Wirecard: The Rise and Fall of a Fintech Giant in Asia
By Paul Condylis and Emir Hrnjic

News broke recently that fintech company Railsbank has agreed to acquire its competitor Wirecard UK's remaining assets, clients, and a number of employees. Moreover, Wirecard sold its operations in Brazil and advanced the process of selling its North American operations.

Once the darling of the fintech industry, Wirecard is now in a predicament.

In a dramatic turn of events, on June 18, 2020, auditing firm EY refused to sign off on its financial statements and Wirecard admitted that roughly €1.9 billion in two Philippine banks did not exist. Within several days, the CEO was arrested for alleged fraud, the company filed for bankruptcy protection, and Wirecard's share price collapsed from more than €100 to less than €2.50.

In the largest auditing scandal since Enron, the Financial Times reported that EY did not do even basic auditing procedures such as confirming with the banks that they held large amounts of cash in Wirecard's trustee accounts.

Even German Finance Minister was aware of potential market manipulation at Wirecard a year and a half ago, but he, too, failed to act.

But how did a tiny German payment processing company manage to enter such a competitive business and develop at such a spectacular rate?

Asian Expansion

After starting a subsidiary in Singapore in 2007, the company grew rapidly in the Asian market due to acquisitions of small Asian mobile payment companies.

Wirecard entered the fringes of the market serving merchants with less-than-stellar reputation such as pornographic websites and online gambling that conventional banks avoided due to high risk and small margins. Wirecard managed to disrupt the payment processing market due to its ability to charge less than its main competitors and willingness to onboard riskier customers.

Moreover, as conventional banks licked their wounds after the global financial crisis in 2008–2009, Wirecard and other fintech companies started processing electronic payments faster than banks and chipping away their market share.

Finally, the fintech companies started heavily investing in powerful machine learning models capable of offering better risk management and fraud detection as well as creating powerful databases of their customers.

After rapid expansion in Asian mobile payment business, the Asian business started earning almost half of the group's revenues.

What Is Next?

Even after the parent company filed for bankruptcy protection in Germany on June 23, the subsidiaries proceeded with their business activities.

Germany's financial regulator BaFin stated that they would "continuously review whether insolvency applications also have to be filed for subsidiaries of the Wirecard Group." On June 26, the British financial regulator FCA suspended the activities of Wirecard's UK-based subsidiary but lifted the restrictions three days later.

Closer to home, the key concern is how Germany's parent's bankruptcy affects the Singapore subsidiary. While the trustee did not rule out that Wirecard subsidiaries may have to file for insolvency, theoretically, businesses of Wirecard's subsidiaries should be judged on their own merits.

In fact, the Monetary Authority of Singapore (MAS) said on June 30 that it is closely monitoring the operations of Wirecard's entities in Singapore. They "have complied with MAS' directions to hold customers' funds in segregated accounts with banks in Singapore," thus ensuring that the funds are safe from the German parent's bankruptcy.

Since Wirecard has very few tangible assets, the risk is that its business will lose substantial value if clients start switching to competitors.

Moreover, FT reported that Wirecard's main 100 customers accounted for more than half of its genuine sales.

Notwithstanding the fact that some Wirecard's transactions were fictitious and Wirecard may not have as many customers as claimed, Wirecard's market share in Singapore is likely sizable.

Customers Jumping Ship

Unfortunately, German parent's bankruptcy likely spooked the customers of Wirecard's subsidiaries in Singapore.

Wirecard entered a payments agreement in March to process transactions made via the GrabPay e-wallet used by more than 600,000 merchants in the region. That partnership was put on hold immediately after the news of German parent's bankruptcy.

Just a few days later, Visa and Mastercard announced that they are considering revoking Wirecard's ability to process payments on their networks.

Bloomberg and Business Times reported that many other Wirecard's clients started leaving the company immediately after the scandal broke.

Moreover, Wirecard's competitors started aggressively poaching Wirecard's customers by offering them attractive custom-tailored packages and expedited migration.

The first customers to jump ship are likely the safest businesses that should be easily onboarded by competitors. As Wirecard's safest customers keep switching, the remaining portfolio will become riskier. As the remaining portfolio becomes riskier, Wirecard will have harder time to retain competitive pricing and the downward spiral is inevitable.

Notwithstanding the fact that subsidiaries did not file for bankruptcy and may not have been involved in the accounting and auditing misdeeds, Wirecard's remaining business is in serious trouble.

The payment processing business is mostly a business of trust and if the trust is lost – business is gone. If Wirecard customers believe that Wirecard will go bankrupt, it will likely go bankrupt as a self-fulfilling prophecy. In the best-case scenario, Singapore subsidiary will be acquired just like its counterparts.

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