ICF International

Pending Olson Acquisition Conference Call

October 21, 2014 at 5:00 PM Eastern

CORPORATE PARTICIPANTS
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James Morgan – *Executive Vice President and Chief Financial Officer*
Douglas Beck – *Senior Vice President, Corporate Development*

PRESENTATION

Operator
Welcome to the ICF International conference call. During the presentation all participants will be in a listen-only mode. Should you need assistance, please signal a conference specialist by pressing the star key following by zero. After today's presentation, there will be an opportunity to ask questions. To ask a question, you may press star, then one, on your touch-tone phone. To withdraw your question, please press star, then two. As a reminder, this conference is also being recorded on October 21st, 2014, and cannot be reproduced or rebroadcast without permission from the company, and now I would like to turn the program over to Douglas Beck, Senior Vice President, Corporate Development. Please go ahead, sir.

Douglas Beck
Thank you Operator. Good afternoon everyone and thank you for joining us on today's call to discuss the pending Olson acquisition. With us today from ICF International are Sudhakar Kesavan, Chairman and CEO; John Wasson, President and COO; and James Morgan, CFO.
During the 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 SEC filings for discussions of some of those risks. Such risks also include the possibility that benefits anticipated from the Olson transaction will not be fully realized, the possibility the transaction may not close and other risks in connection with the proposed transaction. 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 time point—elect to—at some point elect to update the forward-looking statements made today but specifically disclaim any obligation to do so.
Please note that slides accompany this conference call and may be found in the Investors section of our website icfi.com under Recent Webcasts and Presentations.
I will now turn the call over to our CEO Sudhakar Kesavan to discuss today's transaction. Please turn to Slide 3. Sudhakar?

Sudhakar Kesavan
Thank you Doug and thank you all for participating in this call on such short notice.
This afternoon we announced that we have signed a definitive agreement to acquire Olson, a leading digital marketing firm serving a diversified roster of commercial clients. This transaction is a natural extension of the recent organic and acquisition growth of our digital services business around customer and stakeholder engagement and it provides a key element of the Advise, Implement, Improve paradigm that we will now be fully able to replicate in our commercial business.
Olson brings ICF their strategic services and the proprietary technology and analytics that move us up the value chain in our existing strategic communications and digital services business. Our existing business in this area has a run rate of about $150 million in annual revenues. In addition to nearly doubling this business, Olson's expertise has the potential to accelerate our growth in this area across all client categories.
As I have noted, the strategy we are implementing by acquiring Olson follows a path that is similar to how we have built this business on the government side for over two decades. Starting with strategic communications and public relations in the first federal energy efficiency program in the early 1990s, we have developed advisory and implementation services for dozens of government entities around the world that utilize the most sophisticated technologies,

analytics and stakeholder engagement methods. This has become an important differentiator for ICF with many of our government clients.

Just to illustrate the work that reflects how far we have come in this arena, two weeks ago we announced a contract win with the National Cancer Institute to provide comprehensive support for their tobacco cessation efforts valued at up to $100 million over five years. ICF's support of this program combines our behavioral health expertise with our communications and digital media capabilities to address highly-targeted populations and their social networks, such as teen smokers and veterans. By creatively engaging these hard-to-reach populations through online and social media, we are able to deliver tailored messaging and support structures with methods derived from the latest research. This is only the latest example of the sophisticated expertise we bring to government programs utilizing interdisciplinary approaches to communications with digital technology.

The Olson acquisition is well-aligned with our strategy to diversify ICF's revenue sources and increase profit margins as it brings with it a largely commercial client roster and the potential to significantly expand our higher margin commercial business which, on a pro forma basis, accounts for 36 percent of total revenues, up from 28 percent as reported, based on the first half 2014, and this will be an accretive transaction starting in the first quarter of 2015 - neutral for the last 2 months of 2014.

Slide 4 depicts the changing professional services landscape that we have witnessed and responded to over the last few years. Digital services are becoming more and more important for our traditional clients who are recognizing that it is better, cheaper and faster to interact with customers and stakeholders as individuals across mobile platforms, social media and the web. Utilities are using these channels to increase energy efficiency, healthcare companies are using them to influence their clients' choices, transportation companies for transactions and governments for stakeholder engagement. On the commercial side, this has also meant a shift in control of a large part of the IT budgets to the Chief Marketing Officer from the Chief Technology Officer, as digital tools are revolutionizing the marketing function and driving return on investment.

Slide 5 illustrates the actions we have taken to address those digital communications needs of our commercial and government clients. In December 2011 we acquired Ironworks which substantially expanded our digital services offering by providing robust content management and systems integration expertise. This year, we followed on with the February acquisition of Mostra that added additional experience in European strategic communications, and CITYTECH in March, which expanded our content management capabilities in North America. With the Olson acquisition, ICF has the comprehensive and sophisticated suite of solutions needed to develop and manage digital marketing communications programs.

Slide 6 is Olson at a Glance. Olson was founded 22 years ago as a digital marketing technology firm. It is based in Minneapolis where about two-thirds of its 545 employees are located and has major offices in Chicago, Austin and Toronto. In 2009, Olson was acquired by a private equity firm that supported a disciplined approach to financial management that has made Olson a very profitable firm while continuing to grow the firm organically and through acquisition.

The firm works in four major disciplines which I will describe in detail in a moment. The first two, Brand /Digital and Loyalty Programs account for over 60 percent of their total revenues.

Moving to Slide 7, here is a closer look at Brand/Digital, which creates brand identity, marketing campaigns and digital design and implementation work for a group of marquee clients including those pictured here: ECOLAB, an occupational health/environmental management firm, the consumer brand Sharp, and the Belize Tourist Board. This capability provides ICF with a significant scale on the advisory side of digital marketing.

Slide 8 is their 1-to-1 loyalty program offering which uses data analytics to keep clients close to their customers by delivering individualized messages, alerting them to new offerings and creating and managing loyalty programs with millions of individual members. This capability is built around the proprietary CRM-driven Loyalty platform called Tally, a robust software suite capable of reaching consumer, business and employee audiences and delivering analytic insights from the results. Olson is managing loyalty programs for numerous corporate clients, including the ones pictured here: Amtrak, Luxottica, Sun Country Airlines and the recently-won Hyatt program. We see significant opportunities for ICF to leverage the Tally platform for use by clients in our key domains, including utilities, health care, aviation and government.

Slide 9, showing Strategy & Innovation will form another element of our client advisory work. This area collaborates with all disciplines at the firm and utilizes proprietary intellectual property and analytics: Brand Anthropology and Social Media Accelerator, to develop client strategies for brand development, crisis communications and social media strategies.

The fourth discipline, PR/Social, illustrated on Slide 10, involves customer and stakeholder engagement initiatives using social media, events and earned media. There is a multicultural element to this offering illustrated here and very relevant to work we are currently doing for clients, and mirrors Mostra's multilingual and multicultural work in Europe.

Moving to Slide 11, similar to ICF, Olson's client base is well diversified. Their Top 10 clients account for about one-third of their business based on 2013 figures. Olson has been at the forefront of digital marketing; it was founded as a digital firm and has captured the attention and the business of well-established branded companies. It has also been broadly recognized by the industry. Its most recent accolades are listed here on Slide 11, including Agency of the Year in 2014.

Slide 12 sums up the key ways in which Olson is a strategic fit for ICF. It puts us at the forefront of changing professional services landscape and, together with our recent Mostra and CITYTECH acquisitions, it firmly positions ICF in the fast-growing customer engagement space. Olson is a natural complement to our existing digital services business. On the right-hand side of the slide, we have illustrated the complementarity of ICF's and Olson's skills, enabling us to create and manage end-to-end solutions for clients.

Now, I will turn over the call to our CFO James Morgan, who will provide additional insight into the financial implications of this acquisition, which begins with Slide 13.

James Morgan

Thanks Sudhakar. Good afternoon everyone.

We thought it would be helpful to take a look at our year-to-date revenues through June 30th of this year on both an as-reported basis and a pro forma basis to show the impact of the Olson acquisition on our end markets. You may recall that after the Ironworks acquisition, we expanded our Health and Social Programs market to include Consumer and Financial. With the acquisition of Olson, this market, as a percentage of total revenues increases by a few percentage points to 55%.

Based on our current estimates, Health and Energy, broadly defined, will represent over 75% of ICF's total revenues post-transaction, reinforcing the continuing importance of our deep domain expertise in these high-growth markets.

On Slide 14 you will see the same exercise done across client categories. Here the shift following the Olson acquisition is more pronounced with commercial clients estimated to account for 36% of total revenues, up 8 percentage points from the as-reported number of 28%. The key takeaway here, from our perspective is that we have significantly increased our commercial business where there is higher margin potential, yet we have maintained a strong commitment to the federal government space which provides ICF with significant backlog and visibility.

The financial impact of the transaction is detailed on Slide 15. On a pro forma basis, Olson's revenues for the year ended December 31, 2013, was $126 million, and on the same basis, EBITDA margin was 22.5% exclusive of certain pre-transaction expenses such as management fees.

The transaction is scheduled to close by mid-November of this year. We expect the transaction to be neutral to ICF's diluted EPS for the remainder of 2014 and to be accretive beginning in the first quarter of 2015. This is a cash transaction, with no earn-outs, that we are financing through ICF's existing credit facility. As you know, we are a strong generator of operating cash flow, as is Olson, and therefore we expect to be able to bring our net debt-to-EBITDA ratio to below 3 times in short order, within six months of the closing date.

Slide 16 displays ICF's full year 2014 guidance, exclusive of Olson, which we have taken the opportunity to reaffirm given that this announcement will be followed closely by our announcement of third quarter results. We continue to expect high single-digit revenue growth for the year and at the midpoint we are looking for double-digit increases in both adjusted and reported diluted earnings per share, and the cash flow estimate remains the same.

We are firmly within our quiet period with respect to financials for the third quarter and nine months of 2014, so we are not able to provide any additional data on those figures. We will release the full financial statements after market on November 6th followed by a conference call which we hope you will all participate in.

At this point, I would like to turn the call back to Sudhakar for his closing comments.

Sudhakar Kesavan

Thanks James. To reiterate the high points, we are further balancing our portfolio commercial and government clients, increasing our commercial business which should drive margin improvement. Similar to the large Macro acquisition that we completed in 2009, we will invest in a business development infrastructure for Olson to expand their pipeline and accelerate their ability to capture additional share in this fast-growing market. The additional qualification and expertise we will gain from Olson should position us very well to increase our share of the government digital services business. Olson brings intellectual property and proprietary analytics to ICF that we can leverage in our existing businesses and, finally, we have resources across our domestic office network and particularly in Europe that Olson can use to serve its increasingly global client roster.

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

QUESTIONS AND ANSWERS

Operator

We will now begin the question and answer session. To ask a question you may press star, then one, on your touch-tone phone. If you are using a speakerphone, please pick up your handset before pressing the keys. To withdraw your question, please press star, then two. At this time we will pause momentarily to assemble our roster.

Our first question will come from Bill Loomis of Stifel.

Bill Loomis

Hi. Thank you. Good afternoon. Exciting news. It looks like a premier acquisition, but can you just talk a little more about the financials, and when you say double-digit growth this year, are we—that's obviously a pretty big range, 10% or higher. You know, any way you can box that in a little more? Then the margins, you talk about a 22% EBITDA margin. What would be sustainable when we look at 2015, 2016? Is that a sustainable level or do you see that coming down as new business rolls on investments come on? Thank you.

Sudhakar Kesavan

I think to box it in further, Bill, we knew you'd ask this question. 12 to 15%, how's that for boxing in? I think the margins, just like, you know, we were very—we think that they are sustainable but we are going to use some of the dollars to do more business development and there'll be some money spent on integration costs, but inherently the margins are certainly sustainable and I think that from a—what we certainly intend to do is make sure that we quicken the growth and to some extent reinvest some of the dollars associated with the business. So going forward, you know, I think that it will be in the—around the 20% range, so we'll take about 2, 2.5% and reinvest it going forward.

Bill Loomis
Then just to follow in that, James, what's the amortization expected per year and the interest cost?

James Morgan
We're actually looking at providing that as part of our call on November 6th, Bill, so I don't think I want to go into those details currently.

Bill Loomis
But you're using your current line; what is the current rate right now based on where LIBOR is and all that?

James Morgan
Yes, so with the acquisition, obviously at the higher debt level we move up our pricing grid on the credit facility, so it'll be around 2.5%.

Bill Loomis
Okay. Thank you. Congratulations.

James Morgan
Thanks.

Operator
Our next question will come from Ed Caso of Wells Fargo.

Ed Caso
Hi. Good afternoon. Of the top 10 clients, how many are sort of agency-of-record kind of clients and how many of those are coming up for sort of re-bid and renewal?

Sudhakar Kesavan
Ed, I know for a fact that of the top 10 clients I think three or four are agency-of-record and they have—most of the contracts they have won but we can get more specific detail and get back to you on that on the November 6th call.

Ed Caso
So is the rest of the top 10 project-based work or is it some other form of annuity?

Sudhakar Kesavan
No. I think that there's a certain form of annuity in the sense the loyalty platform is an annuity sort of form. The run Amtrak's loyalty program so those are long-term contracts which generate significant revenues and they're pretty sticky.

Ed Caso

Okay, and I assume you're—I don't think you have the capacity on your line so you're going into your accordion to complete the transaction.

James Morgan
Yes.

Ed Caso
What's the rough leverage at the time of the transaction?

James Morgan
We're not going to provide that at this time. I will tell you though within the first six months we expect to be below 3X, but we'll give you an update on our call on November 6th exactly what our leverage will be.

Ed Caso
We did some quick math and we're sort of in the ballpark of 10 times forward EBITDA and 2 times revenue; is that the right ballpark for the valuation on this transaction?

Sudhakar Kesavan
I think it's slightly lower than that. Forward EBITDA it will be more like 9, around 9, 9.5 times, and I think twice revenues is a reasonable number.

Ed Caso
Right. Thank you. Congrats.

Operator
Again, if you would like to ask a question, please press star, then one, at this time. Our next question will come from Tobey Sommer of SunTrust.

Tobey Sommer
Thank you. How much of the legacy ICFI revenue, you know, could be exposed and benefit from the presence of Olson? Because you talk about how it may be able to stimulate growth, I'm just wondering, you know, how—what percentage of revenue could it be applicable to?

Sudhakar Kesavan
Yes Tobey, thanks. Let me go through. First, there are many tiers of synergy which we can talk about. The first one is that Olson at the present time subcontracts some of the technology work to other vendors, so we hope that some of that work can come in-house and that could be an immediate benefit going forward. In addition, we have significant client relationships, for example through the Ironworks and CITYTECH acquisitions which—where we would like to go in and meet with—where we have met with the CMOs, et cetera, but now with the Olson acquisition we certainly have the bandwidth and the ability to do it in a much more sophisticated way. So we certainly intend to go in and meet with those clients. So selling Olson into our existing client set is the net tier. Then of course with the consumerization of technology with the feds looking for ways in which the commercial world does stuff, especially after the healthcare.gov experience, we think that we provide with the Olson acquisition really state-of-the-art what the real world—what the real commercial world is doing, kinds of skills to our traditional government clients which they we think will appreciate.
So those are different tiers of revenues and I think in our verticals we certainly think that in the utility business, as you well know, there's lots of energy efficiency work which is done over digital media, digital platform. In the healthcare arena, the healthcare payers and providers, we

have great insight through the Ironworks acquisition. We are doing a lot of work for healthcare payers and providers and working with ACOs and others, and they're all looking at how they can interact with their consumers because it's—I have, for example, a consumer-directed health plan; I make choices now. So how do I influence consumers to make the choices which will benefit the specific entity? I think that is becoming more and more important. We—in Mostra in Europe we have a very sophisticated strategic communications base and we have a significant presence there so, which I know that Olson would like to work with their clients, US clients in Europe, and they have not had that ability at the moment, plus aviation is an important element. You know, they currently work with one or two airlines on loyalty programs and we certainly hope that we can see what we can do with our existing aviation client base. So there are a number of ways in which we can leverage what they are doing in our existing client set.

Tobey Sommer
Thank you. Could you discuss contracts, visibility, pipeline kind of associated with the business and what metrics will be important for us to pay attention to going forward?

Sudhakar Kesavan
I think just like our commercial business, you know, their pipeline is good but it's not like the government business where we basically look at very long-term, mid-to-long-term contracts. I think they have—their backlog is made up of about 60% hard and soft backlog which is nearly consistent with our commercial business, and 60% is a pretty good number we think. Right now quarter four is just starting and I think most of their backlog really gets developed for the rest of the year in Q4, November and December for the next year. So I think that they are—they have pretty good visibility in their revenue and earnings and it's better than I expected but it's not as good as the government.

Tobey Sommer
Curious, Sudhakar, why no earn-outs? Particularly if we've got kind of the big selling season in front of us.

Sudhakar Kesavan
I'm sorry, I didn't understand the last part. Big selling season?

Tobey Sommer
If they sell a lot of next year's revenue in November and December, you know, why no earn-out?

Sudhakar Kesavan
I think that we are reasonably certain that it's a very established good business. They have a good historical track record which we've seen numbers over the last two or three years and I think there's a repetition this year of the pattern which has been true over the last year or two. So I think that earn-outs sort of hurt collaboration, hurt integration, hurt sort of the whole working together sort of aspect of it, and philosophically I think if we can avoid earn-outs we do, and as you would have noticed in all our acquisitions, we have tried to stay away from earn-outs and I think that that has served us well. So we basically try and work pretty hard to satisfy ourselves that the business is strong, capable going forward and, you know, once we have satisfied ourselves then we do the deal, otherwise we don't because we try and stay away from the earn-outs to the extent we can. So I think that that's fundamentally why we don't have earn-outs and we are reasonably confident that they'll do pretty well going forward.

Tobey Sommer

Thank you very much.

Operator
Our next question comes from Tim McHugh of William Blair.

Matt Hill
Hi. This is Matt Hill in for Tim this afternoon. Just a couple of questions. With regards to the competitive environment and kind of the customer set, the focus going forward, is there any competitors you'd point to for Olson out in the space? Just to kind of give us an idea a little bit better of what they're doing.
Then, I know previously talking the digital interactive, it seems like most of the focus has been on mid-market sized clients. Is that going to change at all, just based on Olson's customer base?

Sudhakar Kesavan
I think that we—they have—Olson's customer base is Midwest-oriented; they have strong relationships in the Midwest and I think that what they bring is these strong relationships and the fact that they've worked with these companies for many, many years. We bring relationships both on the east and the west coast so we think that we can leverage those relationships for them going forward. So I think the focus would continue to be their client set as well as our client set, as I've just answered for—in Tobey's question, and certainly the middle market is a very good focus area for us and if you look at the existing client base of our digital services business it is—a very significant portion of it is middle market. There are some large companies too, but most of it is sort of middle market and we think the middle market is a great area to be in and we certainly welcome growth in that middle market arena.
In terms of competition, you know, they have the traditional competition there. In purely digital agency competition it's Razorfish, to some extent Sapient, the consulting firm; Deloitte Digital and some of the bigger ones, Accenture Interactive. I think the good news is that given the scale we have we can I think compete with them in an effective way now going forward, and especially given the preferred client access we have with our domain area clients, we think that there is some significant leverage we can get from them. So I think that we are pleased with their client set and we are pleased that we can continue to expand ours going forward.

Matt Hill
Okay. Great. Then just—I don't know if you've given a number around this, but looking at post-deal do you have any idea of what the mix overall in the digital American space between government and commercial is going to be specifically?

Sudhakar Kesavan
It's going to be about two-thirds commercial, a third government.

Matt Hill
Okay. Then any ideas, the management team coming over from Olson, plans for integrating the business, how deeply integrated as a unit is it going to be?

Sudhakar Kesavan
Yes, I think we—the management team is fully coming over. The current CFO is going to stay; he's a designee of the private equity firm. I think he's going to stay until the end of the year and then move on, but we certainly—we think that there's enough depth there, and plus we will obviously be looking at that function carefully going forward. But the rest of the management team, all the folks, the CEO, all the presidents of the different—four different lines of business,

the Chief Creative Officer and everybody else is coming over as part of the transaction.

Matt Hill
Okay, great. Thank you.

Operator
Once again if you'd like to ask a question, please press star, then one, at this time. We do have a follow up question from Bill Loomis of Stifel.

Bill Loomis
Hi, thanks. Just following up on that integration, is there any type of retention, or what's going to be involved with that?

Sudhakar Kesavan
Yes. We have given stock instruments to a large number of folks in the company at the senior level and at the mid level which will vest over a period of time, and we believe they are significant value. So we certainly made every effort to make sure that there are significant values which are associated with the vesting schedule and we think that'll encourage them to stay.

Bill Loomis
Is this going to be Olson, an ICF company, or is it going to be—how do you plan on dealing with the company brand?

Sudhakar Kesavan
Yes, I think that for the moment it'll be Olson, an ICF company, and then we'll work with Olson to see how we can—what the brand identity should be going forward.

Bill Loomis
Then just one more thing on the industries. It looks like they're heavy into retail, consumer products, travel and tourism, and you guys don't have a lot of exposure there. I know their services will map well to your customers and your verticals but what are the—when you've looked at this acquisition, what's the likelihood of you providing other ICF services including IT and other types of services to these new vertical markets that they're heavy in.

Sudhakar Kesavan
Yes, I think that we certainly hope to provide significant technology and systems integration skills into their client sets; that's one of the reasons we've done it. I think the—as I said to someone else that they currently don't do as much technology work as they would like to do and I think they sub out some of it so we certainly hope to get some of that work internally. We have more than 500 people focused on commercial clients who do content management, e-commerce, that sort of stuff, and I think we certainly hope to do more of that with their client set.

Bill Loomis
Okay, and then James, just one more question on amortization. I know you don't want to give an amount but is it going to be accelerated, like a two-year type accelerated amortization?

James Morgan
Actually, it's going to be over a 10-year period but it's certainly front loaded.

Bill Loomis

Okay. Okay, thank you.

Operator
Next we have a question from Donald Porter of DGHM.

Donald Porter
Hey guys, how's it going?

Sudhakar Kesavan
Hi there.

Donald Porter
One quick question. So you guys gave the revenue as 2013; what do you expect the 2014 revenue to be, or the trailing 12-month kind of revenue number?

Sudhakar Kesavan
Why don't I say, Donald, that basically as I said, 12 to 15% growth and we—so on the 126 number we've given, you have the range.

Donald Porter
Okay. So we'd expect 2014 to be roughly 12 to 15% higher than what you have on the pamphlet here.

Sudhakar Kesavan
Right.

James Morgan
Right.

Donald Porter
Got you, great. Thanks.

Operator
This concludes our question and answer session. I'd like to turn the conference back over to Management for any closing remarks.

CONCLUSION

Sudhakar Kesavan
Thank you again for participating on today's call on such short notice. We look forward to speaking with you in a couple of weeks when we'll announce the third quarter results. Thank you very much again.

Operator
The conference is now concluded. Thank you for attending today's presentation. You may now disconnect.