VERACITY

CASE STUDY: WIRECARD, ESG, AND THE PERILS OF RELYING ON RATINGS AND SELF-DISCLOSURE

On 17 June, shares of German payments processing firm Wirecard plummeted when it emerged that US$2 billion the company said was in Philippines banks wasn't actually anywhere at all. The firm's value dropped from US$14.5 billion to US$500 million in a matter of days. Within a week, Wirecard had filed for insolvency, and multiple company executives have since been arrested for suspected fraud.

There are many lessons to be learned from Wirecard's stunning fall from grace, not least that **a dose of skepticism around company disclosures is always healthy**. Where Wirecard is particularly instructive for investors, however, is around ESG issues, **and the value of a rigorous, independent vetting of firms' ESG ratings and reputation.**

As the *Financial Times* pointed out on 1 July, "Before its collapse, Wirecard earned median-grade ESG ratings" from multiple notable ESG ratings companies and the company "got picked up by some big ESG exchange traded funds." All of this despite serious shortcomings in governance—the "G" in ESG—that were hiding in plain sight and would give pause to any investor who took the time to look.

In today's investment climate, a thorough, qualitative, and independent assessment of ESG issues is—as the Wirecard saga teaches—a necessity.

Veracity evaluated Wirecard on behalf of a prospective investor several years ago. We examined the company's corporate filings, researched the track records of its principals, and attempted to untangle its web of far-flung subsidiaries and unorthodox financial arrangements.

We reported to our client a "likelihood of illicit business dealings," and we explained that our research revealed "concerns that [Wirecard] and entities affiliated with [it] have engaged in financial impropriety." We drew these conclusions after finding a host of red flags, including that multiple subsidiaries listed in company filings did not appear to be registered with regulators in their respective countries, and that a company principal had previously been accused of money laundering, which was particularly concerning in light of the firm's elaborate and opaque structure.

The approach we took in assessing Wirecard and its practices—quite simply, putting the company's own declarations and the endorsements of others under a microscope—is both tested and replicable, and has been refined over the course of hundreds of investigations on behalf of investors and corporates.

In today's investment climate, in which ESG ratings and testimonials have become virtual shorthand for resilience and best-in-class practices, a thorough, qualitative, and independent assessment of a firm's true attentiveness to ESG issues is—as the Wirecard saga teaches—a necessity.