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PRESENTATION

Operator

Welcome to the ICF International second quarter 2016 results conference call. (Operator Instructions)

As a reminder, this conference is being recorded on Tuesday, August 2, 2016, and cannot be reproduced or rebroadcast without written permission from the Company.

And now, I would like to turn the program over to Lynn Morgen, of MBS Value Partners. Please go ahead.

Lynn Morgen - *MBS Value Partners - IR*

Thank you, Vanessa. Good afternoon, everyone, and thank you for joining us to review ICF's second quarter 2016 performance. With us today from ICF are Sudhakar Kesavan, Chairman and CEO; John Wasson, President and COO; and James Morgan, CFO.

During this conference call, we will make forward-looking statements to assist you in understanding ICF's management's expectations about our future performance. These statements are subject to a number of risks that could cause actual events and results to differ materially, and I refer you to our August 2, 2016, press release and our SEC filings for discussions of those risks.

In addition, our statements during this call are based on our views as of today. We anticipate that future developments will cause our views to change. Please consider the information presented in that light. We may at some point elect to update the forward-looking statements made today but specifically disclaim any obligation to do so.

I will now turn the call over to ICF's CEO, Sudhakar Kesavan, to discuss second quarter 2016 performance. Sudhakar?

Sudhakar Kesavan - *ICF International, Inc. - Chairman & CEO*

Thank you, Lynn, and thank you all for participating in today's call to review our second quarter results and discuss our outlook for the remainder of the year.

This was another strong quarter for us in which we executed well across both our government and commercial businesses and built a foundation for substantial earnings growth in 2016.

The second quarter revenue growth was driven by an 8.4% increase in federal government revenues and an 8.9% year-on-year growth in commercial energy business. This growth continued to be supported by both strong state and local revenue comparisons and sequential improvement in commercial digital services revenues.

In the federal space, we posted solid year-over-year increases in each of our key markets, including energy and health, broadly defined, where ICF is recognized for its subject matter expertise, proprietary analytics, and implementation capabilities.

Our trailing 12-month federal government revenues have increased at an average rate of 5.5%, supporting our confidence that we will see mid-single-digit growth in federal government revenues in 2016. This represents an important trend reversal, making 2016 the first year of meaningful growth in our federal business since 2012.

Another area of substantial growth for us in the second quarter was our commercial energy markets business. The increasing number of advisory assignments that we have won, combined with our energy efficiency contract awards, have set the stage for significant year-on-year growth this year and into 2017.

The high-single-digit growth in federal and commercial energy revenues was supported by another quarter of sequential revenue growth in commercial digital engagement services. Solid execution in existing projects, new client assignments, and a growing pipeline of opportunities point to positive second half year-on-year comparisons. John Wasson will provide more details on this in a moment.

Overall, we expect our commercial business revenues to grow at a double-digit rate in the second half of this year, resulting in mid-single-digit growth for the full year or closer to high single digits if you include work done at commercial rates in energy and digital services for state and local government clients.

In terms of profitability, our diluted earnings per share outpaced revenue growth by a factor of almost three in the second quarter, putting us on track to achieve full-year EPS growth that is in line with our guidance range, even after absorbing the impact of the special severance charges related to our international operations.

We are going to celebrate our tenth anniversary as a public company in September, and I wanted to take a minute here to reiterate our strategy over the last 10 years to grow our revenues and earnings.

We have worked diligently to extend our advisory work to gain larger and longer-term implementation contracts. By playing a larger role in our client successes, ICF has grown its revenues and profits. Accordingly, we have built our program delivery and technology capabilities as a way of implementing the advice we give to our clients.

Over the last few years, we have added capabilities to include an ability to help our clients engage with their customers and stakeholders in a very targeted way. This emphasis on engagement, through the acquisition of Olson, is a recognition that all organizations, public and private, need to reach and engage with their citizens, consumers, employees, and stakeholders and are doing so increasingly through digital channels and technologies.

Our analytics work helps us target the right customers and stakeholders, and digital technologies help us deliver the message in the most cost-effective way. Using these technologies to communicate and engage is a critical component of our strategy to broaden our implementation capabilities and make ICF even more central to the success of all of our clients.

As we move ahead into the second half of this year and plan for 2017, we see ICF as having the domain expertise and program implementation tools I mentioned above to continue to capture our share of addressable government and commercial markets.

Since the beginning of 2015, we have gained substantial revenue synergies from combining our digital engagement services with our existing capabilities and cross selling into our commercial and government client base; these synergies including important contract wins with the California Lottery, a Canadian utility regulator, a western US electric utility and, on the federal government side, with the National Institutes for Health and the Centers for Disease Control.

Today, we are looking at opportunities that reflect demand from our utility clients, trends around the consumerization of healthcare, and the US government's priorities around the adoption of emerging digital technologies. We are confident in our ability to expand our digital engagement work and leverage this expertise across our entire client set.

Our strategy has remained focused and consistent all these years. By expanding our implementation tool set, we continue to leverage our strategy work and increase the quantum of our implementation work.

I will now turn the call over to our President, John Wasson, to provide more details on our second quarter operating performance. John?

John Wasson *- ICF International, Inc. - President & COO*

Thank you, Sudhakar. Good afternoon.

As Sudhakar noted, we executed well in the second quarter and had another solid quarter of announced new contract wins, which brought our trailing 12-month contract awards to $1.3 billion, representing a Company-wide book-to-bill ratio of 1.13.

Our business mix was the same as the prior quarter. US federal government accounted for 49% of total revenues; commercial and state and local were 34% and 11%, respectively, of total revenues; and international government accounted for 6% of total Q2 revenues.

Second quarter revenues from our commercial clients increased 3.5% year over year and, as we expected, showed considerable improvement over first quarter levels, with an increase of 6.4% sequentially. Digital services and energy markets together accounted for 76% of commercial revenue, similar to previous quarters.

This was a very strong quarter for our commercial energy markets business, comprised of both our energy efficiency and energy advisory work, which posted an 8.9% revenue increase compared to last year's second quarter.

Key contract wins announced in the quarter included three programs with Kansas City Power and Light to support residential energy efficiency programs, for a total combined value of $11 million; two contracts worth $4.8 million to support environmental planning and safety for a major utility in the west; and a $4.1 million contract with a utility in the western US to provide social listening tools and other digital services.

In last quarter's call, we mentioned that we had won over $200 million of energy efficiency work as of the date of the Q1 call. Today, year-to-date total energy efficiency wins stand at over $300 million. While we have not been able to publicly announce many of these contracts yet due to certain contract formalities, we have begun work on part of the largest contract under an authorization to proceed and expect to announce it shortly.

Our commercial energy advisory business also maintained its robust growth in revenues, sales, and pipeline in the second quarter. The fast pace of change in power and gas markets is a positive for our business, as clients look for trusted advisers with market, technology, and policy expertise.

As wholesale power prices tumble, our team is helping distressed asset owners restructure and realign their portfolios. To take advantage of low natural gas prices, electric and gas utilities are turning to ICF to help identify and support buying and building new gas infrastructure. And our innovative demand side resource practice continues to help utilities create grid modernization strategies and meet the increasing demands of regulators seeking to enable the next-generation electrical network.

Turning to ICF Olson, it showed modest sequential revenue growth in line with our expectations, as we continue to see that business steadily improve. As noted in our release this afternoon, we won an $8.1 million contract to support digital communication and social marketing with a major healthcare company; a $5.3 million contract for customer loyalty with a Fortune 500 company; a $2.1 million contract for customer loyalty solutions with an international retailer; and a $1.6 million contract to support website operations for a mortgage company. These wins highlight the broad range of services that ICF Olson offers clients in diversified industries.

Last quarter, we mentioned the joint project that ICF Olson has undertaken with our energy practice, working together on a multimillion dollar project for a utility client on marketing, education, and outreach and communications to encourage conservation. ICF Olson leads the marketing and communications portion of the campaign, and I am pleased to report that the client has both expanded the scope of this assignment and extended the term. In addition, we have recently been asked by them to submit our qualifications to become their agency of record.

The ICF Olson pipeline continues to grow in key sectors, including financial services, hospitality and food services, lottery, and distribution of retail. But it is also growing in energy, aviation, and healthcare, which represents an emphasis on cross-Company collaborative bidding.

To date this year, our largest new account wins have been collaborative bids across our commercial businesses. For instance, ICF Olson is collaborating with legacy ICF businesses on a number of sizable projects, including a large statewide utility marketing campaign and a North American tourism marketing opportunity.

Lastly, ICF Olson continues to pursue additional lottery opportunities and currently has seven of them in the pipeline.

Revenues from US federal government clients increased 8.4% compared to last year's second quarter and were up 8.2% sequentially from the first quarter, representing execution on over 1,000 contracts across a broad range of primarily civilian agencies, most notably the Department of Health and Human Services, which includes the Centers for Disease Control and the National Institute of Health, and the Departments of Energy, Transportation, and Education, and the Environmental Protection Agency.

We had two very large wins with the federal government in the second quarter. The first was a $65.7 million, five-year contract with a federal financial services agency to provide advisory and professional services to support the development of a business strategy, as well as manage existing and future agency programs and projects.

The second was a single-award task order of up to $60 million over 10 years with the National Institute of Environmental Health Sciences, through which ICF will provide scientific and technical expertise to help manage scientific information, and we will develop literature-based evaluations related to environmental substances and other sources of public health concerns. This award taps ICF's 30-plus years of experience conducting chemical safety and risk assessments to help federal clients make informed decisions regarding chemical safety, as well as implement measures designed to protect the public health.

Other notable federal contact wins in Q2 included an $11.2 million contract with HUD to support an integrated technical assistance and capacity building initiative; a $9.6 million contract with the Social Security Administration to maintain and improve its security processes and oversight of offices nationwide; an $8.4 million contract with the Department of State to provide information planning and management services for the Bureau of International Narcotics and Law Enforcement; and a $4.8 million task order by the CDC National Center for Injury Prevention and Control to oversee the development of a large-scale targeted communications campaign designed to raise awareness about the risks associated with prescription opioid abuse. As part of this project, ICF will oversee the development and placement of digital and social media ads and maintain an active social media presence for the campaign, leveraging the significant qualifications and expertise that reside in ICF Olson.

US state and local government revenues grew by 16.7% in the second quarter and were up 6.3% sequentially, reflecting a stronger start to the year than we originally anticipated. The increased level of state and local activity was driven by significantly higher passthroughs on several infrastructure and environmental assessment projects, as well as state energy efficiency projects. We now expect our state and local business to grow by double digits for 2016, primarily due to higher passthrough revenues.

Turning lastly to our international business, while revenues were up 13.7% sequentially in Q2, they were down 14.4% from Q2 of last year. As we have discussed in recent earnings calls, implementation of new projects within our largest client in the European Union have been delayed due to issues associated with the migration crisis, security concerns, and with the Brexit vote that occurred at the very end of Q2.

Given these issues, we are now forecasting our international business to shrink by high single digits during the second half of this year. We have taken steps to manage the cost structure of this business, as evidenced by our severance charge this quarter, and we'll continue to manage the business proactively through the remainder of the year.

Let me end by providing you an overview of our business development performance and employee turnover metrics.

Our pipeline was a record $4 billion at the end of the second quarter, after winning $620 million in awards in the first half of the year. The pipeline included 31 opportunities greater than $25 million and 71 opportunities between $10 million and $25 million.

Finally, our year-to-date domestic turnover rate was 6.5%, which translates into an annualized rate of 13.1%.

Now, James Morgan, our CFO, will continue with the financial review. James?

James Morgan - *ICF International, Inc. - EVP & CFO*

Thanks, John. Good afternoon, everyone.

As anticipated, our second quarter results represent sequential and year-over-year improvement in both revenue and earnings. Revenue was $305.4 million for the quarter, an increase of $16.5 million, or 5.7%, over last year's second quarter, driven primarily by growth in work with the federal and state and local government clients and the pickup in revenues from commercial clients, particularly in energy markets.

Service revenue increased 3.2%, to $222.4 million.

Gross profit increased in the second quarter of 2016 by $0.5 million as compared to 2015.

Gross margin decreased from 38.3% in the second quarter of 2015 to 36.4% in the second quarter of 2016, mainly due to a higher mix of passthrough revenues, primarily from government clients, which negatively affected the 2016 Q2 gross margin by an estimated 60 basis points, and severance charges that reduced gross margins by about 30 basis points. And as expected and discussed during our last earnings call, the start-up and implementation phases of certain contracts continued to impact gross margins in Q2, but we expect this impact to decline through the remainder of the year.

Indirect selling expenses for the second quarter were $84.6 million, a $0.9 million year-over-year increase, but a reduction as a percentage of revenue, to 27.7%, in this year's second quarter, from 29% in the second quarter of 2015. This reduction in indirect expenses as a percentage of revenue was mainly driven by year-over-year improvement in staff utilization. For the full year of 2016, we expect to continue effectively managing our indirect costs and selling expenses.

Operating income was $19.4 million in the second quarter, up 3.3% compared to the prior year. Operating income was reduced in the second quarter by $1.1 million in special charges related to international severance and office closures. Without these special charges, operating income would have been $20.5 million in this year's second quarter, up 9.4% compared to last year's second quarter.

Depreciation and amortization expense was $4.1 million, up from $3.9 million in 2015's second quarter.

As expected, due to certain intangibles from our prior acquisitions' becoming fully amortized, amortization of intangibles decreased from $4.3 million reported in 2015's second quarter to $3.1 million in the second quarter of 2016.

The effective tax rate was 37.2% for the quarter, compared to 39.1% in the second quarter of 2015. The 2016 second quarter effective rate was favorably impacted by true-ups to prior year tax returns and state tax credits and the early adoption of new accounting guidance, referred to ASU2016-09, which relates to tax benefits for stock-based compensation.

The early adoption of ASU2016-09 also retroactively impacted our 2016 Q1 effective tax rate, causing it to be reduced from the previously reported 37.6% to 36.3%. As a result, our previously reported 2016 Q1 diluted earnings per share increased by $0.01, to $0.51 per share.

Due to the adoption of ASU2016-09, we now expect a full-year tax rate of no more than 38%.

Net income was $10.6 million, an increase of $1.4 million, or 15.4%, over the second quarter of 2015.

Reported EBITDA was $26.6 million for the quarter, inclusive of the $1.1 million special charges previously mentioned, and similar to the $26.9 million reported in last year's second quarter.

EBITDA margin was 8.7% for the quarter, compared to 9.3% for the second quarter of 2015. In aggregate, the higher passthrough revenues and special charges reduced our 2016 second quarter EBITDA by approximately 50 basis points.

We expect our EBITDA margin to be in the range of 10.5% to 11% for the second half of the year. And as a result, for the full year of 2016, after considering the year-to-date passthrough revenues and special charges, we anticipate our EBITDA margin to be in the range of 9.7% to 10%.

Reported net income was $10.6 million for the quarter, or $0.55 per diluted share, compared to $0.47 in last year's second quarter, an increase of 17%.

Non-GAAP EPS, which excludes amortization of intangibles as well as costs related to severance for international staff realignments, office closures, and acquisitions, was $0.69 per diluted share for the second quarter, as compared to $0.63 in the prior year, an increase of 9.5%.

For the first half of 2016, we reported cash provided by operating activities of $15.7 million, a $10.7 million increase over the $5 million reported in the first half of 2015.

Day sales outstanding for the second quarter were 74 days, as compared to 73 days at the end of 2015. We continue to anticipate the year-end DSO to be in the 72 to 77 day range, including the impact of deferred revenues.

Capital expenditures for the first half of 2016 were $9.8 million.

We repurchased 243,117 shares year to date at an average price of $36.09 per share. As a result, we have more than achieved our previously stated intention to, at a minimum, make share repurchases in 2016 at a level to offset the dilution caused by our employee incentive programs. Per-share guidance for 2016 assumes weighted average diluted shares outstanding of approximately 19.4 million.

Additional full-year 2016 guidance for financial modeling purposes is as follows. As mentioned previously, we expect 2016 EBITDA margin to range from 9.7% to 10% for the full year of 2016. We expect depreciation and amortization expense in the range of $17 million to $18 million for 2016. We expect amortization of intangibles between $12.3 million to $12.8 million, for a tax-affected impact of approximately $0.40 per share. Full-year interest expense is expected to be in the range of $8.5 million to $9.5 million. And as I mentioned earlier, we expect the full-year tax rate to be no more than 38%. And full-year cash flow from operations is projected to be in the range of $85 million to $95 million for 2016.

With that, I'd like to turn the call back to Sudhakar.

Sudhakar Kesavan - *ICF International, Inc. - Chairman & CEO*

Thank you, James. We are pleased with our second quarter results and the improved visibility we have gained over the course of the first half of this year. As noted in today's release, as a result of the higher passthrough revenues we had in the second quarter we now expect that our full-year revenues will come in at the high end of our initial guidance range of $1.15 billion to $1.19 billion, and we maintained our diluted EPS guidance range from [$2.40] (corrected by company after the call) to $2.55 per share, including the impact of second quarter severance costs, and our non-GAAP EPS range remains unchanged at $2.79 to $2.94.

At the midpoint, these guidance metrics point to a year of strong performance for ICF, in line with our initial expectations for 2016.

As I said earlier, we will celebrate the tenth anniversary of ICF's listing on September 20 of this year by ringing the opening bell at the NASDAQ, and that afternoon we will be hosting a meeting in New York for investors and analysts to interact directly with members of our executive leadership team and discuss the drivers of ICF's future growth. Invitations will be sent shortly. We hope you will be able to join us.

Operator, now I would like to open the call to questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Bill Loomis, Stifel.

Bill Loomis - *Stifel Nicolaus & Company - Analyst*

Good results. Sudhakar or James, can you just clarify one thing? Because on the second half revenues, you said international revenues will shrink in the high single digits in the second half. You talked about state and local will grow by double digits in 2016. I'm just a little --. I just want to make sure I'm talking -- are you talking second half or are you talking full-year 2016 when you talked about how each of the segments would grow?

James Morgan - *ICF International, Inc. - EVP & CFO*

I can go through that. So, looking at it from a full-year perspective, it's actually consistent on international government. We're saying that it's going to shrink in the second half high single digits, and for the full year it will be down high single digits also for international government, Bill.

And then, on state and local, we're looking at having double-digit growth for the full year.

Bill Loomis - *Stifel Nicolaus & Company - Analyst*

Okay. And then, on the international, how long --? Obviously, you expect high single digit. First of all, what was the currency impact on that? And what's going to change? Is this just going to be time? Is there --? You've talked in the past about how election cycles have impacted work over there. Where do you see the horizon on when the business will turn internationally?

James Morgan - *ICF International, Inc. - EVP & CFO*

So, I can talk to you real quickly about the currency impact. If you look at our currency impact on a year-to-date basis, it's roughly a little over $1 million; about $1.2 million.

And then, we're anticipating for the full year that --. The numbers that we're giving you with regard to the growth rates, it's based on the exchange rates as of the end of July. So, it takes into account what's happened to the pound subsequent to Brexit. And we have about another $2 million, or so, of impact associated in the back half of the year baked into our forecasted numbers.

Bill Loomis - *Stifel Nicolaus & Company - Analyst*

Okay. And then, just the timing on what dynamics you expect could turn the international?

John Wasson - *ICF International, Inc. - President & COO*

Sure. So, this is John Wasson, Bill. I think as we've talked about in prior calls, I think we have seen slowness in activation of work with our largest client, the European Commission, over the last couple of quarters, certainly with the migration crisis, some of the security concerns.

I would say in the last month we've seen that trend continue and are continuing to see slowness and even more slowness than we expected. Obviously, the Brexit vote occurred towards the end of Q2.

And so, I think we're thinking that for the rest of this year we're going to continue to see this slowness in activation, and it's certainly going to impact us in the second half of the year. We have some early indications from clients that things will start to ramp up later in the year and as we go into next year. But certainly, things have been slow and if have anything gotten slower in the last month in terms of activation of new work with the European Commission.

So, we're monitoring it carefully, but we definitely -- we've seen a slowdown. And so, I think it's slowing down. We're hopeful as we get towards the end of the year it will pick back up.

Bill Loomis - *Stifel Nicolaus & Company - Analyst*

And the cost reductions on the international that you're taking the charge for, was that office closures? Or, is it people? Or, can you detail that (multiple speakers)?

John Wasson - *ICF International, Inc. - President & COO*

It was primarily people. A small portion was office closures, but it was primarily people in Europe.

James Morgan - *ICF International, Inc. - EVP & CFO*

Yes, right.

Bill Loomis - *Stifel Nicolaus & Company - Analyst*

Okay. Thank you.

Operator

Tim McHugh, William Blair & Company.

Tim McHugh - *William Blair & Company - Analyst*

Just wanted to ask about the digital interactive space. I guess you gave some good kind of anecdotal or various data points on it, but can you talk about the visibility to the improving trends in the second half of the year? And I apologize if I missed it in your comments, but just the different pieces and specifically, I guess, the brand piece for that? Are you comfortable that that piece of legacy Olson is ramping back up still?

Sudhakar Kesavan - *ICF International, Inc. - Chairman & CEO*

Sure, Tim. I think the pipeline is strong. It's the strongest it has been over the last year or so. So, given the high velocity of the work, pipeline is a reasonable indicator, especially if you have something in the pipeline it gives you a sense that --. So, the pipeline is one indicator.

And I think to answer your question on brand, as I have said, the run rate in the first half of the year is way ahead of what it was in the last half of the year, especially last quarter of last year. So, I think brand is continuing to improve. And so, we are optimistic that it will continue to do so in the rest of the year.

John Wasson - *ICF International, Inc. - President & COO*

And I think, Bill, if I could just add, it's almost -- I mean, Tim. I think some of the cross-collaborative opportunities I talked about in my script, primarily in the energy space and in the lottery arena, are benefiting or will benefit -- have benefited and will continue to benefit the brand business. And so, I do think that we are certainly making progress on the pipeline for some material opportunities.

Tim McHugh - *William Blair & Company - Analyst*

And I guess just to follow up on that, besides that -- and you talked about kind of cross selling -- has the market changed? You sense the market changed? Do you feel like --? I know you've been spending time on just the sales approach and the sales model. I guess, what do you think is really working, I guess? Or, is it just getting back to what you would expect the business to normally perform at in digital?

John Wasson - *ICF International, Inc. - President & COO*

Well, I guess I would say a couple of things. I think we have brought in new talent into the business, in the brand business. We brought in two, three, four senior staff who I think are making a difference in kind of building out the pipeline and driving the sales process.

And then, I think we are finding -- again, in energy, in aviation, and in lotteries -- that we can cross sell and kind of marry either the subject matter expertise or our longstanding relationships in those industries with the Olson capabilities and cross sell there. And so, I think that's also been an important part of improving the brand business and improving the pipeline.

Tim McHugh - *William Blair & Company - Analyst*

Okay. Great. Thank you.

Operator

(Operator Instructions) Kevin Steinke, Barrington Research.

Kevin Steinke - *Barrington Research - Analyst*

So, good to see you increased the guidance for the federal government business to a mid-single-digit rate for the year. So, I'm just trying to get a sense for what enabled you to increase that outlook? Is it just a matter of some of the new contracts that you discussed are coming in and are going to help the growth? Or, I know you had talked about some contracts winding down in the second half. Is that still what you expect? Just any more color on the federal government outlook would be helpful.

John Wasson - *ICF International, Inc. - President & COO*

I would say a couple of things. I think we continue to see our civilian clients showing a willingness to spend their budgets and begin new programs, begin new initiatives. And so, I think obviously the results are a reflection of that. We continue to see significant proposal activity in the federal space.

And so, we've sustained and obviously increased a bit here in the second quarter the revenue growth in the federal space now for several quarters. And so, I think given that and given that record, we're comfortable moving it to mid single digits.

It's still -- that guidance does assume that we will roll off the couple of contracts we talked about in our call last quarter. There are a couple of contracts that will roll off. And so, that's still baked into the guidance. But I think we're comfortable given the general trends we see and the performance of the business that we can achieve mid single digits for the year.

Kevin Steinke - *Barrington Research - Analyst*

Okay. That's helpful. And the strength in state and local that you saw and the higher passthrough revenues, I assume those are -- was that business that came through since you last provided guidance? And so, is that something new or different that caused you to just tweak down the EBITDA margin guidance a little bit?

John Wasson - *ICF International, Inc. - President & COO*

I would say on the state and local work, these are primarily kind of large implementation projects: high-speed rail, environmental assessment, a few state energy efficiency projects. And frankly, we just had more intense efforts on those projects over the last quarters that have required us to use subcontractors and have other passthroughs in a more intense way than we planned.

We don't tend to make the same markups on passthroughs as we do on business that we're deploying our staff on. And so, we certainly saw more passthroughs and had more intensive efforts on these state-level implementation contracts in Q2, and it does contribute to the slightly lower margins.

Kevin Steinke - *Barrington Research - Analyst*

Okay. That makes sense. And the energy markets business, up 8.9% in the second quarter, is that growth picking up a little faster than you expected? I think last quarter you talked about getting to double-digit growth in the second half of the year in energy markets. So, is that still kind of the expectation? Are we seeing things roll out as planned, a little more quickly than planned? Or, just any comments on the nice growth in the second quarter and the outlook for the second half of the year.

John Wasson - *ICF International, Inc. - President & COO*

I would say it's generally rolling out as planned, although we have won quite a bit of energy efficiency work, as we've talked about this quarter and last quarter, and our energy advisory work is really booming. And so, we certainly expect to see very robust double-digit growth in the second half of the year. And so, if anything, we've become even more optimistic about our growth opportunities in the second half of the year in the energy space. It's really --.

James Morgan - *ICF International, Inc. - EVP & CFO*

And into next year.

John Wasson - *ICF International, Inc. - President & COO*

-- quite robust. And given the visibility on energy efficiency, into next year.

Kevin Steinke - *Barrington Research - Analyst*

Right. Okay. Yes. That's good. And so, digital services, revenue up sequentially. Can we still assume that it was down a little bit maybe year over year but still expecting to ramp to year-over-year growth in the second half? Maybe kind of in that high-single-digit range?

Sudhakar Kesavan - *ICF International, Inc. - Chairman & CEO*

I think that as you point out, Kevin, it was down on the H1 to H1, where we certainly expect it to improve in the second half of the year where the sequential growth will continue. So, I do think that we will have sequential growth right through Q3 and Q4. So, H2 should certainly be better than H1 for our digital business.

Kevin Steinke - *Barrington Research - Analyst*

Okay. Great. Well, thanks for taking my questions.

Operator

Tobey Sommer, SunTrust.

Tobey Sommer - *SunTrust Robinson Humphrey - Analyst*

Speaking of the momentum in the energy markets headed into 2017, do you see in front of you a steady or increasing amount of work to be bidding on as we look into 2017, and therefore --? Or, is your comment more related to harvesting the new bids and the wins that you've already achieved so far this year?

John Wasson - *ICF International, Inc. - President & COO*

Well, I would say we'll certainly harvest the wins we've won this year, and it's obviously going to drive the growth in the latter half of 2016 and into the first half of 2017.

I would say we do still have a robust pipeline of energy efficiency opportunities. And so, I think there is a strong pipeline there that gives us confidence that we will win additional new contracts as we go into 2017 and can sustain quite strong growth there.

And I just would say that, again, the energy advisory piece of the business is really quite strong and, if anything, has been accelerating, both around the issues we've talked about in the past: distributed energy resources, grid modernization. We are also seeing a lot of asset valuation and restructuring opportunities around some of the volatility of commodity prices, and some of that has been litigation, which tends to be quite profitable for us, litigation support.

So, I think that the trends on the advisory side are also quite good and give us -- while the pipeline, we don't have quite as long visibility, given it's an advisory business, the trends have been very strong, Tobey, and I think we really do have confidence we can really drive growth in that business as we go into 2017, too.

Tobey Sommer - *SunTrust Robinson Humphrey - Analyst*

Thank you for that color, particularly on the advisory business. Just to make sure I have the numbers accurate, John, did you say that year to date you have $300 million in new business, versus $200 million?

John Wasson - *ICF International, Inc. - President & COO*

$300 million of new contract awards, year to date through this call, where we've been informed -- either we've signed contracts or we've been informed that we've won and are in final contract negotiations. And that's up from $200 million (multiple speakers).

Tobey Sommer - *SunTrust Robinson Humphrey - Analyst*

Okay. So, that would compare to the (multiple speakers) of the last quarters?

John Wasson - *ICF International, Inc. - President & COO*

It would compare to the $200 million we discussed, I think, at our call last quarter.

James Morgan - *ICF International, Inc. - EVP & CFO*

Right.

Tobey Sommer - *SunTrust Robinson Humphrey - Analyst*

Okay. Thank you. And are --? The passthroughs that you called out and, I guess, discussed a little bit earlier, is that something that's going to come up a little bit more in the business? Is there some sort of change? Or, is this really a one-off? Because I don't recall this being a [common] feature of your quarterly reports.

John Wasson - *ICF International, Inc. - President & COO*

It has not been a [common] feature. I think we are in some pretty intensive and higher-than-expected efforts on a few of these state and local contracts, which has driven this. And so, I wouldn't call this a trend. We've had one quarter of intensive and higher passthroughs. I think we are thinking they will be somewhat higher for the rest of the year, but it won't be at this level.

And so, I wouldn't call it a kind of a -- the intensity we've had in the second quarter the expectation, going forward.

James Morgan - *ICF International, Inc. - EVP & CFO*

Right.

John Wasson - *ICF International, Inc. - President & COO*

I don't know, James, if you want to --?

James Morgan - *ICF International, Inc. - EVP & CFO*

No. I think that's right.

Tobey Sommer - *SunTrust Robinson Humphrey - Analyst*

James, a question for you, since I heard your voice. Just the comment that you made about the tax rate of no greater than 38% for this year. Is that a decent rule of thumb for next year, as well? Or, is it too early to make a comment on that?

James Morgan - *ICF International, Inc. - EVP & CFO*

It's probably a little bit too early, but I would suspect that it's not going to be much different than where we started this year, where we said 38.5%. So, it's certainly not going to be dramatically different than that. We don't expect it to be.

Tobey Sommer - *SunTrust Robinson Humphrey - Analyst*

And then, from a broad perspective, John, I think you mentioned the turnover numbers, around 13% annualized domestic. What's the esprit de corps like at the Firm, now that you kind of seem to have re-accelerated growth and have an outlook because of the contract wins for that to sustain itself for a period of time? Would you expect that turnover maybe even to inch down a bit?

John Wasson - *ICF International, Inc. - President & COO*

Well, I would say, as we've discussed many times, I think our turnover rates have tended to be some of the lowest in the industry, in our comparative group.

Obviously, I've talked about -- we've talked about -- we have a strong culture. We're a growth Company. We want to provide people opportunity. Obviously, to the extent that we're actually achieving all those results and growing more rapidly, we'll certainly be able to provide more opportunity, more interesting work for people.

And so, I think to your point it is a positive trend, and it certainly helps us keep the turnover rates down that we're accelerating growth and, frankly, certainly working on a lot of the leading issues of the day in the energy and other sectors we work in. And so, I think it should certainly help keep it low, if not reduce it, Tobey.

Tobey Sommer - *SunTrust Robinson Humphrey - Analyst*

Okay. Two last questions for me, and I'll get back in the queue. One relates to kind of bid and proposal dollars and activity. With the revenue growth that you've got now and kind of with an eye towards fueling that momentum, Sudhakar, do you feel like you're spending enough on bid and proposal to keep the momentum as we head into next year?

Sudhakar Kesavan - *ICF International, Inc. - Chairman & CEO*

One thing we should have never done is cut back on the bid and proposal activity. We basically, unlike some other firms, tend to be much more -- we invest enormous amounts on bid and proposal. So, I think we'll continue to do that.

We also, as I've mentioned before, are continuing to strengthen our whole marketing and sales setup. We hired Colette LaForce. She joined us as the Chief Marketing Officer. She has a very distinguished track record of helping us set up our whole branding and generally help us with marketing and sales broadly across the Firm. So, I think that's something which we are investing in, and we're bringing other people on board.

So, I think we are quite committed on making sure that we take the appropriate marginal dollar and invest it in sales efforts. And as I've mentioned before, on the commercial sales side we're also in the process of making sure that it works like a machine, as we think it does on the federal and state and local side.

So, I think that we -- and I think we are quite focused on that and on our brand. We will, if you'll join us in September, September 20, in New York City, we will talk to you about how we are trying to make sure that we make our brand more visible and what the brand story is and how that -- and I think generally developing the brand.

I think it's also going to help us, going forward, given that we have some scale and people talk about ICF as the biggest company they don't know. So, I think we want to hope to change that and make sure that that, in itself, has some elements of success in terms of business developments, et cetera, we think.

So, I think that we are quite focused on investing in the whole marketing, sales, and branding effort, with caution but with quite a bit of focus. So, I'd encourage you to join us in September to hear about what we have done and what we intend to do, going forward.

Tobey Sommer - *SunTrust Robinson Humphrey - Analyst*

Okay. I'll take you up on that. Last question from me, on the state and local government revenue, up 17%. I guess that's probably influenced by some of the passthroughs that you talked about. So, I don't know how you could adjust for it exactly, but what kind of might be an underlying rate of growth, excluding or adjusting for some of those above-average passthroughs?

John Wasson - *ICF International, Inc. - President & COO*

That's a tough question. I would say --. We're basically saying double-digit growth, obviously, with the passthroughs. I would say kind of maybe mid-single-digit growth to maybe high-single-digit growth without the passthroughs.

Tobey Sommer - *SunTrust Robinson Humphrey - Analyst*

Okay. That's helpful. Just looking for a [range].

John Wasson - *ICF International, Inc. - President & COO*

(multiple speakers). The passthroughs were certainly material this quarter.

James Morgan - *ICF International, Inc. - EVP & CFO*

Right.

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Tobey Sommer - *SunTrust Robinson Humphrey - Analyst*

Great. That's helpful. Thank you very much.

Operator

Marc Riddick, Sidoti & Company.

Marc Riddick - *Sidoti & Company - Analyst*

I wanted to get a sense of on the digital marketing side if there was any historical seasonality to the business? And if so, if that's something that you would expect to continue now under the umbrella of ICF?

Sudhakar Kesavan - *ICF International, Inc. - Chairman & CEO*

I think that the sense we have is that it's actually the first quarter is a little slower than the other three quarters. So, I think that it tends to be first quarter slower and then the others are pretty similar, is my sense.

James Morgan - *ICF International, Inc. - EVP & CFO*

I think that's right.

Sudhakar Kesavan - *ICF International, Inc. - Chairman & CEO*

Based on what I've --. I think usually what happens when people come back from holidays, there's less activity in the first quarter than there is in two, three, and four in the calendar year. So, I think that is the seasonality we've seen. It's not much, but there is some, some of that.

John Wasson - *ICF International, Inc. - President & COO*

I don't think there's significant seasonality, but I agree. Q1 tends to be a little slower. We're getting our retainer, typically getting our retainers in place late in Q4/early in Q1 for the next year.

James Morgan - *ICF International, Inc. - EVP & CFO*

That's right. There's not a lot of variation beyond that.

Marc Riddick - *Sidoti & Company - Analyst*

Okay. And is that somewhat similar as far as new contracts up for bid or new competitive opportunities? Should we view that as kind of middle of the year where a bulk of that would take place?

John Wasson - *ICF International, Inc. - President & COO*

Again, I would say it's kind of typical to what we just described for the revenue. We don't see the same seasonality in the commercial digital business as we do on the government side, where Q2 and Q3 tend to be a lot higher, both in terms of revenue and sales.

Again, I would say that Q1 typically is we're getting the retainers in place. Other than that, it's generally slowest on revenue and bidding, and then it kind of --.

Sudhakar Kesavan - *ICF International, Inc. - Chairman & CEO*

And I think, Marc, Q3 and Q4 perhaps will be the strongest in terms of new contracts and bids.

James Morgan - *ICF International, Inc. - EVP & CFO*

Yes, I think so.

Marc Riddick - *Sidoti & Company - Analyst*

Okay. And do you get a sense that the governmental clients compared to commercial clients when it comes to digital offerings, are you getting a sense that that behavior is somewhat getting to be somewhat similar, as far as how you're working with them currently? Or, are there meaningful differences that you're running into that maybe you either expected or didn't expect to see when ICF Olson was first brought in?

Sudhakar Kesavan - *ICF International, Inc. - Chairman & CEO*

I think the government clients tend to procure in very similar ways. They have changed some procurement processes where they have accelerated, sort of, challenges -- they call them challenges -- and you do some project very quickly and you bid on it.

So, I think they have changed a little bit (inaudible), actually. They're trying to make it a little quicker. But I think broadly speaking the contracting mechanisms are very similar to our traditional work in the government space, and I think they procure digital in sort of broadly the same way, with some, a few, twists which we've seen.

But I think generally their projects tend to be larger and longer than the commercial ones. And I think that they are -- what they are trying to do is make the process of acquisition quicker than what has been the case in the past.

So, there's not a dramatic change, but there's some change in that process. But I think the contracting mechanisms have stayed exactly the same.

Marc Riddick - *Sidoti & Company - Analyst*

Okay. Great.

John Wasson - *ICF International, Inc. - President & COO*

I would just add -- this is John Wasson -- I would say that we've been pleasantly surprised, quite pleased with the types of opportunities we've seen in the federal space around our, the digital work, both from our more legacy kind of marketing and communications and digitally oriented federal business and, with the Olson acquisition, the additional skills and capabilities they bring into the Company. And I think we've announced several of those contracts over the last several quarters, obviously with a significant health focus, Veterans Administration, other. We certainly are seeing some very nice opportunities in the federal government on the digital side.

Marc Riddick - *Sidoti & Company - Analyst*

Okay. That sounds great. I appreciate it. Thank you very much.

Operator

(Operator Instructions) Bill Loomis, Stifel.

Bill Loomis - *Stifel Nicolaus & Company - Analyst*

Just a quick one on margins, on gross margins. So, if you take the two adjustments you talked about, James, the passthrough impact and then the charge that impacted a portion that went into gross margin, that was 90 basis points. But if we add that back, it's still about 100 basis points lower than a year ago. Why is that? And what's dragging that down?

James Morgan - *ICF International, Inc. - EVP & CFO*

It's really -- the biggest driver is what we talked about during Q1, and I mentioned it's we do have some fairly sizable implementation programs that started up in the first half of this year kind of across the business -- some in the 1to1 business and quite a bit in what we consider our business process outsourcing business -- that have had quite a bit of an impact on our gross margins. That's really the largest driver.

I would say there is certainly north of 50 bps associated with that, probably close in the range of 60 to 70 bps is what we estimate. So, that's the other big impact there.

I will tell you that the implementation phases of those programs are, for the most part -- have ended as of where we are [at state] today.

John Wasson - *ICF International, Inc. - President & COO*

(inaudible). It's really the startup phase.

James Morgan - *ICF International, Inc. - EVP & CFO*

It's the startup phase of the work. And so, that's why we expect to see a pretty significant change in the back half of this year versus the first half.

Bill Loomis - *Stifel Nicolaus & Company - Analyst*

Okay. And then, what's the international doing to the gross margin, with that business declining? Kind of what impact did it have in the second quarter on overall and then now that you've cut some costs there based on still (inaudible) second half? What kind of profitability is that international having at that level?

James Morgan - *ICF International, Inc. - EVP & CFO*

From a gross margin perspective and theoretically, it shouldn't have as much of an impact. If the work isn't there, then the individuals shouldn't be performing on the work and doesn't impact gross margin. Where it does hit is below gross margin, on profitability, but that's where we are proactively taking the action to make sure that we align the staff to mitigate the impact on the bottom line.

Realistically, there may be a little bit of impact, but it shouldn't be a major impact on gross margin.

Bill Loomis - *Stifel Nicolaus & Company - Analyst*

Okay. And then, just to be clear on passthroughs, are you also putting subcontractors that are working for you in the passthrough definition?

James Morgan - *ICF International, Inc. - EVP & CFO*

Yes. Yes, it's a combination of subcontractors and large [ODCs].

Bill Loomis - *Stifel Nicolaus & Company - Analyst*

Okay. Great. Thanks.

Operator

We have no further questions at this time. I will now turn the call over to management for closing remarks.

Sudhakar Kesavan - *ICF International, Inc. - Chairman & CEO*

Thank you very much for participating in today's call. We look forward to seeing you in September, on the 20th, in New York City and keeping you up to date on our progress. Thank you very much, again.

Operator

Thank you, ladies and gentlemen. This concludes today's conference. We thank you for participating. You may now disconnect.
