Q4 2016
CONFERENCE CALL

Prepared remarks from:
David L. Dunkel, Chairman and CEO
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Great People = Great Results®

FOURTH QUARTER 2016 FINANCIAL RESULTS
CONFERENCE CALL, FEBRUARY 7, 2017
PREPARED REMARKS

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DAVID L. DUNKEL, CHAIRMAN AND CEO

You can find additional information about Kforce in our 10-K, 10-Q and 8-K filings with the SEC. We also provide substantial disclosure in our earnings release to assist in better understanding our performance and to improve the quality of this call. We have published our prepared remarks within the Investor Relations portion of our website.

I am going to spend a few minutes discussing Q4 and 2016 then turn to discuss market and industry dynamics and thoughts on 2017. 2016 was a year of considerable transformation for Kforce. Although we are disappointed with our full year financial results, as revenues of $1.32 billion are roughly equal to prior year revenues, we are encouraged about our prospects for 2017 and we are beginning to see the benefits of the actions we have taken in support of our longer term strategy. Key among the many changes we made was to consolidate and streamline our sales and delivery organization under a single leader. This change has allowed us to rapidly rebalance and deploy our talent to more effectively meet customer needs and also drive greater accountability for activities across the enterprise. During the fourth quarter, we made a significant investment to enhance our sales methodology and train our sales associates to engage in more strategic conversations and shape solutions with our clients. During the past year, we also made significant progress toward a 2017 rollout of our new customer relationship management system which incorporates our sales methodology to reinforce execution. This rollout is a major piece of a multi-

year effort to replace and upgrade our technology tools to equip our talented associates with significantly improved capabilities to deliver exceptional service to our clients, enhance productivity and accelerate associate ramp up. As we move into 2017, we believe these actions have laid a solid foundation for a reacceleration of revenue growth and improved associate productivity and is very much aligned to our longer-term profitability objectives.

Revenue in the fourth quarter returned to year-over-year billing day growth, as anticipated. Our intra-quarter trends, as well as the momentum we have carried into the beginning of the first quarter, are providing encouraging signs about our ability to accelerate Tech Flex revenue growth in 2017. Earnings per share in the quarter was 36 cents, which exceeded the top end of our guidance by 3 cents. Dave Kelly, our Chief Financial Officer, will elaborate on these trends and results further in his prepared remarks later in this call.

We continued to return capital to our shareholders in the form of share repurchases and dividends, totaling $56 million for the full year 2016. Over the last three years, we have returned $221.4 million to our shareholders in the form of share repurchases and dividends.

Turning to market and industry observations. Entering the fourth quarter, the presidential election and expectations for a slowing period of economic growth caused uncertainty and a hesitancy by our clients to make new commitments for 2017 investments. It was widely anticipated that we were approaching the end of the business cycle and the staffing industry was entering a recession. The surprise election outcome and corresponding policy expectations had a tangible effect on optimism and brought greater clarity for economic prospects. As a result, and together with the impact of our previously mentioned initiatives, we began to experience improving trends later in the quarter. Given the pace of reform under the Trump administration in large and complex areas such as immigration, health care, financial regulation, and corporate taxation, we are closely monitoring the potential impacts, both positive and negative on our business. To date, most of the details regarding the potential reform in these areas have not yet been communicated.

Skilled technology talent continues to be in high demand with the potential tightening of immigration standards only exacerbating the supply shortages. The secular drivers of technology spend remain intact with many companies now becoming increasingly dependent on the efficiencies provided by technology and the need for innovation to support business strategies and sustain relevancy in today's rapidly changing marketplace. Technology investments, in particular mobility, cloud computing, cyber security, e-commerce, machine learning, digital marketing, advancements in the use of big data, and business intelligence have contributed to the demand landscape for technology resources. We expect the ubiquitous nature of technology and continued advancements in these areas will continue to fuel demand, as companies strive to remain competitive and meet evolving customer expectations.

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We are confident in the structure and strength of our organization and believe that the actions taken during 2016 position us well to maximize our market opportunities and we remain on track to achieve our operating margin commitments of 6.3% at $1.4 billion and 7.5% at $1.6 billion in annualized revenue. Our bias continues to be to invest in our business to generate long-term shareholder value. These investments include measured and balanced additions to our revenue generating talent and enhancing and sustaining sales and delivery training and tools. We also plan to continue our technology-related investments, while taking appropriate care to monitor opportunities that technological advancements might provide to enhance our operating model.

We are very pleased to welcome Randy Mehl to the Kforce Board of Directors. Randy has served as a lead investor and director for other companies in the areas of digital marketing, IT services, analytics, and workforce management, as well as prior experience as a sell-side equity analyst. Randy is well known in the staffing industry and we are excited to have him join the Kforce team.

I will now turn the call over to Joe Liberatore, President, who will provide further details on our Q4 operating results. Dave Kelly, Chief Financial Officer, will then add further color on our Q4 operating trends and financial results as well as provide guidance on Q1.

JOSEPH LIBERATORE, PRESIDENT

Thank you Dave and thanks to all of you for your interest in Kforce.

We have been focused throughout 2016 on positioning our sales and delivery teams to operate with greater consistency and discipline to improve the intimacy with our clients, candidates and consultants. This included rebalancing our revenue generating talent between sales and delivery. We ended 2016 with a 9.1% increase in our sales talent while planned attrition within our delivery talent contributed to overall revenue-generating talent declining 2.9% year-over- year. This rebalance is allowing us to reaccelerate our client facing activities and diversify our client portfolio over a broader range of our largest clients. In addition to the improving revenue trends we are seeing, this rebalancing and implementation of our sales transformation initiative we began in the fourth quarter is resulting in increasing strength in client visits, job orders, submittals and send outs in both Tech Flex and FA Flex.

We are pleased to have returned to year-over-year revenue growth in Tech Flex and FA Flex. The improvements we experienced during the fourth quarter in both of these businesses is also translating into a solid start to our first quarter of 2017.

Now for a bit more detail within each business.

Tech Flex, our largest segment, which accounts for 65% of total revenues, improved 1.1% sequentially and 1.4% year-over-year on a billing day basis. As we noted on last quarter's call, we began to see improvements in sequential

revenue trends coming out of the summer months and into October. While the trends slowed a bit due to the Presidential election and usual seasonality around the holiday months, we are experiencing strength in recovery trends from year end assignment ends. Our activity levels have remained elevated and suggest continued strength in demand within Technology. We are also continuing to benefit from positive trends in the length of our average assignment, which we believe is driven by our client's desire to retain qualified and skilled IT talent.

In terms of performance by industry in Tech Flex, we experienced sequential billing day growth in 6 of our top 10 industry verticals, which suggests to us that the demand environment is broad based. Financial Services, Retail and Communications were particular strengths sequentially and year-over-year.

Our Tech Flex sales talent is being allocated to the markets and clients that have the greatest level of opportunity. From a skillset standpoint, our teams continue to focus on areas of greatest demand in high demand development skill sets, such as .net and java, as well as cybersecurity, project management and business intelligence.

We expect Tech Flex revenues to decline sequentially on a billing day basis in the first quarter due to seasonal year-end assignment ends; however, based upon our strong start to the quarter, we expect further expansion of our year-over-year growth rates.

Our FA Flex business, which represents 24% of our total revenues, increased 8.5% sequentially and 2.1% year-over-year on a billing day basis. Our activity levels and assignment starts volume were particularly strong in the fourth quarter, which has continued into the first quarter of 2017. From an industry perspective, 9 out of our Top 10 verticals saw sequential billing day improvement, with Financial Services, Business Services and Retail experiencing notable growth. Following project ends and elevated conversions in the first half of 2016, we experienced encouraging trends in late Q3 and throughout Q4. Early first quarter 2017 signs are also encouraging and while we expect to experience usual seasonal declines sequentially, we anticipate that our year-over-year growth rate will accelerate.

Revenues for Kforce Government Solutions declined 8.5% sequentially, but increased 4.0% year-over-year on a billing day basis, driven by both service and product revenue increases. We continue to see the majority of awards on the T4 NextGen contract going to small, service disabled veteran owned businesses, though we have seen success on a number of these awards as a subcontractor. With the successful recompete on two projects in January, virtually 96% of KGS' revenue base in 2017 is secure. This will allow KGS the ability to focus their efforts on maximizing the capture of opportunities under the T4 Next Gen contract as well as their other business development efforts. We expect revenues for KGS in Q1 2017 to be flat sequentially on a billing day basis, but to maintain year-over-year growth rates at levels that approximate Q4 2016.

Direct Hire revenues from placements and conversions declined 8.8% on sequential basis and 14.5% year-over-year. This revenue stream is currently 3.5% of total Firm revenues, though the fourth quarter is usually the low point due to seasonality. Our objective is to meet the talent needs of our clients through whatever means they prefer, and we will continue to provide this capability, though investments in talent for our Tech Flex business remains our priority. We believe that the longer average assignment lengths that we are experiencing in our Flex business may be an

indication of our client's reluctance to convert these consultants. January Direct Hire revenue is off to a slower start and we expect revenues to decrease in Q1 2017 sequentially and year-over-year.

From a talent perspective, we have been focused on providing our revenue generating talent with the necessary tools to be more effective and efficient in performing their roles, put them in a better position to collect more relevant business intelligence to enable better evaluation of business opportunities and allow us to elevate the value we are bringing to our clients and consultants. As it relates to this, we completed the initial rollout of our sales transformation initiative in the fourth quarter and have also made solid progress on engraining our enhanced sales process and methodology into our new front-end customer relationship management system that will be deployed in 2017. We believe these investments will generate a significant return by improving how we consistently engage with and deliver services to our clients and enhance our effectiveness and efficiency. Looking ahead to the first quarter, we expect to continue to make selective investments in revenue-generating talent, but overall talent levels may be flat with the fourth quarter as we focus on full adoption and integration of our sales transformation efforts. We believe significant capacity exists to grow revenue with the current mix of tenure within our talent population coupled with improved productivity levels as a result of the investments we have made.

I will now turn the call over to Dave Kelly, Kforce's Chief Financial Officer, who will provide additional insights on operating trends and expectations.

DAVID M. KELLY, CHIEF FINANCIAL OFFICER

Thank you Joe.

Total revenue for the quarter of $326.0 million was in line with our guidance. Revenues grew 1.7% sequentially and 1.1% year-over-year on a billing day basis, as the fourth quarter of 2016 had one less billing day than Q4 2015. Total flexible staffing revenues, which exclude our government business, grew 3.0% sequentially and 1.6% year-over-year on a billing day basis.

Earnings per share of 36 cents in the quarter exceeded the top end of our expectations as we continue to see the benefits of our streamlining activities.

Our gross profit percentage in Q4 of 30.6% fell short of our expectations, decreasing 70 basis points sequentially and 100 basis points year-over-year. The year-over-year decline in gross profit margins was driven by a 60 basis point decline in Flex gross profit margins as well as a reduced concentration of higher margin Direct Hire revenue, which represented 3.5% of revenues in the quarter versus 4.1% a year ago.

Our Flex gross profit percentage of 28.1% in the fourth quarter decreased 50 basis points sequentially and 60 basis points year-over-year. The year-over-year decline in flex margins was driven primarily by compression in bill/pay spreads in our FA Flex business, due to a lower mix of project business in FA from a year ago and a 460 basis point decline in our Government business, which is realizing lower margins on some of its recompete wins and had a lower

mix of higher margin product business than a year ago. Tech flex margins are basically stable year-over-year, as we have seen some recent stability in bill/pay spreads, which are down only 10 basis points year-over-year.

At a transaction level, bill rates and pay rates in Tech Flex and FA Flex increased in tandem during the quarter, though we have begun to see slight wage inflation in both Tech Flex and FA Flex, which will continue to put pressure on spreads. Specific to our Tech Flex spreads, we have had particular success in growing revenue within our 25 largest clients, which now represent approximately 47% of total Tech Flex revenues. Most of these significant users of flexible resources are increasingly looking to consolidate spend with fewer providers and, for that, gain escalating discounts based upon volume increases. In addition, Financial Services, our largest industry vertical, has become a larger presence within our overall portfolio, now representing approximately 20% of total Tech Flex revenues. This business tends to have a lower margin profile than the overall average. As we look forward into the first quarter, we expect margins exclusive of the impact of annual payroll tax resets, to be stable.

SG&A as a percentage of revenue was 25.2% in Q4 2016 versus 24.6% in Q4 2015. The year-over-year increase is due primarily to a 60 basis point impact from the investment we made in the fourth quarter to significantly enhance our sales methodology and train our sales associates. The investments we continue to make in technology enhancements and revenue-generating headcount are being largely offset by the benefits we are deriving from our streamlining activities. Additionally, the Firm recognized a benefit of 25 basis points in the quarter for the true-up of performance-based compensation costs as a result of lower than anticipated full year performance. This true up contributed approximately 2 cents to earnings per share versus initial expectations.

Q4 2016 operating margins were 4.7% as compared to 6.2% in Q4 2015. We take a longer term view of our business and expect to continue to make measured investments in additional revenue generating talent and technology enhancements. Our goal is to significantly improve the productivity of our associates and also capitalize on the efficiencies we gain from servicing large customer engagements to create SG&A leverage and improve operating margins.

With respect to our balance sheet and cash flows, our accounts receivable portfolio continues to perform well, though operating cash flows in the fourth quarter of $10.1 million were lower than expected. As noted last quarter, we brought certain back office functions onshore from Manila to our Tampa headquarters in the fourth quarter, which impacted the timing of cash flows this quarter, though we expect this timing issue to resolve itself in first quarter of 2017. Capital expenditures for Q4 were approximately $3.0 million.

We continue to maintain significant borrowing capacity under our $170 million Credit Facility. Long-term debt at the end of the quarter was $115.5 million, an increase of $10.5 million from Q3 2016.

We repurchased roughly 680 thousand shares for $15.0 million during the fourth quarter and returned approximately $56 million to our shareholders in 2016; $44.0 million in share repurchases and $12 million in dividends. We continue to believe that our strong balance sheet and cash flows provide ample resources to continue to invest in the growth of our business while returning the cash we generate to our shareholders using these

mechanisms. However, the first quarter is typically our lowest cash flow quarter as a result of the timing of cash outlays.

With respect to guidance, the first quarter of 2017 has 64 billing days, which is the same number of days as the first quarter of 2016. We expect Q1 revenue to be in the range of $330 million to $335 million, and for earnings per share to be between 22 and 24 cents. This includes the combined impact to Flex Margins and SG&A of annual payroll tax resets in Q1, which is expected to be approximately 13 cents per share.

Gross margins are expected to be between 29.3% and 29.5%. Flex margins are expected to be between 27.0% and 27.2%, which assumes a 110 basis point negative sequential impact from payroll tax resets. SG&A as a percent of revenue is expected to be between 25.5% and 25.7%. Operating margins are expected to be between 3.0% and 3.3%. This guidance assumes an effective tax rate of 38.0%, which is a bit lower than 2016 as we continue to see an increased benefit from Work Opportunity Tax Credits from improved diligence in this area. Weighted average diluted shares outstanding are expected to be approximately 26.0 million for Q1.

This guidance does not consider the effect, if any, of charges related to the impairment of intangible assets, any one time costs, costs related to any pending tax or legal matters, the impact on revenues of any disruption in government funding, or the Firm's response towards regulatory, legal or tax law changes. As we noted on last quarter's call, there will be certain changes in the accounting for equity-based awards beginning in the first quarter; one of which results in excess tax benefits and tax deficiencies recognized upon the vesting of equity awards being recorded in our income statement through income tax expense. The impact of this change depends upon the valuation of our common stock on the vesting dates. Assuming the current valuation of Kforce stock, the impact is expected to be insignificant.

We believe the actions taken in 2016 to realign our leadership, rebalance our sales and delivery talent, refine our sales strategy and streamline our operations set us up to take advantage of a strong sustained market for highly skilled talent during 2017 and beyond. We believe the combination of these actions will enhance our ability to accelerate revenue growth and create additional operating leverage as the Firm grows and the productivity of our associates improves. We intend to supplement our capabilities with selective additions to our revenue-generating talent and technology enhancements and believe that this collective strategy will lead to longer term success. The actions we have taken reinforce our confidence in honoring our longer term commitment to shareholders to achieve an operating margin of at least 7.5% at $1.6 billion in annualized revenue. We also still expect operating margins to be in excess of 6.3% at $1.4 billion in annualized revenue, which we may see as early as the second quarter of this year.

Operator, we would now like to open up the call for questions.

DAVID L. DUNKEL, CHAIRMAN AND CEO

Thank you for your interest in and support of Kforce. I would like to say thank you to each and every member of our field and corporate teams, and to our consultants and our clients, for allowing us the privilege of serving you.