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INSIGHT FOR NEXT-GENERATION ILECs



DSL devotee

Speeds up to 10 Mb/s are fueling strong multiplay take rates for TDS Telecom CEO Dave Wittwer.

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M2Z proposal would enlist rural partners

DSL devotee

Maybe IPTV isn't for everyone — TDS Telecom is doing just fine with a triple play based on DSL and DISH Network service.

BY JOAN ENGBRETSON
Photographs by Bob Rashid

PERHAPS THE BEST WAY to describe Dave Wittwer, CEO of TDS Telecom, is to call him a DSL devotee.

As leader of one of the larger Tier 2 carriers, which serves 1.2 million customers in 30 states, he has moved to make DSL available to 87% of the people in the company's ILEC service territory. Despite a tough telecom market, DSL subscribers increased 29% between mid-2007 and mid-2008. And an impressive 84% of DSL customers take speeds above 1.5 Mb/s, including 46% who take speeds in the 3 to 6 Mb/s range.

The high percentage of customers taking higher rate service also may have contributed to the company's 8% year-over-year increase in average DSL revenue per user, which is now around \$34. TDS also is launching 10 Mb/s DSL service in some key markets and offers DSL in some additional markets where it operates as a CLEC.

TDS' DSL performance hasn't peaked yet, Wittwer said. "The way people use DSL is different today than yesterday, which was different from the day before," he

said. "A higher percentage of customers will find that broadband is more important in their lifestyle. There's a lot of room to continue to grow our penetration as well as the demand to go faster."

BUNDLES

Wittwer, who has worked for the company for more than two decades, took over at the helm in 2006. He replaced longtime CEO James Barr at a point when the company began to face a critical challenge shared by all incumbent telcos: a decline in its core phone business. Increasingly, customers were opting for alternative forms of phone service using wireless, cable or voice over IP (VoIP).

Like many telcos, TDS has turned to bundling in an effort to sell a wider range of services to its remaining base. Through a partnership with DISH Network, the company is able to deliver a triple-play offering of voice, video and data — or double-play offerings involving two of those three services.

TDS is "very pleased" with the relationship it has



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had with the satellite video provider since the 1990s, Wittwer said. "We aggressively bundle with a premiere product," he said, pointing to the DISH Network's state-of-the-art digital video recorder and strong lineup of high-definition channels. He added that TDS is "working closely with peer companies" in developing new services that may integrate more tightly with DISH service. Although he declined to provide details, it would be logical for such offerings to resemble AT&T's Homezone, which integrates tightly with DISH service to support advanced features such as media file sharing.

TDS also likes to experiment with promotions to drive multiplay take rates. Recent offers included a two-year price guarantee and a year of free DISH service. "We have to keep our promotions fresh," Wittwer said.

As many telcos have found, bundled customers are more loyal customers. When a customer purchases only voice service from TDS, the average churn rate is 1.5% per year. When the customer takes voice plus DSL, that rate drops to 1.3%. And for customers who purchase voice plus DISH, the rate improves further, to 0.9%. The most loyal customers are those who take the triple play, with a churn rate of just 0.4% per year.

The number of customers taking the triple play at TDS has grown. The company added 6600 triple-play subscribers in the second quarter of this year — a 13.5% increase over the previous year, which brought the company's total number of triple-play subscribers to 48,700.

By increasing loyalty, bundling

also may help to minimize access line loss. On the second-quarter earnings call in August, Bill Megan, executive vice president and chief financial officer for TDS, described the company's access line loss today as "steady," at 5% over the same period a year earlier.

One factor that may contribute to that performance is that TDS has a higher percentage of business customers than some other telcos, Wittwer said. "We're much closer to 50/50 business/residential than a traditional ILEC because of our CLEC unit," he added, noting that a typical ILEC gets about 80% of its business on the residential side.

"We like the fact that this creates more stability in our business versus some other telcos," Wittwer said, apparently alluding to the fact that business customers are less likely than residential users to cut their traditional landline

Not all business customers are content with basic phone service, though. Increasingly they are looking for the advanced features that can be enabled by VoIP. To address that demand, TDS recently launched managedIP, a hosted offering for businesses that provides a single converged voice and data communications service supporting capabilities such as advanced call routing to eliminate busy signals, one-number capability and user-friendly administration.

"We know VoIP is important from a feature function," Wittwer said. "We're starting with business, and we'll get to the consumer, offering VoIP that will be feature-rich. ManagedIP is a really nice product, and

we're having really good success with it. It's early, but the take rate has been good. Customers appreciate the features and functionality and that it offers them the opportunity to be productive."

MARKET REALITIES

Being more productive also has been an important focus within TDS. "We continue to manage and change our cost structure to offset revenue decline, thereby holding cash flow steady," Megan said. "We have improved cash flow by combining support functions and lowering our average head count by 5%."

The company also has streamlined its offerings, which may have helped it operate more efficiently — although Wittwer emphasized that the move was a benefit to the customer. "We're making it simple for customers with products that are easy to understand," he said.

One reason TDS may have less to fear from access line loss than some other telcos is that its parent company, Telephone and Data Systems, has a valuable asset many other Tier 2 and Tier 3 carriers lack: It owns 82% of regional wireless carrier U.S. Cellular, so some lines lost may simply be shifting from one business unit to the other.

The landline and wireless business units have substantially different coverage areas, however. And that has made it difficult for the two units to collaborate on a quadruple-play offering, which would include wireless, or on tightly integrated wireless and wireline services, which could further improve customer loyalty and provide new revenue sources.

"We have about 40% of our markets in U.S. Cellular territory, which is a smaller percentage from their perspective," Wittwer said. That means U.S. Cellular would have to use another vendor to supplement a converged fixed/mobile offering.

“That adds complexity from U.S. Cellular’s perspective,” he added.

From a marketing perspective, as well, the two units have found few synergies, said Kevin Roe, president and founder of Roe Equity Research. “Their brand name for wireless is U.S. Cellular, but you can’t use that to brand the DSL business,” he said.

Telephone and Data Systems would be wise to acquire the 18% of U.S. Cellular that it doesn’t already own, Roe said. That move wouldn’t necessarily increase the potential for synergies, but he said, “They would be taking full control of an asset that’s trading well below the strategic value of that asset.”

Eventually, Roe envisions Telephone and Data Systems being involved in a major consolidation. “The march of consolidation can’t be stopped,” he said, speculating that a company such as Verizon, interested primarily in U.S. Cellular, might buy Telephone and Data Systems outright then divest parts of it.

TDS has made some small acquisitions of its own in the last year, including West Point Telephone Co. in Indiana and Mosinee Telephone Co. in Wisconsin. But to date, it has avoided any move toward consolidation with a major carrier.

“We’re very careful buyers,” said Wittwer. “We look for a company that’s been well-run, and we look at the condition of the network and infrastructure that’s in place.”

MOVING FORWARD

Where its own infrastructure is concerned, TDS is deploying deep fiber and IPTV in a few key markets and uses fiber to the home (FTTH) for all new builds — and Wittwer said he anticipates overbuilding more markets in the future with fiber.

“There are a number of markets where we’re aggressively replacing copper with fiber if customer needs demand,” he said. “But if they’re happy with the speeds offered by DSL, we won’t replace that with fiber.”

The company also hasn’t ruled out doing IPTV over DSL. But Wittwer doesn’t believe the technology is ready yet. “Our belief is you need to have reliable VDSL2 to give people the kinds of speeds over copper to support the bandwidth customers need and the channels customers want,” he said.

TDS’ approach is less aggressive than that of telco giants AT&T and Verizon, both of which are widely deploying fiber to support IPTV. Ironically, the TDS approach also is less aggressive than that of some of the smallest telcos, which are able to

AN IDEA worth cloning

A number of independent telcos have found a new revenue opportunity in solving computer problems for customers. But for TDS Telecom, which serves many rural areas, the idea of dispatching a technician to a customer site didn’t make sense.

As an alternative, the company devised Remote PC Support, which lets TDS technicians remotely diagnose customers’ problems.

“We looked at how we handled this within our own company,” said Dave Wittwer, CEO of TDS. Based on that experience, TDS late last year launched its offering, which is based on the same software used by the company’s internal help desk personnel.

A company such as TDS, which has a strong track record within a community, may be an excellent candidate to offer this type of service. As Wittwer said, “I’m not sure we would be as effective if we didn’t have a reputation for customer service.”





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rely on the Universal Service Fund and Rural Utilities Service loans to support the construction of new triple-play infrastructures.

"The capital investment needed to aggressively roll out IPTV is probably a harder pill for publicly traded ILECs to swallow than for smaller telcos that aren't publicly traded and don't have to worry about share price," said Bernie Arnason, managing partner for Independent telco consultancy Pivot Media.

But that's not necessarily a bad thing, Arnason added. "Some still

think FiOS is the wrong move," he said, referring to Verizon's advanced — but costly to deploy — triple-play offering. "Wall Street is so short-term-focused, you see its opinion changes from quarter to quarter."

Roe defended TDS' strategy even more strongly. "A company like TDS never should be, nor will they be, as aggressive in deploying fiber or IPTV as the more-urban telcos," he said.

Another technology that could hold some promise for TDS is WiMAX. TDS already has deployed the technology to provide data

service in some CLEC markets and could use it more extensively if conditions are right, Wittwer said.

"There's not a lot of vendors in that space yet," he said. "It's important to be able to use it for voice and data, and we're still working that out."

Another issue, he said, is that "there aren't any meaningful vendors that have laptop cards to do nomadic WiMAX. Today most laptops aren't equipped for it." While not providing details, he added, however, that TDS plans to have an enhancement to its WiMAX offering by early 2009.

Barring a major technological breakthrough, TDS appears destined to be a DSL devotee for the foreseeable future, and the track record it has built around that product should continue to serve the company well in a challenging market. ●