

BLACKBERRY LIMITED

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED MAY 31, 2019

June 26, 2019

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 months ended May 31, 2019, as well as the Company's audited consolidated financial statements and accompanying notes, and MD&A for the fiscal year ended February 28, 2019 (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 months ended May 31, 2019 and up to and including June 26, 2019.

Additional information about the Company, including the Company's Annual Information Form for the fiscal year ended February 28, 2019 (the "AIF"), which is included in the Company's Annual Report on Form 40-F for the fiscal year ended February 28, 2019 (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 increase, enhance and integrate its product and service offerings;
- the Company's expectations regarding revenue for fiscal 2020;
- 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", "Key Metrics - Recurring Revenue Percentage", "Results of Operations – Three months ended May 31, 2019 compared to three months ended May 31, 2018 - Revenue - Revenue by Product and Service", 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 could significantly harm its business;
- 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 channel partners; 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 changes in technology and the Company's business strategy, evolving industry standards, intense competition and short product life cycles that characterize the industries in which the Company operates. See "Business Overview - Strategy" 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 a trusted security software and services company that provides enterprises and governments with the technology they need to secure the Internet of Things (the "IoT"). Based in Waterloo, Ontario, the company is unwavering in its commitment to safety, cybersecurity and data privacy, and leads in key areas such as artificial intelligence ("AI"), endpoint security and management, encryption and embedded systems. The Company's common shares trade under the ticker symbol "BB" on the New York Stock Exchange and the Toronto Stock Exchange.

Strategy

The Company is widely recognized for productivity and security innovations, and the Company believes that it delivers the most secure endpoint management and communications 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 to secure the IoT. The Company leverages many elements of its extensive technology portfolio to extend best-in-class security and reliability to its solutions for the IoT, including unified endpoint management ("UEM"), cybersecurity solutions, embedded systems, crisis communications, enterprise applications, and related services, with hosting available on the Company's global, scalable, secure network, as well as in the cloud.

The Company intends to continue to increase and enhance its product and service offerings through both organic investments and strategic acquisitions. The Company's goal is to remain a leader in its target enterprise markets by continuing to extend the functionality of its secure platform and delivering innovative solutions focused on strategic industry verticals.

Products and Services

The Company's core software and services offering is its end-to-end platform that comprises endpoint management capabilities, enterprise communication and collaboration software and safety-certified embedded solutions. The Company is developing BlackBerry Spark, a next-generation secure communications platform that will create and leverage trusted connections between endpoints. The Company expects a robust schedule of product launches in fiscal 2020, including new offerings for BlackBerry Spark, BlackBerry Cylance and BlackBerry QNX.

The Company groups its portfolio of product and services offerings as follows: IoT, BlackBerry Cylance, Licensing and Other.

The Company's IoT business is comprised of the Company's suite of security software products and services designed to secure endpoint communications for the IoT, including BlackBerry UEM, BlackBerry Dynamics, BlackBerry AtHoc, Secusmart and the technologies offered by BlackBerry QNX. The IoT business generates revenue predominantly through software licenses, commonly bundled with support, maintenance and professional services. In fiscal 2019, the IoT products and services were included in the Company's Enterprise Software & Services ("Enterprise") and BlackBerry Technology Solutions ("BTS") business groupings.

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 BlackBerry QNX unit is a global provider of real-time operating systems, middleware, development tools, and professional services for connected embedded systems in the automotive, medical, industrial automation and other 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. These solutions include the BlackBerry QNX CAR Platform and the Neutrino operating system, among other technologies.

The Company's IoT offerings also include its BlackBerry Radar asset tracking solution, BlackBerry Workspaces electronic file synchronization and sharing platform, BlackBerry Jarvis code security testing platform, Paratek antenna tuning technology, BlackBerry Certicom cryptography and key management products, BlackBerry Messenger (“BBM”) Enterprise service, BlackBerry Spark Communication Services and BlackBerry Cybersecurity Services.

The BlackBerry Cylance business offers a leading AI and machine learning-based platform consisting of CylancePROTECT, an endpoint threat prevention solution that uses machine learning to prevent suspicious behavior and the execution of malicious code on an endpoint, and CylanceOPTICS, an endpoint detection and response (“EDR”) solution that provides both visibility into and prevention of malicious activity on an endpoint. BlackBerry Cylance also offers professional services and other cybersecurity applications. The Company intends to integrate the intelligent cybersecurity capabilities of BlackBerry Cylance with BlackBerry Spark and BlackBerry QNX technologies.

The Licensing business includes the Company's patent licensing programs and its mobility software licensing arrangements, including 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 to include a broader set of devices and non-smartphone endpoints.

The Company's Other business generates revenue from service access fees (“SAF”) charged to subscribers using the Company's legacy BlackBerry 7 and prior BlackBerry operating systems, as well as revenue relating to unspecified future software upgrade rights for devices previously sold by the Company.

Recent Developments

The Company continues to execute on its strategy in fiscal 2020 and announced the following achievements:

- Entered into a collaborative supply agreement expanding the Company's partnership with LG Electronics Inc. to accelerate the deployment of connected and autonomous vehicle technology for automotive OEMs and Tier 1 vendors;
- Announced that BlackBerry QNX Software is embedded in more than 150 million vehicles;
- Achieved Federal Risk and Authorization Management Program (“FedRAMP”) Ready status for the BlackBerry Government Mobility Suite, a cloud-based endpoint management solution developed specifically for U.S. government agencies;
- Announced support of Canada's Digital Charter, aimed at protecting the privacy and data security of Canadians, and that the Company has been recognized by the Government of Canada as a benchmark for trusted technology;
- Announced that Forrester found that BlackBerry Cylance's AI-driven endpoint security products delivered a 99 percent return on investment;
- Announced that BlackBerry Cylance has completed an Australian Information Security Registered Assessors Program (IRAP) assessment to obtain certification as a security solutions provider to Australian federal government agencies;
- With WITTENSTEIN high integrity systems, announced a new embedded software platform that enables the development of safety-certified and mission-critical applications on heterogenous system-on-chip processors;
- Launched BlackBerry Radar H2, a new intelligent, data-driven asset monitoring device that can help automate operations, improve utilization of trailers, containers, chassis and other remote assets, as well as ensure assets are safe and secure;
- Established BlackBerry Government Solutions, to accelerate the company's FedRAMP initiatives and deepen ties with U.S. federal agencies;

- BlackBerry Limited announced that the NATO Communications and Information (NCI) Agency has awarded a contract for BlackBerry's SecuSUITE® for Government to encrypt the conversations of its technology and cyber leaders;
- Announced that Verizon added BlackBerry Cylance's AI-driven antivirus security solutions to its Managed Security Services portfolio; and
- Introduced CylancePERSONA, the first proactive endpoint behavioral analytics solution.

Inducement Awards

In the first quarter of fiscal 2020, the Board approved an agreement to grant performance-based equity awards ("Inducement Awards") to the co-founders of Cylance covering up to 4,182,189 common shares. Up to 25%, 35% and 40% of the Inducement Awards may be earned at the end of the Company's 2020, 2021 and 2022 fiscal years, respectively, if certain performance conditions are met, and any earned amounts will vest at the end of fiscal 2022. The Company also notes that 75% of the awards eligible to vest in a given year are based on achievement of a billings goal and 25% are based on achievement of a contribution margin goal.

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 June 26, 2019, the Company announced financial results for the three months ended May 31, 2019, 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.

For the three months ended May 31, 2019, these measures were adjusted for the following (collectively, the "Q1 Fiscal 2020 Non-GAAP Adjustments") (all items pre-tax and after-tax):

- the Q1 Fiscal 2020 Debentures Fair Value Adjustment (as defined below under "First Quarter Fiscal 2020 Summary Results of Operations – Financial Highlights – Debentures Fair Value Adjustment") of approximately \$28 million;
- restructuring charges from the Resource Allocation Program ("RAP") consisting of amounts associated with employee termination benefits, facilities, and certain other costs of approximately \$1 million;
- software deferred revenue acquired but not recognized due to business combination accounting rules of approximately \$20 million;
- software deferred commission expense acquired but not recognized due to business combination accounting rules of approximately \$5 million;
- stock compensation expense of approximately \$17 million;
- amortization of intangible assets acquired through business combinations of approximately \$35 million;
- business acquisition and integration costs incurred through business combinations of approximately \$1 million; and
- income tax valuation allowance related to the acquisition of Cylance of approximately \$1 million.

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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 percentage, 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 are therefore unlikely to 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 May 31, 2019 was included in the Company's press release dated June 26, 2019, and is reflected in the table below:

Q1 Fiscal 2020 Non-GAAP Adjustments		For the Three Months Ended May 31, 2019 <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		\$ 247	\$ 177	71.7%	\$ (33)	\$ (35)	\$ (0.06)
Debentures fair value adjustment ⁽¹⁾	Debentures fair value adjustment	—	—	—%	(28)	(28)	
RAP charges ⁽²⁾	Cost of sales	—	1	0.4%	1	1	
Software deferred revenue acquired ⁽³⁾	Revenue	20	20	2.1%	20	20	
Software deferred commission expense acquired	Selling, marketing and administration	—	—	—%	(5)	(5)	
Stock compensation expense	Cost of sales	—	1	0.3%	1	1	
Stock compensation expense	Research and development	—	—	—%	3	3	
Stock compensation expense	Selling, marketing and administration	—	—	—%	13	13	
Acquired intangibles amortization	Amortization	—	—	—%	35	35	
Business acquisition and integration costs	Selling, marketing and administration	—	—	—%	1	1	
Acquisition valuation allowance	Income taxes	—	—	—%	—	(1)	
Adjusted		<u>\$ 267</u>	<u>\$ 199</u>	<u>74.5%</u>	<u>\$ 8</u>	<u>\$ 5</u>	<u>\$ 0.01</u>

⁽¹⁾ See "First Quarter Fiscal 2020 Summary Results of Operations – Financial Highlights - Debentures Fair Value Adjustment".

⁽²⁾ See "First Quarter Fiscal 2020 Summary Results of Operations – Financial Highlights - Restructuring Charges".

⁽³⁾ \$19 million was included in BlackBerry Cylance revenue and \$1 million was included in IoT revenue.

Similarly, on June 22, 2018, the Company announced financial results for the three months ended May 31, 2018, which included certain non-GAAP financial measures, including adjusted revenue, adjusted gross margin, adjusted gross margin percentage, adjusted EBITDA, adjusted EBITDA margin percentage, adjusted income (loss) before income taxes, adjusted net income (loss) and adjusted earnings (loss) per share.

For the three months ended May 31, 2018, these measures were adjusted for the following (collectively, the "Q1 Fiscal 2019 Non-GAAP Adjustments") (all items pre-tax and after tax):

- a fair value adjustment associated with the Company's 3.75% unsecured convertible debentures (the "Debentures") of approximately \$28 million (the "Q1 Fiscal 2019 Debentures Fair Value Adjustment");
- RAP charges of approximately \$4 million;
- software deferred revenue acquired but not recognized due to business combination accounting rules of approximately \$4 million;
- stock compensation expense of approximately \$18 million;
- amortization of intangible assets acquired through business combinations of approximately \$22 million; and
- business acquisition and integration costs incurred through business combinations of approximately \$1 million.

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A reconciliation from the most directly comparable U.S. GAAP measures to these non-GAAP financial measures for the three months ended May 31, 2018 was included in the Company's press release, dated June 22, 2018, and is reflected in the table below.

For the Three Months Ended May 31, 2018

(in millions)

	Income statement location	Revenue	Gross margin (before taxes)	Gross margin % (before taxes)	Income (loss) before income taxes	Net income (loss)	Basic earnings per share
As reported		\$ 213	\$ 161	75.6 %	\$ (59)	\$ (60)	\$ (0.11)
Debentures fair value adjustment	Debentures fair value adjustment	—	—	—	28	28	
RAP charges	Research and development	—	—	—	2	2	
RAP charges	Selling, marketing and administration	—	—	—	2	2	
Software deferred revenue acquired ⁽¹⁾	Revenue	4	4	0.4 %	4	4	
Stock compensation expense	Cost of sales	—	1	0.5 %	1	1	
Stock compensation expense	Research and development	—	—	—	3	3	
Stock compensation expense	Selling, marketing and administration	—	—	—	14	14	
Acquired intangibles amortization	Amortization	—	—	—	22	22	
Business acquisition and integration costs	Selling, marketing and administration	—	—	—	1	1	
Adjusted		<u>\$ 217</u>	<u>\$ 166</u>	<u>76.5 %</u>	<u>\$ 18</u>	<u>\$ 17</u>	<u>\$ 0.03</u>

⁽¹⁾ Included in IoT revenue.

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The Company also reported adjusted EBITDA and adjusted EBITDA margin percentage, as presented in the tables below, for the three months ended May 31, 2019 of \$23 million and 9%. 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 May 31, 2019 <i>(in millions)</i>
Operating loss	\$ (36)
Non-GAAP adjustments to operating loss	
Debentures fair value adjustment	(28)
Restructuring charges	1
Software deferred revenue acquired	20
Software deferred commission acquired	(5)
Stock compensation expense	17
Acquired intangibles amortization	35
Business acquisition and integration costs	1
Total non-GAAP adjustments to operating loss	41
Non-GAAP operating income	5
Amortization	53
Acquired intangibles amortization	(35)
Adjusted EBITDA	\$ 23
Adjusted revenue (per above)	267
Adjusted EBITDA margin	9%

Adjusted EBITDA and adjusted EBITDA margin percentage for the three months ended May 31, 2018 are reflected in the table below:

	For the Three Months Ended May 31, 2018 <i>(in millions)</i>
Operating loss	\$ (65)
Non-GAAP adjustments to operating loss	
Debentures fair value adjustment	28
RAP charges	4
Software deferred revenue acquired	4
Stock compensation expense	18
Acquired intangibles amortization	22
Business acquisition and integration costs	1
Total non-GAAP adjustments to operating loss	77
Non-GAAP operating income	12
Amortization	41
Acquired intangibles amortization	(22)
Adjusted EBITDA	\$ 31
Adjusted revenue (per above)	217
Adjusted EBITDA margin	14%

The Company also reported free cash flow as described in "First Quarter Fiscal 2020 Summary Results of Operations - Free Cash Flow", below.

Key Metrics

The Company regularly monitors a number of financial and operating metrics, including the following key metrics, in order to measure the Company's current performance and estimate future performance. Readers are cautioned that recurring revenue percentage, annual recurring revenue ("ARR") and dollar-based net retention rate ("DBNRR") do not have any standardized meaning prescribed by U.S. GAAP and are therefore unlikely to be comparable to similarly titled measures reported by other companies.

Recurring revenue percentage

The Company defines recurring revenue percentage as subscription, license and support revenue (which includes revenue relating to support for perpetual licenses) less IP and professional services for the period divided by revenue for the period. The Company uses recurring revenue percentage to provide visibility into the revenue expected to be recognized in the current and future periods.

Total software and services revenue, excluding IP and professional services, was greater than 90% recurring in the first quarter of fiscal 2020. Total software and services includes IoT, BlackBerry Cylance and Licensing. The Company expects that in fiscal 2020, between 85% and 90% of software and services revenue, excluding IP and professional services, will be recurring.

Annual Recurring Revenue ("ARR")

The Company defines ARR as the annualized value of all active subscription contracts as of the end of the reporting period. The Company uses ARR as an indicator of business momentum for the BlackBerry Cylance product line.

BlackBerry Cylance ARR was approximately \$172 million in the first quarter of fiscal 2020, an increase of approximately \$40 million, or 30%, compared to approximately \$130 million in the first quarter of fiscal 2019.

Dollar-Based Net Retention Rate ("DBNRR")

The Company defines DBNRR as the percentage of total annual contract value ("ACV") from its subscription customer base at the end of a trailing 12-month period over the ACV of the same tranche of customers at the beginning of that 12-month period. The Company uses DBNRR to evaluate the long-term value of BlackBerry Cylance's customer relationships, measuring the ability of the business to retain and expand recurring revenue from its existing customer base.

BlackBerry Cylance DBNRR was greater than 100% in the first quarter of fiscal 2020 and in the first quarter of fiscal 2019.

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.

Leases

On March 1, 2019, the Company adopted the new standard on leases, Accounting Standards Codification 842 ("ASC 842"). The Company determines if an arrangement is or contains a lease at inception. Such determination requires consideration of all relevant facts and circumstances. Operating leases are included in operating lease right-of-use ("ROU") assets, accrued liabilities, and operating lease liabilities on the Company's consolidated balance sheets. Finance leases are included in property, plant and equipment, net, accrued liabilities, and other long-term liabilities on the Company's consolidated balance sheets.

Operating lease ROU assets and operating lease liabilities are recognized based on the present value of the future minimum lease payments over the lease term at the commencement date. As most of the Company's leases do not provide an implicit discount rate, the Company primarily uses its incremental borrowing rate, based on the information available at the commencement date of the lease, in determining the present value of future payments. The Company's incremental borrowing rate is determined based on the rate of interest that the Company would have to pay to borrow an amount equal to the lease payments on a collateralized basis over a similar term in a similar economic environment. The operating lease ROU asset includes any lease payments made, lease incentives and initial direct costs incurred. The lease terms include options to extend or terminate the lease when it is reasonably certain that the Company will exercise that option. Lease expense for minimum lease payments is recognized on a straight-line basis over the lease term. In some cases, the Company has index-based variable lease payments for which an estimated rate is applied to the initial lease payment to determine future lease payments amounts.

The Company has building, car and data center lease agreements with lease and non-lease components that are accounted for separately. The Company has elected the short-term lease exemption, which allows the Company to not apply the recognition requirements to lease terms of 12 months or less on commencement date. The Company also elected the package of practical expedients where lease classification, embedded leases, and initial direct costs are not reassessed upon adoption of ASC 842.

For additional information concerning the Company's leases, see Note 12 to the Consolidated Financial Statements.

Derivative financial instruments

On March 1, 2019, the Company adopted the new Accounting Standards Update ("ASU") 2017-12 related to accounting for hedging activities. The Company uses derivative financial instruments, including forward contracts and options, to hedge certain foreign currency exposures. The Company does not use derivative financial instruments for speculative purposes.

The Company records all derivative instruments at fair value on the consolidated balance sheets. The fair value of these instruments is calculated based on notional and exercise values, transaction rates, market quoted currency spot rates, forward points, volatilities and interest rate yield curves. The accounting for changes in the fair value of a derivative depends on the intended use of the derivative instrument and the resulting designation.

For derivative instruments designated as cash flow hedges, the entire change in the value of the hedging instrument included in the assessment of hedge effectiveness is initially reported as a component of accumulated other comprehensive income (loss) ("AOCI"), net of tax, and subsequently reclassified into income in the same period or periods in which the hedged item affects income. In order for the Company to receive hedge accounting treatment, the cash flow hedge must be highly effective in offsetting changes in the value of the hedged item and the relationship between the hedging instrument and the associated hedged item must be formally documented in the same quarter in which the hedge relationship was designated. Hedge effectiveness is formally assessed, both at hedge inception and on an ongoing basis, to determine whether the derivatives used in hedging transactions are highly effective in offsetting changes in the value of the hedged items and whether they are expected to continue to be highly effective in future periods.

The Company formally documents relationships between hedging instruments and associated hedged items. This documentation includes: identification of the specific foreign currency asset, liability or forecasted transaction being hedged; the nature of the risk being hedged; the hedge objective; and the method of assessing hedge effectiveness. If an anticipated transaction is deemed no longer likely to occur, the corresponding derivative instrument is de-designated as a hedge and any associated unrealized gains and losses in AOCI are recognized in income at that time. Any future changes in the fair value of the instrument are recognized in current income.

For any derivative instruments that do not meet the requirements for hedge accounting, or for any derivative instruments for which hedge accounting is not elected, the changes in fair value of the instruments are recognized in income in the current period and will generally offset the changes in the U.S. dollar value of the associated asset, liability or forecasted transaction.

Issued Accounting Pronouncements

In June 2016, the FASB issued guidance related to the measurement of credit losses on financial instruments, ASU 2016-13. This guidance replaces the incurred loss impairment methodology in current U.S. GAAP with a methodology that reflects expected credit losses, requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates, and requires entities to estimate an expected lifetime credit loss on its financial assets. The guidance is effective for interim and annual periods beginning after December 15, 2019. The Company will adopt this guidance in the first quarter of fiscal 2021 and is currently evaluating the impact that the adoption will have on its results of operations, financial position and disclosures.

First Quarter Fiscal 2020 Summary Results of Operations

The following table sets forth certain unaudited consolidated statements of operations data for the quarter ended May 31, 2019 compared to the quarter ended May 31, 2018 under U.S. GAAP.

	For the Three Months Ended					
	<i>(in millions, except for share and per share amounts)</i>					
	May 31, 2019		May 31, 2018		Change	
Revenue ⁽¹⁾⁽²⁾	\$ 247	100.0%	\$ 213	100.0%	\$ 34	
Gross margin ⁽¹⁾⁽²⁾	177	71.7%	161	75.6%	16	
Operating expenses ⁽¹⁾⁽²⁾	213	86.2%	226	106.1%	(13)	
Income before income taxes	(33)	(13.4%)	(59)	(27.7%)	26	
Provision for income taxes	2	0.8%	1	0.5%	1	
Net income ⁽¹⁾	<u>\$ (35)</u>	<u>(14.2%)</u>	<u>\$ (60)</u>	<u>(28.2%)</u>	<u>\$ 25</u>	
Earnings (loss) per share - reported						
Basic	<u>\$ (0.06)</u>		<u>\$ (0.11)</u>		<u>\$ 0.05</u>	
Diluted ⁽³⁾⁽⁴⁾	<u>\$ (0.09)</u>		<u>\$ (0.11)</u>		<u>\$ 0.02</u>	
Weighted-average number of shares outstanding (000s)						
Basic ⁽⁵⁾	551,845		536,964			
Diluted ⁽³⁾⁽⁴⁾	612,345		536,964			

- (1) See "Non-GAAP Financial Measures" for the impact of the Q1 Fiscal 2020 Non-GAAP Adjustments on adjusted revenue, adjusted gross margin, adjusted operating expenses and adjusted net income in the first quarter of fiscal 2020.
- (2) See "Non-GAAP Financial Measures" for the impact of the Q1 Fiscal 2019 Non-GAAP Adjustments on adjusted revenue, adjusted gross margin and adjusted operating expenses in the first quarter of fiscal 2019.
- (3) Diluted loss per share on a U.S. GAAP basis for the first quarter of fiscal 2020 and fiscal 2019 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 9 to the Consolidated Financial Statements for the Company's calculation of diluted loss per share.
- (4) Diluted loss per share on a U.S. GAAP basis for the first quarter of fiscal 2019 does not include the dilutive effect of the Debentures as it would be anti-dilutive. See Note 9 to the Consolidated Financial Statements for the Company's calculation of diluted loss per share.
- (5) Basic loss per share on a U.S. GAAP basis for the first quarter of fiscal 2020 includes approximately 4,182,189 common shares to be issued in equal instalments on the next three anniversary dates of the Cylance acquisition, in consideration for the acquisition. There are no service or other requirements associated with the issuance of these shares.

Financial Highlights

In the first quarter of fiscal 2020, the Company recognized revenue of \$247 million and incurred a loss of \$35 million, or \$0.06 basic loss per share on a U.S. GAAP basis. The Company incurred a diluted loss per share of \$0.09 on a U.S. GAAP basis. The Company recognized adjusted revenue of \$267 million and adjusted net income of \$5 million, or adjusted earnings of \$0.01 per share, on a non-GAAP basis. See also "Non-GAAP Financial Measures".

The Company had approximately \$935 million in cash, cash equivalents and investments as of May 31, 2019.

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 May 31, 2019, the Company's net cash used in operating activities was \$64 million and capital expenditures were \$2 million, resulting in the Company reporting free cash usage of \$66 million. Free cash usage was \$49 million for the three months ended May 31, 2019 before considering the impact of acquisition and integration expenses, restructuring costs and legal proceedings.

Debentures Fair Value Adjustment

As previously disclosed, the Company elected the fair value option to account for 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 first quarter of fiscal 2020, the fair value of the Debentures decreased by approximately \$20 million. For the three months ended May 31, 2019, the Company recorded a non-cash charge relating to changes in fair value from instrument-specific credit risk of \$8 million in AOCI and non-cash income relating to changes in fair value from non-credit components of \$28 million (pre-tax and after tax) (the "Q1 Fiscal 2020 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 months ended May 31, 2019, the Company incurred approximately \$1 million in total pre-tax charges related to this program.

Results of Operations - Three months ended May 31, 2019 compared to three months ended May 31, 2018

Consolidated Revenue

Consolidated revenue increased \$34 million to approximately \$247 million in the first quarter of fiscal 2020 from \$213 million in the first quarter of fiscal 2019. The increase was primarily due to an increase of \$32 million in BlackBerry Cylance revenue to \$32 million from nil, an increase of \$10 million in IoT revenue to \$136 million from \$126 million and an increase of \$9 million in Licensing revenue to \$72 million from \$63 million, offset by a decrease of \$17 million in Other revenue to \$7 million from \$24 million. See "Results of Operations - Three months ended May 31, 2019 compared to three months ended May 31, 2018 - Revenue - Revenue by Product and Service" below.

BlackBerry Cylance revenue of \$32 million was due to the acquisition of Cylance in the fourth quarter of fiscal 2019.

The increase in IoT revenue of \$10 million was primarily due to increased revenue from professional services, royalties and development seat revenue from BlackBerry QNX.

The increase in Licensing revenue of \$9 million was primarily due to the completion of certain performance obligations relating to the BBM Consumer licensing arrangement and certain mobility licensing arrangements and higher IP revenue from 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, partially offset by the impact of an IP settlement in the first quarter of fiscal 2019.

Other revenue includes revenue from SAF and the Company's legacy handheld devices business. The decrease in Other revenue of \$17 million was primarily attributable to a decrease in SAF revenue and revenue from the legacy handheld business. The 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 and lower revenue from those users compared to the first quarter of fiscal 2019. The decrease in revenue from the legacy handheld business is primarily attributable to the release of previously accrued amounts in the first quarter of fiscal 2019 when the Company determined it had no further performance obligations.

Consolidated Gross Margin

Consolidated gross margin increased by \$16 million to approximately \$177 million in the first quarter of fiscal 2020 from \$161 million in the first quarter of fiscal 2019. The increase was primarily due to an increase in gross margin associated with BlackBerry Cylance and Licensing, partially offset by a decrease in gross margin associated with Other.

The increase in gross margin associated with BlackBerry Cylance and Licensing is primarily due to the reasons discussed above in "Consolidated Revenue". The decrease in gross margin associated with Other is primarily due to the decline in SAF revenue discussed above in "Consolidated Revenue", as the cost of goods sold associated with SAF was consistent in the first quarter of fiscal 2020 and the first quarter of fiscal 2019 due to certain fixed costs associated with SAF infrastructure and the decrease in gross margin associated with the legacy handheld business was primarily due to the decline in revenue discussed above in "Consolidated Revenue".

Consolidated Gross Margin Percentage

Consolidated gross margin percentage decreased by 3.9%, to approximately 71.7% of consolidated revenue in the first quarter of fiscal 2020 from 75.6% of consolidated revenue in the first quarter of fiscal 2019. The decrease was primarily due to a lower gross margin percentage associated with BlackBerry Cylance which has a higher proportion of revenue related to professional services.

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)					
	May 31, 2019		May 31, 2018		Change	
Revenue by Geography						
North America	\$ 160	64.8%	\$ 139	65.3%	\$ 21	15.1%
Europe, Middle East and Africa	61	24.7%	52	24.4%	9	17.3%
Other regions	26	10.5%	22	10.3%	4	18.2%
	<u>\$ 247</u>	<u>100.0%</u>	<u>\$ 213</u>	<u>100.0%</u>	<u>\$ 34</u>	<u>16.0%</u>

North America Revenue

Revenue in North America was \$160 million, or 64.8% of revenue in the first quarter of fiscal 2020, reflecting an increase of \$21 million compared to \$139 million, or 65.3% of revenue, in the first quarter of fiscal 2019. The increase in revenue is primarily due to increases in BlackBerry Cylance revenue and Licensing revenue due to the reasons discussed above in "Consolidated Revenue", partially offset by a decrease in Other revenue due to the reasons discussed above in "Consolidated Revenue".

Europe, Middle East and Africa Revenue

Revenue in Europe, Middle East and Africa was \$61 million or 24.7% of revenue in the first quarter of fiscal 2020, reflecting an increase of \$9 million compared to \$52 million or 24.4% of revenue in the first quarter of fiscal 2019. The increase in revenue is primarily due to increases in IoT and BlackBerry Cylance revenue, partially offset by a decrease in Other revenue. The increase in revenue in IoT is primarily attributable to an increase in royalty revenue and the upfront revenue recognition on certain software elements related to BlackBerry UEM and BlackBerry AtHoc deals. The increase in BlackBerry Cylance revenue is due to the reasons discussed above in "Consolidated Revenue". The decrease in Other revenue is due to the reasons discussed above in "Consolidated Revenue".

Other Regions Revenue

Revenue in other regions was \$26 million or 10.5% of revenue in the first quarter of fiscal 2020, reflecting an increase of \$4 million compared to \$22 million or 10.3% of revenue in the first quarter of fiscal 2019. The increase in revenue is primarily due to increases in Licensing and BlackBerry Cylance, partially offset by a decrease in Other revenue. The increase in Licensing revenue is primarily attributable to the completion of performance obligations on certain mobility licensing agreements. The increase in BlackBerry Cylance revenue is due to the reasons discussed above in "Consolidated Revenue". The decrease in Other revenue is due to the reasons discussed above in "Consolidated 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 Three Months Ended (in millions)					
	May 31, 2019		May 31, 2018		Change	
Revenue by Product and Service						
IoT ⁽¹⁾	\$ 137	51.3%	\$ 130	59.9%	\$ 7	5.4 %
BlackBerry Cylance ⁽¹⁾	51	19.1%	—	—%	51	— %
Licensing	72	27.0%	63	29.0%	9	14.3 %
Other	7	2.6%	24	11.1%	(17)	(70.8)%
	<u>\$ 267</u>	<u>100.0%</u>	<u>\$ 217</u>	<u>100.0%</u>	<u>\$ 50</u>	<u>23.0 %</u>

⁽¹⁾ See “Non-GAAP Financial Measures” for the relevant Q1 Fiscal 2020 Non-GAAP Adjustments and Q1 Fiscal 2019 Non-GAAP Adjustments made to BlackBerry Cylance and IoT.

IoT

IoT non-GAAP revenue was \$137 million, or 51.3% of revenue, in the first quarter of fiscal 2020, an increase of \$7 million compared to revenue of \$130 million, or 59.9% of revenue, in the first quarter of fiscal 2019. Within IoT, BTS non-GAAP revenue increased by 16% and Enterprise non-GAAP revenue increased by a nominal amount in the first quarter of fiscal 2020 compared to the first quarter of fiscal 2019. IoT non-GAAP revenue increased due the reasons described above in Consolidated Revenue, partially offset by a decrease of \$3 million in the non-GAAP adjustment of deferred software revenue acquired to \$1 million in the first quarter of fiscal 2020 from \$4 million in the first quarter of fiscal 2019 and due to the reasons described above in “Consolidated Revenue”.

Excluding the deferred software revenue acquired adjustment described under “Non-GAAP Financial Measures”, IoT U.S. GAAP revenue was \$136 million, or 55.1% of revenue, in the first quarter of fiscal 2020, compared to \$126 million, or 59.2% of revenue, in the first quarter of fiscal 2019, representing an increase of \$10 million, or 7.9%, due to the reasons described above in “Consolidated Revenue”.

During the first quarter of fiscal 2020, the Company made significant changes to the Enterprise sales leadership team. The Company expects sequential Enterprise non-GAAP revenue growth through the remainder of fiscal 2020 due in part to expected product launches related to BlackBerry Spark.

BlackBerry Cylance

As the Company acquired Cylance at the end of fiscal 2019, no revenue was reported in the first quarter of fiscal 2019.

BlackBerry Cylance non-GAAP revenue was \$51 million, or 19.1% of revenue, in the first quarter of fiscal 2020. Excluding the deferred software revenue acquired adjustment described under “Non-GAAP Financial Measures”, BlackBerry Cylance U.S. GAAP revenue was \$32 million, or 13.0% of revenue, in the first quarter of fiscal 2020.

Cylance recorded revenue of \$39 million for the three months ended May 31, 2018. After removing the effect of the purchase accounting related adjustment, BlackBerry Cylance non-GAAP revenue was \$51 million for the three months ended May 31, 2019, representing an increase of \$12 million, or 30.8% over the prior year period.

Licensing

Licensing revenue was \$72 million, or 27.0% of revenue, in the first quarter of fiscal 2020, an increase of \$9 million compared to \$63 million, or 29.0% of revenue from the first quarter of fiscal 2019. Licensing revenue increased due to the reasons described above in “Consolidated Revenue”. The Company expects Licensing revenue in the second half of fiscal 2020 to be higher than in the first half of fiscal 2020.

Other

Other revenue was \$7 million related to SAF, or 2.6% of revenue, in the first quarter of fiscal 2020, compared to \$24 million, or 11.1% of revenue, in the first quarter of fiscal 2019, representing a decrease of \$17 million, or 70.8%. The \$17 million decrease in Other revenue 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 expense for the quarter ended May 31, 2019, compared to the quarter ended February 28, 2019 and the quarter ended May 31, 2018. The Company believes it is also meaningful to provide a sequential comparison between the first quarter of fiscal 2020 and the fourth quarter of fiscal 2019.

	For the Three Months Ended (in millions)					
	May 31, 2019		February 28, 2019		May 31, 2018	
	\$	% of Revenue	\$	% of Revenue	\$	% of Revenue
Revenue	\$ 247		\$ 255		\$ 213	
Operating expenses						
Research and development ⁽¹⁾⁽²⁾⁽³⁾	\$ 71	28.7 %	\$ 52	20.4 %	\$ 61	28.6%
Selling, marketing and administration ⁽¹⁾⁽²⁾⁽³⁾	121	49.0 %	110	43.1 %	100	46.9%
Amortization ⁽¹⁾⁽²⁾⁽³⁾	49	19.8 %	31	12.2 %	37	17.4%
Debentures fair value adjustment ⁽¹⁾⁽²⁾⁽³⁾	(28)	(11.3)%	(6)	(2.4)%	28	13.1%
Settlements, net ⁽³⁾	—	— %	(9)	(3.5)%	—	—%
Total	\$ 213	86.2 %	\$ 178	69.8 %	\$ 226	106.0%

(1) See "Non-GAAP Financial Measures" for the impact of the Q1 Fiscal 2020 Non-GAAP Adjustments on adjusted operating expenditures in the first quarter of fiscal 2020.

(2) See "Non-GAAP Financial Measures" for the impact of the Q1 Fiscal 2019 Non-GAAP Adjustments on adjusted operating expenditures in the first quarter of fiscal 2019.

(3) In the fourth quarter of fiscal 2019, the Company recognized non-cash income associated with a change in the fair value of the Debentures of approximately \$6 million (the "Q4 Fiscal 2019 Debentures Fair Value Adjustment"), net restructuring charges of approximately \$2 million in selling, marketing and administration expenses, stock compensation expense of \$3 million and \$10 million in research and development and selling, marketing and administration expenses, respectively, acquired intangibles amortization of \$18 million, business acquisition and integration costs of \$8 million in selling, marketing and administration expenses and settlements of \$9 million, net of legal costs included in settlements, net (collectively the "Q4 Fiscal 2019 Non-GAAP Adjustments").

Operating expenses increased by \$35 million, or 19.7%, to \$213 million, or 86.2% of revenue, in the first quarter of fiscal 2020, compared to \$178 million, or 69.8% of revenue, in the fourth quarter of fiscal 2019. The increase was primarily attributable to an increase in salaries and benefits primarily due to the acquisition of Cylance in the fourth quarter of fiscal 2019, amortization expense, and settlements, net in the fourth quarter of fiscal 2019, partially offset by the difference between the Q1 Fiscal 2020 Debentures Fair Value Adjustment and Q4 Fiscal 2019 Debentures Fair Value Adjustment.

After giving effect to the relevant Q1 Fiscal 2020 Non-GAAP Adjustments and Q4 Fiscal 2019 Non-GAAP Adjustments, non-GAAP operating expenses increased by \$42 million. The increase was primarily attributable to an increase in salaries and benefits, infrastructure costs and marketing and advertising costs primarily due to the acquisition of Cylance in the fourth quarter of fiscal 2019, partially offset by claims filed with the Ministry of Innovation, Science and Economic Development Canada relating to its Strategic Innovation Fund program's investment in BlackBerry QNX and a decrease in bad debt expense.

Operating expenses decreased by \$13 million, or 5.8%, to \$213 million or 86.2% of revenue in the first quarter of fiscal 2020, compared to approximately \$226 million or 106.0% of revenue in the first quarter of fiscal 2019. The decrease was primarily attributable to the difference between the Q1 Fiscal 2020 Debentures Fair Value Adjustment and Q1 Fiscal 2019 Debentures Fair Value Adjustment, claims filed with the Ministry of Innovation, Science and Economic Development Canada relating to its Strategic Innovation Fund program's investment in BlackBerry QNX and a decrease in restructuring charges, partially offset by an increase in salaries and benefits expense, amortization expense, infrastructure costs and marketing and advertising costs primarily due to the acquisition of Cylance in the fourth quarter of fiscal 2019.

After giving effect to the relevant Q1 Fiscal 2020 Non-GAAP Adjustments and Q1 Fiscal 2019 Non-GAAP Adjustments, non-GAAP operating expenses increased by \$40 million in the first quarter of fiscal 2020, compared to the first quarter of fiscal 2019. The increase was primarily attributable to an increase in salaries and benefits expense, infrastructure costs and marketing and advertising costs primarily due to the acquisition of Cylance in the fourth quarter of fiscal 2019.

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 increased by \$10 million, or 16.4%, to \$71 million in the first quarter of fiscal 2020 compared to \$61 million in the first quarter of fiscal 2019. After giving effect to the relevant Q1 Fiscal 2020 Non-GAAP Adjustments and Q1 Fiscal 2019 Non-GAAP Adjustments, non-GAAP research and development expenses increased by \$12 million. The increase was primarily attributable to an increase in salaries and benefits expense, professional services and infrastructure costs primarily due to the acquisition of Cylance in the fourth quarter of fiscal 2019, partially offset by claims filed with the Ministry of Innovation, Science and Economic Development Canada relating to its Strategic Innovation Fund program's investment in BlackBerry QNX.

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 increased by \$21 million, or 21.0%, to \$121 million in the first quarter of fiscal 2020 compared to \$100 million in the first quarter of fiscal 2019. After giving effect to the relevant Q1 Fiscal 2020 Non-GAAP Adjustments and Q1 Fiscal 2019 Non-GAAP Adjustments, non-GAAP selling, marketing and administration expenses increased by \$29 million. The increase was primarily attributable to an increase in salaries and benefits expense and marketing and advertising costs primarily due to the acquisition of Cylance in the fourth quarter of fiscal 2019 and legal expense.

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 first quarter of fiscal 2020 compared to the first quarter of fiscal 2019. 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		
	May 31, 2019	May 31, 2018	Change	May 31, 2019	May 31, 2018	Change
Property, plant and equipment	\$ 5	\$ 3	\$ 2	\$ 1	\$ 2	\$ (1)
Intangible assets	44	34	10	3	2	1
Total	\$ 49	\$ 37	\$ 12	\$ 4	\$ 4	\$ —

Amortization

Amortization expense relating to certain property, plant and equipment and intangible assets increased by \$12 million to \$49 million for the first quarter of fiscal 2020, compared to \$37 million for the first quarter of fiscal 2019. The increase in amortization expense reflects the intangible assets acquired as part of the Cylance acquisition in the fourth quarter of fiscal 2019.

After giving effect to the relevant Q1 Fiscal 2020 Non-GAAP Adjustments and Q1 Fiscal 2019 Non-GAAP Adjustments, non-GAAP amortization expense decreased by \$1 million.

Cost of Sales

Amortization expense relating to certain property, plant and equipment and intangible assets employed in the Company's service and IP operations was consistent at \$4 million for the first quarter of fiscal 2020, compared to \$4 million for the first quarter of fiscal 2019.

Investment Income

Investment income, which includes the interest expense from the Debentures, decreased by \$3 million to \$3 million in investment income in the first quarter of fiscal 2020, compared to investment income of \$6 million in the first quarter of fiscal 2019. The decreased investment income was due to lower cash and investment balances in the first quarter of fiscal 2020 versus the first quarter of fiscal 2019 as a result of the use of cash to fund the Cylance acquisition.

Income Taxes

For the first quarter of fiscal 2020, the Company's net effective income tax expense rate was approximately 6%, compared to a net effective income tax expense rate of approximately 2% 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 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.

After giving effect to the relevant Q1 Fiscal 2020 Non-GAAP Adjustments, the Company's non-GAAP income tax rate was approximately 38% compared to a net effective income tax expense rate of approximately 2% for the same period in the prior fiscal year. The increase is due to current year taxable items that could not be offset with carried forward tax attributes such as tax losses.

Net Income

The Company's net loss for the first quarter of fiscal 2020 was \$35 million, reflecting a decrease in net loss of \$25 million, compared to a net loss of \$60 million in the first quarter of fiscal 2019, primarily due to the difference between the Q1 Fiscal 2020 Debentures Fair Value Adjustment and Q1 Fiscal 2019 Debentures Fair Value Adjustment and an increase in gross margin, partially offset by an increase in operating expenses, as described above in "Operating Expenses". After giving effect to the relevant Q1 Fiscal 2020 Non-GAAP Adjustments and Q1 Fiscal 2019 Non-GAAP Adjustments, the Company's non-GAAP net income was \$5 million for the first quarter of fiscal 2020 compared to non-GAAP net income of \$17 million for the first quarter of fiscal 2019, reflecting a decrease in non-GAAP net income of \$12 million primarily due to an increase in operating expenses as described above in "Operating Expenses", partially offset by an increase in gross margin.

For the first quarter of fiscal 2020, U.S. GAAP basic loss and diluted loss per share were \$0.06 and \$0.09, respectively, compared to U.S. GAAP basic and diluted loss per share of \$0.11 for the same period in the prior fiscal year. After giving effect to the relevant Q1 Fiscal 2020 Non-GAAP Adjustments and Q1 Fiscal 2019 Non-GAAP Adjustments, the Company's non-GAAP basic earnings per share was \$0.01 for the first quarter of fiscal 2020 compared to non-GAAP basic earnings per share of \$0.03 for the first quarter of fiscal 2019.

The weighted average number of shares outstanding was approximately 552 million common shares for basic loss per share and 612 million common shares for diluted loss per share for the three months ended May 31, 2019, and approximately 537 million common shares for basic and diluted loss per share for the three months ended May 31, 2018.

Common Shares Outstanding

On June 21, 2019, there were 548 million common shares, 8 million options to purchase common shares, 23 million restricted share units and 0.9 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.

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 May 31, 2019. 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.

(in millions, except per share data)

	Fiscal Year 2020		Fiscal Year 2019				Fiscal Year 2018	
	First Quarter	Fourth Quarter	Third Quarter	Second Quarter	First Quarter	Fourth Quarter	Third Quarter	Second Quarter
Revenue	\$ 247	\$ 255	\$ 226	\$ 210	\$ 213	\$ 233	\$ 226	\$ 238
Gross margin	177	206	170	161	161	177	168	175
Operating expenses	213	178	112	122	226	194	426	153
Income (loss) before income taxes	(33)	32	60	44	(59)	(14)	(275)	23
Provision for (recovery of) income taxes	2	(19)	1	1	1	(4)	—	4
Net income (loss)	\$ (35)	\$ 51	\$ 59	\$ 43	\$ (60)	\$ (10)	\$ (275)	\$ 19
Earnings (loss) per share								
Basic earnings (loss) per share	\$ (0.06)	\$ 0.09	\$ 0.11	\$ 0.08	\$ (0.11)	\$ (0.02)	\$ (0.52)	\$ 0.04
Diluted earnings (loss) per share	\$ (0.09)	\$ 0.08	\$ (0.01)	\$ (0.04)	\$ (0.11)	\$ (0.06)	\$ (0.52)	\$ (0.08)

Financial Condition

Liquidity and Capital Resources

Cash, cash equivalents, and investments decreased by \$70 million to approximately \$935 million as at May 31, 2019 from approximately \$1.01 billion as at February 28, 2019, primarily as a result of changes in working capital. The majority of the Company's cash, cash equivalents, and investments are denominated in U.S. dollars as at May 31, 2019.

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

*As at
(in millions)*

	May 31, 2019	February 28, 2019	Change
Cash and cash equivalents	\$ 358	\$ 548	\$ (190)
Short-term investments	489	368	121
Restricted cash and cash equivalents	33	34	(1)
Long-term investments	55	55	—
Cash, cash equivalents, and investments	\$ 935	\$ 1,005	\$ (70)

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

*As at
(in millions)*

	May 31, 2019	February 28, 2019	Change
Current assets	\$ 1,166	\$ 1,194	\$ (28)
Current liabilities	476	471	5
Working capital	\$ 690	\$ 723	\$ (33)

Current Assets

The decrease in current assets of \$28 million at the end of the first quarter of fiscal 2020 from the end of the fourth quarter of fiscal 2019 was primarily due to a decrease in cash and cash equivalents of \$190 million, partially offset by an increase in short-term investments of \$121 million, accounts receivable of \$30 million, other current assets of \$7 million and other receivables of \$4 million.

At May 31, 2019, accounts receivable was \$224 million, an increase of \$30 million from February 28, 2019. The increase reflects the higher revenue recognized over the three months ended May 31, 2019 and an increase in days sales outstanding to 79 days at the end of the first quarter of fiscal 2020 from 61 days at the end of the fourth quarter of fiscal 2019.

At May 31, 2019, other receivables were \$23 million, an increase of \$4 million from February 28, 2019. The increase is primarily due to claims filed with the Ministry of Innovation, Science and Economic Development Canada relating to its Strategic Innovation Fund program's investment in BlackBerry QNX.

At May 31, 2019, income taxes receivable was \$9 million, consistent with the balance at February 28, 2019.

At May 31, 2019, other current assets were \$63 million, an increase of \$7 million from February 28, 2019. The increase in other current assets was primarily due to increases in prepaid maintenance, prepaid insurance and deferred commission.

Current Liabilities

The increase in current liabilities of \$5 million at the end of the first quarter of fiscal 2020 from the end of the fourth quarter of fiscal 2019 was primarily due to an increase in deferred revenue, current of \$32 million, income taxes payable of \$2 million, accounts payable of \$1 million, partially offset by a decrease in accrued liabilities of \$30 million.

As at May 31, 2019, deferred revenue, current was \$246 million, reflecting an increase of \$32 million from February 28, 2019, which was primarily attributable to acquired deferred revenue from the Cylance acquisition.

Accrued liabilities were \$162 million, reflecting a decrease of \$30 million from February 28, 2019, which was primarily attributable to the decreases in variable incentive plan accrual and vendor liabilities compared to the fourth quarter of fiscal 2019, partially offset by the current portion of operating lease liabilities from the adoption of ASC 842.

Cash flows for the three months ended May 31, 2019 compared to the three months ended May 31, 2018 were as follows:

	For the three months ended		
	<i>(in millions)</i>		
	May 31, 2019	May 31, 2018	Change
Net cash flows provided by (used in):			
Operating activities	\$ (64)	\$ (7)	\$ (57)
Investing activities	(129)	(293)	164
Financing activities	3	2	1
Effect of foreign exchange on cash and cash equivalents	(1)	(2)	1
Net decrease in cash and cash equivalents	<u>\$ (191)</u>	<u>\$ (300)</u>	<u>\$ 109</u>

Operating Activities

The decrease in net cash flows provided by operating activities of \$57 million for the first three months of fiscal 2020 primarily reflects the net changes in working capital and lower net income after adjustments for non-cash items.

Investing Activities

During the three months ended May 31, 2019, cash flows used in investing activities were \$129 million and included cash used in transactions involving the proceeds on sale or maturity of short-term and long-term investments, net of acquisitions in the amount of \$122 million, intangible asset additions of \$7 million, and acquisitions of property, plant and equipment of \$2 million, offset by proceeds expected from the decrease in consideration paid for the Cylance acquisition. For the same period in the prior fiscal year, cash flows used in investing activities were \$293 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 \$281 million, intangible asset additions of \$7 million and acquisitions of property, plant and equipment of \$5 million.

Financing Activities

The increase in cash flows provided by financing activities was \$1 million for the first three months of fiscal 2020 due to an increase in common shares issued.

Aggregate Contractual Obligations

Purchase obligations and commitments amounted to approximately \$480 million as at May 31, 2019, including future interest payments of \$33 million on the Debentures and operating lease obligations of \$204 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 May 31, 2019 increased by \$38 million as compared to the February 28, 2019 balance of approximately \$442 million, which was attributable to increases in purchase orders for goods and services used in operations.

Debenture Financing and Other Funding Sources

See Note 7 to the Consolidated Financial Statements for a description of the Debentures.

The Company had \$30 million in collateralized outstanding letters of credit in support of certain leasing arrangements entered into in the ordinary course of business as of May 31, 2019. See Note 2 to the Consolidated Financial Statements for further information concerning the Company's restricted cash.

Cash, cash equivalents, and investments were approximately \$935 million as at May 31, 2019. 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 May 31, 2019, 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 11 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 first quarter of fiscal 2020 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, British pounds, and other global currencies. At May 31, 2019, approximately 14% of cash and cash equivalents, 18% of accounts receivables and 18% of accounts payable were denominated in foreign currencies (February 28, 2019 – 9%, 29% and 4%, 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 3 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 May 31, 2019 was \$25 million (February 28, 2019 - \$25 million). There were two customers that each comprised more than 10% of accounts receivable as at May 31, 2019 (February 28, 2019 - one customer comprised more than 10%). During the first quarter of fiscal 2020, the percentage of the Company's receivable balance that was past due increased by 9.8% compared to the fourth quarter of fiscal 2019. 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 first quarter of fiscal 2020 (one customer comprised more than 10% of the Company's revenue in the first quarter of fiscal 2019).

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 three months ended May 31, 2019 the Company did not record any other-than-temporary impairment charges related to investments (May 31, 2018 - nil).

See Note 3 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 May 31, 2019, the Company implemented new controls as part of its adoption of ASC 842, which was effective for the Company on March 1, 2019. The new controls relate to leases under the adopted standard. There were no other changes in 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.