



## Top Stories: Unsung Heroes: Surfing Against the Tide

By **Kevin Petrie**  
Staff Reporter

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*This story is part of our weeklong series, Unsung Heroes. Please see our [introduction](#).*

'When people on Wall Street are in love with something, we look the other way'  
-- Mike Margolies



It takes bravado to knock a Wall Street darling -- especially a hot technology company blessed by all the white-shoe firms. Like **Ciena** ([CIEN](#):Nasdaq), for instance.

Early this year, remember, Ciena's venture capitalists, employees and mutual-fund investors had few doubts. The company had captured the lead in a revolutionary new technology to send more voice and data signals across fiber-optic networks. As revenue zoomed from zero to \$500 million in six years, Ciena boasted about leaving rivals like **Lucent** ([LU](#):NYSE) in the dust. Business publications -- *TSC* included -- gave Ciena glowing coverage as its stock soared.

Amid the exuberance, though, a Florida research firm urged investors to steer clear or, better yet, bet on a slide in Ciena's stock. **Avalon Research Group** -- founded in 1996 by **Oppenheimer & Co.** alumnus **Mike Margolies** -- issued a "sell/sell short" recommendation on Ciena way back in February when it was trading at 58.

"We got a lot of heat," says Margolies. The few other skeptics stuck with neutral ratings. Avalon, though, stands out because it draws no underwriting or advisory revenue from the companies it covers. Hence Margolies' sell rating.

His dissenting voice was brushed off as Wall Street lauded the proposed Ciena marriage to **Tellabs** ([TLAB](#):Nasdaq). Ciena's stock continued to climb.

But this summer the music stopped. Ciena lost a few key contracts. Then Tellabs fled the scene. Ciena stock fell 90% from its high of 92 in July.



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## Taking the Other Side of the Trade

A 16-year Wall Street veteran, Margolies started Avalon partly because he believes mutual-fund managers need some unbiased investment research amid all the wild enthusiasm. "When people on Wall Street are in love with something, we look the other way," he says.

Ciena is not the only target. His research team also has made other contrarian calls -- both on the long and short side. For example, **Chromatics Color Sciences** ([CCSI:Nasdaq](#)) is more than 50% lower since Avalon went bearish on it in February, though the stock initially rose and didn't crack until late spring. **Arterial Vascular Engineering** ([AVEI:Nasdaq](#)) is about 20% lower since a bearish call also made in February.

It's Ciena call, however, that earns Margolies a place on our list.

Sure, Ciena had seemed to revolutionize a new fiber-optic technology called wavelength division multiplexing, or WDM. This technology allows optical fibers to carry extra waves of light and more data.

## Game of Leapfrog

Yet, as Margolies noted in his Feb. 20 report, suppliers like Ciena would soon leapfrog each other to offer greater numbers of WDM channels. As an example, just look at the memory chip business. Once one megabit of memory was deemed sufficient, but soon companies were offering four megabits, 16 megabits and 64 megabits. Memory chips were treated as a commodity and prices fell dramatically.

The WDM business was a race of channels. Lucent and **Northern Telecom** ([NT:NYSE](#)) had already built the four-channel products, and even though Ciena had the lead with a 16-channel offering, its lead was by no means set in stone. Rivals with deep pockets such as Lucent were quickly adding more channels.

"You tend to be a little removed from all the **hype.**"

Did the Avalon call help clients? When asked about his 200 or so clients, Margolies said, "It's none of your business who our clients are. We never reveal the names of our clients -- we are like

priests."

But at least one manager shorted Ciena briefly after checking with Avalon and doing some independent sleuthing. "I thought they had a very good call on the stock," the manager says. "Events have proven them to be quite correct in their analysis."

Detractors might say Avalon missed the huge run-up in Ciena's stock -- from about 58 in February to 92 in July before it crashed to 8. Margolies concedes it's tough to time stocks. But investors who followed his call from the start at least would have staved off an 86% loss on a February investment -- a

loss that includes the year's gains. "We try to judge it the best we can, but sometimes the market just gets carried away," he says.

One footnote to all of this: Margolies briefly recommended buying Ciena on a short-term basis when it fell near 8 last month. Now that the stock is in the 19 range, he's neutral.

**Hero at a Glance:  
Michael Margolies**

Age 40

Job President, Avalon  
Research Group

Best Call Told investors to short  
Ciena in February

Challenges like Ciena are familiar territory to Margolies. Having grown up in Far Rockaway, N.Y., Margolies regularly surfed in the Atlantic Ocean. Now 40, he takes advantage of his Boca Raton location to head down to Costa Rica to surf, sans wet suit. In Boca, he practices yoga to relax.

Although Margolies works outside the establishment now, he served hard time in Manhattan, starting as a clerk on the floor of the stock exchange in 1982 and eventually rising to senior vice president with Oppenheimer. All without a college degree. He likes Boca Raton as a base, because it affords a clearer view of investing.

"You tend to be removed from all the hype," he says. "You can slow down half a click and see what's going on." In the case of Ciena, at least, his off-Wall Street perspective paid off.



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