

September 27, 2011

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

Rating: Buy  
12-Month Target: \$118.00

**PROCESS CONTINUES: STOCK FUNDAMENTALLY UNDERVALUED**

MARKET INFO: IDCC-Q			
Closing Price	\$49.54		
Quarterly Dividend	\$0.10		
Annualized Yield (Based on Last Trade)	0.81%		
Target Price	\$118.00		
Potential ROI (Based on Last Trade)	238.2%		
52 Week Range (\$)	\$22.81 / \$82.50		
Market Cap (\$mm) (Based on Last Trade)	\$2,251.30		
Cash (mm)	\$701.11		
Debt (mm)	\$188.88		
Enterprise Value (mm) (Based on Last Trade)	\$1,739.06		
Shares o/s (mm)	45.4		
FD Shares o/s (mm)	51.3		
Avg Volume (previous 3 months)	2,577,970		
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	4.4X	4.4X	3.6X
EV/EBITDA	6.6X	6.7X	5.1X
P/E	14.4X	14.4X	11.8X

Source: Capital IQ, M Partners



**PROCESS CONTINUES**

- Last night Interdigital announced that the process it began July 19<sup>th</sup> continues. We reiterated this in an inter-day note yesterday.
- The company continues to explore multiple strategic options, which include the sale of the entire company or select assets, to a single buyer or a consortium. We believe that a transaction will occur soon and that last night's press release is a direct response to unfounded rumours that caused the stock to decline by over 20% Monday afternoon.

**SUM-OF-THE-PARTS VALUATION RANGES ABOVE OUR TARGET**

- Preponderance of evidence from various third-party experts assert that IDCC ranks among the top two or three 4G/LTE patent portfolios globally.
- Although the actual values of the Nortel LTE patents acquired earlier this year remain undisclosed, third-party assessments range from a low of \$1.4B to a high of \$2.0B. The Nortel patent portfolio is ranked among the top 6 or 7 LTE patent portfolios.
- We estimate the IDCC LTE patents to be worth \$3.6B or approximately \$70.00 per diluted share. At \$1.4B, third-parties have articulated the potential LTE patent portfolio to be worth \$3.3B.
- Using a DCF analysis based on IDCC's potential value to a strategic acquirer, the high value range for IDCC's business calculates to \$167 per share.

**WITH 4G/LTE PATENTS WORTH BETWEEN \$3.3B AND \$3.6B**

- We derive a value for IDCC's 3G patents of \$27.50 per fully-diluted share, based on our pre-takeout valuation for the 3G patents which included the discounted value of existing per-unit agreements, and the value of LG and Samsung renewals and other fixed licenses, less per-unit prepayments. Our 3G valuation does not include potential licenses with Nokia, ZTE, Huawei and others. We remind investors that InterDigital has recently initiated litigation against these companies.
- We derive a value of \$14.50 per fully-diluted share, based on net cash after the exercise/conversion of dilutive securities.
- Previously, we estimated IDCC's engineers to be worth about \$615.5M, or \$12.00 per fully-diluted share.
- Incorporating \$3.3B LTE portfolio value, our sum-of-the-parts valuation derives a fully-diluted per share value of approximately \$118.00. Our \$3.6B value assessment of LTE patents implies a value of \$124.00. Both of these sum-of-the-parts calculations are at or above our current \$118.00 target.

Sum of Parts	Value (In MM)	Per Share
Net cash*	\$701.1	\$13.67
Cash from exercise of warrants/options, less converted debt	\$44.8	\$0.87
Existing Per-Unit Agreements	\$738.7	\$14.40
LG and Samsung Renewals	\$773.9	\$15.09
Other Fixed Licensees	\$72.3	\$1.41
4G/LTE Asset	\$3,300.0	\$64.33
Engineers/Human Capital	\$615.5	\$12.00
Less: Per Unit Pre-Payments	-\$179.9	-\$3.51
<b>TOTAL</b>	<b>\$6,066.4</b>	<b>\$118.26</b>

Effect of Dilution (MMs)	Shares Issued	Net Cash Received
Existing Common Stock	45.4	\$0.0
Options	0.7	\$9.4
Restricted Stock Units	1.2	\$0.0
Convertible Debt*, Net of Hedging Program	4.0	\$265.4
<b>TOTAL</b>	<b>51.3</b>	<b>\$274.8</b>

\*Debt cancelled by conversion  
Source: M Partners, Company reports

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**SUM-OF-THE-PARTS BUY-OUT VALUATION IS IMPORTANT TO KEEP RUMOURS IN CONTEXT**

- Regardless of the strategic decisions that the company makes regarding assets, the total sum-of-the-parts should calculate within a reasonable range of our target. We believe that the fairway resides between \$110.00 and \$130.00 per share.
- There are likely to be more rumours regarding valuation until the process concludes. We suggest that investors maintain perspective on rumours and treat bear rumours as buying opportunities.

**DCF VALUATION – LICENSING & CROSS-LICENSING – INFERS THE HIGH-END RANGE**

- Based on a strategic acquirer licensing (or deriving value through cross-licensing) 85% of the market for all 3G and 4G/LTE devices, we derived an enterprise value of approximately \$7.7B and a fully-diluted market cap of \$8.5B. Our estimate used an 18% after-tax discount rate with a terminal decline in licensing revenue of 10% beginning 2017, and assumed a mean licensing rate of 0.7% for 3G and 1.1% for 4G/LTE. On a fully-diluted basis, we derived a value of roughly \$167 per share.

**THE STOCK TRADES LIKE THERE IS NO TRANSACTION – AND IT IS UNDERVALUED ON A FUNDAMENTAL BASIS**

- For the first 6 months of the year, IDCC's average trading price was \$45.25 and our 12-month price target was \$54.50. After the Nortel auction, we increased our price target to \$65.50, to reflect the increased value of the company's 4G/LTE portfolio.
- After closing at \$49.54 yesterday, the company is fundamentally undervalued. Last night's announcement by the company makes IDCC shares a screaming buy at these levels.

**OUR VALUATION IS BASED ON THE CONCLUSION OF A MEANINGFUL TRANSACTION**

- We do not know what strategic outcome will occur. However, the company maintains that it would not have entered into this process if it did not believe that the patent portfolios were worth more than the current fundamental value of the operating company.
- Our fundamental valuation does not include potential cash flow from Nokia, Huawei, and ZTE.

**We reiterate our BUY recommendation and \$118 price target.**

# M | PARTNERS

Toronto Dominion Centre  
Canadian Pacific Tower  
100 Wellington Street West  
Suite 2201, P.O. BOX 320  
Toronto, Ontario M5K 1K2  
Main line: 416-603-4343  
Fax: 416-603-8608

## Contact Information

### Research

Brendon Abrams	ba@mpartners.ca
Alan Breuer	ab@mpartners.ca
David Buma	db@mpartners.ca
Marc Johnson	mj@mpartners.ca
Michael Krestell	mk@mpartners.ca
Kelsey Lobsinger	kl@mpartners.ca
Ingrid Rico	irico@mpartners.ca
John Safrance	jsafrance@mpartners.ca
Ron Shuttleworth	rs@mpartners.ca
Tom Varesch	tv@mpartners.ca

### Trading

Jennifer Burke	jb@mpartners.ca
Steve Isenberg	si@mpartners.ca
Cameron Loree	cl@mpartners.ca
Kyle Maister	km@mpartners.ca
Jeff Maser	jmaser@mpartners.ca
Tommy Matthews	tm@mpartners.ca
Garett Prins	gp@mpartners.ca
Helen Spasopoulos	hs@mpartners.ca
Mark Vendramin	mv@mpartners.ca
Jeff Zicherman	jz@mpartners.ca

### Advisory

Christopher Dingle	cd@mpartners.ca
Richard Goodman	rg@mpartners.ca
Kelly Klatik	kk@mpartners.ca
Thomas Kofman	tk@mpartners.ca
Daniel Lee	dl@mpartners.ca
Jason Matheson	jm@mpartners.ca
Michael McIntosh	mm@mpartners.ca
Thupten Samchok	ts@mpartners.ca

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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%