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PRESENTATION

Operator

Welcome to the Fourth Quarter and Full Year 2017 ICF Earnings Conference Call. My name is Vanessa, and I will be your operator for today's call. (Operator Instructions) As a reminder, this conference is being recorded on Tuesday, February 27, 2018, and cannot be reproduced or rebroadcast without written permission from the company.

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

Lynn Morgen

Thank you, operator. Good afternoon, everyone, and thank you for joining us to review ICF's fourth quarter and full year 2017 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 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 February 27, 2018 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 declaim any obligation to do so.

I will now turn the call over to ICF CEO, Sudhakar Kesavan, to discuss fourth quarter and full year 2017 performance. Sudhakar?

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

Thank you, Lynn, and thank you all for joining us this afternoon to review our fourth quarter and full year 2017 results and discuss our outlook for 2018.

Our fourth quarter results represented a strong finish to 2017 and brought our full year performance in line with the guidance we provided at this time 1 year ago.

Revenue growth was led by a strong double-digit increase in our commercial business where we saw a significant year-on-year improvement across the client set that was supported by higher pass-through revenues. In addition to the strong growth in our commercial business, revenues from our government clients increased at a low single-digit rate, driven by strong growth from our European Union clients and slight growth in the U.S. federal market. Overall, we were pleased with our service revenue growth of 5.3% in the fourth quarter, all of which represented organic growth and reflected positive demand trends from both government and commercial clients.

Exclusive of the quarter-specific items that James Morgan will detail later in this call, operating income increased 9.7% in the fourth quarter, substantially ahead of service revenue growth, representing significant operating leverage. On the same basis, operating income increased 5.7% for full year 2017, considerably ahead of our total revenue and service revenue growth for the year.

As we anticipated, our results continued to improve through 2017, and we ended the year with positive momentum and tailwinds that point to continued growth in 2018 in each of our key business areas.

Let's discuss each of these areas. First, in our government business, we expect year-over-year revenue growth in 2018. These expectations are based on our current backlog and pipeline. We're also pleased with the passing of the recent Bipartisan Budget Act as it represents the highest increases in years for civilian agency budgets, and it provides a framework to pass and enact fiscal year 2019 appropriations bills on time. We have not included any significant benefit from higher civilian budgets in our 2018 revenue guidance given the time it generally takes to move from budget agreement to revenue recognition.

The current schedule gives lawmakers through 23rd of March to reconcile the House and Senate bills for each of the 12 appropriations subcommittees. Once the appropriations bills are signed, the agencies generally develop internal operating plans that show how they will flow the funds down to the specific organizational units. If Congress gets the bills done by March 23, we should expect to see monies placed by the end of September. This means the revenues on contracts won are not expected to flow until the fourth quarter at the earliest, with ramp-up of new programs coming in early 2019.

So while the Bipartisan Budget Act is good news and should benefit our business late in the year, it will be more of a needle-mover for ICF in 2019. That being said, many of the specific elements of the budget are closely aligned with ICF capabilities and business development focus areas, particularly around public health and infrastructure spending. In addition, almost $90 billion had been allocated for disaster relief in Texas, Florida, California, Puerto Rico and the U.S. Virgin Islands. The Act did provide timetables for the disaster recovery funding, which should move faster, and we expect to see a number of RFPs issued in the coming months.

Now let's look at our second area, our commercial business. Revenues from commercial clients are expected to increase at a mid-single-digit rate in 2018, following the very strong showing we had in 2017.

With respect to our business with commercial energy clients, we anticipate continued revenue growth in 2018. We are executing on more than 150 energy efficiency contracts for utilities across the country, continuing to win new work and expanding the scope of existing work.

At the same time, our new business pipeline in energy markets remains robust. In addition to energy efficiency, we have been gaining traction in energy markets advisory work, particularly around distributed energy resource consulting and in providing our traditional financial analysis and transaction-related valuation services.

Also, our commercial marketing services business is positioned for year-on-year growth in 2018, building upon our growth in 2017. Improved economic conditions should drive expanded marketing and communications budgets, and our new business pipeline continues to grow both in overall size and average dollar value of new opportunities.

In January, we acquired a boutique loyalty and strategy marketing company in the U.K., which is operating as part of ICF Olson's one-to-one loyalty practice. The firm we acquired is a leader in developing loyalty strategies for clients in Europe that we believe we can leverage in our work for U.S. clients. Additionally, this gives us the ability to extend our work into Europe for our current global loyalty clients and to build new relationships.

In the aggregate, our marketing services work for commercial and government clients amounted to over $325 million in revenues in 2017, giving ICF substantial qualifications to leverage in business development.

James Morgan will provide additional details on the impact of the tax law changes in our results. Given our strong operating cash flow, we are able to utilize the benefit of our lower effective tax rate to return capital to shareholders by the initiation of a quarterly cash dividend of $0.14 per share. Our capital allocation priorities, however, remain unchanged. We continue to focus on making strategic acquisitions to expand our access to attractive markets, deepen our domain expertise and improve our implementation capabilities. At the same time, we are investing in business development, innovation and training. We will continue to repurchase shares to at least offset any dilution due to employee incentive programs and will continue to pay down debt.

As you can see, our outlook for 2018 and beyond is quite positive. Our backlog at year-end 2017 was $2.1 billion, of which 51% is funded. We had contract wins last year of $1.31 billion, the majority of which represented new business, and we ended the year with a new business pipeline of $4.2 billion, all of which provides ICF with positive momentum heading into 2018.

I would now like to turn the call over to ICF President, John Wasson, for a more detailed review of our results. John?

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

Thank you, Sudhakar, and good afternoon, everyone. The fourth quarter was a period of solid execution across the key areas of our business, which is continuing as we move through 2018. As in previous periods, the benefits of ICF's diversified business model were clear in the fourth quarter and for full year 2017. Of the 10.9% total revenue growth we posted in the fourth quarter, 5.3% represented service revenue growth, with the remainder due to higher pass-through revenue.

Our government business continued to perform well in the fourth quarter, with revenue increasing by 2.7% overall, thanks to another strong showing by our international government business and a slight year-over-year uptick in our federal business, which more than compensated for the quarterly decline in state and local government revenue.

Excluding the impact of pass-through revenue, federal government revenue would have increased about 1% in the fourth quarter and was stable for full year 2017. This was in line with our original guidance and an accomplishment given the slowdown caused by the transition to a new administration in Washington and the significant delay in getting a fiscal 2017 budget approved.

Federal government revenue accounted for 45% of total revenue for the year, although in the fourth quarter, it dipped to 40% given the substantial commercial revenue growth in the period.

We were awarded a significant number of high-value and strategically important federal contracts in 2017 across a broad group of agencies, including the Department of Health and Human Services and the Department of Defense, and the Departments of State, Homeland Security, Interior, Energy, Transportation and others.

In 2017, ICF launched campaigns for the Centers for Disease Control on 3 priority public health issues: opioid abuse, sepsis and antibiotic resistance. As a result of our excellent work on these campaigns, we've already heard that the client plans to expand these campaigns, and we are very well positioned to benefit from the bipartisan appropriations for the CDC, which includes $6 billion to combat the opioid crisis.

This was also a strong year for us at the Department of Defense, where we won a $93 million cybersecurity services re-compete from the U.S. Army Research Laboratory. Additionally, in the first quarter of this year, we were one of 2 awardees eligible to compete to provide scientific and engineering support services through an IDIQ with the Army Research Laboratory, and we won a new task order valued at $22 million to perform full-spectrum defense cyber operations and research management.

The Bipartisan Budget Act includes approximately $120 billion in additional civilian agency spending over government fiscal years 2018 and 2019, which has provided a more positive outlook for federal government revenue growth in the latter part of 2018 and through 2019.

As Sudhakar mentioned, some of the priority spending areas are in ICF's sweet spots. In addition to the $6 billion to deal with the opioid epidemic, there is $20 billion for infrastructure spending included in the new budget. And there's an additional $89 billion earmarked for post-hurricane disaster relief aid. All these are areas in which ICF has deep domain expertise.

As you know, we see significant opportunities for ICF arising from the housing recovery programs that will be needed following the severe damage caused by the August and September hurricanes. We continue to expect RFPs to be released in support of Community Development Block Grant-funded housing recovery over the next several quarters, and we are investing to ensure that we are well positioned to win a material amount of work in this area.

In the fourth quarter, revenue from state and local clients declined by 11% and was off 3% for 2017, accounting for 10% of total revenue for the full year. The fourth quarter decline was caused by the planned completion and slowdown of certain infrastructure projects and delays in new project ramp-up due to fires and weather conditions in California, which we signaled during our third quarter earnings call. We expect to see growth in this category in 2018 given the large ongoing projects we have won on the West Coast, specifically our high-speed rail work in California, our contracts with Los Angeles County Metro, the California Department of Water Resources, Caltrans, the California State Water Resource Control Board, the Washington State Department of Transportation, and many other state and local clients across our environment and planning service businesses.

Rounding out the government client category is our international work, which continues to post substantial year-on-year improvement. Revenue increased 42% in the fourth quarter and 20% for the year to account for 7% of total 2017 revenue. Here, we are benefiting from a solid backlog and a double-digit increase in the value of contracts won in 2017 compared to 2016. We expect to see continued strong growth in international government revenue in 2018.

Revenues from commercial clients increased 25% in the fourth quarter and accounted for over 42% of total revenue. For the full year, revenue from commercial clients increased 11% and represented 38% of total revenue.

Energy markets remained an excellent performer. Revenue from energy efficiency programs increased at a substantial double-digit rate, and in the fourth quarter alone, we were awarded more than $140 million in energy efficiency work, representing expanded contract scopes, and we also saw a sustained pickup in our energy market consulting services.

Our distributed energy and resources consulting business has performed well and has acquired several new contracts, including utility pilot programs testing distributed energy technologies, which we believe point the way to future utility implementation programs beyond traditional energy efficiency.

We continue to see engagements in our traditional energy market and financial analysis areas, with strong interest in the transactional end of the business associated with development of wind and solar resources. We also have been assisting several utilities with resiliency planning activities.

Based on our current backlog and robust energy markets pipeline, we are looking ahead at continued strong performance in commercial energy. The California energy efficiency market represents additional growth opportunities for us, and the first tranche of RFPs are expected to be released in the third quarter as the state alters its approach to energy efficiency, renewable energy and greenhouse gas reduction.

Our commercial marketing services business also did well in the fourth quarter, and the pipeline increased substantially heading into 2018. The positive momentum in our loyalty business continued in the fourth quarter, and we expect to see additional expansion of that part of our business with the integration of The Future Customer, a boutique firm in London that has been very successful in developing leading-edge strategies for well-known European brands.

In the meantime, we continue to cross-sell engagement services across our client set. Since we integrated Olson into ICF, we have captured revenue synergies of $105 million, representing new business in neither ICF nor Olson could have independently won. In the fourth quarter, our pipeline grew considerably and is comprised of an increasing number of integrated opportunities involving ICF Olson and ICF's legacy clients, providing positive momentum for 2018.

ICF's business development pipeline was $4.2 billion at the end of the year and included 30 opportunities greater than $25 million and 82 opportunities between $10 million and $25 million. Our annualized personnel turnover was 14.5%.

In summary, we are pleased with our fourth quarter results and ICF's positioning this year. We expect to report higher revenue from our key business areas in 2018 and to progressively see the benefits of the growth catalysts that Sudhakar spoke about as we move through the year.

I will now turn the call over to James Morgan, our CFO, for a financial review. James?

James C. Morgan - *ICF International, Inc. - CFO and EVP*

Thank you, John. Good afternoon, everyone. I'm pleased to report on our 2017 financial performance and on the positive momentum that we saw in the fourth quarter.

Total revenue for the fourth quarter of 2017 was $321.2 million, a 10.9% increase over last year's $289.6 million. This double-digit growth reflected increased revenues from both government and commercial clients and the higher pass-through revenue levels that we guided to on our third quarter earnings call.

Service revenues increased 5.3% to $217.8 million, up from $206.8 million in the fourth quarter of 2016. Pass-through revenues of $103.4 million for the fourth quarter were up 25% year-over-year from $82.8 million last year.

Gross profit dollars increased 6.4% to $113.9 million in the fourth quarter of 2017 from $107.1 million in the year-ago quarter. From a margin perspective, the 25% year-over-year growth in pass-through revenues, which typically generate little associated margin, resulted in gross margin of total -- on total revenue decreasing 150 basis points to 35.5% in the fourth quarter of 2017 as compared to 37% in last year's fourth quarter. However, gross margin on service revenue was up 50 basis points year-to-year to 52.3% in the fourth quarter of 2017.

Indirect and selling expenses for the fourth quarter were $86.8 million or 27% of revenue, up from $77.7 million or 26.8% of revenue last year. Roughly half of the $9.1 million year-to-year increase, or $4.3 million, was the result of special charges, including the impact of a strategic tax planning decision to change the mix of some of our bonus payout from equity to cash, as well as severance related to organizational staff realignments, office closures and acquisition-related expenses associated with the acquisition of The Future Customer. As always, we continue to look for opportunities to reduce our costs and to provide a positive return and net benefit over the mid to longer term.

Let me take a minute to discuss the strategic decision regarding our incremental cash bonus expense in more detail. Given the higher corporate tax rates in 2017 versus 2018 and beyond, we elected to pay roughly 10% more of our year-end bonuses in cash instead of in equity-related instruments, which accelerated tax deductible expense into 2017, where we had a higher tax rate. This decision saved the company roughly $400,000 in taxes and also mitigated future share dilution caused by our employee incentive programs. This decision did not change the nature of the bonus payouts to executive officers nor did it change the aggregate value of bonuses. It only changed the mix of bonus for nonexecutives. We will benefit from this decision beginning in 2018, but the decision initially increased our fourth quarter indirect and selling expenses by $3 million.

Adjusted EBITDA of $31.4 million was up 5.2% year-to-year from last year's $29.9 million, in line with service revenue growth. Adjusted EBITDA margin on service revenue was 14.4% for the fourth quarter of 2017, flat with the fourth quarter of last year. As a reminder, adjusted EBITDA excludes the impact of special charges I noted before, including the incremental cash bonus expense, office closures, severance and acquisition costs. For the fourth quarter, reported EBITDA was $27.1 million, a $2.4 million reduction year-to-year in EBITDA.

Adjusting for the $4.3 million of special charges, operating income of $24.5 million was up 9.7% year-to-year from last year's $22.3 million adjusted operating income. The 9.7% growth reflected nearly 2x the growth of our service revenue, evidencing improved operating leverage. As a result of the onetime incremental cash bonus expense and other special charges, operating income reported of $20.2 million was down $1.8 million from the fourth quarter of last year.

Also benefiting our year-over-year operating income comparisons was a 13.9% reduction in amortization of intangibles from acquisitions to $2.7 million in the fourth quarter of 2017 as compared to $3.1 million in 2016's fourth quarter, as certain intangibles became fully amortized throughout the year.

The recently enacted Tax Cuts and Jobs Act gave us a onetime tax benefit of $16.2 million from the provisional adjustment of our deferred tax liabilities and deferred tax assets. This onetime benefit was the key contributor to the $113.6 million -- 113.6% net income increase year-over-year to $27.1 million versus $12.7 million a year ago and added $0.85 to our diluted EPS, which was $1.41 per diluted share for the fourth quarter.

Non-GAAP diluted EPS, which excludes this onetime tax benefit as well as costs of $0.22 per share related to the previously mentioned special charges and amortization of intangibles, was $0.78 in the fourth quarter of 2017 as compared to $0.76 in the prior year.

Now let's turn to the 2017 full year results. For 2017, we had a record revenue of $1,229,000,000, up 3.7% year-on-year and at the upper end of our revenue guidance. Service revenue was up 2.3% year-over-year to $884.2 million from $864.8 million last year. Pass-through revenues were up 7.7% over last year.

While EBITDA decreased year-over-year by -- slightly by $900,000 to $111 million, adjusted EBITDA, which excludes the special items I just mentioned, increased to $117.9 million from $113.9 million in 2016 and was 13.3% of service revenue, up 16 basis points over 2016. This is in line with our objective of increasing adjusted EBITDA margin on service revenue by 10 to 20 basis points per year while continuing to invest in the business to support future growth.

While depreciation and amortization expense of $17.7 million was up from $16.6 million in 2016, amortization of intangibles decreased 12.8% to $10.9 million in 2017 from $12.5 million last year.

Operating income of $82.4 million as reported was essentially flat with a year ago, but adjusting for the $7.2 million of special charges, was up 5.7%. Net income increased 35% to $62.9 million in 2017 compared to $46.6 million last year, primarily due to the onetime tax benefit in the fourth quarter of 2017.

Reported diluted earnings per share were $3.27 for 2017 compared to $2.40 in 2016, an increase of 36.3%. Adjusting for the full year tax benefit of $0.84 per share, EPS would have been $2.43 for 2017.

Non-GAAP diluted EPS, which excludes amortization of intangibles and special charges mentioned earlier as well as the tax benefit, was $3.02 per diluted share for 2017, up 5.2% as compared to $2.87 last year.

Our cash provided by operating activities in 2017 of $117.2 million compared favorably with our guidance of $90 million to $100 million and to our 2016 operating cash flow of $80.1 million. Favorable cash flow was achieved due to excellent collection activity, to include some receivable collections that moved slightly to the left into 2017 as opposed to being collected in 2018.

Days sales outstanding for the fourth quarter of 71 days compared favorably to 78 days in the fourth quarter of 2016. We anticipate DSOs to be in the range of 72 to 77 days, including the impact of deferred revenues in 2018.

With regard to capital allocation, capital expenditures in 2017 were $19.3 million. We utilized $53.1 million during the full year to pay down debt under our credit facility, which totaled $206.3 million at year-end.

Additionally, we made stock purchases under our share repurchase program totaling $30.7 million during the full year of 2017 and exceeded our goal of offsetting the dilution from our employee incentive programs to maintain our fully diluted weighted average share count below 19.5 million for the year. In fact, for 2017, the fully diluted weighted average share count was 19.2 million. As of year-end 2017, we have $100 million left on our current repurchase authorization, which was renewed in November of 2017.

Now I will provide some details regarding our expectations for the full year 2018. First, we continue to expect expansion of adjusted EBITDA margin on service revenue of 10 to 20 basis points in 2018. We expect to achieve this while continuing to invest in the business to improve the ability of the company to scale efficiently and deliver ongoing organic growth.

We are currently forecasting full year depreciation and amortization expense to be in the range of $19.5 million to $20.5 million for 2018. We are forecasting amortization of intangibles to be approximately $9 million. We are expecting full year interest expense of $6.5 million to $7.5 million. Capital expenditures are anticipated to be in the $24 million to $26 million range, somewhat higher than in previous years as we make additional infrastructure investments to further improve the operating efficiencies of the company and invest more in developing intellectual property. We expect a full year tax rate of no more than 26.5%, and we expect fully diluted weighted average shares of approximately 19.1 million for 2018.

Lastly, I would like to mention that as a result of the recent Tax Reform Act and the related reduction in our U.S. federal tax rate, we reviewed our capital allocation strategy. Given our already strong cash flow, we are using our tax savings to initiate a dividend program to pay a quarterly dividend of $0.14 per share, payable on April 16, 2018, to shareholders on record as of March 30. The implementation of the dividend program reflects management's desire to enhance our returns to our shareholders and our confidence in the underlying health and momentum of our business.

With the cash benefits to be received by the Tax Reform Act, the initiation of a dividend program does not change the capital allocation strategy that we have historically employed. We still have significant cash flow to fund acquisitions and to execute share repurchases that, at a minimum, will offset the dilution caused by our employee incentive programs.

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

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

Thank you, James. In summary, we are heading into 2018 with multiple growth catalysts. We also continue to focus on making our back office leaner and more efficient, as James mentioned. This gives us confidence in our ability to continue to generate significant operating leverage while investing in our business for future growth.

For 2018, GAAP earnings per diluted share are expected to be in the range of $3.25 to $3.45, exclusive of any special charges. Normalizing for the impact of the Tax Act, our GAAP earnings guidance at the midpoint represents 16.7% year-on-year growth on total revenue of $1.245 billion to $1.285 billion. The midpoint of our total revenue guidance is equivalent to 2.9% growth in total revenue and approximately 4% increase in service revenue -- effectively all of it organic growth. At the midpoint of our revenue guidance, approximately 80% of the revenue is either already in backlog or in final stages of capture in our pipeline.

Non-GAAP earnings per share is expected to range from $3.60 to $3.80. As I mentioned earlier, our revenue guidance does not include any material impact from increased federal civilian spending given the expected timing of appropriations. The same holds true for hurricane-related recovery spending. We will certainly update you on any developments in these areas as we progress through the year.

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

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And we have our first question from Tobey Sommer with SunTrust.

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

I was wondering if you could give us an update on your perspective of where we sit with community development block grant funding associated with the hurricanes. Seeing some news of HUD dispersing monies down to local governments, but curious what that represents in terms of the time line between that kind of news and RFPs.

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

Sure, Tobey. It's John Wasson. I would say, a couple of things. I think, as you know, the initial appropriation several months back provided about $7 billion or $7.5 billion of total funding for CDBG programs. So I think that money has been allocated to the states in Puerto Rico, and so we're just beginning to see some other piece related to that. The most recent budget agreement that added another approximate $90 billion of hurricane funding still needs to be appropriated, and that will come later in the summer, we expect. And so we really expect to see the majority of the RFPs and most of the bids coming by mid-summer and would expect to see awards later in the summer. So I still think we're early in that process in terms of CDBG-related funding flowing down to the states and seeing the RFPs turn into work.

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

I would just add that of the $7.5 billion, I think $2 billion was CDBG. The rest was sort of FEMA-related, I think. And there was -- most of the work is being done on debris removal, et cetera. I think the housing recovery starts are still to commence. So I think that, that will take its time as we had suggested to you on a call or 2 ago. So I think we are still in the same process as we thought we would be, and we will follow this carefully.

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

How many potential customers do you expect to receive CDBG funds associated with residential reconstruction? And then secondly, is ICF competing for infrastructure-related projects as opposed to residential reconstruction?

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

Well, I think the clients, depending on the states, are going to be different. There could be the states -- in Texas, for example, the state could be a client or be -- come from the governments. In the affected areas, there will be clients. In Florida, their different counties will be clients. I think in Puerto Rico, it's the Governor of Puerto Rico, which is going to be the likely client. So I think that -- all that depends on how the money is divvied up and how it all works. We just have to make sure we follow how the process works out. And I think on the infrastructure side, we might be looking at ways in which we can help utilities and other sort of entities on resiliency, et cetera. So I think that is what we might be looking at, too. But I don't know that I want to say anything more than that.

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

Okay. Is the $90 billion or so in appropriations to date, is that the final total, in your opinion? Or do you think there might be more from what you've heard from prospective customers?

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

If you're talking different customers, they all expect large amounts of money. I think that certain states expect that amount just to come to them. So I think that it's difficult to say. I mean, I think we just have to follow -- if I have to take a bet, I think there will be more appropriations coming.

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

Okay. Shifting gears, could you discuss the -- or give a little bit more color about the pass-through revenues in the quarter and also describe your expectation for elevated levels in 2018? What's driving that?

James C. Morgan - *ICF International, Inc. - CFO and EVP*

Tobey, I can cover it. As far as -- this is James. In Q4, really, there were 2 areas that we expected to have elevated pass-through revenues in the quarter and has -- came to fruition. One was with our international government business with the European Commission. We had some elevated pass-through revenues associated with that work. And then also with our commercial digital marketing business, we had some elevated pass-throughs. Those were the 2 major drivers for fourth quarter of 2017. As far as for next year, if you look at pass-throughs and what we're anticipating, and certainly, this year was a higher-than-normal year for pass-throughs. We were a little over 28% of our revenues or pass-through revenues. Typically, that's 1.5 points or 2 higher than what we typically see. We expect to be -- the next year down a little bit, maybe closer to roughly the 27% range, give or take 10 or 20 basis points.

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

Okay. That's helpful. And 2 other things from you. If you could update us on the size of the California energy opportunities that are coming to market in the third quarter and maybe provide some additional color on your increased intellectual property investment that you described. Is that an overhaul of the IPM? Or anything else you can give color and describing what those intellectual property investments are.

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

I think on the California RFP and energy efficiency, I think the state has decided to outsource more of the energy efficiency business than they used to. And I think that that's something which we were pleased about, and I think we mentioned it an earnings call or 2 ago. So I think those RFPs are coming out. They are traditional energy efficiency RFPs, which you would see -- some of them are nontraditional, and we will -- California is a large market, as you know, and we will look at that carefully. It's also a leading market and they're trying -- and there's lots of pilot projects, et cetera, that they do. So we will see how those things come out. On the intellectual property investment, I think we basically are improving our loyalty programs. We also are trying to make sure that we invest in them to help utilize them in various other markets, including the customer engagement business in the utility industry. And we are also trying to make sure that we have other variance of certain programs, which we -- which I would -- I just don't want to talk about too much, but basically, whether the large market in the utility industry where if we just spend a little bit of money and had the right angle on our existing Tally platform, we could use it in a much more effective way and we would have an immediate potential for particularly amount of sales. So I think that we are -- that's what we are doing, spending more money on -- the IPM is in pretty good shape. Over the years, that investment has continued, but most of the investment there is from client work. So it's really not -- that hasn't required too much of investment from the company.

Operator

Our next question comes from Marc Riddick with Sidoti & Company.

Marc Frye Riddick - *Sidoti & Company, LLC - Research Analyst*

I wanted to follow up a couple of things, a couple of things you covered with the commentary around the CapEx increase. I was wondering if you could shed a little bit more light on that around maybe what you're looking at. Is that from a technology spend perspective? Are we looking at that from a time frame that you might be looking at, that we should think about?

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

Well, as I said, we are -- the largest business and a very solid business for us. It's -- the revenue, as you know, the nature of the revenue is quite sticky. We basically think that if we spend a little bit more money on it and make it a little more modular, we think that we can cater to clients of all sizes. So we are doing that. We're also modifying it to make sure that, as I just said, we cater to the utility industry, which has its own characteristics. And we are adding some other elements to it, which will help us unseat certain competitors in the utility industry, which we think are -- where the industry is using products, which are perhaps not as effective as this would be going forward. So I think that that's helpful because we should be able to get the development done in the next year or so at different times of the year, and we will certainly go to market as we get it done. So I think that's basically what we are doing on that front. We're also spending on the CapEx front. We're also making sure that we modify our back office systems, which are -- which needed some upgrades. We have certain HR system, et cetera, which are going obsolete. So we are trying to make sure that we get those up-to-speed and up-to-date. And I think that we are doing something there also. So that's basically what we are doing on CapEx.

Marc Frye Riddick - *Sidoti & Company, LLC - Research Analyst*

Okay. Great. And I was wondering if you could touch a little bit on the new commercial wins that took place during the quarter. And I wanted to get a sense of, from -- given what you saw there and the pickup that you saw there with new business wins in the commercial space, are we maybe looking at sort of -- just sort of an overall gain in momentum there? And would it make sense to sort of look at commercial as potentially being over 40% of revenue going forward for a while now that you seem to gain some momentum there? And then maybe just from a standpoint of magnitude, is that -- commercial specific, is that one of the larger quarters of new business wins? Maybe if you could sort of help us sort of get a framework of the magnitude of that.

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

I think that we certainly have -- over the last quarter, I think, most of our wins, as I suggested in the overall sales, were primarily new work and we certainly won our fair share of more commercial work than we did -- than we have in the past. I don't know that 1 quarter makes a trend, so we will just wait and watch and see. I think that it will take more than a quarter to -- for us to reach to 40% or more on commercial. I think we certainly are headed that way, and we hope that it continues to grow as rapidly as it did, but we'll wait and watch. But we are optimistic.

Marc Frye Riddick - *Sidoti & Company, LLC - Research Analyst*

Okay. Then one last one for me. I was wondering if you could spend a little bit of time on the international growth and maybe some of the revenue drivers there and some of the trends that you're seeing that perhaps may have had some influence on your guide for 2018.

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

Yes, sure. This is John Wasson. I mean, I think as we've talked over the last year to 18 months on the international side, we have certainly won a significant amount of new contracts and new contracts with European Commission. The issue was activation of work under those contracts. And I think we've seen in the last couple of quarters, certainly, that a return to activating other work and -- is getting back to business as usual. Obviously, the last year to 18 months has been a number of distractions, Brexit, the migration crisis, and I think we're getting -- what you're seeing is we're getting past that, and the European Union, European Commission is going back to its mission and certainly resulting in activation of work under contracts we have won in the last year to 18 months, and we expect that to continue. That's really what's driving the revenue growth right now.

Operator

Our next question comes from Joseph Vafi with Loop Capital.

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

Could you repeat the guidance methodology for the year based on what percent of visibility in your backlog right now?

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

I think we have about 80% of our revenues is in backlog, which is not dissimilar to what it has been in the past, Joe.

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

Okay. And if you kind of look at that visibility, I mean, I know that 2017 was -- there was uncertainty in that 80% number. Would you characterize the amount of uncertainty and how hard that 80% visibility is versus a year ago? Is it -- would you call it really apples-to-apples? Or is it potentially a harder visibility on the 80% versus a year ago?

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

Yes, I would say, certainly, the (inaudible) certainly, Joe, are better the last time when we had this call. The administration had made certain statements, which seem to be quite dire, and I think things have settled down since then, last year when we talked to you. So I think that we certainly think the quality of 80%, and that's what you're alluding to, exactly better than what would have been last year.

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

Okay. That's helpful. And I'm trying to know -- from our discussions during the year, I know you were continuing to look forward to see more second-, third-level political appointees across agencies and departments, et cetera, that kind of help drive new policy and that would maybe ripple into potentially more opportunities for you. Have you seen any progress on that front to kind of help drive those new policies and then potential work for you on those new policies?

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

Yes, I would say there's been some improvement, Joe. There's still more room. There's additional employments that could certainly be made and need to be made. But there's been some progress on that.

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

Okay. And then, I mean, it's nice to see a dividend with the tax break. I mean, it's clearly not something that's going to really slow down any M&A efforts. Was the idea just to -- is the M&A environment changing at all? And it's not that much money really that's going out to dividend versus other capital allocation strategies. Is anything going on in the M&A front that say, hey, maybe we just dividend it out right now?

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

As you pointed out, I think that we basically -- as I emphasize, too, Joe, we think that there is lots of interesting things out there. And so we are not changing our sort of overall allocation strategy. We clearly thought that given that the tax rate had gone down and we have an opportunity to return some capital to shareholders, we should do that. That's the responsible thing to do, that's what we did. But I don't think our posture has changed any in terms of how we want to make sure we grow the business.

James C. Morgan - *ICF International, Inc. - CFO and EVP*

Yes. And keep in mind, we still have a very healthy credit facility with capacity on it for us to help support our acquisition desires as we move forward. So paying the dividend will not hinder our ability at all to do acquisitions. In addition, that we expect to have great cash flow this coming year.

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

Okay. That's helpful. And then just perhaps, finally, I mean, it's been kind of ongoing modest restructuring here and there, and it sounds like you're talking about a little bit of operating leverage next year or this year, I guess. Should we think about these restructurings as helping more long term on the operating leverage front?

James C. Morgan - *ICF International, Inc. - CFO and EVP*

Yes, it certainly will. I mean, as we have talked about in the past, we have been taking efforts over the last few years to continue to improve our profitability. And some of that's been getting reinvested back into the business to grow long term. And as we've mentioned, we're investing more in some of our internal intellectual property as well as some of our systems. So some of the dollars or savings are going into reinvestment back into the company. But at the same time, we will continue to drive margin improvement of at least 20 to -- 10 to 20 basis points per year margin on service revenue. So we believe we can continue to deliver those margins as we move forward. And I think as we ramp up some of our internal programs, we'll be able to deliver more in the future years. But for right now, we're (inaudible) it up to 10 to 20 basis points of improvement per year.

Operator

Our next question comes from Lucy Guo with Cowen and Company.

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

First, to start off, can we please just clarify. It sounds like there's very low hurricane kind of work baked into your 2018 plan. Is it fair to assume given the timing of that, that you may be able to get to a mid-single-digit type growth in 2019?

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

This is John Wasson. I guess what I would say on the hurricane front is we've baked in about $20 million of revenue for disaster recovery into our 2018 guidance. I would say about $5 million of that is Sandy related that will be ramping up $15 million of work from the hurricanes that occurred last summer. I think there is significant potential upside, depending on the funding and timing of the opportunities in front of us. And if we're successful, I think I've -- we've spoken in other forums about our history on the hurricane recovery work. And if you look at that history, certainly in the efforts around Superstorm Sandy, we did about $50 million worth of housing CDBG-related work over 4 or 5 years. I think the maximum revenue certainly in 1 year was about $20 million. So that's one bookend. I would say that's a conservative bookend. But when you think about our history -- and obviously, we did the Road Home. And there, we did north of $300 million in a single year of revenues on CDBG programs and other Road Home program. And so kind of $20 million to $25 million to $300 million is how I would book end the history. I think given the scale and the breadth of the impacts from these recent storms, that's a pretty good range. I think as we said that these opportunities from an RFP perspective will play out this summer and into the fall. We'd expect it to ramp up and win work as we get later into the fall and into the fourth quarter, and then it could potentially be a very significant opportunity for 2019. I hesitate to pick a growth rate for 2019 or give guidance out of a specific percentage. I would just say to you, those 2 bookends, the range of revenues we've had or experienced under Sandy and on the Road Home, I think is a reasonable range to -- is a reasonable way to look at the potential opportunities in front of us.

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

That's helpful. If you consider that, along with potential more further appropriations on federal civilian agencies, especially with the HHS health care, would it be -- do you need to hire more people in order to support those contracts and awards and to support your potentially accelerating organic growth?

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

I mean, again, I would say on the additional civilian appropriations that are in the recent budget agreement, first of all, I would say, what I'm about to say is separate from the hurricane. So this is just talking about facility appropriations, independent of the hurricanes, disaster recovery funds. Again, I think we see those as -- given the timing of the flow of those funds -- firstly, budget needs to be appropriated, the funds need to flow through the agencies. And so we really see any pickup or upside from our guidance as largely a Q4 ramp-up and then really providing material upside in 2019. And so we baked in some ramp-up in Q4 -- small amount of ramp-up in Q4 into our guidance but then see it as really a needle mover, again, on top of the hurricanes for 2019. In terms of the employees, I would say that I don't think we need to hire a significant amount of additional employees to take advantage of any opportunities we see from the additional appropriations as we get later into the year. Of course, there are people business, and of course, increase our revenues. If it's a material increase, we need to add folks. But I think there's room on the margin for periods to increase utilization with the staff we have, and I would expect we'd be able to do that to support the additional appropriations as we get later -- for funding from additional appropriations as we get later into the year.

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

Got it. And maybe a couple of questions for James. On the question of pass-through revenue, I thought you had a large state department contract that was also driving the pass-through variances over the course of 2017. That contract seemed to maybe up for re-compete by late this year. Is that the case? And is that fully baked into your lower pass-through revenue mix?

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

This is John. Maybe I'll start here. It is true. We have a large state department contract. It's actually with the USAID that is a significant contributor to our pass-throughs. That contract is up for re-compete this year. And so that is a potential contributor. We've had that contract for many, many years. I want to say 20, 25 years, I think for 6 or 7 cycle of re-competes. And so we're confident about our prospects on that re-compete. But that contract has had material pass-throughs, and there have been some timing associated with some of the international development work we do in that contract from a health perspective around -- specific in countries, you see developing countries, it's around political issues or USAID approving us to begin work in certain countries. James, do you want to add anything on that?

James C. Morgan - *ICF International, Inc. - CFO and EVP*

Yes. I guess I would just say with regard to 2018 and the level of pass-throughs, what we've done -- what we've baked into our plan for 2018 for that contract is essentially the same level of pass-throughs that we had in 2017. So we're keeping it somewhat conservative until we see a change.

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

But your initial point is correct. The pass-throughs on that contract, they've been down several quarters of 2017 and certainly impacted our pass-through ratio.

James C. Morgan - *ICF International, Inc. - CFO and EVP*

That's right.

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

At the end of -- latter half of 2017, yes.

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

My last question is, James, if you can help us quantify some of the moving pieces in your operating cash outlook in terms of the proceeds from tax savings and then the offset. It looks like a pretty large increase in CapEx, and if there's any other offsets in there.

James C. Morgan - *ICF International, Inc. - CFO and EVP*

For 2018? Or are you referring to 2017?

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

For 2018. So your operating cash flows of $100 million to $110 million is down from the $117 million that you reported.

James C. Morgan - *ICF International, Inc. - CFO and EVP*

Yes. So what we -- I mean, at the very high level, you may recall that we had guidance for 2017 of $90 million to $100 million of operating cash flow. So at midpoint of $95 million, going at $117 million, we beat that by $22 million at the midpoint. And that was really driven by the fact that we had some -- there were some contracts, especially associated with our international work and also some of our domestic commercial work, whereby we receive some advanced payments for the work, and that's why our deferred revenue balances went up. In addition, we had some receivables that basically moved to the left by a few days from 2018 into 2017. And when you sum all that up, it gets you close to that $22 million difference. What we're anticipating for 2018, if you look at kind of our net income and our noncash performance, we're expecting -- if you add that up, you would expect to be just somewhere between $100 million to $105 million of cash flow. And we believe we'll get a little bit of a benefit from a tax perspective just because we've -- our tax rate is down and we have some receivable balances and taxes that will reverse. And -- but then we do expect that our DSO will go up slightly. We were at a little less than 71 days in 2017. We expect that'll get a little bit closer to the middle of our range for 2018, our range being 72 to 77 days. So that's causing a little bit of a use of cash from a working capital perspective. And that's what's taking this to the midpoint of $105 million. Hopefully, that helps.

Operator

(Operator Instructions) And we have our next question from Ben Klieve with NOBLE Capital.

Benjamin David Klieve - *NOBLE Capital Markets, Inc., Research Division - Senior Government Services and Defense Technology Analyst*

I have 2 questions. First, is there a certain segment of your business that has especially strong potential to beat your 2018 guidance?

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

Could you repeat the question?

Benjamin David Klieve - *NOBLE Capital Markets, Inc., Research Division - Senior Government Services and Defense Technology Analyst*

Is there a certain segment of your business that seems like it could -- seems like have a strong potential to beat your 2018 guidance, revenue guidance?

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

I guess, based on at least to the months we made, I think that, clearly, if we get some of the disaster recovery work earlier, that would help us more than what we've anticipated. We've got $15 million built in here. But as a run rate which is higher than that, that certainly helped beat the guidance. And also if the budget process and reconciliation process moves more quickly and the agencies have monies earlier and we start getting projects on existing contracts, we have other contract vehicles, which we -- which are required, that could also up the numbers. So both the civilian agency spending issues and I think disaster recovery are the 2 things which can potentially up the number.

Benjamin David Klieve - *NOBLE Capital Markets, Inc., Research Division - Senior Government Services and Defense Technology Analyst*

Okay. Great. And my second question is, could we expect the CapEx for 2018 to be similar to fiscal 2017 levels? Or will there be any meaningful change there?

James C. Morgan - *ICF International, Inc. - CFO and EVP*

So 2017, we were, as I've said, $19.3 million in CapEx. Our guidance range that we gave for CapEx for 2018 is $24 million to $26 million. So it's about $5 million, $6 million higher at the midpoint. And as we mentioned, that's been driven by some investments that we're making internally from intellectual property perspective as well as we are making some investments in some of our internal systems, HR and financial systems, that's driving capital up.

Operator

And 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 today's conference. We thank you for participating. You may now disconnect.
