in the Asian mind. Suddenly, the connections with the past that were cut off by two hundred years of Western domination will now be reestablished. So you will see a kind of cultural effervescence in Asia, which is going to be quite remarkable. As Asian societies succeed, they do well, they prosper, they will trade more, you get more peace, you get more stability, you get more customers.

So that is a positive vision that I have for the future of Asia. We are at a remarkably plastic moment in world history, of a kind we've not seen in two hundred years or more.

● Kishore Mahbubani is the Dean and Professor in the Practice of Public Policy at the National University of Singapore. He is one of Asia's leading intellectuals, with a distinguished career as a diplomat and author. With the Singapore Foreign Service from 1971 to 2004, he had postings in Cambodia, Malaysia, Washington DC and New York, where he served two stints as Singapore's Ambassador to the UN and as President of the UN Security Council in January 2001 and May 2002. His latest book *The New Asian Hemisphere* released this year argues the case that Western domination of world affairs is waning and that Asian societies are poised to be co-drivers in global economic, political and cultural matters.

## Tapping the real potential

**Value creation in developing markets such as the Asia/Pacific requires innovation and imagination. Speaking at ING's International Conference for Senior Management in May, Professor C.K Prahalad, a leading management strategist, argued that a change of thinking is required for global companies to successfully tap the full range of opportunities in developing markets.**

The very poor – those at the bottom of the economic pyramid – constitute a massive global group, comprising four billion people who mostly subsist on less than two dollars a day and are largely considered too difficult and unprofitable by western businesses to access. However, Professor C.K Prahalad believes that in attempting to service the demand for goods and services for this group, companies could unlock major profitable growth opportunities and business value.

"Embedded in the poor living conditions, is the opportunity for businesses to make breakthrough innovations. We have to think differently. You have to imagine your way into this opportunity; analysis of the current situation will not get us there." He says entrepreneurial ingenuity is required to target this group, for which business success is based on creating profits from providing services at very low cost, while maintaining high quality standards often using new technologies and serving a mass population. It is from here, Prahalad contends – not just the Silicon Valley, or other wealthy regions – that some of the most interesting companies of the future will emerge.

He cites the example of a hospital in India, a leader in world class cataract surgery, performing surgery to 250,000 people a year (more than any other hospital in the world) at a fraction of the cost of similar surgery in the US. The hospital produces over 100% rate of return on capital employed. Companies, he says, need to think in terms of cost, not necessarily price. The traditional business formula of cost plus profit equals price needs to be adapted to price less profit equals cost to successfully tap into the mass underdeveloped market.

Because dramatic cost reduction is critical, companies need to think very differently about how they can adapt their existing business model. In fact, innovation and access to consumers, particularly to the millions that are currently considered inaccessible, are inextricably linked, he argues. "If companies want to double the number of customers in the Asia/Pacific, they might not need to do much. Strong growth means just maintaining the status quo will take them there. But if they want 500 million new consumers, they may have to think a little bit.

"Approximately 50% of humanity, 3 billion people live in the Asia/Pacific. No-one in Asia thinks about 3% growth. If you are only growing by 20%, there is something wrong with you. Look at the billions of people who need the services you can provide, he told the audience. "If you cannot access them because you cannot innovate, then you have a problem. You cannot analyse your way into this opportunity. You must imagine your way into this opportunity. You must believe, you must have passion, cour-

age, a lot of humility, humanity... and some intellect. Imagination is more important than knowledge." He said most global companies are unable to access the massive market of the very poor because of their cost structures. The question he poses though is: are companies willing to change the way they work so they can access "trillions of dollars of opportunity" or do companies walk away from that opportunity because of their current way of working and their current cost structure?"

The very poor, he says, live in the high cost, inefficient "unorganised sector". He says they are caught in a "poverty penalty" trap, in that they pay relatively more for most services. An example is local money lenders charging significantly above local bank lending rates. Professor Prahalad believes global companies with their organised systems, national and global competition, world class quality, affordable prices, access to information, advanced technology and new business models have much to offer. "If global companies can successfully bring a significant number of people from the "unorganised sector" into the "organised" sector, this dramatically changes the numbers of people companies can serve, and their future business prospects. "Which is the better choice: change the systems or forego the opportunity?" he says.

● Professor C.K Prahalad is the Paul and Ruth McCracken Distinguished University Professor of Strategy, Ross School of Business, University of Michigan. He was named "The World's Most Influential Management Thinker" in 2007 by the Times in London and "the most influential thinker on business strategy today" by BusinessWeek.

# Column Why stagflation won't persist

**Mark Cliffe, ING Group's Chief Economist, discusses seven reasons why 'stagflation', the toxic mix of high inflation and weak economic growth, is unlikely to persist.**

Over the past few months, talk of 'stagflation' has resurfaced. This is the ugly word for the ugly combination of high inflation and weak, or even negative, economic growth.

For the asset markets, stagflation is a good-for-nothing mix. High inflation puts upward pressure on bond yields. In turn, this compounds the damage from weak economic growth on stocks and other assets. Central banks then face a dilemma: do they raise interest rates to fight inflation, or cut them to boost growth? Unfortunately, the signs are that they will have to struggle with this for at least the next few months.

However, there are some reasons why the stagflation is unlikely to turn into a persistent problem:

- Oil and commodity prices, which have accounted for much if not all the rise in global inflation, are unlikely to keep rising at the same pace. Although it is too soon to say whether the recent sharp drop represents a peak in the commodity price cycle, so long as commodity prices merely rise less rapidly, they will take the pressure off headline inflation, not to mention consumers' purchasing power.
- Core inflation, which excludes food and energy, has been well contained, and is likely to remain so. A critical factor behind this is that, despite the sharp pick up in headline inflation, labour costs have not accelerated. As unemployment turns upwards, led by the US, workers are finding it harder to secure faster pay rises.
- The very fact that the housing market in the US and an increasing number of other economies is weighing on growth will help to curb inflation. At least in the developed world, housing is the biggest single component of consumer spending, so falling housing costs will accordingly be an increasing offset to the commodity led inflation seen so far.
- The impact of the credit crunch on the real economy, initially in the US and Europe, is still far from fully played out. The resulting contraction in credit is inherently deflationary. Borrowers' consumption and investment will be increasingly constrained by the banks' efforts to deleverage. To the extent that this continues to keep asset prices under downward pressure, this will lead to more write-downs by the banks, further limiting their willingness to lend.
- Central banks are generally delivering on their pledges to restrain inflation. In some cases, this has been largely rhetorical so far, but the European Central Bank and a number of others have already responded by raising interest rates, even in the face of concerns about slowing the credit crunch.
- The downturn in global growth is unlikely to be very deep, even if the credit crunch threatens to prolong it. This is probably true in China and other parts of the emerging world, which, far from suffering stagflation, have been enjoying an economic boom. In their cases, inflation has been more a symptom of economy overheating than of stagflation. In fact, despite the apocalyptic forecasts inspired by the problems in the construction and finance sectors, even the US has undergone a relatively moderate downturn so far.
- Policy-makers are unlikely to repeat the mistakes that exacerbated the stagflation of



Mark Cliffe

the 1970s. These mistakes were not confined to monetary policy: fiscal policy was excessively loose too, and efforts to control prices and wages directly largely failed. Sharp increases in inflation, as wages and prices chased each other upwards, subsequently necessitated painful corrective action. The lessons learnt in that period were subsequently embodied in policy frameworks in the developed and then the emerging world.

That said, the 1970s stagflation cannot simply be pinned on failures of economic policy. The roots of stagflation lie in market failures that disrupt supply – a prime example from the 1970s being the OPEC oil embargo – and thereby simultaneously raising prices while reducing output. Supply disruptions are arguably only part of the most recent commodity boom, but that does not mean that they could not emerge again as a threat to the global economy. Currently, the most obvious and dramatic risk of this kind would be further escalation of conflict in the Middle East, which could send oil prices shooting to well beyond \$200/bbl. However, it is more likely that we will be entering 2009 worrying less about stagflation than a straightforward global economic slowdown. ■



Manolo Valdés (1942), *Ariadne* 2007  
Bronze 142x130x128 cm  
ING Collection

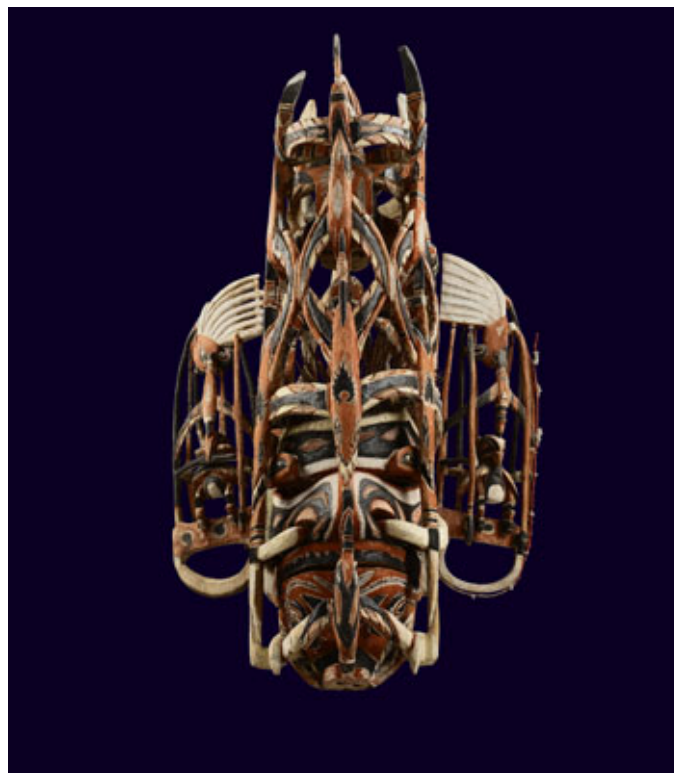
## Ariadne in ING House

A contemporary interpretation of an ancient character now decorates the entrance hall of ING House in Amsterdam. The newly acquired sculpture of Spanish born artist Manolo Valdés' interpretation of the mythical figure of Ariadne greets everyone who enters the building.

The sculpture *Ariadne* (2007), completed in bronze, depicts a serene female head with a wreath of metal spiralling outward and upward. The sculpture is part of a large series of women's heads by Valdés, who made various interpretations on this theme. The sculpture refers to the ancient Greek myth of the Labyrinth of the Minotaur. The headdress of the sculpture is a reference to the thread with which Ariadne helped her hero Theseus to find his way out of the labyrinth after he killed the Minotaur.

### Manolo Valdés

World-renowned artist Manolo Valdés was born in Valencia, Spain, in 1942. At the age of 15, he began art academy training, but after two years he dropped out to pursue painting full-time. A few years later, together with two friends, he formed the Equipo Cronica group, which disbanded two years later. The work produced by this group was similar to Pop art and contained elements of veiled social criticism. Valdés is a versatile artist: he is one of the few contemporary artists who has successfully mastered the disciplines of drawing, painting, sculpture and graphics. To date, he has had over 250 solo exhibitions around the world and has received many international awards.



Mask, New Ireland, northern part of the island of Tabar Wood, shell (operculum),  
© studio R. Asselberghs - Frédéric Dehaen Brussels

## Unique art from Oceania

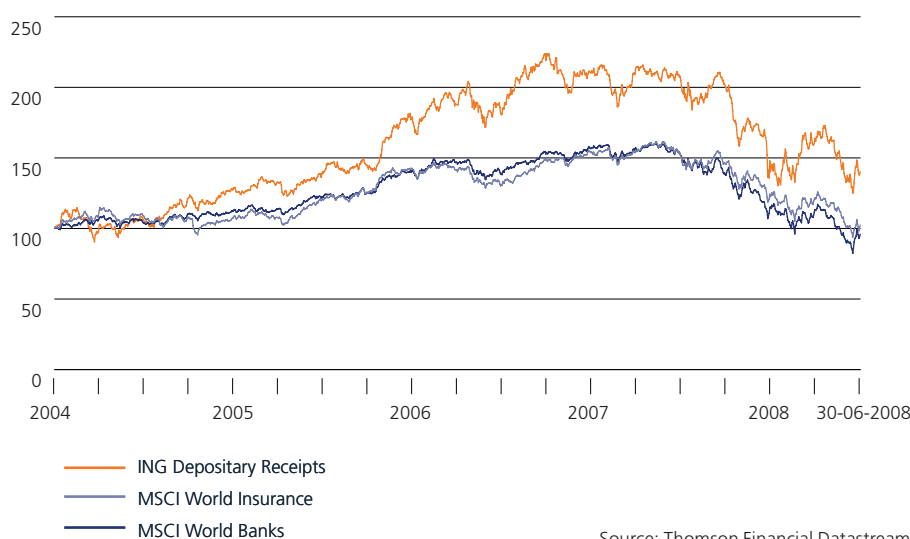
For the very first time in Belgium, some 200 unique works of art from Oceania will be exhibited in Brussels. ING Belgium is bringing together, from mainly Belgian private collections, this impressive valuable display, which provides a clear and fascinating look at the far-off and less-well-known Pacific cultures.

The exhibition *Oceania, Ritual Signs, Authority Symbols*, is divided into three parts, each representing one cultural region: Melanesia, Polynesia and Micronesia. The exhibition has been designed as an imaginary journey in which the visitor discovers and encounters sculptures, utensils, weapons and ornaments of great richness. Together, these works present a vivid picture of the different ancient cultures of Oceania. The name Oceania refers to the region that consists of numerous

lands, mostly (volcanic) islands and coral atolls in the Pacific Ocean with small human populations. For centuries, artists from Oceania created ritual artefacts and symbols of power which gave each of the dozens of cultures in the region its own identity.

From the islands of Melanesia there are panels and masks for the *malagan*, the ritual to commemorate the dead. From the Polynesian islands, including the Fiji islands and Easter Island, the exhibition features elegant, refined sculptures and ritual utensils. The islands of Micronesia are represented by a small but high-quality selection of utensils such as dishes, ornaments and masks. The exhibition runs from 23 October to 15 March 2009 at the ING Cultural Centre, Place Royale in Brussels.

## Total return index



## Global financials top 20 (based on market value in EUR billion)

1	HSBC Holdings	115.0
2	JPM Chase	74.8
3	Banco Santander	71.0
4	Mitsubishi UFJ Financial	62.3
5	Bank of America Corp	60.8
6	Citigroup Inc	54.3
7	BNP Paribas	52.0
8	Wells Fargo	50.2
9	Allianz	50.0
10	Unicredito	48.8
11	<b>ING</b>	<b>45.3</b>
12	BBVA	44.9
13	Amer Intl Group	44.0
14	Intesa Sanpaolo	43.5
15	Goldman Sachs	42.8
16	Royal Bank Scotland	40.7
17	Axa	38.2
18	Sumitomo Mitsui Financial	36.9
19	Royal Bank of Canada	36.8
20	UBS	36.3

Source: MSCI, Bloomberg, 8 July 2008

## Fortune Global 500

1 Wal-Mart Stores	11 Daimler
2 Exxon Mobil	12 General Electric
3 Royal Dutch Shell	13 Ford Motor
4 British Petroleum	14 Fortis
5 Toyota Motor	15 AXA
6 Chevron	16 Sinopec
7 <b>ING</b>	17 Citigroup
8 Total	18 Volkswagen
9 General Motors	19 Dexia Group
10 ConocoPhillips	20 HSBC Holdings

Source: Fortune, July 2008, [http://money.cnn.com/magazines/fortune/global500/2008/full\\_list/](http://money.cnn.com/magazines/fortune/global500/2008/full_list/) (based on several parameters, including revenues, net profit, shareholder value and number of employees)

## ING in FTSE4Good index again

ING has again been included in the FTSE-4Good index as one of 900 companies from a field of 2400 that perform best on sustainability issues. ING has been included in the FTSE4Good since 2001, the year the index was established.

The FTSE4Good Index Series is designed to identify companies that are working towards environmental sustainability, developing positive relationships with stakeholders and upholding and supporting universal human rights.

## Key dates in 2008 and 2009

**Thursday, 21 August 2008**

Payment date interim dividend 2008 NYSE Euronext

**Thursday, 28 August 2008**

Payment date interim dividend 2008 NYSE

**Friday, 19 September 2008**

ING Investor Day

**Wednesday, 12 November 2008**

Publication results Q3 2008

**Wednesday, 18 February 2009**

Publication results Q4 2008

**Monday, 27 April 2009**

Annual General Meeting of shareholders

(All dates are provisional)



## Disclaimer

ING Group's Annual Accounts are prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRS-EU').

In preparing the financial information for this publication, the same accounting principles are applied as in the 2007 ING Group Annual Accounts. All figures in this publication are unaudited. Small differences are possible in the tables due to rounding.

Certain of the statements contained in this publication are statements of future expectations and other forward-looking statements. These expectations are based on management's current views and assumptions and involve known and unknown risks and uncertainties. Actual results, performance or events may differ materially from those in such statements due to, among other things, (i) general economic conditions, in particular economic conditions in ING's core markets, (ii) changes in the availability of, and costs associated with, sources of liquidity such as interbank funding, as well as conditions in the credit markets generally, including changes in borrower and counterparty creditworthiness, (iii) the frequency and severity of insured loss events, (iv) mortality and morbidity levels and trends, (v) persistency levels, (vi) interest rate levels, (vii) currency exchange rates, (viii) general competitive factors, (ix) changes in laws and regulations, and (x) changes in the policies of governments and/or regulatory authorities. ING assumes no obligation to update any forward-looking information contained in this document.