SUMMARY

THE WISDOM OF FINANCE

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Summary of “The Wisdom of Finance” by Mihir A. Desai

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Learn about the surprising life lessons we can glean from the world of finance.

Introduction

When you think of the financial sector, what comes to mind? Do you envision corporate fat cats strolling down Wall Street? Do you imagine shady business dealings and billionaires haggling over more money than you'll ever see in a lifetime? If so, you're not alone! There's no doubt about it: whether we're thinking about Wall Street or the IRS, our perceptions of the financial sector don't inspire warm and fuzzy feelings. But Mihir Desai argues that the world of finance is more complex-- and, in fact, more beautiful-- than our current perspective imagines. Because we've all heard the saying "life imitates art," but you might be surprised to learn that life, art, and finance are intricately connected to one another! And by exploring their relationship, the author posits that we can actually learn a number of valuable life lessons. So, over the course of this summary, we'll learn about the interconnectedness of art and finance and the wisdom these disciplines can offer us.

The Great Divide

Would you say you're comfortable with the world of finance? Do you know the ins and outs of a mortgage? Can you competently do your own taxes every year? Does the legalese of a loan make sense to you? If you're like most people, you'll probably answer those questions with a resounding, "No!" In fact, most of us feel lucky if we're able to successfully write checks and pay our bills. Many people struggled through high school or college economics and now we're only too happy to put our bills on AutoPay or trust our banking apps to keep track of our purchases for us. Similarly, we're very glad to hand our taxes over to an account or a software program like TurboTax every year. But have you ever wondered why that is?

The author has explored this question in detail and concluded that our comfort with financial ignorance stems from something he refers to as the "Wall Street/Main Street" divide. Put simply, this means that the average person thinks of Wall Street (and, by association, the entire financial sector) as existing in a world of its own. And it doesn't help that the language is hardly accessible to the layman. As a result, the world of finance appears to be secretive, secluded, a private club that may or may not grant us admission. Add the fact that the financial sector has substantial power over our hard-earned money and the feelings of confusion and animosity only intensify. And because we neither understand nor trust the world of finance, we're also not very interested in learning more about it. So, we drift through life with negative assumptions and a lack of financial knowledge that could really help us in our daily lives.

But the author believes that financial knowledge should be accessible to everyone. In fact, he argues that the guiding principles of the financial sector are actually so versatile that they can help us make better life decisions! So, in the following chapters, we're going to take a look at his top tips for crossing the "Wall Street/Main Street" divide and applying financial knowledge to our daily lives.

The Principles of the Stock Market Can Help You in Real Life

How much do you know about the stock market? We see it on the news all the time, with headlines announcing that the stock market has “closed for the day,” or that a certain type of stock has decreased in value or suddenly gone up in value. But what does any of that mean? Most of us don’t know much about how it works. This is especially true for members of our younger generations, as our education system often neglects to teach them practical financial tips for life. So, before we dive in to the stock market’s actionable tips for our daily lives, let’s take a minute to learn a bit about how the stock market works.

We can think of the stock market as being like the grocery store. If you want to buy groceries, you go to the supermarket, right? Similarly, if you want to buy stocks, you go to the stock market. Just like a grocery store, the stock market offers stocks or “mutual funds” in pretty much every flavor you could imagine. Unlike the supermarket, however, the stock market isn’t in a single, physical location and it doesn’t have fixed business hours in the same way that your local grocery store might close at 10:00 pm. Instead, you can purchase stocks online. (Yes, it’s really that easy!) It might surprise you to know that you don’t have to be a professional investor or even someone with a great deal of financial acumen; anybody can buy stocks! In fact, with just a little friendly financial advice, you can invest in stocks through your employee retirement plan (often called an IRA) or something called a brokerage account.
But why do people invest in the stock market? And what can you hope to get out of it? The primary reason people invest in the stock market is because it gives you an opportunity to grow your money. By investing in a company’s success, your money can literally double itself without you having to do anything! So, let’s say you invest in a company like Exxon. As the company grows and succeeds, their stock increases in value, and you profit from that success. But let’s imagine that you invest in Exxon and only in Exxon. If Exxon’s stock does really well, you’re making money and everything seems pretty awesome. But what if Exxon’s stock suddenly decreases in value? What if your stock is now totally worthless? What if you realize that you’ve made an investment and you’ve just lost everything? What do you do now?

Well, this is why we have the principle of diversification. Diversification is a financial term that does exactly what it sounds like: it's all about diversity or having stocks in a diverse variety of companies. For example, instead of sinking all your money in one company or one industry, you should spread it across multiple areas so that you have stocks in the banking industry, the beer industry, or the automotive industry. This is a great strategy because it provides you with multiple contingency plans and diversifies your financial risks. For example, maybe it's not a great time for Exxon right now; maybe the oil and gas industry is just really struggling at the moment. But luxury automotives might be really hot right now! So, even though your Exxon stock is a bust, your Ferrari stock is doing great! This means that even if you lose in one area, you haven't put all your eggs in one basket; your stocks are diverse enough that their success can cancel out another's failure. As a result, your losses aren't quite so substantial because you're continuing to make money!

And this is where the life lessons come in because this principle applies to other facets of the human experience as well. In life, as in the stock market, human beings have a tendency to put all their eggs in one basket. For example, we might bank on getting one job in particular or on spending our lives with a certain person. And if these things don't work out, we feel shattered, displaced, and shaken to the core, just as we would if we invested all our money in something and then lost it. That's why the author believes that it's vital to diversify our relationships, expectations, and interests as well. So, if you've just started dating someone new, don't neglect your friendships and spend all your time with that new partner. And if you have a dream job in mind, don't live as though that's the only job you'll ever get; make a few backup plans along the way so you have some opportunities to fall back on. Diversification is important in all areas of our lives because it helps us plan for contingencies and cultivate stable futures. Plus, if you diversify your interests, hobbies, and friendships, you'll be a happier and more interesting person! So, don't let yourself get stuck in a rut and don't allow your perspective to become limited and myopic. Diversify and let yourself (and your finances) grow!

All's Fair in Love and Finance

At first glance, that title might sound unfathomably weird. After all, what could those two things possibly have in common? When we think of love, for example, we think of all things pure, kind, and wholesome. By contrast, we often refer to money as being "the root of all evil." So, if love is what brings us together, surely money is what tears us apart. The author agrees that this can often be true, but he acknowledges that there's another side to the financial sector; in fact, it's a side that can teach us a lot about our romantic relationships. So, let's take a look at a transaction that we would never equate with romance: a financial merger.

It might sound like these relationships have nothing in common, but let's think about it for a minute. Because a merger is what happens when two businesses come together. And a romantic relationship is what happens when two people in love come together. In both cases, two become one because both parties think that the union will be mutually beneficial. And in some cases, that's true! Sometimes, mergers are a great idea and both companies (or people) reach new heights of success. But what about the times when it isn't such a great idea? What about those times when we rush into things or use another person to fill a hole in our lives? Sadly, those mergers rarely work out-- whether they occur in our personal lives or the financial sector-- and they can be disastrous for both our hearts and our finances. And yet, they occur all too often.

Many times, businesses rush into mergers without really getting to know the other company or their business practices. This means you're likely to be blindsided by unexpected problems later on and that can be deadly for your company. For example, let's say that you buy out another company and assume that it's going to be a great fit. Because that company seems compatible with yours on the surface, you neglect to perform your due diligence in checking them out and run headlong into the merger. But then you start noticing some discrepancies in their accounting system or some major issues in their HR policies. Now, you're stuck with a company that's actively engaged in fraud or in discriminatory hiring policies and their flaws have the potential to wreck your company.

The same is true when we rush into relationships. Sometimes we meet a person who seems attractive and charming or who gives us those romantic butterfly feelings you hear about in love songs. Maybe they laugh at your jokes and make you feel good about yourself. On the surface, everything seems perfect, so you jump into a relationship with them, only to discover that-- once you really get to know them-- they're selfish, lazy, and inconsiderate. Instead of being blissful and romantic, your new relationship now causes you a lot of confusion and pain. This is especially true when we try to use someone else to fill a hole in our lives. On a personal level, this might happen because you're lonely and you meet someone who makes you feel less alone. In the financial sector, this often occurs when you feel like your company is lacking something and it needs a boost. For example, maybe you don't know how to market your product to younger consumers, so you join forces with a hip new tech company, thinking they can fix your image.

But in both cases, these are only temporary fixes born of desperation. This means that they are almost always unhealthy and therefore unlikely to lead to success. That's because neither of these pairings are based on genuine compatibility with another person or organization. So, as you can see from these examples, financial mergers have a lot in common with romantic relationships! And as we learn about best practices within the financial sector, we can also learn some practical lessons for life and relationships.

Final Summary

We often view the world of finance as being aloof and unrelated to the lives of the average person. But the financial sector actually has a lot in common with our daily lives and financial top tips can teach us some practical life lessons. For example, we can see that diversification is always a good thing, whether it's applied to your life or your stock portfolio. And as we study corporate mergers, we can see that rushing into relationships is never a good idea, whether it's with another company or a romantic partner. Instead, it's best to take your time, assess your relationships for mutual compatibility, and cultivate a wide variety of friends, relationships, opportunities, and interests.