



# Telephone & Data Systems (TDS)

Updated November 15<sup>th</sup>, 2022 by Quinn Mohammed

## Key Metrics

<b>Current Price:</b>	\$11	<b>5 Year CAGR Estimate:</b>	16.9%	<b>Market Cap:</b>	\$1.3 B
<b>Fair Value Price:</b>	\$19	<b>5 Year Growth Estimate:</b>	0.5%	<b>Ex-Dividend Date<sup>1</sup>:</b>	12/14/2022
<b>% Fair Value:</b>	56%	<b>5 Year Valuation Multiple Estimate:</b>	12.1%	<b>Payment Date<sup>2</sup>:</b>	12/30/2022
<b>Dividend Yield:</b>	6.7%	<b>5 Year Price Target</b>	\$19	<b>Years of Dividend Growth:</b>	48
<b>Dividend Risk Score:</b>	F	<b>Retirement Suitability Score:</b>	D	<b>Rating:</b>	Buy

## Overview & Current Events

Telephone & Data Systems is a telecommunications company that provides customers with cellular and landline services, wireless products, cable, broadband, and voice services across the United States. The company's Cellular Division accounts for more than 75% of total operating revenue. TDS started in 1969 as a collection of 10 rural telephone companies. Today the company has a market cap of \$1.3 billion and more than \$5.3 billion in annual revenues.

On November 3<sup>rd</sup>, TDS reported financial results for the third quarter of 2022. The company's total operating revenues were \$1.392 billion, up 5% compared to the same period one year ago. Net income was \$(25) million, down from last year's \$28 million. Diluted earnings per share of \$(0.22) also compared unfavorably to the \$0.24 earned one year ago. Higher postpaid average revenue per user (ARPU) at US Cellular drove service revenue growth since customers chose higher-value plans. Postpaid ARPU of \$50.21 was a 4.3% increase year-over-year.

Total broadband connections increased 4% year-over-year to 506,500 connections and residential revenue per connection grew 4.5% to \$60.32. In 2022, TDS plans to grow its broadband business and continue expanding its fiber footprint as wide as it can.

Management reduced the top end of 2022 guidance and expect service revenues at U.S. Cellular of around \$3.125 billion. Total expected operating revenues for TDS Telecom is unchanged around \$1.02 billion.

## Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
<b>EPS</b>	\$0.75	\$1.29	-\$1.26	\$1.98	\$0.39	\$1.37	\$1.17	\$1.03	\$1.93	\$1.00	<b>\$0.03</b>	<b>\$0.95</b>
<b>BPS<sup>3</sup></b>	\$37.16	\$37.85	\$36.39	\$37.86	\$37.67	\$38.45	\$40.00	\$40.46	\$42.02	\$41.84	<b>\$42.10</b>	<b>\$44.25</b>
<b>DPS</b>	\$0.48	\$0.51	\$0.52	\$0.56	\$0.59	\$0.60	\$0.64	\$0.66	\$0.68	\$0.70	<b>\$0.72</b>	<b>\$0.83</b>
<b>Shares<sup>4</sup></b>	108.0	109.0	108.0	109.0	110.0	112.0	115.0	116.0	116.0	116.0	<b>116.0</b>	<b>125.0</b>

TDS has an 82% stake in U.S. Cellular and essentially relies on this stake to achieve growth. In 2021, U.S. Cellular focused on connecting customers in underserved areas with their high-quality network, as well as market share expansion, increasing business with government customers in 5G and IoT, and improving network modernization and 5G programs. TDS Telecom grew broadband revenue with an increase in customer connections and expanded the reach of their fiber and 1Gig services. In 2022, all this continues, with strengthened focus on broadband and fiber.

The company has exhibited a volatile earnings record. During the last nine years, its earnings-per-share have increased approximately 3% compounded per year on average and decreased by 1.4% compounded per year on average for the last five years. Book value per share, on the other hand has grown by 1.3% and 1.8% per year over the last nine and five years on average. The book value trend is much more consistent. As TDS distributes more than half of its earnings in

<sup>1</sup> Estimate

<sup>2</sup> Estimate

<sup>3</sup> Book value per share

<sup>4</sup> In millions

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dividends, we are projecting a book value per share around \$43.16 by 2027 for a 0.5% average annual growth of book value over the next five years.

## Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/B	0.64	0.67	0.7	0.74	0.73	0.75	0.73	0.73	0.50	0.49	<b>0.25</b>	<b>0.45</b>
Avg. Yld.	2.1%	2.0%	2.1%	2.1%	2.1%	2.2%	2.2%	2.3%	3.4%	3.3%	<b>6.7%</b>	<b>4.2%</b>

Due to the volatility in the company's earnings history, we believe that the best way to assess the valuation of TDS is by looking at its price-to-book ratio. TDS is currently trading at a price-to-book ratio of 0.25, which is much lower than its 10-year average of 0.67. If the stock reverts closer to its average valuation level over the next five years, it will enjoy a 12.1% annualized gain.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

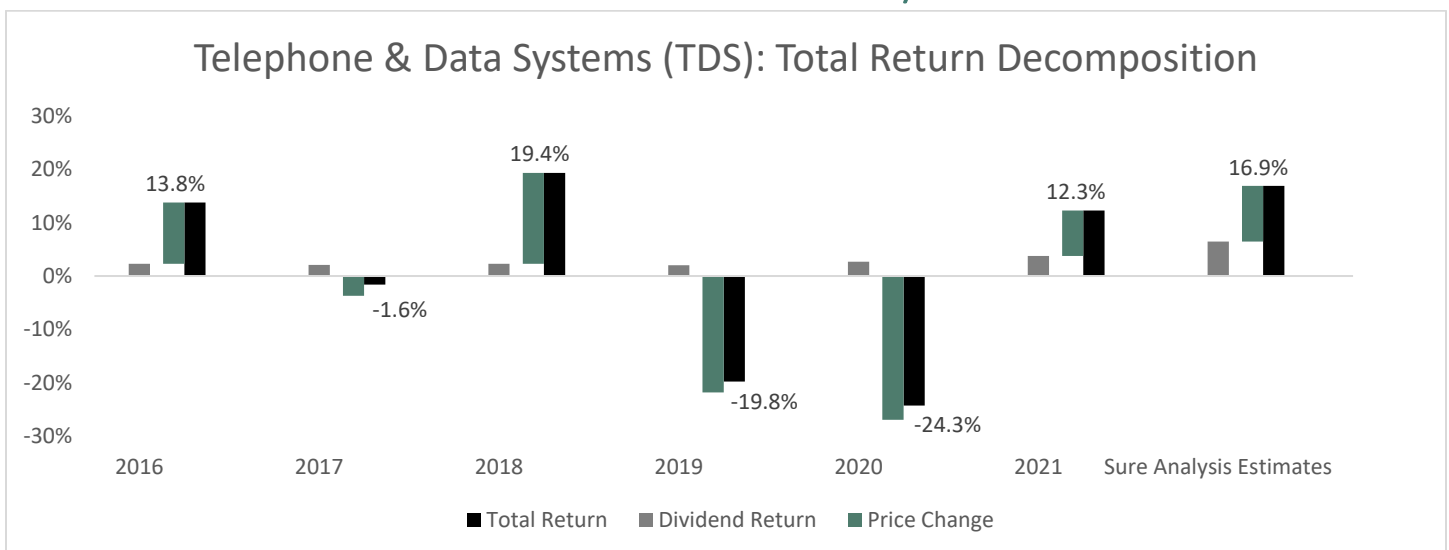
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	64%	40%	-41%	28%	151%	44%	55%	64%	35%	70%	<b>167%</b>	<b>83%</b>

TDS has raised its dividend for 48 consecutive years. It has grown its dividend by 3% per year on average over the past 5 years. Today, its 6.7% dividend yield is significantly higher than the yield of the S&P. As TDS and U.S. Cellular operate in a highly competitive business, the corporation lacks a meaningful competitive advantage. As U.S. Cellular generates the vast majority of the revenues and earnings of TDS and is currently its most important growth driver, any headwind that may show up in the way of U.S. Cellular will have an impact on TDS. TDS Telecom is fortunate in that its services have been heavily in demand throughout the coronavirus pandemic.

## Final Thoughts & Recommendation

TDS relies heavily on the performance of U.S. Cellular, however management is not forecasting exceptional growth currently. We forecast the stock will offer a 16.9% average annual return over the next five years. We have been somewhat conservative in our growth forecast due to the volatile performance record. We expect the bulk of returns to come from a mix of valuation expansion and yield. While the corporation trades well below our estimate of fair value and has strong total return prospects, we rate TDS a buy today.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
<b>Revenue</b>	5,345	4,901	5,009	5,210	5,155	5,044	5,109	5,176	5,225	5,329
<b>Gross Profit</b>	3,073	2,676	2,498	2,795	2,726	2,685	2,773	2,839	2,871	2,857
<b>Gross Margin</b>	57.5%	54.6%	49.9%	53.6%	52.9%	53.2%	54.3%	54.8%	54.9%	53.6%
<b>SG&amp;A Exp.</b>	2,034	1,948	1,865	1,781	1,762	1,689	1,694	1,717	1,681	1,677
<b>D&amp;A Exp.</b>	814	1,018	837	844	850	844	883	932	909	895
<b>Operating Profit</b>	225	-290	-204	170	114	152	196	190	281	285
<b>Operating Margin</b>	4.2%	-5.9%	-4.1%	3.3%	2.2%	3.0%	3.8%	3.7%	5.4%	5.3%
<b>Net Profit</b>	82	142	-136	219	43	153	135	121	226	156
<b>Net Margin</b>	1.5%	2.9%	-2.7%	4.2%	0.8%	3.0%	2.6%	2.3%	4.3%	2.9%
<b>Free Cash Flow</b>	110	-389	-404	-11	146	91	239	54	164	-48
<b>Income Tax</b>	74	126	-5	172	40	-279	46	64	19	33

## Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
<b>Total Assets</b>	8,624	8,904	8,854	9,422	9,446	9,295	9,783	10,781	12,525	13,493
<b>Cash &amp; Equivalents</b>	740	830	472	985	900	619	921	465	1,429	367
<b>Accounts Receivable</b>	410	552	549	705	753	861	992	1,005	1,004	1,058
<b>Inventories</b>	161	245	274	158	151	145	150	169	154	178
<b>Goodwill &amp; Int. Ass.</b>	2,336	2,456	2,534	2,901	2,938	3,020	2,957	3,266	3,398	4,841
<b>Total Liabilities</b>	3,967	4,234	4,398	4,717	4,695	4,402	4,479	5,366	6,922	6,748
<b>Accounts Payable</b>	377	496	387	349	365	368	365	374	508	481
<b>Long-Term Debt</b>	1,723	1,722	1,942	2,454	2,445	2,457	2,439	2,326	3,429	2,934
<b>Shareholder's Equity</b>	4,012	4,118	3,926	4,126	4,144	4,269	4,560	4,653	4,804	4,853
<b>LTD/E Ratio</b>	0.43	0.42	0.49	0.59	0.59	0.58	0.53	0.50	0.71	0.50

## Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
<b>Return on Assets</b>	1.0%	1.6%	-1.5%	2.4%	0.5%	1.6%	1.4%	1.2%	1.9%	1.2%
<b>Return on Equity</b>	2.1%	3.5%	-3.4%	5.4%	1.0%	3.6%	3.1%	2.6%	4.8%	3.2%
<b>ROIC</b>	1.3%	2.2%	-2.1%	3.2%	0.6%	2.1%	1.8%	1.6%	2.7%	1.7%
<b>Shares Out.</b>	108.0	109.0	108.0	109.0	110.0	112.0	115.0	116.0	116.0	116.0
<b>Revenue/Share</b>	49.07	44.91	46.38	47.36	46.44	45.04	44.82	44.62	45.43	45.94
<b>FCF/Share</b>	1.01	-3.57	-3.74	-0.10	1.32	0.81	2.10	0.47	1.43	-0.41

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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