

William Stephen Kamman  
1332 McGee Avenue  
Berkeley, CA 94703  
917 626 7439  
[Steve@King-Alpha.com](mailto:Steve@King-Alpha.com)

May 7, 2019

**LETTER #2 In Advance of Meeting with Don Listwin**

Don Listwin,  
c/o Ms. Suzanne Tom  
Corporate Secretary, Calix  
2777 Orchard Parkway,  
San Jose, California 95134

Dear Don,

I'm sending this for a few reasons.

It saves you listening to me hash it through. I might find that cathartic, but it would waste our time and your time.

It gives you time to digest it.

Awkward things are often better and more clearly said in writing.

Per my e-mail: *“What I want is in your best interests, Calix's best interests, and Carl's best interests. How we get there? I'm flexible. If come out of this with my ego bruised and Calix on a path to realize its latent potential, then sign me up. I'll get over it. But lets not repeat the same experiment and hope for different results.”*

***What assumption am I making? What is axiomatic to the conversation?***

My letter reflects general investor concerns. Investors use quarterly execution as a proxy for general management competence. Calix's track record has given it a *general* reputation for strong vision and weak execution.

- Investor's assume; *“If they can manage the earnings game smoothly, they are probably managing the internals smoothly. And vice versa.”* Arbitrary and inexact, but rational. Investors can't sit in on board or management meetings. So we use the best proxy we have.
- Investors set the rules. Playing by them is in Calix's best interests. Calix's interests come ahead of Carl's ego. Carl may not enjoy playing by those rules. But Calix is not his hobby farm.

***What is my primary source of concern? Why did I pull the fire alarm?***

Per my letter: *“We are one mis-step away from a ruinous cash crunch.”*

- I got home from a conference, updated my model, and realized the gravity of Calix's

cash situation. Trading volumes are too low for me to “vote with my position” and just exit. I can't risk a cash raise. Nor can you.

- I'd already decided engaging with Carl wasn't helping. Thinking through post-call scenarios, I realized how much confidence I'd lost. I'm having to plan for the worst.
- No-one wins if Calix slides politely into a cash crisis.

### ***Why am I proposing that Calix hire a COO?***

I meant what I said in my letter. *“Carl has taken Calix to the cusp of great things. He has delivered inspired, visionary innovation. “But [Carl's] execution has taken Calix to the brink of a cash crisis... At this point, Calix needs execution more than it needs vision. Especially given the tight cash situation. Hiring a strong COO will cost shareholders less than raising cash on ruinous terms.”*

- I like Carl as a person. I'm sad to have to burn this bridge. I respect his intelligence and vision. AXOS and EXOS are genius, gutsy ideas in a space where no-one else saw room for innovation. They never would have happened without Carl. I'd like to keep Carl's vision and ability engaged at Calix. And Carl deserves to take the victory lap if/when it bears fruit.
- But the cash cushion has gotten too thin to keep indulging Carl on executing to that vision. There are all sorts of mitigating circumstances. But nothing other companies don't navigate with less drama.
- We don't know how much an empowered COO can help, but he/she probably can't hurt.
- We don't have enough margin of error to risk doing nothing.
- Calix has shown a persistent pattern of unrealistic forecasts with unrealistic margins of error. Execution to forecast is the market's proxy for general management competence. At some point, perception becomes reality.

### ***What I didn't say in my letter. Calix needs a fresh face to tell a fresh story.***

Calix will have a great story to tell in a quarter or so. But a lot of people are (justifiably) unwilling to hear it from Carl.

That is why it is so hard to get meetings. Too many bridges burned too many times in too many places with too many people. *“Every time we've listened to this guy, we've lost money. So I just won't take the meeting. Saves me an hour and the risk we lose money again.”*

Calix needs a fresh face to tell a fresh story.

This is my key question/concern/takeaway point for our meeting. *Do Don and the Board understand...*

- *...how badly damaged Calix's reputation and prospects are among investors? **No buy-and-hold investor has ever made money in CALX.** It comes up in conversation as a joke or cautionary tale. Mostly it just doesn't come up at all.*
- *...the damage isn't temporary? Low trading volumes and multiples make that clear.*
- *...how much Carl's “Carlax” (as he used to call Calix) messaging over the past 8 years*

*has personalized and concentrated that negativity on Carl himself?*

- *...how long it would take Carl to rehabilitate his reputation? We don't have that kind of time.*
- *...how resistant Carl is to playing the game by the rules investors set? When was the last time you sat in on a 1-on-1? I've tried to engage Carl on this over the last 18 months. My conclusion is Carl is unwilling or unable to change his approach.*
- *...how hard it would be to raise cash if a downturn hits? It would be brutal.*
- *...how close Calix is to losing analyst coverage? Coverage is a privilege not a right. Calix has burned a lot of sell-siders. Ask them.*
- *...how much multiples and trading volumes would rebound if investors simply regain confidence the trains will run on time? We need a fresh face to do that.*

A credible, competent, fresh-face COO can get a fresh hearing. Putting his/her (earned elsewhere) credibility on the line. The facts should carry CALX from there. Presuming the COO has the mandate and authority to deliver reliable execution and quarterly results.

***Don't Take My Word For It. Talk to Investors and Analysts.***

Double-check the above. Spend a day in Boston and New York. See what other investors and analysts think. Especially shops that won't take a meeting with Carl. People *will* take a meeting with you. *What do we need to do for Calix to re-gain consideration?*

Your reaching out would, itself, be a positive catalyst. It will get Calix a fresh look.

A roadshow does put your reputation on the line. That can serve as a useful gut check. If taking that reputational risk on gives you pause, you've got your own answer on whether change is needed at Calix.

***Calix needs a higher stock price for internal reasons.***

Employees are the ultimate buy and hold investors in a company. A steadier, get-it-done COO could shore up enthusiasm among a workforce that probably needs a boost as much as investors do. Everyone wants to feel their team is playing for a win.

A win in this game means a higher stock price. Based on more reliable results. Founded in renewed investor and employee confidence in execution. Communicated by a fresh face with the credibility to tell the story. Playing to win by the market's rules.

Feel free to share this with the board when you discuss my original letter. To that end, I am sending it via Ms. Tom.

Sincerely yours,

Steve Kamman

Steve Kamman  
1332 McGee Avenue  
Berkeley, CA 94703  
917 626 7439  
[steve@king-alpha.com](mailto:steve@king-alpha.com)

April 24, 2019

**LETTER #1 Raising My Concerns With the Board**

Don Listwin, Chairman of the Board  
c/o Corporate Secretary, Ms. Suzanne Tom  
Calix  
2777 Orchard Parkway,  
San Jose, California 95134

Dear Don and Members of the Calix Board,

I have grave concerns about the current and future direction of Calix. I assume you share many of them. Sometimes it helps to have someone else put those concerns into words. Hence this letter.

Carl needs help. He may be too proud to admit it. But you can help him nonetheless.

In my view, Calix needs a strong, empowered COO to help Carl run operations day-to-day.  
Someone whose joy is making the trains run on time.

Calix has the potential to do great things. But it needs someone to dig in and *do* those things. It needs consistent, focused, careful execution that drives steady cash flows. Especially given how far Calix has run down its cash reserves.

Taking that load off Carl serves the best interests of the majority of (non-executive) Calix shareholders. A COO's salary is less expensive than a cash raise.

Continuing with an un-changed executive structure would amount to repeating the same experiment, but hoping for different results.

***Carl Needs Help. He's Taken Calix as Far as He Can Alone.***

Carl has taken Calix to the cusp of great things. He has delivered inspired, visionary innovation. But his *execution* has taken Calix to the brink of a cash crisis.

- The trap was loaded by spending \$40 million of cash reserves on share buybacks just before losing tens of millions on cash-burning Services contracts – all while operating at a structural loss.
- Calix now risks springing that trap shut after mis-executing a crash plan to shift production out of China in only 2 quarters.
- We are one mis-step away from a ruinous cash crunch.

In his prior roles, Carl has done best when paired with strong, operationally-minded executives

to handle the day-to-day. Calix shareholders have suffered from the absence of that complementary, counter-balancing skill set.

Calix' stock is @60% below its IPO price over a period the S&P 500 returned 198%. CALX has generally traded below 1x EV/Sales for 3+ years. The company has burned down cash. It is now navigating its 2<sup>nd</sup> self-inflicted operational crisis in 2 years. We may risk a cash crunch. All while the economic backdrop has been improving.

***I've Owned a Lot For a Long Time. I Know Calix and Carl Well.***

I own 300,000 shares of Calix (some since 2011). That puts me among your top 10-20 shareholders. If you eliminate computer-driven and index funds, I am likely one of your top 10 *human* shareholders.

I know Telecom Equipment and Calix. I covered both at Fidelity Investments and CIBC/Oppenheimer since 2001. At Fidelity, I bought into Calix's 2010 IPO at \$13. Over 2011-2013, I experienced first-hand a now-familiar pattern of bold promises (taking CALX to \$22) and weak follow-through (driving it down to \$5).

I also know Carl Russo well. I first met Carl in 2001. I am personally fond of Carl. But I have done my due diligence over those 18 years. Carl is a visionary thinker and a great salesperson. He is less strong in execution.

Over the past year and a half, I have sought to engage with Carl. I have concluded that is no longer, and may never have been, constructive.

***Calix's Recent Track Record Points to Continuing, Structural Weakness in Oversight, Controls, and Operational Execution.***

Operational discipline has been a recurring weakness at Calix since the IPO. But I will focus here on patterns over the past two years. In 2017 and now 2019, mistakes were made that lie directly in the remit of a CEO or COO.

- Supervision, oversight, and remediation of Executive-level errors.
- Internal communications and chain of command.
- Investor communications, relationships and reputation.

**2017:** Unrealistic targets, weak oversight and flawed execution dragged Calix into a self-inflicted crisis that consumed tens of millions of dollars. We can't quantify revenues lost from un-signed customers worried about viability/valuation. Most investors walked away.

Carl is not responsible for negotiating those money-losing contracts. But look past that immediate error. Consider the response that followed.

*My concern lies in how long it took - 5 to 8 months - to uncover, investigate, and scope those losses. It was a delayed, fumbling reaction that points to deeper structural problems. That failure of supervisory oversight was the CEO's responsibility.*

- On the May 9, 2017 call, Calix gave guidance for an extremely strong second half rebound. This was based on (false) confidence the Services problem was confined to Windstream. In retrospect, that guidance was clearly fantastical.

- **Evidently, 5+ months in, senior executives still hadn't understood the breadth and depth of the baked-in contract losses that would drag down the rest of 2017.** Calix had already fired the executive responsible. *Why hadn't anyone dug deeper by May 9<sup>th</sup>?* An effective operational manager would have immediately investigated and quantified the risks embedded in *all* the contracts. Instead, Calix sailed on blindly toward an iceberg dead ahead.
- **A broken internal communications dynamic is the most likely explanation for how senior management remained ignorant long enough to deliver that fantastical May 9<sup>th</sup> guidance.** It took 5 to 8 months for Executives to understand the damage buried in those contracts. *It beggars belief that lower-level staff at Calix didn't already know more Services contracts were rotten. So why didn't senior management know until sometime between May 9<sup>th</sup> and August?* Middle and line management clearly chose NOT to pass the bad news up the chain of command. Senior management didn't dig deep enough to find out. Then it bubbled up in the numbers.
- Calix didn't disclose the damage to shareholders until the scheduled August 2017 call. With no pre-announcement, the result was a chaotic “surprise” call that lacked clarity. The stock dropped @40%. The reputational damage was far greater. Analysts have dropped coverage. Meeting schedules are hard to fill. I know first hand than many investors have simply removed CALX from consideration. Calix is generally perceived as a sort of “hobby farm” for Carl.

**2019 - Echoes of 2017:** Calix is exhibiting a similar pattern of failure in the botched production shift out of China. I do not yet know, before the call, how bad the situation truly is. *Even if it isn't as bad, 2019 bears the same hallmarks of insufficient oversight and poor internal/external communication.*

- Overly aggressive targets set beyond the organisation's capability to deliver.
- Weak oversight of day-to-day execution to reach those targets.
- Delayed recognition and/or disclosure of the problem. Calix held its call on February 5<sup>th</sup>. *Someone at Calix already had to know production was going badly 5 weeks in with only 7 weeks to go.*
  - If Senior Management didn't know. *Why isn't bad news making it up the chain? What structural/cultural failings does this point to?*
  - If Senior Management did know. *Wasn't it already evident by February that Calix would struggle to make its 1Q19 production goals? Why wasn't that disclosed? When was the Board told?*
  - The February call also saw a -25% stock price drop from a revenue miss Calix' management did not judge material enough to pre-announce. *News that cuts the price -25% would seem “material” by definition. That judgement call further undermined investor confidence in Calix.*

**To Achieve Carl's Vision, Calix Needs Someone to Execute On It. A Different Skill Set.**

Steady, focused, operational oversight is critical at any company. A repeated pattern of failure

in 2017 and 2019 makes clear that is lacking at Calix.

Carl is a visionary thinker and a brilliant salesman. He deserves tremendous credit for bringing Calix to the cusp of great things.

But Carl is (still) operating without the effective, empowered counter-balance he so clearly needs. That balance was key to his prior success.

Mistakes will be made. A COO won't stop that. A strong COO *can* minimize shareholder's losses from those mistakes. Surfacing problems before Calix sails blind into an iceberg. Setting achievable targets with realistic margins for error.

*At this point, Calix needs execution more than it needs vision.* Especially given the tight cash situation. Hiring a strong COO will cost shareholders less than raising cash on ruinous terms.

***An Intervention Serves the Best Interests of Non-Executive Shareholders. The Board Should Help Carl. Even if He Isn't Asking for Help.***

Today, Carl is still alone at the helm. He is too stretched. He has no-one to counterbalance his blind spots. He needs someone.

The situation does not give me a great deal of confidence in Calix's prospects. Especially over an operationally critical 2 years with so little cash on hand.

I invested in Calix because its valuation did not appear to square with its future prospects. Today, Calix *still* could be on a path to great things. That much-delayed potential is why I have so far held on to my investment.

- With Verizon, CityFibre, and others ramping up spending, 2020 Revenues of \$500m to \$600m and Earnings of \$0.50 to \$1.00 seem reasonably achievable.
- With 5G ramping up and broadband becoming a basic utility, revenues and EPS well above that are achievable in 2021 and beyond.

Calix needs focused, steady, patient execution.

Carl needs help.

Hire someone to help. Get the trains running on time.

Your views may differ, but I am sure you have considered some of this yourselves. My hope is this letter might clarify those thoughts and encourage you to act on them. I look forward to discussing this further.

Sincerely yours,

Steve Kamman