DIVIDENDS PAID TO SHAREHOLDERS: HOW FAIRPOINT COMPARES TO MID-SIZED AND LARGER TELECOMMUNICATIONS FIRMS

Communications Workers of America and International Brotherhood of Electrical Workers

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FairPoint is a highly leveraged company that pays very high dividends. The following analysis compares FairPoint's dividend policy to mid-sized rural telecommunications firms and some of the impacts this policy will have if the proposed purchase of Verizon's Maine-New Hampshire-Vermont operations is approved.

Dividend Comparisons between FairPoint and Other Telecommunications Firms

It is useful to compare FairPoint's current dividend policy to other rural telecommunications firms. FairPoint can be compared to three other relatively small rural firms with approximately the same number of access lines as FairPoint: Consolidated Communications, Iowa Telecommunications and Alaska Communications. However, it is probably more instructive to compare FairPoint to the mid-major rural companies such as Windstream, Citizen, Embarq and CenturyTel since FairPoint's proposed acquisition of Verizon's Northern New England properties would vaunt it into 8th largest telecommunications firm in the country.

Financial analysts often use two ratios to calculate the dividends paid to shareholders as a portion of corporate earnings and market value. One ratio is called the "payout ratio" the other is called the "dividend yield." Both are examined in the following chart.

Dividend Comparisons Between FairPoint and Selected Other Telecommunications Companies

	Dividend	Yield	Payout Ratio
FairPoint	$ 1.59	9.0%	222%
Consolidated Com	$ 1.55	6.9%	300%
Iowa Telecom	$ 1.62	6.9%	161%
Windstream	$ 1.00	6.7%	141%
Citizens	$ 1.00	6.6%	119%
Alaska Com	$ 0.86	5.4%	107%
Embarq	$ 2.50	4.0%	31%
Verizon	$ 1.62	3.9%	77%
AT&T	$ 1.42	3.7%	69%
CenturyTel	$ 0.26	0.5%	8%

Source: finance.yahoo.com visited on June 28, 2007 using data supplied by Hernscott Americas.

The "dividend yield" is used to evaluate how much a company pays out to its shareholders in dividends. The dividend yield equals the share price divided by total dividends paid out. FairPoint's dividend yield of 9.0% is much higher than the mid-sized rural telecommunications firms: 1,700% greater than CenturyTel, 125% greater than Embarq, 36% greater than Citizens, and 34% greater than Windstream. FairPoint's dividend yield also is higher than the three other small firms: 67% greater than Alaska Communications, and 30% greater than Consolidated Communications and Iowa Telecom.

The "payout ratio" is determined by dividing net income by the total dividends paid out. FairPoint's "payout ratio" of 222% means that it paid out 122% more in dividends than it earned in net income. FairPoint had a much higher payout ratio than the mid-sized rural telecommunications companies: 214% greater than CenturyTel, 191% greater than Embarq, 103% greater than Citizens, and 81% greater than Windstream. FairPoint also had a much higher payout ratio than two of the smaller firms: 115% greater than Alaska Communications and 61% greater than Iowa Telecom. Consolidated Communications was the only company that had a payout ratio higher than FairPoint.

FairPoint's commitment to maintaining some of the highest dividend yields and payout ratios in the industry may appear to be shareholder friendly. However, Morgan Stanley has stated that on a standalone basis, the company "will not generate enough cash to cover its current dividend in 2008, with increasing deficits in the years that follow…we are concerned that FairPoint may be in a position where the Verizon NE lines has become a necessity for the stock rather than an option."[1]

Some Implications of FairPoint's Dividend Policy if the Acquisition is Approved

FairPoint will be burdened with an additional $85 million in dividend payouts following the acquisition since it has made a commitment to maintain its high $1.59 per share dividend. Deutsche Bank, FairPoint's own investment advisor, projected that **through 2015, FairPoint would obtain $290 million in cumulative profits while paying out $1.1 billion in dividends – a payout ratio of $4 in dividends for every $1 in projected profits**! This policy of high dividend payouts will further strain FairPoint's ability to fulfill all the promises it has made in connection with its proposed acquisition including hiring hundreds more workers, significantly expanding broadband build out, improving service quality, improving the condition of the telecommunications infrastructure, reducing operational expenses by 25-30% and maintaining retail and wholesale rates while simultaneously replacing 600 Verizon operational, support and administrative systems, integrating 1.5 million new customers, adding $1.7 billion in debt.

[1] Morgan Stanley, *FairPoint Communications: Lowering 2008 Estimates on New Company Forecasts*, June 5, 2007.