Operator. Ladies and gentlemen, thank you for standing by. Welcome to the CTG Second Quarter Financial Results Conference Call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session, and instructions will be given at that time. As a reminder, today's conference is being recorded. I would now like to turn the conference over to our host, Mr. Jim Culligan. Please go ahead, sir.

Jim Culligan. Thank you, Brad, and good morning, everyone. With me on today's call are Filip Gydé, CTG's President and Chief Executive Officer, and 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, Tuesday, July 23, 2019. 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 today's earnings release, as well as in the company's SEC filings.

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

Filip Gydé. Thank you, Jim. Good morning to everyone joining us on the phone and via webcast. It's my pleasure to be with you on today's call.

As reported in our press release earlier today, we had a second strong quarter, which clearly indicates that our strategy is working and that we are executing well against our strategic initiatives. Revenue grew more than 8% year-over-year and reached $100 million for the first time in five years. Further demonstrating our continued momentum, total revenue for the first half of 2019 grew nearly 13% over the same six-month period in 2018. Importantly, we also achieved marked improvement in our overall bottom-line results, with adjusted EPS in the second quarter representing a multiyear high. Underpinning these results was our team's successful and disciplined execution during the quarter as we benefitted from combination of continued organic growth and the first full quarter of revenue contribution from Tech-IT.

In addition to our solid financial results, we made meaningful progress on our strategic transformation toward a more solutions-centric organization. This is demonstrated by our Solutions business expanding more than 20% year-over-year in the second quarter to 35.5% of total revenue. This, as with quarterly revenue, represents the highest mix of Solutions revenue in nearly five years. Our growing mix of Solutions business was a key contributor to the improvement of our operating results in the second quarter.

Within our Solutions business, we are continuing to leverage and build on the growing momentum for our Application Advantage and EIM Advantage solutions. These core global solutions offerings serve as comprehensive platforms, each consisting of a portfolio of complementary services designed to deliver measurable business value and actionable information for CTG's clients. Today, our pipeline of opportunities for both Application Advantage and EIM Advantage remains very solid across hospital and healthcare system clients as well as broader market verticals such as energy and financial services. Building on the significant commercial validation we've achieved to date, we are continuing to make focused investments to further expand our global solutions offerings, including the development of innovative solutions tailored to specific end markets.

In Q2, our Health Solutions business had another strong quarter, generating double-digit year-over-year growth for the fourth consecutive quarter. We are continuing to realize a meaningful return on our investments to expand and fully align CTG's solutions offerings with current trends in the healthcare industry, particularly towards increasing adoption of value-based care.

During the quarter our Health Solutions business gained incremental traction in both North America and Europe. We secured multiple new and expanded contracts with key healthcare system clients in the Northeastern U.S., and we also successfully executed the first go-live implementation of the University of Brussels' Primuz EHR application at a hospital in Belgium. The visibility from this initial commercial ramp in Belgium has been notable as it is now helping to drive increased interest and lower the barriers to commercial implementations by other prospective hospital clients in the region.

Speaking of Europe, CTG's broader European operations continued to meaningfully outperform our service markets through a combination of solid organic growth and the contribution from our previous strategic acquisitions. Collectively, revenue from Europe grew 25% year-over-year in local currency to represent 38% of total revenue. In addition to further expanding the contracted services we provide to European institutions, the team secured a double-digit number of new clients, spanning both Belgium and Luxembourg.

Also during the quarter, we began seeing increased traction on engagements for our DMS, or Disclosure Management System, solutions in the U.K. as well as adjacent European countries. We also continued to be very pleased with the performance of our respective acquisitions in France and Luxembourg, each of which are contributing tangible value to the larger organization. Together they've served to expand CTG's presence and client base in Europe and deepen our penetration of existing market verticals while providing us with a broader portfolio of offerings and increasing our mix of higher margin Solutions business.

The integration of our most recent acquisition, Tech-IT, is progressing well, and we are on-track to substantially complete the remaining integration activities by yearend. Although we are already successful leveraging and benefitting from joint selling efforts on new business and potential expanded engagements, we are still in the early stages of unlocking and realizing the full potential of the respective sales synergies and cross-selling opportunities from both of our prior acquisitions. We currently have dedicated initiatives focused on advancing these synergies and expect to realize growing contribution from these ongoing efforts in the coming quarters.

In our Staffing business, we continued to be focused on a refined and more disciplined sales approach in support of ongoing improvement to operational performance, particularly in North America. As discussed on last quarter's call, we've recently consolidated functions into regional teams led by regional managing directors and also appointed a new executive vice president of North American operations to drive the transformation and improve performance in this area of the business.

Within this new operating structure, we are being more selective on new engagements and emphasizing higher quality revenue opportunities for IT and for professional staffing services. We've also increased our sales teams' focus on middle market companies, and during the quarter we successfully secured several new middle market-sized clients in North America.

Additionally, we continued to be considered for expanded opportunities at key existing clients and CTG was recently selected as one of two tier one IT staffing vendors for a new division at an existing Fortune 500 client. We've meaningfully grown the business we provide to this client over the last year, and we believe this prominent technology services company could ultimately grow to become a top IT staffing client.

Consistent with our strategic shift toward a higher mix of Solutions business, we are continuously pursuing initiatives to better align resources, optimize cost efficiencies and strengthen our sales and delivery approach across the organization. As part of these enterprise-wide efforts, we are also selectively exploring potential opportunities to upsell or convert certain existing staffing services to solutions engagement model. While opportunities to transition a portion of existing staffing services will take time to cultivate and implement, today we are actively laying the foundation to support future strategic staffing engagements as a new potential solution opportunity.

To close out my opening remarks, I continue to believe the expansion of our Solutions business and offerings remains fundamental to our strategy, as we work to replicate the performance and track record achieved within our European business across the larger organization, and increasingly position CTG as a premier, global solutions provider. In addition to delivering value to our clients, Solutions offerings provide the opportunity for a more favorable margin profile, deeper client engagement, and increased client loyalty. As we continue to execute on our strategic objectives, we remain confident that a higher mix of Solutions business will contribute towards sustained revenue growth and increasing improvement to our operating and bottom-line financial results.

I will now turn the call over to John for a detailed review of our second quarter financial results and outlook for the balance of 2019.

John Laubacker. Thank you, Filip. Good morning to all of you joining us on today's conference call. As reported in this morning's press release, consolidated revenue in the second quarter was $100.4 million compared with $97.2 million in the first quarter of 2019, and $92.7 million in the second quarter of 2018. Currency translation had a negative $2.4 million impact on revenue in the second quarter. Billable days in the second quarter were 64, compared with 63 days in the first quarter of 2019 and 64 days in the year ago second quarter.

Solutions revenue in the second quarter of 2019 increased nearly 7% sequentially and 22% year-over-year to $35.6 million or 35.5% of total revenue. As Filip mentioned, this represents the highest mix of Solutions business in nearly five years. The sequential and year-over-year increase in Solutions business was driven by a combination of organic growth in our European and Health Solutions operations and the first full quarter of revenue contribution from Tech-IT.

Staffing revenue in the second quarter was $64.8 million or 64.5% of total revenue, compared with $63.8 million or 65.6% of total revenue in the first quarter of 2019, and $63.4 million or 68.4% of total revenue in the second quarter of 2018.

Revenue from IBM in the second quarter was $21.1 million or 21.1% of total revenue, compared with $20.9 million or 21.6% of total revenue in the first quarter, and $21.9 million or 23.6% of total revenue in last year's second quarter. No other client represented more than 10% of revenue in the second quarter of 2019 or during the comparable periods.

Direct costs as a percentage of revenue were 81.7% in the second quarter of 2019, compared with 81.8% in the first quarter of 2019 and 81% of revenue in the year ago quarter.

GAAP net income in the second quarter of 2019 was $943,000, or $0.07 per diluted share, and included approximately $400,000 in acquisition-related expenses. Non-GAAP net income was $0.09 per diluted share. This compared with GAAP net income of $632,000, or $0.05 per diluted share, in the first quarter of 2019, which included approximately $300,000 in acquisition-related expenses. GAAP net income in the year ago second quarter was $940,000, or $0.07 per diluted share, which included approximately $200,000 in acquisition-related expenses.

The effective income tax rate in the second quarter of 2019 was 36.6%, compared with 33.3% in the first quarter, and 27.9% in the second quarter of 2018.

CTG's total headcount at the end of the second quarter was approximately 4,350, which was the same as the end of the first quarter of 2019 and compared with 4,150 at the end of the year ago second quarter. The year-over-year increase in headcount primarily reflects a combination of the Tech-IT acquisition in February 2019, as well as organic growth in Europe. Approximately 91% of our second quarter 2019 headcount was billable, consistent with the percentage in the comparable periods.

Turning to our balance sheet, cash and cash equivalents at the end of the second quarter were $11.3 million and the company had $17 million of outstanding long-term debt at quarter end. Outstanding debt at the end of the first quarter of 2019 was $13.3 million. The increase in outstanding debt for the first quarter was due to the second quarter ending on a payroll date in the United States.

Capital expenditures in the second quarter of 2019 were $384,000, compared with $283,000 in the first quarter of 2019 and $488,000 in the second quarter of 2018.

Turning to our guidance for the remainder of 2019, following our solid financial results, and continued momentum in the first half of the year, we are providing a narrowed range on the company's previous guidance for the full year 2019, which includes raising the midpoint of our previous guidance for revenue and reaffirming the midpoint for earnings per share. More specifically, we now expect full-year revenue to range from $390 million to $405 million, a $2.5 million increase in the midpoint from previous guidance, and for GAAP net income to range from $0.22 to $0.28 per diluted share. Excluding certain acquisition-related expenses associated with our previously-completed transactions, we expect non-GAAP net income for the full year to range from $0.32 to $0.38 per diluted share.

Consistent with historical trends, we expect third quarter results to reflect—or traditional seasonality and an associated lower utilization rate due to summer vacations, primarily related to our European operations and our U.S. staffing operations. As indicated by our updated outlook for the year, even when considering the seasonal lower utilization in the third quarter, we continue to anticipate significant year-over-year revenue growth and the sustained important of our profitability during the second half of the year, as a result of a higher mix of Solutions business, more selectivity on Staffing engagements and the continued focused execution on operational performance across the organization.

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

Operator. We do have a question from the line of Vincent Colicchio with Barrington Research. Please go ahead.

Vince Colicchio. Filip, on the mid-market staffing projects that you added, was the margin better than your average for staffing? I know that you're trying to get to better margins for the middle market.

Filip Gydé. Yes, we see that in the contracts we are signing with middle market-sized clients, we are realizing what we expected. We have higher margins with those companies.

Vince Colicchio. What's driving the better traction? Is it simply better execution? Have you changed up your targets or what's going on there?

Filip Gydé. Well, Tom Niehaus, as you know who we've recruited, he is focused on improving execution within our Staffing business as we are emphasizing the higher margin opportunities in the middle market. And, the fact that we're landing these several new contracts are proving that we're making progress. Tom is really creating a culture of execution, and I'm confident we'll achieve continued progress in expanding this business.

Vince Colicchio. You talked about the electronic medical record delivery in Europe driving increased interest. Is that a meaningful level of potential new business? What does that pipeline look like?

Filip Gydé. Well, I would characterize these EHRs in Belgium as good opportunities for CTG, but we have to realize that these hospitals in Belgium are not nearly as large as the systems in the States. We do have several implementations lined up and this first one going live successfully accelerates that plan. So, we're of course pleased with this first go-live but this is just one initiative underway to deliver significant shareholder value.

Vince Colicchio. You mentioned that you're pleased with the performance of acquisitions in Europe. Does that mean that the performance has been in line with your expectation? What does that look like?

Filip Gydé. Yes, if you're looking at both of the acquisitions, we're still in the process of fully integrating Tech-IT and to a lesser extent Soft Company, but both of them deepen our penetration of new and existing markets. And, they are really providing the seeds that I was talking about last time around, which we can generate future growth.

We are seeing the first benefits of our Tech-IT implementation, sharing resources, answering joint RFPs, and we have our first contracts that we wouldn't have had if both companies would have continued on their own. So, I cannot be more pleased with these initial successes.

Vince Colicchio. Nice job on the quarter. I'll go back in the queue. Thank you.

Operator. We do have a question from the line of Zach Cummins with B. Riley FBR. Please go ahead.

Zach Cummins. Starting off with a housekeeping item, I don't believe I saw it in the press release, but John, can you provide the quarterly number for depreciation and amortization as well as the equity-based compensation expense number?

John Laubacker. The depreciation and amortization was $690,000, and the equity-based compensation number was $450,000.

Zach Cummins. In terms of the gross margin, I know it was a slight sequential improvement but was still down year-over-year. Was gross margin in line with internal expectations or were there any one-time items or events impacting that line?

John Laubacker. No, it really was in line with where we expected it to be. There weren't really any one-time impacts. I think last year it was a little bit higher. We had really some fantastic things happen in the first half of last year, first quarter, second quarter, maybe offset as you work your way down through the income statement by all the investments we were making to grow the business. But, this year's margin was exactly where we thought it would be. Very happy with the progress that we're making, matching investments and matching improvement to existing results.

Zach Cummins. Understood. Filip, in terms of the Staffing business, it sounds like with the new strategic approach, you're really focused on these higher value opportunities. Does this imply that you're turning down business opportunities that you would have potentially taken in the past now that you're focusing on some of these higher margin opportunities?

Filip Gydé. That is part of the longer-term plan, yes. We're looking at the middle-market-sized clients to deliver a higher margin but we're also looking at our existing clients, like the win we announced this morning, but also in discussing with our long-term existing clients about how we can transition part of that staffing into a managed-services or solutions approach, which is going to yield higher margins if we do apply our expertise in that area.

Zach Cummins. That's all the questions I had thus far. So, thanks for taking the questions and congrats on the strong quarter.

Operator. Gentlemen, it does appear at this time there are no further questions from the phone lines. Please continue.

Filip Gydé. In closing, and as we've conveyed throughout today's call, we made meaningful progress during the second quarter in support of our strategic transformation to more solutions-centric company. I believe we are well-positioned with the right strategy in place to continue growing and expanding our Solutions business.

We also remain committed to ongoing efforts to refine our approach and optimize the performance within our Staffing business, while more broadly continuing to strengthen our sales, recruiting and delivery capabilities throughout the organization. Together with disciplined execution, I'm confident in our ability to maintain our recent positive momentum, achieve sustained profitable growth and generate increased value for CTG shareholders.

We appreciate you joining us on today's call, and your continued support of CTG. We look forward to reporting another quarter of progress on our Q3 conference call in late October.
