THOMSON REUTERS

EDITED TRANSCRIPT

Q4 2018 ICF International Inc Earnings Call

EVENT DATE/TIME: FEBRUARY 26, 2019 / 9:30PM GMT

CORPORATE PARTICIPANTS

James C. Morgan *ICF International, Inc. - CFO & Executive VP*
John Wasson *ICF International, Inc. - President and COO*
Sudhakar Kesavan *ICF International, Inc. - Executive Chairman & CEO*

CONFERENCE CALL PARTICIPANTS

Joseph Anthony Vafi *Loop Capital Markets LLC, Research Division - Analyst*
Lucy Guo *Cowen and Company, LLC, Research Division - VP*
Marc Frye Riddick *Sidoti & Company, LLC - Business and Consumer Services Analyst*
Tobey O'Brien Sommer *SunTrust Robinson Humphrey, Inc., Research Division - MD*
Lynn Morgen

PRESENTATION

Operator

Welcome to the ICF International Fourth Quarter 2018 Earnings Conference Call. My name is Vanessa, and I will be your operator for today's call. (Operator Instructions) Please note, this conference is being recorded on Tuesday, February 26, 2019, and cannot be reproduced or rebroadcast without permission from the company.

I would now like to turn the program over to Lynn Morgen of AdvisIRy Partners.

Lynn Morgen

Thank you, Vanessa. Good afternoon, everyone, and thank you for joining us to review ICF's fourth quarter and full year 2018 performance.

With us today from ICF are Sudhakar Kesavan, Chairman and CEO; John Wasson, President and COO; and James Morgan, CFO.

During this call, we will make forward-looking statements to assist you in understanding ICF management's expectations about our future performance. These statements are subject to a number of risks and could cause actual events and results to differ materially. I refer you to our February 26, 2019, 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 fourth quarter and full year 2018 performance. Sudhakar?

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

Thank you, Lynn, and thank you all for joining us today to review our 2018 fourth quarter and full year results and discuss our outlook and guidance for 2019.

Our fourth quarter performance represented a strong finish to a record year for ICF. Revenues increased 18% year-on-year and non-GAAP EPS increased 50%. Revenue in each of our client categories grew, driven by increasing demand for our advisory and implementation services.

In line with our guidance, we reported an exceptional adjusted EBITDA-to-service revenue margin of 16.5% in the fourth quarter, benefiting from a 10% increase in service revenue, higher utilization and a favorable mix of business.

Additionally, the value of contract awards won during the year reached a record $1.8 billion at year end, 40% above the prior year, resulting in an annual book-to-bill ratio of 1.4. And our business development pipeline was $5.8 billion at the end of the year, up 38% year-on-year and 7% ahead of third quarter levels.

These metrics underscore our confidence in ICF's expected growth in 2019 as we continue to execute well across our diversified portfolio.

Looking at market dynamics, we see 4 key growth catalysts for ICF in 2019 and beyond. First, we expect growth in federal government revenues in 2019 based on our backlog, which includes the significant contract wins in the second half of 2018. We also believe that the additional time that our civilian agency clients have this year to plan and issue procurements will allow them to spend their budgetary allocations in a more timely fashion. Additionally, we have a record pipeline of qualified opportunities that we are pursuing.

Second, our disaster recovery program work for state and local government clients will be an important growth driver for ICF in 2019 and beyond. In addition to our contract wins to date, we have submitted proposals for additional contracts that are expected to be awarded in the next few months. The acquisition of DMS that we completed in August last year has added to our bandwidth in this key area and has strengthened our competitive position. DMS also has brought new disaster planning capabilities, which will allow us to help state and local governments improve their response planning ahead of specific natural disasters. And we are continuing to build on our qualifications in resiliency and disaster preparedness, which we believe will develop into an ongoing and sustainable source of revenue for ICF.

Third, in the marketing services area, digital channels continue to increase their share of marketing spend, reflecting growing demand to engage with customers and stakeholders in a focused and cost-efficient manner. We recently launched ICF Next, which brings together 1,700 technologists, strategists, marketing specialists, creatives and communicators, into a single integrated team to support our growing portfolio of public and private sector clients. This integrated offering has sharpened our ability to offer a more comprehensive set of capabilities and gives us considerable scale and a body of work that has garnered some of the industry's highest honors.

And fourth, we are looking ahead to continued growth in our commercial energy business, thanks to a robust pipeline that includes many energy efficiency program opportunities. On the advisory side, we believe our expertise in infrastructure security and resiliency has become increasingly relevant in the aftermath of 5 major hurricanes in the last 2 years. Additionally, we see significant growth potential for ICF in the areas of distributed and renewable energy resources, including storage, solar and electric vehicles. This trend also offers significant program implementation opportunities over the next several years.

So to summarize, while 2018 was a record year for ICF, we believe that 2019 will be even better. We remain active on the acquisition front. Given our significant cash flow, we are focused on deploying these resources that we generate in a manner consistent with what we have done successfully in the past. We continue to look at opportunities in all ICF domains and in our functional areas of expertise, including the government arena where increased specialization and scale is required to win larger, multi-year contracts, and in the commercial energy markets that deepen our expertise and further strengthen our offerings.

Now I would like to turn the call over to ICF's President, John Wasson, for his business review. John?

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

Thanks, Sudhakar, and good afternoon, everyone. Business trends in the fourth quarter were in line with our expectations and reflected the positive momentum that we observed throughout the second half of 2018 and expect to continue in 2019.

Revenue performance came in ahead of our forecasts, driven by our disaster recovery work in Puerto Rico and increases in our marketing services work for both commercial and international government clients.

From an overall business perspective, we were very pleased with our results and continue to see positive growth catalysts present across our key markets.

James will speak in a moment about some of the special items that affected our earnings results for the fourth quarter.

Revenues in our government business increased 22% in the fourth quarter and represented 60% of full year 2018 revenues, and each client category within our government market showed year-on-year revenue growth.

Revenues from federal government clients in Q4 increased 2% year-on-year, bringing full year revenue performance to just 1% below 2017 levels. This growth in the quarter was slightly below our expectations due to the slower ramp-up of a couple of civilian agency contracts, but importantly represented an acceleration in our federal business and a return to growth that augurs well for 2019.

The revenue impact of the partial federal government shutdown was approximately $3 million for Q1 2019. We expect to be able to recapture the lost revenue by the end of the year, although we will absorb the costs of maintaining our staff in this year's first quarter.

We are expecting revenues from federal government clients to achieve low- to mid-single digit growth in 2019. Last year, we were awarded over $865 million in federal contracts, most of which were won in the second half, and over 55% of that dollar amount represented new business. This represented an annual book-to-bill ratio of 1.6 and sets us up very well for growth in 2019 and beyond.

As we mentioned last quarter, we see opportunities across a broad range of federal agency clients, including at our largest, the Department of Health and Human Services, as well as with the Department of State, the Department of Defense, the Department of Energy and the Department of Homeland Security. Additionally, we are bidding more aggressively on cybersecurity work, which is slated to increase at the Department of Defense and across civilian agencies, following our significant contract wins in 2018 at the U.S. Army Research Laboratory and the U.S. Air Force.

An even greater growth driver this year will be our disaster recovery work following the 2017 hurricanes. In the fourth quarter, revenues from state and local government clients increased 115%, reflecting our execution on the FEMA-funded contract we were awarded by the government of Puerto Rico in June of last year and the initial ramp-up of the several contracts that ICF was awarded to support post-hurricane housing and infrastructure programs in Texas that we mentioned on last quarter's call. These contracts are with The Texas State General Land Office and the City of Houston.

Given the severity of the post-hurricane damage, we believe that each of these contracts has potential for expansion, and we have a robust pipeline of additional opportunities in Puerto Rico and Texas on which we have submitted proposals and are awaiting award decisions. Additionally, we are pursuing opportunities in Florida and the Carolinas following the 2018 hurricanes. For 2019, we expect revenues from state and local governments to increase by 30% or more compared to 2018.

Revenues from international government clients continue to show positive momentum, increasing 15% in the fourth quarter and 34% for the full year. While we do not expect to replicate that exceptional growth rate this year, trends in that market remain favorable for ICF. We have a solid new business pipeline and thus expect mid- to high single-digit growth in this market for 2019.

We continue to execute very well on marketing and communications work for the European Commission, on providing policy, economic and programmatic support to European Commission and U.K. government clients and supporting international development work focused on energy planning and clean energy sources in Asia and Africa for European development agency clients.

Moving to our commercial clients, the 12% increase in commercial revenues in the fourth quarter reflected robust year-on-year growth in both marketing services and energy markets, the largest components of this client set. Commercial marketing services benefited from organic revenue growth and the October acquisition of the U.K.-based, We are Vista. We continued to bring integrated solutions to clients in the fourth quarter, achieving more than $21.6 million in integrated sales, bringing the total to more than $177 million of integrated wins since we acquired Olson at the end of 2014. The average size of our contract wins continued to increase in the fourth quarter, and total sales were up year-on-year.

In early 2019, we unveiled ICF Next, a new global engagement and transformation partner for brands, public sector agencies and other organizations to help them take advantage of the breakneck pace of change in the marketing services industry. Few players of our size can offer the breadth of services in an integrated way across areas as diverse as digital strategy, earned media, loyalty, technology and e-commerce, which differentiates ICF in the marketplace. And, with aggregate revenues in excess of $350 million, and experienced management in place, we have the scale and gravitas to capture larger contracts with the private sector, regulated industries and governments.

Finally, our commercial energy markets business continued to perform well in the fourth quarter. Revenue growth benefited from large advisory assignments supporting clients on restructuring and M&A activities in the power sector and our significant energy efficiency program implementation work for utilities. The majority of utilities plan on increasing spending on energy efficiency programs by as much as 10% through 2020, and we continue to maintain a strong pipeline. Several states are significantly expanding their energy efficiency goals via new legislation or regulatory action. These include Massachusetts, New Jersey, Illinois, New York, Virginia and California.

As you know, California offers considerable opportunities for us. The first tranche of requests for abstracts were released in Q4 as the state alters its approach to energy efficiency, renewable energy and greenhouse gas reduction. The ultimate goal by 2022 is to have 60% of the investor-owned utility energy efficiency budgets in California be outsourced to firms like ICF, up from historical outsourcing levels of 20%.

Additionally, our distributed energy resources consulting business performed well as states and utilities address the impact of distributed resources on the grid. These efforts involve utility pilot programs testing distributed energy technologies, which point the way to developing future utility implementation programs beyond traditional energy efficiency that will drive additional long-term growth.

Given the robust performance of our commercial marketing services and energy business in Q4 and the general market trends discussed above, we expect at least mid-single-digit growth in our commercial businesses for 2019.

In summary, we are pleased with our overall business performance in the fourth quarter, which together with 2018 contract awards and a record year-end pipeline, positions us for another year of substantial growth in 2019. We're also looking ahead to margin expansion in 2019, thanks to continued high utilization rates and our expectations that ICF's commercial business and our state and local disaster recovery work in the aggregate will account for an increasing percentage of this year's revenue.

At year-end, our business development pipeline was at a record-high at over $5.8 billion. There were 48 opportunities larger than $25 million and 89 opportunities between $10 million and $25 million.

Our annual personnel turnover rate was 16.2%.

Now, I'll turn over the call to James Morgan, our CFO, for the financial review.

James C. Morgan ***ICF International, Inc. - CFO & Executive VP***

Thank you, John. Good afternoon, everyone. I am pleased to provide a more detailed look at ICF's fourth quarter and full year 2018 financial performance.

Fourth quarter revenue was $377.9 million, up 17.7% from the $321.2 million in last year's fourth quarter, driven by double-digit revenue growth from both government and commercial clients. Our revenue mix by client category in the fourth quarter showed considerable variations from the prior year fourth quarter. This reflected the significant increase in revenue from state and local clients, which accounted for 16% of total revenue in this year's fourth quarter, up from the 9% last year.

The other major change was in revenue from federal government clients, which represented 35% of total revenue in the fourth quarter of 2018, down from the 40% in the similar 2017 period. Both of these changes were driven mainly by our new work to support disaster recovery efforts, which is classified as state and local.

Service revenue increased 10% to $239.6 million from $217.8 million in the fourth quarter of 2017. Gross profit increased 13.1% to $128.9 million from $113.9 million in the fourth quarter of 2017. Given the higher pass-through revenues, gross margin was 34.1% in 2018's fourth quarter compared to 35.5% last year. Conversely, gross margin on service revenue expanded 150 basis points year-over-year to 53.8% in 2018 as compared to 52.3% in the fourth quarter of 2017.

Indirect and selling expenses for the fourth quarter increased 5.9% to $92 million compared to $86.8 million in the comparable quarter of 2017. As a percentage of service revenues and after exclusion of special charges, indirect and selling expenses improved to 37.3% of total revenue compared to 37.9% in the fourth quarter of 2017.

EBITDA totaled $36.9 million, 36.1% ahead of last year's $27.1 million. And adjusted EBITDA, which excludes special charges, was $39.4 million, up 25.5% from $31.4 million reported in the fourth quarter of 2017.

In addition to the typical seasonal strength in the fourth quarter for adjusted EBITDA margin on service revenue, as expected and mentioned in our third quarter's earnings call, our 2018 fourth quarter reflected the confluence of positive factors, including higher utilization related to the ramp-up of new contracts, a higher level of incentive fee payments, and a significant increase in higher-margin service revenue. These factors resulted in an exceptional adjusted EBITDA on service revenue of 16.5% in the fourth quarter of 2018 as compared to 14.4% in last year's fourth quarter.

It should be noted that our fourth quarter EPS year-over-year comparisons were impacted by special charges, which totaled $0.09 per share after tax, and included a $1.24 million reserve, or $0.05 per share, related to the bankruptcy of Pacific Gas and Electric. For context, our work with PG&E is mostly on the consulting side, and we are working to get critical vendor status as we provide environmental-related advisory work that is required by the State of California.

In addition to the $0.09 in special charges, our Q4 results were lower than anticipated due to 3 factors. First, our tax rate of 29.8% in the fourth quarter was higher than anticipated, primarily due to valuation allowances of foreign tax credits. The higher-than-anticipated effective tax rate negatively impacted our fourth quarter EPS by $0.04. Second, we had higher interest expense than anticipated due to timing issues related to collections on certain receivables. And third, our share count was slightly higher than anticipated. These last 2 items amounted to roughly $0.02 per share after tax.

As a reminder, in the fourth quarter of 2017, we had a onetime tax benefit of $16.2 million, or $0.85 per share, due to the revaluation of our deferred tax liabilities and deferred tax assets associated with the implementation of the Tax Reform Act. Additionally, our fourth quarter 2017 EPS results reflected the impact of $0.13 in special -- in tax-effected special charges.

Inclusive of these 2018 and 2017 items, we reported net income for the fourth quarter of 2018 of $18.7 million, down from the $27.1 million we reported in last year's fourth quarter, and diluted EPS was $0.97 per share compared to $1.41 in the fourth quarter of 2017, which as I mentioned, included a onetime tax benefit of $0.85 per share associated with the implementation of the Tax Reform Act.

Non-GAAP diluted EPS, which excludes the impact of the previously mentioned special items and amortization of intangibles, was $1.17 in the fourth quarter of 2018, an increase of 50% from $0.78 reported in the fourth quarter of 2017.

Now let me give you an overview of our 2018 full year results. We had record revenue of $1.34 billion, up 8.9% year-on-year. Service revenue was up 4.7% year-over-year to $925.8 million from $884.2 million in 2017. Pass-through revenues increased by 19.5% to $412.2 million. Adjusted EBITDA increased to $123.7 million and accounted for 13.4% of service revenue in 2018, as compared to 13.3% in 2017. This is in line with our objective of improving our year-over-year adjusted EBITDA margin on service revenue by continuing to invest in business -- in the business to support future growth.

Net income amounted to $61.4 million in 2018 compared to $62.9 million in 2017. As mentioned previously, the 2017 results include the onetime tax benefit of $16.2 million associated with the implementation of the Tax Reform Act.

Reported diluted earnings per share were $3.18 for 2018, inclusive of the $0.05 related to the bankruptcy of Pacific Gas and Electric that I previously mentioned, as well as an additional $0.12 in tax-effected special charges comprised of office closure expenses, staff realignment charges and acquisition-related costs. This compares to $3.27 per diluted share in 2017, which included a onetime tax benefit of $0.84 per share associated with the implementation of Tax Reform Act and $0.24 of tax-effected special charges.

Non-GAAP diluted EPS for the full year, which excludes the special charges I've just mentioned as well as amortization of intangibles, was $3.73 per diluted share for 2018, up 23.5% compared to the $3.02 reported last year.

In 2018, we had $74.7 million cash provided by operating activities, which was below our most recent guidance range. The shortfall was due to timing issues associated with the collection of more than $10 million of receivables, which have now been collected in the first quarter of 2019 and which are reflected in our 2019 cash flow guidance.

Throughout 2018, we made significant investments in our infrastructure and intellectual property, which resulted in a $6.2 million year-over-year increase in capital expenditures that totaled $25.5 million in 2018. Borrowings on our credit facility at the end of December were $200.4 million. Days sales outstanding for the fourth quarter, including the impact of deferred revenues, was 77 days, within our typical range.

As you've heard today, we expect 2019 to be a year of considerable growth for ICF. For modeling purposes, we want to share our expectations for certain 2019 financial metrics, based on our current portfolio of business. As you saw in today's earnings release, we are expecting substantial revenue and earnings growth in 2019. We expect the realization of our revenues and EPS to follow a similar pattern to that of 2018, with about 45% materializing in the first half of the year and 55% in the second half. This takes into account the first quarter 2019 impact of the government shutdown of approximately $3 million in revenues and $0.05 in diluted EPS.

Second, we anticipate full year 2019 depreciation and amortization expense to be in the range of $20.5 million to $21.5 million for the full year of 2019. Amortization of intangibles should be in the range of $8 million to $8.5 million.

Third, full year interest expense should range from $7.5 million to $8.5 million.

Fourth, capital expenditures are anticipated to be relatively flat with 2018, and in the range of $25 million to $28 million as we continue to invest to support future growth.

Fifth, we expect a full year tax rate of approximately 27.5%.

And finally, we expect fully diluted weighted average shares of approximately 19.3 million for 2019.

Please note that in 2018, we repurchased 214,000 shares under our share repurchase program for a total outlay of $13.9 million to partially offset the dilution from our employee incentive programs.

Going forward, our capital allocation priorities remain the same: investing in our business, making strategic acquisitions, paying off debt, making share repurchases to offset dilution caused by our employee incentive programs, and returning capital to our shareholders in the form of dividends. On that last subject, today, ICF declared a quarterly cash dividend of $0.14 per share payable on April 16, 2019, to shareholders of record on March 29, 2019.

With that, I will turn back the call to Sudhakar. Sudhakar?

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

Thank you, James. In conclusion, we are very pleased with ICF's position as we move ahead in 2019. Key to our success is the mission and results-driven culture that is reflected in our relatively low employee turnover rates and deeply committed staff. As part of this, we have invested in human capital by establishing the ICF Learning Institute for leadership and management development and by bringing in senior experienced staff. We have modernized our primary brand to reflect the broader scope of ICF services. We continue to invest in systems and processes to become more efficient and scalable. Through it all, we have maintained the agility and specialized capabilities required to focus our resources and capabilities to capitalize on major opportunities.

With this as a backdrop, we are pleased to provide full year guidance for 2019 that reflects significant year-on-year revenue growth and further margin expansion.

We have good visibility into 2019 based on our existing contract backlog, which accounts for over 80% of our revenue guidance of $1.45 billion to $1.5 billion. This does not include any substantive new disaster recovery-related contract wins that may occur nor any potential acquisitions. GAAP earnings per diluted share are expected to range from $3.75 to $3.95, exclusive of any special charges; and non-GAAP diluted EPS should be between $4.05 and $4.25. Operating cash flow is estimated to be between $100 million and $120 million.

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

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And we have our first question from Joseph Vafi with Loop Capital.

Joseph Anthony Vafi ***Loop Capital Markets LLC, Research Division - Analyst***

I was wondering if we could talk a little bit about that Q4 service margin performance. It was strong and I suspect there was 2 things going on, a combination of mix and utilization. And I was wondering to get a little more color on what was driving that and how we think about utilization into 2019? Then I have a follow-up.

James C. Morgan ***ICF International, Inc. - CFO & Executive VP***

Joe, this is James. Now, really, it's what I mentioned, it really was driven by higher utilization. We had our highest utilization for the year in Q4 with the ramp-up of the new contracts that we have won in the back half of the year. And in addition to that, we had, as you know, we typically have higher incentive fees associated with our energy efficiency work that get realized in the fourth quarter, so that certainly benefited the quarter. And those are -- I mean, those are 2 of the biggest items. And for us, that was our share in controlling of indirect expenses.

Joseph Anthony Vafi ***Loop Capital Markets LLC, Research Division - Analyst***

Got it. Is there more room for utilization upside from here? Or are we kind of that -- of comfortable level relative to utilization?

James C. Morgan ***ICF International, Inc. - CFO & Executive VP***

Yes, I don't think there will be much more increase. I mean, as you would expect, when you win new contracts, typically you're running a little bit harder on the front end and then you continue to adjust your staff and get back to an appropriate level, so that you can make sure you're investing and driving the long-term growth of the business. So I don't think that there'll be much upside to the utilization we recognized in Q4.

Joseph Anthony Vafi ***Loop Capital Markets LLC, Research Division - Analyst***

Okay. And then focusing a little bit on the digital marketing business that -- it sounded like you're expecting -- I know there's probably a little less backlog there than other parts of your business, but just wanted to confirm that you were looking at potentially mid-single digit growth there in 2019?

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

Yes, hi, Joe. It's John Wasson here. I think that as we said in the guidance for commercial, we're expecting at least 5% growth in our commercial business. And I certainly think that applies to our commercial marketing services business. Obviously, we had a very strong quarter there. And so -- but certainly for the year -- for last year, the marketing services business was in the mid-single digit range. We expect it to stay there for 2019 in terms of organic growth.

Joseph Anthony Vafi ***Loop Capital Markets LLC, Research Division - Analyst***

Okay. And then since that business is kind of doing better now than it was a year ago, how has the margin profile in that business changed? Has it changed with more strength in the business or margin profile and whatever?

James C. Morgan ***ICF International, Inc. - CFO & Executive VP***

Yes, I mean, as we've talked about in the past, typically -- or actually it's more than typical it is, our commercial margins are a little bit better than, on average, the rest of our business. And we certainly expect that to be that way in that case as we move into 2019. And certainly as you would expect, as you continue to have growth in the business, we were able to have some leverage and continue to improve our margins over what we realized in past years.

Joseph Anthony Vafi ***Loop Capital Markets LLC, Research Division - Analyst***

Okay. And then finally, just one last one on disaster recovery. It sounds like some of those down-selects in Texas have moved forward. Are there still additional contracts that have not been adjudicated in Texas? And -- relative to that 2017 hurricane season? And do you have a feel for kind of dollar value of the yet to be adjudicated contracts that you may be eligible to win?

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

It's John Wasson, again, Joe. We certainly have opportunities in the pipeline in Texas, both at the state and local level, on the housing recovery front that are waiting adjudication or in the proposal stage. As we talked about in our remarks, we've obviously won several opportunities in Texas that we talked about in our last quarter. I think we said they were $50 million in total over 2 to 3 years. I would expect the opportunities that are still out there to be in that magnitude range. I would say that we do see potential upside in those opportunities if we perform well. I think there's a lot of work to do there. So certainly in Texas, there remains to be opportunities. I think initially, they'd be like the ones we've won to date, but there will be upside. And as Sudhakar noted, we're still waiting on awards in Puerto Rico on our Community Development Block Grant housing opportunities. Those proposals are in and we're waiting award decisions, and as we talk about those, those have the potential to be significant over time, too.

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

And I think there are also perhaps opportunities in the Carolinas and in Florida on the hurricanes of last year. So...

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

Which will play out later next -- this -- play out later this year.

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

Later this year, yes, correct.

Operator

We have our next question from Tobey Sommer with SunTrust.

Tobey O'Brien Sommer ***SunTrust Robinson Humphrey, Inc., Research Division - MD***

My first question also on the disaster recovery side. I mean, what does the -- if you could put the FEMA contract win in context from 6 or 7 months ago, what does that do to your -- the T&M in kind of the markets that you're able to address because historically the company has kind of tapped into helping out the distribution of the Community Development Block Grant money in public infrastructure, contract of the size is kind of a relatively new thing. How do we put that in context and think about how that changes the opportunities in the company over time?

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

Well, I think that the kinds of work we are doing on this contract are not dissimilar to what we have done on CDBG contracts in the past, so there is -- it's just they address a slightly different set of constituencies, small businesses and sort of public municipality and public infrastructure. So the kinds of work we're doing are quite similar. I think the way it helps is that we have significant infrastructure experience now and performance in Puerto Rico, which obviously, the clients they can see and so hopefully, that helps us position well for other contracts in other areas as we move forward. And I think that it's a small community. So if we do well in one area, people talk about it in other states. So I think it just strengthens our capability to win other work in other jurisdictions going forward, especially given that the disaster recovery work is moving more and more towards block grants, even in the non-CDBG world. And I think knowing how to do this work sort of helps us across the country as we have to deal with increasing number of disasters going forward.

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

I would just also add that I think that there is a shift in the market or an expansion in the market around resiliency in, not only how do you rebuild immediately after a storm, whether it's housing, or public infrastructure, or public buildings. But how do you strengthen that infrastructure to prevent it from having damage and having to go through this cycle of repair after every storm. And that's a kind of -- a set of expectation we've been developing over the years, given our broader set of work around infrastructure and climate change, was how to really improve resiliency. So I think what's also happening here, Tobey, is that we can leverage that expertise and that capability we've built in both, into the FEMA market and into the housing market. So and as you see, under some of the recent storms in 2017, there's been quite significant increase in funding pointed towards resiliency and infrastructure, both within FEMA and within the Community Development Block Grant program. So I think that's a positive trend for us that I think allows us to play a larger role in those 2 markets over time.

Tobey O'Brien Sommer ***SunTrust Robinson Humphrey, Inc., Research Division - MD***

Okay. With respect to timing of the Puerto Rican opportunities, how are things progressing? It seems like -- I'm curious if the shutdown may have delayed anything, I'm not sure. That the process was thrown a monkey wrench by the shutdown?

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

Yes, and I think we still expect these awards in the next couple of months, next 2 to 3 months. And I don't think we have any insights into what the exact date these will come forward, but I think we still expect them in the near term and -- I don't know Sudhakar, do you want to...

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

Given the need and given the fact that there is the requirement to do this work, we do think the next 2 or 3 months. Sometimes these decisions just take time, longer than you would like, but these just take time.

Tobey O'Brien Sommer ***SunTrust Robinson Humphrey, Inc., Research Division - MD***

And Sudhakar, you referenced the storms from last year potentially being opportunities for the company later this year. What kind of -- would you have opportunities both on the FEMA kind of work that you've already won in Puerto Rico as well as the residential side that you, I guess, you hope to win at some point in the future?

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

Yes, I think it would be. As I said, I think it's both -- certainly on the housing side under Community Development Block Grant, around the whole resiliency and how to strengthen infrastructure in the face of future storms, which could span both CDBG and FEMA. I think it's opportunities in both places, and so we're certainly paying attention to those markets in there and capture around those types of opportunities.

Tobey O'Brien Sommer ***SunTrust Robinson Humphrey, Inc., Research Division - MD***

Okay. One last question for me on the energy efficiency side and I'll get back in the queue. Are you noticing any increased level of competition or conversely sort of change in the size of projects that maybe help the company because you are a scale provider and maybe the changes in the size of contracts, reduced competition? Any dynamics there that you think are occurring now and likely to in the future?

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

I don't think we've seen any significant shift in the competitive landscape in that market. I think we -- we're obviously a market leader in that area. It is competitive, but I think we win our fair share. I think that we've talked at some length that as utilities look to bundle contracts and opportunities, it plays to our strength. We've seen that in certain markets. And certainly in California as they look to outsource a higher proportion of their efforts, I think they will have to go to larger contracts over time, and that will be a positive trend for us. But I don't want to say there's been a significant shift in the competitive landscape or the set of players in those markets.

Operator

We have our next question from Lucy Guo with Cowen and Company.

Lucy Guo ***Cowen and Company, LLC, Research Division - VP***

First is to clarify on disaster recovery. You talk about that some upside is not in your guidance. Is it the $310 million-or-so of contract awards to-date that's in the guidance?

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

Yes, I think the contracts that have been awarded today are in our guidance and potential and upside that we see on those existing contracts is reflected in our guidance range. There are no material new contract awards, either in Puerto Rico or Texas, that's in our guidance range.

Lucy Guo ***Cowen and Company, LLC, Research Division - VP***

Got it. And the potential is roughly -- it could be as much as a couple of hundred million or a few hundred million-or-so that, that was the -- what I remember that you've said before. Is that still the case?

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

I mean, we haven't given -- I mean, I would say that over multiple years, the potential opportunities could reach those kind of levels. I think that's correct.

Lucy Guo ***Cowen and Company, LLC, Research Division - VP***

Okay, got it. And then maybe a question for James in terms of your EBITDA margin. Q4 was obviously very good execution plus some timing of potentially milestone payments and such. But once you just -- I understand you're still targeting the 10 to 20 bps per year increase on the service margin but overall EBITDA on an adjusted basis, any thoughts on what could potentially offset the higher pass-through that you'll see on the state and local work?

James C. Morgan ***ICF International, Inc. - CFO & Executive VP***

So I guess I would just say that as we move into 2019, we do expect that we'll do a little bit better than the 10 to 20 basis points of margin improvement that we've been doing over the last few years. It's probably more in the neighborhood of 30 basis points. And actually, that's after taking into account the impact of the government shutdown, which is impacting our margins in 2019 by, call it, 10 to 15 basis points. So without the impact of the government shutdown, we would be improving margins year-over-year in the neighborhood of 40 to 50 basis points. So that's really what we're targeting as we go forward this coming year.

Lucy Guo ***Cowen and Company, LLC, Research Division - VP***

Is that a factor of -- you mentioned the improved utilization. Are you projecting changes to your bid and proposal expense or business development expense? And any other factor that you can point to would be helpful.

James C. Morgan ***ICF International, Inc. - CFO & Executive VP***

Yes. No, it's really a combination of factors. I mean, it's everything from the fact that the federal line, as we continue to get more in scale, we have the ability to leverage and improve our profitability. The other part of it is looking at our mix of our business. I mean, certainly, as we've said before, our commercial business is a little bit more profitable than our government business and we're looking at that growing faster than our federal business. And then we've also talked about the fact that our disaster recovery work, it's on the high end of the government margin. So the confluence of those 2 factors are helping to improve the mix of our profitability of our business. So those are 2 big drivers.

Lucy Guo ***Cowen and Company, LLC, Research Division - VP***

Got it. That's helpful. And then just also looking for some color, I think earlier on in your commentary you mentioned there were some slower ramp on certain federal civilian contracts. If you can talk about any details there.

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

Sure. It's John Wasson. I think we had a handful of contracts that ramped a little slower. We had a water reclamation contract in California within 2 departments that ramped a little slower as they were working out some policy issues. And we have contracted 2 EPAs that ramped a little slower. So just a handful of civilian contracts. Not like there's any underlying trend, they just ramped a little slower in the fourth quarter.

Operator

We have our next question from Marc Riddick with Sidoti.

Marc Frye Riddick ***Sidoti & Company, LLC - Business and Consumer Services Analyst***

Wondering if you could take a moment and you had mentioned some of the bidding process and some -- maybe some changes as far as aggressiveness with bidding on cyber business, I believe it was. I was wondering if you could add a little bit of color to that commentary?

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

Well, I would just say that we're seeing significant growth opportunities in the cyber market, both on the defense side and in civilian markets. We do have a cybersecurity business and I just think that they're -- given the underlying trends in those markets and the focus across the government on cyber, we're seeing a lot of opportunity, and we've been particularly successful here in the last year, 18 months, both with the Army Research Lab, the Air Force and so are winning work both on the defense side and, obviously, given the relationships we have throughout civilian agencies, as budgets go up to support cyber work, it's generally a positive trend for us. And so that is a market where we are seeing increases in spend and growth. And I've also talked -- and so I think that's really what's driving it.

Marc Frye Riddick ***Sidoti & Company, LLC - Business and Consumer Services Analyst***

Okay, great. And then I was wondering if you could touch a little bit -- I know that the announcement around Next was only a little while ago. But I was wondering if there's any sort of general feedback as to sort of the repositioning, if you will, with as far as feedback that you've received from clients. Obviously, you mentioned some positive commentary around commercial, but I was wondering maybe if you could talk about some of the benefits that you foresee for clients and how that could help in gaining new business wins?

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

Sure. Yes. And I think to what -- so I think we certainly are seeing benefits from ICF Next with our clients. I think the -- I mean, one is, is I think our clients, they didn't fully recognize kind of the full scale and set of capabilities that we can bring to market across our commercial and our government and our international markets. And prior to ICF Next, we used to go-to-market under several different brands, with several different logos. And so frankly, a big part of this was getting our customer sets to understand the full scale and set of integrated opportunities that we could bring. And I think, frankly, a lot of them had been quite surprised and very positive as they've come to understand the breadth of capabilities and the scale and the depth of our experience. And so I think that's helped us a lot. I think we're also very focused from an account perspective of leveraging all of the relationships we have in specific accounts, whether it's commercial accounts or government accounts. Of bringing the entire set of ICF capabilities into those accounts. Whereas before, we've been going to market under these different logos. We didn't bring the full company set of capabilities into each of those accounts. And so we've had very positive feedback from clients. I think they have been pleasantly surprised with all that we can do. And I've talked about some of the opportunities within -- we've won that -- of an innovative nature since the Olson acquisition, I think this ICF Next announcement has accelerated that. I can't name clients. So we've had several clients where we've gone in with integrated pitches under the ICF Next brand here in the last month or 6 weeks, a couple of months, and won much larger assignments with much broader set of work. So I think the signs are very positive. And I think you're seeing that momentum and that activity in the results. I mean, we're -- I think we've had now 4 quarters of growth in our marketing services business, and I think this will only help further on that front.

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

I would also add to that, that the Forrester Wave is something which we benefited from being a leader in our loyalty business. Similarly, we -- there has been a Forrester Wave for mid-sized marketing services and digital services firms, and we are part of that Forrester Wave, so that's a great way of generating -- they came out with a report about a month ago, and that's a great way of generating enormous leads associated with that. We had to do a whole song and dance there to be part of that. And I think that -- and that's ICF Next because I think we could showcase a broad range of skills and understanding of consulting and service technologies, which helped us there. So I think that it's a promising start, and we certainly hope that, that will generate leads and incoming calls on us being able to help those clients, too.

Operator

(Operator Instructions) And we have a follow-up question from Tobey Sommer with SunTrust.

Tobey O'Brien Sommer ***SunTrust Robinson Humphrey, Inc., Research Division - MD***

In 2019, are there any changes to the composition or weighting of incentive compensation for executive management or kind of the next level below?

James C. Morgan ***ICF International, Inc. - CFO & Executive VP***

I don't think we're foreseeing any significant changes in executive management compensation or the next level below. I don't think -- no, I don't think so.

Tobey O'Brien Sommer ***SunTrust Robinson Humphrey, Inc., Research Division - MD***

No changes in the mix or weighting? Okay. That was it for me.

Operator

Thank you. 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. - Executive Chairman & CEO***

Thank you all for participating in today's call. We look forward to keeping you up-to-date on developments at ICF. Thank you again.

Operator

And thank you. Ladies and gentlemen, this concludes our conference. We thank you for participating. You may now disconnect.