

The image shows the Wirecard logo in large, illuminated, 3D letters mounted on a building's facade. The letters are dark blue with a bright white glow around them. The building's structure, including a dark metal grate, is visible in the background against a clear blue sky.

Wirecard

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FS ASSOCIATES

2020

# WIRECARD AG POST MORTEM ANALYSIS

REPORT BY QUIRIN ZUNDL

TO: FS ASSOCIATES INVESTMENT DEPARTMENT



FS ASSOCIATES  
STUDENT INITIATIVE OF  
FRANKFURT SCHOOL

A vertical image on the left side of the page shows a hand holding a pen over a document with some handwritten notes and diagrams. In the background, a calculator is visible. The image is partially obscured by a blue vertical bar on the far left.

*This report aims at assessing our mistakes with regard to our Wirecard position, which turned out to be a massive fraud and had a significant negative impact on our returns.*

*In the case of Wirecard, we had three main convictions which motivated the long exposure:*

*a) We were convinced that Wirecard had a fantastic business model in a growing market of the future, namely digital payment*

*b) We believed that accusations regarding fraud from diverse sources including short sellers and the Financial Times (FT) were unfounded and false*

*c) Undervaluation: The earnings multiple was well below that of peers such as Adyen and Paypal, mainly due to the fraud suspicion. We believed that as soon as the fraud suspicion would be eradicated, a multiple expansion would take place*

*In retrospect, all three pillars of our investment thesis were false.*



# 1. TIMELINE

At FS Associates, we started looking at Wirecard in October 2019 when the company had recently fallen roughly 30% after a FT article. However, the story starts in March 2019, when I bought my first personal shares in Wirecard, at the time for 110€ per share. I bought the shares after a series of negative FT articles and a subsequent positive report by the law firm Rajah & Tann. By the summer of 2019, the shares were trading at 150-160€ per share, Wirecard had received a €900m investment from Softbank and declared a business partnership with Aldi. At the time, things looked great, at least that is how it seemed. I sold some of my shares, but held on to the majority expecting further price increases which would lead the stock to its past all time high at €200 per share.

Then, in October 2019, a new FT article led to the sharp 30% decline described above. I was convinced that this was again for no reason and believed the same pattern would occur as in February to September 2019, this time linked to a positive KPMG report.

The KPMG report arrived on April 28th, 2020 and stated that the auditors could neither confirm nor disconfirm a significant portion of the Third Party Acquiring (TPA) business of Wirecard. The market sold off this news and on June 18th, 2020, Wirecard did not publish its 2019 Annual Report but instead reported that €1.9bn in cash were “missing”. Seven days later, Wirecard filed for bankruptcy. The share now trades at roughly €1, Markus Braun, the former CEO and founder, is in custody and Jan Marsalek is on the run.



## 2. MAJOR EVENTS AND INTERPRETATION

### 2.1 PUBLICATION OF FT ARTICLE OCTOBER 15TH 2019

The publication of this article and the subsequent 30% price drop marked the beginning of the interest at FS Associates in the Wirecard issue. I had personally benefitted from such a development in the six months prior and believed we could repeat this at FS Associates.

A major mistake at this point is that we did not conduct sufficient due diligence and business model analysis to properly assess the risks linked to this endeavor. Instead, we believed the figures presented to us in the company's financial publications regarding margins, earnings and revenue growth, cash flows etc. - this was a mistake, because we were not able to sensibly opine whether these figures were plausible. In retrospect, the first red flag should have been the consistency with which Wirecard stated growth at over 20% each year and seemingly independent of market conditions.

### 2.2 FS ASSOCIATES BUYS IN NOVEMBER 4TH 2019

We bought in on November 4th at €119 per share and gradually increased the position

over time, buying dips which occurred. In fact, there were two opportunities to sell the position in the €140 range, namely in February 2020 and April 2020. We did not sell, as we stuck to our above-mentioned convictions and expected much higher prices.

We ignored, at the time of the purchase, that Wirecard had net cash (more cash and cash equivalents than financial debt) and at the same time a high-yield bond on the market. This should have been a second red flag. Today, we know that the cash was fake and that Wirecard actually had net debt, which also explains why they did not pay down the high-yield bond.

### 2.3 KPMG REPORT IS PUBLISHED APRIL 28TH 2020

Of all the events, the KPMG report was the most relevant because it marked a clear turning point. KPMG stated it could neither confirm nor disconfirm a majority of Wirecard's TPA business. For an outsider, this is horrible news, as it is not KPMG's job to prove fraud but rather to confirm accounts and business activity. As KPMG was not able to do so, this report was a huge red flag and we should have closed the position at this point.



Instead, I followed the narrative of Dr. Braun who saw Wirecard relieved of fraud accusations due to KPMG's incapacity to disconfirm the existence and size of the TPA business. This was mainly driven by confirmation bias and greed, in retrospect difficult to understand, particularly for people who were not invested. However, being invested in this company changed my view on basically any news they published and lead me to ignore even the largest red flag imaginable in a possible fraud case. The lesson to be learned here is that such events require open-minded discussions with people who have a contrarian opinion to properly assess the findings.

What makes matters worse, is that the fraud could not be detected in a classical way, e.g. capitalized costs, aggressive revenue recognition etc. Instead, the fraud was hidden in the cash position, in escrow accounts that never existed. However, in the financial statements audited and approved by EY up to 2018, it all added up perfectly fine.

I have to admit that I am amazed by the fact that EY, Wirecard's auditor since 2009, did not bother to take a look at the cash balances. Put differently, I always believed that cash was not fakeable, in a sense that

either it is there or not there - much easier to audit than for instance the value of an intangible asset. But apparently, either EY did a really bad job at checking the cash position, or Braun and his team were geniuses at fraud. Personally, I find a combination of the two plausible, however being good at fraud and lies is certainly not something to be proud of. And it does not make me feel any better to have been tricked by crooks who were good at what they did.

## **2.4 €1,9BN IN CASH "MISSING" JUNE 18TH, 2020**

On June 18th, 2020, Wirecard was supposed to publish its overdue 2019 Annual Report. Instead, they informed the public that €1,9bn in cash were apparently "missing". EY had at last cared to look more closely at the cash positions and discovered the fraud. A week later, Wirecard declared bankruptcy. In a matter of 7 days, the stock price fell by 98% - the perfect short - if one had read the KPMG report in an unbiased way.

I still record sitting in front of my screen in shock and amazement on this historic day. I write historic because I cannot record any similar event in the DAX30 index. In fact, Wirecard being in the DAX index gave me an unfounded illusion of safety - it was completely unthinkable for me that something like this could happen.

# 3. CONCLUSION

First and foremost, I want to point out that Dan McCrum, his colleagues, and the Financial Times did a tremendous job at uncovering this scandal and reported about it in a very professional way, despite obstruction attempts from the German regulators and Wirecard. This was a masterpiece of investigative journalism and in my point of view this deserves special mentioning.

For me and FS Associates, the Wirecard disaster was costly and unfortunate, however a great learning experience. In fact, it emphasizes the importance of thoroughly analyzing the business models of potential investments and to do good due diligence. Additionally, I will avoid companies with fraud allegations in future or only invest very small sums in such companies.

With regard to the mistakes, many of them were derived from psychological factors and the rest was too superficial research. Our new team structure where one investment team does the research and the other team tries to defend the opposite opinion should enable us to avoid such cases in the future. Particularly if several red flags appear this must be considered in future.

  
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