

August 3, 2011

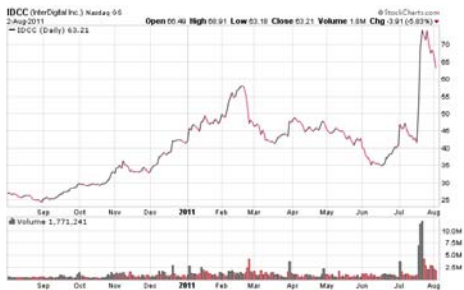
**INTERDIGITAL INC. (IDCC-Q)**

**Rating: Buy**  
**12-Month Target: \$118.00**

**SAMSUNG ENTERS THE PROCESS**

MARKET INFO: IDCC-Q			
Closing Price	\$63.21		
Quarterly Dividend	\$0.10		
Annualized Yield	0.63%		
Target Price	\$118.00		
Potential ROI	86.7%		
52 Week Range (\$)	\$22.81 / \$82.50		
Market Cap (\$mm)	\$2,872.52		
Cash (mm)	\$701.11		
Debt (mm)	\$192.60		
Enterprise Value (mm)	\$2,364.00		
Shares o/s (mm)	45.4		
Avg Volume (previous 3 months)	1,440,890		
FYE: Dec 31	FY2010A	FY2011E	FY2012E
Revenue (mm)	394.55	396.86	483.56
EBITDA (mm)	263.80	258.88	344.00
EBITDA margin (%)	66.9%	65.2%	71.1%
EPS	\$3.48	\$3.14	\$4.26
FD EPS	\$3.43	\$3.11	\$4.22
VALUATION	FY2010A	FY2011E	FY2012E
EV/Sales	6.0X	6.0X	4.9X
EV/EBITDA	9.0X	9.1X	6.9X
P/E	18.4X	18.4X	15.0X

Source: Capital IQ, M Partners



**EVENTS UNFOLDING AS EXPECTED – MORE TO COME**

- Last night, a news report issued by Bloomberg speculates that, based on “people familiar with the story”, Samsung is currently evaluating InterDigital’s portfolio with possible intent to participate in the process.
- We believe Samsung’s interest in IDCC’s patents to be highly probable for the following reasons:
  - It’s \$100M per annum 3G royalty agreement with IDCC is up for renewal in 2012, and will likely be extended to include 4G/LTE. In the hands of AAPL or GOOG, the patent renewals are likely to be more damaging to Samsung’s margins than if renewed by InterDigital.
  - Samsung is already in a significant intellectual property battle with Apple and may not be well armed at this point to defend its margins against Apple. The InterDigital patents are likely to be perceived as solid armament.
  - Apple is also an InterDigital licensee, with its 3G royalty agreement up for renewal in 2014. Apple currently benefits from a very favourable royalty agreement with InterDigital. In the hands of, for example Samsung, 3G renewals and 4G/LTE extensions could turn out to be more punitive for Apple.
- Events are unfolding exactly as we anticipated two weeks ago. With more bidders likely to come, demand tension should increase for the combined essential patent portfolio managed by InterDigital, along with 180 engineers that continue to solve wireless capacity issues with new inventions almost daily.
- As a reminder, based on about 1 billion mobile devices sold each year, and an average retail price of about \$400.00, each 1% of margin is worth about \$3.5B per year. Manufacturers allocate between 5% and 15% of gross margin on a device to pay IP royalties. Those with the most patents usually pay the least in IP royalties due to cross-licensing.

**PATENT GEEKS KEEP FORGETTING ABOUT THE REAL GEEKS**

- As indicated in our July 22<sup>nd</sup> note, from a buyer’s perspective the 8,800 issued patents and 9,700 pending patents would be worth between \$118.00 and \$167.00 per share based on 1% of margin related to IP being worth between \$3.0B and \$4.0B per annum to device manufacturers. At our \$118.00 per share target price, the patents are estimated to be worth \$0.28M each. Bidders paid \$0.75M each for Nortel’s patents.
- What seems to be missing from the equation is the value of the engineers themselves, which file new patents at a pace of about 1,000 per year or approximately 5 patents per engineer per year. At \$0.28M per patent, the annual output per engineer is \$1.4M, aggregating to \$250.0M per annum in new patent output for the team. Assuming that an acquirer is able to keep the team together for three years before 100% turnover, the NPV of the engineering team is approximately \$12.00 per share at a 18% discount rate. We do not include this in our \$118.00 share price target.
- As a result, we reiterate our BUY recommendation with a \$118.00 target price based on the takeout value of the stock.** Our target price is the low-end of a range between \$118.00 and \$167.00, so we urge investors to buy the stock at these levels. The stock is trading in a range near our original fundamental target. At close yesterday, the stock was trading at a 9.1x EV/EBITDA multiple, which is a 25% discount to its peer set, which traded at 12.1x. The stock should not be trading at fundamental levels because the stock should be valued based on takeout.

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### Rating System

Buy: price expected to rise  
Sell: price is inflated and expected to decrease  
Hold: properly priced  
Speculative Buy: price expected to rise; material risk to the investment exists  
Under review: not currently rated

Summary of Recommendations		
As of June 30, 2011		
Buy	40	95%
Sell	1	2%
Hold	1	2%
Total	42	100%

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