

BlackBerry Limited

Second Quarter Fiscal Year 2024 Results Conference Call

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CORPORATE PARTICIPANTS

John Chen, *Executive Chair and Chief Executive Officer*

Steve Rai, *Chief Financial Officer*

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CONFERENCE CALL PARTICIPANTS

Mike Walkley, *Canaccord*

Luke Junk, *RW Baird*

Trip Chowdhry, *Global Equities Research*

Paul Treiber, *RBC Capital Markets*

Dan Chan, *TD Cowen*

PRESENTATION

Operator

Good afternoon and welcome to the BlackBerry Second Quarter Fiscal Year 2024 Results Conference Call. My name is Rocco, and I will be your conference moderator for today's call. During the presentation, all participants will be in a listen-only mode. We will be facilitating a brief question-and-answer session towards the end of the conference. [Operator Instructions] As a reminder, this conference is being recorded for replay purposes.

I would now like to turn today's call over to Tim Foote, Vice President of BlackBerry Investor Relations. Sir, please go ahead.

Tim Foote

Thank you, Rocco. Good afternoon and welcome to BlackBerry's second quarter fiscal 2024 earnings conference call. With me on the call today are Executive Chair and Chief Executive Officer, John Chen, 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 of applicable US and Canadian securities laws. We'll indicate forward-looking statements by using words such as expect, will, should, model, intend, 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 a reconciliation between our GAAP and non-GAAP numbers, please see the earnings press release published earlier today, which is available on the EDGAR, SEDAR and blackberry.com websites.

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

John Chen

Thanks, Tim. Good afternoon everyone, and thank you for joining us today. Let me start with the IoT business unit. Revenue for the quarter increased 9% sequentially, to \$49 million, and gross margin increased by 400 basis points to 84%. The most important long-term leading indicator of the health of this business is securing new design wins and building royalty backlog, and we had another strong quarter. In fact, by the end of the first half, we have secured more than two thirds of our FY24 annual target for new backlog and expect to exceed it.

In the quarter QNX secured 20 new design wins in Auto, and 7 in General Embedded Market verticals. The largest of these was an 8-figure estimated lifetime revenue ADAS win with one of the top 5 global automakers to deploy our QNX OS for Safety. This win illustrates the strong secular trend of consolidation of software into centralized compute domains – with this ADAS module powering driver monitoring, surround view, lane keep assist, adaptive cruise control and other safety features all on a single chip.

As automotive software stacks become more complex, and require significantly higher compute power, it plays to QNX's strengths. In addition to our strong win rate for ADAS, we are also the clear market leader for foundational software in the digital cockpit. The combination of our high performance safety-critical RTOS and hypervisor allows for mixed criticality in this domain. Given our market leading position, our design wins continue to be well diversified across all major global markets.

In Asia, we secured a design win with LG Electronics, that included our Hypervisor and will be deployed in a number of vehicle models for a top 10 global automaker. We also secured wins with Visteon and leading OEM Chery, via Bosch, among others.

In Europe, a digital cockpit win also included our acoustics middleware. This is exciting because feedback from customers suggests that this relatively new market opportunity for software-defined acoustics is likely to be fast growing. As well as our very strong footprint in Auto, QNX is well diversified in other verticals, particularly medical and industrial.

Building on our position in surgical robotics, this quarter we secured a design win for our QNX Medical OS for Safety to be deployed in a robotic arm for dentistry. These design wins confirm that the QNX business is strongly positioned for the long term. With revenue for Q2 being largely in line with expectations, we continue to expect IoT to deliver solid year-over-year growth this fiscal year.

That said, we are taking a prudent view on our IoT revenue outlook for the next two quarters. Automakers are currently addressing a number of significant challenges, including industry strike action, the transition to software-defined vehicles, as well as the electrification pivot and supply chain challenges.

Delays to either pre-production software development programs or to production schedules could impact our revenue this fiscal year, however, we expect these to be relatively short-term, timing issues.

As a result, we've revised and broadened the IoT revenue outlook range to \$225 to \$240 million. This represents 9 to 17% year-over-year growth. This means that we still expect to have a strong second half to the fiscal year. We expect further sequential growth into Q3, and we currently expect Q4 to be the strongest quarter for revenue in QNX's history. This confidence is based on a combination of the pipeline of potential new design wins, our services schedule and royalties expected from the backlog.

Turning now to product. At our Analyst Day in May, we announced the upcoming launch of our next generation QNX real-time operating system, 'QNX 8.0', targeted for December. This release will mark a fundamental shift in market performance and we expect it to further cement QNX's leadership position in automotive and beyond. Feedback from the Beta trials has been very positive, with customers and partners impressed with performance, scalability and functionality. Perhaps some of these will convert into revenue in Q4.

This significant enhancement of performance and scalability comes at a time when chipmakers are focused on developing hardware to power Generative AI. We believe that our QNX 8.0 software is uniquely positioned to maximise the potential of GenAI in embedded systems, particularly in safety-critical use cases. QNX 8 will combine best-of-breed performance with the ability to run mission critical processes safely and securely alongside GenAI stacks on the same chip.

Now moving onto IVY. We were delighted to announce that IVY was selected by Tier 1 supplier, Mitsubishi Electric to power new FlexConnect.X in-cabin system. IVY's edge technology, and the high quality real-time insights that it provides, will help enhance road safety and enable new in-vehicle experiences.

In addition, we have solid traction with new IVY proof of concept trials. Currently, we are progressing POCs with a number of major OEMs, including a top-10 global automaker, and leading commercial vehicle OEM, Scania. The strong level of interest for IVY POCs clearly confirms our strategy.

On the product front, this month we released an updated version, with significant enhancements to cloud features, and increased hardware and software support. IVY's development has moved from the early

'heavy lifting' phase, and the focus is now on refinements: enhancing stability, expanding sensor support and improving the developer experience.

The IVY ecosystem continues to expand and mature. We now have over 40 partners currently building on IVY, and there are more than 20 pre-integrated solutions that are being used by customers in POC trials and at industry events.

This month the IVY innovation fund made its latest investment, this time in CorrActions, an exciting Israeli start-up. CorrActions has developed an AI-powered application that will leverage the IVY platform's sensor insights to detect potential driver awareness issues. Their AI model analyzes micro muscle movements, such as through steering wheel sensor data, to understand brain activity, and we are pleased to add them to the ecosystem.

Moving now to the Cybersecurity business unit. Revenue for the quarter was \$79 million, and total contract value billings were \$74 million. Gross margin was 54%. ARR came in at \$279 million. The dollar-based net retention rate was stable at 81%. Revenue this quarter was lower than expectations due to deal slippage. BlackBerry, along with many others in the cybersecurity space, is experiencing elongated deal cycles. Deals are requiring multiple rounds of review and scrutiny, and while this isn't impacting win rates, it is having a real impact on the timing of when deals close. This is especially true in government, where BlackBerry has a very strong presence. In particular, a small number of large, mainly perpetual deals, which therefore had a significant proportion of in-quarter revenue, slipped to later quarters. While this materially impacted Q2's reported revenue, we remain confident with how these deals are progressing and expect them to close this fiscal year.

Further, we have a well-defined pipeline of significant deals, that are progressing well. These deals are primarily in the government vertical, where BlackBerry is well known and trusted, and where we have strong customer relationships.

Due to this overall confidence in a strong improvement in revenue in the second half, compared to the first, we are reiterating the full-year Cyber revenue outlook for the current fiscal year. Because large government deals like these are both complex and binary, we'll of course update you on the progress made in closing them during the next earnings call.

Let me now highlight some of the deals closed during the quarter. In government we secured new deals with the US Department of Justice, Department of State, Department of Energy, and Department of Education. Also, the Internal Revenue Service, the Canada Revenue Agency, the US National Nuclear Security Administration, Customs and Border Protection and the Ministry of Justice Quebec.

Outside of North America, we secured business with the Bank of Italy, Netherlands SSC-ICT as well as the Federal Court of Australia, The Australian Federal Police and the Directorate General of Forces Intelligence in Bangladesh. In fact, we see a good pipeline of opportunities developing in Asia Pacific currently.

In addition to government customers, we secured wins with leading banks, including Morgan Stanley and Santander, as well as with leading technology firms LG, Philips and Toshiba, to name a few.

Moving now to product. Cylance is the pioneer in the use of Artificial Intelligence in cybersecurity, with AI at the very core of its suite of products, long before it became today's buzz word. Our battle-hardened AI model has been trained for many years, continually learning to distinguish threats from non-threats by

referencing trillions of data points. Last month we released a major update to this model, which has been rolled out to our customers, providing an increased level of protection. The model has driven even stronger threat prevention rates than before, and further reduced false positives.

This release is part of the investment we've made in our product portfolio, and these enhancements are being well-received by our customers. This is validated by Cylance Endpoint, our AI-driven prevention, detection and response solution, being placed in the top right-hand quadrant for the Gartner Peer Insights Customers' Choice.

This positioning is based on feedback from real customers, reflecting their experience of our product and us as a company. This pairs nicely with the same recognition received by BlackBerry UEM in February, where it was the only endpoint management solution identified as a Customers' Choice.

Let me now hand the call over to Steve who will provide more colour on our financials.

Steve Rai

Thank you, John. As usual, my comments on our financial performance for the second quarter will be in non-GAAP terms, unless otherwise noted.

Total company revenue for the quarter was \$132 million. IoT revenue was \$49 million, Cybersecurity revenue was \$79 million and Licensing revenue was \$4 million. Software product revenue as a percentage of total revenue, remained in the range of 85 to 90%, with professional services making up the balance. The percentage of software product revenue that was recurring remained at approximately 90%.

Total company gross margin was 65%. Operating expenses for the second quarter were \$114 million, lower sequentially, in part, due to one-time costs associated with the patent sale in Q1 that did not recur, and the release of some IP-related accruals in Q2.

Non-GAAP operating expenses exclude: A \$6 million fair value gain on the convertible debentures; \$10 million in amortization of acquired intangibles; \$10 million in stock based compensation expense; \$3 million in restructuring expenses; and \$1 million in impairment of long-lived assets. The non-GAAP operating loss was \$28 million, and non-GAAP net loss for the second quarter was \$23 million. The 4 cent non-GAAP basic loss per share for the quarter beat expectations. Adjusted EBITDA, excluding the non-GAAP adjustments previously mentioned, was negative \$22 million.

BlackBerry remains laser focused on maximizing efficiency and expanding margins, and we remain on course for both positive operating cash flow and non-GAAP EPS in the fourth quarter, and for the fiscal year as a whole.

Total cash, cash equivalents and investments decreased by \$59 million to \$519 million as at August 31, 2023. Net cash used by operations this quarter was \$56 million. The current debentures mature in November, and we intend to fully repay them. With respect to raising any new debt, the outcome of Project Imperium will obviously have a significant bearing on future needs. Accordingly, we are developing clear, executable plans for a number of the potential scenarios that could arise.

That concludes my comments and I'll turn the call back to John.

John Chen

Thank you, Steve. Before we open the lines for Q&A, let me quickly summarize the key messages. While this quarter saw some volatility in reported revenue due to slipped deals, we remain confident in the pipeline of opportunities for our Cyber business. We expect this to translate into a much stronger second half, and subject to successfully closing a number of our larger government opportunities, we expect to finish within our reiterated full-year revenue range for Cyber. We also remain very confident and excited about the fundamentals of our IoT business, and like Cyber, expect a stronger second half, albeit we are taking a prudent view given delays in the start of some development programs as well as auto industry labour actions.

Let me also provide you with an update regarding Project Imperium. The Board and its advisors are very actively engaged in the process and recognize that it is in everyone's interests that it be completed as soon as possible. All stakeholders should rest assured that we will provide an update as soon as we possibly can.

That concludes my prepared remarks. We will now take your questions. Operator, please can you open the lines for Q&A?

Operator

Absolutely. We will now begin the question-and-answer session. [Operator Instructions] And ladies and gentlemen, our first question today comes from Mike Walkley with Canaccord Genuity. Please go ahead.

John Chen

Hey, Mike.

Mike Walkley – Canaccord

Hey, John. Thank you for taking my question. The first one is just really on the Cybersecurity business. Can you provide a little more granularity on which parts of the Cybersecurity are driving these big perpetual government contracts that you expect to close? Is it mainly Secusmart or is it kind of evenly spread across the portfolio?

John Chen

Mainly Secusmart. Also, UEM, the Spark platform. So mainly, those two.

Mike Walkley – Canaccord

Great. Thank you. And then, I guess on my follow-up question, just any update on how Cylance is trending in the market? You had some good technology there, but some larger companies such as CrowdStrike and others are moving more into the SMB market. Can you maybe talk about how Cylance is fairing in the marketplace?

John Chen

Yeah. We do actually reasonably well. The numbers are obviously smaller than the competitors, but we do reasonably well in the win rates on SMB. We actually had a pretty good quarter with new logos, and it will continue. I said it many times, our products are now up to class, it took us a while. We are working very hard with channel partners to swing them our way. Once we have more achievement there, we will have more leverage. But clearly, the product could win and Guard is a good solution.

Mike Walkley – Canaccord

That's helpful. Thanks for taking my two questions. I'll pass the line.

John Chen

Sure. Thank you.

Operator

Thank you. And our next question today comes from Luke Junk with Baird. Please go ahead.

Luke Junk – RW Baird

Good afternoon. Thanks for taking the questions. John, for starters, last few quarters, your customers' software delays have been seen – we've seen repeat a few times. It would just be great to get your perspective on how widespread this issue within your customer base is right now. And most importantly, what the effect that customers are telling you needs to get done to get back on track? You mentioned in the script that you have confidence this will be a relatively short-term timing issue. Could you just expand on the reasons why you believe that to be the case? Thank you.

John Chen

Right, okay. Well, that's a good question. The companies that are looking at their software design vehicle effort and that have pushed out some and delayed either the start of the designs or starting into the production, are the really big companies. And some of them are very visible. They've announced reorgs. That actually, the outcome favors the software-defined vehicle strategy. Toyota has announced a reorg. VW has announced a reorg. I mean, and a number of others that have not announced reorgs, and then pardon me for not being able to repeat that because that's customer proprietary information. They will not be happy with me. You could get that sense.

However, everybody has kind of told us that it's like not in a position way, but it's kind of like a one-year move, four-quarter move. Frankly speaking, we are in the third or the fourth quarter already. This is one of the reason why the team has some really strong pipeline that they believe in for Q4, and as I want to repeat this, we expect Q4 to be the best quarter for revenue for QNX, ever.

Luke Junk – RW Baird

Okay, great. Thank you for that, John. And then for my follow-up, I'll stay within IoT. Going back to the Analyst Day earlier this year, one of the things that you mentioned strategically was looking to continue to engage more directly with OEMs as a Tier 1 and accelerating your OEM account coverage. I'm just wondering to what extent the current delays you're seeing impact your appetite for those sorts of investments in IoT that are outward facing, and just reconcile that with the overall desire to expand margins a little bit. Thank you.

John Chen

Right. We have – because we believe our fundamentals are so strong and because we believe our new product 8.0 scalability is so good, we are not slowing down any of our appetite at all. We are steadfastly moving forward. IoT is hiring people. We don't – won't worry about us kind of taking our foot off the gas pedal. That's not going to happen.

Luke Junk – RW Baird

Understood. Thank you.

John Chen

Sure.

Operator

And our next question today comes from Trip Chowdhry with Global Equities Research. Please go ahead.

John Chen

Hi, Trip.

Trip Chowdhry – Global Equities Research

Thank you very much. Hello, John. The auto industry seems to be super excited with QNX. And now, at least like companies like NXP, they term something like you talk IoT as Edge Square, where they put a lot of AI and they call 'Tiny ML' that powers these devices.

I was wondering, like QNX definitely with the low footprint and real-time operating system is ideal, but I was also wondering, have you come across some new sensors, the category that may have been created because of AI in the edge and these neural network processors like NXP that they make? The industry is trying to – industry structure is changing. That's my basic question, is if Tiny ML, Edge Square, QNX and some new use cases that may be evolving. So, I was wondering if you have any thoughts on that.

John Chen

Yeah. It's a good point. I think there's still – what you are explaining is, I read it, it's still early in the industry. And I also want to emphasize the fact that we are an embedded operating system, real-time secure operating systems. And so, we tend to go into the MPU type, the central complex, computing complex.

The edge of this, which will be driven with different new use cases, some of them are AI-based and all that, but that's a level higher than us. Of course, we will be benefiting from it from needing more central compute power. I guess we do benefit from it. We don't directly go and create a selling motion into the edge, and that edge selling motion and use cases are created by a code that is on the stack that is one level above us.

Trip Chowdhry – Global Equities Research

Excellent. And...

John Chen

Make sense?

Trip Chowdhry – Global Equities Research

Yes, I got it. The second question is regarding IVY. Phenomenal traction on the developer side apps. I don't know, probably, we are about six, eight months away from it. But I was wondering, have you come across any new categories of apps that may be coming on top of IVY? And that's all for me. Thank you very much.

John Chen

Well, the AI and sensing, oh, are actually interesting. To tieback to your first question, the different type of sensors that are being demanded in a car, we have seen different types and more increased and more complex. And like one of the examples, when I talk about CorrActions was that they monitor the sensors on the steering wheel. And then through that, they monitor – they help define the micro muscles of the individual and then dictate or indicate what the status is of the driver on an alertness basis and awareness basis.

This is a little bit more esoteric than just measuring how much gas you have in the tank or how much charging amps that you still have before you need to do the next charge. We have seen more and more modern types of applications, but I still believe for the initial usage of IVY, it's going to be very fundamentally managing the safety and the comfort of the car.

Trip Chowdhry – Global Equities Research

Got it. Thank you so much.

John Chen

Thank you, Trip.

Operator

And our next question today comes from Paul Treiber with RBC Capital Markets. Please go ahead.

John Chen

Hey, Paul. Hi, Paul.

Paul Treiber – RBC Capital Markets

Hi, John. Good afternoon.

John Chen

Good afternoon.

Paul Treiber – RBC Capital Markets

Just in regards to your comments about Q4 being the best quarter for IoT, how do we think about the momentum beyond Q4? Like, do you expect it to be carried through to the subsequent year or is it more just a one-quarter phenomenon?

John Chen

No. It's a good question. I don't believe we're going to have a Q1 FY 2025 bigger than Q4, if that's what you're asking. But I do believe that we have – we still fall into the 20% growth on year-over-year, that we presented to you all in the May meeting.

You do expect us to have double-digit growth and pushing to a 20% growth year-over-year. By then, I hope that these so-called software-defined vehicle efforts delay and, hopefully, everybody seems to have a reasonable handle on the supply chain despite the political situation between US, China, Western world and so forth. That's gradually getting under control.

Electrification is on everybody's – it's in their product specs, so to speak. Although to us, it's really hoping that that drives more volume of cars, not so much as electric versus gas, we have a difference there. If that is removed, then we will start seeing design wins that will turn into developer seats, to professional services engagements, and then ultimately turn into royalty backlog – royalties.

Fundamentally, we see nothing concerning at all. We see this as a purely a timing issue and we see it starting to get better in Q4, unless there's some other industry events like the UAW strikes that last longer, then we – that's a little bit out of our control. Even though, even the UAW strikes, it's not going to last. As you probably know this very well, it's not going to last into perpetuity and – because both sides get hurt. I think they will resolve it, I certainly hope they will, and then it will get back on track.

Paul Treiber – RBC Capital Markets

Okay, then. My second question, I don't know how much you can answer it, but I'll throw it out there, just in regards to Project Imperium, I know you can't give specifics, but have you or the board reached a point where you've narrowed down to a few high-level paths, and can you sort of share the high-level paths?

John Chen

Yes. I can't comment on it, but the answer is yes.

Paul Treiber – RBC Capital Markets

Okay. Thanks for taking the questions.

John Chen

Sure.

Operator

And our next question today comes from Daniel Chan with TD Cowen. Please go ahead.

Dan Chan – TD Cowen

Hey, John.

John Chen

Hey.

Dan Chan – TD Cowen

You expected the strategic review to conclude by the end of summer and your contract with BlackBerry is quickly approaching. Would it be possible that this review goes past November or should we expect something in the next month or so?

John Chen

I think there is better than a 50/50 chance that you should expect something sooner.

Dan Chan – TD Cowen

Okay. That's helpful. And then maybe another question on the timing, to what extent do you think the uncertainty from the strategic review is having an impact on the near-term financial performance, whether it be from staff productivity or even customers waiting for a conclusion?

John Chen

No. Actually, I mean, really seriously. I check this a lot, because that's an obvious concern. And from a customer point of view, no, I don't see that. There might be one or two conversations I've had, but it was like kind of like, oh, by the way, when I talk to the customer, they say, oh, by the way, what's going on there, that kind of thing, and – or somebody asks me as part of a long conversation and also – and they say, "oh, should I be concerned about this?", and I said, "No, no, you have nothing to be concerned about. We stand behind everything we do, and build, and deliver."

Not much really coming – and the sales force has not, in fact, fed back to me about this being a roadblock of any sorts. But having said that, the longer it lingers on, the worst it's going to get, and even though it is not a big problem. So, I have no intention. Because of being an operator, I got employees, partners, customers, shareholders to worry about. We're not going to let this thing – it might take a long time, multiple steps, but there will be some decision made.

Dan Chan – TD Cowen

That's helpful. Thanks, John.

John Chen

Sure.

Operator

Thank you. I would like to turn the call back over to John Chen, Executive Chair and CEO of BlackBerry, for closing remarks.

John Chen

Thank you, Operator. Before we end today's call, I'd like to remind everyone of our upcoming BlackBerry Summit on October 17th at the Conrad New York Downtown. The event, anchored around the theme of "Trust", has been expanded this year to include IoT and we have a strong line up of keynotes, as well as product demos and breakout sessions. You can register to attend at BlackBerry.com/Summit. Stay tuned for more announcements around the event.

Thank you to everyone for joining the call. I look forward to speaking with you very soon.

Operator

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