



Telephone & Data Systems (TDS)

Updated May 5th, 2023 by Quinn Mohammed

Key Metrics

Current Price:	\$8	5 Year CAGR Estimate:	19.4%	Market Cap:	\$1.1 B
Fair Value Price:	\$15	5 Year Growth Estimate:	0.5%	Ex-Dividend Date¹:	06/14/2023
% Fair Value:	53%	5 Year Valuation Multiple Estimate:	13.7%	Payment Date²:	06/30/2023
Dividend Yield:	9.3%	5 Year Price Target	\$15	Years of Dividend Growth:	49
Dividend Risk Score:	B	Retirement Suitability Score:	A	Rating:	Hold

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 \$1.1 billion and more than \$5.4 billion in annual revenues.

TDS declared a 2.8% dividend increase to \$0.185 quarterly on February 16th, 2023, marking its 49th annual increase.

On May 4th, 2023, TDS reported financial results for the first quarter of 2023. Investors were clearly unimpressed with the results as shares of TDS tumbled 17% on the day following the report. The company's total operating revenues were \$1.3 billion, down 1% compared to the same period one year ago, and \$30 million short of analyst estimates.

Net income was \$(9) million, down from last year's \$44 million. Diluted earnings per share of \$(0.08) also compared unfavorably to the \$0.37 earned one year ago, and missed analysts' estimate by ten cents.

Postpaid ARPU of \$50.66 was a 1.9% year-over-year increase. Total broadband connections increased 4% year-over-year to 515,400 connections and residential revenue per connection grew 4% to \$60.24. During the quarter, TDS repurchased nearly 291,000 of its common shares for \$3 million.

Management reaffirmed its prior 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
EPS	\$1.29	-\$1.26	\$1.98	\$0.39	\$1.37	\$1.17	\$1.03	\$1.93	\$1.00	(\$0.07)	(\$0.45)	\$0.80
BPS³	\$37.85	\$36.39	\$37.86	\$37.67	\$38.45	\$40.00	\$40.46	\$42.02	\$41.84	\$42.63	\$43.00	\$44.09
DPS	\$0.51	\$0.52	\$0.56	\$0.59	\$0.60	\$0.64	\$0.66	\$0.68	\$0.70	\$0.72	\$0.74	\$0.79
Shares⁴	109.0	108.0	109.0	110.0	112.0	115.0	116.0	116.0	116.0	112.0	113.0	125.0

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.

¹ Estimate

² Estimate

³ Book value per share

⁴ 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 per share 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	0.18	0.35
Avg. Yld.	2.0%	2.1%	2.1%	2.1%	2.2%	2.2%	2.3%	3.4%	3.3%	4.3%	9.3%	5.1%

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 0.18, which is much lower than its 10-year average of 0.64, reflecting severely depressed investor sentiment. If the stock reverts closer to its average valuation level over the next five years, it will enjoy a 13.7% annualized gain. However, when taking into consideration that TDS has \$5.4 billion of licenses, goodwill and other intangible assets on its balance sheet, the intangible book value of TDS is negative, which paints a grim picture of the company's current situation.

Safety, Quality, Competitive Advantage, & Recession Resiliency

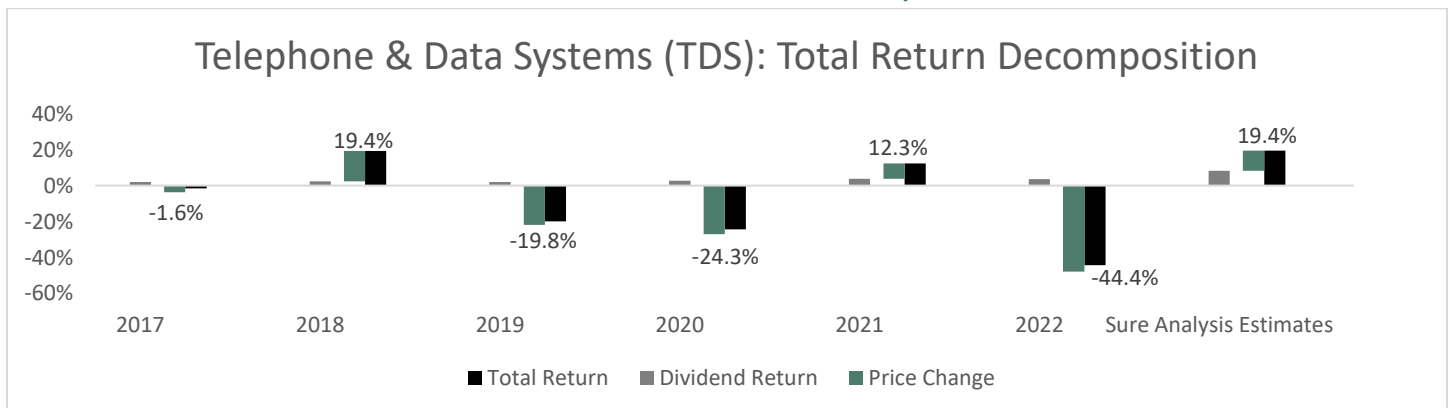
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	40%	---	28%	151%	44%	55%	64%	35%	70%	---	---	98%

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 9.3% dividend yield is significantly higher than the yield of the S&P. However, the dividend is not backed by earnings, thus it is in grave 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, which is not forecasting much growth. Shares of TDS could offer a 19.4% average annual return over the next five years, with the bulk of returns coming from a mix of valuation expansion and yield. Although the company has strong total return prospects, which would typically merit a buy rating, given the riskiness of the dividend and the volatility of its results, we assign TDS a hold rating.

Total Return Breakdown by Year



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Income Statement Metrics

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

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	8,904	8,854	9,422	9,446	9,295	9,783	10,781	12,525	13,493	14,550
Cash & Equivalents	830	472	985	900	619	921	465	1,429	367	360
Accounts Receivable	552	549	705	753	861	992	1,005	1,004	1,058	1,069
Inventories	245	274	158	151	145	150	169	154	178	268
Goodwill & Int. Ass.	2,456	2,534	2,901	2,938	3,020	2,957	3,266	3,398	4,841	5,450
Total Liabilities	4,234	4,398	4,717	4,695	4,402	4,479	5,366	6,922	6,748	7,935
Accounts Payable	496	387	349	365	368	365	374	508	481	506
Long-Term Debt	1,722	1,942	2,454	2,445	2,457	2,439	2,326	3,429	2,934	3,750
Shareholder's Equity	4,118	3,926	4,126	4,144	4,269	4,560	4,653	4,804	4,853	4,775
LTD/E Ratio	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
Return on Assets	1.6%	-1.5%	2.4%	0.5%	1.6%	1.4%	1.2%	1.9%	1.2%	0.4%
Return on Equity	3.5%	-3.4%	5.4%	1.0%	3.6%	3.1%	2.6%	4.8%	3.2%	1.3%
ROIC	2.2%	-2.1%	3.2%	0.6%	2.1%	1.8%	1.6%	2.7%	1.7%	0.6%
Shares Out.	109.0	108.0	109.0	110.0	112.0	115.0	116.0	116.0	116.0	114
Revenue/Share	44.91	46.38	47.36	46.44	45.04	44.82	44.62	45.43	45.94	47.48
FCF/Share	-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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