Liar's Poker: Rising Through the Wreckage on Wall Street Study Guide

Liar's Poker: Rising Through the Wreckage on Wall Street by Michael Lewis (author)

Contents

Plot Summary

This semi-autobiographical non-fiction work is published in 1989. Liar's Poker relates actions and events that occur primarily in New York and London from the years 1979 to 1988. Michael Lewis writes about the experiences, traits and character of managers, employees, customers and competitors of Salomon Brothers Wall Street investment bank. He writes from his own experience as job applicant, trainee and bond salesman to 1988. This short successful career account with Salomon from 1985 to 1988 is enhanced with a condensed history of the Salomon mortgage bond trading department startup from 1979. Salomon's rapid growth to the leading Wall Street mortgage bond firm by the mid-1980s is described. Salomon's loss of the bond trading led to a competitive Michael Milken's startup junk bond department for Drexel Burnham is also portrayed.

The author leaves Salomon Brothers in 1988 at twenty-seven years old for other interests. This is an insider's story of his experiences with friends and colleagues at a multi-billion dollar Wall Street investment firm. His subtitle "Rising Through the Wreckage on Wall Street" describes the story of an era when traders master a quick killing. Michael Lewis describes the center of a modern day gold rush where twenty-four-year-olds with little skill or experiences make more money than ever before trading and selling million dollar investments. Michael leaves after three successful years because he professes "it would be better to tell the story than to go on living the story."

This 249-page non-fiction book is comprised of eleven chapters plus a preface and epilogue. Chapter lengths are short with descriptive titles that are straightforward and readily understandable. Titles clearly state what the chapter is about and provide a touch of humor such as, "The Fat Men and Their Marvelous Money Machine" followed by "The Salomon Diet." Michael Lewis mixes personal experiences and technical jargon that makes the story easy to understand and a pleasure to read. The author uses literary techniques of flashback and perspective to develop reader understanding of the history and timeline. A blend of lighthearted humor and anecdote is colorful and enlivening to describe characters; i.e., bond traders that by profession and legend are a "boor" at parties. Lewis brings their personalities to life. His free-form style of telling stories before, after and within other tales could create confusing timelines that Lewis' writing approach is able to avoid.

Liar's Poker

Liar's Poker Summary and Analysis

Liar's Poker relates actions and events that occur primarily in New York and London from the years 1979 to 1988. Michael Lewis writes about the experiences, traits and character of managers, employees, customers and competitors of Salomon Brothers Wall Street investment bank. He writes from his own experience as job applicant, trainee and bond salesman to 1988.

Early in 1986, John Gutfreund, Chairman of the declining Salomon Brothers investment firm, walks around the trading floor to gather information about the day's business. His meanderings about the department are disconcerting to the traders who feel a need to be busy as he approaches. Ironically his name is pronounced "Good friend" but he stirs fear like a grizzly bear in silent approach to a small animal. He may not say anything but the telltale expensive cigar ash he drops shows his presence. The King of Wall Street's $40 million gain on the sale of Salomon and his $3.1 million salary is greater than any other Wall Street CEO. On this day he walks directly to the trading desk of John Meriwether, a bond trader and fellow board member of Salomon Inc. to place a bet.

Gutfreund becomes a legend by saying, "One hand, one million dollars, no tears." He wants to play one hand of Liar's Poker for a million dollars. The six bond traders and Meriwether regularly play with the outmatched Gutfreund but his million dollar bet is way over his normal loss of a few hundred dollars. Meriwether is King of the Game and champion Liar's Poker player. The comment "no tears" by Gutfreund is puzzling since it means the loser expects a lot of pain with no complaining. The author notes he wants to be one of the boys by displaying courage. Meriwether alone has enough cash and daring to meet Gutfreund's bet. The trader controls his emotions and expressions of fear and greed, which makes him the best bond trader on Wall Street and a dangerous Liar's Poker player. Most of the six traders working for Meriwether have Ph.D.s but are obsessed with the game. Gutfreund is once a trader but is now an outsider in the game. Since becoming manager he knows he is hostage to the producing traders who take risks to make money for the company. A high stakes hand of Liar's Poker shows he can still be a player too.

Liar's Poker is played by two to ten players gathered around in a circle. Each player has a dollar bill with a serial number he uses to fool the other players by making a bet like the card game "I Doubt It." The opening player states a number or numbers he wagers is in the other players' hidden bills serial number. The player to the left of the opening bidder can bid higher by either the same quantity of a higher number or a greater quantity of any number. Alternatively he can challenge the outstanding bid. Bidding continues until all players agree to challenge one player's bid. The players then show their dollar bill serial numbers to reveal who is bluffing. Probabilities of recurrent numbers in random serial numbers are estimated to evaluate risks as they play. Bond traders in several Wall Street firms play a version of Liar's Poker but stakes are highest on Meriwether's trading floor.

Meriwether's player code requires all challenges be accepted but he is in a no-win situation. Winning the game upsets Gutfreund, his boss, but losing the game costs a million, which is worse. Meriwether counteroffers a $10 million wager that bluffs Gutfreund into declining. Gutfreund tells Meriwether he's crazy but they both realize this is a win-win. They play a wagered hand without starting a game. Liar's Poker is a metaphor for investing with Salomon and other Wall Street investment banks. Ironically, customers of the firm are unwitting but regular players in the hands of Liar's Poker.

Never Mention Money

Never Mention Money Summary and Analysis

Prior to employment with Salomon Brothers, the author, Mike Lewis is a twenty-four year old student living in London in 1984. He attends the London School of Economics to complete his master's degree in economics. His cousin is the wife of a German baron. She provides an invitation to a black tie fund-raising dinner held by the queen mother at St. James Palace. The senior managing director's wife dines at the same table with Mike. She asks about his plans for a job. He comments on investment banking and she asks why he doesn't come to work at Salomon Brothers trading. Mike replies that John Gutfreund's rough and tumble trading floor does not sound like fun compared to his image of investment banking. She asks if he wants to spend all day in an office, where is his chutzpah and if he is a numbnut. Mike asks if she is authorized to offer a job and she says her husband will take care of it. The queen mother passes with her corgis and the wife shouts out how nice her dogs are. Mike is convinced the "crude, rude, and socially unacceptable" culture of Salomon Brothers is the kind of investment banker that could be his people. Her husband shows him the London offices.

Leo Corbett is the head of Salomon New York recruiting and meets him for breakfast a few days later. They get along well during breakfast but no job offer is made. Mike discovers they do not make job offers but ironically he can take the job. Leo Corbett is pleased to get Mike's call to take the job and schedules him for training with the other trainees in July. Leo does not mention pay. Mike is aware of recruiting, interviewing and hiring steps that six thousand other applicants undergo that year. He is ashamed to be hired through connections but not as much as being unemployed. Mike recalls how discouraging it is to apply for an investment banking analyst job in 1981 as a senior at Princeton. Trading is not considered when compared to a prestigious sounding analyst job. Mike's undergraduate study in art history rather than more practical economics however only qualifies him to amuse several investment bank interviewers.

By 1982 the author interviews with Lehman Brothers, which enables him to develop some insight into investment banking. The Princeton University career center hosts Lehman Brothers' interviews for students willing to stand in snow with fifty other applicants for employment. The applicants are required to define some specific terms including the Glass-Steagall Act. This Act is passed by the U.S. Congress in 1934 to define and clarify the differences and responsibilities between commercial banking and investment banking. Most banking finance professionals after the act are commercial bankers with a few more elite professionals making deals as investment bankers. After that date, neither profession performs the functions of the other. Lehman Brothers is an investment banker that requires employment applicants to undergo a series of interview styles that includes defining terms, stress testing and career questioning. Two Lehman employees ask interview questions that Mike answers. His reply that he wants to be an investment banker to make money however, ends the interview. Mentioning money, he finds out later is forbidden despite the irony of millions made on Wall Street. Lehman and others reject his application but Salomon refuses to even consider one from him.

Learning to Love Your Corporate Culture

Learning to Love Your Corporate Culture Summary and Analysis

Michael begins his first day of work at Salomon Brothers with a walk around Wall Street. He feels like a lottery winner with his undeserved M.B.A. pay of $42,000 that doubles what his London School of Economics professor earns at twice Mike's age. Salomon is the most profitable firm on Wall Street and dominates the entire bond market in 1985. Ironically, bond traders are considered boring at parties and are relatively uneducated despite their risk-taking and money-making skills. Salomon traders' undisclosed commissions add a tiny fraction of each multi-million dollar transaction at each step along the way. The author compares commissions to second and third helpings of dressing in an overstuffed turkey. The Federal Reserve initially stuffs the bird with actions like Chairman Paul Volcker's fixing the money supply in late 1979 that lets interest rates float. As a result the price, or value of fixed interest rate bonds goes up or down opposite interest rates. The principal in a conservative bond investment can now be gained or lost by a change in interest rates. American borrowers at all levels add to the stuffing by borrowing more money than ever before. Salomon Brothers gain by their position, size and reputation for valuing, trading and selling boring bonds to earn a small commission fraction of each transaction. This rapid growth in bond trading from five million weekly to three hundred million dollars daily fuels the increased demand for trading "professionals" to include Mike and 127 other trainees in the Class of 1985.

Salomon Brothers training begins in a hot, stuffy room more like a prison than the jungle its first speaker calls the trading floor. The author compliments the first speaker's control of the "back row" jungle where they sleep or throw paper wads at the front row Harvard graduate trainees. The training program supports the myth that a great trader is a great savage among trader-savages. Trainee value is established by department managers who debate their merits by trading them like slaves on the job board. Trainees promote their desirability by rumor, groveling and friends. Japan produces large trade surpluses so its trainees are protected from the politics and even sleep in the front row seats. The jungle metaphor extends to Mike's image of an elephant's swaying trunk when a new employee makes a multi-million dollar trade and is labeled a "Big Swinging Dick" by his managing director. This is the prize accolade desired by male and female trainee alike. However, when Sally Findlay in the front row asks a "brown-nosing" question of the speaker, she is labeled with the booby prize assignment "Equities in Dallas" on the job placement board.

Training class ends after three o'clock daily on the twenty-third floor. Trainees go to the forty-first floor trading room if they want to be remembered for a job. Mike recalls his first job on the trading floor to get a burger with ketchup for a rude trader who makes fun of his suspenders. Traders sit next to each other at connected desks in rows in a trading room one third a football field long. Mike's red suspenders with gold dollar signs mark him a trainee to CEO Gutfreund who walks the trading floor. All trainees are deemed idiots except Myron Samuels. He is assumed to have connections, be a genius and carpools with two managing directors and a senior trader. Mike tries to stay out of sight and feels lower than life until he notices someone from corporate finance walk out wearing a jacket on the trading room floor and realizes he doesn't have a clue.

Adult Education

Adult Education Summary and Analysis

After four weeks of classes, trainees settle into a more casual training environment with bagels, coffee and newspapers or crossword puzzles. Susan James moderates classes and warns trainees to settle down because the next speaker's impression can affect career pay. Jim Massey, stern executive committeeman in charge of sales, enters to speak and answer questions. He reminds the trainees Salomon is the best trading firm in the world and that teamwork is important. No one asks questions since all they really want to know is how much money they can make and if Massey is concerned about reckless expansion of the firm and the number of trainees he is hiring. A month later another executive committee member Dale Horowitz speaks. He is called Uncle Dale and known as the original rabbi, or mentor, who offers to answer any questions. A question about the Arabs blacklisting Salomon gets a snap reaction and another question about Salomon shareholder ethics gets no comment from the erstwhile uncle. Chairman John Gutfreund speaks a few days later. His British style and statesmanlike calmness does not fit his Wall Street image of brutal power player. Upper management speeches reveal them to benefit from events of fortune rather than skill and cunning. Henry Kaufman, head of bond research and known as Dr. Gloom, alone expresses the opinion Salomon itself helps create their financial problem.

The training program's eighth week brings a speaker from the equity department, which is on the fortieth floor with low ceilings and no windows. Salomon equity traders and some bond salesmen work on the fortieth floor. When fixed stock commissions end in 1975, fortunes of the equity department change for the worse as dramatically as the Fed's fixing the money supply in 1979 changes fortunes of the bond department for the better. Salomon's equity department makes money competing with other stockbrokers unlike Salomon's bond department that monopolizes certain markets. Ironically, equity people have less money and more contentment but the bond people have more money and less contentment. The equity department relies more on raw experience than formulas or theory. The equity speaker is unable to answer a trainee's options question. Trainees are horrified when six of them including the author are targeted for its outreach program.

Training comes to an end with trainees becoming traders or salesmen. The traders rule and bonuses are based on trading profits. Salesmen bonuses are determined by traders. Mike's nature is not like a trader, so he chooses to become a bond salesman. Training finishes with specialist traders. Mike calls one the Human Piranha since he speaks about government bonds in raw terms like copulating and ripping faces off. A corporate bond speaker chills trainees with questions about LIBOR and TED spread. Mike names him Sangfroid for the ice water in his veins. Ironically the Human Piranha and Sangfroid are his favorite traders for their brutally fair honest speech. Richard O'Grady speaks about his experience as a lawyer for the firm and as invited applicant. Corbett issues O'Grady an ultimatum to accept a job offer on the spot or else. He tells

Corbett where to stick his job, storms out and takes a job with another Wall Street firm. Salomon calls O'Grady a year later with an apology and another offer. O'Grady tells trainees his approach works best with traders. Lewie Ranieri is listed next but cigar-smoking three hundred pound senior mortgage traders appear. Mike is assigned to London as a bond salesman where he watches the mortgage trading market develop and thrive under Lewie Ranieri.

A Brotherhood of Hoods

A Brotherhood of Hoods Summary and Analysis

In January of 1985, Matty Oliva is a Harvard graduate who passes the Salomon training course and is selected for one of five mortgage trading desk trainee jobs. His first regular assignment is to fetch lunch and other duties the senior traders demand. Mortgage traders are fat men who throw their weight around like sumo wrestlers. They eat all the time and Matty brings as much food as he can carry. He fills up food trays in the Salomon cafeteria and sneaks out without paying. The scheme is "dine and dash" and is normal but bragging about it to fat traders is not. He gets a call from someone claiming to be from the SEC monitoring ethical standards and the theft of food that he laughs off. Michael Mortara is a managing director who meets him at his desk the next morning to confirm the story. Growth in mortgage trading puts Matty's volume in line to be a "Big Swinging Dick" but the SEC worries him. He is told to report to Gutfreund where he and Mortara both chastise him. When he leaves the meeting mortgage traders, Gutfreund and Mortara are all laughing at the joke, or "goof" they play on him. He is embarrassed and runs out to wander in the Street wondering where else to go. Andy Stone, his "slave master," tells him the goof shows they like him and Salomon mortgage trading is the best place to be.

The first Wall Street mortgage security department forms in 1978. A Salomon Brothers partner named Robert Dall notices the growth in home mortgages may out-pace savings and loan financing. By January 1980 outstanding mortgages are $1.2 trillion from $700 billion in 1976. Mortgage market exceeds United States stock markets and is the world's largest capital market. Home mortgages are typically made and serviced by local thrifts since individual mortgages are too small and personal for Wall Street volume. Mortgages by dollar amount and interest rate may be pooled and traded. Dall sees prepayment as a flaw to pooling Ginnie Mae mortgages. Dall's committee report recommends Gutfreund form a mortgage department in 1978 with Ranieri as manager. Ranieri is an unlikely choice by his utility bond background but Dall selects him as a strong trader with the mentality to create a market. Ranieri is at his goal by working his way up from the mailroom with neither college degree nor resume and looks like an Italian chef not investment banker.

Ironically, Lewie Ranieri is not as confident until six years later when his mortgage department is making more money than all other Salomon businesses combined. When Dall gets ill Lewie starts a research department and a sales force of twelve who report to him. Bob Dall is squeezed out by him but ironically Ranieri refers to "Bobby's vision." Ranieri is appointed officially in charge by Gutfreund in 1979. Ranieri forms a group of traders that are like him. They are self-educated with back office experience, Italian, loud and fat. Their first names are Lewie, Johnny, Peter, Manny, Billy and Ronnie that they go by. Lewie takes one trainee in 1979. Jeffrey Kronthal is skinny, Jewish and an M.B.A. from Wharton to be the junior clerk. Mortgage traders are Italian or Jewish and none are black, Oriental, or female. Volcker's speech in 1979 makes short term rates skyrocket, deals stop and over the next three years 962 thrifts collapse. Firms that try to start mortgage departments fold and Ranieri hires their salesmen. Salomon's executive committee wants out of the mortgage business and starts cutting off the thrifts. Ranieri digs in to build the mortgage department despite Salomon. In 1981 Salomon Brothers is sold to Phillips Brothers and becomes a corporation.

The Fat Men and Their Marvelous Money Machine

The Fat Men and Their Marvelous Money Machine Summary and Analysis

In October 1981, Congress passes a tax break that allows thrifts to sell their money losing mortgage loans and reinvest the proceeds for higher returns. Losses incurred by these mortgage loan sales can offset any taxes paid over the previous ten years. Thrifts have a lot of bad loans to sell. Ranieri's mortgage traders at Salomon are the only ones buying. Thrifts have to sell to remain in business. The hundreds of billions of dollar turnover is a massive subsidy to Wall Street. Bob Dall is correct about mortgage business growth but the source is not housing demand. Thrift managers must sell the loans whether or not they understand Salomon's terms. Ranieri has the whole loans they buy transformed into bonds by getting a stamp of the U.S. Government agencies nicknamed Ginnie or Fannie Mae, or Freddie Mac. The stamp is proof of the U.S. Government's guarantee that makes trading mortgage bonds possible. Ranieri is in the right place at the right time for his traders to average $215 million over three years 1983 to 1985. Salomon's loose management style lets Ranieri run with his program. His department generates 40 percent of Salomon's revenue in 1983 and in 1985 he is on Gutfreund's short list for future chairman.

Salomon mortgage traders are both buyer and seller of mortgage loans. They often find themselves able to make rules of mortgage trading as they go along. Ranieri can call several thrifts to get them to buy his position. Some younger, more educated traders like Kronthal look into specific markets. Two of them make a game from identifying projects that may prepay as a gamble, while other traders play to predict homeowner prepayments. Despite greater sophistication in analysis traders grow in number from six to twenty-five and fatter and cruder in size and manner. Typically they start with sending a trainee to fetch onion cheeseburgers at eight in the morning. Fridays are "Food Frenzy" days and customers are told to call back. Ranieri treats traders to Atlantic City trips by helicopter and returns in time to trade the next morning. Antics in the mortgage trading department are like fraternity hazing from folks with too much time and money on their hands.

Howie Rubin is an instinctive trader who is most like Lewie Ranieri. Rubin is a chemical engineer making $17,500 a year from New Jersey. He goes to Las Vegas with $3,000 he wagers into $80,000 counting cards. He enrolls in Harvard and discovers the world of trading bonds that he prefers. He generates $25 million his first year out of training and can make at most $90,000. He generates $30 million trading his second year and gets a maximum $175,000. In 1985 he quits Salomon for a three million dollar guarantee and percentage of trading profits at Merrill Lynch. By 1986 four profitable young mortgage traders leave for million dollar pay at other Wall Street firms.

The Salomon Diet

The Salomon Diet Summary and Analysis

Dinner at Le Perigord at the end of 1985 when Gutfreund confronts the mortgage traders over their pay marks a beginning disintegration of the mortgage department. The money saved by refusing Rubin's million dollar demands can hire twelve others that look the same. Performance is not the same. As these competitive traders leave for higher pay at other firms Salomon loses its Wall Street mortgage monopoly. Eventually other firms become more competitive. Salomon's non-competitive policies let qualified traders go to other mortgage departments with skills and contacts learned from Ranieri & Co. Margins get slimmer as the market develops and Salomon loses its monopoly. The metaphor of a bicycle built for two ad run in the Wall Street Journal shows a fat man on the front seat slumping and exhausted and a thin man on the rear seat pedaling energetically. Ironically, the collateralized mortgage obligation (CMO) Salomon created to overcome mortgage inefficiency in 1983 is the instrument that dominates the mortgage market in 1986.

The CMO structure addresses the uncertainty of the investor not knowing when his investment is returned to him. For example, a three hundred million dollar CMO is comprised of ordinary mortgage bonds that are guaranteed by Ginnie Mae, Fannie Mae or Freddie Mac placed in a trust that pays interest to its owners represented by a certificate. The CMO is divided into three groups or tranches that receive prepayments in order. The first tranche receives all prepayments until paid off then the second tranche receives all prepayments and then the third. Maturity of the first tranche is short, say no more than five years, the second between seven and fifteen years and the third between fifteen and thirty years. Investors can buy a first, second or third tranche based on their investment horizon. Other pool variations develop to separate interest or principal only payments such as IOs and POs that create a bond for every investor like a supermarket. Trading is more specialized by type and trader. Lewie Ranieri becomes more involved in firm business. When he does visit trading his questions offend them. When Lewie decides to spend some time on the trading desk the others sabotage him with practical jokes and blame it on Mortara. By April 1986 mortgage trading loses from $35 million to $65 million that they hide from senior management. The following year 1987 is worse with declining revenue and increasing costs. Gutfreund hires Tom Strauss, Voute, and Ranieri to form a special committee in the Office of Chairman to help run the firm. They are former traders and salesmen from competing departments that cause rivalry, animosity and petty bickering. Mortgage trading is a money maker but traders feel underpaid, so they consider excessive costs just part of their due. Internal squabbles run rampant.

Howie Rubin, a former Salomon trader is found in early 1987 to lose $250 million at Merrill Lynch. He apparently put the PO part of an IOPO bond in his desk drawer and is unable to work his way out of the transaction before Salomon's Smith undercut the trade. In December of 1986 Lewie Ranieri is no longer officially in charge of mortgage trading because John Gutfreund appoints him to help run the firm. In July 1987 Ranieri is on the West Coast when Gutfreund fires him for absurd reasons such as no one likes him, he is disruptive and is too big for Salomon. Rubin is fired by Merrill Lynch and hired by Bear Sterns. Ranieri opens his own Ranieri & Co. just north of Salomon after a nineteen year career with the firm that begins in the mailroom and ends in the boardroom.

From Geek to Man

From Geek to Man Summary and Analysis

Mike's first assignment in 1985 for Salomon is in the London office working for Stu Willicker from Bald Knob, Arkansas. Stu tells him to call everyone in Paris that is a French money manager with fifty or more million dollars to invest. Their names are listed in "The Euromoney Guide." Mike is uncomfortable calling someone he doesn't know to sell him something he doesn't want. When his first call results in refusal to take the call from "Salomon bastards" he wonders why he takes the job at all.

A "geek" in Salomon's London office is whatever the trader says and may mean someone just out of training at a larval state between trainee and man. Mike is a geek in London. Six top management positions are held by Americans who are from the forty-first floor in New York but Europeans set the office pace. Gutfreund visits branch offices where he is treated with respect, fear and trepidation. London office employees treat him like a rude American tourist. Europeans graduate from the right schools to honor customer relations not financial gadgets. Subordination to the visiting head of an American corporation is laughable to them. Gutfreund and Strauss, who is in charge of international operations, share vision to make Salomon a global investment bank with Nomura of Japan, Citicorp an American commercial bank and other American investment banks but no European banks. Japan has trade surplus and investment dollars but confusing laws. London is enough like America to link moderate European financial regulations and opportunities.

Mike is one of twelve geeks sent to the London office. Three salesmen and Mike are under Stu's flexible leadership of the most profitable unit in the office. Dash Riprock is a salesman who helps Mike. Dash makes cryptic comments about his nine months sales experience that Mike may not understand but learns from. He comments on deteriorating financial conditions and management of Salomon. American bond market growth draws European investors eager to speculate with tiny down payments to leverage risks beyond casino gambling. Charts give their wagers a reason to believe. Mike's first customers are small institutions with under a hundred million to invest. Geeks are expected to lose a few small investors before advising large investors. Herman is Mike's first customer persuaded to buy bonds his trader claims are a good deal. Mike's sale is announced on the Salomon system-wide loudspeaker called "hoot and holler." The trader says "our" and Mike finds out he is duped. Herman buys $60,000 loss bonds from Mike and is fired.

Mike's ability to imitate lets him learn quickly from Dash Riprock and another Salomon salesman he calls Alexander. Mike relies on Alexander because he understands markets with instincts of a trader. Mike replaces him in London when Alexander returns to New York. He notes Alexander's spin habits follow either a contrarian, or opposite pattern, or look past immediate disruption to second and third level impact. Dash provides Mike with an example of style in persuasive sales phone manners. These tools help Mike get the critical acclaim of Salomon employees. In 1986 Michael sells $86 million dollars of Olympia & York bonds to a French investor. For two days he is congratulated by executives of Salomon for his accomplishment. However, when the Human Piranha congratulates Mike and calls him one "Big Swinging Dick" he finally succeeds.

The Art of War

The Art of War Summary and Analysis

In August 1986, Michael is waking up from a nightmare to be calmed by his wife. Ever since he becomes a ""Big Swinging Dick" by selling the Olympia & York he is haunted by anxious nightmares of being disrespected by bellhops who don't have bathrobes and fruit bowls ready in his hotel suite. He fears British Airways might downgrade him from Club to economy class and other indignities. On this day he is to encounter the intrigue and backstabbing for which investment bankers are famous. Losing money is a reason for employees to pin blame on one another and making money is a reason for them to fight with each other for credit. New product is easily copied and lacking the ability of being patented can be sold by other firms. Plagiarism is common across firms and even within Salomon.

For example, Alexander and Michael design a warrant on German interest rates to sell for a transaction fee of $700,000 dollars with no risk. A veteran salesman and vice-president called "opportunist" offers to help and gets German government approval. The day on which the deal is launched he issues a memo describing the deal and flies to New York to take sole credit. Michael and Alexander devise a second deal with the same structure but Japanese warrants and do not tell the opportunist. This deal closes but when the opportunist's boss asks him about it he knows nothing and his ruse is exposed.

By the fall of 1986 Michael's fortunes and those of Salomon begin to change. Although he is able to bring a lot of dollars to the firm they don't show up profitably and Christmas bonuses look thin. Market forces and Salomon Brothers mismanagement are combining to cause deep trouble. American investment firm policies and practices become irritating to European investors. None of the American managing directors in London speak any other language than English. London office of Salomon is moved from the financial district to a new high-tech Victoria Plaza location. The trading floor seems twice the size of New York's forty-first floor. Michael's French investor in Olympia & York bonds wonders aloud whether he pays for the new carved oak banister.

Gutfreund issues the edict that bonuses have a specific floor and ceiling or band that no one is paid more or less regardless of accomplishment. First and second year employees speculate about the band. Bonus day is met with relief, joy, anger or some mix of the three. Distribution of bonuses is accompanied with an interview about how the employee bonus fits with others by the paymaster. Alexander tries to help Michael understand the unsatisfied hunger or greed that makes all of them feel underpaid. As the firm begins to look riskier, employees want more in the short-run before it collapses. By mid-1987 the Victoria Plaza office has nine hundred employees with an average length of service less than two years and average age of twenty-five. When Michael arrives in 1985 the average age of the 150-person staff is well over thirty.

How Can We Make You Happier?

How Can We Make You Happier? Summary and Analysis

The small sales unit follows a routine of monthly performance evaluation, weekly office meeting and daily phone calls. Dash beats Michael to the desk by an hour daily. They talk about the future, beating the market, Salomon Brothers' fate or the three geeks that work for them. The routine is broken on September 24, 1987, when the hostile raider Ronald O. Perelman, bids for Salomon stock to put it "in play." He is backed by Drexel Burnham and advised by First Boston's Perella and Wasserstein in the first time Wall Street firms turn on each other. Customers call to sympathize or gawk like onlookers at an accident. Gutfreund and Michael Milken are unfriendly since 1985. Gutfreund insults Milken at a breakfast meeting and throws an angry Milken out of the building. Gutfreund cuts Milken's firm Drexel Burnham out of deals. Michael thinks these bad feelings plus customer and employee defections to Drexel explain Milken funding a raid on Salomon. Michael and Dash think Perelman's raid could turn Salomon into a stronger business.

The rapid growth and domination of mortgage bond trading by Ranieri at Salomon is equaled by Milken's junk bond trading at Drexel. Salomon is the leading bond trader and most profitable Wall Street investment bank until 1986 when Drexel takes the lead. Like Lewie Ranieri with mortgage bonds, Michael Milken persuades investors that investing in junk bonds is a safe bet. They are equally zealous, tactless, uncouth and both outsiders with devoted employees. Milken relocates to California but Ranieri stays in New York under Gutfreund. Milken learns at Wharton but Ranieri learns in the mailroom. Milken succeeds by deal size and pay but Ranieri succeeds by staff size and board recognition.

Before 1981, thrift companies lend only homeowner mortgages under deposit guaranty by the federal government. In 1981 Congress authorizes them to speculate their way out of trouble by investing in junk bonds. Columbia Savings & Loan pays its manager ten million dollars in salary that encourages thrift managers across the country to invest in junk bonds. One of Mike's training classmates quits to join other Salomon bond experts in 1987 at Milken's firm in Beverly Hills. In the early 1980's, the entire thrift industry is served almost exclusively by Salomon. The firm could be a major dealer in junk bonds with its new junk bond department started in 1981 by Bill Voute. Ranieri discourages his thrift customers from investing in junk bonds which drives them to Milken's firm instead. Junk bond volume reaches $53 billion from 1980 to 1987. Milken has more money than junk bonds alone can absorb so he funds raids on undervalued companies. A raider may bid to takeover an undervalued firm that Milken finances with junk bonds. A transaction takes advisers for both raider and target firms and four or more investment banks to play.

Ironically, Salomon is in play because Gutfreund's hostility to Milken blinds him to the junk bond market raiders fund takeovers with. Gutfreund knows his largest shareholder

Minorco wants to sell but his slow reply makes them seek buyers elsewhere. If Minorco sells 14 percent to Revlon, then 11 percent more swings control. Gutfreund asks Warren Buffet to help block Perelman. Buffet agrees to purchase nine year convertible preferred bonds at 9 percent that he can convert to stock if Salomon thrives. Gutfreund keeps his job and control by threatening to resign if the board turns down Buffet's offer. Under his control Salomon misses the opportunity to trade entire industries like Milken is doing.

When Bad Things Happen to Rich People

When Bad Things Happen to Rich People Summary and Analysis

Two weeks after Perelman's take-over bid the author is instructed that Salomon Brothers' new priority is junk bonds. The first transaction is a bridge loan with Goldman Sachs for the period between Southland Corporation management's $4.9 billion buyout of 7-Eleven stores and the sale of Southland Corporation junk bonds to pay back the loan. Michael's success with Olympia & York assures him the reputation to be able to sell these bonds too. Salomon's junk bond specialists assure him it is a good investment, since they have the most to gain or lose. Michael breaks his resolution to not sell things people should not buy within months. Gutfreund is convinced he can show Salomon to be a force on the market and the Southland junk is his example. Michael is required to call his French customer while a bond specialist watches. The specialist praises Michael's pitch to the Frenchman without knowing he convinces his customer in coded speech to be wary.

October 12, 1987 begins an eight-day period of trauma and distress at Salomon. News is leaked over the weekend one thousand Salomon personnel are to be fired that is denied in London until New York fires municipal bonds and money market departments later that day. Ironically, despite being unprofitable, the municipal bond department is the nation's leading underwriter and the money market department among the leaders. Gutfreund acts like a trader cutting losses rather than like a businessman restoring profitability. By the end of the day five hundred of the one thousand announced in the disputed leak are gone and the leaker is unknown. On day three Tom Strauss advises the London branch is most in need of cuts, but no specifics are provided. By day five the first hurricane in a hundred years hits London and 170 people who struggle to work are fired. Younger ones without experience or seniority that cost least go first. Michael is still employed. He flies to New York on day six to give a prearranged training speech and lobby for his annual bonus.

On day seven, Monday October 19, 1987 Michael has a day before his speech to visit the forty-first floor trading room. It has many empty seats and much less activity than usual. The market crashes on this day and Michael rushes back and forth between fortieth and forty-first floor trading rooms. Market winners are joyous and losers are confused and despairing. The Southland junk bond deal collapses and Michael's Frenchman thanks him for not selling him any bonds. Michael is grateful he is a middleman. He observes Gutfreund again in his element making trading decisions and holding strategy meetings. Salomon shares are sinking. Michael overhears Gutfreund buy three hundred thousand shares of Salomon and buys some himself. Michael speaks to trainees and Jim Massey reassures them they can stay. Bonus day is

December 17, 1987. Michael estimates his bonus at $140,000 according to Gutfreund's compensation band policy. The policy is changed and he receives $225,000, which makes him the highest paid of his remaining trainee class. Ironically he receives more now when the firm has its worst year ever to seal his loyalty among few remaining veteran employees. Apparently the management does not know money does not keep him or make him leave, which he does for other reasons.

Characters

Michael Lewis

Michael Lewis is the author of "Liar's Poker" and is referred to in this summary as Mike, Michael, Lewis or the author. He writes this book subtitled "Rising Through the Wreckage on Wall Street" in 1989, after three years with Salomon Brothers. He begins this semi-autobiographical tale as a twenty-four year old graduate student living in 1984 London. He attends London School of Economics to complete his master's degree in economics. His cousin is the wife of a German baron who links him to a Salomon job connection that repulses him but is preferable to unemployment. Mike wants to become an investment banker to make money. However, saying that is forbidden despite the irony of millions being made on Wall Street. He applies in 1982 to Lehman, Salomon and other investment bankers that reject or even refuse to consider his Princeton degree in art history. He feels like a lottery winner when landing a $42,000 job at Salomon Brothers. Mike wears red suspenders with gold dollar signs that mark him a trainee. He is one of twelve New York trainees assigned to the London office in 1985. His manager is Stu Willicker from Bald Knob, Arkansas who tells him to call everyone in Paris with $50 million dollars to invest. When he hears his first call say "Salomon bastards" he doubts taking the job at all.

Mike is uncomfortable calling someone he doesn't know to sell him something he doesn't want. However, when he gets to know Herman his first German customer to sell him ATT bonds he worries they're a bad deal. Mike is thanked on the hoot by the trader and Herman is fired for losing money on the bonds. Three salesmen and Mike work under Stu's flexible lead of the most profitable unit in the London office. Mike learns to use tools that Dash Riprock in London and Alexander in New York employ to improve sales and strategy skills. Mike begins to be praised by other employees and by mid-1986 is advising Salomon traders. When he sells eighty-six million dollars of Olympia & York bonds to his Frenchman he gets an ultimate goal. He is congratulated for two days by members and executives of Salomon for his accomplishment. However, when the Human Piranha telephones Michael to brand him one "Big Swinging Dick" he finally knows he succeeds.

John Gutfreund

John Gutfreund is the Chairman and CEO of Salomon Brothers Wall Street investment banking firm. He is known as the King of the Street. His $40 million gain on the sale of Salomon and $3.1 million salary is more than any other Wall Street CEO receives in 1986. His British style and statesmanlike calmness belies his Wall Street image of brutal power player. His name is pronounced "Good friend" but he stirs fear like a grizzly bear to a small animal. He silently walks the trading floor saying nothing but dropping cigar ash where he goes. As manager he knows he is hostage to the producing traders who take risks to make money for the company. Although once a trader, he is now an outsider in the game. A hand of Liar's Poker for high risk stakes lets him show off that he can be a player too. Gutfreund becomes a legend by saying, "One hand, one million dollars, no tears."

Gutfreund visits branch offices where he gets respect, fear and trepidation except from London office employees who treat him like a rude American tourist. To older Europeans subordination to the visiting head of an American corporation is laughable. Gutfreund wants Salomon to become a global investment bank with Japan's Nomura and America's Citicorp but no Europeans. He has a lighter side that seems friendly had he not shown it at the expense of a trainee whose trading volume has him in line to be a "Big Swinging Dick" but for an SEC inquiry. The trainee reports to Gutfreund's office where he and Mortara both chastise him and watch him leave as they laugh at the joke, or "goof" they play on him. He does reward employee performance by putting Ranieri in charge of mortgage bonds in 1979 and considering him on the short list for future chairman in 1985 since his traders generate 40 percent of the firm's revenue in 1983. In 1987 Gutfreund tries to involve middle managers in running the firm by appointing Tom Strauss, Bill Voute and Lewie Ranieri to a special committee in the office of chairman.

John Gutfreund is the boss and his desk is where the buck stops regardless of his attempts to suggest otherwise. He begins in the business as a trader and runs the business of Salomon like a trader as well. On the same day Salomon shares are sinking Michael sees Gutfreund trading, strategizing and buying three hundred thousand shares of Salomon stock to make a profit from his own company's loss. Similarly with the Salomon board twice since the mid-1970s Gutfreund threatens resignation to force them to let him keep his job for the good of Salomon Brothers that gives his friend Buffet a windfall of $126 million in bond value.

Pay for employee performance is the critical deficiency in Gutfreund's control of the firm. His edict that bonuses have a specific floor and ceiling or band that no one is paid more or less regardless of accomplishment makes competitive traders leave for higher pay at other firms and Salomon to lose its Wall Street mortgage monopoly. His opinion at the end of 1985 that the money saved by refusing one trader's million dollar demand can hire twelve others that look the same misses the point of paying for qualified performance. By 1986 four profitable young mortgage traders leave for million dollar pay at other Wall Street firms.

John Meriwether

John Meriwether is a Salomon trader and known as King of the Game. He is the champion and a dangerous Liar's Poker Game player. Meriwether has enough cash and courage to meet Gutfreund's bet. Meriwether is the best bond trader on Wall Street because he controls his emotions and expressions of fear and greed. He has six traders working for him that have Ph.D.s but are obsessed by the game.

Salomon Brothers Managing Director's wife

Salomon Brothers Managing Director's wife is the person who gets Michael Lewis a job. The senior managing director's wife and Mike dine at the same table for the invitation-only black tie fund-raising dinner held by the queen mother. She asks about his plans for a job and why he doesn't come to work at Salomon Brothers trading. He says trading does not sound like fun compared to his image of investment banking. She asks if he wants to spend all day in an office, where is his chutzpah and is he a numbnut? The queen mother passes with her corgis and the wife shouts out how nice her dogs are. Mike is convinced by her manners the "crude, rude, and socially unacceptable" culture of Salomon Brothers could fit and agrees to her offer. She arranges for her husband to meet him at the London offices and is his connection to get a job at Salomon Brothers. A few days later he meets Leo Corbett, the head of Salomon New York recruiting, for breakfast.

Jim Massey

Jim Massey is the stern executive committeeman in charge of sales. He enters the training room to give a short speech and answer questions. He reminds trainees that Salomon Brothers is the best trading firm in the world and that teamwork is important. No one asks any questions since they really just want to know how much money they can make. The trainees also want to know whether Massey is concerned about expansion of the firm and the number of trainees he is hiring.

Dale Horowitz

Dale Horowitz is another executive committee member who speaks to the trainees. He is nicknamed Uncle Dale and considered the original rabbi or mentor. He offers to answer any questions the trainees might have. A question about the Arabs blacklisting Salomon gets a snap reaction. Another question about Salomon shareholder ethics gets no comment from the erstwhile uncle.

The Human Piranha

The Human Piranha is a nickname for one of the specialist bond traders. Mike identifies him as The Human Piranha because he speaks about government bonds in raw speech including copulating objects and ripping faces off. The Human Piranha is another of the author's favorite traders for brutally fair honest speech.

Sangfroid

Sangfroid is a nickname for the corporate bond speaker who chills the trainees with intimidating questions about LIBOR and the TED spread. Mike names this trader

Sangfroid for the ice water running in his veins. Sangfroid is one of the author's favorite traders for his brutally fair honest speech.

Richard O'Grady

Richard O'Grady is a younger bond salesman who speaks to trainees about his experience as an invited applicant. Salomon's recruiter Corbett issues O'Grady an ultimatum to accept his job offer. O'Grady tells Corbett where to stick his job, storms out and takes a job with another Wall Street firm. O'Grady's experience confirms that confrontational approach works best with traders since Salomon calls him a year later to apologize and make another offer.

Lewie Ranieri

Lewie Ranieri is a Salomon utility bond trader who establishes the mortgage bond market. Ranieri seems an unlikely choice because he has neither a college degree nor a resume and looks more like an Italian chef than investment banker. At the time Lewie is at his goal by working his way up from the mailroom. Robert Dall recommends him in 1978 to manage the new department that his idea and insight envisions because Lewie is a strong trader with the mentality to create a market. Lewie embodies Gutfreund's worst fears. Since becoming manager Gutfreund knows he is hostage to traders who take risks to make money for the company.

Lewie typically takes charge. When Dall is ill Lewie starts a research department and then a sales force of twelve who report to him. Lewie is appointed officially in charge by Gutfreund in 1979. Ranieri measures his success by the number of employees and recognition as a board member. Lewie's traders all look like him, self-educated back office skills, Italian, loud and fat except the junior clerk trainee Jeffrey Kronthal who is skinny, Jewish and has an M.B.A. from Wharton. Lewie is confident six years later when his mortgage department makes more money that year than all the other Salomon businesses combined. However, by December of 1986 Lewie is no longer officially in charge of mortgage trading since Gutfreund promotes him to help run the firm. In July 1987 Lewie is on the West Coast when Gutfreund fires him for absurd reasons, i.e., no one likes him, he is disruptive and too big for Salomon. Lewie opens his own Ranieri & Co. after nineteen years that begin in the mailroom and end in the boardroom.

Robert Dall

Robert Dall is a Salomon Brothers partner who notices that the growth trend in home mortgages may out-pace savings and loan financing. Dall previously helps finance William Simon's government bond purchases. Simon says a homeowner prepayment option is a flaw in the pooling of Ginnie Mae mortgages. Dall's executive committee report recommends Gutfreund form a mortgage department in 1978 with Ranieri as manager. The mortgage department that Dall envisions is wildly successful under

Ranieri's management. The typical take-charge style of Ranieri squeezes him out and Bob Dall finally leaves the firm in 1984. Ironically, Ranieri still refers to "Bobby's vision."

Paul Volcker

Paul Volcker is a Chairman of the Federal Reserve System who causes a major impact on the U.S. economy and markets. Volcker's speech in 1979 makes short term rates skyrocket, deals stop and over the next three years 962 thrifts collapse.

Mike Milken

Mike Milken is the junk bond guru of Drexel Burnham. The rapid growth and domination of mortgage bond trading by Ranieri at Salomon is paralleled by Milken's rapid growth and domination of junk bond trading at Drexel. In the early 1980s Ranieri and Milken meet on the road while they are both out looking for bond buyers. Like Lewie Ranieri with mortgage bonds, Michael Milken persuades investors that investing in junk bonds is a safe bet. Unlike Ranieri however, Michael Milken is Wharton educated and takes control of his operation by moving it to California. Milken is zealous, tactless, uncouth and an outsider with devoted employees. Milken measures and rewards success of his own and his employees by number of deals and pay.

Salomon is the leading bond trader and most profitable investment bank on Wall Street until 1986 when Milken's Drexel Burnham takes the lead. Milken impacts Ranieri's business by losing employees and customers to him with competitive junk bond compensation and rates. Milken has more funds than junk bonds alone can absorb so he begins to finance raids on undervalued companies. A raider, like Ron Perelman, is identified to initiate the takeover bidding of an undervalued firm that Milken can finance with junk bonds.

Howie Rubin

Howie Rubin is a trader who is most like Lewie Ranieri with his innate skills. Rubin is trained as a chemical engineer making $17,500 a year from New Jersey. He goes to Las Vegas with $3,000 he wagers into $80,000 by counting cards. He enrolls in Harvard and discovers trading bonds that he prefers. He generates $25 million his first year out of training, which makes him ask who makes the money. First year traders receive at most $90,000, which is his salary for the $25 million he produces for the firm. Similarly in his second year he generates $30 million and is paid the maximum $175,000 for a second year trader. He quits Salomon in 1985 for a three million dollar guarantee and percent of trading profits at Merrill Lynch. In 1986 four more of the most profitable young mortgage traders follow his example by leaving Salomon for million dollar pay at other Wall Street firms.

In early 1987 Howie loses $250 million at Merrill Lynch. He is fired by Merrill Lynch and hired by Bear Sterns on the same day.

Dash Riprock

Dash Riprock is a pseudonym for one of the London salesmen that helps Mike and is admired by him. Dash makes cryptic comments about his nine months sales experience that Mike may not understand but learns from. Many of his comments refer to deteriorating financial conditions and management of Salomon. Dash provides Mike with an example of style in persuasive sales phone manners.

Alexander

Alexander is a pseudonym for another Salomon salesman from the forty-first floor in New York. Mike relies on Alexander because he understands markets with instincts of a trader. Mike meets him in London and replaces him when Alexander returns to New York. The author observes Alexander's spin habits that follow one of two patterns. The first pattern is to actively seek the opposite of what others are doing and is called contrarian. His second pattern looks beyond immediate dislocation or disaster to second and third level impacts. Alexander and Michael design a warrant on German interest rates to sell for a transaction fee with no risk. A veteran salesman and vice-president called "opportunist" offers to help get German government approval and then tries to take sole credit. Michael and Alexander devise a second deal but avoid the opportunist. This deal also closes but when the opportunist's boss asks him about it he is exposed.

Ronald O. Perelman

Ronald O. Perelman is the hostile raider that announces a bid for Salomon stock to put it "in play." He is financed by Drexel Burnham. Milken backs Perelman's cosmetic company Revlon to raid Salomon. Michael and Dash think Perelman may turn Salomon into a business rather than John Gutfreund's global empire.

Objects/Places

Salomon Brothers

Salomon Brothers is the investment bank where the author Michael Lewis takes employment. The firm has a "crude, rude, and socially unacceptable" culture that attracts him. Salomon is the most profitable firm on Wall Street and dominates the entire bond market in 1985. Salomon Brothers gain by their position, size and reputation for valuing, trading and selling bonds that earns them a small commission on each transaction.

Wall Street

Wall Street is the name of the financial district located in New York City. Investment banks including Salomon Brothers as well as other national and international financial firms have offices there. Michael starts his first day at Salomon Brothers by walking around Wall Street.

Liar's Poker

Liar's Poker is a name used to identify several facets of Michael Lewis' book. "Liar's Poker" is the title of this book describing his experiences as a trainee and employee of Salomon Brothers Wall Street investment bank. Liar's Poker is a popular game played in the trading room of Salomon Brothers. The game involves wagering until the players challenge one player's bid to reveal who is bluffing. Other Wall Street firms play a version of Liar's Poker. Lastly, Liar's Poker is a metaphor for trading on Wall Street. Ironically, customers of the firm are unwitting but regular bidders in the hands of Liar's Poker players.

London

London is the name of a city in England where the author, Michael Lewis is living as a twenty-four year old student in 1984. He attends London School of Economics to complete his master's degree in economics prior to beginning employment with Salomon Brothers.

The Great Hall of St. James Palace

The Great Hall of St. James Palace is the location at which Michael Lewis is invited to attend an invitation-only black tie fund-raising dinner held by the queen mother. Dinner attendees include two managing directors of Salomon Brothers and their wives. One of the wives meets Michael at dinner where she encourages him to consider working for

Salomon Brothers. She makes a connection for him through her husband that results in his employment.

Princeton University

Princeton University is the name of the college where Michael earns a degree in art history. In 1981 he gets discouraged applying for investment banking jobs but does not consider trading. His degree amuses investment bankers. The Princeton University career center hosts Lehman Brothers' interviews where Michael gains insight to investment banking.

The Glass-Steagall Act

The Glass-Steagall Act is the name of an Act passed by the U.S. Congress in 1934 to define differences and responsibilities between commercial banking and investment banking. Most banking finance professionals after the Act are commercial bankers. Some more elite professionals make deals as investment bankers. Under the Act neither profession performs the functions of the other.

Lehman Brothers

Lehman Brothers is an investment banker that requires employment applicants undergo a series of interview styles that includes defining terms, stress testing and career questions. Lehman staff interview Michael. A reply that he wants to be an investment banker to make money ends his interview in 1981. His application is rejected by Lehman but Salomon refuses to even consider him.

Goof

Goof is the name given to a practical joke at Salomon Brothers. The practical jokes are like college hazing or fraternity initiation rites that occur at all levels of Salomon. For example, a trainee who is sent to fetch food for the traders is accused of stealing from the cafeteria supposedly by the SEC. The Chairman Gutfreund and Managing Director Mortara laugh about "goofing" the trainee but his "slave master" tells him a goof shows they like him.

Ginnie Mae, Fannie Mae and Freddie Mac

Ginnie Mae, Fannie Mae and Freddie Mac are nicknames referencing United States Government Agencies that guarantee various types of mortgage loans. Ranieri transforms mortgages they agree to buy into bonds by getting a stamp of these U.S. Government agencies that the selling thrift pays for. A stamp proves the U.S. Government guaranty to give the mortgage bonds trade value.

Collateralized Mortgage Obligation (CMO)

Collateralized Mortgage Obligation (CMO) is the name of the security type that Salomon creates in 1983 to overcome mortgage inefficiency. CMOs become the instrument that dominates the mortgage market in 1986. A CMO lets an investor determine investment return based on investment horizon. For example, the CMO is divided in three groups with prepayments in order of up to five years, from seven to fifteen years or from fifteen to thirty years.

IOs and POs

IOs and POs are abbreviations used to represent other mortgage pool variations developed to separate interest or principal only payments such as IOPOs offer a bond choice for every investor.

Geek

A "geek" in Salomon's London office is whatever the trader says it is. One meaning is someone just out of training at a larval state between trainee and man. A geek puts a few small investors out of business to get large investors.

Hoot and Holler

The "hoot and holler" is the Salomon Brothers system-wide loudspeaker over which important and not so important announcements are made. Mike's sale of ATT bonds and the Olympia & York priority is announced on the "hoot."

Convertible Preferred Bond

Convertible preferred bond is the name of a security that gives a purchaser the right to turn debt, i.e., the bond, into equity at his sole choice. John Gutfreund asks Warren Buffet to lend $700 million he can use with Salomon's capital totaling $809 million to block Perelman's bid. Buffet agrees to purchase a convertible preferred bond at 9 percent that at the least earns interest for nine years if the firm just continues. If Salomon does well however, Buffet has a right to convert the bond to shares of Salomon stock if conversion provides a better return to him. His only risk is Salomon bankruptcy. Buffet acquires a windfall over purchase price of $126 million based on bond value at purchase.

Themes

Bond Market Innovation

Bond market innovation develops from a market deficiency recognized by one or more individuals. For example, Robert Dall becomes aware demand for financing in the thrift industry will outstrip capital provided by its current financing mechanisms. Similarly, Michael Milken knows demand for financing the corporate bond market is satisfied for blue chip firms because they are considered investment grade by credit agency ratings. However, developing companies on the way to profitability have no ready market for public financing because they are not investment grade—they are "junk."

Salomon creates the collateralized mortgage obligation (CMO) to overcome mortgage inefficiencies in 1983 and takes over the mortgage market by 1986. Ranieri improves and assures tradability of the mortgage loan instrument by a stamp from one of three government agencies. Government guaranteed mortgage loan documents must let homeowners prepay the principal balance due. This provision makes maturity date of a mortgage bond, i.e., principal repayment, uncertain. To accommodate investors with specific investment horizons CMOs structure short, medium and long-term repayment by tranche. Some investors prefer interest only (IO) or principal only (PO) payments that fit their horizon. IOPOs allow CMO parts to be traded separately.

Drexel Burnham's Milken creates the junk bond to overcome corporate financing inadequacy in 1980. Junk bond volume reaches $53 billion from 1980 to 1987 when it dominates the corporate bond market. Milken starts selling junk bonds when Salomon exclusively services the thrift industry and could be a major dealer to thrifts with Bill Voute's new junk bond department. However, Ranieri discourages his thrift customers from investing in junk bonds so they invest with Drexel Burnham. Milken attracts more money than providing junk bonds to developing firms alone can absorb. He uses excess investment funds to finance raids on undervalued companies. Milken identifies a raider to initiate the takeover bid of an undervalued firm with a leveraged buyout (LBO) that he finances with junk bonds. A transaction may involve four or more investment banks and advisers that make it a lucrative source of revenue.

Under Gutfreund's control Salomon misses the innovation from trading bonds to trading entire industries that Milken capitalizes on. Gutfreund eventually tries to show Salomon is a force on the market with Southland as his first example. The transaction is a bridge loan with Goldman Sachs for the period between Southland Corporation management's $4.9 billion leveraged buyout (LBO) of 7-Eleven stores and sale of Southland Corporation junk bonds to pay the loan. Ironically, Gutfreund brings this product to market just as the market collapses in October 1987. A critical factor of market innovation is timing a product with market need and salability.

Paying Players to Play, or Not

The key, but unspoken concept in investment banking is that employees become investment bankers for the money. Pay for the job is not mentioned when Mike is interviewed and takes the job.Gutfreund's policy and practice offer promise of promotion and perks rather than pay for performance. For example Ranieri is promoted over a nineteen year career with the firm that begins in the mailroom and ends in the boardroom. Recognition is provided as a prize for performance when a new employee, male or female, makes a multi-million dollar trade and is labeled a "Big Swinging Dick" by his managing director.

Gutfreund is known as King of the Street because he is the highest paid CEO. He collects $40 million at a partial sale of Salomon and $3.1 million in annual salary. Salomon leads the market until Gutfreund's pay policies drive off talented employees to other firms that pay for performance in new bond departments. Drexel takes the lead in junk bonds with competitive pay that attracts underpaid Salomon employees. Disintegration of the Salomon lead in mortgage business occurs through Gutfreund's management policies of employee compensation.

Gutfreund formulates a compensation band within which first, second and third year trainee employees are paid. Gutfreund allows first year traders to get at most $90,000 and second year traders a maximum $175,000 regardless of outstanding performance. For example, Howie Rubin receives the first year maximum salary for the $25 million he produces that year, and the second year maximum for the $30 million he generates trading that year. In his third year, 1985 Howie quits Salomon for a three million dollar guarantee and percentage of trading profits at Merrill Lynch. Gutfreund shows disdain for talented traders when he publicly comments on Howie by saying for the same money he can "hire twelve others just like him."

When Salomon has financial difficulties Gutfreund reacts like a trader by cutting investment losses rather than a businessman restoring profitability to the company he manages. For example, Salomon's municipal bond department is the nation's leading underwriter and its money market department among the leaders that are both fired on the same day. London has its first hurricane in a hundred years when 170 Salomon employees who struggle getting to work find out they are fired when they arrive. In July 1987 Ranieri is fired by Gutfreund because no one likes him, he is disruptive and is too big for Salomon. Ironically, Michael is still employed and receives a bonus of $225,000, which is more now when the firm has its worst year ever. Apparently his policy changes to secure the loyalty of remaining employees. Michael estimates his bonus should be $140,000 according to Gutfreund's longstanding pay policy.

It's All a Game

King of the Game versus King of the Street demonstrates Gutfreund management, i.e., Meriwether and six "game-obsessed" Ph.D. traders against Gutfreund's wager. Meriwether is the only trader with enough money and skill to meet Gutfreund's bid.

However, Meriwether recognizes the no-win wager and raises to ten million that calls the Chairman's bluff. Gutfreund stays on top with the legend of a "million dollar bet" that shows he is still a player despite not playing the game.

This theme permeates Gutfreund's management style. He sets up situations that instigate a poker game setting at every level of operation. For example, he threatens the board of directors to resign twice as a ploy to keep his job, for the "good of the company." Similarly Gutfreund establishes a committee comprised of traders and salesmen from competing departments in the Office of Chairman to "help" run Salomon. Lastly he follows Robert Dall's recommendation for Lewie Ranieri to set up Dall's mortgage department then puts Lewie officially in charge when Dall is temporarily out sick. Gutfreund's management style keeps him "on top" no matter the cost to directors, employees or the firm. The tactic he uses forms working teams whose goals are incompatible with Gutfreund's stated goal. Like Liar's Poker players in a circle team members are individual players opposing each other. Consequently, Gutfreund stays on top and out of the fray.

His committee in the Office of Chairman is typical. By 1987 Salomon revenue is declining and costs are increasing. Gutfreund enlists the help of Tom Strauss in charge of international relations who shares his global vision. Bill Voute is in charge of corporate bonds but Gutfreund refuses to let him take advantage of an opportunity in junk bonds. Lewie Ranieri manages the mortgage department until Gutfreund promotes him to this committee. All three are traders, salesmen and managers from competing departments. They have no reason to work together. They are picked like poker players in a circle with their own interests to protect. The mix causes rivalry, animosity and petty bickering. Lewie's mortgage traders make money but feel they are underpaid so consider excessive costs just part of their pay. Each has exceptional skills that Gutfreund uses to set up and keep his own game in play.

Style

Perspective

The author Michael Lewis is a Princeton art history major and holds a London School of Economics Masters degree in economics. He meets the wife of a Salomon Brothers Managing Director in 1984 at a fund-raising dinner held by the British Royal family. He takes a job with the Salomon Brothers Wall Street investment banking firm as a trainee in New York City. During training he is exposed to the trading floor in New York and after training is completed Michael is assigned to Salomon's London office as bond salesman. The author spends three years successfully employed with Salomon Brothers until 1988 when the twenty-seven year old resigns for other interests. This book is an insider's story of experiences he has directly and indirectly with friends and colleagues at a multi-billion dollar Wall Street investment firm. Michael acknowledges he "became fairly handy with a few hundred million dollars" but feels lost deciding what to do with a few thousand.

He writes this book subtitled "Rising Through the Wreckage on Wall Street" to illustrate the events and attitudes he experiences while working at Salomon Brothers Wall Street investment bank. He describes this book as the story of an era when traders are masters of the quick killing. The ten years or so from 1979 through 1988 describe a period when mortgage and junk bond trading develops and grows into a multi-million dollar industry niche. Michael Lewis describes experiences at the center of a modern day gold rush in which twenty-four-year-olds with little skill or experiences make more money than ever before trading and selling million dollar investments. Michael is an honest player in a game that he leaves after three successful years because he professes "it would be better to tell the story than to go on living the story."

Liar's Poker is written to benefit many who think money matters and that it represents the value one has to a society. Michael's father believes one receives money for the worth he brings to society until his son reveals the hundreds of thousands of dollars he makes as a twenty-seven year old for just making a phone call. The author hopes to provide some degree of more realistic perspective about money and finance to the readers of his book.

Tone

Much of the book is written in a subjective rendering of his experiences in the Wall Street investment firm Salomon Brothers. He begins as a trainee describing his own and the experiences of his fellow training classmates' experiences in the training class and then on the other experiences as a bond salesman. Chapters 1 through 4 are his subjective first person account of his life as investment bank trainee. This first person subjective style lets the reader feel at home with his friendly, folksy tone. The author tells experiences of any frustrated job seeker who once he gets a job undergoes training with all its attendant ills that make him wonder why he wanted the job at all.

The author writes the middle part of the book from the vantage point of his job in the Salomon London office commenting on and watching the development of the mortgage bond trading department. This section of the book puts his personal story on hold while he develops an historical record of Lewie Ranieri and his mortgage trading department. Chapters 5 through 7 are an objective third person rendering of the rise and fall of the Salomon Brothers mortgage trading department. This third person objective style could be dry and historical except for the humor Michael introduces to his stories of the "goof" and the "Italian family." This section that discusses development of the mortgage and junk bond business could be tedious and technical. The author introduces a lighthearted humor that makes these pages easy and fun to read.

Finally, the last part of the book returns to Mike's experience as a sales trainee, or geek, in the London office. He expresses his personal observations, feelings and opinions as he rises through the ranks as first, second and third year Salomon bond salesman. Chapters 8 through 11 are a subjective, first person story of himself as investment banker trainee. This semi-autobiographical conclusion to the book is surprisingly entertaining despite the persistent use of writing style in the first person singular pronoun.

Structure

This 249-page semi-autobiographical book is comprised of eleven chapters plus a preface and epilogue with neither glossary nor index. Chapter length ranges from 17 to 32 pages. Chapter titles are descriptive, straightforward and readily understandable. Titles clearly state what the chapter is about although the text within chapter context provides further dimension and nuance to be discovered upon reading.

Michael Lewis uses a mix of personal experiences and technical jargon that is easy to understand and a pleasure to read. The author uses the literary techniques of flashback and perspective with virtually seamless integration to assure reader understanding. There is a blend of lighthearted humor and anecdotes about important people in the book that is colorful and enlivening about folks like bond traders that by profession and legend are a "boor" at parties. Michael Lewis brings their personalities to life.

The rather free-form style of telling stories before, after and within other tales could create confusing timelines that Lewis is able to avoid. For example, the book opens in 1986 with a Liar's Poker game but within five pages reverts to London in 1984 and in another five pages back to 1981 Princeton. Specifically, writing within ten interesting and lively pages is chock full of tales about poker with Wall Street and Game Kings, the Queen Mother and her corgis at dinner, Mike's new job and his frustrating interview as an undergraduate when he actually mentions making money at a Lehman interview. Mike's style of writing promises never a dull moment despite being substantially full of informative facts and stories about a Wall Street investment banker's life.

Quotes

"And if you wanted to show off, Liar's Poker was the only way to go. The game had a powerful meaning for traders. People like John Meriwether believed that Liar's Poker had a lot in common with bond trading. It tested a trader's character. It honed a trader's instincts. A good player made a good trader, and vice versa. We all understood it." Chapter 1, pp.16

"We stood immediately at the queen mother's side. The Salomon Brothers wife glowed. I'm sure I glowed, too. But she glowed more. Her desire to be noticed was tangible. There are a number of ways to grab the attention of royalty in the presence of eight hundred silent agents of the Prudential, but probably the surest is to shout. That's what she did. Specifically, she shouted, 'Hey, Queen, Nice Dogs You Have There!'" Chapter 2, pp.20

"Economics was practical. It got people jobs. And it did this because it demonstrated that they were among the most fervent believers in the primacy of economic life." Chapter 1, pp. 25

"The men on the trading floor may not have been to school, but they have Ph.D.'s in man's ignorance. In any market, as in any poker game, there is a fool. The astute investor Warren Buffet is fond of saying that any player unaware of the fool in the market probably is the fool in the market." Chapter 3, pp. 35

"The movements of the trading floor respond to the movements of the markets as if roped together. The American bond market, for example, lurches whenever important economic data are released by the U.S. Department of Commerce. The bond trading floor lurches with it. The markets decide what are important data and what are not. One month it is the U.S. trade deficit, the next month the consumer price index. The point is that the traders know what economic number is the flavor of the month and the trainees don't." Chapter 3, pp. 52

"And we knew that in general the quality of treatment we received in the training class varied inversely with the desirability of the job held by the speaker. In this there was a lesson: To get the best job, you had to weather the most abuse." Chapter 4, pp. 63

"The difference between a trader and a salesman was more than a matter of mere function. The traders ruled the shop, and it wasn't hard to see why. A salesman's year-end bonus was determined by traders. A trader's bonus was determined by the profits on his trading books. A salesman had no purchase on a trader, while a trader had complete control over a salesman. Not surprisingly, young salesmen dashed around the place looking cowed and frightened, while young traders smoked cigars." Chapter 4, pp. 68

"Wall Street brings together borrowers of money with lenders. Until the spring of 1978, when Salomon Brothers formed Wall Street's first mortgage security department, the term borrower referred to large corporations and to federal, state, and local governments. It did not include homeowners." Chapter 5, pp.83

"The problem was more fundamental than a disdain for Middle America. Mortgages were not tradable pieces of paper; they were not bonds. They were loan made by savings banks that were never supposed to leave the savings banks. A single home mortgage was a messy investment for Wall Street, which was used to dealing in bigger numbers." Chapter 5, pp. 85

"Dall felt sure this was the wave of the future. He thought the boom in demand for housing would outstretch the sources of funding." Chapter 5, pp. 89

"From the moment the Federal Reserve lifted interest rates in October 1979, thrifts hemorrhaged money. The entire structure of home lending was on the verge of collapse. There was a time when it seemed that if nothing were done, all thrifts would go bankrupt." Chapter 6, pp.103

"But if you planned to run with this new market, you did not have time to check every last property in a package of loans. Buying whole loans (that is what the traders called home loans, to distinguish them from mortgage bonds) was an act of faith, like eating bologna." Chapter 6, pp.107

"The beautiful inefficiency of mortgage bonds was spoiled for Salomon by one of its own creations, called the collateralized mortgage obligation (CMO). It was invented in June 1983, but not until 1986 did it dominate the mortgage market. The irony is that it achieved precisely what Ranieri had hoped: it made home mortgages look more like other bonds. But making mortgage bonds conform in appearance had the effect, in the end, of making them only as profitable as other kinds of bonds." Chapter 7, pp. 136

"In explaining the birth of the mortgage department, for example, the author unearthed old newspaper quotes from the likes of Bob Dall, saying, 'What Salomon has that no other major firm has is a tremendous flexibility to let your skills end up where they are most productive.' The most interesting thing about this statement is what was going on behind the speaker's back when he made it. The quote was recorded six months before Dall was shoved aside by Ranieri to be left twisting in the wind by Gutfreund." Chapter 8, pp. 160

"There was in every office of Salomon a systemwide loudspeaker, called the hoot and holler or just the hoot. Apart from money, success at Salomon meant having your name shouted over the hoot. The AT&T trader's voice came loudly over the hoot: 'Mike Lewis has just sold three million of our AT&Ts for us, a great trade for the desk, thank you very much, Mike.'" Chapter 8, pp. 165

"So, in New York, bond and stock deals are driven not by whether investors (lenders) want to buy them but by whether companies want to raise the money." Chapter 9, pp. 196

"We had built a giant and omnipotent mortgage department; then we let half of it leave and fired the rest." Chapter 10, pp. 211

"Not surprisingly, the line between debt and equity, so sharply drawn in the mind of a Salomon bond trader (Equities in Dallas!), becomes blurred in the mind of a Drexel bond trader. Debt ownership in a shaky enterprise means control, for when a company fails to meet its interest payments, a bondholder can foreclose and liquidate the company." Chapter 10, pp. 217

"In that case, someone in New York made some pretty quick decisions, because later today two entire departments on 41, municipal bonds and money markets, consisting of around five hundred people, were summarily dismissed." Chapter 11, pp. 232

"Who'd have imagined that our largest single equity underwriting would coincide with the largest drop in history in the stock market? Then who'd have imagined that our first big junk bond deal would coincide with the crash of the junk bond market? It was striking how little control we had of events, particularly in view of how assiduously we cultivated the appearance of being in charge by smoking big cigars and saying fuck all the time." Chapter 11, pp. 241-242

Topics for Discussion

Identify and describe key features of the game Liar's Poker

Explain the process of employment search and interview Michael Lewis undergoes to secure a job in investment banking.

Identify and describe the characteristics of the over-stuffed turkey example that the author uses to illustrate how Salomon Brothers and other investment banking firms make money.

Describe and discuss the training process that Salomon uses to introduce new employees to the various departments.

Identify and describe several examples of goofs that occur at Salomon. Identify and discuss the impact of this type of activity in your own life.

Explain and discuss several features of the U.S. economy that allows Ranieri to develop and expand his mortgage bond department.

Describe and identify specific reasons why the traders begin to leave Salomon.

Explain the structure of a CMO that enables broader investor group interest.

Discuss and identify the characteristics of a geek and how a Salomon employee may advance beyond that name.

Describe and discuss the transaction that Michael and Alexander devise together.