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Marie-Curie-Str. 24-28
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March 15, 2019

Dear Jean-Pierre,

As a global market participant and an institutional fiduciary, there is nothing more sacred than the freedom and integrity of the markets. In my business I focus exclusively on fundamentally-driven short selling and at my fund, Safkhet Capital, we conduct investigative due diligence over the course of hundreds and even thousands of hours, to answer the excruciating and uncomfortable questions. Our work is costly, precise, and can often lead to the revelation of a profound chasm between a company's public narrative and its reality. The required effort compounded by the symmetry of risk and reward with this strategy means my ability to safeguard my investors' capital and necessarily generate positive returns is ultimately dependent on market efficiency.

I am a short seller, but I am also a vocal advocate for free markets and all that demands, including greater corporate transparency, accountability, and appropriate regulatory oversight. When actions are taken to disrupt market order, no matter by whom, I have a duty of care to seek remediation and help to ensure artificial forces do not distort the climate for fluid, receptive price discovery. BaFin's February 18th decision to ban all new short sales of Wirecard AG, publicly traded on Xetra, was one such moment.

In the interest of full disclosure, since Safkhet Capital's inception in January 2018, the firm has held a significant short position in Wirecard equity and remains significantly short. Prior to initiating this position, the team spent months investigating Wirecard, and all associated entities, across all geographies. This process involved reviewing and independently corroborating prior allegations levied against the company, and most importantly establishing evidence that corporate transgressions have potentially been sustained through to present day, becoming ever more expansive. However, the purpose of my correspondence is not to discuss the many reasons my fund is short Wirecard.

The relevance of our short investment is our process—the essence of our strategy—which should attest to the sincere and purposeful way by which we engage with the markets. We do not seek to benefit from the short-term price volatility created by any single catalyst, such as a news publication. We singularly bet against crime, fraud, and failure after exhaustive, independent inquiry. Safkhet Capital and its investors, including I myself, are directly, disproportionately harmed by the imprudent decision by your organization to ban all short sales in Wirecard. We are further alarmed by BaFin's history of taking actions against critics, including those of Wirecard, with active investigations into the Financial Times and Zatarra Research. We unequivocally support actions taken to address all forms of market manipulation. However, such seemingly unilateral regulatory effort, prompted without sufficient evidentiary disclosure, can create a toxic environment where whistleblowers will avoid coming forward for fear of civil or criminal penalty for telling the truth. BaFin's actions may set a dangerous precedent for market cosseting and capitulation to corporate influence.

Here, I will rely on an extensive history of academic research and market behavior to empirically demonstrate the following:

- The pivotal market role of short selling
- The counterintuitive impact of short sale bans
- The frailty of BaFin's rationale for this ban
- The dangerous repercussions of regulatory capture

It is my genuine hope that BaFin will carefully consider this, not only when evaluating the Wirecard short sale ban, but all future restrictions on trading activity. I believe that financial regulators, such as BaFin, at their core share a similar motivation to me: to preserve market integrity. We are all susceptible to shortcomings and the best we can do is acknowledge them and correct course before irreparable damage is done.

Short Selling: Liquidity, Price Discovery, and Fraud Detection

The vast majority of daily trading is driven by algorithms and technical signals, trading which includes buying and selling (or equivalently, short sales). In a 2017 JP Morgan report, it is estimated that only 10% of trading volume is driven by fundamental, discretionary traders.[1] It follows that the insipid issuer

[1] Cheng E (2017) Just 10% of trading is regular stock picking, JPMorgan estimates. In: CNBC. https://www.cnbc.com/2017/06/13/death-of-the-human-investor-just-10-percent-of-trading-is-regular-stock-picking-jpmorgan-estimates.html.

song and dance of blaming "short sellers" for price declines is wholly disingenuous. It plays on the emotions of retail investors to whom short sellers are the Bogeyman—evil, mythic creatures set out to enrich themselves through robbing others of their wealth. It is a much more compelling story than the reality: faceless algorithms, agnostic to the particulars of any single company, dictate momentum. Just as quickly as those algorithms initiate a short sale, they may cover that sale.

As a trading strategy, short selling is widely acknowledged as beneficial and a necessary countervailing force to maintain market efficiency. In response to the EU Commission report on short selling, IMF staff wrote, "Short selling has many benefits which help improve market quality…. Augments liquidity, for every (short) seller there is a party on the other side of the transaction who is willing to pay the given price."[2] Whether a short sale is initiated by the algorithms or the Bogeyman, most empirical studies have concluded that short sellers are informed traders whose activity helps correct overvaluation[3,4,5] and support liquidity provisions,[6] particularly in large market capitalization companies.[7]

In 2012, Boehmer and Wu analyzed daily short-selling flow data to precisely characterize the impact of short sales on price discovery and informational efficiency through analysis of transaction-based high-frequency measures of efficiency, lower-frequency price-delay measures, post-earnings-announcement drift anomalies, and short selling around large price movements and price reversals. After their technically comprehensive study, they conclude that when short sellers are active, prices appear to be closer to efficient or fundamental values and the magnitude of this effect is similar to that of large institutional holdings and three times that of sell-side analyst coverage. The study found no signal of price destabilization or manipulative trading by short sellers.[8]

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[2] "IMF Staff Comments on EU Commission Consultation on Short Selling." *IMF*, 5 Aug. 2010, www.imf.org/external/np/eur/2010/pdf/080510.pdf.

[3] Asquith, P., & Meulbroek, L. K. (1995). An empirical investigation of short interest. Division of Research, Harvard Business School.

[4] Dechow, P. M., Hutton, A. P., Meulbroek, L., & Sloan, R. G. (2001). Short-sellers, fundamental analysis, and stock returns. Journal of Financial Economics, 61(1), 77-106.

[5] Diether, K. B., Lee, K. H., & Werner, I. M. (2008). Short-sale strategies and return predictability. The Review of Financial Studies, 22(2), 575-607.

[6] Diether, K. B., Lee, K. H., & Werner, I. M. (2009). It's SHO time! Short-sale price tests and market quality. The Journal of Finance, 64(1), 37-73.

[7] Blau, B. M., & Whitby, R. J. (2018). How does short selling affect liquidity in financial markets?. Finance Research Letters, 25, 244-250.

[8] Boehmer, E., & Wu, J. (2012). Short selling and the price discovery process. The Review of Financial Studies, 26(2), 287-322.

Market history and scientific study are near-unanimous in understanding the critical role of short sales in the market. Despite the decades-old Bogeyman story perpetrated by failing companies, the data indicates it is all but a strawman. Those charged with safeguarding financial markets should know better than to perpetrate such a deceptive narrative.

In fact, such regulators should be closely monitoring short sale behavior, not to blunderingly investigate criminal intent behind short sales, but because fundamental short selling can be a valuable indicator of fraud and misrepresentation. There is no greater wealth destroyer than corporate deceit and in the interest of investors large and small, regulators must use all information at hand to mitigate and prevent such losses.

In 2010, Karpoff and Lou investigated if short sellers identify overpriced firms and their effect on other investors. They conclude that short sellers are very competent at identifying financial irregularities well before the issues are publicly revealed. The magnitude of short selling is also correlated to the egregiousness of the misrepresentations. Karpoff and Lou did not find evidence that short selling imposes harm upon investors, but in fact conveys benefits by reducing price inflation for fraudulent issuers, reducing potential losses.[9]

More recently in 2016, Fang et al. conducted a randomized, controlled experiment whereby they analyzed data from the SEC's pilot program where one-third of Russell 3000 index stocks were arbitrarily chosen as pilot companies and exempted from short-sale price tests in order to assess the impact of short sales on earnings management and fraud detection. The analysis found that pilot companies were more likely to be caught committing fraud that began before the program. The lowered cost of short selling in the pilot increased short sellers' incentives to closely scrutinize pilot firms' earnings and uncover misconduct and concurrently, due to the prospect of increased short selling, issuers reduced earnings management. Fang et al. concluded that short selling has a positive impact on issuer business decisions.[10]

As a short seller, the empirical data resonates strongly with my own experiences—logic and objectivity are fortunately not only reserved for the Ivory Tower. Those charged with market oversight must see this body of evidence with eyes wide open. Short selling, writ large, affords positive externalities on the broader market, and more specifically to the investors which regulators have a duty to protect. I also reiterate that the data does not support the existence of any material level of short seller manipulation. Dyck et

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[9] Karpoff, J. M., & Lou, X. (2010). Short sellers and financial misconduct. The Journal of Finance, 65(5), 1879-1913.

[10] Fang, V. W., Huang, A. H., & Karpoff, J. M. (2016). Short selling and earnings management: A controlled experiment. The Journal of Finance, 71(3), 1251-1294.

al. explain how fraud detection rarely begins with standard corporate governance actors, but instead with those who have monetary incentives to uncover and reveal fraud.[11] Interpreting this finding in the context of the empirical studies I have cited above, in markets where short selling is allowed to persist as any other trading, there is an implicit first line of defense against fraud and subsequent losses. And because of these de facto watchdogs, issuers are disincentivized to engage in fraud as they are more likely to face real economic repercussions. Problems arise when this natural check on fraud is artificially restricted.

Short Sale Bans Fan the Flames

The propagation of short selling mythology, while deliberately ignoring the data that categorically dismantles those myths, is perilous. In times of crisis this perspective is often conducive to short-sighted decisions such as banning or significantly restricting short seller activity. Perhaps such measures may temporarily stop a decline in price, but ultimately exacerbate losses by delaying effective price discovery and emboldening fraudulent executives to maintain criminal behavior with the confidence of regulatory protection and short seller banishment. I am not alone in this belief. Staff of the IMF, of which Germany is a prominent member, write, “There is little evidence on the effectiveness of short sale bans… market efficiency and quality in fact deteriorated substantially following the introduction of the various bans.”[12] Even former SEC Chairman, Christopher Cox, whose actions prompted global bans on short sales in 2008 later acknowledged, “Knowing what we know now, I believe on balance the Commission would not do it again. The costs appear to outweigh the benefits.”[13]

With the stratospheric rise in equity valuations these past ten years, some have forgotten the lessons of the Great Financial Crisis. However, such a fugue is inexcusable for those charged with market regulation. In Beber and Pagano’s 2013 study of the evidence from short selling bans around the world during the Crisis, they conclude that the main benefit of the ban has been in “…generating a large amount of evidence about the effects… It is to be hoped that this lesson will be remembered when security markets face the next crisis.”[14] In line with previously cited literature, they discuss the detrimental market impact of the ban, but state further that the effects were even greater in markets outside of the US and resulted in

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[11] Dyck, A., Morse, A., & Zingales, L. (2010). Who blows the whistle on corporate fraud?. *The Journal of Finance*, *65*(6), 2213-2253.

[12] “IMF Staff Comments on EU Commission Consultation on Short Selling.” *IMF*, 5 Aug. 2010, www.imf.org/external/np/eur/2010/pdf/080510.pdf.

[13] Younglai R (2008) SEC chief has regrets over short-selling ban. In: Reuters. https://www.reuters.com/article/us-sec-cox/sec-chief-has-regrets-over-short-selling-ban-idUSTRE4BU3GG20081231.

[14] Beber, A., & Pagano, M. (2013). Short-selling bans around the world: Evidence from the 2007–09 crisis. The Journal of Finance, 68(1), 343-381.

lower returns for non-US countries. Marsh and Payne studied the UK's ban, a market similar to Germany, and found that liquidity was drained, trading costs increased, and there was reduced market efficiency as the trading process became less informative.[15]

Putting aside all issuer-specific information, the data and corresponding objective analyses indicate that short selling is critically beneficial to markets and historical attempts to stymie it have had deleterious, counter-productive repercussions. Regulators, including BaFin, are tasked with market oversight. When perceived market crises occur, regulators must not act impulsively with haphazard attempts to cater to biased parties—whether that's issuers, shareholders, or short sellers. There is sufficient evidence available with which regulators can make informed decisions that will help curtail market losses. Banning short sales, regardless of circumstance, is among the most ineffective ways of doing so.

The peculiar case of banning short sales in Wirecard AG raises serious questions over BaFin's intent. The ban has effectively tampered the free flow of information, related to potential fraud and misconduct at Wirecard. The release of this information ultimately benefits shareholders who deserve the opportunity to assess a company's true value without disruptive regulatory overreach. The simultaneous actions taken to investigate mainstream, credible news agencies reporting on Wirecard may prevent additional whistleblowers from coming forward with price-critical information. In the context of near-universal denouncement of absolute short sale bans, with the data-driven support of the informational advantage short sellers provide, BaFin's rationale for the ban is anemic at best, contrived at worst.

BaFin's Bizarre, Backwards Ban

On January 30th, 2019, only hours after Wirecard stock fell significantly on a dismal fourth quarter earnings preview, The Financial Times reported that a Wirecard senior executive was suspected of using forged, fraudulent contracts for suspicious transactions, potentially inflating Wirecard Asia revenues.[16] Unsurprisingly, Wirecard stock continued to fall. Then, in a reprehensible ode to today's press vilification, Wirecard called the report "…false, inaccurate, misleading, and defamatory… lacks any substance and is completely meaningless."[17] Immediately the following day, BaFin stated that it will look into Wirecard's share decline for signs of possible stock market manipulation.[18]

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[15] Marsh, I. W., & Payne, R. (2012). Banning short sales and market quality: The UK's experience. *Journal of Banking & Finance*, *36*(7), 1975-1986.

[16] Crum D, & Palma S (2019) Executive at Wirecard suspected of using forged contracts. In: Financial Times. https://www.ft.com/content/03a5e318-2479-11e9-8ce6-5db4543da632.

[17] Valero M (2019) Wirecard Falls Most Since '16 After FT Reports Alleged Fraud. In: Bloomberg Terminal.

[18] Comfort N (2019) Bafin to Check for Market Manipulation in Wirecard News. In: Bloomberg Terminal.

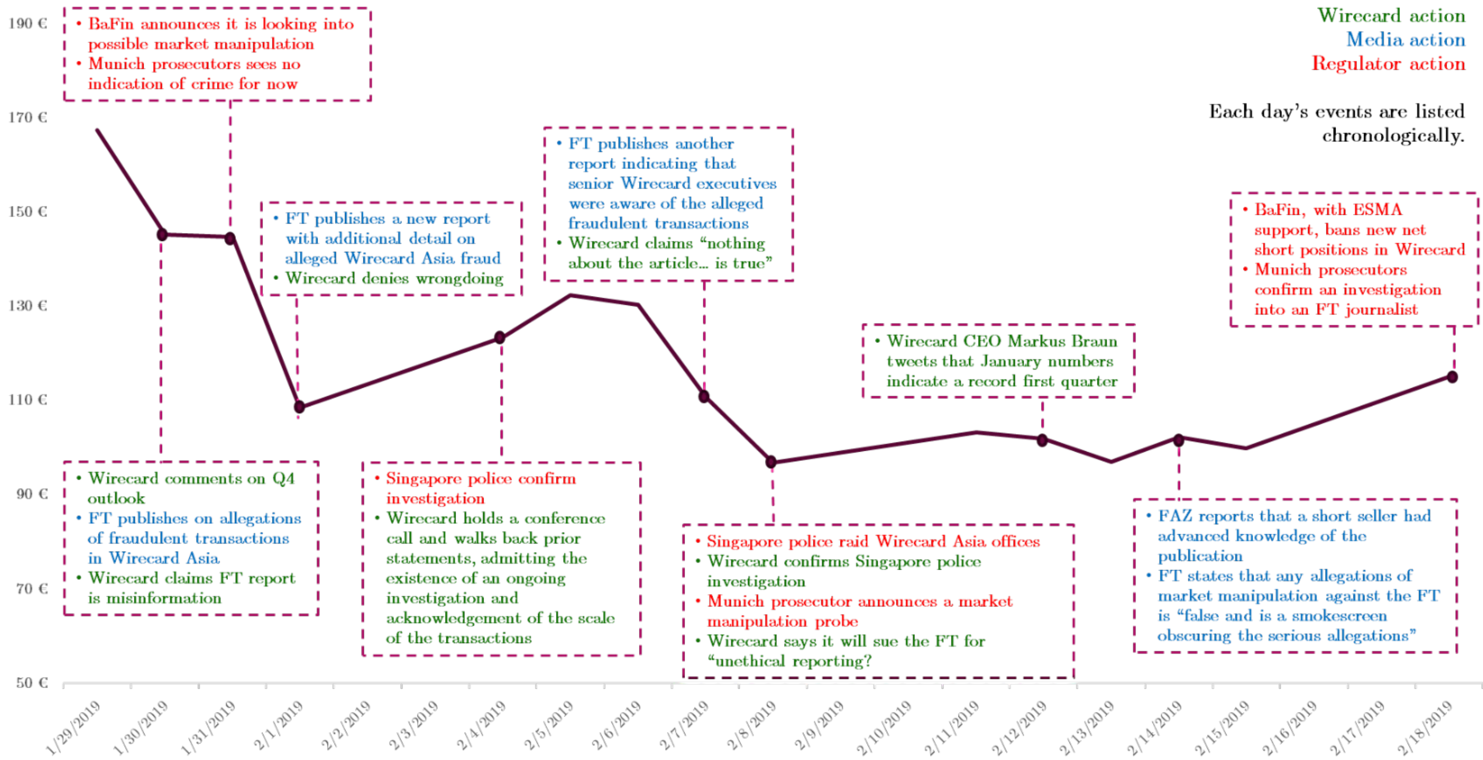

Figure One. Chronology of Key Events Leading to a Ban in Wirecard Short Sales[19]

On January 30th, Wirecard shares fell just 13% despite investor disappointment on weak fundamentals, emerging information related to potential fraud from internal Wirecard employees, and a dizzying near 300% share rally since January 30th, 2014. I ask you if BaFin was aware of these elementary facts when it evoked the short selling Bogeyman through its "market manipulation" probe. I am a proud participant in various public markets globally and until January 30th, I had never seen a regulator—on such an immaterial price decline—so prematurely provide tacit support to an issuer facing serious allegations of fraud while demonizing the financial media. Prior to that date, I naively believed such behavior was reserved for the dregs of online investment forums – deconstructive discourse that I avoid.

And unfortunately, as the allegations continued, the regulatory discourse further deteriorated into conspiracy theory and an eschewal the basic duty of investigating legitimate allegations of corporate fraud. Figure One above shows the key events that preceded your decision to ban short sales of Wirecard. Consistently over that period, BaFin and the German public prosecutor's statements appear almost perfectly prompted by Wirecard's varied empty rejections to the FT's allegations, even after Wirecard itself made some admissions. Just as the stock began to creep below 100€ after Singapore police confirm a raid at Wirecard Asia offices, the public prosecutor announced a market manipulation probe and

[19] Various News Sources (2019) Wirecard Annotated Daily News Over Time. In: Bloomberg Terminal.

Wirecard followed up with threats to sue the Financial Times. Meanwhile, Markus Braun, Wirecard CEO, perhaps in an attempt to salvage Wirecard price further, teases the market about a "record" first quarter. I ask you, is BaFin investigating Braun for market manipulation? In the United States, the SEC is unafraid of investigating and suing executives for their use of social media to abuse the market. Braun seems invigorated after Wirecard, for over a year, provided no disclosure regarding the investigation and to this day continues to minimize the implications it has on the broader business, even though very senior level executives at Wirecard headquarters and Wirecard Asia are alleged to be a part of the scheme. If indeed executives are implicated, then that would serve as indication of greater systemic, tone at the top issues which are material to investors and should be addressed with gravity and transparency.

I appeal to your sense of integrity and innate understanding of the profundity of your actions and how they can set a precedent for decades to come. The discourse leading to the ban and the divergence of Singapore and German regulatory action, enveloped in Wirecard's facile dismissals of serious allegations of fraud is inarguably problematic. What is even greater cause for concern was BaFin's decision to waive the standard procedure of holding a hearing and instead put the ban into immediate effect. While we have previously discussed that you cannot provide further evidence on the factors that led you to your decision, I believe you have a responsibility to financial markets to provide further clarity on why you broke protocol given the widespread impact it has had.

Until then, I will focus on an objective discussion of the facts you have outlined in your rationale for instituting the ban.

You qualify the highly unusual decision by stating that you are only banning any uncovered short sales and preventing an increase in aggregate net short positions, excepting market makers, thereby avoiding detriment to market efficiency. I ask that you refamiliarize yourself with the concept of market efficiency. Liquidity is but one variable. If you will recall from what I discussed above, short selling largely promotes market efficiency through its informational content. Most critically, short selling directionally informs valuations and is a key indicator for fraud. BaFin therefore cannot credibly claim it has preserved efficient markets because the ban, which comes on the heels of serious revelations of price-critical information, prevents market participants from reassessing the value of Wirecard, robbing the market of a key catalyst for price discovery. I reiterate, BaFin's actions have done just the opposite of promote an efficient market.

You further state that the ban will not have far-reaching market impact within Germany. Yet, you also argue that the price and volatility of Wirecard will have far-reaching market impact and necessitates a ban. Not only are both statements contradictory, neither statement is fully accurate.

Wirecard, as you've described is a global payment processor and the vast majority of its business is done overseas—in fact, it was this precise point that was used by your colleagues at the public prosecutor's office to avoid investigating the Wirecard Asia suspicious transactions. BaFin cannot alter its interpretation of the facts to arrive at a convenient conclusion, whether for themselves or interested parties such as Wirecard. Facts are simply facts. Germany has other domestic issuers, whose businesses largely impacted German consumers and financial markets, with similar if not greater levels of share declines.

We examined all DAX components, with the addition of Commerzbank AG which Wirecard replaced late last year. We pulled data ending the day of the Wirecard short sale ban. Just a precursory glance at Figure Two below shows that the vast majority of DAX components underperformed Wirecard in just the past year and not a single issuer's five-year returns can approach Wirecard's. BaFin is correct that Wirecard's volatility is higher than usual, but volatility is a simple measure of dispersion and given Wirecard's returns, the risk appears skewed towards the upside. Wirecard's price has increased rapidly, by a wide margin compared to the DAX, while it is the most expensive DAX stock on a price to earnings basis—all factors which contribute to the stock's extreme volatility.

We went on to calculate a Ban Score (BS) for each issuer that takes one-year and five-year returns and volatility and determines the quartile each issuer falls within, so if in the top quartile for five-year average volatility, an issuer is given a "4" for that factor, and scores are then summed across all four factors so the highest possible score is a 16. Figure Three below shows each issuer's BS and the general distribution of these scores. While this is an incredibly rudimentary descriptive, it does categorize the various DAX components by the factor risks BaFin seems to have considered. Thirteen issuers share a similar BS as Wirecard. Many of these issuers have also faced significant headline risk in the relevant period. These factors do not indicate anything particularly anomalous about Wirecard and the stock behavior is not dissimilar to other technology or growth companies. Wirecard's extreme volatility is not a recent phenomenon, so again I fail to see how someone could have used this data to come to such a wildly different conclusion.

Did BaFin, after witnessing the carnage brought on by these other investigations, decide that it would not allow the same to occur to yet another domestic issuer? If true, BaFin has created a closed market where it does not serve as neutral oversight, but instead singlehandedly dictates price. A regulator's duty of care to the markets is not to ensure perennially upward pricing, but to eliminate market abuses, such as fraud or market manipulation, so that prices are ultimately indicative of value. Perhaps if BaFin wants to inflate prices of Wirecard, it should lobby government to create a sovereign wealth fund to own shares of Wirecard, or any other German issuer whose shares expectedly fall after legitimate questions are raised.

What is also disappointing about BaFin's rationale is its insistence that Germany is singled out by short sellers. The transparency required for short sales in European markets naturally deter some short sales, relative to markets like the US. Bloomberg recently reported that over the past five years, Germany has lagged all major markets in the number of activist short seller campaigns, as shown in Figure Four below.

Developed markets regulators, such as the SEC, generally use activist commentary and mainstream news to inform their investigative process and to identify companies that may benefit from further disclosure or other legal remedies to protect shareholders. These actions are motivated by the fact greater transparency and information leads to healthier markets.

Meanwhile, BaFin exposes an entirely aberrant perspective when it states, "Only such an extended prohibition will ensure that the share price of Wirecard AG is not adversely affected in the current situation…" What consideration does BaFin afford shareholders that will have significant losses to bear if the allegations against Wirecard AG are found to be even partially true? BaFin continues a victimhood narrative stating that short sellers profiting from their investments pose "a risk to market integrity in Germany and to trust in fair and efficient price determination."[20] This is perhaps the single most dangerous statement of all as it lays bare BaFin's willful blindness and bias towards sheltering domestic corporations, even if they are engaged in fraud.

I agree with BaFin that recent Wirecard-related activity does pose a dire threat to German markets. Market participants are quickly realizing that German regulators cannot be relied upon to effectively or objectively engage with the markets and are deliberately besmirching their fundamental duties. When such a degree of doubt is introduced as far as regulatory intent, market integrity quickly disintegrates.

[20] "Wirecard AG: General Administrative Act on the prohibition on establishing and increasing of net short positions." BaFin, 18 Feb. 2019, https://www.bafin.de/.

Ticker	Issuer Name	1-Year Total Return (2/18/19)	1-Year Average Volatility (2/18/19)	Price to Earnings Multiple	5-Year Total Return (2/18/2014-2/18/2019)	YTD Total Reeturn (to 2/18/19)	5-Year Average Volatility (2/18/2014-2/18/2019)
CBK	Commerzbank AG	-47.38%	15.87%	8.23	-47.73%	16.38%	33.90%
TKA	thyssenkrupp AG	-42.40%	7.01%	--	-32.73%	-12.14%	31.30%
1COV	Covestro AG	-41.85%	12.62%	4.56	--	17.97%	30.03%
DBK	Deutsche Bank AG	-39.34%	12.61%	--	-72.72%	11.32%	34.34%
CON	Continental AG	-38.73%	7.94%	8.33	-10.10%	14.58%	26.19%
BAYN	Bayer AG	-27.74%	7.99%	33.64	-23.37%	12.55%	25.34%
DPW	Deutsche Post AG	-27.68%	4.37%	14.15	14.71%	9.20%	21.91%
DAI	Daimler AG	-26.60%	16.77%	6.77	-6.37%	9.78%	23.50%
FRE	Fresenius SE & Co KGaA	-25.42%	-1.96%	11.61	25.19%	11.30%	24.84%
HEI	HeidelbergCement AG	-24.33%	4.68%	18.49	17.17%	16.49%	24.11%
FME	Fresenius Medical Care AG & Co	-21.17%	-3.10%	8.75	36.59%	20.83%	23.33%
BAS	BASF SE	-20.99%	6.62%	14.08	-4.82%	9.50%	21.65%
HEN3	Henkel AG & Co KGaA	-17.16%	15.16%	17.97	12.46%	-7.46%	19.46%
BMW	Bayerische Motoren Werke AG	-16.28%	0.98%	6.62	0.17%	-0.16%	23.84%
LHA	Deutsche Lufthansa AG	-14.87%	0.22%	6.11	34.56%	12.03%	31.41%
VOW3	Volkswagen AG	-12.71%	0.39%	5.90	-23.39%	2.75%	30.00%
SIE	Siemens AG	-12.19%	-0.60%	15.80	17.83%	0.25%	21.37%
DAX		**-9.26%**	**-1.09%**	**14.45**	**16.97%**	**7.01%**	**17.28%**
IFX	Infineon Technologies AG	-8.82%	-3.19%	18.11	169.16%	14.34%	29.36%
BEI	Beiersdorf AG	0.36%	-1.19%	28.40	29.73%	1.05%	17.96%
ALV	Allianz SE	3.58%	-5.62%	10.05	83.24%	8.21%	19.68%
DB1	Deutsche Boerse AG	7.85%	-6.13%	23.53	119.48%	6.48%	21.58%
ADS	adidas AG	11.66%	-10.86%	21.56	149.62%	8.85%	25.24%
SAP	SAP SE	13.37%	-1.60%	25.42	74.20%	8.37%	19.64%
DTE	Deutsche Telekom AG	14.55%	-4.88%	32.22	41.53%	-2.97%	20.95%
WDI	**Wirecard AG**	**15.77%**	**99.33%**	**44.32**	**253.25%**	**-13.40%**	**33.05%**
MUV2	Muenchener Rueckversicherung	16.95%	-6.96%	12.34	61.68%	6.90%	17.85%
MRK	Merck KGaA	18.00%	-0.73%	36.53	69.79%	7.87%	21.96%
EOAN	E.ON SE	22.15%	-5.76%	6.30	-4.84%	11.72%	27.60%
VNA	Vonovia SE	22.19%	-11.54%	9.05	177.58%	11.72%	20.80%
RWE	RWE AG	50.32%	-2.44%	5.50	-11.16%	17.37%	34.26%
LIN	Linde PLC	--	-8.28%	--	--	8.55%	27.35%

Figure Two. Chart of DAX components and Commerzbank including various factors[21]

[21] Data was sourced from the Bloomberg Terminal. "1-Year Total Return" is calculated by Bloomberg and defined as the one-year total return prior to 2/18/2019. "1-Year Average Volatility" is calculated by Bloomberg and defined as the average 30-day volatility for the one-year period prior to 2/18/2019. "Price to Earnings" multiple is calculated by Bloomberg and is defined as the ratio of the share price and the company's earnings per share. "5-Year Total Return" is calculated by Bloomberg and is the five-year total return prior to 2/18/2019. "5-Year Average Volatility" is calculated by Bloomberg and is defined as the average 30-day volatility for the five-year period prior to 2/18/2019.

Ticker	Issuer	Total Score
BAYN	Bayer AG	11
CBK	Commerzbank AG	11
CON	Continental AG	11
DAI	Daimler AG	11
DBK	Deutsche Bank AG	11
TKA	thyssenkrupp AG	11
WDI	Wirecard AG	11
FRE	Fresenius SE & Co KGaA	10
VOW3	Volkswagen AG	10
BAS	BASF SE	9
BMW	Bayerische Motoren Werke	9
DPW	Deutsche Post AG	9
FME	Fresenius Medical Care AG	9
HEI	HeidelbergCement AG	9
LHA	Deutsche Lufthansa AG	9
1COV	Covestro AG	8

Ticker	Issuer	Total Score
BEI	Beiersdorf AG	8
EOAN	E.ON SE	8
HEN3	Henkel AG & Co KGaA	8
IFX	Infineon Technologies AG	8
RWE	RWE AG	8
SIE	Siemens AG	8
ADS	adidas AG	7
ALV	Allianz SE	7
DTE	Deutsche Telekom AG	7
LIN	Linde PLC	7
MRK	Merck KGaA	7
MUV2	Muenchener Rueckversiche	7
SAP	SAP SE	7
DB1	Deutsche Boerse AG	6
VNA	Vonovia SE	5

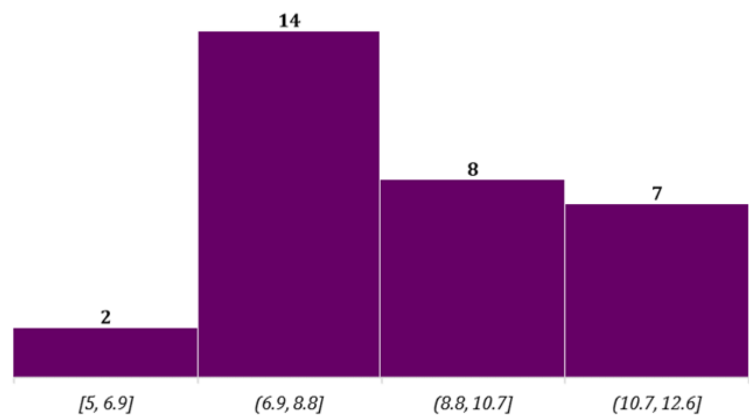

Figure Three. Ban Scores and distribution[22]

[22] Figure Three is a histogram of the calculated ban scores. The data used to calculate the BS was sourced from the data found in Figure Two. To generate the BS, each parameter from Figure Two, excluding Price to Earnings and YTD return, was provided a quartile score ranking from 1-4. Quartile rankings for Total Returns were distributed with 1 being the highest quartile, and thus the highest total return segment. Quartiles were established by calculating the maximum and minimum of the range of the total returns provided and dividing the returns into four equally spaced segments based on the nominal value. For the rankings of 1-Year and 5-Year volatility parameters, the quartiles were reversed, whereby a score of 4 indicated the greatest volatility segment and a score of 1 indicated the lowest volatility segment. The four scores generated for each were summed to provide the final total BS.

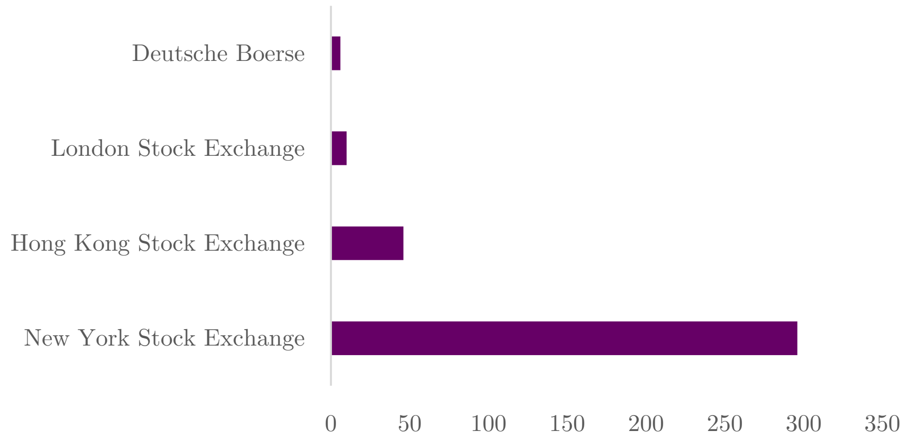

Figure Four. Activist short campaigns by major markets, from 2013-2018, as reported by Bloomberg[23]

The Dangers of Corporate Despotism

From my seat, it is impossible to confirm or evidence the extent of regulatory capture in Germany. However, the actions regulators have taken to combat market manipulation without offering proportionate attention to corporate fraud, is incredibly dangerous and perhaps indicative of a cultural complacency towards equal enforcement of domestic entities. Whether this is nationalism or regulatory capture, only you and your colleagues can reflect on; however, if gone unabated, the risk of corporate despotism increases and regardless of how that may impact my own investing, I do believe it is a negative for the average German and history supports this sentiment.

Regulatory capture is a reality of all economic systems and its existence is not sinister so much as it is a product of our own human fallibilities. Where we must be cautious is when one single source of influence captures a disproportionate amount of power over a regulator. Under-regulation caused by capture is particularly treacherous. Some of the greatest financial calamities from the Great Financial Crisis to Deepwater Horizon were rooted in a breakdown of regulatory enforcement. In 2010, Andrew Baker describes how economic boons disincentivize politicians to correct or dampen corporate risk-taking, while regulators are under-resourced and unable to question the sustainability of the boon, creating a mutually dependent lifecycle. He concludes with dismay that current regulatory reform efforts do not

[23] Pham L (2019) Activist Short-Sellers Are Wary of Germany. Here's Why. In: Bloomberg. https://www.bloomberg.com/news/articles/2019-02-18/activist-shorts-steer-clear-of-germany-as-officials-target-bears.

comprehensively address this “lifecycle” and believes given regulatory capture’s pro-cyclicality, the same lifecycle that led to the Great Financial Crisis may again result in the same outcomes.[24]

Part of the persistence of this lifecycle may be that financial and reputational incentives exist only to continue the cycle, not to slow it down or reverse it. For example, politicians want to maintain corporate success so they may receive greater electoral funding and favorability ratings. Auditors are paid by the corporations and incentivized to maintain or grow their business relationship. Regulators may have previously worked at these corporations or seek to work there following their public service.

Wirecard is a prime economic boon. It has exemplified German market growth and clear incentives exist for regulators to maintain the cycle. However, as a sophisticated and developed regulatory body, BaFin and its enforcement peers should review Wirecard’s lifecycle in the context of other devastating financial collapses in Germany and better understand what actions can be taken now so a doomsday cycle may be avoided. In 2011, Christensen et al. empirically analyzed the capital-market effects of securities regulation in the EU and concluded that stronger securities regulation has significant economic benefits and that the magnitude of these benefits is greater in countries with a history of higher regulatory quality and traditionally stronger securities regulator.[25] BaFin can affect German financial markets more positively by taking a cautious, skeptical perspective on Wirecard’s boon rather than by sustaining the status quo.

With Wirecard, BaFin has finally been presented with forces whose incentives run counter to the boon lifecycle, including financial journalists and short sellers. BaFin should embrace these views as it lends credence and justification for greater enforcement of the darling of the DAX. Hazer Croall in 2004 describes corporate fraud regulation and states that “political will is necessary to develop and implement the kind of sanctions… not only on the basis of deterrence but also to underline the moral and symbolic role of regulation or control… may also be adversely affected where there is a continuing cultural or subcultural tolerance for offenses.”[26]

In this letter, in the investigative reports published by journalists and short sellers alike, the unifying motivation is to bring stricter enforcement to Wirecard because the company may be lying, misleading the markets, and taking advantage of its investors. It may be an unbridled, unprecedented abuse of public

[24] Baker, A. (2010). Restraining regulatory capture? Anglo-America, crisis politics and trajectories of change in global financial governance. International Affairs, 86(3), 647-663.

[25] Christensen, H. B., Hail, L., & Leuz, C. (2011). Capital-market effects of securities regulation: The role of implementation and enforcement. National Bureau of Economic Research.

[26] Croall, H. (2004). Combating financial crime: regulatory versus crime control approaches. Journal of Financial Crime, 11(1), 45-55.

trust—German trust—that BaFin has the opportunity to restore. This is the type of moral regulatory role that Croall alludes to that is most effective at combatting and deterring financial crime.

Short sellers stand to profit if fraud is exposed to the markets and facilitates downwards price discovery. However, this precise economic incentive is why BaFin should listen so carefully to the short selling information traders—the more credible and material this information, the greater profit. The current ban on Wirecard short sales removes this critical incentive. And yet, no market participant is more acutely aware of the criminal repercussions of disseminating misinformation than short sellers.

BaFin's decision unfortunately plays directly to the flourishment of a libertine corporate lifecycle where truth is treated as an illicit currency, journalists and whistleblowers are demonized, while executives are given free rein to act without fear of criminal enforcement. BaFin has the opportunity to steer markets back towards integrity and make strides towards acknowledging and mediating the negative consequences of regulatory capture.

I sincerely hope BaFin takes this into full consideration and I am fully available to you and any regulatory peers to discuss the Wirecard matter or the role of short selling in Germany more generally. I will be submitting copies of this letter to ESMA, who supported your decision, and the SEC as Wirecard depository receipts trade in the US. For public interest and education, I will be making a version of this letter available online in the future.

Please do not hesitate to reach out to me and thank you for your time. I look forward to continuing this discussion and seeing the changes BaFin will make to better protect the market from fraud.

Sincerely yours,

Fahmi Quadir
Founder, Chief Investment Officer
Safkhet Capital Management LLC

CC European Securities and Markets Authority
Securities and Exchange Commission