

# Calix (CALX) - Its a Hobby Farm, But Still 2x or Greater Upside. Update 26May2019

I figured I owed an update on Calix after a pretty eventful month. Over the course of May, I've written two letters to Calix's Board and met once with Calix's Chairman Don Listwin. I also wrote an investment outlook in Seeking Alpha. All are attached.

The meeting with Calix's Chairman was productive, but not constructive. My specific suggestion was that Calix hire an empowered, execution-oriented COO to balance its more visionary CEO. He flatly rejected that idea. Nor did he accept my other concerns.

My “*Getting Better or Getting Worse?*” conclusion is below, but I would encourage you to read the attached documents. The letters were carefully written to be as constructive as circumstances allowed.

The Seeking Alpha investment write-up was my attempt to answer the Chairman's repeated question of “*If you are so unhappy, why don't you just sell the stock?*” That I would instead try to effect change as a co-owner seemed to perplex him. More worrying, it seemed equally beyond him that Calix's Board might take action itself. His passivity left me perplexed in turn.

## *Getting Better or Getting Worse?* **Getting Better**, but Calix Will Always Be a Hobby Farm.

Per my 3Q18 comment, “*things are good enough even these yahoos (probably) can't screw it up.*” I was wrong then, but still (I think) directionally correct..

### Short Term – Positive Catalyst Ahead

- Calix remains cheap vs estimates for a reason. No-one has confidence they can execute and actually *hit* those estimates. The cash situation is now also dangerously tight - the immediate reason I decided to write to the Board.
- But all that negativity baked into the stock also creates a clear, near-term positive catalyst if they fix recent production problems. Critically, that fix is less a bet on Calix's (in)competence and mostly a bet on the competence of their outside contract manufacturer. The CM's are generally competent folks, so this is probably a good bet at the current price.
- Calix still has great technology with customers that will drive strong revenue growth as 2019 plays out. The second half of 2019 was always going to show solid organic demand. The 1st/2nd quarter production shortfalls will further boost the second half by adding in catch-up sales on previously unfilled orders. That solves for a strong 2H19 which should put Calix back on the path past \$11. Where it was in December before their most recent screw-ups.
- From there, I'll re-assess my position. Factoring what I've learned about Calix's long-term execution and governance weaknesses into that decision. See the attached [Seeking Alpha article](#) for more details, valuation and price outlook.

### Long Term – Calix Will Never Amount to More Than a Hobby Farm (Absent External Activism).

- If Calix had better management, Calix could be a great company. It doesn't. It won't be. Calix's Board is unlikely to change or shore up current management.

- In my letters and meeting, I did my best to puncture the bubble of mutually-reinforcing self-regard surrounding the CEO, Chairman, and at least one other Board member. I believe I failed to do so. The emperor still thinks his new clothes are just dandy. His buddies are still reassuring him “everyone” agrees. [The parade goes on](#). I’ve got a more psychologically explanatory analogy rooted in Orson Welles “Citizen Kane,” but it was too much to dive into here.
- In short, Calix will remain a hobby farm - run primarily for the CEO and insider's gratification. I did consider that risk 3 years ago. My bet was the CEO would fear the public shame of investor indifference (now verging towards ridicule) more than the private shame of asking for (needed) help. That bet proved wrong.

**Depressing, but still a 2x or more return from where it is today. Going from “Awful” to “OK” still makes for a nice gain.** Its too bad going from “OK” to “Good/Great” looks so unlikely. But if Calix's CEO and Board won't square up to that, we don't have to stay along for their ride.

## Meeting with Chairman Don Listwin – Productive, But Not Constructive

Productive. I learned a lot.

- I learned a lot about Calix's governance. Or lack thereof.
- I came away more confident with the bet Calix likely recovers from its production woes and posts decent 2H19 numbers. *Why?* The Chairman seemed to be almost daring me to sell out at \$6.50.
  - From his tone, he was presumably anticipating my future regret after CALX's price recovered. I read that as confirmation he believed the short-term cash situation is manageable and the contract manufacturer is likely to resolve the production problems. Of course I may have misread him. *Also his confidence in Calix could prove misplaced.* It has certainly disappointed before. Per the attached article, I'm basing my bet on the more solid plank of the contract manufacturer's competence and incentives. Plus what we already know publicly about customer demand.

But Not Constructive. I concluded Calix is a hobby farm. Per my meeting wrap-up notes.

- Chairman Don Listwin does not seem particularly interested in constructive engagement with shareholders. He seems to view public markets investors more as renters than as co-owners. He expects shareholder concerns to be dealt with by shareholder exits, not by Board action. He asked me several times “*why haven't you just sold the stock.*” I felt like a vexatious tenant being asked by a landlord “*if you're so unhappy, why don't you just move out?*” It was not a conversation between co-owners.
- He did not see scope for the Board to take action that might realize more value faster for all owners. In general, he had a curiously passive, victim's view of his and management's role at Calix.
  - He seemed to view the low share price as reflecting poor judgment by overly short-term investors. The valuation stemmed from the market's lack of vision, not investor's lack of confidence in execution based on Calix's prior track record.
  - What I saw as mis-execution, he saw as Calix management falling victim to unfortunate external circumstances.
  - He did not see room or reason for the Board to take action that might improve or reinforce management and execution.

- Absent a split within the Board, I concluded further private engagement with Calix's Board probably wouldn't be constructive or productive. I remain unclear as to why the activist investor on the Board (Dan Plants of Voce Capital) has had so little impact. Regardless, given the above, internal change is unlikely at Calix given the current Board. Change will come either through further external activism, or not at all.

## The Seeking Alpha Article

Don kept pushing me on why I hadn't sold already. I went away and asked that same question myself. The article linked to below and attached came out of that exercise. Setting out the balanced investment case as I saw it. It is worth a review if you own CALX yourself. With particular reference to the section on management and governance.

*Why did I publish it?* I saw no point in further dialogue-of-the-deaf. So I figured I would make double use of the write-up. Seeking Alpha is a crowd-sourced research site. I've found it a useful resource for under-followed stocks. I figured a write-up there would shine a light into an otherwise ignored corner of the market. Any illumination is better than none, even if it necessarily casts a fairly harsh light.

<https://seekingalpha.com/article/4264289-calix-cheap-reason>