Management's Discussion and Analysis of Results of Operations and Financial Condition

Telephone and Data Systems, Inc. ("TDS") is a diversified telecommunications company providing high-quality telecommunications services to approximately 5.5 million wireless telephone and wireline telephone equivalent access lines in 36 states at December 31, 2003. TDS conducts substantially all of its wireless telephone operations through its 82.1%-owned subsidiary, United States Cellular Corporation ("U.S. Cellular") and its incumbent local exchange carrier and competitive local exchange carrier wireline telephone operations through its wholly-owned subsidiary, TDS Telecommunications Corporation ("TDS Telecom").

The following discussion and analysis should be read in conjunction with TDS's audited consolidated financial statements and footnotes included herein and the description of TDS's business included in Item 1 of the TDS Annual Report on Form 10-K for the year ended December 31, 2003, as amended.

TDS has restated certain portions of its management's discussion and analysis of results of operations and financial condition included in its Annual Report on Form 10-K for the year ended December 31, 2003 that was originally filed on March 12, 2004. The restatement of TDS's 2003 and 2002 financial statements relates to the implementation of Statement of Financial Accounting Standards ("SFAS") No. 142 "Goodwill and Other Intangible Assets," which was adopted on January 1, 2002. Prior to January 1, 2002, TDS allocated the excess of purchase price over tangible assets and liabilities acquired to wireless license costs and goodwill. At that time, the accounting treatment for the TDS's wireless license costs and goodwill was the same for book purposes, with both asset classes amortized over an expected life of 40 years. However, no deferred taxes were provided on the amounts allocated to goodwill.

Based upon a subsequent review of goodwill, TDS has restated the allocation of $138.9 million of purchase price recorded as goodwill to wireless license costs as of January 1, 2002, the date of the adoption of SFAS No. 142. In connection with this restatement, an additional deferred tax liability of $90.7 million was recorded as of January 1, 2002. The additional deferred tax liability recorded in conjunction with this restatement increased the carrying value of wireless license costs by a corresponding $90.7 million. Following these adjustments, TDS reperformed the impairment tests for its wireless license costs as of January 1, 2002, and recorded an impairment loss of $10.4 million ($20.9 million before income taxes of $8.2 million and minority interest of $2.3 million). This impairment has been recorded as a cumulative effect of an accounting change at January 1, 2002, the date of the adoption of SFAS 142.

In the first quarter of 2003, TDS had recorded a loss on assets held for sale related to the pending disposition of certain wireless properties. The wireless license costs upon which the impairment was recorded in the first quarter of 2002 included the wireless license costs of these properties. As a result, a portion of the originally recognized loss on assets held for sale in the first quarter of 2003 was recognized in the first quarter of 2002. Consequently, loss on assets held for sale in 2003 has been reduced by $1.9 million, before income taxes of $0.8 million and minority interest of $0.2 million. In the third quarter of 2003, TDS had originally recorded an income tax expense upon the closing of the disposition of such wireless properties. This tax expense has been reduced due to the reversal of additional deferred tax liabilities that were recorded with respect to the wireless properties exchanged in conjunction with the restatement from goodwill to wireless license costs. Consequently, income tax expense in 2003 has been reduced by $10.7 million and minority interest by $1.9 million.

In addition, as a result of the restatement discussed above, TDS also reperformed the annual impairment test for its wireless license costs for 2003, which was originally performed during the second quarter of 2003. This resulted in the recognition of an additional impairment loss of $49.6 million, before income taxes of $19.6 million and minority interest of $5.4 million. This additional loss has been recorded in the second quarter of 2003. See the Restatement section of Note 1 – Summary of Significant Accounting Policies.

Amounts reported in this discussion and analysis for 2003 and 2002 reflect amounts as restated.

OVERVIEW

The following is a summary of certain selected information from the complete management discussion that follows the overview and does not contain all of the information that may be important. You should carefully read this entire management discussion and analysis and not rely solely on the overview.

U.S. Cellular – U.S. Cellular positions itself as a regional operator, focusing its efforts on providing wireless service to customers in the geographic areas where it has licenses to provide such service. U.S. Cellular differentiates itself from its competitors through a customer satisfaction strategy, reflecting broad product distribution, a customer service focus and a high-quality wireless network.

U.S. Cellular's business development strategy is to operate controlling interests in wireless licenses in areas adjacent to or in proximity to its other wireless licenses, thereby building contiguous operating market areas. U.S. Cellular's operating strategy is to strengthen the geographic areas where it can continue to build long-term operating synergies and to exit those areas where it does not have opportunities to build such synergies. Three of U.S. Cellular's most recent transactions are summarized below.

- On August 1, 2003, U.S. Cellular completed the transfer of properties to AT&T Wireless and the assignments to it by AT&T Wireless of a portion of the wireless licenses covered by the agreement with AT&T Wireless. On the initial closing date, U.S. Cellular also received approximately $34 million in cash and minority interests in six wireless markets in which it currently owns a controlling interest. Also on the initial closing date, U.S. Cellular transferred wireless assets and customers in 10 markets in Florida and Georgia to AT&T Wireless.

U.S. Cellular has deferred the assignment and development of 21 licenses it has the right to acquire from AT&T Wireless for up to five years from the original closing date of August 1, 2003. When this transaction is fully consummated, U.S. Cellular will have received 36 wireless licenses in 13 states, approximately $34 million in cash and minority interests in six licenses in which it previously owned the controlling interest. The licenses received are contiguous to and overlap existing U.S. Cellular licensed areas in the Midwest and Northeast.

- On November 26, 2003, U.S. Cellular announced that it had entered into a definitive agreement to sell its wireless properties in southern Texas to AT&T Wireless. The closing of the transaction occurred in February 2004. The U.S. Cellular assets sold to AT&T Wireless in this transaction included wireless properties in six markets and 76,000 customers.
- On August 7, 2002, U.S. Cellular completed the acquisition of a 20 megahertz license in the Chicago basic trading area (excluding Kenosha, Wisconsin). U.S. Cellular acquired 320,000 customers in this transaction. This acquisition was important to U.S. Cellular as it filled in U.S. Cellular's coverage area in the Midwest, enabling it to expand its network to cover a contiguous area including most of Illinois, Wisconsin and Iowa.

U.S. Cellular operating income decreased 58% in 2003 and decreased 11% in 2002 primarily due to expenses related to increased customer usage along with development of the Chicago market. U.S. Cellular's operating income was significantly affected by the loss on assets held for sale and the loss on impairment of intangible assets in 2003. The operating income margins (as a percent of service revenues) were 4.9% in 2003, 13.4% in 2002 and 17.4% in 2001. TDS expects continued pressure on U.S. Cellular operating income and margins in the next few years due to slower customer growth, customer acquisition and retention, competition, increased customer usage, launching service in new areas and continued enhancements to its wireless networks. In the exchange and divestiture transactions listed above, U.S. Cellular has divested operations that were generating revenues, cash flows from operations and operating income. In exchange, U.S. Cellular received or will receive licenses that will be in a development phase for several years and also received cash. U.S. Cellular anticipates that it may require debt or equity financing over the next few years for capital expenditures, for the development of these new markets and to further its growth in the Chicago market and its other recently launched markets.

See "Results of Operations – Wireless Telephone Operations."

TDS Telecom – TDS Telecom provides high-quality telecommunication services, including full-service local exchange service, long-distance telephone service, and Internet access, to rural and suburban communities. TDS Telecom's business plan is designed to leverage TDS Telecom's strength as an incumbent local exchange carrier into a full-service telecommunications company that includes competitive local exchange carrier operations. TDS Telecom is focused on achieving three central strategic objectives: growth, market leadership, and profitability. TDS Telecom's strategy includes gaining additional market share and deepening penetration of vertical services within established markets. The strategy places primary emphasis on small and medium-sized commercial customers and residential customers.

Both incumbent local exchange carriers and competitive local exchange carriers are faced with significant challenges, including the industry decline in long-distance minutes of use and use of second lines by customers, growing competition from wireless and other wireline providers, changes in regulation, new technologies such as Voice over Internet Protocol, and the downturn in the economy. These challenges could have a material adverse effect on the financial condition, results of operations and cash flows of TDS Telecom.

Despite these challenges, TDS Telecom was able to increase customers and revenues in 2003 primarily through the increase in penetration of existing markets by its competitive local exchange operations. While the incumbent local exchange carrier operations increased revenues by four percent in 2003, the competitive local exchange operations increased revenues by 21%. TDS Telecom continues to look for ways to control costs while increasing the penetration of its competitive local exchange markets.

See "Results of Operations – Wireline Telephone Operations."

Financing Initiatives – TDS and its subsidiaries had Cash and cash equivalents totaling $937.7 million, $1,296.6 million of revolving credit facilities and an additional $75.0 million of bank lines of credit as of December 31, 2003. TDS and its subsidiaries are also generating substantial internal funds from operations. Cash flow from continuing operating activities totaled $920.4 million in 2003, $793.6 million in 2002 and $545.8 million in 2001. In addition, TDS currently has access to public and private capital markets to help meet its long-term financing needs. TDS anticipates that it may require funding over the next few years for capital expenditures, for the development of new wireless markets at U.S. Cellular and to further its growth in the Chicago market. Management believes that cash on hand, expected future cash flows from operations and existing sources of external financing provide substantial financial flexibility and are sufficient to permit TDS and its subsidiaries to finance its contractual obligations and anticipated capital expenditures.

TDS is committed to maintaining a strong balance sheet and its investment grade rating. During 2003 and 2002, TDS entered into several financing transactions that have provided financial flexibility as it continues to grow its wireless and wireline businesses.

TDS reduced its debt by redeeming $300 million of its Trust Originated Preferred Securities in 2003. Medium-term notes of $70.5 million and $51.0 million were redeemed in 2003 and 2002, respectively. TDS also repurchased 1,961,000 of its Common Shares for $92.4 million, or an average price of $47.10 in 2003.

U.S. Cellular sold $444 million of 30-year 6.7% Senior Notes in 2003 and $130 million of 30-year 8.75% Senior Notes in 2002 under an existing shelf registration statement. In December 2003, U.S. Cellular increased the capacity of its revolving credit agreement entered into in 2002 from $325 million to $700 million. U.S. Cellular also terminated its $500 million revolving credit agreement it had in place since 1997.

In 2002, TDS and U.S. Cellular monetized their investments in marketable equity securities through forward contracts which mature in 2007 and 2008, receiving proceeds of $1.6 billion.

See "Financial Resources" and "Liquidity and Capital Resources."

RESULTS OF OPERATIONS

Operating Revenues increased 15% ($446.7 million) to $3,445.2 million during 2003 and increased 16% ($410.0 million) to $2,998.5 million during 2002 from $2,588.5 million in 2001 reflecting growth in wireless customers and equivalent access lines in both years. Despite the transfer of 141,000 wireless customers to AT&T Wireless in August, wireless customers and equivalent access lines increased by 390,400 in 2003. There were no acquisitions in 2003. In 2002, internal growth added 415,200 wireless customers and equivalent access lines, while acquisitions contributed 332,000 additional wireless customers and 27,000 additional equivalent access lines. U.S. Cellular revenues increased $385.2 million to $2,582.8 million in 2003 and increased $302.8 million to $2,197.6 million in 2002 from $1,894.8 million in 2001 on 7% and 19% increases in customers, respectively. The acquisition of the Chicago market and two small markets contributed customer growth of 10% in 2002 at U.S. Cellular. TDS Telecom revenues increased $61.5 million to $862.4 million in 2003 and increased $107.2 million to $800.9 million in 2002 from $693.7 million in 2001 as equivalent access lines increased by 8% and 15%, respectively. The increase in equivalent access lines is primarily related to the growth in the competitive local exchange operations. Acquisitions contributed equivalent access line growth of 3% in 2002 at TDS Telecom.

Operating Expenses rose 22% ($565.2 million) to $3,177.3 million in 2003 and rose 21% ($459.7 million) to $2,612.1 million in 2002 from $2,152.4 million in 2001. U.S. Cellular operating expenses increased $547.4 million to $2,463.8 million during 2003 and increased $338.8 million to $1,916.4 million during 2002 from $1,577.6 million in 2001 due primarily to the costs associated with providing service to an expanding customer base, additional depreciation expense and acquisitions. Also included in U.S. Cellular's operating expenses in 2003 is $45.9 million of losses on assets of operations held for sale and $49.6 million of losses on impairment of intangible assets. TDS Telecom operating expenses increased $17.8 million to $713.5 million during 2003 and increased $121.0 million to $695.7 million during 2002 from $574.7 million in 2001. The increase in 2003 was primarily caused by increased cost of services and products, offset somewhat by a decline in competitive local exchange carrier costs by not entering new markets. The increase in 2002 was a result of the expansion of the competitive local exchange business, acquisitions and growth in incumbent local exchange carrier products and services. Also included in TDS Telecom's operating expenses in 2003 was $5.0 million of losses recorded on impairment of assets. Of this amount, $4.6 million was recorded by the competitive local exchange carriers and $0.4 million was recorded by the incumbent local exchange carriers. Operating expenses for all operations in 2003 and 2002 do not include amortization of license costs and goodwill as a result of the adoption of Statement of Financial Accounting Standards ("SFAS") No. 142 effective January 1, 2002. Amortization expense of license costs and goodwill in 2001 totaled $36.5 million at U.S. Cellular, $6.6 million at the incumbent local exchange carriers and $0.2 million at the competitive local exchange carriers.

Operating Income decreased 31% ($118.5 million) to $267.9 million in 2003 and decreased 11% ($49.8 million) to $386.4 million in 2002 from $436.2 million in 2001. U.S. Cellular's operating income decreased 58% ($162.2 million) to $119.0 million in 2003 and decreased 11% ($36.0 million) to $281.2 million in 2002 from $317.2 million in 2001. The decline in U.S. Cellular operating income in 2003 and 2002 reflects the costs associated with the acquisition of the Chicago market and increased marketing and depreciation expenses. U.S. Cellular's operating income was significantly affected by the loss on assets held for sale and the loss on impairment of intangible assets in 2003. TDS Telecom's operating income increased 42% ($43.7 million) to $148.9 million in 2003 primarily from improved results from the competitive local exchange business. TDS Telecom's operating income decreased 12% ($13.8 million) to $105.2 million in 2002 from $119.0 million in 2001 primarily due to increased incumbent local exchange carrier and competitive local exchange carrier bad debts and increased operating losses from expanding the competitive local exchange carrier business.

Investment and Other Income (Expense) primarily includes dividend and interest income, investment income, gains and (losses) on marketable equity securities and other investments, loss on debt extinguishment and interest expense.

Dividend and interest income decreased by $37.4 million to $19.9 million in 2003 and increased by $43.1 million to $57.3 million in 2002 from $14.2 million in 2001 due primarily to a $45.3 million Deutsche Telekom common share dividend TDS received in 2002. Deutsche Telekom did not pay a dividend in 2003. The decrease in dividend income in 2003 was offset by an increase in interest income reflecting increased cash balances earning interest. Proceeds from the monetization of marketable equity securities in 2002 earned interest in short-term interest bearing accounts in 2003. See Financial Resources – Cash Flows from Continuing Financing Activities for a discussion of proceeds from the monetization activities.