Operator. Ladies and gentlemen, thank you for standing by, and welcome to the CTG Second Quarter 2018 Earnings Release. (Operator Instructions) And as a reminder, we are recording today. I will now like to turn the conference over to Jim Culligan, Director of Investor Relations. Please go ahead.

Jim Culligan. Thank you, Art. And good morning, everyone. With me on today's call are Bud Crumlish, CTG's President and Chief Executive Officer; John Laubacker, Executive Vice President and Chief Financial Officer. Before we begin, I want to mention that statements during the course of this conference call that state the company's or management's intentions, hopes, beliefs, expectations and predictions for the future are forward-looking statements. It's important to note that the company's actual results could differ materially from those projected. These forward-looking statements are based on information as of today, Thursday, July 19, 2018. The company assumes no obligation to update these statements based on information from and after the date of this conference call. Additional information concerning factors that could cause actual results to differ from those made in the forward-looking statements is contained in our earnings release as well in the company's filings with the SEC.

Also, the company's press release and management's statements during the call will include discussions of certain adjusted non-GAAP measures and financial information. These financial measures and a reconciliation of GAAP to non-GAAP results are provided in both today's press release and the related Form 8-K. With that, I will turn the call over to Bud for his opening remarks.

Bud Crumlish. Thanks, Jim, and good morning to everyone joining us on the call. As highlighted in our press release earlier this morning, CTG had a strong second quarter, as we continue to build on the momentum that began taking hold late last year.

Starting with an overview of our financial results for the second quarter, consolidated revenue grew 12% sequentially and over 22% year-over-year to $92.7 million. Revenue exceeded our guidance range as a result of solid organic growth in both staffing and solutions as well as continued strength in Europe. We also recognized the first full quarter of revenue contribution from Soft Company, which we acquired in February.

Our operating results were in line with our expectations, as we continued to scale into our previous investments in CTG sales organization. Even when considering certain acquisition-related expenses in addition to the cost associated with ramping several new client engagements, second quarter earnings per share were at the midpoint of our guidance. When looking at the first 6 months of 2018 specifically, consolidated revenue increased by 15% compared with the first half of 2017, and non-GAAP earnings per share grew over 27% during the same period after adjusting for acquisition-related expenses.

Underlying these solid financial results was the continued increase in new business activity during the quarter. Through a combination of expanded business with existing clients as well as the addition of numerous new clients, we delivered a second consecutive quarter of sequential growth in staffing and a third consecutive quarter of growth in our solutions business. As further evidence of our recent new business momentum, we achieved the second consecutive quarter of sequential revenue growth in North America, which was 100% organic.

Now I'll address the latest development specific to both our staffing and solutions business including more detailed highlights of our recent progress in Europe and healthcare. In staffing, revenue grew 10% sequentially and 20% year-over-year to $63.4 million, representing approximately 68% of total revenue. The strong growth in the quarter was primarily driven by the completed transition of more than 350 employees for the incremental business we secured late last quarter at our largest client. As we stated on last quarter's call in April, the transition of these employees was a result of CTG's designation as the sole source provider for this new contract, which is an addition to being selected as a preferred provider for a new division at this long-standing client.

Collectively, revenue from this important client grew 15% year-over-year during the second quarter, indicating the ongoing strength of this relationship. Also during the quarter, we secured multiple new client wins and experienced positive activity across other existing staffing accounts. Demand continues

to be strong, and the war for talent is further intensified by the very low unemployment rate in the U.S., which actually increases demand for permanent placements.

In order to ensure CTG remains best positioned to compete in the current market environment and meet the evolving needs of our clients, we are actively executing on multiple strategic initiatives in our staffing business. As part of these efforts, first, we are continuingly evaluating our sales organizations, looking for ways to achieve maximum effectiveness. Each individual has specific performance targets in addition to our larger team corporate objectives. This uniform benchmark process allows us to identify the areas of strength and weakness readily, and in turn, continuously up-level the team to improve performance. During the quarter, we onboarded two new account executives with extensive experience to focus on strategic markets.

Another key initiative is the enhancement of CTG's recruiting organization. This is a critical driver of our overall performance. Our core strategic objectives in recruiting are centered around streamlining the recruiting process to increase efficiency and continuously cultivate a disciplined approach to the allocation of the recruiting resources. More specifically, this entails the rigorous profiling of requirements then focusing individual recruiters on the specific requirements in order to maximize the effectiveness.

In support of these efforts, we recently promoted an accomplished team member at CTG to the leadership role of recruiting, and we believe this strategic initiative has the potential to produce a meaningful increase in our success rate over the coming quarters.

Shifting to solutions, revenue in the second quarter was $29.3 million or approximately 32% of total revenue, representing 16% sequential growth and 30% year-over-year growth. Consistent with our comments last quarter, we are confident that the improving conversion rate on our healthy pipeline of new business opportunities will meaningfully contribute to a sustainable uptrend in our solution business.

Growth during the second quarter was driven by a combination of continued momentum in Europe and a series of new contract wins within health solutions. Other notable contributors to our progress within solutions included our commencements of work on a previously secured win with a large municipality in Alaska as well as the successful transition of service on the 3-year multimillion dollar EIM engagement with one of the world's largest energy companies, which we highlighted last quarter.

In Europe, as previously mentioned, we recognized our first full quarter of revenue contribution from Soft Company. This business has already begun to demonstrate its growth potential, and we continue to be very pleased with its performance since the acquisition. We made further progress during the quarter on integration activities, which remain on plan, and we are focused on cultivating collaboration across all the business development teams in Europe.

In fact, we recently secured the first contract as a result of cross-selling between an existing client, and we are now actively pursuing proposals as part of new joint selling opportunities.

Our organic business in Belgium and Luxembourg continued to perform well and delivered another consecutive quarter of strong results driven by increased demand for CTG's testing and GDPR solutions. Additionally, we secured two significant multiyear contracts with the European ministries, which will begin to add to our financial results late in 2018. For one of these institutions, we will now be the leader of a consortium—rather than a participant—due to our exceptional long-standing performance.

Despite converting several sizable engagements in the contracted business, the number of opportunities in the pipeline expanded during the quarter and remains very healthy. We also demonstrated notable progress in our health solutions business. Repositioning this business for renewed growth has been a key focus area over the last 24 months, and I am pleased to report that healthcare was a meaningful contributor to CTG's growth during the second quarter.

In conjunction with our expanded and renewed bookings across a number of existing clients, health solutions headcount increased by 25% sequentially and supported eight newly secured clients, which includes our recently announced win at Catholic Health Initiatives, or CHI, to implement Epic. This

electronic health record implementation for CHI spans 3 hospitals and 30 clinics as well as other medical facilities in Tennessee and Georgia.

In addition to Catholic Health Initiatives, these new accounts are U.S.-based clients, and they consist of a combination of EHR implementation and optimization work, legacy application support as well as a Level 1 service desk solution for a notable children's hospital in the Midwest.

Also during the quarter, we expanded our solutions offering with the formal launch of EIM Advantage. Developed as part of our ONE CTG initiative, this new offering consolidates several existing enterprise information management, or EIM, services into a new comprehensive solution that enables clients to capture, manage, analyze and transform data into actionable information.

As the amount of data generated by the IT devices and systems continues to grow, companies across all industries are finding it increasingly difficult to utilize this data effectively. CTG's EIM Advantage empowers clients with a scalable suite of services to unlock the value within their data to solve business challenges and improve performance. One of the key areas within healthcare that we're targeting with EIM Advantages is value-based care. The industry's growing trend towards value-based care models requires that hospitals, health systems and providers aggregate data in order to make business decisions that indicate performance under these new models.

CTG worked with these clients to build a foundation that will allow them to reap the benefits of analytic tools and platforms. With this foundation in place, these clients will be better positioned to optimize performance under the at-risk models of value-based care.

To conclude my remarks, CTG's strong second quarter results further validate the effectiveness of our growth initiatives as well as the team's ability to execute against our strategic plan. As a result of our increased traction on new business engagements and a higher conversion rate on pipeline opportunities, we are beginning to realize growing revenue contribution from the increased levels of activity of new contracts we've won in recent quarters. One in particular included a meaningful transition of newly awarded service desk business at our largest client. We also initiated work on sizable contracts for health solutions at new clients as well as delivering continued growth momentum in Europe with significant multiyear contracts with the European ministries.

Additionally, we have already begun to see the initial benefits of our Soft Company acquisition and believe they will be a strong contributor to our future growth and opportunities.

Although, we expect summer seasonality will result in lower utilization and a temporary pause in our sequential growth in the third quarter, which John will discuss more in a few minutes, we remain very optimistic about our prospects for continued sequential growth in the fourth quarter and for the full year, which is reflected in a higher midpoint of our full year revenue guidance. Moreover, we are fully committed to achieving our longer-term financial objectives by the end of 2019.

I'll now turn the call over to John for a more detailed review of our second quarter financial results and guidance.

John Laubacker. Thank you, Bud. Good morning, everyone. We appreciate you joining us on today's conference call. As we reported in this morning's press release, consolidated revenue in the second quarter grew to $92.7 million, compared with $82.7 million in the first quarter of 2018 and $75.5 million in the second quarter of 2017. Second quarter 2018 revenue included $2.5 million of favorable currency translation. Billable days in second quarter were 64, the same number as in the first quarter of 2018 and the year-ago second quarter.

Staffing revenue in the second quarter was $63.4 million, representing an increase of 10.3% sequentially and growth of 19.7% year-over-year, which was primarily driven by a combination of incremental new business at our largest client and strong demand resulting from several recent client wins.

Solutions revenue was $29.3 million in the second quarter of 2018, an increase of 15.6% sequentially and 29.8% compared with the year-ago quarter.

Growth in our solutions business primarily reflected the continued momentum in our European operations, including the first full quarter of revenue contributions from Soft Company and several new engagements in our U.S.-based healthcare vertical market.

Revenue from IBM in the 2018 second quarter grew to $21.9 million or 23.6% of total revenue, compared with $18.9 million or 22.8% in the first quarter of 2018 and $19 million or 25.1% of total revenue in last year's second quarter. No other client represented more than 10% of revenue during the first or second quarters of 2018. Direct costs as a percentage of revenue were 80.9% in both the first and second quarters of 2018 and 81.9% of revenue in the year-ago quarter.

GAAP net income in the second quarter of 2018 was $940,000 or $0.07 per diluted share, which included $0.01 per share in acquisition-related expenses. GAAP net income in the first quarter of 2018 was $414,000 or $0.03 per diluted share, which included $0.03 per share of acquisition-related expenses, and GAAP net income in the year-ago second quarter was $434,000 or $0.03 per diluted share, which included severance-related charges of $0.03 per diluted share.

Non-GAAP net income in the second quarter of 2018 was $1.1 million or $0.08 per diluted share compared with $881,000 or $0.06 per diluted share in the first quarter of 2018 and $1 million or $0.06 per diluted share in the second quarter of 2017.

As a reminder, following the acquisition of Soft Company, which utilizes a large number of subcontractors, we revised how we define and calculate headcount in order to provide a better representation of total billable consultants, which now includes both employees and subcontractors.

Based upon this approach, CTG's total headcount at the end of the second quarter was approximately 4,150 compared with 3,650 at the end of the first quarter of 2018 and 3,500 at the end of the year-ago second quarter. Approximately 91% of our second quarter 2018 headcount was billable, which is consistent with previous levels.

Turning to our balance sheet, cash and short-term investments at the end of the second quarter were $9.7 million, and we had $6.3 million of outstanding long-term debt. Capital expenditures in the second quarter of 2018 were $488,000. As previously announced, we completed a tender offer resulting in the purchase of approximately 1.5 million shares of CTG common stock at a price of $8.85 per share for an aggregate cost of approximately $13.5 million. Including the tender offer, the company has now purchased 19% of total outstanding shares over the past two years and has $8.9 million remaining under our recently expanded repurchase authorization.

Turning to our guidance, we expect typical seasonality in the third quarter related to summer vacations, primarily in our European operations, to result in a temporary decline in utilization and billable time. As our European operations now represent 35% of consolidated revenue, an increase from 25% of total revenue in the prior year, and given the current forecast for utilization and billable time in Europe, we expect a more pronounced impact from seasonality this year than in previous years.

Total revenue for the third quarter of 2018 is expected to range from $86 million to $90 million. Additionally, we expect third quarter GAAP net income to range from $0.03 to $0.05 per diluted share, and non-GAAP net income, excluding acquisition-related expenses and amortization of intangible assets, to range from $0.05 to $0.07 per diluted share. There are 63 billing days in the third quarter of 2018.

Importantly, we remain very optimistic about future growth as a result of our recent ramp-up of new business and a robust pipeline of opportunities. As a result, we have narrowed the range of our full year revenue guidance, and 2018 revenue is expected to range from $350 million to $360 million, reflecting a higher midpoint compared with our previous guidance. GAAP net income for the full year 2018 is expected to range from $0.20 to $0.26 per diluted share, and non-GAAP net income is expected to range from $0.30 to $0.36 per diluted share.

Revised earnings per share guidance for 2018 reflects our continued investment in business development and recruiting in third quarter to further enhance long-term growth and profitability.

Importantly, we expect to make continued progress toward our three-year financial plan over the coming quarters, and we remain committed to achieving our long-term goals and financial results in 2019.

With that, we'll now open the call for questions. Art, can you please manage our question-and-answer session?

Operator. And we have Kevin Liu from B. Riley.

Kevin Liu. I just wanted to start off here on the guidance, more so for the full year. Now through the first half, you've obviously been on track from both the revenue and earnings per share standpoint. As we look to the back half with earnings per share guidance coming down a bit, I'm just wondering if you could flush that out for us? Is that more reflective of the type of revenue mix that you see going on in the back half? Or are there other factors in terms of higher incremental investments or the like that you anticipate for the back half?

John Laubacker. I really think it's a combination of two or three things all at the same time. Part of that is mix. Our mix has been good to date, as we expected to grow the solutions business, so that's been very good. Part of that is the continued investment in business development and recruiting. The management team and the board have on a very dedicated basis, made a decision to invest in business development to grow this business in the long-term. So we are really looking at the business long-term in 2019, '20 and so on rather than trying to put some short-term gains or points on the board.

And lastly, as I just mentioned, talking about the guidance, when we estimate or analyze the seasonality in the staffing business, primarily in Europe but also in the U.S. over the summer months, we realize employees take holidays and vacation. We look at a range of where we've been in a number of years prior to this and we estimate what we think will be based upon staffing levels, clients, and consultation with line and business managers. At the time that we put the forecast together, earlier in the year, we expected to sort of be in the midpoint of the range of where we've been in previous years, considering last year, the year before and so on. The latest forecast has got us at a utilization that's dipping a little bit more toward the high end of the range (less utilization), and that's why we think we've been reasonable in lowering the guidance for the year, because we think that there's a bigger impact with that over the summer.

Kevin Liu. Both you and Bud have talked about your confidence in getting to your longer-term targets exiting fiscal ‘19. The biggest one I wanted to focus on there is you've talked previously about getting to 3% to 3.5% operating margin. Guidance for '18 currently implies you're probably somewhere sub-2%. How confident are you that you can get there? And can you talk a little bit about what needs to happen in order to ensure that you're within that operating margin range?

John Laubacker. It's a very good question. In the short-term, we focus more on revenue, which we're rapidly driving toward that $400 million level which is our 2019 goal, and earnings per share. It is absolutely part of our long-term goal to raise the operating margin. But at this time, we believe that's going to be at a slower pace than we had before. So our focus is turned not primarily but directionally toward making sure we get the revenue, making sure we get the EPS and making sure as part of that, we drive the operating margin up over time. Your math is good. We'd probably be closer to 2% than the 3% to 3.5% this year, and so we are a little bit behind in the margin plan, but we're very focused on the other parts of the goal.

Bud Crumlish. As these investments start kicking in, and they have so far this year—the additional investments that we're making—that's going to make a difference as well. So we're investing right now, and it definitely will improve in the future.

Kevin Liu. Lastly from me, it certainly sounds like continued strong traction in Europe. During your script, you mentioned being a leader of the consortium instead of a participant. Can you just talk about the nuances of that? What does that imply in terms of your growth versus what you've done historically?

And then also just over the long-term here, as you look across kind of the portfolio of services you're offering now, is that 7% compounded annual growth rate still a good target? Or do you see it either accelerating more so, given the opportunities you have?

Bud Crumlish. The European ministries' deal is like this: We were always a participant in these. It's always a group. It's a large volume of work, and it's difficult to get resources in Europe with the movement of people from one company to another, so it's always a consortium type of effect that works for the European ministries. Because we have been so strong over the last seven years, and with the diligent work effort that we've put forward, they have the confidence that we can lead this consortium, so this will be the first time we've done that. So it's a lot of accolades to our European colleagues.

And as far as the portfolio of services, with the Soft Company we added some additional service areas that we weren't in before specifically—industry expertise especially in data analytics—I mean that's a big deal over there. So I think that's going to drive business in all of the countries that we're working in. And as well as the 7.5%, it's a very good time to be in Europe, and we have a lot of successes and a lot of wins, and as weeks go by, as months go by, we're involved in more deals and winning at a higher level, and we have a really strong team throughout all the countries we're there, so I feel very optimistic about Europe.

Operator: Next we have Vince Colicchio with Barrington Research Associates.

Vince Colicchio. Bud, on the healthcare side, can you just drill down a bit more into where you're seeing the strength in the pipeline. I know you've got the electronic health record deal that you're working on now and your new service offering is out there and so forth. Just a little bit more color would be helpful.

Bud Crumlish. When you look at electronic health records, there have been a lot of implementations. We really kind of peaked out in that in 2012, as the market did. I think we're pretty comparable with everybody else. But there are a couple of things that are going on now that are driving this business. First, there is merger and acquisition activity going on, and that's exactly what happened with this Catholic Health Initiative that we won. A large hospital group acquired two more hospitals, and they are on Epic. Those other two hospitals weren't, so they have to convert their current systems over to Epic so they can all communicate collectively. That's one thing.

The other thing here is that some of these electronic medical record implementations were completed 10 years ago, and there's a useful life of the application, and it gets to the point where we have to do a redo on the implementation. We're seeing some of that as well. So those are the two main factors that are driving the business. So, I expect to see more business in EHR, whether it's implementations or optimization. I think that's going to definitely grow in the short-term and the long-term. So it's something that's a continuous thing out there.

Aside from some of the other things we're doing in healthcare, we're very strong in Application Advantage, and those are some of the other deals we've got. We have these relationships with a number of hospitals and with EIM—enterprise information management. EIM deals with their data, with data analytics, building data lakes, data warehouses, your security around the data, and how can you take that information and actually make decisions—and that ties perfectly into value-based care which in terms of healthcare is really a (single) fee for service. It's a (single) fee for everything that happens in the hospital and it goes to insurance company and gets processed.

Value-based care means that there's going to be a certain dollar value allocated to a specific procedure or getting you to a certain point of how well you want that population to be, and that's where the analytics really comes into play. You have to be the most efficient organization out there with all the data so that you can put programs in place to reduce cost and increase the care level of the community. And that's what we see in market.

Vince Colicchio. A question on the earnings outlook for the year. The step-up in business development spending, that's clear. Just for clarity purposes, the lower-than-expected utilization rate in Europe, could you take us through how that happened?

John Laubacker. What we typically do when we look at a forecast for a succeeding year, especially when it comes to the summer months and utilization, we take a look at historically what we've seen as far as the decrease in utilization, whether it be Europe or our own staffing business here in U.S. Europe tends to have a larger impact than we've seen in the U.S. So, we analyze where we've been over a period of time, we establish a range, and then we have very detailed discussions with line and business managers, talking about clients and opportunities and projects, and what's coming on board, what's coming off. A lot of analysis goes into it.

When looking at 2018, we had come up with what we thought would be a decrease in utilization, sort of, at the midpoint of the range of recent years of where that utilization goes down to, and what we are experiencing now with the current forecast is, I believe, that the decrease in utilization is at the high end of the range, so it really is having part of the impact—besides the business development—on the earnings guidance.

Bud Crumlish. Thank you, Art. Before we close out today's call, I'd like to reiterate the meaningful and growing progress that we've achieved, year-to-date, consistent with our strategic plan, our targeted investments in stronger leadership and business development, expanded solutions offerings as well as a highly strategic acquisition are now beginning to see contribute to incremental improvement in our financial results.

In fact, during the first half of 2018, we've demonstrated tangible evidence of renewed growth in effectively every area of CTG's business. As we continue to grow the revenue contribution from new business, we expect the benefits of greater scale and operating leverage to increasingly drive meaningful improvement and profitability in the coming years. Importantly, we also remain resolute in our commitment to creating increased shareholder value, which both the board and executive management believe has served well through further alignment with our fellow shareholders.

With that, thank you again for joining today's call and for your support of CTG. We look forward to reporting on our continued progress next quarter.

Note: This transcript has been edited slightly to make it more readable. It is not intended to be a verbatim recreation of the Computer Task Group (CTG) financial results teleconference and webcast that occurred on the date noted. Please refer to the audio version of the call, which is available on the Company's Web site (www.ctg.com) for approximately 90 days after the call date, as well as to information available on the SEC's Web site (www.sec.gov) before making an investment decision. Please also refer to the opening remarks of this call for CTG's announcement concerning forward-looking statements that were made during this call.