BlackBerry Limited

First Quarter Fiscal Year 2025 Results Conference Call

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CORPORATE PARTICIPANTS

John Giamatteo - *Chief Executive Officer*

Steve Rai - *Chief Financial Officer*

Tim Foote - *Chief Financial Officer, Cyber Security Division and Head of Investor Relations*

PRESENTATION

Operator
Good afternoon, and welcome to the BlackBerry First Quarter Fiscal Year 2025 Results Conference Call. My name is Cole and I'll be your conference moderator for today's call. During the presentation, all participants will be in a listen-only mode. We'll be facilitating a brief question and answer session towards the end of the conference. Should you need assistance during the call, please signal a conference specialist by pressing the "*" key followed by "0." And as a reminder, this conference is being recorded for replay purposes.

I would now like to turn today's call over to Tim Foote, CFO, Cyber Security Division and Head of Investor Relations. Please go ahead.

Tim Foote
Thank you, Cole. Good afternoon, everyone, and welcome to BlackBerry's first quarter fiscal year 2025 earnings conference call. Joining me on today's call is BlackBerry's Chief Executive Officer, John Giamatteo, and Chief Financial Officer, Steve Rai.

After I read our cautionary note regarding forward-looking statements, John will provide a business update and Steve will review the financial results. We will then open the call for a brief Q&A session. This call is available to the general public via call-in numbers and via webcast in the investor information section at blackberry.com. A replay will also be available on the blackberry.com website. Some of the statements we'll be making today constitute forward-looking statements and are made pursuant to the Safe Harbor provisions applicable to US and Canadian Securities Laws. We'll indicate forward-looking statements by using words such as expect, will, should, model, intend, and believe and similar expressions.

Forward-looking statements are based on estimates and assumptions made by the company in light of its experience and its perception of historical trends, current conditions and expected future developments, as well as other factors that the company believes are relevant. Many factors could cause the company's actual results or performance to differ materially from those expressed or implied by the forward-looking statements. These factors include the risk factors that are discussed in the company's annual filings and MD&A. You should not place undue reliance on the company's forward-looking statements.

Any forward-looking statements are made only as of today and the company has no intention and undertakes no obligation to update or revise any of them, except as required by law. As is customary during the call, John and Steve will reference non-GAAP numbers in their summary of our quarterly results. For reconciliation between our GAAP and non-GAAP numbers, please see the earnings press release published earlier today, which is available on EDGAR, SEDAR+ and blackberry.com websites.

And with that, I'll turn the call over to John.

John Giamatteo
Terrific. Thanks, Tim. And thanks to everyone for joining us today. I'm pleased to report another solid quarter for BlackBerry. We believe our strategy is working. This past quarter, we made further progress with establishing our IoT and Cybersecurity businesses as standalone divisions, while at the same time driving additional cost efficiencies.

We delivered our third consecutive quarter of sequentially better free cash usage despite the impact of seasonality. We also moved further along the path to profitability by improving both adjusted EBITDA and non-GAAP earnings per share. On the top line, both our IoT and Cybersecurity divisions delivered better than expected revenue, and our Cybersecurity business achieved improvements in its key ARR and dollar-based new retention rate metrics.

So let me begin with the IoT division. Revenue for the quarter was $53 million, above the top end of the range we provided previously. Gross margin remains strong at 81%. As expected, due to the timing of OEM programs, development seat revenue returned to a more typical lower level than the record set in Q4. However, both royalties and professional services remain strong and at near record levels. In fact, royalties were stronger than expected and largely drove the IoT revenue outperformance.

Double-clicking a little further, automotive accounted for approximately 80% of the total revenue in the first quarter, above the more typical 75%, driven in particular by digital cockpit and ADAS. Our professional services team is operating at near record levels. To support our customers and their development programs, we continue to invest in scaling our services team. This not only helps drive near-term revenue, but also assists customers in starting production and unlocking our $815 million royalty backlog.

Within automotive, this quarter we won a number of new design wins for digital cockpit and ADAS. Among the largest was a top-five global automaker that is utilizing the QNX hypervisor and acoustics module as well as the QNX ADAS sensor framework in a global deployment. Another win was with a leading European OEM that will leverage a high performance Qualcomm Snapdragon chipset in the cockpit and a leading electrical vehicle OEM that will deploy QNX in their latest range of SUVs and pickups.

In ADAS, we secured a win with Geely, a top-five Chinese automaker that will leverage the QNX RTOS and a Black Sesame chipset to power an L2+ ADAS stack. The stack includes navigation on autopilot, automated lane control, adaptive cruise control, and other high performance features. Building on the initial design wins in Q4 for the latest next generation version of our RTOS SDP 8.0, this past quarter we secured further new business for this high performance, highly scalable operating system.

Digicare Biomedical, a US-based medical equipment OEM, selected QNX SDP 8.0 to power a multi-parameter patient monitoring system. In other non-automotive, general embedded market wins, QNX will be used for an orthopedic surgical robot that will be utilized in knee, hip, spine, and other complex surgical procedures.

In industrial automation, among other wins, was a next-generation robotic controller that will run on NXP silicon. Last quarter, we mentioned how customers are increasingly requesting that we provide more of the software plumbing, including integrating third-party software products directly into QNX. Interest for this continues to build, and we held a number of customer workshops this past quarter.

Turning to market conditions, leading analysts expect global light vehicle production in calendar year 2024 to be stable compared to 2023 at approximately 90 million units. QNX's growth is being driven by a greater penetration of this total number of units, as well as an increased content per vehicle as they become progressively smarter and more software defined. Despite a pullback in electric vehicle demand, global battery electric vehicle or BEV production is still expected to grow approximately 27% in 2024.

It's important to emphasize that the systems that QNX supports, the digital cockpit, ADAS, chassis, and others, are just as applicable to internal combustion engine vehicles as they are to EVs. QNX is well diversified and largely agnostic to the mix of powertrain. That said, in the near term, the challenges automakers are experiencing in delivering software development programs continue. These industry-level challenges remain a headwind for the QNX business this fiscal year.

However, despite this, we continue to expect revenue for the full-year to be in the range of $220 million to $235 million. For the second fiscal quarter, we expect revenue to be in the range of $50 million to $54 million. We expect solid revenue from royalties and professional services with potential for some sequential uplift in development seat license revenue.

So, switching now to the Cybersecurity division. This was a good quarter where we continue to see the benefits from the product and go-to-market changes that we've made. We further…we saw further modest, but encouraging improvement in two key metrics for this division. Annual recurring revenue or ARR increased for the second consecutive quarter to $285 million. The dollar-based net retention rate or DBNRR also increased for the third consecutive quarter to 87%. Revenue was $85 million and above our guidance range. This outperformance was largely driven by improved ARR and another strong quarter for our SecuSmart business.

Cybersecurity gross margin was 59% sequentially lower, again, due to the strength in SecuSmart. SecuSmart's market-leading NSA certified end-to-end encryption voice solution is really resonating in mission-critical environments, especially large governments. This quarter, BlackBerry secured two large renewal and expansions that delivered both in-quarter revenue, as well as ARR. Given the strong book of business, we expect Q2 to be another solid quarter for SecuSmart. This is likely to mean that cyber gross margins will remain lower this coming quarter.

For Cylance, over the last couple of quarters, we focused on the segments where our win rates are strongest and we're pleased with the traction we're getting. These segments include operational technology and small and medium-sized enterprises. Further, in managed services, we see a large opportunity in a highly fragmented market that has no clear leader.

To better address this market, this past quarter we rebranded our GUARD solution as Cylance MDR for clarity and launched an on-demand solution that allows customers to obtain support from our MDR SOC team for issues where they need some additional help. We see this as a bridge between software only and full 24/7 MDR coverage. We're encouraged by the pipeline that these MDR initiatives are generating, as well as the amount of new business already secured.

Another focus area has been to ensure customers are using the latest versions of our Cylance product. These are the most feature rich and included capabilities such as our new AI assistant. More than 80% of Cylance customer endpoints now use version 3.0 or newer, and customer satisfaction is high. This was demonstrated by Cylance recently winning Gartner's Customers Choice Award for endpoint protection platforms for the second year in a row. The impact of this and upselling customers to our MDR offering has helped drive a third consecutive quarter of sequential DBNRR improvement for Cylance.

Our UEM product delivered better than expected renewal rates. Its high security offering, especially in on-premise environments, continues to resonate with our core customers. In the quarter, we secured a number of significant renewals in government and financial services, including a top-five US Bank, top-five Canadian bank, CIBC, the US Transportation Security Administration, or TSA, among others.

Finally, turning to AtHoc, our critical events management platform, customer retention rates remain very strong, particularly among our federal government and emergency services. On the product front, this month we launched a new geo-fencing feature that enables more accurate tracking of key personnel in preparation for and during critical events. Feedback from leading emerging services agencies has been very positive. In addition to revenue, costs for Cybersecurity business came in better than planned, driven in part by initiatives to significantly streamline our public cloud costs.

So, moving on to the outlook for the cyber business, despite a challenging macro environment that continues to elongate sales cycles across the industry, we are reiterating our full year outlook. We continue to expect Cybersecurity revenue for the full fiscal year to be in the range of $350 million to $365 million. For the second fiscal quarter, we expect revenue to be in the range of $82 million to $86 million.

Let me comment briefly on our licensing business. Revenue came in a little better than we expected at $6 million. The gross margin was at 67%. We understand from Malikie, the party that purchased our non-core patent portfolio, that they're making good progress in ramping up their efforts. And while we aren't expecting any further revenue from that arrangement this fiscal year, it does present a significant potential upside for future years.

So, before I turn the call over to Steve, let me provide a quick update on the efforts to separate and streamline our two core businesses. Significant progress was made this past quarter in separating and tailoring internal processes to fit the two businesses. This includes further delegating decision-making authority to the divisional management teams. Work has begun on a number of IT systems projects that we expect to deliver both a more custom-fit product for each of the two businesses, as well as drive significant cost reductions.

On costs, non-GAAP OPEX this past quarter came in at $109 million, a sequential decrease of $4 million. The $109 million was $21 million better than the $130 million baseline we gave you during the last earnings call, or $84 million better on an annualized basis. This demonstrates the significant impact of the actions that we've taken. All of this comes against the backdrop of improving fundamentals as illustrated by improvements in Cybersecurity ARR and DBNRR.

However, we haven't stopped there. This past quarter, we took further actions that will, in the fullness of time, drive incremental annual cost savings of approximately $20 million, the actions taken included reductions in back-office headcount and facilities. The $20 million of additional cost reduction builds on the $50 million from Q3 of last year and $55 million from Q4, meeting a total of approximately $125 million to-date. This is a significant achievement by the BlackBerry team and I'm proud of how far we've come in such a short period of time. Given the progress that we've made and continue to make, we are reiterating our expectation of generating positive cash flow and adjusted EBITDA in our fourth quarter fiscal...our fourth fiscal quarter.

So let me now turn the call over to Steve, who will discuss with you our financials in more detail. Steve…

Steve Rai
Thank you, John, and Good afternoon, everyone. As a reminder, unless otherwise noted, all numbers provided during my remarks, except for revenue, will be non-GAAP. Total company revenue was $144 million, which exceeded the upper end of our previously provided outlook range.

As John mentioned, revenue was comprised of $53 million for IoT, $85 million for Cybersecurity, and $6 million for licensing and other. Software product was approximately 85% of revenue, and professional services was the balance, at approximately 15%. Of the software product component, approximately 80% was recurrent. We're pleased that such a meaningful portion of our business is repeatable and reliable.

Total company gross margin was 67%. As John mentioned, we continue to make great progress on cost reductions. Operating expenses came in $4 million lower, sequentially at $109 million. Research and development was 28% of revenue for the quarter, sales and marketing 25% and G&A 20%. Non-GAAP operating loss was $12 million and adjusted EBITDA meaningfully beat expectations at negative $7 million.

We beat expectations for net cash used in operations at $15 million, and free cash usage was $16 million, a $1 million sequential improvement compared to Q4. Given timing of some larger customer payments, we do expect a sequential increase in operating cash usage in Q2, although still significantly better than the $56 million used in Q2 last year. For the second half, we expect operating cash flow to improve sequentially in Q3 before achieving positive operating cash flow in Q4, as John mentioned.

We expect adjusted EBITDA for Q2 to be in the range of negative $5 million to negative $15 million and non-GAAP EPS of negative $0.02 to negative $0.04. For the full fiscal year, we are reiterating our expectations. We expect adjusted EBITDA to be in the range of break-even to positive $10 million, and non-GAAP EPS to be between negative $0.03 and negative $0.07.

With that, I'll pass the call back to John.

John Giamatteo
Terrific. Thank you, Steve. So why don't we go ahead and proceed now to Q&A. So, Carl, if you don't mind opening the lines, we can take some questions.

QUESTION AND ANSWER

Operator
Certainly. And we will now begin the question and answer session. To ask a question, you may press “*” then “1” on your telephone keypad. Please make sure your line is unmuted. Again, press “*” then “1” to ask a question. We will pause for just a moment to allow everyone the opportunity to signal for questions and we request that you please limit yourself to one question and one follow-up.

And our first question today will come from Luke Junk with Baird. Please go ahead.

Luke Junk
Good afternoon. Thanks for taking the question. John. I'm hoping on near term if you could just unpack what's driving the improvement that you're seeing in the IoT royalties? Is it the new launches coming online? Is it ramping on prior launches? And given what's driving it, just how

sustainable would you think that improvement that we're seeing in the royalties is right now? Thank you.

John Giamatteo
Yes. No, I…that's really being driven by…obviously the $815 million backlog. We've got a number of major design wins that have some pent-up demand. But it's a bit of both. It's existing design wins, things that are rolling off the line as well as some new implementations. So overall, we're really pleased to see kind of more broadly across both sides of the business that, you know, volume had picked up a little bit in the first quarter.

Luke Junk
And then for my follow-up, maybe a bigger picture question. You know there's been some investor concern emerging about auto software suppliers and compute and whatnot being supplanted by OEM partnerships potentially in the wake of VW and Rivian last night. I'd just be curious to get your perspective on that. And especially, this is pretty real time, but I'd be maybe even more curious about just your insight from ongoing dialogue with your customers and what the OEMs you're engaged with are thinking and saying? Thank you.

John Giamatteo
I think in a lot of ways our customers kind of look to us as a trusted advisor who understands the software side of this business better than anyone. So, we work really closely with them. We're definitely collaborating with them on future designs, both from EV as well as in internal combustion. But overall, we kind of feel like we're becoming an increasingly more trusted advisor to them on these kind of matters and going deeper into their organization we’re providing a little bit more value around software-defined vehicle capabilities.

Tim Foote
And I just probably add to that, Luke, if I may, that I don't think those recent announcements really change anything. The moat…the competitive moat around this QNX business continues to remain very deep. And to John's point, if anything, we're in a fairly strong position here that OEMs are coming to us and asking us to do more. So, I don't see any significant headwinds as a result of announcements like last night's.

Luke Junk
That's helpful color. Thanks, Tim.

Operator
And our next question will come from Paul Treiber with RBC Capital Markets. Please go ahead.

Paul Treiber
Thanks for taking the question. Just a comment in regards or a question in regards to the cost reductions. It's good to see more progress. And I think you're at year up to $125 million. How do we think about the path or the opportunity to achieve the remaining $25 million to reach your target of $150 million?

John Giamatteo
Yes. Thanks for the question, Paul. We feel really good about it. I think we've got a comprehensive program around it. We've obviously executed on the $125 million. We're taking further actions to simplify some of the more complex things. I think, I mentioned before things like our IT systems that are kind of hardwired into both of the divisions as we get to the next level of unwinding some of that and building capabilities that are just right for the size of those

businesses, we see a good line of sight to getting to that additional $25 million. So, just as you said, $50 million in Q3, we did an additional $55 million in Q4, $20 million in Q1, and we feel really good about our line of sight to get to the rest.

Paul Treiber
And then a follow-up on the IT systems, is that the bottleneck or the constraint in terms of the separation of the business units at this point? And then once you get through that, will you be effectively ready to separate or split the two units?

John Giamatteo
Yes, I think so. I think when you have systems like Microsoft or Salesforce.com or NetSuite from Oracle that permeates both parts of the businesses, unwinding…we have existing agreements at the parent level, unwinding that, aligning them into the divisions, I think is the next step of really firmly separating the two. But that being said, I will tell you where we are now from where we were in the beginning of the year, these are systems that kind of connect the two business units to one another, because of the nature of how the parents licensed them over the years, but operationally, we've got the separate leadership teams with their separate governance structures. They're operating, I would tell you, faster from a decision-making perspective than we've ever seen them operate. And in my mind, that's the bigger…honestly, that's the bigger lift and the bigger benefit is the fact that these teams can be much more agile and quicker to market opportunities than maybe we were when we were all one big kind of integrated BlackBerry.

Paul Treiber
Okay. Thanks for taking the questions.

John Giamatteo
Thanks Paul.

Operator
And our next question will come from Todd Copeland with CIBC. Please go ahead.

Todd Copeland
Okay. Continue along the lines of the split of the business. When would you expect to provide segmented results for the two units below the revenue line?

John Giamatteo
Yes, Todd, that's a great question. Top of mind for us. Honestly, we've kind of got some pro forma things here in the room right now we're working on. And we're getting them ready for prime time and planning on introducing it to all of you at our analyst update in October.

Todd Copeland
Okay, great. So, you'll break it out, I guess, with the summer quarter's results, and you'll present that at the Analyst Day?

Tim Foote
So, we'll have an earnings call, Todd, as normal. So that will be at the end of September. And then just a couple of weeks later, you can kind of run the wrap for John's prepared remarks actually, which is, that we'll have an Investor Day on October 16th.

Todd Copeland
October 16th. Okay. And October 16th is when you plan to unveil the segmented reporting below the revenue line.

John Giamatteo
Correct, absolutely.

Todd Copeland
Okay. My second question is, I didn't quite understand the headwind comment in IoT. So, I got the upside from royalties in the quarter, but then you went on to talk about mix of drive trains and that's a headwind to the business. And so, I just wanted to make sure I understood what's causing that and is that going to cause the IoT growth rate to settle below the 18% as we go through the year? Just talk through that again, please. Thank you.

Tim Foote
Yes, of course. So, I'll take this one. So the point there, Todd, was that we're agnostic largely to the drivetrain. And there's obviously a lot of talk at this point around some softness on the EV side of the house. The point there was, if we see some softness in EV that almost certainly means it's going to be strength in hybrid or ICE engines. So, we don't actually see that as necessarily a headwind due to the diversification that QNX enjoys. We did reiterate, however, though, that the programs that we've been talking about that have been delayed. Well, we still see that. We'd say there's some signs, some encouraging signs that things are getting better on that front, but it's still very much a headwind. So, when we reiterated our full-year outlook, you need to keep those headwinds in mind when thinking about it. Does that help?

Todd Copeland
Yes, that does help. And those headwinds for the programs, that's not new. That's been going on for a little while, right?

Tim Foote
Yes, we've been talking about that for several quarters now.

Todd Copeland
Yes. And what breaks the logjam on that with what you see today? Just talk through how you're thinking about that? Thanks very much.

John Giamatteo
Well, it's going to vary by OEM and ultimately, we've described it as really they're having to go through a huge transformation from being traditional automakers to having to be software developers. And what they've had to do is ramp up software development team side and that comes with huge challenges and it's not an easy task. So, yes, we've been talking about this for some time. I think ultimately this is not going to be a problem forever. The OEMs will get their hands around it and they will make progress. And I think we're seeing some early signs that that's happening. On our side, we're definitely committed to helping all our customers and the demand for our professional services is possibly an indicator of that. And we're helping to fire that engine by adding some additional headcount into that side of the business. So, we're doing everything we can to help lighten the load for OEMs, but ultimately they're going to get there in the end regardless. So, yes, stay tuned on that one.

Todd Copeland
Great. Appreciate it. Thank you.

Operator
And once again, if you would like to ask a question, please press “*” then “1.” Our next question will come from Kingsley Crane with Canaccord Genuity. Please go ahead.

Kingsley Crane
Hi. Thanks for taking the question. So, between CylanceMDR and MDR on demand, can you talk more about the expansion opportunities you have with respect to endpoint outside of bringing more endpoints under coverage?

John Giamatteo
Well, I think, obviously, a multifaceted approach that we…from a growth of the Cylance business. Certainly, we've got a large installed base of Cylance customers that many of them which are just licensing today our software directly and upselling and upgrading them to MDR services is one kind of track that we're running hard on. Another is focusing on particular verticals where we tend to perform exceptionally well. I think on OT, I think on healthcare customers, customers that have old operating systems that have a variety of different devices, healthcare devices that need to be secured with a small agent and the AI capabilities that we provide is another very, very focused target for us to do there.

And then third, I would say, is kind of that mid to small level market. These are smaller companies that are, say 2,000 seats or smaller. They generally don't have the cyber talent, the cyber resources to manage those environments. So, we see that as a huge opportunity. It's a growing market. MDR is a growing space because they're looking for vendors like us to provide more of that capability. So those are probably the three main tracks that we're focused on to keep that Cylance business, the renewal rates and the ARR moving in the right direction.

Kingsley Crane
Right. Okay. That's really helpful. And so, on the cyber business as a whole, you've done a remarkable job rationalizing costs. Can you talk about what product initiatives you are excited about investing in and how you expect those could drive growth?

John Giamatteo
Yes, I mean I would say, everything we just talked about within Cylance has been investments over the course of the past few years. But one thing I would call out that maybe we don't talk enough about is our SecuSmart. Our SecuSUITE portfolio, which has been really working well for us on that, is we pivoted that business from a very hardware-centric type of approach to a more software token based approach, which we found has opened up a tremendous amount of new use cases and a tremendous amount of new opportunities. So, this was a business when you look back a few years, it was primarily coming out of this special relationship we had with the German government.

When you look at the overall diversification of that business globally with some of our deployments in Canada and the US and Malaysia and Bangladesh and others that we've got some interesting pipeline, that’s an investment that we made in the SecuSUITE platform to really address a completely different segment of the market. That would be another one, I would say, above and beyond that. And then we're very excited, AtHoc, we're releasing our geo-fencing capability. It's a unique capability that differentiates our solution from other solutions that are out there in the market. And we've seen a tremendous amount of demand in governments, police organizations, emergency services. So, it's probably something we haven't talked enough about, but investments we've made in AtHoc and in SecuSmart that have driven growth and driven some nice pipeline for us.

Kingsley Crane
Thank you. Appreciate the time. Great to see the progress.

Operator
And this will conclude our question and answer session. I'd like to turn the conference back over to John Giamatteo, CEO for BlackBerry, for any closing remarks.

CONCLUSION

John Giamatteo
Terrific. Thank you, Carl. So let me just quickly one more time summarize the quarter. We still have a lot of work to do. We know that. But we do believe our strategy is starting to deliver results. We made significant progress in separating our IoT and cyber business and towards profitability. Cash usage in the quarter was better than expected and we improved both adjusted EBITDA and non-GAAP EPS. Revenue for both IoT and cyber beat expectations. IoT had a number of design wins in the quarter, including SDP 8.0, and we saw further small but important improvements in our key metrics like cyber ARR and DBNRR.

So, before we end the call, I guess we kind of preempted this in one of the previous questions, but we do want to let you know that we're excited to be hosting an Investor Day at the New York Stock Exchange on October 16th, where during this event we'll perform a deep dive on the products, the markets, some of the financial profiles that we talked about before of both divisions, and I'm sure you're going to find it valuable. The event will be hybrid with the sessions being live streamed on the day. So, thanks again for joining us today. We'll look forward to seeing you next time.

Operator
This concludes today's call. Thank you for your participation and you may now disconnect.