

2015
SHAREHOLDER
UPDATE

Q1



TO OUR SHAREHOLDERS:

The following is our report on the first quarter of 2015, highlighted by growth in consolidated net operating revenues driven by a 4.6% increase in strategic revenues. Residential broadband revenues were up 2.4%, driven by growth in Fiber Internet and Fiber TV products. Wireline business services revenues were up 4.7% with gains in Fiber Internet, cloud voice, and IP voice systems. Data center revenues were up 8.2% as businesses' appetites for outsourcing data management and IT services continue to gain momentum. Strategic revenues comprised nearly 70% of net operating revenues for the quarter.

Consolidated net operating revenues for the first quarter of 2015 were \$22.6 million, up 1% from the prior year. Operating expenses were up 7% due to absorbing allocated costs related to our wireless operations, which were covered by transition services payments in the first quarter of 2014, and increased costs associated with growth in our fiber products and data center expansion. Operating income for the quarter was \$1.9 million compared to \$3.1 million. Nonoperating income was \$2.0 million in the first quarter of 2015, up from \$1.7 million in 2014, reflecting a 13.4% increase in the equity of our Verizon wireless partnership. EBITDA was \$8.6 million compared to \$9.8 million. Net income was \$2.4 million for the quarter. Earnings per share were \$1.09 compared to \$1.27 for the year earlier period.

Cash flows from operating activities were \$6.6 million in the first quarter of the year compared to \$8.4 million in the first quarter of the previous year, the result of lower net income for the quarter and working capital changes. Capital expenditures were \$8.0 million during the quarter, up from \$4.1 million, due to higher investments in fiber build-outs in 2015, increased success based costs associated with adding new fiber customers, and capital investment in our new Charlotte, NC-region data center. Cash distributions from our wireless partnership were \$1.4 million, down from \$2.1 million as the partnership increased capital spending during the quarter. Free cash flow was \$0.1 million in the first quarter of 2015 compared to \$6.0 million in the first quarter of 2014, reflecting increased capital spending during the quarter. Dividends paid were \$3.0 million during the quarter, the same levels as the first quarter of 2014.

We continue to invest heavily in the Internet ecosystem. While we are investing in fiber to homes and businesses as well as cloud-based data centers, at the same time we are investing in platforms, systems and people, setting the stage for new products and long-term opportunities. Thank you for your interest in North State.



J. Patrick Harman
Chairman



Royster Tucker III
President & CEO



Jonathan M. Cage
Vice President & CFO

Summary of Statements of Net Income—Unaudited

Amounts in millions except per share amounts

Three Months Ended March 31,	2015	2014	Change	% Change
Net operating revenues (after uncollectibles):				
Residential broadband	\$5.7	\$5.6	\$0.1	2.4%
Business wireline	6.2	5.9	0.3	4.7%
Data center	3.4	3.1	0.3	8.2%
Total strategic	15.3	14.6	0.7	4.6%
Residential legacy telecom	3.3	3.5	(0.2)	-5.0%
Wholesale	3.2	3.5	(0.3)	-7.1%
Advertising and search	0.8	0.8	0.0	-3.6%
Net operating revenue	22.6	22.4	0.2	1.0%
Operating expense:				
Cost of sales and services	9.3	9.0	0.3	3.1%
Selling, general, and administrative	6.9	5.5	1.4	24.5%
Depreciation and amortization	4.5	4.8	(0.3)	-6.1%
Total operating expense	20.7	19.3	1.4	7.0%
Operating income	1.9	3.1	(1.2)	-36.7%
Nonoperating income (expense):				
Interest income	0.0	0.0	0.0	-9.2%
Interest expense	(0.2)	(0.2)	0.0	12.8%
Equity in earnings of unconsolidated entities	2.2	1.9	0.3	13.4%
Net gain (loss) on sale of investment securities	0.0	0.0	0.0	981.3%
Other income (expense), net	0.0	0.0	0.0	-54.6%
Total nonoperating income	2.0	1.7	0.3	17.1%
Income before income taxes	3.9	4.8	(0.9)	-17.3%
Income taxes	1.5	1.9	(0.4)	-21.0%
Net income	2.4	2.9	(0.5)	-15.0%
Earnings per average common share (EPS)	\$1.09	\$1.27	(\$0.18)	-14.2%

Consolidated Balance Sheets—Unaudited

At March 31,	2015	2014
Assets		
Current assets:		
Cash and cash equivalents	\$ 10,047,052	\$ 8,890,372
Investment securities	1,608,610	13,962,275
Accounts receivable, net of allowance for doubtful accounts	7,270,479	8,143,264
Escrow receivable from wireless sale	-	2,350,156
Materials and supplies	2,199,498	1,756,868
Prepayments	2,011,066	1,267,931
Income taxes recoverable	-	583,382
Deferred income taxes	696,586	694,114
Total current assets	<u>23,833,291</u>	<u>37,648,362</u>
Property, plant, and equipment	481,602,334	467,131,966
Less accumulated depreciation	<u>335,660,117</u>	<u>322,867,112</u>
Property, plant, and equipment, net	<u>145,942,217</u>	<u>144,264,854</u>
Other assets:		
Investment securities	4,731,125	4,626,325
Investments in unconsolidated entities	9,108,044	8,686,653
Intangibles, net of amortization	15,783,483	17,079,950
Goodwill	27,232,656	27,232,656
Other noncurrent assets	<u>1,167,914</u>	<u>1,259,276</u>
Total other assets	<u>58,023,222</u>	<u>58,884,860</u>
Total assets	<u>\$ 227,798,730</u>	<u>\$ 240,798,076</u>
Liabilities and Stockholders' Equity		
Current liabilities:		
Current maturities of bank note	\$ 5,500,000	\$ 5,500,000
Accounts payable and payroll withholdings	3,815,469	2,944,184
Advance billings and customer deposits	3,211,047	3,391,146
Income taxes payable	931,962	1,486,798
Accrued expenses	6,666,443	9,030,066
Accrued taxes	<u>706,813</u>	<u>606,870</u>
Total current liabilities	<u>20,831,734</u>	<u>22,959,064</u>
Other liabilities:		
Bank note, net of current maturities	39,875,000	45,375,000
Deferred income taxes	26,256,800	31,691,835
Accrued pension benefits	31,967,159	17,201,981
Accrued postretirement benefits	808,406	973,446
Other liabilities and deferred credits	<u>655,168</u>	<u>711,209</u>
Total other liabilities	<u>99,562,533</u>	<u>95,953,471</u>
Total liabilities	<u>120,394,267</u>	<u>118,912,535</u>
Stockholders' equity:		
Preferred stock	1,914,900	1,946,300
Common stock	11,393,380	11,419,800
Paid in capital	54,062	47,324
Retained earnings	119,227,104	121,941,136
Accumulated other comprehensive loss	<u>(25,184,983)</u>	<u>(13,469,019)</u>
Total stockholders' equity	<u>107,404,463</u>	<u>121,885,541</u>
Total liabilities and stockholders' equity	<u>\$ 227,798,730</u>	<u>\$ 240,798,076</u>

Consolidated Statements of Net Income—Unaudited

Three Months Ended March 31,	2015	2014
Operating revenues:		
Residential broadband	\$ 5,986,437	\$ 5,950,171
Business wireline	6,293,835	5,999,344
Data center	3,419,990	3,162,028
Total strategic	15,700,262	15,111,543
Residential legacy telecom	3,230,174	3,594,843
Wholesale	3,219,271	3,463,898
Advertising and search	740,415	761,315
Total operating revenues	22,890,122	22,931,599
Less uncollectible revenue	287,147	557,437
Net operating revenues	22,602,975	22,374,162
Cost of sales and service:		
General support	1,549,493	1,327,424
Central office	2,140,394	2,158,591
Communication termination	2,816,419	2,502,013
Cable and wire facilities	877,812	1,251,928
Network operations	1,927,430	1,791,368
Total cost of sales and service	9,311,548	9,031,324
Gross margin	13,291,427	13,342,838
Depreciation and amortization expense	4,465,436	4,755,816
Selling, general, and administrative expense:		
Customer operations	4,555,732	3,651,682
Corporate operations	2,002,665	1,559,290
Taxes, other than income taxes	343,818	334,927
Total selling, general, and administrative expense	6,902,215	5,545,899
Net operating income	1,923,776	3,041,123
Nonoperating income (expense):		
Interest income	28,604	31,514
Interest expense, net of capitalized interest	(222,935)	(255,751)
Equity in earnings of unconsolidated entities	2,192,945	1,933,400
Net gain (loss) on sale of investment securities	9,545	(1,083)
Other income (expense), net	5,517	12,149
Net nonoperating income	2,013,676	1,720,229
Income before income taxes	3,937,452	4,761,352
Income taxes	1,463,448	1,852,207
Net income	2,474,004	2,909,145
Preferred stock dividends	-	-
Net income available to common stockholders	\$ 2,474,004	\$ 2,909,145
Earnings per average common share		
	\$1.09	\$1.27
Dividends per common share		
	\$1.30	\$1.30
Weighted average common shares outstanding		
	2,278,839	2,283,960

Consolidated Statements of Comprehensive Income—Unaudited

Three Months Ended March 31,	2015	2014
Net income	\$ 2,474,004	\$ 2,909,145
Other comprehensive income, net of tax:		
Unrealized holding gains arising during the period, net of tax expense in 2015 of \$15,206 and tax expense in 2014 of \$16,175	24,372	24,932
Other comprehensive income, net of tax	24,372	24,932
Comprehensive income	\$ 2,498,376	\$ 2,934,077

Consolidated Statements of Stockholders' Equity—Unaudited

Three Months Ended March 31,	Preferred Stock	Common Stock	Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Income			Total Stockholders' Equity
					Retirement Plans	Marketable Securities	Total	
Balance, January 1, 2014	\$ 1,946,300	\$ 11,423,490	\$ 47,324	\$ 122,047,933	\$ (13,791,294)	\$ 297,343	\$ (13,493,951)	\$ 121,971,096
Acquisition of stock		(3,690)						(3,690)
Net income				2,909,145				2,909,145
Common stock dividends				(2,969,148)				(2,969,148)
Acquisition of common stock in excess of stated value				(46,794)				(46,794)
Unrealized gain on marketable securities, net of tax expense						24,932	24,932	24,932
Balance, March 31, 2014	\$ 1,946,300	\$ 11,419,800	\$ 47,324	\$ 121,941,136	\$ (13,791,294)	\$ 322,275	\$ (13,469,019)	\$ 121,885,541
Balance, January 1, 2015	\$ 1,915,200	\$ 11,395,825	\$ 53,936	\$ 119,745,974	\$ (25,616,655)	\$ 407,300	\$ (25,209,355)	\$ 107,901,580
Acquisition of stock	(300)	(2,445)	126					(2,619)
Net income				2,474,004				2,474,004
Common stock dividends				(2,962,376)				(2,962,376)
Acquisition of common stock in excess of stated value				(30,498)				(30,498)
Unrealized gain on marketable securities, net of tax expense						24,372	24,372	24,372
Balance, March 31, 2015	\$ 1,914,900	\$ 11,393,380	\$ 54,062	\$ 119,227,104	\$ (25,616,655)	\$ 431,672	\$ (25,184,983)	\$ 107,404,463

Consolidated Statements of Cash Flows—Unaudited

Three Months Ended March 31,	2015	2014
Cash flows from operating activities:		
Net income	\$ 2,474,004	\$ 2,909,145
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	4,465,436	4,755,816
Loss (gain) on sale of investment securities	(9,545)	1,083
Loss on sale, disposal, and abandonment of other assets	64,827	115,021
Equity in earnings of unconsolidated entities	(2,192,945)	(1,933,400)
Deferred income taxes	(463,647)	47,875
Deferred pension and postretirement benefits	357,502	(117,246)
Changes in operating assets and liabilities:		
Accounts receivable	462,576	915,032
Materials and supplies	(533,982)	19,674
Other assets	4,359,602	1,286,575
Accounts payable and payroll withholdings	(2,888,252)	(1,069,374)
Accrued expenses	1,105,717	1,787,115
Other liabilities	(542,431)	(261,914)
Net cash provided by operating activities	<u>6,658,862</u>	<u>8,455,402</u>
Cash flow from investing activities:		
Additions to property, plant, and equipment	(8,006,276)	(4,150,888)
Cost of removal of telephone plant, net of salvage	(8,953)	(103,360)
Proceeds from sale of wireless assets-escrow, net	2,350,000	-
Proceeds from sale of investment securities	2,080,000	4,100,000
Purchases of investment securities	-	(4,676,574)
Distributions from equity investments	23,834	-
Distributions from unconsolidated entities	1,452,625	2,091,780
Net cash provided by (used in) investing activities	<u>(2,108,770)</u>	<u>(2,739,042)</u>
Cash flows from financing activities:		
Principal payments on term loan	(1,375,000)	(1,375,000)
Loan origination fees	(1,606)	-
Acquisition of preferred stock	(174)	-
Acquisition of common stock	(32,943)	(50,484)
Cash dividends paid	(2,962,376)	(2,969,148)
Net cash used in financing activities	<u>(4,372,099)</u>	<u>(4,394,632)</u>
Net change in cash and cash equivalents	177,993	1,321,728
Cash and cash equivalents at beginning of period	9,869,059	7,568,644
Cash and cash equivalents at end of period	<u>\$ 10,047,052</u>	<u>\$ 8,890,372</u>
Short term investment securities at end of period	<u>\$ 1,608,610</u>	<u>\$ 13,962,275</u>
Total cash, cash equivalents, and short term investment securities	<u>\$ 11,655,662</u>	<u>\$ 22,852,647</u>
Supplemental cash flow information:		
Cash paid for (refunds of) income taxes	<u>\$ (2,000,000)</u>	<u>\$ (150,532)</u>
Cash paid for interest	<u>\$ 227,980</u>	<u>\$ 249,171</u>

I, Jonathan M. Cage, hereby certify that the accompanying unaudited consolidated balance sheets of North State Telecommunications Corporation and Subsidiaries as of March 31, 2015 and 2014 and the related unaudited consolidated statements of net income, comprehensive income, stockholders' equity, and cash flows for the three months then ended have been prepared from the Corporation's and Subsidiaries' accounting records. Internal accounting controls and review procedures provide assurance that these statements are materially accurate.

This is the 4th day of May 2015.



Jonathan M. Cage
VP-Chief Financial Officer

BOARD OF DIRECTORS

J. Patrick Harman—Chairman
Royster Tucker III—Vice Chairman
C. Hayden McKenzie
Jonathan M. Cage
William H. Dula

David L. Harman
Coulson S. Mucher
Sarah M. Olson
Lizbeth W. Privette

OFFICERS

J. Patrick Harman
Chairman

Lynn Welborn
Vice President
Chief Administrative Officer

Royster Tucker III
President
Chief Executive Officer

Mark Dula
Vice President
Chief Operating Officer

Jonathan Cage
Vice President
Chief Financial Officer

Richard Worden
Vice President
Chief Business Officer

CORPORATE OFFICES

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