Financial Institutions Ratings

ING Group N.V. – AT1 rating report

Security Ratings (assigned 29 February 2016)	
Outlook	Positive
6.00% USD 1bn perpetual AT1 contingent convertible securities	BBB-
6.50% USD 1.25bn perpetual AT1 contingent convertible securities	BBB-

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The ratings have not been solicited by the issuer; the analysis is based solely on public information.

Rating rationale

We have assigned a rating of BBB-, with Positive outlook, to the above noted perpetual subordinated contingent convertible securities issued by ING Groep N.V. based on the following:

- ICSR: A, Positive outlook
- Minimum notches down from the ICSR: 4
- Additional notches: 0

Please refer to Scope's *Bank Capital Instruments Rating Methodology first* published in July 2014 and updated in July 2015 for more details about the minimum notching for AT1 securities. The lack of additional notching for these securities reflects the following:

- A single trigger at the group level, which is 7% on a transitional basis
- The distance to the combined buffer requirement is average and the distance to trigger is at the higher end of the range compared to other rated AT1 securities. Moreover, we deem the group capable of accumulating capital if needed.

ICSR

With the disposal of investment management and insurance businesses, the balance sheets of ING Bank and ING Group have converged. We therefore have the same rating of A on the two entities.

The ICSR of A for ING is driven by its strong and resilient retail and commercial banking franchise in the Benelux region. As well, ING continues to be at the forefront of direct retail banking operations in several important markets, including Germany. The bank has remained profitable despite restructuring, impairments on financial assets and elevated credit costs. At the same time, both the bank's funding profile and capital position have been strengthened. Management's success in restructuring and the normalisation of earnings are key drivers for the Positive Outlook. Meanwhile, with management now focused on executing its "Think Forward" strategy, we see some uncertainties related to the potential risks of the group's growth strategies.

Summary terms

Issuer	ING Groep N.V.
Issue Date	16 April 2015
Amount	USD 1bn
Coupon	• 6.00% fixed until first call date, reset every 5 years thereafter • If any, payable semi-annually
Format	• Perpetual subordinated contingent convertible securities, callable April 2020 and every five years thereafter • Redeemable at the issuer discretion after first call date or at any time following a Regulatory or Tax event, in either case subject to regulator consent
ISIN	US456837AE31
Issue Date	16 April 2015
Amount	EUR 1.25bn
Coupon	• 6.50% fixed until first call date, reset every 5 years thereafter • If any, payable semi-annually
Format	• Perpetual subordinated contingent convertible securities, callable April 2025 and every five years thereafter • Redeemable at the issuer discretion after first call date or at any time following a Regulatory or Tax event, in either case subject to regulator consent
ISIN	US456837AF06
Capital Treatment	Additional Tier 1
Coupon Cancellation	• Fully discretionary • Mandatory: - if there are insufficient distributable items to pay coupons on these securities and future payments on other own funds items in the then current financial year or - if aggregated with other distributions would cause the MDA to be exceeded
Principal Loss Absorption	• Full conversion into ordinary shares upon trigger breach at conversion price • Upon exercise of the Dutch Bail-in Power by the relevant resolution authority
Trigger for Principal Loss Absorption	Consolidated group CET1 < 7% on a transitional basis

Source: Prospectus, Scope Ratings

Key risk: coupon cancellation

Coupon payments are fully discretionary and are subject to payment restrictions. Notwithstanding coupon cancellation on the securities, the issuer would be allowed to make dividend and interest payments in relation to other securities. During its roadshow presentation for the securities, however, ING specified that during the financial crisis it continued to pay coupons on Tier 1 instruments, while dividend payments were suspended.

There is mandatory cancellation of coupons in the event of insufficient available distributable items (ADI). We do not expect the lack of ADI to be limiting factor for the payment of coupons. As of YE2014, the ADI of the issuer, ING Group, stood at EUR 36.2bn. For 2015, the group reported a net result of EUR 4bn.

ING has not issued any other CRD IV compliant AT1 securities.

Combined buffer requirement

In Opinion 2015/24 dated 18 December 2015, the EBA clarified the interaction between Pillar 1 and Pillar 2 capital requirements and the CBR (see "*EBA Opinion 24/2015: Clarity added to the MDA debate*", January 2016). The buffers sit on top of Pillar 1 and Pillar 2 requirements and restrictions on distributions apply when CET1 capital falls below the buffers. These restrictions became effective from 1 January 2016 and are based on transitional CET1 requirements.

Helpfully for investors, banks have started to disclose their capital requirements stemming from the Supervisory Review and Evaluation Process (SREP). The SREP capital requirement comprises the minimum Pillar 1 CET1 requirement, an institution-specific Pillar 2 CET1 requirement for risks not covered explicitly under CRD IV and a frontloading of the capital conservation buffer.

Along with 4Q 2015 results, ING Group disclosed its SREP capital requirement of 9.5% for 2016. In addition, ING is subject to a 3% systemic risk buffer imposed by De Nederlandsche Bank, to be phased-in from 2016 over four years. The countercyclical capital buffer rate for exposures in the Netherlands is currently set at 0% and will be reviewed quarterly. Assuming the countercyclical buffer remains at 0%, the group would be subject to a CET1 requirement of 12.5% in 2019. It is our understanding that SREP capital requirements should not change materially between now and 2019 as the capital conservation buffer has been front-loaded.

Consequently, management has set a new CET1 target for the group of above 12.5% and will over time build a "comfortable management buffer". As of YE2015, ING Group's fully-loaded CET1 capital ratio stood at 12.7% while the transitional figure was 12.9%. We believe that the group's solvency is strong and that their dividend policy, which resumed relatively aggressively this year, already incorporates these capital targets.

Table 1: Estimated distance to combined buffer requirement

	2016E	2017E	2018E	2019E
Combined buffer:				
- Capital Conservation Buffer	0.63%	1.25%	1.88%	2.50%
- Systemic[1]	0.75%	1.50%	2.25%	3.00%
- Countercyclical[2]	0.00%	0.00%	0.00%	0.00%
ECB SREP requirement add-on[3]	4.38%	3.75%	3.13%	2.50%
Minimum CET1 (Pillar I)	4.50%	4.50%	4.50%	4.50%
Required CET1 associated with distribution restrictions	**10.25%**	**11.00%**	**11.75%**	**12.50%**
ING Group's CET1 / target (FL)	12.70%	12.5% + management buffer		
Distance to CBR (%)	2.45%			
Distance to CBR (EUR bn) [4]	7.9			

[1] Buffer for Dutch systemic banks. Phased-in between 2016 and 2019

[2] If applicable, may range from 0-2.5%. Would normally be phased-in between 2016 and 2019

[3] Based on SREP capital requirement of 9.5%

[4] Based on fully-loaded CET1 ratio of 12.7% and EUR 321bn RWA as of YE2015

Source: Company data, Scope Ratings

Key risk: principal loss absorption

Under the terms of the securities, there is full conversion into shares when the trigger level is breached, i.e. when the consolidated group transitional CET1 ratio falls below the 7% threshold.

In addition, investors in the security agree and consent to the exercise of any Dutch bail-in power by the relevant resolution authority that may result in the cancellation of all, or a portion, of the principal amount of and/or conversion of all or a portion of the principal amount of the securities into shares or other securities.

When these securities were issued in April 2015 the Netherlands had not transposed BRRD into national legislation, which they did in November 2015. Reference to the Point of Non-viability (PONV) is only present in the General Risk Factors, and gives power to the resolution authority to write down and convert notes at the PONV independently from any other resolution tool.

Distance to trigger

ING Group reported a transitional CET1 ratio of 12.9% as of YE2015. The gap for 2015 was 5.9% or almost EUR 19bn, which we consider to be material compared to other issuers. In January 2016, ING further reduced its stake in NN Group to 14.1%, adding 30 bps to the fully-loaded CET1 capital ratio. Pro-forma for the full divestment of NN Group, the CET1 ratio is expected to reach 13.4%. Going forward, we expect the gap to trigger to be at least 550 bps in light of the group's CET1 target, but potentially wider in 2016, given the last disposal which would complete the restructuring agreed with the European Commission.

Table 2: Distance to trigger

	2015	2016E	2017E	2018E	2019E
Trigger level	7.0%	7.0%	7.0%	7.0%	7.0%
ING Group CET1 ratio (transitional) / target (fully-loaded)	12.9%	12.5% + management buffer			
ING Group Gap (%)	5.9%	>5.5%	>5.5%	>5.5%	>5.5%
ING Group Gap (EUR) [1]	19.0				

[1] Based on EUR 321bn RWA as of YE2015

Source: Company data, Scope Ratings

Regulatory Disclosures

Information pursuant to Regulation (EC) No 1060/2009 on credit rating agencies, as amended by Regulations (EU) No. 513/2011 and (EU) No. 462/2013

Responsibility

The party responsible for the dissemination of the financial analysis is Scope Ratings AG, Berlin, District Court for Berlin (Charlottenburg) HRB 161306 B, Executive Board: Torsten Hinrichs (CEO), Dr. Stefan Bund.

The rating analysis has been prepared by Pauline Lambert, Executive Director

Responsible for approving the rating: Sam Theodore, Managing Director

The rating concerns a newly-issued financial instrument which was evaluated for the first time by Scope Ratings AG.

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Prior to publication, the rated entity was given the opportunity to examine the rating and the rating drivers, including the principal grounds on which the credit rating or rating outlook is based. The rated entity was subsequently provided with at least one full working day, to point out any factual errors, or to appeal the rating decision and deliver additional material information. Following that examination, the rating was not modified.

Methodology

The methodologies applicable for this rating "Bank Rating Methodology" (May 2015) & "Bank Capital Instruments Rating Methodology" (July 2015) are available on www.scoperatings.com. The historical default rates of Scope Ratings can be viewed on the central platform (CEREP) of the European Securities and Markets Authority (ESMA): http://cerep.esma.europa.eu/cerep-web/statistics/defaults.xhtml. A comprehensive clarification of Scope's credit rating, definitions of rating symbols and further information on the analysis components of a rating can be found in the documents on methodologies on the rating agency's website.

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