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Why This Fintech Star Can't Shake Off Short Sellers

German payments giant needs to shine more light on the sources of its spectacular growth

By Paul J. Davies
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German payments company Wirecard has grown spectacularly and some expect an equally spectacular fall. The fintech star's best defense is to explain its rise much more clearly.

Wirecard, which last year overtook the market value of Germany's two largest listed banks, shouldn't be that complicated. It is meant to be a scalable, technology-driven company that processes transactions for retailers and offers some risk-management services. But a history crowded with acquisitions has made its accounts complex and hard to follow, attracting short sellers.

The stock has lost 30% since late January, when Wirecard admitted a law firm was investigating accusations of accounting misconduct in Asia. It denied wrongdoing and promised to release the findings. Even after the fall, its shares trade on 25 times prospective earnings, ahead of many peers.

What is clear from a thorough analysis of its results is that Wirecard has racked up huge debts in its expansion drive. Since 2015, it has also been taking greater, largely unexplained risks by lending money to retailers and fintech platforms. This mix of acquisitions, financing and lending casts doubt on the sustainability of its revenue growth and the strength of its cash flows.

It is possible to find the scale of Wirecard's lending within its financial statements, with help from the company. But there is no disclosure on the riskiness of the loans, or more important how they contribute revenue from interest income, related fees, or from tying clients into other services.

Wirecard last year overtook the market value of Germany's two largest listed banks. PHOTO: WOLFGANG RATTAY/REUTERS

The company has for years been aggressive in defending itself against short sellers and journalists, but questions keep coming. In November, Bank of America analysts found Wirecard had much lower market share than expected in Germany, which gave them concerns about its revenue sources. Its lack of disclosure has also kept it out of mainstream payments industry rankings, such as the Nilson Report.

For years, Wirecard's revenue has outpaced industry growth rates, hitting €1.4 billion in the first nine months of 2018. It has expanded more than 30% a year since 2012.

But its debt has grown faster, hitting €1.3 billion at the end of September, up from less than €100 million in 2012. That has funded spending on takeovers, customer relationships, software development and other things. Total investment spending has been similar to revenue growth in each of the past five full years through 2017.

Now it is cranking up lending, too. Its latest focus is advancing funds to merchant retailers, which began in 2017. This generates interest income, but also fees and relationship charges that aren't clear.

Since 2015, it has ramped up lending to fintech clients and to borrowers on peer-to-peer platforms. Among them is U.K.-listed Funding Circle, which guarantees Wirecard a 5-6% return but keeps income above that threshold. Total fintech lending, across several unidentified platforms, has grown to €260 million, from less than €40 million in 2013. Again, there is no disclosure on exactly how this adds to revenue—or risk.

Nature abhors a vacuum, and Wirecard's skeptics thrive on a lack of financial disclosure. The company needs to open itself up to much more scrutiny to show its growth is sustainable and justify its still-high valuation.

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