



# Telephone & Data Systems (TDS)

Updated March 15<sup>th</sup>, 2023 by Quinn Mohammed

## Key Metrics

<b>Current Price:</b>	\$10	<b>5 Year CAGR Estimate:</b>	18.8%	<b>Market Cap:</b>	\$1.5 B
<b>Fair Value Price:</b>	\$19	<b>5 Year Growth Estimate:</b>	0.5%	<b>Ex-Dividend Date<sup>1</sup>:</b>	03/14/2023
<b>% Fair Value:</b>	52%	<b>5 Year Valuation Multiple Estimate:</b>	13.9%	<b>Payment Date<sup>2</sup>:</b>	03/31/2023
<b>Dividend Yield:</b>	7.3%	<b>5 Year Price Target</b>	\$20	<b>Years of Dividend Growth:</b>	49
<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 \$1.5 billion and more than \$5.4 billion in annual revenues.

TDS declared a 2.8% dividend increase to \$0.185 quarterly on February 16<sup>th</sup>, 2023.

On February 16<sup>th</sup>, 2023, TDS reported financial results for the fourth quarter of 2022. The company's total operating revenues were \$1.357 billion, down 1% compared to the same period one year ago.

Net income was \$(43) million, down from last year's \$14 million. Diluted earnings per share of \$(0.38) also compared unfavorably to the \$0.11 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 \$50.60 was a 4.1% year-over-year increase.

Total broadband connections increased 4% year-over-year to 510,000 connections and residential revenue per connection grew 3.5% to \$59.91.

During the quarter, TDS repurchased nearly 1.16 million of its common stock for \$14 million.

Management provided 2023 guidance and expect service revenues at U.S. Cellular of around \$3.1 billion. Total expected operating revenues for TDS is around \$1.045 billion.

## Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
<b>EPS</b>	\$1.29	-\$1.26	\$1.98	\$0.39	\$1.37	\$1.17	\$1.03	\$1.93	\$1.00	(\$0.07)	<b>(\$0.32)</b>	<b>\$1.15</b>
<b>BPS<sup>3</sup></b>	\$37.85	\$36.39	\$37.86	\$37.67	\$38.45	\$40.00	\$40.46	\$42.02	\$41.84	\$42.63	<b>\$43.00</b>	<b>\$44.09</b>
<b>DPS</b>	\$0.51	\$0.52	\$0.56	\$0.59	\$0.60	\$0.64	\$0.66	\$0.68	\$0.70	\$0.72	<b>\$0.74</b>	<b>\$0.86</b>
<b>Shares<sup>4</sup></b>	109.0	108.0	109.0	110.0	112.0	115.0	116.0	116.0	116.0	112.0	<b>112.0</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. TDS made investments in 2022 towards growing its client base, expanding into new territories, as well as improving their network technologies, in an effort to boost the company's competitiveness. In the year, TDS Telecom increased its footprint by 9% and delivered 133K new marketable fiber service addresses, bringing the total to 582K. The company has a goal of achieving 1.2 million fiber service addresses by 2026.

<sup>1</sup> Estimate

<sup>2</sup> Estimate

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

<sup>4</sup> In millions

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The company has exhibited a volatile earnings record. During the last nine years and five years, its earnings-per-share have shrunk considerably. Book value per share, on the other hand, has grown by 1.3% and 2.1% per year over the last nine and five years on average. The book value trend is much more consistent. We are projecting a book value per share of \$44.09 by 2028 for a 0.5% average annual growth of book value over the next five years.

## Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/B	0.67	0.7	0.74	0.73	0.75	0.73	0.73	0.50	0.49	0.38	<b>0.23</b>	<b>0.45</b>
Avg. Yld.	2.0%	2.1%	2.1%	2.1%	2.2%	2.2%	2.3%	3.4%	3.3%	4.3%	<b>7.3%</b>	<b>4.3%</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 0.23, which is much lower than its 10-year average of 0.64. If the stock reverts closer to its average valuation level over the next five years, it will enjoy a 13.9% annualized gain.

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

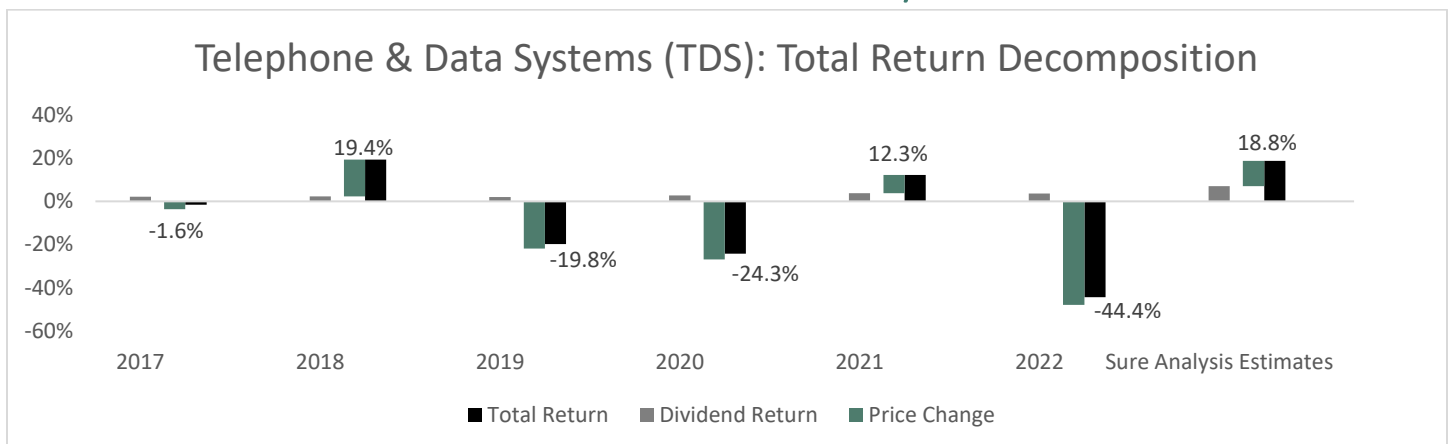
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	40%	---	28%	151%	44%	55%	64%	35%	70%	---	---	75%

TDS has raised its dividend for 49 consecutive years. It has grown its dividend by 3.7% per year on average over the past 5 years. Today, its 7.3% dividend yield is significantly higher than the yield of the S&P. However, the dividend is not backed by earnings, thus it is in danger of being cut. 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 were 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 an 18.8% average annual return over the next five years. We expect the bulk of returns to come from a mix of valuation expansion and yield. The corporation trades well below our estimate of fair value and has strong total return prospects, thus we rate TDS a buy, but only for investors who can stomach the volatility of its results and its shaky dividend.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
<b>Revenue</b>	4,901	5,009	5,210	5,155	5,044	5,109	5,176	5,225	5,329	5,413
<b>Gross Profit</b>	2,676	2,498	2,795	2,726	2,685	2,773	2,839	2,871	2,857	2,848
<b>Gross Margin</b>	54.6%	49.9%	53.6%	52.9%	53.2%	54.3%	54.8%	54.9%	53.6%	52.6%
<b>SG&amp;A Exp.</b>	1,948	1,865	1,781	1,762	1,689	1,694	1,717	1,681	1,677	1,768
<b>D&amp;A Exp.</b>	1,018	837	844	850	844	883	932	909	895	929
<b>Operating Profit</b>	-290	-204	170	114	152	196	190	281	285	151
<b>Operating Margin</b>	-5.9%	-4.1%	3.3%	2.2%	3.0%	3.8%	3.7%	5.4%	5.3%	2.8%
<b>Net Profit</b>	142	-136	219	43	153	135	121	226	156	62
<b>Net Margin</b>	2.9%	-2.7%	4.2%	0.8%	3.0%	2.6%	2.3%	4.3%	2.9%	1.1%
<b>Free Cash Flow</b>	-389	-404	-11	146	91	239	54	164	-48	-6
<b>Income Tax</b>	126	-5	172	40	-279	46	64	19	33	53

## Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
<b>Total Assets</b>	8,904	8,854	9,422	9,446	9,295	9,783	10,781	12,525	13,493	14,550
<b>Cash &amp; Equivalents</b>	830	472	985	900	619	921	465	1,429	367	360
<b>Accounts Receivable</b>	552	549	705	753	861	992	1,005	1,004	1,058	1,069
<b>Inventories</b>	245	274	158	151	145	150	169	154	178	268
<b>Goodwill &amp; Int. Ass.</b>	2,456	2,534	2,901	2,938	3,020	2,957	3,266	3,398	4,841	5,450
<b>Total Liabilities</b>	4,234	4,398	4,717	4,695	4,402	4,479	5,366	6,922	6,748	7,935
<b>Accounts Payable</b>	496	387	349	365	368	365	374	508	481	506
<b>Long-Term Debt</b>	1,722	1,942	2,454	2,445	2,457	2,439	2,326	3,429	2,934	3,750
<b>Shareholder's Equity</b>	4,118	3,926	4,126	4,144	4,269	4,560	4,653	4,804	4,853	4,775
<b>LTD/E Ratio</b>	0.42	0.49	0.59	0.59	0.58	0.53	0.50	0.71	0.50	0.64

## Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
<b>Return on Assets</b>	1.6%	-1.5%	2.4%	0.5%	1.6%	1.4%	1.2%	1.9%	1.2%	0.4%
<b>Return on Equity</b>	3.5%	-3.4%	5.4%	1.0%	3.6%	3.1%	2.6%	4.8%	3.2%	1.3%
<b>ROIC</b>	2.2%	-2.1%	3.2%	0.6%	2.1%	1.8%	1.6%	2.7%	1.7%	0.6%
<b>Shares Out.</b>	109.0	108.0	109.0	110.0	112.0	115.0	116.0	116.0	116.0	114
<b>Revenue/Share</b>	44.91	46.38	47.36	46.44	45.04	44.82	44.62	45.43	45.94	47.48
<b>FCF/Share</b>	-3.57	-3.74	-0.10	1.32	0.81	2.10	0.47	1.43	-0.41	-0.05

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

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