

BLACKBERRY LIMITED

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS FOR THE THREE AND SIX MONTHS ENDED AUGUST 31, 2018

September 28, 2018

The following Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") should be read together with the unaudited interim consolidated financial statements and the accompanying notes (the "Consolidated Financial Statements") of BlackBerry Limited (the "Company" or "BlackBerry") for the three and six months ended August 31, 2018, as well as the Company's audited consolidated financial statements and accompanying notes, and MD&A for the fiscal year ended February 28, 2018 (the "Annual MD&A"). The Consolidated Financial Statements are presented in U.S. dollars and have been prepared in accordance with United States generally accepted accounting principles ("U.S. GAAP"). All financial information in this MD&A is presented in U.S. dollars, unless otherwise indicated.

The Company has prepared this MD&A with reference to *National Instrument 51-102* "Continuous Disclosure Obligations" of the Canadian Securities Administrators. Under the U.S./Canada Multijurisdictional Disclosure System, the Company is permitted to prepare this MD&A in accordance with the disclosure requirements of Canada, which are different from those of the United States. This MD&A provides information for the three and six months ended August 31, 2018 and up to and including September 28, 2018.

Additional information about the Company, including the Company's Annual Information Form for the fiscal year ended February 28, 2018 (the "AIF"), which is included in the Company's Annual Report on Form 40-F for the fiscal year ended February 28, 2018 (the "Annual Report"), can be found on SEDAR at www.sedar.com and on the U.S. Securities and Exchange Commission's website at www.sec.gov.

Cautionary Note Regarding Forward-Looking Statements

This MD&A contains forward-looking statements within the meaning of certain securities laws, including under the U.S. Private Securities Litigation Reform Act of 1995 and applicable Canadian securities laws, including statements relating to:

- the Company's plans, strategies and objectives, including the anticipated benefits of its strategic initiatives and its intentions to grow revenue and increase and enhance its product and service offerings;
- the Company's expectations regarding its free cash flow, recurring total software and services revenue, excluding intellectual property ("IP") and professional services, total software and services revenue growth, Enterprise software and services revenue, BTS revenue growth, IP revenue, BlackBerry Radar revenue, total software and services billings growth, BTS billings growth, Licensing, IP and other billings growth, Enterprise software and services billings growth and non-GAAP earnings per share for fiscal 2019;
- the Company's estimates of purchase obligations and other contractual commitments; and
- the Company's expectations with respect to the sufficiency of its financial resources.

The words "expect", "anticipate", "estimate", "may", "will", "should", "could", "intend", "believe", "target", "plan" and similar expressions are intended to identify forward-looking statements in this MD&A, including in the sections entitled "Business Overview", "Business Overview -Strategy", "Second Quarter Fiscal 2019 Summary Results of Operations - Financial Highlights - Free Cash Flow", "Results of Operations – Three months ended August 31, 2018 compared to three months ended August 31, 2017 - Consolidated Revenue", "Results of Operations – Six months ended August 31, 2018 compared to six months ended August 31, 2017 – Net Income (Loss)", and "Financial Condition – Debenture Financing and Other Funding Sources". Forward-looking statements are based on estimates and assumptions made by the Company in light of its experience, historical trends, current conditions and expected future developments, as well as other factors that the Company believes are appropriate in the circumstances. Many factors could cause the Company's actual results, performance or achievements to differ materially from those expressed or implied by the forward-looking statements, including, without limitation, the factors discussed in the "Risk Factors" section of the AIF and the following:

- the Company's ability to enhance, develop, introduce or monetize products and services for the enterprise market in a timely manner with competitive pricing, features and performance;
- the Company's ability to maintain or expand its customer base for its software and services offerings to grow revenue or achieve sustained profitability;

- the intense competition faced by the Company;
- the occurrence or perception of a breach of the Company's network or product security measures, or an inappropriate disclosure of confidential or personal information;
- risks related to the Company's continuing ability to attract new personnel, retain existing key personnel and manage its staffing effectively;
- the Company's dependence on its relationships with resellers and distributors;
- the risk that network disruptions or other business interruptions could have a material adverse effect on the Company's business and harm its reputation; and
- risks related to acquisitions, divestitures, investments and other business initiatives, which may negatively affect the Company's results of operations.

All of these factors should be considered carefully, and readers should not place undue reliance on the Company's forward-looking statements. Any statements that are forward-looking statements are intended to enable the Company's shareholders to view the anticipated performance and prospects of the Company from management's perspective at the time such statements are made, and they are subject to the risks that are inherent in all forward-looking statements, as described above, as well as difficulties in forecasting the Company's financial results and performance for future periods, particularly over longer periods, given the ongoing transition in the Company's business strategy and the rapid technological changes, evolving industry standards, intense competition and short product life cycles that characterize the industries in which the Company operates. See "Business Overview - Strategy, Products and Services" in this MD&A, as well as the "Narrative Description of the Business - Strategy" section in the AIF.

The Company has no intention and undertakes no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by applicable law.

Business Overview

The Company is an enterprise software and services company focused on securing and managing Internet of Things ("IoT") endpoints. Based in Waterloo, Ontario, the Company was founded in 1984 and operates in North America, Europe, Asia, Middle East, Latin America and Africa. The Company's common shares trade under the ticker symbol "BB" on the Toronto Stock Exchange and the New York Stock Exchange.

Strategy

The Company is widely recognized for productivity and security innovations, and the Company believes that it delivers the most secure end-to-end mobile enterprise solutions in the market. With these core strengths, the Company's broad portfolio of products and services is focused on serving enterprise customers, particularly in regulated industries.

The Company is focused on delivering an end-to-end software and services platform for the Enterprise of Things. The Company defines the Enterprise of Things as the network of devices, computers, vehicles, sensors, equipment and other connected endpoints within the enterprise that communicate with each other to enable smart business processes. The Company leverages many elements of its extensive technology portfolio to extend best-in-class security and reliability to its solutions for the Enterprise of Things, including unified endpoint management ("UEM"), embedded systems, crisis communications, enterprise applications, and related services, with hosting available on the Company's global, scalable, secure network, as well as on public clouds.

The Company intends to continue to increase and enhance its product and service offerings through both strategic acquisitions and organic investments. The Company's goal is to maintain its market leadership in the enterprise mobility segment by continuing to extend the functionality of its platform for the Enterprise of Things and, on top of this extensive foundation, deliver cybersecurity software and embedded solutions focused on strategic industry verticals.

Products and Services

The Company's core software and services offering is the BlackBerry Secure platform, which integrates a broad portfolio of enterprise communication technologies and safety-certified embedded solutions, including BlackBerry UEM, BlackBerry Dynamics, the QNX CAR Platform and Neutrino Operating System, AtHoc Alert, AtHoc Account, SecuSUITE, and BlackBerry Workspaces. BlackBerry UEM offers a "single pane of glass", or unified console view, for managing and securing devices, applications, identity, content, and IoT endpoints across all leading operating systems. BlackBerry Dynamics offers a best-in-class development platform and secure container for mobile applications, including the Company's own enterprise applications such as BlackBerry Work and BlackBerry Connect for secure collaboration. BlackBerry AtHoc provides secure, networked crisis communications solutions, and Secusmart provides secure voice and text messaging solutions with advanced encryption and anti-eavesdropping capabilities. The Company recently announced its forthcoming Enterprise of Things platform, BlackBerry Spark, designed and built for ultra-secure hyperconnectivity.

The BlackBerry QNX unit is a global provider of real-time operating systems, middleware, development tools, and professional services for connected embedded systems, primarily in the automotive, medical and industrial automation markets. A leader in software for automotive electronics, BlackBerry QNX offers a growing portfolio of certified safety-critical modules and platform solutions and is focusing on achieving design wins with automotive original equipment manufacturers, Tier 1 vendors and automotive semiconductor suppliers.

The Company also offers its BlackBerry Radar asset tracking solution, Paratek antenna tuning technology, Certicom cryptography and key management products, and its BlackBerry Messenger ("BBM") Enterprise service, together with the BBM Enterprise SDK for the Communications Platform as a Service market.

The Company is also engaged in the development and licensing of the Company's secure device software and the outsourcing to partners of all design, manufacturing, sales and customer support for BlackBerry-branded, and white label handsets. The Company intends to expand its security software and brand licensing program, under which the BlackBerry KEY2 and BlackBerry KEY2 LE, BlackBerry Evolve and Evolve X, BlackBerry KEYone, BlackBerry Aurora, and BlackBerry Motion smartphones have been launched to date, to include a broader set of devices and non-smartphone endpoints. The Company also licenses its other intellectual property assets, including certain of its patents as well as assets related to the BBM Consumer service.

In addition, the Company continues to generate service access fees ("SAF") charged to subscribers using the Company's legacy BlackBerry 7 and prior BlackBerry operating systems, and an allocation of revenue relating to service obligations and unspecified future software upgrades associated with BlackBerry 10 devices.

Please also see the "Narrative Description of the Business - Strategy" section in the AIF, which is included in the Annual Report.

Recent Developments

The Company continues to execute on its strategy in fiscal 2019 and announced the following achievements:

- Announced new software and services as part of BlackBerry Spark, the Company's new Enterprise of Things platform designed and built for ultra-secure hyperconnectivity;
- Recognized as a leader in Gartner's magic quadrant for unified endpoint management tools;
- Recognized as a leader in the 2018 IDC MarketScape assessment of enterprise mobility management vendors;
- Launched three new automotive software products certified to ISO 26262, the automotive industry's functional safety standard: BlackBerry's QNX Hypervisor for Safety, QNX Platform for ADAS 2.0, and QNX OS for Safety 2.0, enabling automakers to accelerate development timelines and reduce cost;
- Announced that BlackBerry QNX software is embedded in the advanced driver assistance system, digital instrument clusters, connectivity modules, handsfree systems or infotainment systems of more than 120 million cars on the road;
- Entered into a strategic partnership with Microsoft Corp. to offer enterprises BlackBerry Enterprise Bridge, a solution that integrates BlackBerry's expertise in mobility and security with Microsoft's cloud and productivity products;
- Entered into a multi-year agreement with Jaguar Land Rover to collaborate and develop technology for the automotive manufacturer's next-generation vehicles;
- Collaborated with the Government of Canada to modernize their operations centers during G7 ministerial meetings and the 2018 G7 Summit;
- Joined the OmniAir Consortium as an executive member to help advance the testing, certification, and deployment of technologies for connected vehicles and intelligent transportation systems;
- Signed a technology and brand licensing deal for BlackBerry Secure with Swiss consumer electronics maker Punkt Tronics AG;

- Entered into a licensing agreement with Bullitt Group to embed BlackBerry cybersecurity technology into a range of highly-secure, rugged Caterpillar- and Land Rover-branded connected devices to be certified as “BlackBerry Secure”;
- Entered into an arrangement with electric vehicle maker BYTON to license BlackBerry QNX technologies for the in-car experience within its first series of production vehicles;
- Entered into a multi-year strategic relationship with Samsung Electronics Co. Ltd. to collaborate on integrated solutions to accelerate the digital transformation of their shared enterprise customers;
- Launched a new ransomware recovery capability within BlackBerry Workspaces that allows organizations to quickly recover from cyberattacks;
- Entered into a global independent software vendor partnership with Check Point Software Technologies Ltd. to mitigate cybersecurity threats; and
- Entered into a partnership with L-SPARK to help small and medium-sized technology enterprises grow their businesses and bring new products to market using BlackBerry QNX technology.

2019 Executive Chair Incentive Grant

In the first quarter of fiscal 2019, the Company granted a time-based equity award, a long-term market performance-based equity award and a contingent cash award to the Company's Executive Chair and CEO as an incentive to remain as Executive Chair until November 3, 2023.

The time-based equity award consists of five million time-based RSUs that will vest annually in five equal tranches beginning on November 3, 2019. The market performance-based equity award consists of five tranches, each of one million market-condition RSUs that will become earned and vested when the 10-day average closing price of the Company's common shares on the New York Stock Exchange reaches \$16, \$17, \$18, \$19 and \$20, respectively. Any market-condition RSUs that have not been earned before November 3, 2023 will terminate on such date. The contingent cash award consists of a cash amount of \$90 million that will become payable when the 10-day average closing price of the Company's common shares on the New York Stock Exchange reaches \$30. If unearned, the contingent cash award will terminate on November 3, 2023.

Normal Course Issuer Bid

The common share repurchase program that the Company commenced on June 23, 2017 expired on June 26, 2018. Over the course of the program, the Company repurchased for cancellation approximately 2 million common shares for approximately \$18 million. During the three months ended August 31, 2018, the Company did not repurchase any common shares.

Non-GAAP Financial Measures

The Consolidated Financial Statements have been prepared in accordance with U.S. GAAP, and information contained in this MD&A is presented on that basis unless otherwise noted. On September 28, 2018, the Company announced financial results for the three and six months ended August 31, 2018, which included certain non-GAAP financial measures, including adjusted revenue, adjusted gross margin, adjusted gross margin percentage, adjusted EBITDA, adjusted EBITDA margin, adjusted income (loss) before income taxes, adjusted net income (loss) and adjusted earnings (loss) per share. The Company believes the presentation of these non-GAAP measures provides management and shareholders with important information regarding the Company's financial performance due to the financial statement impact of the Company's transformation from a hardware-focused handset manufacturer to an enterprise software and services company with recurring revenue streams.

For the three months ended August 31, 2018, these measures were adjusted for the following (collectively, the “Q2 Fiscal 2019 Non-GAAP Adjustments”) (all items pre-tax and after-tax):

- the Q2 Fiscal 2019 Debentures Fair Value Adjustment (as defined below under “Second Quarter Fiscal 2019 Summary Results of Operations – Financial Highlights – Debentures Fair Value Adjustment”) of approximately \$70 million;
- restructuring charges from the Resource Allocation Program (“RAP”) and recoveries from Cost Optimization and Resource Efficiency (“CORE”) programs consisting of amounts associated with employee termination benefits, facilities, and certain other costs of approximately \$3 million on a net basis;
- software deferred revenue acquired but not recognized due to business combination accounting rules of approximately \$4 million;
- stock compensation expense of approximately \$21 million;
- amortization of intangible assets acquired through business combinations of approximately \$22 million; and
- business acquisition and integration costs recovered through business combinations of approximately \$2 million.

BlackBerry Limited
Management's Discussion and Analysis of Financial Condition and Results of Operations

The Company believes that presenting non-GAAP financial measures that exclude the impact of those items enables it and its shareholders to assess the Company's operating performance relative to its consolidated financial results in prior and future periods on a more comparable basis. Readers are cautioned that adjusted revenue, adjusted gross margin, adjusted gross margin percentage, adjusted EBITDA, adjusted EBITDA margin, adjusted income (loss) before income taxes, adjusted net income (loss), adjusted earnings (loss) per share and similar measures do not have any standardized meaning prescribed by U.S. GAAP and therefore might not be comparable to similarly titled measures reported by other companies. These non-GAAP financial measures should be considered in the context of the U.S. GAAP results, which are presented in the Consolidated Financial Statements and are described in this MD&A. A reconciliation from the most directly comparable U.S. GAAP measures to these non-GAAP financial measures for the three months ended August 31, 2018 was included in the Company's press release dated September 28, 2018, and is reflected in the table below:

Q2 Fiscal 2019 Non-GAAP Adjustments		For the Three Months Ended August 31, 2018 <i>(in millions, except for per share amounts)</i>					
	Income statement location	Revenue	Gross margin <i>(before taxes)</i>	Gross margin % <i>(before taxes)</i>	Income before income taxes	Net income	Basic earnings per share
As reported		\$ 210	\$ 161	76.7%	\$ 44	\$ 43	\$ 0.08
Debtentures fair value adjustment ⁽¹⁾	Debtentures fair value adjustment	—	—	—%	(70)	(70)	
Restructuring charges ⁽²⁾	Cost of sales	—	1	0.4%	1	1	
Restructuring charges ⁽²⁾	Selling, marketing and administration	—	—	—%	2	2	
Software deferred revenue acquired ⁽³⁾	Revenue	4	4	0.5%	4	4	
Stock compensation expense	Cost of sales	—	1	0.4%	1	1	
Stock compensation expense	Research and development	—	—	—%	3	3	
Stock compensation expense	Selling, marketing and administration	—	—	—%	17	17	
Acquired intangibles amortization	Amortization	—	—	—%	22	22	
Business acquisition and integration costs recovered	Selling, marketing and administration	—	—	—%	(2)	(2)	
Adjusted		<u>\$ 214</u>	<u>\$ 167</u>	<u>78.0%</u>	<u>\$ 22</u>	<u>\$ 21</u>	<u>\$ 0.04</u>

(1) See "Second Quarter Fiscal 2019 Summary Results of Operations – Financial Highlights - Debtentures Fair Value Adjustment".

(2) See "Second Quarter Fiscal 2019 Summary Results of Operations – Financial Highlights - Restructuring Charges".

(3) Included in Enterprise software and services revenue.

For the six months ended August 31, 2018, these non-GAAP measures were adjusted for the following (collectively, the "Fiscal 2019 Non-GAAP Adjustments") (all items pre-tax and after-tax):

- the Fiscal 2019 Debtentures Fair Value Adjustment (as defined below under "Second Quarter Fiscal 2019 Summary Results of Operations – Financial Highlights – Debtentures Fair Value Adjustment") of approximately \$42 million;
- restructuring charges from RAP and recoveries from CORE programs consisting of amounts associated with employee termination benefits, facilities, and certain other costs of approximately \$7 million on a net basis;
- software deferred revenue acquired but not recognized due to business combination accounting rules of approximately \$8 million;
- stock compensation expense of approximately \$39 million;
- amortization of intangible assets acquired through business combinations of approximately \$44 million; and
- business acquisition and integration costs recovered through business combinations of approximately \$1 million.

BlackBerry Limited
Management's Discussion and Analysis of Financial Condition and Results of Operations

A reconciliation from the most directly comparable U.S. GAAP measures to the non-GAAP financial measures for the six months ended August 31, 2018 is reflected in the table below.

Fiscal 2019 Non-GAAP Adjustments		For the Six Months Ended August 31, 2018 <i>(in millions, except for per share amounts)</i>					
	Income statement location	Revenue	Gross margin <i>(before taxes)</i>	Gross margin % <i>(before taxes)</i>	Income (loss) before income taxes	Net income (loss)	Basic earnings (loss) per share
As reported		\$ 423	\$ 322	76.1%	\$ (15)	\$ (17)	\$ (0.03)
Debtentures fair value adjustment ⁽¹⁾	Debtentures fair value adjustment	—	—	—%	(42)	(42)	
Restructuring charges ⁽²⁾	Cost of sales	—	1	0.3%	1	1	
Restructuring charges ⁽²⁾	Research and development	—	—	—%	2	2	
Restructuring charges ⁽²⁾	Selling, marketing and administration	—	—	—%	4	4	
Software deferred revenue acquired ⁽³⁾	Revenue	8	8	0.4%	8	8	
Stock compensation expense	Cost of sales	—	2	0.5%	2	2	
Stock compensation expense	Research and development	—	—	—%	6	6	
Stock compensation expense	Selling, marketing and administration	—	—	—%	31	31	
Acquired intangibles amortization	Amortization	—	—	—%	44	44	
Business acquisition and integration costs recovered	Selling, marketing and administration	—	—	—%	(1)	(1)	
Adjusted		<u>\$ 431</u>	<u>\$ 333</u>	<u>77.3%</u>	<u>\$ 40</u>	<u>\$ 38</u>	<u>\$ 0.07</u>

(1) See "Second Quarter Fiscal 2019 Summary Results of Operations – Financial Highlights - Debtentures Fair Value Adjustment".

(2) See "Second Quarter Fiscal 2019 Summary Results of Operations – Financial Highlights - Restructuring Charges".

(3) Included in Enterprise software and services revenue.

Similarly, on September 28, 2017, the Company announced financial results for the three and six months ended August 31, 2017, which included certain non-GAAP financial measures, including adjusted revenue, adjusted gross margin, gross margin percentage, adjusted EBITDA, adjusted income before income taxes, adjusted net income and adjusted earnings per share.

For the three months ended August 31, 2017, these measures were adjusted for the following (collectively, the "Q2 Fiscal 2018 Non-GAAP Adjustments") (all items pre-tax and after tax):

- a fair value adjustment associated with the Company's convertible debtentures of approximately \$70 million;
- a long-lived asset impairment charge (the "Fiscal 2018 LLA Impairment Charge"), recognized when the carrying value exceeds the fair value of an asset group of \$11 million;
- RAP charges of approximately \$18 million;
- software deferred revenue acquired but not recognized due to business combination accounting rules of approximately \$11 million;
- stock compensation expense of approximately \$12 million;
- amortization of intangible assets acquired through business combinations of approximately \$24 million; and
- business acquisition and integration costs incurred through business combinations of approximately \$1 million.

For the six months ended August 31, 2017, these measures were adjusted for the following (collectively, the "Fiscal 2018 Non-GAAP Adjustments") (all items pre-tax and after tax):

- recovery of the overpayment of royalties from the Qualcomm arbitration award of \$815 million;
- interest income related to the overpayment of the above royalties of \$139 million;
- the Fiscal 2018 LLA Impairment Charge of \$11 million;
- a fair value adjustment associated with the Company's convertible debtentures of approximately \$148 million (the "Fiscal 2018 Debtentures Fair Value Adjustment");

BlackBerry Limited
Management's Discussion and Analysis of Financial Condition and Results of Operations

- RAP charges of approximately \$35 million;
- software deferred revenue acquired but not recognized due to business combination accounting rules of approximately \$20 million;
- stock compensation expense of approximately \$25 million;
- amortization of intangible assets acquired through business combinations of approximately \$49 million; and
- business acquisition and integration costs incurred through business combinations of approximately \$12 million.

A reconciliation from the most directly comparable U.S. GAAP measures to these non-GAAP financial measures for the three and six months ended August 31, 2017 was included in the Company's press release, dated September 28, 2017, and is reflected in the table below.

	Income statement location	For the Three Months Ended August 31, 2017				For the Six Months Ended August 31, 2017			
		<i>(in millions)</i>							
		Revenue	Gross margin (before taxes)	Income before income taxes	Net income	Revenue	Gross margin (before taxes)	Income before income taxes	Net income
As reported		\$ 238	\$ 175	\$ 23	\$ 19	\$ 473	\$ 325	\$ 695	\$ 690
Debtentures fair value adjustment	Debtentures fair value adjustment	—	—	(70)	(70)	—	—	148	148
LLA impairment charge	Impairment of long-lived assets	—	—	11	11	—	—	11	11
RAP charges	Cost of sales	—	3	3	3	—	6	6	6
RAP charges	Research and development	—	—	1	1	—	—	4	4
RAP charges	Selling, marketing and administration	—	—	14	14	—	—	25	25
Software deferred revenue acquired ⁽¹⁾	Revenue	11	11	11	11	20	20	20	20
Stock compensation expense	Cost of sales	—	1	1	1	—	2	2	2
Stock compensation expense	Research and development	—	—	3	3	—	—	7	7
Stock compensation expense	Selling, marketing and administration	—	—	8	8	—	—	16	16
Acquired intangibles amortization	Amortization	—	—	24	24	—	—	49	49
Business acquisition and integration costs	Selling, marketing and administration	—	—	1	1	—	—	12	12
Qualcomm arbitration award	Qualcomm arbitration award	—	—	—	—	—	—	(815)	(815)
Qualcomm arbitration award	Investment income, net	—	—	—	—	—	—	(139)	(139)
Adjusted		<u>\$ 249</u>	<u>\$ 190</u>	<u>\$ 30</u>	<u>\$ 26</u>	<u>\$ 493</u>	<u>\$ 353</u>	<u>\$ 41</u>	<u>\$ 36</u>

(1) Included in Enterprise software and services revenue

BlackBerry Limited
Management's Discussion and Analysis of Financial Condition and Results of Operations

The Company also reported adjusted EBITDA and adjusted EBITDA margin, as presented in the tables below, for the three and six months ended August 31, 2018 of \$33 million and 15%, and \$64 million and 15%, respectively. These are non-GAAP financial measures that do not have any standardized meaning as prescribed by U.S. GAAP and are therefore unlikely to be comparable to similar measures presented by other companies.

	For the Three Months Ended August 31, 2018 <i>(in millions)</i>	For the Six Months Ended August 31, 2018 <i>(in millions)</i>
Operating income (loss)	\$ 39	\$ (26)
Non-GAAP adjustments to operating income (loss)		
Debentures fair value adjustment	(70)	(42)
Restructuring charges	3	7
Software deferred revenue acquired	4	8
Stock compensation expense	21	39
Acquired intangibles amortization	22	44
Business acquisition and integration recovery	(2)	(1)
Total non-GAAP adjustments to operating income (loss)	(22)	55
Non-GAAP operating income	17	29
Amortization	38	79
Acquired intangibles amortization	(22)	(44)
Adjusted EBITDA	\$ 33	\$ 64
Adjusted revenue (per above)	214	431
Adjusted EBITDA margin	15%	15%

Adjusted EBITDA and adjusted EBITDA margin for the three and six months ended August 31, 2017 are reflected in the table below:

	For the Three Months Ended August 31, 2017 <i>(in millions)</i>	For the Six Months Ended August 31, 2017 <i>(in millions)</i>
Operating income	\$ 22	\$ 558
Non-GAAP adjustments to operating income		
Debentures fair value adjustment	(70)	148
LLA impairment	11	11
RAP charges	18	35
Software deferred revenue acquired	11	20
Stock compensation expense	12	25
Acquired intangibles amortization	24	49
Business acquisition and integration costs	1	12
Arbitration award	—	(815)
Total non-GAAP adjustments to operating income	7	(515)
Non-GAAP operating income	29	43
Amortization	45	96
Acquired intangibles amortization	(24)	(49)
Adjusted EBITDA	\$ 50	\$ 90
Adjusted revenue (per above)	249	493
Adjusted EBITDA margin	20%	18%

The Company also reported free cash flow as described in "Second Quarter Fiscal 2019 Summary Results of Operations - Free Cash Flow", below.

Accounting Policies and Critical Accounting Estimates

There have been no changes to the Company's accounting policies or critical accounting estimates from those described under "Accounting Policies and Critical Accounting Estimates" in the Annual MD&A, with the exception of those noted below.

In May 2014, the Financial Accounting Standards Board (the "FASB") issued ASC 606, a new accounting standard on the topic of revenue contracts, which replaces the existing revenue recognition standard. The new standard amended a number of requirements that an entity must consider in recognizing revenue and requires improved disclosures to help readers of financial statements better understand the nature, amount, timing and uncertainty of revenue recognized. For public entities, the new standard was effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. The Company adopted this guidance in the first quarter of fiscal 2019. See Note 1 to the Consolidated Financial Statements for a further discussion on the Company's revenue recognition policy under ASC 606 and the impact to the Company's financial statements.

In January 2016, the FASB issued ASU 2016-01 on the topic of financial instruments. The amendments in this update address certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. The standard primarily affects the accounting for equity investments, financial liabilities under the fair value option, and the presentation and disclosure requirements for financial instruments. In addition, the guidance clarifies that an entity should evaluate the need for a valuation allowance on a deferred income tax asset related to available-for-sale securities. The guidance is effective for interim and annual periods beginning after December 15, 2017. The Company adopted this guidance in the first quarter of fiscal 2019. As a result of the adoption of ASU 2016-01, the Company recognized approximately \$8 million in unrecognized losses on equity securities that had previously been recorded to other comprehensive income (loss), through a cumulative addition to deficit in the consolidated balance sheet as of March 1, 2018. The Company recognized approximately \$14 million on the change in fair value from instrument-specific credit risk that had previously been recorded to deficit, through a cumulative decrease to accumulated other comprehensive loss ("AOCI") in the consolidated balance sheet as of March 1, 2018. The Company will also account for equity investments without a readily determinable fair value using the practicability exception. The investments will be measured at cost, less any impairment, plus or minus any changes resulting from observable price changes in orderly transactions for an identical or similar investment of the same issuer.

In November 2016, the FASB issued ASU 2016-18 on the topic of the statement of cash flows. The amendments in this update require that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. The amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. This guidance is effective for interim and annual periods beginning after December 15, 2017. The Company adopted this guidance in the first quarter of fiscal 2019.

Recently Issued Accounting Pronouncements

In February 2016, the FASB issued a new accounting standard on the topic of leases. The new standard requires companies to include lease obligations in their balance sheets, including a dual approach for lessee accounting under which a lessee would account for leases as finance leases or operating leases. Both finance leases and operating leases will result in the lessee recognizing a right-of-use ("ROU") asset and a corresponding lease liability. For finance leases, the lessee will recognize interest expense and amortization of the ROU asset, and for operating leases, the lessee will recognize a straight-line total lease expense. The guidance is effective for interim and annual periods beginning after December 15, 2018. Early adoption is permitted. The Company expects to adopt this guidance in the first quarter of fiscal 2020 and is currently evaluating the impact that the adoption will have on its results of operations, financial position and disclosures. The Company established a cross-functional coordinated team to conduct the implementation of the lease standard, which will be responsible for identifying and implementing the appropriate changes to the Company's relevant business processes, systems and controls to support any required accounting and disclosure changes.

Second Quarter Fiscal 2019 Summary Results of Operations

The following table sets forth certain unaudited consolidated statements of operations data for the quarter ended August 31, 2018 compared to the quarter ended August 31, 2017 under U.S. GAAP.

	For the Three Months Ended				
	<i>(in millions, except for share and per share amounts)</i>				
	August 31, 2018		August 31, 2017		Change
Revenue ⁽¹⁾⁽²⁾	\$ 210	100.0%	\$ 238	100.0%	\$ (28)
Gross margin ⁽¹⁾⁽²⁾	161	76.7%	175	73.5%	(14)
Operating expenses ⁽¹⁾⁽²⁾	122	58.1%	153	64.3%	(31)
Income before income taxes	44	21.0%	23	9.7%	21
Provision for income taxes	1	0.5%	4	1.7%	(3)
Net income	<u>\$ 43</u>	<u>20.5%</u>	<u>\$ 19</u>	<u>8.0%</u>	<u>\$ 24</u>
Earnings (loss) per share - reported					
Basic	<u>\$ 0.08</u>		<u>\$ 0.04</u>		<u>\$ 0.04</u>
Diluted ⁽³⁾⁽⁴⁾	<u>\$ (0.04)</u>		<u>\$ (0.08)</u>		<u>\$ 0.04</u>
Weighted-average number of shares outstanding (000s)					
Basic	537,299		531,381		
Diluted ⁽³⁾⁽⁴⁾	597,799		591,881		

- (1) See "Non-GAAP Financial Measures" for the impact of the Q2 Fiscal 2019 Non-GAAP Adjustments on adjusted revenue, adjusted gross margin and adjusted operating expenses in the second quarter of fiscal 2019.
- (2) See "Non-GAAP Financial Measures" for the impact of the Q2 Fiscal 2018 Non-GAAP Adjustments on adjusted revenue, adjusted gross margin and adjusted operating expenses in the second quarter of fiscal 2018.
- (3) Diluted loss per share on a U.S. GAAP basis for the second quarter of fiscal 2019 and fiscal 2018 does not include the dilutive effect of in-the-money options and RSUs that will be settled upon vesting by the issuance of new common shares, as it would be anti-dilutive. See Note 10 to the Consolidated Financial Statements for the Company's calculation of diluted earnings (loss) per share.
- (4) The Company's MD&A for the three and six months ended August 31, 2017, included in the calculation of diluted shares for the three months ended August 31, 2017 the effect of in-the-money options and RSUs which, if included after accounting for the dilutive effect of the convertible debentures using the if-converted method instead of before, is antidilutive. The Company previously calculated a weighted average of 606,645 thousand diluted shares and a diluted loss per share of \$0.07 for three months ended August 31, 2017, a difference of 14,764 thousand shares and approximately \$0.01 loss per share from the above.

Financial Highlights

The Company had approximately \$2.35 billion in cash, cash equivalents and investments as of August 31, 2018.

In the second quarter of fiscal 2019, the Company recognized revenue of \$210 million and net income of \$43 million, or \$0.08 basic earnings per share on a U.S. GAAP basis. The Company incurred a diluted loss per share of \$0.04 on a U.S. GAAP basis. The Company recognized adjusted revenue of \$214 million and adjusted net income of \$21 million, or adjusted earnings of \$0.04 per share, on a non-GAAP basis. See also "Non-GAAP Financial Measures".

Free Cash Flow

Free cash flow is a measure of liquidity calculated as operating cash flow minus capital expenditures. Free cash flow does not have any standardized meaning as prescribed by U.S. GAAP and therefore may not be comparable to similar measures presented by other companies. For the three months ended August 31, 2018, the Company's net cash provided by operating activities was \$31 million and capital expenditures were \$4 million, resulting in the Company reporting free cash flow of \$27 million. Before taking into account the costs related to restructuring and the impact of legal proceedings, free cash flow was \$37 million.

The Company anticipates generating positive free cash flow for fiscal 2019 before taking into account the costs related to restructuring and the impact of legal proceedings.

Debentures Fair Value Adjustment

As previously disclosed, the Company elected the fair value option to account for the 3.75% unsecured convertible debentures (the "Debentures"); therefore, periodic revaluation has been and continues to be required under U.S. GAAP. The fair value adjustment does not impact the terms of the Debentures such as the face value, the redemption features or the conversion price.

In the second quarter of fiscal 2019, the change in the fair value of the Debentures was approximately \$71 million. For the three months ended August 31, 2018, the Company recorded non-cash income relating to changes in fair value from instrument-specific credit risk of \$1 million in AOCI and non-cash income relating to changes in fair value from non-credit components of \$70 million (pre-tax and after tax) (the "Q2 Fiscal 2019 Debentures Fair Value Adjustment") in the Company's consolidated statements of operations. For the six months ended August 31, 2018, the Company recorded non-cash income relating to changes in fair value from instrument-specific credit risk of \$1 million in AOCI and non-cash income relating to changes in fair value from non-credit components of \$42 million (pre-tax and after tax) (the "Fiscal 2019 Debentures Fair Value Adjustment") in the Company's consolidated statements of operations.

Restructuring Charges

During the first quarter of fiscal 2016, the Company commenced the RAP with the objectives of (i) reallocating resources to capitalize on growth opportunities, (ii) providing the operational ability to better leverage contract research and development services relating to its handheld devices, and (iii) reaching sustainable profitability. Other charges and cash costs may occur as programs are implemented or changes are completed. During the three and six months ended August 31, 2018, the Company incurred approximately \$4 million and \$8 million, respectively, in total pre-tax charges related to this program. During the three and six months ended August 31, 2018, the Company recovered approximately \$1 million, in total pre-tax recoveries related to the CORE program.

Results of Operations - Three months ended August 31, 2018 compared to three months ended August 31, 2017

Consolidated Revenue

Consolidated revenue decreased by \$28 million to approximately \$210 million in the second quarter of fiscal 2019 from \$238 million in the second quarter of fiscal 2018. The decrease was primarily due to a decrease of \$25 million in SAF revenue to \$12 million from \$37 million, a decrease of \$11 million in handheld devices revenue to \$5 million from \$16 million and a \$3 million decrease in Enterprise software and services revenue to \$88 million from \$91 million, partially offset by an increase of \$11 million in BTS revenue to \$49 million from \$38 million. See "Results of Operations - Three months ended August 31, 2018 compared to three months ended August 31, 2017 - Revenue - Revenue by Product and Service" below.

The \$25 million decrease in SAF, which is generated from users of BlackBerry 7 and prior BlackBerry operating systems, is primarily attributable to a lower number of BlackBerry 7 users, lower revenue from those users and a continued shift in the mix of the Company's customers from higher-tiered unlimited plans to prepaid and lower-tiered plans, compared to the second quarter of fiscal 2018.

The decrease in handheld devices revenue of \$11 million was primarily attributable to the Company's transition from an outsourced handset manufacturing model to the development and licensing of the Company's secure device software and the outsourcing to partners of all design, manufacturing, sales and customer support for BlackBerry-branded handsets. As a result, the Company's handheld device revenue over the period of transition has consisted solely of sales of the Company's owned handheld inventory, which is not being replenished as handheld devices are no longer produced by or on behalf of the Company, followed solely by the release of previously accrued amounts when the Company determines it has no further performance obligations.

The decrease in Enterprise software and services revenue of \$3 million was due to a reduction in revenue recognized on perpetual licenses as a result of the adoption of ASC 606.

The increase in BTS revenue of \$11 million was primarily due to increased revenue from infotainment products and royalty revenue, increased revenue from the Company's agreement with Qualcomm Technologies Inc. ("Qualcomm") to optimize select Qualcomm hardware platforms with BlackBerry QNX software, beginning in the third quarter of fiscal 2018, and increased development seats revenue.

Total software and services revenue, excluding IP and professional services, was approximately 81% recurring (subscription based) in the second quarter of fiscal 2019. The Company expects that in fiscal 2019, between 80% and 85% of software and services revenue, excluding IP and professional services, will be recurring. In the first quarter of fiscal 2019, the Company stated that it expected between 85% and 89% of software and services revenue, excluding IP and professional services, to be recurring in fiscal 2019. The Company's expectation has been revised given an increase in the proportionate

share of software products in respect of which the Company fulfilled the performance obligation and could recognize all of the associated revenue upfront. The Company generates recurring Licensing, IP and other revenue of between \$40 million and \$45 million per quarter.

The Company expects year-over-year total software and services revenue growth of between 8% and 10% in fiscal 2019, with the growth weighted to the fourth quarter of fiscal 2019. Total software and services includes Enterprise software and services, BTS, and Licensing, IP and other.

The Company expects Enterprise software and services revenue to grow sequentially in the third and fourth quarters of fiscal 2019, and to be lower in fiscal 2019 compared to fiscal 2018 due to the implementation of ASC 606 on March 1, 2018 by high single digit to low double-digits on a percentage basis.

The Company expects BTS revenue to grow between 20% and 25% in fiscal 2019. The Company expects IP revenue of between \$120 million and \$140 million in fiscal 2019. The Company expects to generate \$100 million in cumulative revenue from its BlackBerry Radar asset tracking solution over the next three years.

The Company expects double-digit year-over-year total software and services billings growth in fiscal 2019, due to growth in BTS and Licensing, IP and other billings. The Company expects Enterprise software and services billings to grow sequentially in the third and fourth quarters of fiscal 2019, and to be relatively flat in fiscal 2019 compared to fiscal 2018.

Consolidated Gross Margin

Consolidated gross margin decreased by \$14 million to approximately \$161 million, or 76.7% of consolidated revenue in the second quarter of fiscal 2019 from \$175 million, or 73.5% of consolidated revenue in the second quarter of fiscal 2018. The decrease was primarily due to a decrease in gross margin associated with SAF and Enterprise software and services offset by an increase in gross margin associated with BTS.

The decrease in gross margin associated with SAF is primarily due to the decline in SAF revenue discussed above in "Consolidated Revenue", as cost of goods sold associated with SAF were consistent in the second quarter of fiscal 2019 and the second quarter of fiscal 2018 due to certain fixed costs associated with SAF infrastructure. The decrease in gross margin associated with Enterprise software and services is primarily due to the reasons discussed above in "Consolidated Revenue". The increase in gross margin associated with BTS is primarily due to the reasons discussed above in "Consolidated Revenue".

Revenue

Revenue by Geography

Comparative breakdowns of the geographic regions on a U.S. GAAP basis are set forth in the following table:

	For the Three Months Ended (in millions)					
	August 31, 2018		August 31, 2017		Change	
Revenue by Geography						
North America	\$ 133	63.3%	\$ 133	55.9%	\$ —	— %
Europe, Middle East and Africa	53	25.3%	76	31.9%	(23)	(30.3)%
Other regions	24	11.4%	29	12.2%	(5)	(17.2)%
	<u>\$ 210</u>	<u>100.0%</u>	<u>\$ 238</u>	<u>100.0%</u>	<u>\$ (28)</u>	<u>(11.8)%</u>

North America Revenue

Revenue in North America was unchanged at \$133 million, or 63.3% of revenue, in the second quarter of fiscal 2019, compared to \$133 million, or 55.9% of revenue, in the second quarter of fiscal 2018. An increase in BTS revenue due to the reasons discussed above in "Consolidated Revenue", was offset by decreases in SAF revenue, Enterprise software and services revenue and handheld device revenue due to the reasons discussed above in "Consolidated Revenue".

Europe, Middle East and Africa Revenue

Revenue in Europe, Middle East and Africa was \$53 million or 25.3% of revenue in the second quarter of fiscal 2019, reflecting a decrease of \$23 million compared to \$76 million or 31.9% of revenue in the second quarter of fiscal 2018. The decrease in revenue is primarily due to a decreases in SAF revenue and handheld device revenue due to the reasons discussed above in "Consolidated Revenue", partially offset by an increase in BTS revenue due to an increase in sales of development seats.

Other Region Revenue

Revenue in other regions was \$24 million or 11.4% of revenue in the second quarter of fiscal 2019, reflecting a decrease of \$5 million compared to \$29 million or 12.2% of revenue in the second quarter of fiscal 2018. The decrease in revenue is due to a decrease in SAF revenue due to the reasons discussed above in "Consolidated Revenue", partially offset by an increase in BTS revenue due to an increase in sales of development seats.

Revenue by Product and Service

Comparative breakdowns of revenue by product and service on a non-GAAP basis are set forth below.

	For the Three Months Ended (in millions)					
	August 31, 2018		August 31, 2017		Change	
Revenue by Product and Service						
Enterprise software and services ⁽¹⁾	\$ 92	43.0%	\$ 102	41.0%	\$ (10)	(9.8)%
BTS	49	22.9%	38	15.3%	11	28.9 %
Licensing, IP and other	56	26.2%	56	22.5%	—	— %
Handheld devices	5	2.3%	16	6.4%	(11)	(68.8)%
SAF	12	5.6%	37	14.8%	(25)	(67.6)%
	<u>\$ 214</u>	<u>100.0%</u>	<u>\$ 249</u>	<u>100.0%</u>	<u>\$ (35)</u>	<u>(14.1)%</u>

(1) See "Non-GAAP Financial Measures" for the relevant Q2 Fiscal 2019 Non-GAAP Adjustments and Q2 Fiscal 2018 Non-GAAP Adjustments made to Enterprise software and services revenue.

Enterprise Software and Services

Enterprise software and services revenue includes revenue from the Company's security, productivity, collaboration and end-point management solutions through the BlackBerry Secure platform, which includes BlackBerry UEM, BlackBerry Dynamics, BlackBerry Workspaces and BBM Enterprise, as well as revenue from the sale of the Company's AtHoc Alert secure networked crisis communications solution, its Secusmart SecuSUITE secure voice and text solution, and professional services from BlackBerry Cybersecurity Services.

Enterprise software and services non-GAAP revenue was \$92 million, or 43.0% of revenue, in the second quarter of fiscal 2019, a decrease of \$10 million compared to revenue of \$102 million, or 41.0% of revenue, in the second quarter of fiscal 2018. Enterprise software and services non-GAAP revenue decreased due to the reasons described above in "Consolidated Revenue" and due to a decrease of \$7 million in the non-GAAP adjustment of deferred software revenue acquired to \$4 million in the second quarter of fiscal 2019 from \$11 million in the second quarter of fiscal 2018.

Excluding the deferred software revenue acquired adjustment described under "Non-GAAP Financial Measures", Enterprise software and services U.S. GAAP revenue was \$88 million, or 41.9% of revenue, in the second quarter of fiscal 2019, compared to \$91 million, or 38.2% of revenue, in the second quarter of fiscal 2018, representing a decrease of \$3 million, or 3.3%, due to the reasons described above in "Consolidated Revenue".

BTS

BTS includes revenue from the Company's QNX CAR Platform and Neutrino Operating System, as well as revenue from the Company's BlackBerry Radar asset tracking solution, Paratek antenna tuning technology, and Certicom cryptography and key management products.

BTS revenue was \$49 million, or 22.9% of revenue, in the second quarter of fiscal 2019, an increase of \$11 million compared to \$38 million, or 15.3% of revenue, in the second quarter of fiscal 2018. BTS revenue increased due to the reasons described above in "Consolidated Revenue".

Licensing, IP and Other

Licensing, IP and other revenue includes revenue from the Company's mobility licensing software arrangements, including revenue from licensed hardware sales, the Company's Intellectual Property and Licensing business, and from its BBM Consumer licensing arrangement.

Licensing, IP and other revenue were \$56 million, or 26.2% of revenue, in the second quarter of fiscal 2019, consistent with the \$56 million, or 22.5% of revenue from the second quarter of fiscal 2018.

Handheld Devices

Handheld devices includes revenue from the sale of the Company's remaining inventory of legacy smartphones and smartphone accessories, as well as non-warranty repair services. Handheld device revenue was \$5 million, or 2.3% of revenue, in the second quarter of fiscal 2019, compared to \$16 million, or 6.4% of revenue, in the second quarter of fiscal 2018, representing a decrease of \$11 million, or 68.8%. The \$11 million decrease in handheld devices revenue was primarily due to the reasons discussed above in "Consolidated Revenue".

Service Access Fees

SAF revenue decreased by \$25 million, or 67.6%, to \$12 million, or 5.6% of revenue, in the second quarter of fiscal 2019, compared to \$37 million, or 14.8% of revenue, in the second quarter of fiscal 2018. The decrease was due to the reasons discussed above in "Consolidated Revenue".

Operating Expenses

The table below presents a comparison of research and development, selling, marketing and administration, and amortization expense for the quarter ended August 31, 2018, compared to the quarter ended May 31, 2018 and the quarter ended August 31, 2017. The Company believes it is also meaningful to provide a comparison between the second quarter of fiscal 2019 and the first quarter of fiscal 2019.

	For the Three Months Ended (in millions)					
	August 31, 2018		May 31, 2018		August 31, 2017	
	\$	% of Revenue	\$	% of Revenue	\$	% of Revenue
Revenue	\$ 210		\$ 213		\$ 238	
Operating expenses						
Research and development ⁽¹⁾⁽²⁾⁽³⁾	\$ 51	24.3 %	\$ 61	28.6%	\$ 60	25.2 %
Selling, marketing and administration ⁽¹⁾⁽²⁾⁽³⁾	106	50.5 %	100	46.9%	113	47.5 %
Amortization ⁽¹⁾⁽²⁾⁽³⁾	35	16.7 %	37	17.4%	39	16.4 %
Impairment of long-lived assets ⁽²⁾	—	— %	—	—%	11	4.6 %
Debentures fair value adjustment ⁽¹⁾⁽²⁾⁽³⁾	(70)	(33.3)%	28	13.1%	(70)	(29.4)%
Total	<u>\$ 122</u>	<u>58.1 %</u>	<u>\$ 226</u>	<u>106.0%</u>	<u>\$ 153</u>	<u>64.3 %</u>

- (1) See "Non-GAAP Financial Measures" for the impact of the Q2 Fiscal 2019 Non-GAAP Adjustments on adjusted operating expenditures in the second quarter of fiscal 2019.
- (2) See "Non-GAAP Financial Measures" for the impact of the Q2 Fiscal 2018 Non-GAAP Adjustments on adjusted operating expenditures in the second quarter of fiscal 2018.
- (3) In the first quarter of fiscal 2019, the Company recognized non-cash charge associated with a change in the fair value of the Debentures of approximately \$28 million (the "Q1 Fiscal 2019 Debentures Fair Value Adjustment"), RAP charges of approximately \$2 million and \$2 million in research and development and selling, marketing and administration expenses, respectively, stock compensation expense of \$3 million and \$14 million in research and development and selling, marketing and administration expenses, respectively, acquired intangibles amortization of \$22 million and \$1 million in business acquisition and integration costs in selling, marketing and administration expenses (collectively the "Q1 Fiscal 2019 Non-GAAP Adjustments").

Operating expenses decreased by \$104 million, or 46.0%, to \$122 million, or 58.1% of revenue, in the second quarter of fiscal 2019, compared to \$226 million, or 106.0% of revenue, in the first quarter of fiscal 2019. The decrease was primarily attributable the difference between the Q2 Fiscal 2019 Debentures Fair Value Adjustment and Q1 Fiscal 2019 Debentures Fair Value Adjustment, a decrease in salaries and benefits, a decrease in restructuring charges, and a lower amortization expense.

After giving effect to the relevant Q2 Fiscal 2019 Non-GAAP Adjustments and Q1 Fiscal 2019 Non-GAAP Adjustments, non-GAAP operating expenses decreased by \$4 million. The decrease was primarily attributable to a decrease in salaries and benefits and a lower amortization expense, partially offset by an increase in legal expenditures and unfavourable foreign currency translation.

Operating expenses decreased by \$31 million, or 20.3%, to \$122 million or 58.1% of revenue in the second quarter of fiscal 2019, compared to approximately \$153 million or 64.3% of revenue in the second quarter of fiscal 2018. The decrease was primarily attributable to a decrease in restructuring charges, the Fiscal 2018 LLA Impairment Charge that did not recur in the second quarter of fiscal 2019, and a lower amortization expense, partially offset by unfavourable foreign currency translation.

After giving effect to the relevant Q2 Fiscal 2019 Non-GAAP Adjustments and Q2 Fiscal 2018 Non-GAAP Adjustments, non-GAAP operating expenses decreased by \$11 million. The decrease was primarily attributable to a reduction in salaries and benefits, a decrease in professional fees and a reduction in outsourcing costs.

Research and Development Expenses

Research and development expenses consist primarily of salaries and benefits for technical personnel, new product development costs, travel expenses, office and building costs, infrastructure costs and other employee costs.

Research and development decreased by \$9 million, or 15.0%, to \$51 million in the second quarter of fiscal 2019 compared to \$60 million in the second quarter of fiscal 2018. After giving effect to the relevant Q2 Fiscal 2019 Non-GAAP Adjustments and Q2 Fiscal 2018 Non-GAAP Adjustments, non-GAAP research and development expenses decreased by \$8 million. The decrease was primarily attributable to a decrease in salaries and benefits, and a decrease in outsourcing costs.

Selling, Marketing and Administration Expenses

Selling, marketing and administration expenses consist primarily of marketing, advertising and promotion, salaries and benefits, external advisory fees, information technology costs, office and related staffing infrastructure costs and travel expenses.

Selling, marketing and administration expenses decreased by \$7 million, or 6.2%, to \$106 million in the second quarter of fiscal 2019 compared to \$113 million in the second quarter of fiscal 2018. After giving effect to the relevant Q2 Fiscal 2019 Non-GAAP Adjustments and Q2 Fiscal 2018 Non-GAAP Adjustments, non-GAAP selling, marketing and administration expenses decreased by \$1 million. The decrease was primarily attributable to decreases in professional fees, facilities costs, and salaries and benefits, partially offset by unfavourable foreign currency translation.

Amortization Expense

The table below presents a comparison of amortization expense relating to property, plant and equipment and intangible assets recorded as amortization or cost of sales for the second quarter of fiscal 2019 compared to the second quarter of fiscal 2018. Intangible assets are comprised of patents, licenses and acquired technology.

	For the Three Months Ended (in millions)					
	Included in Amortization			Included in Cost of Sales		
	August 31, 2018	August 31, 2017	Change	August 31, 2018	August 31, 2017	Change
Property, plant and equipment	\$ 3	\$ 5	\$ (2)	\$ 1	\$ 4	\$ (3)
Intangible assets	32	34	(2)	2	2	—
Total	\$ 35	\$ 39	\$ (4)	\$ 3	\$ 6	\$ (3)

Amortization

Amortization expense relating to certain property, plant and equipment and intangible assets decreased by \$4 million to \$35 million for the second quarter of fiscal 2019, compared to \$39 million for the second quarter of fiscal 2018. The decrease in amortization expense reflects the full depreciation of certain assets.

After giving effect to the relevant Q2 Fiscal 2019 Non-GAAP Adjustments and Q2 Fiscal 2018 Non-GAAP Adjustments, non-GAAP amortization expense decreased by \$2 million.

Cost of Sales

Amortization expense relating to certain property, plant and equipment and intangible assets employed in the Company's service operations decreased by \$3 million to \$3 million for the second quarter of fiscal 2019, compared to \$6 million for the second quarter of fiscal 2018. The decrease primarily reflects the full depreciation of assets, partially offset by a portion of the amortization of patents being classified as cost of goods sold due to the Company's intellectual property licensing arrangements.

Investment Income

Investment income, which includes the interest expense from the Debentures, increased by \$4 million to \$5 million in investment income in the second quarter of fiscal 2019, compared to investment income of \$1 million in the second quarter of fiscal 2018. The increased investment income was due to a higher yield on the Company's average cash and investment balances.

Income Taxes

For the second quarter of fiscal 2019, the Company's net effective income tax expense rate was approximately 2%, compared to a net effective income tax expense rate of approximately 17% for the same period in the prior fiscal year. The Company's net effective income tax rate reflects the impact of the United States enacted tax reform legislation through the Tax Cuts and Jobs Act and the fact that the Company has a significant valuation allowance against its deferred tax assets, and in particular, the change in fair value of the Debentures, amongst other items, was offset by a corresponding adjustment of the valuation allowance. The Company's net effective income tax rate also reflects the geographic mix of earnings in jurisdictions with different income tax rates.

Net Income

The Company's net income for the second quarter of fiscal 2019 was \$43 million, reflecting an increase in net income of \$24 million, compared to net income of \$19 million in the second quarter of fiscal 2018, primarily due to the absence of the LLA Impairment Charge and a decrease in operating expenses, as described above in "Operating Expenses". After giving effect to the relevant Q2 Fiscal 2019 Non-GAAP Adjustments and Q2 Fiscal 2018 Non-GAAP Adjustments, the Company's non-GAAP net income was \$21 million for the second quarter of fiscal 2019 compared to non-GAAP net income of \$26 million for the second quarter of fiscal 2018, reflecting a decrease in non-GAAP net income of \$5 million primarily due to a decrease in gross margin, as described above in "Consolidated Gross Margin", partially offset by a decrease in operating expenses as described above in "Operating Expenses".

For the second quarter of fiscal 2019, basic earnings and diluted loss per share were \$0.08 and \$0.04, respectively, compared to basic earnings and diluted loss per share of \$0.04 and \$0.08, respectively for the same period in the prior fiscal year. After giving effect to the relevant Q2 Fiscal 2019 Non-GAAP Adjustments and Q2 Fiscal 2018 Non-GAAP Adjustments, the Company's non-GAAP basic earnings per share was \$0.04 for the second quarter of fiscal 2019 compared to non-GAAP basic earnings per share of \$0.05 for the second quarter of fiscal 2018.

The weighted average number of shares outstanding was approximately 537 million common shares for basic earnings per share and 598 million common shares for diluted loss per share for the three months ended August 31, 2018, and approximately 531 million common shares for basic earnings per share and 592 million common shares for diluted loss per share for the three months ended August 31, 2017.

Common Shares Outstanding

On September 25, 2018, there were 538 million common shares, options to purchase 1 million common shares, 24 million restricted share units and 0.7 million deferred share units outstanding. In addition, 60.5 million common shares are issuable upon conversion in full of the Debentures as described in Note 8 to the Consolidated Financial Statements.

The Company has not paid any cash dividends during the last three fiscal years.

Results of Operations - Six months ended August 31, 2018 compared to six months ended August 31, 2017

The following table sets forth certain unaudited consolidated statements of operations data as at August 31, 2018 and August 31, 2017 under U.S. GAAP.

	For the Six Months Ended				
	<i>(in millions, except for share and per share amounts)</i>				
	August 31, 2018		August 31, 2017		Change
Revenue ⁽¹⁾⁽²⁾	\$ 423	100.0%	\$ 473	100.0%	\$ (50)
Gross margin ⁽¹⁾⁽²⁾	322	76.1%	325	68.7%	(3)
Operating expenses ⁽¹⁾⁽²⁾	348	82.3%	(233)	(49.3%)	581
Income (loss) before income taxes ⁽²⁾	(15)	(3.5%)	695	146.9%	(710)
Provision for income taxes	2	0.5%	5	1.1%	(3)
Net income (loss)	<u>\$ (17)</u>	<u>(4.0%)</u>	<u>\$ 690</u>	<u>146.0%</u>	<u>\$ (707)</u>
Earnings (loss) per share - reported					
Basic	<u>\$ (0.03)</u>		<u>\$ 1.30</u>		<u>\$ (1.33)</u>
Diluted	<u>\$ (0.08)</u>		<u>\$ 1.26</u>		<u>\$ (1.34)</u>
Weighted-average number of shares outstanding (000s)					
Basic	537,136		531,234		
Diluted	597,636		546,132		

(1) See "Non-GAAP Financial Measures" for the impact of the Fiscal 2019 Non-GAAP Adjustments on adjusted revenue, adjusted gross margin and adjusted operating expenses in fiscal 2019.

(2) See "Non-GAAP Financial Measures" for the impact of the Fiscal 2018 Non-GAAP Adjustments on adjusted revenue, adjusted gross margin, adjusted operating expenses and adjusted income (loss) before income taxes in fiscal 2018.

Consolidated Revenue

Consolidated revenue decreased by \$50 million to approximately \$423 million in the first six months of fiscal 2019 from \$473 million in the first six months of fiscal 2018. The decrease was primarily due to a decrease of \$47 million in SAF revenue to \$28 million from \$75 million, a decrease of \$40 million in handheld devices revenue to \$13 million from \$53 million and a decrease of \$16 million in Enterprise software and services to \$167 million from \$183 million, offset by an increase of \$31 million in Licensing, IP and other revenue to \$119 million from \$88 million and an increase of \$22 million in BTS revenue to \$96 million from \$74 million.

The \$47 million decrease in SAF revenue, which is generated from users of BlackBerry 7 and prior BlackBerry operating systems, is primarily attributable to a lower number of BlackBerry 7 users, lower revenue from those users and a continued shift in the mix of the Company's customers from higher-tiered unlimited plans to prepaid and lower-tiered plans, compared to the first six months of fiscal 2018.

The decrease in handheld devices revenue of \$40 million was primarily attributable to the Company's transition from an outsourced handset manufacturing model to the development and licensing of the Company's secure device software and the outsourcing to partners of all design, manufacturing, sales and customer support for BlackBerry-branded handsets. As a result, the Company's handheld device revenue over the period of transition has consisted solely of sales of the Company's owned handheld inventory, which is not being replenished as handheld devices are no longer produced by or on behalf of the Company, followed solely by the release of previously accrued amounts when the Company determines it has no further performance obligations.

The decrease in Enterprise software and services revenue of \$16 million was due to a lower number of perpetual licenses sold and a reduction in revenue recognized on perpetual licenses as a result of the adoption of ASC 606.

The increase in Licensing, IP and other revenue of \$31 million was primarily due to higher IP revenue as a result of the Company's patent licensing agreement with Telety that allows it to sublicense a broad range of the Company's patents to a majority of global smartphone manufacturers, beginning in the third quarter of fiscal 2018 and an IP settlement.

The increase in BTS revenue of \$22 million was primarily due to the Company's agreement with Qualcomm Technologies Inc. ("Qualcomm") to optimize select Qualcomm hardware platforms with BlackBerry QNX software, beginning in the third quarter of fiscal 2018, and increased revenue from infotainment products, royalty revenue and services offerings.

Consolidated Gross Margin

Consolidated gross margin decreased by \$3 million to approximately \$322 million in the first six months of fiscal 2019 from \$325 million in the first six months of fiscal 2018. The decrease was primarily due to the decrease in gross margin associated with SAF and Enterprise software and services offset by an increase in gross margin associated with Licensing, IP and other and BTS.

The decrease in gross margin associated with SAF is primarily due to the decline in SAF revenue discussed above in "Consolidated Revenue", as cost of goods sold associated with SAF were consistent in the first six months of fiscal 2019 and the first six months of fiscal 2018 due to certain fixed costs associated with SAF infrastructure. The decrease in gross margin associated with Enterprise software and services is primarily due to the reasons discussed above in "Consolidated Revenue". The increase in gross margin associated with Licensing, IP and other and BTS is primarily due to the reasons discussed above in "Consolidated Revenue".

Revenue

Revenue by Product and Service

Comparative breakdowns of revenue by product and service on a non-GAAP basis are set forth below.

	For the Six Months Ended							
	(in millions)							
	August 31, 2018		August 31, 2017		Change			
Revenue by Product and Service								
Enterprise software and services ⁽¹⁾⁽²⁾	\$	175	40.6%	\$	203	41.2%	\$ (28)	(13.8)%
BTS		96	22.3%		74	15.0%	22	29.7 %
Licensing, IP and other		119	27.6%		88	17.8%	31	35.2 %
Handheld devices		13	3.0%		53	10.8%	(40)	(75.5)%
SAF		28	6.5%		75	15.2%	(47)	(62.7)%
	<u>\$</u>	<u>431</u>	<u>100.0%</u>	<u>\$</u>	<u>493</u>	<u>100.0%</u>	<u>\$ (62)</u>	<u>(12.6)%</u>

(1) See "Non-GAAP Financial Measures" for the relevant Fiscal 2019 Non-GAAP Adjustments made to Enterprise software and services revenue.

(2) See "Non-GAAP Financial Measures" for the relevant Fiscal 2018 Non-GAAP Adjustments made to Enterprise software and services revenue.

Enterprise Software and Services

Enterprise software and services non-GAAP revenue decreased by \$28 million, or 13.8%, to \$175 million, or 40.6% of revenue, in the first six months of fiscal 2019, compared to \$203 million, or 41.2% of revenue, in the first six months of fiscal 2018. The \$28 million decrease in Enterprise software and services non-GAAP revenue was primarily due to the reasons described above in "Consolidated Revenue" and also due to a decrease of \$12 million in the non-GAAP adjustment of deferred software revenue acquired to \$8 million in the first six months of fiscal 2019 versus \$20 million in the first six months of fiscal 2018.

Excluding the deferred software revenue acquired adjustment, Enterprise software and services U.S. GAAP revenue was \$167 million, or 39.5% of revenue in the first six months of fiscal 2019, compared to \$183 million, or 38.7% of revenue, in the first six months of fiscal 2018, representing a decrease of \$16 million, or 8.7%.

BTS

BTS revenue increased by \$22 million, or 29.7%, to \$96 million, or 22.3% of revenue, in the first six months of fiscal 2019, compared to \$74 million, or 15.0% of revenue, in the first six months of fiscal 2018. BTS revenue increased due to the reasons described above in "Consolidated Revenue"

Licensing, IP and Other

Licensing, IP and other revenue increased by \$31 million, or 35.2%, to \$119 million, or 27.6% of revenue in the first six months of fiscal 2019, compared to \$88 million, or 17.8% of revenue, in the first six months of fiscal 2018. The \$31 million increase was primarily due to the reasons described above in "Consolidated Revenue"

Handheld Devices

Handheld devices revenue was \$13 million, or 3.0% of revenue, in the first six months of fiscal 2019 compared to \$53 million, or 10.8% of revenue, in the first six months of fiscal 2018, representing a decrease of \$40 million, or 75.5%. The \$40 million decrease in handheld devices revenue was primarily due to the reasons discussed above in "Consolidated Revenue".

Service Access Fees

SAF revenue decreased by \$47 million, or 62.7%, to \$28 million, or 6.5% of revenue, in the first six months of fiscal 2019, compared to \$75 million, or 15.2% of revenue, in the first six months of fiscal 2018.

The decrease in SAF revenue is primarily due to the reasons discussed above in "Consolidated Revenue".

Operating Expenses

The table below presents a comparison of research and development, selling, marketing and administration, and amortization expenses for the six months ended August 31, 2018, compared to the six months ended August 31, 2017.

	For the Six Months Ended (in millions)					
	August 31, 2018		August 31, 2017		Change	
	\$	% of Revenue	\$	% of Revenue	\$	% of Change
Revenue	\$ 423		\$ 473		\$ (50)	(10.6)%
Operating expenses						
Research and development ⁽¹⁾⁽²⁾	\$ 112	26.5 %	\$ 121	25.6 %	\$ (9)	(7.4)%
Selling, marketing and administration ⁽¹⁾⁽²⁾	206	48.7 %	223	47.1 %	(17)	(7.6)%
Amortization ⁽¹⁾⁽²⁾	72	17.0 %	79	16.7 %	(7)	(8.9)%
Impairment of long-lived assets ⁽²⁾	—	— %	11	2.3 %	(11)	(100.0)%
Debentures fair value adjustment ⁽¹⁾⁽²⁾	(42)	(9.9)%	148	31.3 %	(190)	(128.4)%
Qualcomm arbitration award ⁽²⁾	—	— %	(815)	(172.3)%	815	(100.0)%
Total	<u>\$ 348</u>	<u>82.3 %</u>	<u>\$ (233)</u>	<u>(49.3)%</u>	<u>\$ 581</u>	<u>(249.4)%</u>

(1) See "Non-GAAP Financial Measures" for the impact of the Fiscal 2019 Non-GAAP Adjustments on adjusted operating expenditures in fiscal 2019.

(2) See "Non-GAAP Financial Measures" for the impact of the Fiscal 2018 Non-GAAP Adjustments on adjusted operating expenditures in fiscal 2018.

Operating expenses increased by \$581 million, or 249.4%, to \$348 million or 82.3% of revenue in the first six months of fiscal 2019, compared to approximately \$(233) million or (49.3)% of revenue in the first six months of fiscal 2018. The increase was primarily attributable to the Qualcomm arbitration award in the first quarter of fiscal 2018, unfavourable foreign currency translation, and an increase in stock-based compensation, partially offset by the difference between the Fiscal 2019 Debentures Fair Value Adjustment and the Fiscal 2018 Debentures Fair Value Adjustment, and the Fiscal 2018 LLA Impairment Charge.

After giving effect to the relevant Fiscal 2019 Non-GAAP Adjustments and Fiscal 2018 Non-GAAP Adjustments, non-GAAP operating expenses decreased by \$6 million due to the reasons discussed below in "Research and Development Expenses", "Selling, Marketing and Administrative Expenses" and "Amortization Expense".

Research and Development Expenses

Research and development expenses decreased by \$9 million to \$112 million, or 26.5% of revenue, in the first six months of fiscal 2019, compared to \$121 million, or 25.6% of revenue, in the first six months of fiscal 2018. After giving effect to the relevant Fiscal 2019 Non-GAAP Adjustments and Fiscal 2018 Non-GAAP Adjustments, non-GAAP research and development expenses decreased by \$6 million. The decrease is primarily attributable to a decrease in salaries and benefits and a reduction in outsourcing costs compared to the first six months of fiscal 2018.

Selling, Marketing and Administration Expenses

Selling, marketing and administration expenses decreased by \$17 million to \$206 million, or 48.7% of revenue, in the first six months of fiscal 2019, compared to approximately \$223 million, or 47.1% of revenue, in the first six months of fiscal 2018. After giving effect to the relevant Fiscal 2019 Non-GAAP Adjustments and Fiscal 2018 Non-GAAP Adjustments, non-GAAP

BlackBerry Limited
Management's Discussion and Analysis of Financial Condition and Results of Operations

selling marketing and administration expenses increased by \$2 million. The increase is primarily attributable to unfavourable foreign currency translation and an increase in legal costs, partially offset by a decrease in salaries and benefits compared to the first six months of fiscal 2018.

Amortization Expense

The table below presents a comparison of amortization expense relating to property, plant and equipment and intangible assets recorded as amortization or cost of sales for the six months ended August 31, 2018 compared to the six months ended August 31, 2017. Intangible assets are comprised of patents, licenses and acquired technology.

	For the Six Months Ended (in millions)					
	Included in Amortization			Included in Cost of sales		
	August 31, 2018	August 31, 2017	Change	August 31, 2018	August 31, 2017	Change
Property, plant and equipment	\$ 6	\$ 10	\$ (4)	\$ 3	\$ 11	\$ (8)
Intangible assets	66	69	(3)	4	6	(2)
Total	\$ 72	\$ 79	\$ (7)	\$ 7	\$ 17	\$ (10)

Amortization

Amortization expense relating to certain property, plant and equipment and certain intangible assets decreased by \$7 million to \$72 million in the first six months of fiscal 2019 compared to \$79 million for the comparable period in fiscal 2018. The decrease in amortization expense primarily reflects the full depreciation of certain assets.

After giving effect to the relevant Fiscal 2019 Non-GAAP Adjustments and Fiscal 2018 Non-GAAP Adjustments, non-GAAP amortization expense decreased by \$2 million.

Cost of sales

Amortization expense relating to certain property, plant and equipment and certain intangible assets employed in the Company's service operations decreased by \$10 million to \$7 million in the first six months of fiscal 2019 compared to \$17 million for the comparable period in fiscal 2018. This decrease primarily reflects the full depreciation of assets, partially offset by a portion of the amortization of patents being classified as cost of goods sold due to the Company's intellectual property licensing arrangements.

Investment Income

Investment income, which includes the interest expense from the Debentures, decreased by \$126 million to \$11 million in investment income in the first six months of fiscal 2019, from an investment income of \$137 million in the comparable period of fiscal 2018. The decrease is primarily attributable to the interest received from the Qualcomm arbitration award in the first six months of fiscal 2018.

Income Taxes

For the first six months of fiscal 2019, the Company's net effective income tax expense rate was approximately 13%, compared to a net effective income tax expense rate of approximately 1% for the same period in the prior fiscal year. The Company's net effective income tax rate reflects the fact that the Company has a significant valuation allowance against its deferred tax assets, and in particular, the impairment charges and the change in fair value of the Debentures and the impact of the Qualcomm arbitration award, amongst other items, was offset by a corresponding adjustment of the valuation allowance. The Company's net effective income tax rate also reflects the geographic mix of earnings in jurisdictions with different income tax rates.

Net Income (Loss)

The Company's net loss for the first six months of fiscal 2019 was \$17 million, reflecting a decrease in net income of \$707 million compared to net income of approximately \$690 million in the first six months of fiscal 2018, primarily due to the Qualcomm arbitration award in the first six months of fiscal 2018, offset by the difference between the Fiscal 2019 Debentures Fair Value Adjustment and Fiscal 2018 Debentures Fair Value Adjustment, the absence of the LLA Impairment Charge and a decrease in operating expenses, as described above in "Operating Expenses". After giving effect to the relevant Fiscal 2019 Non-GAAP Adjustments and Fiscal 2018 Non-GAAP Adjustments, the Company's non-GAAP net income for the first six months of fiscal 2019 was \$38 million compared to non-GAAP net income of \$36 million for the first six months of fiscal 2018, reflecting an increase in net income of \$2 million primarily due to a reduction in operating expenditures.

Basic and diluted loss per share were \$0.03 and \$0.08, respectively, in the first six months of fiscal 2019, compared to a basic and diluted earnings per share of \$1.30 and \$1.26, respectively, in the first six months of fiscal 2018, due to the reasons noted above. After giving effect to the relevant Fiscal 2019 Non-GAAP Adjustments and Fiscal 2018 Non-GAAP Adjustments, the Company's non-GAAP basic earnings per share was \$0.07 for the first six months of fiscal 2019 compared to non-GAAP basic earnings per share of \$0.07 for the first six months of fiscal 2018. The Company expects positive adjusted non-GAAP earnings per share for fiscal 2019.

The weighted average number of shares outstanding was approximately 537 million common shares for basic loss per share and 598 million for diluted loss per share for the six months ended August 31, 2018, and approximately 531 million common shares for basic earnings per share and 546 million for diluted earnings per share for the six months ended August 31, 2017.

Selected Quarterly Financial Data

The following table sets forth the Company's unaudited quarterly consolidated results of operations data for each of the eight most recent quarters, including the quarter ended August 31, 2018. The information in the table below has been derived from the Company's unaudited interim consolidated financial statements that, in management's opinion, have been prepared on a basis consistent with the audited consolidated financial statements of the Company and include all adjustments necessary for a fair presentation of information when read in conjunction with the audited consolidated financial statements of the Company. The Company's quarterly operating results have varied substantially in the past and may vary substantially in the future. Accordingly, the information below is not necessarily indicative of results for any future quarter.

	<i>(in millions, except per share data)</i>							
	Fiscal Year 2019		Fiscal Year 2018				Fiscal Year 2017	
	Second Quarter	First Quarter	Fourth Quarter	Third Quarter	Second Quarter	First Quarter	Fourth Quarter	Third Quarter
Revenue	\$ 210	\$ 213	\$ 233	\$ 226	\$ 238	\$ 235	\$ 286	\$ 289
Gross margin	161	161	177	168	175	150	172	193
Operating expenses	122	226	194	426	153	(386)	229	307
Income (loss) before income taxes	44	(59)	(14)	(275)	23	672	(49)	(118)
Provision for (recovery of) income taxes	1	1	(4)	—	4	1	(2)	(1)
Net income (loss)	<u>\$ 43</u>	<u>\$ (60)</u>	<u>\$ (10)</u>	<u>\$ (275)</u>	<u>\$ 19</u>	<u>\$ 671</u>	<u>\$ (47)</u>	<u>\$ (117)</u>
Earnings (loss) per share								
Basic earnings (loss) per share	<u>\$ 0.08</u>	<u>\$ (0.11)</u>	<u>\$ (0.02)</u>	<u>\$ (0.52)</u>	<u>\$ 0.04</u>	<u>\$ 1.26</u>	<u>\$ (0.09)</u>	<u>\$ (0.22)</u>
Diluted earnings (loss) per share	<u>\$ (0.04)</u>	<u>\$ (0.11)</u>	<u>\$ (0.06)</u>	<u>\$ (0.52)</u>	<u>\$ (0.08)</u>	<u>\$ 1.23</u>	<u>\$ (0.10)</u>	<u>\$ (0.22)</u>

Financial Condition

Liquidity and Capital Resources

Cash, cash equivalents, and investments decreased by \$1 million to approximately \$2.35 billion as at August 31, 2018 from approximately \$2.35 billion as at February 28, 2018, primarily as a result of acquisitions of intangible assets and property, plant and equipment and cash used in operations. The majority of the Company's cash, cash equivalents, and investments are denominated in U.S. dollars as at August 31, 2018.

A comparative summary of cash, cash equivalents, and investments is set out below:

	As at <i>(in millions)</i>		
	August 31, 2018	February 28, 2018	Change
Cash and cash equivalents	\$ 581	\$ 816	\$ (235)
Short-term investments	1,683	1,443	240
Restricted cash and cash equivalents	32	39	(7)
Long-term investments	56	55	1
Cash, cash equivalents, and investments	<u>\$ 2,352</u>	<u>\$ 2,353</u>	<u>\$ (1)</u>

BlackBerry Limited
Management's Discussion and Analysis of Financial Condition and Results of Operations

The table below summarizes the current assets, current liabilities, and working capital of the Company:

	As at (in millions)		
	August 31, 2018	February 28, 2018	Change
Current assets	\$ 2,528	\$ 2,545	\$ (17)
Current liabilities	393	411	(18)
Working capital	<u>\$ 2,135</u>	<u>\$ 2,134</u>	<u>\$ 1</u>

Current Assets

The decrease in current assets of \$17 million at the end of the second quarter of fiscal 2019 from the end of the fourth quarter of fiscal 2018 was primarily due to a decrease in cash and cash equivalents of \$235 million, other receivables of \$19 million and income taxes receivable \$11 million, partially offset by an increase in short-term investments of \$240 million and other current assets of \$14 million.

At August 31, 2018, accounts receivable was \$145 million, a decrease of \$6 million from February 28, 2018. The decrease reflects the lower revenue recognized over the six months ended August 31, 2018 partially offset by a decrease in days sales outstanding to 60 days at the end of the second quarter of fiscal 2019 from 61 days at the end of the fourth quarter of fiscal 2018.

At August 31, 2018, other receivables were \$52 million, a decrease of \$19 million from February 28, 2018. The decrease is due to the funds recovered from escrow relating to the Good Technology Corporation litigation.

At August 31, 2018, income taxes receivable was \$15 million, a decrease of \$11 million from February 28, 2018. The decrease in income taxes receivable was due to refunds received in the first six months of fiscal 2019.

At August 31, 2018, other current assets were \$52 million, an increase of \$14 million from February 28, 2018. The increase in other current assets was primarily due to increases in deferred commission as a result of the adoption of ASC 606 and prepaid maintenance.

Current Liabilities

The decrease in current liabilities of \$18 million at the end of the second quarter of fiscal 2019 from the end of the fourth quarter of fiscal 2018 was primarily due to a decrease in accrued liabilities of \$43 million and accounts payable of \$12 million offset by an increase in current deferred revenue of \$35 million. As at August 31, 2018, current deferred revenue was \$177 million, reflecting an increase of \$35 million from February 28, 2018, which was primarily attributable to the adoption of ASC 606. Accrued liabilities were \$162 million, reflecting a decrease of \$43 million from February 28, 2018, which was primarily attributable to the decreases in vendor liabilities and a variable incentive plan accrual compared to the fourth quarter of fiscal 2018.

Cash flows for the six months ended August 31, 2018 compared to the six months ended August 31, 2017 were as follows:

	For the Six Months Ended (in millions)		
	August 31, 2018	August 31, 2017	Change
Net cash flows provided by (used in):			
Operating activities	\$ 22	\$ 867	\$ (845)
Investing activities	(264)	(1,002)	738
Financing activities	2	(14)	16
Effect of foreign exchange on cash and cash equivalents	(2)	3	(5)
Net decrease in cash and cash equivalents	<u>\$ (242)</u>	<u>\$ (146)</u>	<u>\$ (96)</u>

Operating Activities

The decrease in net cash flows provided by operating activities of \$845 million for the first six months of fiscal 2019 primarily reflects the Qualcomm arbitration award in the first six months of fiscal 2018.

Investing Activities

During the six months ended August 31, 2018, cash flows used in investing activities were \$264 million and included cash used in transactions involving the acquisitions of short-term and long-term investments, net of the proceeds on sale or maturity in the amount of \$240 million, intangible asset additions of \$16 million, and acquisitions of property, plant and equipment of \$9 million. For the same period in the prior fiscal year, cash flows used in investing activities were \$1,002 million and included cash used in transactions involving the acquisitions of short-term and long-term investments, net of the proceeds on sale or maturity in the amount of \$985 million, intangible asset additions of \$14 million and acquisitions of property, plant and equipment of \$6 million offset by proceeds on sale of property, plant and equipment \$3 million.

Financing Activities

The increase in cash flows provided by financing activities was \$16 million for the first six months of fiscal 2019 due to common share repurchases made under the normal course issuer bid discussed under "Business Overview - Normal Course Issuer Bid" above in the first six months of fiscal 2018.

Aggregate Contractual Obligations

Purchase obligations and commitments amounted to approximately \$271 million as at August 31, 2018, including future interest payments of \$50 million on the Debentures and operating lease obligations of \$120 million. The remaining balance consists of purchase orders for goods and services utilized in the operations of the Company. Total aggregate contractual obligations as at August 31, 2018 decreased by \$34 million as compared to the February 28, 2018 balance of approximately \$305 million, which was attributable to decreases in purchase orders for goods and services used in operations, decreases in operating lease obligations and a decrease in future interest payments on the Debentures.

Debenture Financing and Other Funding Sources

See Note 8 to the Consolidated Financial Statements for a description of the Debentures.

The Company had \$29 million in collateralized outstanding letters of credit in support of certain leasing arrangements entered into in the ordinary course of business as of August 31, 2018. See Note 2 to the Consolidated Financial Statements for further information concerning the Company's restricted cash.

Cash, cash equivalents, and investments were approximately \$2.35 billion as at August 31, 2018. The Company's management remains focused on maintaining appropriate cash balances, efficiently managing working capital balances and managing the liquidity needs of the business. Based on its current financial projections, the Company believes its financial resources, together with expected future operating cash generating and operating expense reduction activities and access to other potential financing arrangements, should be sufficient to meet funding requirements for current financial commitments and future operating expenditures not yet committed, and should provide the necessary financial capacity for the foreseeable future.

The Company does not have any off-balance sheet arrangements as defined in Item 303(a)(4)(ii) of Regulation S-K under the Securities Exchange Act of 1934, as amended, or under applicable Canadian securities laws.

Legal Proceedings

The Company is involved in litigation in the normal course of its business, both as a defendant and as a plaintiff. Management reviews all of the relevant facts for each claim and applies judgment in evaluating the likelihood and, if applicable, the amount of any potential loss. Where a potential loss is considered probable and the amount is reasonably estimable, provisions for loss are made based on management's assessment of the likely outcome. Where a range of loss can be reasonably estimated with no best estimate in the range, the Company records the minimum amount in the range. The Company does not provide for claims for which the outcome is not determinable or claims for which the amount of the loss cannot be reasonably estimated. Any settlements or awards under such claims are provisioned for when reasonably determinable.

As of August 31, 2018, there are no claims outstanding for which the Company has assessed the potential loss as both probable to result and reasonably estimable, therefore no accrual has been made. See Note 12 to the Consolidated Financial Statements for a further discussion of the Company's legal matters.

Market Risk of Financial Instruments

The Company is engaged in operating and financing activities that generate risk in three primary areas:

Foreign Exchange

The Company is exposed to foreign exchange risk as a result of transactions in currencies other than its functional currency, the U.S. dollar. The majority of the Company's revenue in the second quarter of fiscal 2019 were transacted in U.S. dollars. Portions of the revenue were denominated in Canadian dollars, euros and British pounds. Purchases of raw materials were primarily transacted in U.S. dollars. Other expenses, consisting mainly of salaries and certain operating costs were incurred primarily in Canadian dollars, but were also incurred in U.S. dollars, euros and British pounds. At August 31, 2018, approximately 7% of cash and cash equivalents, 25% of accounts receivables and 6% of accounts payable were denominated in foreign currencies (February 28, 2018 – 9%, 35% and 6%, respectively). These foreign currencies primarily include the Canadian dollar, euro and British pound. As part of its risk management strategy, the Company maintains net monetary asset and/or liability balances in foreign currencies and engages in foreign currency hedging activities using derivative financial instruments, including currency forward contracts and currency options. The Company does not use derivative instruments for speculative purposes. See Note 4 to the Consolidated Financial Statements for information concerning the Company's foreign currency hedging activities.

Interest Rate

Cash and cash equivalents and investments are invested in certain instruments of varying maturities. Consequently, the Company is exposed to interest rate risk as a result of holding investments of varying maturities. The fair value of investments, as well as the investment income derived from the investment portfolio, will fluctuate with changes in prevailing interest rates. The Company has also issued the Debentures with a fixed 3.75% interest rate. The fair value of the Debentures will fluctuate with changes in prevailing interest rates. Consequently, the Company is exposed to interest rate risk as a result of the long-term nature of the Debentures. The Company does not currently utilize interest rate derivative instruments to hedge its investment portfolio or changes in market value of the Debentures.

Credit and Customer Concentration

The Company, in the normal course of business, monitors the financial condition of its customers and reviews the credit history of each new customer. The Company establishes an allowance for doubtful accounts ("AFDA") that corresponds to the specific credit risk of its customers, historical trends and economic circumstances. The AFDA as at August 31, 2018 was \$23 million (February 28, 2018 - \$24 million). There were two customers that individually comprised more than 10% of accounts receivable as at August 31, 2018 (February 28, 2018 - no customers comprised more than 10%). During the second quarter of fiscal 2019, the percentage of the Company's receivable balance that was past due increased by 4.8% compared to the fourth quarter of fiscal 2018. Although the Company actively monitors and attempts to collect on its receivables as they become due, the risk of further delays or challenges in obtaining timely payments of receivables exists. The occurrence of such delays or challenges in obtaining timely payments could negatively impact the Company's liquidity and financial condition. There was one customer that comprised more than 10% of the Company's revenue in the second quarter of fiscal 2019 (one customer comprised more than 10% of the Company's revenue in the second quarter of fiscal 2018).

Market values are determined for each individual security in the investment portfolio. The Company assesses declines in the value of individual investments for impairment to determine whether the decline is other-than-temporary. The Company makes this assessment by considering available evidence including changes in general market conditions, specific industry and individual company data, the length of time and the extent to which the fair value has been less than cost, the financial condition, the near-term prospects of the individual investment and, in the case of debt securities, the Company's ability and intent to hold the investments to maturity. During the six months ended August 31, 2018 the Company did not record any other-than-temporary impairment charges related to investments (August 31, 2017 - nil).

See Note 4 to the Consolidated Financial Statements for additional information regarding the Company's credit risk as it pertains to its foreign exchange derivative counterparties.

Changes in Internal Control Over Financial Reporting

During the three months ended August 31, 2018, no changes were made to the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.