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HOW MONEY BECAME DANGEROUS

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The world of money used to be simple. A person might have both a checking and a savings account, a home mortgage and a car loan, and maybe some basic investments in the markets, like municipal bonds or shares in Sears, Roebuck or General Motors. But rarely were a person's finances more complex than that. Wall Street wasn't particularly controversial. The financial services industry didn't have a reputation for being impersonal, selfish, and reckless. Most of the time, it was seen as just another facet of a functioning and growing society.

That all started to change rapidly in the 1980s as our financial system became increasingly complicated, with each evolution moving the world of money further beyond the understanding of the general public. Wall Street began to feel like an adversary, an enigmatic and potentially dangerous force controlled by slippery bankers whom we didn't trust. After the mortgage crisis, collapse of banks, and Great Recession of 2008, our wariness boiled over into anger. The system no longer seemed to be working for the average person.

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How did we get here? In just one generation, how did our financial system become so labyrinthine and loaded with peril as we became more disconnected from its workings? Why do we care so little that the national debt is more than $20 trillion and growing? Why do we care so little that our government employee pension system is massively underfunded, with the gap growing wider each year? Why do we care so little that we have grossly insufficient funding for promised Social Security and healthcare benefits? Why do we care so little that student debt stands at $1.6 trillion, weighing down millions of graduates who can't find jobs worthy of their degrees and are incapable of repaying what they owe?

Is it really the case that we don't care about these looming crises, or is it that we feel shackled by our lack of understanding and connection? Whatever the reason, the result is the same. As the world of money continues to become a bigger and bigger part of our lives, we understand it less and less. Everyone talks about sustainability these days—in regard to the environment, or food, or economic matters, or cultural and social issues—but no one is talking about the sustainability of our financial system, despite the fact that it occupies such a prominent place in our human existence and future well-being. This is the most important discussion that we are not yet having.

If we stand by, remaining disengaged from the world of money, we are headed to a dangerous place. Regardless of your background or occupation, this will affect you in your lifetime, most assuredly altering your children's quality of life. It is imperative that we increase our knowledge and engagement with the financial world and change the current trajectory. Otherwise it will end badly for us all.

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My first exposure to the financial world was in 1970 in the second grade, when Mr. Samson, the manager of Springfield Savings and Loan, came to speak to our class about banks. There was nothing exotic about Mr. Samson; he wore a gray suit, red tie, and shiny grown-up shoes. He circled the room with a stack of booklets, passing one to each of us. On the cover, the logo of the bank was printed, along with a place for me to scrawl my name. I flipped through its pages of unfilled lines and boxes, each page backed by the ghosted portrait of a US president. As we inspected our booklets, Mr. Samson instructed us to pull out the dimes we'd been asked to bring to class. Mine had been burning a hole in my pocket all day.

"Those dimes," he said, "are your first deposit. If you bring in a dime every week, I'll come by on Fridays to collect them and give you a stamp for your book, then I'll deposit your money in the bank. While it's in the bank, your money will collect interest, which means we'll reward your account with a little bonus each month. And during the time your money is with us, we might use it for other purposes, such as loaning it out to people who are opening a new shop or buying a house. Any time you want to withdraw your money, you just come down to see us. But if you leave it alone and let it grow, after time, you'll have accumulated savings."

Our teacher told us to line up. At the table in the front of the room, Mr. Samson collected our dimes in a black leather bag and stamped the first pages of our books to verify our deposits.

"There are thirty weeks left in the school year," he said. "If you bring in your dime every week, you'll have saved three dollars by summer break."

We were floored by the prospect that we could someday possess that much money. Back at my desk, I quickly calculated how much I could save if I did this for three additional years, until the end of fifth grade. Three plus three plus three plus three. Whoa—I could have twelve dollars. From that day on, I brought in my dime every week, without fail, and assiduously filled my book with stamps.

My parents' experience with money wasn't much more complicated than what Mr. Samson taught us that day in second grade. Back then, in the late 1960s, when their friends paid off their mortgages, they would often throw a party at which they would burn their mortgage slips. Finance was simple enough that the common path for a family was to purchase a home, dutifully work to pay down the mortgage, then enjoy an easier retirement. That level of simplicity is almost unheard of today.

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We spend so much time worrying about money now—almost around the clock—and I can't say that makes us better off. Yet on the flip side, there was a time not too long ago when we didn't have the many advantages the financial world now provides. For example, mortgages weren't widely available to the general public. If you wanted to buy a house, you had to save up the entire purchase price. So the increase in complexity in the financial world has also brought with it products that have made many people's lives better. Modern finance always seems a double-edged sword, which is why the universe of money has long intrigued me.

I got my first glimpse of the dangerous side of money in high school, when my family moved from Springfield, Massachusetts, to Orange County, California. My father had been offered a new job as CEO of a company that had been acquired in a leveraged buyout. I vividly recall him distraught at the dinner table, talking about how interest rates had skyrocketed, and as a result, he was forced to cut costs at his new company in order to service the debt. Cutting costs meant cutting jobs, and my father felt a heavy responsibility for his employees and concern for their families. At that young age, seeing the effect of those pressures on my father and his company, I had little understanding of leveraged buyouts and the movement of interest rates, yet I was filled with apprehension—what would happen to the people who lost their jobs due to the cutbacks? How did those larger, external economic factors force my father to make uncomfortable and unpopular decisions? It would take years before I could begin to understand these concepts and their impact on people's lives.

Ending up working in finance, however, surprised me at first, because I've never had the cutthroat personality for which Wall Street is notorious—I worked at Disneyland while studying liberal arts at Occidental College—nor have I ever developed a lust for fast cars, fancy watches, and vacation houses, the tokens of status and accomplishment that are the trophies of the banking world. I simply loved the work. And I've been lucky enough to have a role in or a ringside seat for many of the big financial moments over the past three decades. After college in the 1980s, I started as a corporate lending officer for Bank of America, loaning money to gold and diamond wholesalers in LA's jewelry district, then attended The Wharton School. I landed at Salomon Brothers in the 1990s, working my way from the trading floor through the investment bank until I served as the global head of Citi's TMT (technology, media, and telecom) group, head of the National Investment Bank and the regional offices, as well as Citi's first culture czar. After twenty years, I left Wall Street to cofound a private equity firm in Silicon Valley.

I was an unlikely person to end up in these positions. Both sides of my family were Greek immigrants from Sparta. We led a normal middle-class life. As a teenager, to save for college, I not only worked at Disneyland but a slew of other odd jobs, from pool cleaner to peanut vendor. I definitely was not on the career track for Wall Street, nor did I know that such a track existed. But, in ending up there, I found that my unorthodox background gave me a unique perspective as someone who has, at times, been an insider, an outsider, a participant, and a skeptical observer.

I'm not claiming to be the only person with such proximity to the big moments in finance over the past three decades, but it is not a large group, and I may be one of the few who thought to chronicle each event as it happened. I'm certainly the only one who started off his Wall Street career wearing a polka dot vest and bow tie at Disneyland.

In our contemporary discourse, there are defenders of Wall Street and there are condemners, with few in between. The defenders argue that Wall Street should be appreciated for providing our modern world with the opportunities and advantages that most of us enjoy, from the financing of bridges and public schools to the issuance of home mortgages and small business loans. For the defenders, Wall Street is undeniably a force for good. The condemners stand defiantly on the opposite end of the spectrum. To them, Wall Street has poison in its veins. They believe that its corruption and greed are solely responsible for the 2008 Great Recession and most of the evils visited upon a defenseless population. The system is irredeemable, they say, and needs to be torn down.

The chasm between these two groups is vast and growing. But could it be that the truth lies somewhere in the middle? Could Wall Street be both necessary and troubled, essential to a functioning society and yet increasingly difficult to understand and govern?

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The majority of the big changes in the financial world over the past thirty-plus years were initially made with good intentions and, for a time, resulted in the betterment of society. There's an industry saying: "Every bad idea on Wall Street started as a good idea." Those changes were ultimately pushed too far until, in the end, each change became a manifestation of both good and bad forces, both beneficial and destructive. Recognizing these contradictions is key to our finding a positive and effective path forward. Here are a few key examples of how evolutions in our financial system can achieve great progress while also leading to undesired behaviors and outcomes:

In the 1980s, the introduction of the computer spreadsheet unleashed the creative energy of the financial industry, while helping to eliminate human subjectivity and biases.

And yet…

The computer spreadsheet led to the erosion of analytical integrity and the loss of character.

In the early 1990s, many Wall Street partnerships began to go public, allowing them to obtain the capital required to achieve the scale necessary to offer the products and services demanded by increasingly large corporations and clients.

And yet…

The separation of risk from accountability led to the diminution of oversight, which in turn led to destructive behaviors, including the ability to make dangerously large bets with other people's money.

In the '80s, corporate raiders and activist investors recharged American and global business by holding management teams accountable for their performance.

And yet …

When corporations were forced to pursue shareholder value over all else, that allowed for rationalizing management decisions that inappropriately prioritized profit over people and product.

Speed and precision have enabled the creation of new products and made markets more efficient, increasing access and lowering costs.

And yet …

Speed, efficiency, and perceived precision have supplanted thoughtful, careful analysis in all areas of finance, including those best served by analytical reflection.

Public company reporting requirements have increased transparency in the financial system, making progress toward leveling the playing field for all investors.

And yet …

Those same reporting requirements have further compressed the measurement period of financial performance used by public investors and management teams, all at the expense of long-term investment and vision.

The construction of financial supermarkets created platforms capable of efficiently delivering the breadth and depth of products demanded by increasingly vast and complex international businesses and markets in a globalizing world.

And yet …

The advent of financial supermarkets led to the creation of financial institutions that are unwieldy and challenging to manage, as well as to the deterioration of the corporate culture needed to foster and sustain desired behaviors.

Commerce moving to the cloud facilitated the creation of new products and markets at prices that made them widely accessible to the general public.

And yet …

The move of commerce to the cloud has contributed to the loss of community and personal connectivity.

There's an industry saying: "Every bad idea on Wall Street started as a good idea."

Increased compensation transparency has shifted negotiation leverage to employees, empowering individuals with the data to support demands for fair market compensation.

And yet …

That same transparency has led to the shortening of investment horizons and an unhealthy focus on compensation as the primary determinant of one's worth in society.

The market economy's takeover of the social order has empowered the amateur, democratized advertising and media, and opened up a larger world to people who may not otherwise have had access.

And yet …

The market economy's takeover of the social order has replaced meritocracy and community with an unhealthy pursuit of exclusive access and special privilege.

The disconnection of the populace from public finance has allowed for elected officials to manage more efficiently the complexities of funding government operations, for which the public does not have the time, background, or desire to provide input or oversight.

And yet …

That same disconnection has created a vacuum of accountability and oversight in public finance, often leading to irresponsible decisions that prove destructive.

The tradeoffs inherent in each evolutionary change help explain why reaching a consensus on the way forward is so difficult. Where some see only an industry serving important needs, others see only hazard. Both viewpoints, to a certain degree, are correct. Yet rather than work to appreciate the dichotomies of modern money, our public discourse has failed us, and so we're in a standoff between those who believe the financial industry to be vital to a functioning world, and those who believe it to be a dangerous beast that must be contained or euthanized if we are to avoid repeated crises.

This tendency toward extremes has yielded an industry without leadership or oversight that is producing large financial and social bubbles, which continue to swell to potentially catastrophic levels. Ultimately, each bubble will burst, with a tipping point impossible to predict. These cycles will inflict their damage time and again, with increasing intensity, as long as we lack the leadership needed to tackle these intractable challenges and as long as we remain detached from the workings of the financial world. The truth is that these cycles of boom and bust are a necessity if we are to have the freedom to innovate, create, and compete. And our system has usually proven resilient, bouncing back after most challenges, but the challenges highlighted here possess the potential to push bubbles to a point where the center does not hold and the system breaks. How do we achieve a healthier balance in which the swings from prosperity to crash are less extreme and destructive? There are no easy solutions, and no one person, entity, or action is going to fix these problems for us. We need a constructive discussion between the disparate corners of our culture, so we can work toward creating the financial system on which a healthy society must rely, one that serves the interests of the people by supporting the basic necessities of life and the pursuit of dreams and aspirations. Our success and failure as a society are directly connected with how our financial system is constructed and managed.

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By the time I reached high school in Orange County, I no longer brought dimes to class, but Mr. Samson's lesson had stuck with me, and I'd continued to save and deposit income from various jobs—mowing lawns, washing cars, cleaning the neighborhood pool each Saturday morning. As graduation neared, I found that I'd amassed two hundred dollars, which sat in a savings account accumulating interest. I left it alone until four years later, on the cusp of finishing college, when I was home visiting my parents. I was about to begin my first job postgraduation, working at Bank of America as a corporate lending officer, and I figured it would be a good idea to move my account from the regional Orange County bank to that of my new employer. As I entered the lobby, I could only imagine what my balance had become after four years of steady growth. A two-hundred-dollar savings account wasn't going to buy me a house or nice car, but I expected it might have swelled into a decent chunk of change.

After waiting in the teller line, I was directed to see a bank officer. I settled into a chair across the desk from him. "Name and account number?" he said without looking at me as he typed my information into his computer. It must have been 45 degrees in the bank; the air-conditioning was running full tilt. "I'd like to withdraw my funds," I said, with a twinge of anticipation, or perhaps it was a shiver from the blast of cold air descending on us.

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The man stared into his monitor. "That account," he said, with an excruciatingly long pause, "is empty."

"What? How could that be?"

He swiveled his head and regarded me over the top of his glasses. "There were no funds in the account. So it was closed."

"But I haven't touched that money for four years."

He studied his computer terminal again. "It looks as though a fee was initiated two years ago," he said, "of ten dollars per month, and eventually your balance was zeroed out by the service charges."

While it was only two hundred dollars, the loss of that money meant more to me than any other financial loss later in life, no matter the amount. I had done so much to save that money. To have it wiped out in such a callous, impersonal way made me start to question the institution that I had long trusted. **The situation seemed unfair, but I didn't have enough knowledge or experience to articulate why that was so. I looked across the desk at this bank officer, unsure of what to say. And he didn't seem to have anything more to say to me. So I left, climbed into my old hand-me-down car, and drove away, thinking back on those halcyon days of saved dimes and neighborhood jobs, of the friendly smile of Mr. Samson and my naïve trust that the system cared, somehow, about my well-being.**

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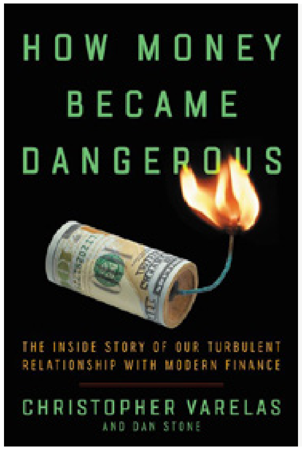

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Responsible for brokering some of the biggest mergers and acquisitions in finance, **Chris Varelas** was listed among the top 100 dealmakers by the New York Times and was named top technology rainmaker by DealMakers Monthly magazine. After working as Citi's head of technology, media, and telecommunications during the first dot-com boom and then leading the company's national investment bank and regional offices, Varelas left Citi in 2008 to cofound Riverwood Capital, a premier private equity firm in Silicon Valley.

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