Q4 2016
CONFERENCE CALL

PREPARED REMARKS FROM:
Peter T. Dameris, Chief Executive Officer, On Assignment, Inc.
Edward L. Pierce, Executive Vice President and Chief Financial Officer, On Assignment, Inc.
Theodore S. Hanson, President, On Assignment, Inc.
Randolph C. Blazer, President, Apex Systems, LLC

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On Assignment

FOURTH QUARTER 2016 FINANCIAL RESULTS CONFERENCE CALL
FEBRUARY 14, 2017
PREPARED REMARKS

EDWARD L. PIERCE
CFO, On Assignment:

Good afternoon and thank you for joining us today. Before we get started, I would like to remind everyone that our presentation contains forward-looking statements representing our current judgment of what the future holds. Although we believe these statements are reasonable, they are subject to risks and uncertainties and our actual results could differ materially from those statements. Some of these risks and uncertainties are described in today's press release and in our SEC filings. We do not assume the obligation to update statements made on this call.

For your convenience, our prepared remarks can be found in the Investor Relations section of our website.

Please note that on this call we will be referencing certain non-GAAP measures, such as Adjusted EBITDA and Adjusted Net Income. These non-GAAP measures are intended to supplement the comparable GAAP measures. Reconciliations between the GAAP and non-GAAP measures are included in today's press release.

I will now turn the call over to Peter Dameris, our CEO, who will provide an overview of our results for the quarter.

PETER T. DAMERIS
CEO, On Assignment:

I would like to welcome everyone to the On Assignment 2016 fourth quarter earnings conference call. With Ed and me today are Ted Hanson, President of On Assignment and Rand Blazer, President of Apex Systems.

During our call today, I will give a review of the markets we serve and our operational highlights, followed by a discussion of the performance of our operating segments by Ted and Rand. I will then turn the call over to Ed for a more detailed review and discussion of our fourth quarter results, and our estimates for the first quarter of 2017. We will then open the call up for questions.

Now, on to the fourth quarter results. Our results for the quarter exceeded the high-end of our previously announced financial estimates for revenue, and we were within the range of our estimates for adjusted EBITDA. Revenues for the quarter were $620.9 million, up 7.5 percent year-over-year. This marked the twelfth consecutive quarter that our company grew above the IT staffing industry's projected annual growth rate since January 1, 2013. Our growth rate reflected, among other things, the deepening of many new larger customer relationships that we have established over the last three years.

Virtually all of our divisions contributed to our strong fourth quarter performance. Our size and service offerings enables us to grow faster than the published staffing industry growth rate of 4 percent and we believe that we are well positioned to generate solid, above-market revenue growth in the future. Revenue growth came from both our local, mid-market and large national accounts reflecting strong customer demand. We believe, based on current operating performance, that this solid growth will continue into the first quarter.

Our IT business continues to see high demand from its customers, driven in part by greater adoption of staff augmentation as a viable alternative to outsourcing, offshoring and consulting. Wage inflation continues to be manageable, however, in certain large accounts, there is resistance to simultaneously passing along wage increases. Going forward, due to supply/demand imbalances in IT candidates, we believe our customers, as they have always done, will permit us to increase pay wages for our consultants and thereby increase our bill rates.

With respect to recent production, our weekly assignment revenues, which exclude conversion, billable expenses and direct placement revenues averaged $46.5 million for the last two weeks, up 8.8 percent over the same period in 2016. Adjusted EBITDA for the quarter was $70.7 million or 11.4 percent of revenues, compared with $70.7 million or 12.2 percent of revenues in the fourth quarter of 2015. Cash generation continues to be at or above our expectations.

Since closing the Creative Circle acquisition on June 5, 2015, we have repaid $219.0 million of our debt. At December 31, 2016, our leverage ratio was 2.32 times trailing twelve months Adjusted EBITDA. During the quarter we repaid $19.0 million of our debt. We estimate our leverage ratio to be approximately 2.29 times by the end of the first quarter of 2017.

As you will recall, we announced on June 13, 2016 that our Board of Directors authorized a new $150 million share repurchase program. Since inception, we have repurchased approximately 1,362,384 shares at an average price of $39.07. During the fourth quarter we purchased 525,642 shares at an average price of $39.04 and quarter-to-date we have purchased an additional 228,831 shares at an average price of $44.31. We intend to continue to execute our share repurchase program based on share price and market conditions.

We continue to see signs that the ongoing debate regarding the “on demand” workforce or “gig-economy” is accelerating the usage of contract labor. “Fractionalization of human capital” by using the staffing industry’s services is the only way to avoid the risk of misclassification of employees as independent contractors. Our customers have and are realizing this and that is why we believe the secular growth opportunities for the entire professional staffing industry are so attractive. We also believe that we are well positioned to service our customers' IT needs as technology rapidly evolves and is adopted.

On February 9, 2017, we announced the launch of a $50 million expansion for our revolving line of credit and an amendment to lower the pricing of our Term B loan.

Throughout the year, we continued to benefit from further adoption of our development/deployment model (i.e. staff augmentation) and we continue to see solid demand from the end markets we serve.

Ed will give you our first quarter guidance shortly, however, I did, want to comment on our profitability in the fourth quarter. While we exceeded our revenue growth estimate by approximately $3 million, we were at the lower end of the estimate range for adjusted EBITDA. The lower adjusted EBITDA was attributed to the following expenses that are not reoccurring nor were they contemplated in our published estimates for the fourth quarter: $0.7 million in one-time retirement payments to Mike McGowan, $0.4 million in negative currency translation related to an inter-company loan and $5.6 million in higher than projected expenses for cost of services at Apex Systems.

Finally, as you all know from our previous announcements, Ted Hanson has been promoted to President of On Assignment. Ted will report directly to me and will be responsible for operations management.

I would now like to turn the call over to Ted Hanson, who will review the operations of the segments and then over to Rand.

THEODORE S. HANSON
President, On Assignment:

As Peter noted, revenues from our Apex and Oxford Segments grew collectively 7.5 percent or 9.8 percent on a same billable day basis. The Apex Segment had another quarter of double digit growth led by Apex Systems, our largest division, and Creative Circle both of which Rand will address in his comments. While our Oxford Segment grew year-over-year, its performance still trails our internal expectations. Our IT and creative digital marketing offerings continue to show the most strength and demand in those end markets remains solid. Our Life Science and Engineering offerings have shown less demand and in turn lower growth. Now on to the Oxford results.

The Oxford Segment is comprised of Oxford Core, CyberCoders, our permanent placement business, and Life Sciences Europe. For the fourth quarter of 2016, Oxford Segment revenues were $144.8 million, up 1.3 percent year-over-year on an as reported basis, while up 3.4 percent year-over-year on a same billable day basis.

Oxford Core revenues were up 3.8 percent year-over-year on an as reported basis, while up 6.0 percent year-over-year on a same billable day basis. Our Oxford European unit together with our US Healthcare IT practice showed the most strength within Oxford Core, while we faced challenges in growing our engineering, life sciences and HIM practices. CyberCoders, our permanent placement service offering, experienced lower revenue year-over-year due mostly to the same trends we have discussed in prior quarters related to the permanent placement market as well as the seasonal nature of the business during the fourth quarter. Life Sciences Europe was up in revenues year-over-year on a same billable day basis in line with their industry growth rate.

Gross margin for the segment was 39.9 percent, down 280 basis points year-over-year, which was primarily due to a lower mix of permanent placement revenues, which was 13.1 percent of segment revenues for the quarter, down from 15.4 percent in the fourth quarter of 2015.

While the Oxford Segment had revenue growth year-over-year in the fourth quarter, the segment continues to be challenged in finding similar growth in adjusted EBITDA. Over the last two quarters, we have been experiencing lower than historic growth rates at a lower gross margin with higher SG&A expenses. Our Oxford Core business, which is the largest component of this segment, is growing at industry growth rates but below our internal expectations. Also, the lack of growth in CyberCoders permanent placement revenues, against double digit growth comparisons in the fourth quarter of 2015, is having a measurable impact on revenues and gross margin for the segment. Although some of the slowing in permanent placement is a market based trend, our estimates for permanent placement revenue in the first quarter of 2017 show more stability versus the prior quarters. We are also being affected by lower gross margins due to business mix. Our Oxford Healthcare Technology practice, which historically carries a slightly lower gross margin, grew faster during 2016 than other higher margin Oxford practices. As we stated last quarter, many investments made in the Oxford Core business in 2016 have not yet provided a return to adjusted EBITDA. In order to address this, coming out of the quarter and into January we are beginning to make some important changes within the Oxford Core business. First, we are shifting certain leaders and skill practices within Oxford Core in order to better leverage management and be more productive. Second, we have identified some areas where we can reduce expense to find a better return on remaining invested SG&A which we believe will create opportunities for operating leverage in Oxford Core during the course of 2017. We believe that as we implement these actions, together with experiencing a more stable permanent placement market, we can return to higher growth rates and EBITDA margins.

I will now turn the call over to Rand Blazer.

RANDOLPH C. BLAZER
President, Apex Systems:

The Apex Segment, which consists of Apex Systems, Apex Life Sciences (which was the old US Lab Support and Valesta business now rebranded to Apex Life Sciences effective January 2017), and Creative Circle business units reported strong results for the quarter. Revenues for the segment were $476.1 million, up 9.6 percent year-over-year on an as reported basis, or up 12.0 percent year-over-year on a same billable day basis.

Apex Systems, which accounts for 74.0 percent of the Segment's revenues, were up 9.6 percent year-over-year on an as reported basis and paced the Segment's year-over-year growth rate on a same billable day basis. This performance is particularly noteworthy considering the quarterly year-over-year revenue growth for Apex was 17.5 percent in the fourth quarter of 2015.

Apex Life Science's revenue growth was flat in the fourth quarter of 2016 on a year-over-year basis while Creative Circle reported revenue growth outpacing the growth rate for the segment. Our Creative Circle unit continues to perform well, with a year-over-year growth rate for the quarter continuing at a high rate, consistent with our expectations when we purchased them in June 2015.

Overall, the full year 2016 pro forma growth in revenues for the Apex Segment was 14.4 percent and for Apex Systems the year-over-year growth rate was 15.0 percent.

Gross Margin for the segment was 29.5 percent, which was slightly below our estimates. While pricing for the quarter remained stable in our end markets with bill/pay spreads increasing slightly from the previous quarter in Apex and Apex Life Sciences, our gross margin for the quarter was adversely affected by out-of-period adjustments of $5.6 million relating to costs of services at Apex Systems. Excluding these out-of-period adjustments, the gross margin for the Apex Segment would have been 30.7 percent, or approximately 120 basis points higher than our reported results. Later on this call, Ed will make some brief comments on these adjustments.

Our Segment's contribution in terms of EBITDA continued strong with solid conversion of gross profit to EBITDA paced by the increasing productivity of our sales and delivery teams despite the out-of-period costs of services referred to previously. With respect to Apex Systems, our IT staffing division, revenue growth was propelled by a number of factors including:

- Growth in four of our seven industry verticals with double digit revenue growth in Aerospace and Defense, Financial Services, and Healthcare accounts and high single digit growth in the Consumer and Industrial industry accounts.
- The Business Services, Technology, and Telecommunications industry accounts exhibited slight negative growth year-over-year, although the Technology and Business Services industry revenue growth in the fourth quarter of 2015 were our highest growth industry verticals thus impacting our fourth quarter of 2016 results.
- Apex revenue growth continued to be paced by strong revenue growth primarily in "top" accounts. Local branch, mid-market accounts also grew and grew at a slightly higher rate than in the third quarter of 2016.
- Finally, as mentioned, field productivity continued strong in the quarter supporting Apex revenue performance and conversion rates.

The Apex Life Sciences and Creative Circle units continue to see good opportunities for growth with the market for creative marketing skillsets remaining strong. Overall, the Apex Segment had another strong quarter with revenue and earnings growth continuing on a year-over-year basis.

I will now turn the call over to Ed Pierce to discuss On Assignment's overall financial results.

EDWARD L. PIERCE
CFO, On Assignment:

Revenues for the quarter exceeded the high end of our previously-announced financial estimates. Our revenue growth rate for the quarter was 7.5 percent, which was 2.5 percentage points, or 50 percent higher than the published IT staffing industry growth rate. Using the same number of billable days as Q4 of last year, revenues on a same "Billable Day" basis were up 9.8 percent year-over-year. Assignment revenues were $592.0 million, up 8.6 percent year-over-year and permanent placement revenues were $28.9 million, down 11.4 percent year-over-year. The effect of year-over-year fluctuations in foreign exchange rates was minimal.

Gross margin for the quarter was 31.9 percent, which was below the low end of our previously-announced estimates, and down 150 basis points year-over-year primarily due to two things. First, a lower mix of permanent placement revenues, which was 4.7 percent of revenues down 1 percentage point from 5.7 percent of revenues in Q4 of last year. And second, out-of-period adjustments totaling $5.6 million to correct the under accrual of costs of services at Apex Systems. Excluding the effect of the out-of-period adjustments, our consolidated gross profit would have been $203.8 million and consolidated gross margin would have been 32.8 percent, or 90 basis points higher.

The effect of these out-of-period adjustments was immaterial to all prior periods. Approximately one-half related to 2015 and the remainder to the first nine months of 2016. The system and process issues that caused the understatement in costs of services have been evaluated and the necessary modifications made to ensure accurate and complete accruals of costs of services.

SG&A expenses were $142.6 million, or 23.0 percent of revenues. After adjusting for $1.6 million in acquisition and integration expenses, which were not in our financial estimates, SG&A expenses were in line with our previously-announced estimates. SG&A expenses also included two other items totaling $2.1 million that were not included in our estimates. The first item was $1.7 million in expenses related to the retirement of the president of Oxford, which included $1.0 million in stock based compensation. The second item was a foreign exchange loss of $0.4 million on an intercompany note related to the strengthening US dollar that occurred post-election.

Net Income for the quarter was $24.0 million, or $0.45 per share on a diluted basis, up from $19.3 million, or $0.36 per share in the fourth quarter of last year. Net income for the quarter was burdened with after-tax effects of the $5.6 million in out-of-period adjustments and $3.7 million in SG&A expenses not included in our financial estimates. On an after-tax basis, these expenses totaled $5.6 million or $0.10 per diluted share.

Adjusted EBITDA for the quarter was $70.7 million, or 11.4 percent of revenues, compared with $70.7 million, or 12.2 percent of revenues in the fourth quarter of 2015. Adjusted EBITDA was burdened by the out-of-period adjustments and the cash portion of the two SG&A expense items discussed above.

Excluding these items, Adjusted EBITDA would have been $6.7 million higher and above the high end of our financial estimates.

Cash flows from operating activities were $55.9 million and capital expenditures were $6.6 million. During the quarter, we paid down $19.0 million on our long-term debt, which reduced our leverage ratio to 2.32 to 1 at the end of the year. For the full year 2016, we generated Adjusted EBITDA of $285.0 million, cash flows from operating activities of $196.3 million and free cash flow, a non-GAAP measure, of $169.1 million, which reflected a conversion rate of Adjusted EBITDA into Free Cash Flow of 59.3 percent. The reconciliations of the non-GAAP measures to the comparable GAAP measurements are included in today's press release.

Now turning to our financial estimates for the first quarter of 2017, we are estimating revenues of $614.0 to $624.0 million; Net Income of $21.5 to $23.4 million, or $0.41 to $0.44 per diluted share; and Adjusted EBITDA, a non-GAAP measure of $62.5 to $65.5 million. These estimates do not include any acquisition or integration costs.

After adjusting for fewer billable days in the quarter, the above estimates imply year-over-year growth between 6 to 8 percent. The growth rate for the quarter reflects a more difficult comparable as the year-over-year growth rate for Q1 2016 was 17.7 percent, which was the highest growth quarter over the last eight quarters. Our revenue estimates also assume approximately $2.5 to $3.5 million for the estimated effects of inclement weather in the quarter.

Our estimates for the quarter include the effects of the payroll tax reset, which occurs at the beginning of each year. This reset results in an estimated sequential increase in payroll taxes of approximately $11.6 million (or approximately 1.9 percent of revenues) of which approximately $7.4 million relates to costs of services and the remainder to SG&A expenses.

I will now turn the call back over to Peter for some closing remarks.

PETER T. DAMERIS
CEO, On Assignment:

We continue to believe our scale, size and breadth of services has us well positioned to take advantage of what we believe will be historic secular growth for the staffing industry and dynamic changes in the technology world as it moves more into the digital one. While the entire On Assignment team is very proud of our performance, we remain focused on continuing to profitably grow our business and increase our rate of growth. We would like to once again, thank our many loyal, dedicated and talented employees whose efforts have allowed us to progress to where we are today. I would like to now open the call up to participants for questions.