Operator. Ladies and gentlemen, thank you for standing by. Welcome to the CTG Quarterly Conference Call. As a reminder, this conference is being recorded. I would now like to turn the conference over to your host, Jim Culligan. Please go ahead.

Jim Culligan. Thank you, Greg, and good morning everyone. With me on today's call are Bud Crumlish, 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, Thursday, October 18, 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 today's earnings press release as well as with the company's filings with the SEC.

Also, the company's press release and management's statements during the call 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 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 this call. I'll begin with a brief overview of our financial results for the quarter.

Revenue for the third quarter increased 22% year-over-year to $90.3 million exceeding our guidance range of $86 million to $90 million. Revenue was better than anticipated primarily due to the ramp up of recently secured health solutions business across multiple new clients, as well as the continued growth in our European operations. Our acquisition of France-based Soft Company earlier this year has further complemented the favorable trends in Europe and we continue to be pleased with the performance of this highly strategic acquisition.

Third quarter earnings per share excluding the gain from life insurance proceeds were in line with our expectations as we continued to reinvest in sales and new business development to drive sustainable growth. Given the notable traction we achieved within healthcare during the quarter, I would like to start by addressing several positive developments in our broader solutions business, followed by commentary specific to the staffing portion of our business.

Revenue from solutions expanded to approximately 32% of consolidated revenue in the third quarter or $28.9 million, reflecting a 32% year-over-year growth. In the year-ago quarter, solutions represented only 30% of total revenue which clearly demonstrates our early success in increasing the revenue contribution from higher-margin solutions business over the last year. In further support of this objective, we are continuing to gain increased traction as positive new market trends emerge, particularly within healthcare.

Speaking of healthcare, I am proud to highlight that *Modern Healthcare* magazine recently recognized CTG as one of the best places to work in healthcare for the fifth time in the last six years. This recognition is a great testament to the strength and culture of our healthcare team, which serves as an important foundation for renewed growth in health solutions.

In fact, our health solutions business in the U.S. had a very strong quarter, highlighted by multiple contract wins for our application advantage offering, as well as the ramp up of previously secured accounts over the past few quarters. We also expanded or extended contracts with 10 existing healthcare clients during the quarter, and most recently expanded the scope of services we're providing to Catholic Healthcare Initiatives, a partnership we announced in July to implement Epic's Electronic Health Record application. Adding to this growing business momentum in health solutions, subsequent to quarter end we also significantly advanced a meaningful new engagement for legacy system support on an EHR implementation with a sizable U.S.-based hospital system. We are actively working to formalize a contract with this new account which we anticipate completion in the fourth quarter.

Overall, total billable headcount within health solutions increased during the quarter as we experienced growing demand for our expanding portfolio of cost-effective solutions. We continue to position many of our current offerings to capitalize on prevailing transition towards value-based care including application advantage, EHR services, and enterprise information management. Across the healthcare industry, providers have a growing need for effective data and information management to improve efficiency and optimize performance. In fact, our recently launched EIM offering is specifically targeted at addressing these acute needs, and we expect to gain additional traction with this solution over the coming quarters.

We are also gaining traction for our EIM Solution outside healthcare in areas such diversified industrials. Our solution's team in Alaska recently secured a new five-year, multimillion dollar contract for EIM with a subsidiary of a large existing energy client. This represents only one example of the broad and growing number of engagements that we are actively pursuing for EIM solutions outside of the healthcare market.

Turning to Europe, the performance of this area of our business continues to be well above the industry average, with quarterly revenue from our European operations growing more than 50% year-over-year. Revenue from Europe expanded to approximately 34% of consolidated revenue, compared with 27% of revenue in the same period last year. In addition to Soft Company contributing to our growing momentum in Europe, our teams in Belgium and Luxembourg continue to generate organic growth through a combination of new and expanded contract wins, most notably with European institutions.

Results from our European operations are also reflective of the current market environment for skilled professionals in the region, which remains extremely competitive. Our above-average retention of highly skilled technical resources is a testament to the dedication of our team in Europe, and our recruiting organization aggressively works to attract quality talent in preparation of the ramp-up of multiple recently secured contracts.

Specific to Soft Company, we made further progress on our integration efforts during the quarter and the acquired business continues to perform well and in line with our expectations. Although it's still early, we have already begun to realize the initial sales synergies as our respective teams in Europe increasingly work together and conduct operations as a combined organization.

To close out my remarks on Solutions, I want to emphasize that our Solutions business has been a key strategic area in which we have invested over the past two years. The proceeds of these efforts are not only increasingly evident in our results, they are also positioning CTG for future growth. As we continue to execute on our expanding pipeline of new business engagements and contracts, we expect to generate further positive momentum over the coming quarters.

Now turning to the Staffing business. Third quarter revenue from staffing grew 18% year-over-year to $61.3 million, representing approximately 68% of CTG's consolidated revenue. This area of our business largely performed as expected during the quarter, including a modest degree of seasonal softness typically associated with the summer months. More broadly, the macroeconomic environment and seemingly resilient economic growth is giving many companies the confidence to increase IT spend, resulting in additional staffing opportunities.

During the quarter, we secured 11 new staffing clients and also expanded services in the new divisions at four existing clients, marking continued progress on our objectives to expand and diversify CTG's portfolio of staffing client. Additionally, the record low unemployment rates in the U.S. are cultivating growing demand for permanent placements. In order to more directly address this prevailing market trend, we have recently assembled our recruiting team dedicated to specific clients. Even though the current revenue contribution is still relatively small, we have already seen a definite increase in the pace of permanent placements as a direct result of this recently implemented effort.

As I mentioned in our previous call, we are up-leveling our sales organization and increasing the effectiveness of our business development activities. As part of these ongoing efforts, we hired two new account executives in the third quarter and made further enhancements to the alignment of our recruiting and delivery teams in key strategic areas. We also made several net additions to our total recruiter headcount during the quarter. In addition to supporting our larger growth objectives, the strategic initiatives in our staffing business will continue to further streamline the organization and drive increased efficiencies.

Before I turn over to John for a more detailed review of the financials, I would like to conclude my opening remarks by emphasizing the consistent and notable progress we are making across multiple areas of the organization. I am especially pleased by the tangible traction we demonstrated during the quarter within health solutions, as well as the continued strong performance of CTG's European operations. As evidenced by our results, our execution is producing meaningful growth and has also enabled us to establish a growing pipeline of new engagements.

We plan to continue reinvesting in the highest performing areas of the business to accelerate the conversion of new and existing opportunities into incremental revenue. Additionally, we are improving the quality of revenue we generate from our staffing services, which together with increased efficiencies will contribute to enhancing our overall profitability.

Now, I'll turn the call over to John for a more detailed review of our third quarter financial results and future guidance.

John Laubacker. Thank you, Bud. Good morning, everyone. We appreciate you joining us today on the conference call. As we reported in this morning's press release, consolidated revenue increased 21.9% in the third quarter to $90.3 million compared with $92.7 million in the second quarter of 2018, and $74 million in the third quarter of 2017. The impact of currency translation on revenue in the third quarter was negligible. Billable days in the third quarter were 63, compared with 64 days in the second quarter of 2018 and 63 days in the year-ago third quarter.

Solutions revenue was $28.9 million in the third quarter of 2018, which was effectively flat compared with the second quarter on a billable days' basis. Year-over-year, Solutions revenue increased 32% reflecting continued momentum in our European operations, as well as the ramp up of several new health solutions engagements in the U.S. during the quarter.

Staffing revenue in the third quarter were $61.3 million reflecting a 3% sequential decline largely associated with seasonality during the summer months. Staffing revenue increased 17.6% year-over-year driven by our largest staffing clients and a continued conversion of new engagements into revenue generating accounts. Revenue from IBM in the third quarter was $19.8 million, or 22% of total revenue compared with $21.9 million, or 23.6% in the second quarter of 2018 and $18.6 million, or 25.1% of total revenue in last year's third quarter. No other client represented more than 10% of revenue during the third quarter of 2018.

Direct costs as a percentage of revenue were 80.8% in the third quarter of 2018 compared with 80.9% in the second quarter of 2018, and 82.4% of revenue in the year-ago quarter. GAAP net income in the third quarter of 2018 was $1.2 million, or $0.08 per diluted share, which included $0.04 per share on acquisition-related expenses and $0.06 per share from a non-taxable gain from life insurance. This compares with GAAP net income in the second quarter of $940,000, or $0.07 per diluted share, which included $0.01 per share of acquisition-related expenses.

GAAP net income in the year-ago third quarter was $40,000, or $0.00 per diluted share, which included unusually high medical costs associated with the company's self-insured plan. Non-GAAP net income in the third quarter of 2018, excluding acquisition related costs and the non-taxable gain from the life insurance, was $900,000, or $0.06 per diluted share, compared with second quarter non-GAAP net income of $1.1 million, or $0.08 per diluted share, excluding the acquisition-related expenses, and $740,000, or $0.05 per diluted share, in the third quarter of 2017, which excluded the unusual medical costs.

As a reminder, we revised how we define and calculate headcount following the acquisition of Soft Company, where we utilize a large number of subcontractors in order to better reflect total billable consultants. Accordingly, CTG's total headcount at the end of the third quarter was approximately 4,150 compared with 4,150 at the end of the second quarter of 2018 and 3,450 at the end of the year ago third quarter. Approximately 91% of our third quarter 2018 head count was billable which is consistent with previous levels.

Turning to our balance sheet; cash and cash equivalents at the end of the third quarter were $10.5 million and we had $3.1 million of outstanding long-term debt. Capital expenditures in the third quarter of 2018 were $610,000 compared with $488,000 in the second quarter.

During the third quarter the company used $1 million to repurchase 178,000 shares of CTG's common stock at an average price of $5.90 per share. At quarter end, we had approximately $7.8 million remaining under the existing repurchase authorization.

Turning to our guidance, total revenue for the fourth quarter of 2018 is expected to be in the range of $89 million to $94 million. Additionally, we expect fourth-quarter GAAP net income to range from $0.03 to $0.07 per diluted share. Non-GAAP net income excluding acquisition related expenses and amortization of intangible assets is expected to range from $0.06 to $0.10 per diluted share. There are 64 billable days in the fourth quarter of 2018, and we anticipate an effective tax rate of approximately 30%.

For the full year 2018, revenue is expected to range from $355 million to $360 million. GAAP net income for the full year 2018 is anticipated to range from $0.21 to $0.25 per diluted share and non-GAAP net income is expected to range from $0.26 to $0.30 per diluted share. At the midpoint of our fourth-quarter guidance, we are on track to achieve our revenue goals for 2018 with strong top-line growth of 19% for the full year.

As Bud indicated earlier, we continue to make focused investments in the highest performing areas of our business which is having a short-term impact on our bottom-line results. We have more work to do in order to improve the mix of higher margin business within staffing, while also increasing the productivity and the pace by which certain investments are materializing in the bottom line results.

Looking forward, our priority is to maximize the return on our strategic investments and deliver improved profitability in the coming quarters as we remain intent on achieving our three-year financial plan in 2019 targets.

With that, we will now open the call for questions. Greg, can you please manage our Q&A session?

Operator. Thank you. One moment please for your first question. Your first question comes from the line of Vincent Colicchio from Barrington Research. Please go ahead.

Vince Colicchio. Could you help us understand the staffing margin, the challenges in terms of impacting guidance for the balance of the year? Any color would be helpful.

Bud Crumlish. Vince, as you know we've grown our larger volume staffing business and with that it's pushing the margins lower, and when you look at the entire mix, we're diligent about growing the higher margin midmarket activities, and we are working on that. But that's really probably the most dramatic thing that's impacting the fourth quarter is the volume that we have with the larger accounts.

Vince Colicchio. Do you think it’s a vertical focus issue? Is it need more sales force in place, anything else?

Bud Crumlish. On the sales force, we're adding salespeople and they take time to ramp up, especially when you're going out to the midmarket accounts; a lot of it is relationship based and although we have direct communication with the buyers of services, relationships just take time to develop. It's a smaller portion of our staffing business, and it's going in the right direction. But it's just certainly taking probably longer than we want, of course, but it's still going in the right direction.

Vince Colicchio. And then IBM, I think I was expecting a bit higher of a number or maybe I was being too optimistic. How did IBM come in versus your expectations? And what does it look like going forward?

Bud Crumlish. We're growing IBM and we've got certainly other opportunities with them. So I feel very positive about not only the relationship but the level of business we're getting. And, as you know, we've been dealing with them for a long time. And we know how to work with them and really make money. Some of the other things that may impact it a little bit is that they had a division that was sold off and some of that revenue that we had considered as IBM before is in a different account. It had to do with the chip business.

Vince Colicchio. Soft Company, I know you had mentioned in the past, if I remember correctly, that you have some existing accounts you think they'd be able to help you gain share at? Is there any chance of that happening in the near future?

Bud Crumlish. Yes, that's working out. We actually got some synergy with a couple of different clients. In fact, Soft Company really helped out on a proposal that we were working on. Because of their contacts—they said we're now part of this larger group with more capabilities—that actually helped us close a deal that otherwise we wouldn't have, and so that's a start. We have some work from Soft Company actually. We brought them into the Belgium area to do some work there for us. So the sales teams are connecting together and really pushing the market in both ways, because we do have different services in different countries, and so we're rolling it out to other clients. So it's going very well.

Operator. Your next question comes from the line of Zach Cummins from B. Riley FBR.

Zach Cummins. Good morning, Bud and John. Congrats on the strong results in Q3. Can you talk a little bit more about some of the factors that are driving the strength in your healthcare business? And some of the potential pipeline opportunities that you see going forward, specifically in North America?

Bud Crumlish. With the consolidation in the healthcare industry, hospitals want to standardize on their electronic health applications. So as more and more hospitals come in under the fold of a larger organization, they want to have consistency and standardization. And that's what we're doing at the Catholic Health Initiatives. And they have multiple hospitals to standardize, so that's certainly been a driver.

There's also a bit of a trend where you put in an application and it typically lasts ten years; at least some applications were put in in 2005-2007 timeframe and it's so complicated now they have to do a complete refresh. They're actually going out for RFPs and putting in a whole new system. So that's driving some activity as well.

I think it also with our Clinical Service Desk as part of the Application Advantage, these are complex systems and it's also an affordability thing, like 24 by 7 just to answer physicians' calls for very critical information at times. We're really good at doing the health and clinical piece and they're looking to us to really kind of take that over. So that's been a really nice growing portion of our business, and we continue seeing that to grow where we actually handle the calls.

For example, say there's a surgery going on and a radiologist is trying to get some information, trying to get a certain MRI or something and they can't get it. They would call one of our people. These are highly skilled people—it's not just a helpdesk—very highly skilled people that actually did implementations themselves, and they walk the radiologist through the system and get them the information they need so they can move on with the procedure.

So those are a couple of the areas. There's also the whole conversion to value based care. And all of our solutions complement value-based care either directly or indirectly, whether it's population health or a lot of things are going to more outpatient-type of services to drive cost on and gain efficiencies, and we're working with our clients on that as well.

Zach Cummins. That's really helpful. In terms of the Q4 EPS guidance, it sounds like there are really some headwinds related to margins in your higher volume staffing business. Can you talk about more of the investments or changes that you need to make to improve the mix of your staffing business going forward?

Bud Crumlish. We're hiring account executives to go after markets where we already have a presence. It's a much smaller portion of our staffing business and it's taken time to really build up the amount of volume to have a significant impact, but we're really going after those smaller ones where we can get to higher margins. And as I mentioned before, it's takes direct relationships and it just takes time. You want everything to happen very quickly, but it takes time to get these solidified so that, as we add more and more people, there's a certain amount of call it an absorption rate so we can add account executives, and maintain our profitability while we continue to push forward in the marketplace.

And we're doing that now. It's taking probably longer than what we want, but it's moving in the right direction. And we're trying to increase that as much as possible with a lot of diligence.

Operator. At this time there are no further questions. I'd like to now turn the call back to the management for closing remarks.

Bud Crumlish. Before closing on today's call, I want to express my well-founded confidence in CTG's ability to achieve both continued growth as well as enhanced profitability. As a result of deliberate execution, we are consistently demonstrating measured progress and significant top-line growth across all areas of our business. In Solutions, our European operations continue to outperform and also experience growing momentum, further enhanced by our strategic acquisition of Soft Company earlier this year.

As I highlighted in my earlier remarks, we are gaining meaningful new traction for our expanding health solutions offerings. And in Staffing, we continue to win new business and are determined to improve the quality of incremental revenue in order to enhance overall profitability.

Looking forward, we remain focused on driving continued top-line growth and increased efficiencies, as well as maximizing the return on investments in support of achieving our financial goals and objectives for 2019.

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