CACI INTERNATIONAL INC
Second Quarter FY19 Conference Call

PRESENTATION

Operator
Good day, ladies and gentlemen, thank you for standing by. Welcome to the CACI International Second Quarter Fiscal Year 2019 Earnings Conference Call. Today's call is being recorded. At this time, all lines are in a listen-only mode. Later, we will announce the opportunity for questions and instructions will be given at that time. If you should need any assistance during this call, please press Star "0" and an operator will help you.

At this time, we would like to turn the conference over to Mr. Dan Leckburg, Senior Vice President of Investor Relations for CACI International. Please go ahead, sir.

INTRODUCTION AND SAFE HARBOR STATEMENT

Dan Leckburg
Thanks, Phil and good evening, everyone. I am Dan Leckburg, Senior Vice President of Investor Relations for CACI International, and I thank you for joining us this evening. We are providing presentation slides, so let's move to slide number two.

About our written and oral disclosures and commentary, there will be statements in this call that do not address historical facts and, as such, constitute forward-looking statements under current law. These statements reflect our views as of today and are subject to important factors that could cause our actual results to differ materially from anticipated. Those factors are listed at the bottom of this evening's earnings release and described in the company's SEC filings. Our Safe Harbor statement is included on this exhibit and should be incorporated as part of any transcript of this call.

I would also like to point out that our presentation will include discussion of non-GAAP financial measures. These non-GAAP measures should not be considered in isolation or as a substitute for performance measures prepared in accordance with GAAP.

Now let's turn to slide 3, please. To open our discussion this evening here is Ken Asbury, President and Chief Executive Officer of CACI International. Ken…

CEO OVERVIEW

Ken Asbury
Well, thanks Dan and good evening, everyone. Thank you for joining us to discuss our Fiscal Year 2019 second quarter results and our two most recent acquisitions. I'd like to thank you all for your flexibility in joining us tonight. With the acquisitions coinciding with our earnings call, we wanted to provide you all with an opportunity for a fulsome discussion and questions as soon as possible this evening rather than waiting until tomorrow morning.

And with me tonight are John Mengucci, our Chief Operating Officer; Tom Mutryn, our Chief Financial Officer; DeEtte Gray, President of U.S. Operations; and Greg Bradford, President of CACI Limited, who is joining us from the UK.

Let's turn to slide 4, please. Earlier this evening, we released our second quarter earnings for Fiscal Year 2019 and announced two very exciting acquisitions. I'd like to take a minute to walk through the highlights related to our quarter then turn to the acquisitions, which John and Tom will comment on as well.

We delivered record revenue and operating income in our second quarter Fiscal 2019. We continue to generate organic revenue growth while expanding margins at the same time. On top of that, we won $1.3 billion worth of contract awards with 70% of that business that is new to CACI.

As you know, the government was partially shut down for much of January and now fully open. We saw no revenue or profit impacts as a result of that in our second quarter. In January, there was a very minimal impact to our outlook, given the partial nature of the shutdown and the business concentration we have in defense, national security, and other essential missions, which were fully funded.

Lastly, we are raising our revenue and net income guidance for Fiscal 2019, reflecting strong continuing operational performance of our core business and incorporating our two recent acquisitions, which I am going to turn to and comment on now.

Let's turn to slide 5 please. On Friday, January 25th, we signed an agreement to acquire LGS Innovations. LGS is a cutting-edge technology company supporting the national security mission of the federal government with a legacy of innovation and invention going back to the original Bell Laboratories. They have over 1,300 employees, a combination of high-end scientists and engineers, of which almost 80% hold security clearances. And given the proprietary and unique nature of their products and solutions, a majority of their revenue is contracted for on a sole-source basis.

On Tuesday, yesterday, January 29th, we closed on our acquisition of Mastodon Design. Mastodon provides rapid design in manufacturing of rugged SIGINT, electronic warfare and cyber operations products and solutions. Their modular designs are small-form factor, light weight, consume much less power and provide mission flexibility to a number of very sophisticated buyers.

While both companies are impressive as a standalone, the combination of CACI, LGS, and Mastodon will be truly powerful in the market. We will produce highly relevant products and solutions to address current and future signals intelligence, electronic warfare, laser communications, C4ISR and cyber requirements. Current CACI products and solutions will utilize the technologies and manufacturing capabilities of both LGS and Mastodon. Likewise, LGS and Mastodon can integrate CACI's set of capabilities into their products and solutions while greatly expanding their access to the CACI customer base. Combined, we will be able to provide truly differentiated offerings in real time spectrum management, signals analysis and exploitation, NEW, photonics, and cyber.

I'd like to take a moment to frame our acquisition of LGS and Mastodon in the context of our long-term strategy. Over the past several years, M&A has been our priority for capital deployment to add high value, highly relevant capabilities. Our acquired companies fill specific gaps aligned to the broader market opportunities and emerging customer requirements. LGS and Mastodon are a continuation of that strategy as we started this about five or six years ago with the acquisition of Six3. And they will contribute to our growth, margin expansion and our ability to solve our customers' most difficult challenges in important areas of each of our markets.

Slide 6 please. We are purchasing LGS for $750 million and Mastodon for $225 million, with a combined purchase price of $975 million. There is also a combined transaction associated tax asset worth about $140 million on a net present value basis. Based on our expectations, this represents a forward EBITDA multiple of about ten times, net of the value of the tax asset. We expect the combined contributions to be accretive to top line growth, EBITDA margins, and net income in the first year excluding one-time transaction costs. This is an all-cash transaction utilizing our existing credit facility. The LGS acquisition is subject to customary regulatory approvals and is expected to close by March 1, 2019.

Let's turn to slide 7, please. This transaction is going to drive significant value and capability to our combined customers. Our unified software-defined, open architecture offerings will be highly differentiated within the market. And putting these companies together strengthens the security of our software and hardware supply chain. This is a key risk area that our customers are paying a great deal of attention to.

Our combined employees will share a commitment to values, integrity, and customer missions. We see that already. And in addition, LGS and Mastodon employees will have access to enhance professional development, training, research and development resources, and a broader customer base. And importantly, the combination will unlock significant growth potential and value for our shareholders. While we expect it to be accretive over the next 12 months, we are most excited about the long-term value of this combination.

With that, I'll turn the call over to John, who will dive a bit better into the transactions. John…

OPERATIONS OVERVIEW

John Mengucci
Thanks Ken and good evening, everyone.

Let's go to slide 8, please. As Ken noted, these two acquisitions are extremely exciting: LGS, an established provider of products and solutions with the unique array of relevant technologies; Mastodon, a disruptive technology company with the unique product portfolio and agile manufacturing capability. Both are high-growth, high-margin companies acquired at an opportune time in their respective growth phases. We are confident these companies will drive significant shareholder value both near and long term.

The combination of CACI, LGS and Mastodon will accelerate our position to the forefront of high-value and sophisticated products and solutions in the areas of signals intelligence, electronic warfare, and cyber operations. Together, we will deliver increased capability, functionality, mission flexibility, and greater value to our customers.

Let me spend a few minutes talking about the value this combination creates for our customers. The simple fact is, customers are looking to procure and deploy capability faster than ever before. They cannot afford to be handcuffed by a long acquisition cycles and multi-year development efforts. That model is unacceptably slow to counter new threats. It's also hardware-centric with upgrades to capability requiring platform down-time and pulling precious resources out of mission execution. This traditional model is just too slow, too costly and too cumbersome.

What customers tell us they need, and are budgeting for today, is agility, flexibility, and speed. Capability must be deployed in near real-time as quickly as new threats emerge without platform down-time. This is where the value of these transactions really shines. Our combined software-defined expertise and agile manufacturing capability will push new SIGINT and EW capabilities out to our customers quicker than ever before.

Slide 9 please. To understand the value of the combination, one needs to see what each company provides. Specifically, Mastodon brings radio frequency, or RF, expertise in small-form factor devices. LGS has high-end signal processing, proprietary detection algorithms, and advanced engineering. Combining these capability sets with CACI's inventory of SIGINT and EW programs, platform integration capabilities, advanced cyber operations, and comprehensive customer access will be game changing. We can now offer SIGINT and EW products and solutions that are smaller, more efficient, can process more data and target more signal simultaneously. This expands our market presence and continues to differentiate what we can and will offer.

Slide 10 please. Let me provide some specific examples of current programs that will benefit immediately from this combination with the two companies, collectively. Today, CACI offers a man-portable SIGINT, EW, and Counter-UAS product within our SkyTracker family of products called the Battlespace Attack Module. With Mastodon's superior sensors and small-form factor devices, we can shrink that product while adding greater capability.

LGS has an array of signal capabilities not currently addressed in current models. The end result is a significantly smaller handheld device with increased capacity, much more capability, and the ability to perform multiple missions and address many more threats

Slide 11, please. Just as both companies effectively provide joint capabilities, each company provides, on their own, ways to grow and enhance future solutions, and product offerings. The first is in the secured communication space with Mastodon. Today, CACI provides a top secret level secured device which includes encrypted software and a set of features available for war fighters. Mastodon adds RF expertise and handheld radio solutions. Combining those two will create a multi-mission capable of communication in SIGINT radio, optimize for contestant environments--basically combining two devices into one with enhanced features that our customers are asking for today.

The second is in the integrated SIGINT space with LGS. CACI currently provides terrestrial layers SIGINT, EW communication solutions. LGS is known for the aerial layer of similar capabilities. Integrating these solutions into a single layered offering will provide multi-domain operations for greater joint mission effectiveness, thus reducing the needs for independent solutions. These were just a few examples of many highly relevant additional and enhanced offerings which the combination of our companies will provide to customers in the future.

With an eye towards growth, these acquisitions further expand our total addressable market into high-value products and solutions in our Intelligence Systems, Cyber, Space, and Communications market. Given the global threat environment of near-peer potential threats and the emergence of more nation-state actors, customers require products and solutions such as those I described to meet those demands. And with 95% of LGS and Mastodon's revenues supporting the Defense Department and Intelligence Community, the business aligns extremely well to budget priorities which, for CACI, places us in an envious position—a position we began to establish with both the acquisition of Six3 and our discussions over the last three years of increasing our investments in SIGINT and EW to provide products and solutions to meet the most pressing national security needs.

With that, I'll turn the call over to Tom.

FINANCIAL OVERVIEW

Tom Mutryn
Thank you, Ken, and good evening everyone.

Please turn to slide number 12. As Ken mentioned, the transactions represent a total purchase price of $975 million. As part of the transaction, we expect to realize a $140 million net tax benefit on a present value basis. This benefit reflects our ability to deduct a portion of the purchase price from income taxes over a 15-year period, effectively lowering the economic purchase price to $835 million.

Over the next 12 months we expect these acquisitions to generate $480 million of revenue and $82 million of EBITDA, excluding the one-time, pre-tax transaction costs of $17 million. This represents an adjusted EBITDA multiple of around ten times. This multiple includes the value of the tax benefit in the expected net synergies. The acquisitions will have an adjusted EBITDA margin of around 17%, significantly above CACI's core margin, which is just north of 9%.

Over the next 12 months, we expect $39 million of additional interest expense and $32 million of additional depreciation and amortization expense. We expect the combination to add $0.30 to $0.35 to GAAP earnings per share over the next 12 months, excluding one-time costs. These numbers include around $0.70 of non-cash, deal-driven amortization expense. All-in-all, these are high-quality properties purchased at the right time with substantial contracted growth already in hand.

We borrowed under our recently expanded credit facility to finance Mastodon and we will also borrow under the facility for LGS. We expect to pay LIBOR plus 150 basis points, post-closing. And we will have adequately remaining capacity to pursue additional opportunities. Pro forma and net debt to trailing 12-month EBITDA is expected to be at 3.5 times be at the beginning of March when the LGS transaction closes.

In December, we entered into an accounts receivable purchase facility to sell up to $200 million of our receivables. This agreement has multiple benefits. It effectively allows us to borrow at lower costs. It provides for increased debt capacity for future acquisitions. It lowers our leverage as calculated to our pricing facility…as calculated to our credit facility, allowing us to move down the pricing grid quicker. Let me note that as a result of the sales of the receivables, we will realize a one-time increase in third quarter GAAP operating cash flow equal to the amount of sold receivables at the end of the quarter.

Please turn to slide 13. Before I turn the call back over to Ken, I would like to provide details on what was a very strong second quarter. We generated $1.2 billion of revenue, 8.6% higher than last year with organic growth at 2.4%, our eighth consecutive organic growth quarter. Pre-tax income was $93 million, 20% higher than a year ago driven by new business wins on contract growth, acquired contracts, continued strong program performance, and cost control.

Slide 14, please. Net income for the quarter was $69 million, 14% higher than our adjusted net income which assumes tax reform within place for all of last year. To help you make the appropriate comparisons we provided a table in our earnings release and presentation reconciling last year's GAAP results to what they would have been assuming a full year of tax reform.

Please turn to slide 15. We generated $56 million of operating cash flow in the quarter. We ended the quarter with net debt to trailing 12 months EBITDA at 2.1 times. DSO was 73 days. This increase over the last quarter was due to payment fluctuations as well as timing of collections due to the closure of certain payment offices in the last few days of the quarter. We expect collections to return to a more normalized level during the fiscal year. And as a result, there was no change to our forecast of operating cash flow for the year of at least $340 million, excluding the impact of our AR purchase facility, which I mentioned earlier.

Please turn to slide 16. Our forward indicators continue to be strong. As of the end of December 97% of our planned revenue will now come from existing business, 2% from recompetes, and 1% from new business. Our backlog at the end of the quarter was nearly $13 billion, 16% higher than a year ago. Funded backlog was $2.5 billion, nearly 30% higher than a year ago.

Our pipeline of opportunities increased from the end of last quarter and now stands at $9.8 billion of submitted bids, with nearly 80% of those for new business. And we expect to submit another $14.3 million of bids between now and the end of June, with almost 70% of those for new businesses. None of these numbers yet include the contribution from Mastodon or LGS.

Slide 17, please. Turning to our fiscal year guidance, we are increasing and narrowing our revenue guidance range to reflect improved performance in the core CACI business and an approximate $125 million revenue contribution from these two acquisitions. We are also increasing our Fiscal Year 2019 net income guidance, primarily due to expectations for increases in the core CACI business profitability in the second half of Fiscal 2019, stronger than anticipated second quarter results, and the positive contribution of the two acquisitions. This will be partially offset by approximately $13 million of one-time tax-effected transaction costs. We now expect Fiscal 2019 revenue of between $4.875 billion and $5.025 billion and net income of between $255 million and $265 million.

With that, I'll turn the call back over to Ken.

CEO CLOSING COMMENTS

Ken Asbury
Well, thank you, Tom and John, I appreciate your comments this evening.

Let's all turn to slide 18, please. I think you can tell by our commentary that we are pleased with our second quarter performance and our prospects for the rest of Fiscal 2019. And we are very excited about the acquisitions of LGS and Mastodon.

We delivered organic revenue growth, single-digit overall growth…high single-digit overall growth, strong profitability, and robust contract awards during the quarter. And the combination again of CACI, LGS, and Mastodon will be truly differentiating for both our company, as well as, the marketplace that we are pursuing.

The acquisitions are a continuation of our strategy to invest in the product and solutions side of our business and to pursue our government's most complex needs. They are accretive on an adjusted basis for both the remainder of our year and over the next 12 months. And we expect strong forward financial performance in the years thereafter. These are high-growth companies adding valuable capabilities that are in line with our customer's most critical investment areas.

Before I open up the call up for questions, I'd like to welcome the employees of Mastodon to CACI, and we will look forward to welcoming the LGS team on or about March 1st. We have a great deal of respect for your…for both teams' cutting-edge innovation, their expertise and their unwavering commitment to their customers' missions. The combination of all three companies is going to be powerful. And I look forward with great anticipation to the accomplishments I know we will make together. So welcome.

Lastly, I would like to thank the employees of CACI for another great performance quarter. I continue to be impressed by your ability to deliver quality for our customers and execute our strategy to deliver growth and margin expansion. Thank you.

With that, Phil, let's open the call up for questions.

QUESTION AND ANSWERS

Operator
Operator instructions.

The first question comes from Krishna Sinha with Vertical Research Partners. Please go ahead.

QUESTION ON CACI'S FORWARD MIX OF REVENUE AMONG SOLUTIONS AND PRODUCTS

Krishna Sinha
Hi, thanks guys. You know, Ken, you alluded to this in your remarks a little bit—but can you kind of talk to us about the trajectory of your product mix? Before Six3, how much of your revenue was what I would consider solutions? Or, you know, product oriented? And now, what will it be, pro forma, once you include these new acquisitions? Like, what's the growth of your solutions

business over the last five years? And how much of your revenue is now from what you consider solutions compared to, you know, traditional maybe IT services work?

Ken Asbury
Yes, Krishna, this is Ken. Thanks for the question.

So, if I go back six years, we were largely a professional services-oriented company. And we did—we had some things that came as a result of acquisitions that still remain with us. We have several product lines like SystemWare and a couple others that have always been—they were part of another acquisition that we did, which were largely services based.

When we went through the Budget Control Act period of 2013, about six years ago, we decided that we really need to find a more enduring place to be in the marketplace. So we started looking for solutions and then seeing where there were attended products, maybe associated with some of those solutions companies.

I would tell you that Six3 was the beginning of that. And that was a little bit of a mix of two very fine, high-end solution companies with a little bit of product that they did and then a mix of services. Over time, that business has continued to grow on a high-single to low double-digit basis—that core business while some of the—during the Budget Control Act period of ‘13 through ’15, we saw some degradation in the professional services and overall services business. So that business has stayed steady and growing—which we have added some other things that we've not even mentioned because they were smaller—that continue to add to that. And they grow at a higher rate than the normal business.

As we look—we go back and forth on this on what the mix is. We sometimes want to measure it with cost plus versus fixed price, but you can't do that because we just added $84 or a couple $100 million worth of largely naval engineering that was on a cost-plus basis.

So if we look at this going forward, we will probably start to get closer to a 60:40 mix in terms of things that we can call overall services—that will be 60% in solutions and products. We haven't differentiated the two of those quite completely yet. So we're going to keep them lumped together for now.

But the characteristic of those is we would expect to get a higher return because we're using either intellectual property or unique skill-sets of our people to drive value to particular customer sets. And as we—how should I say it—as we bring in and fully integrate both Mastodon and LGS, we will have a better picture of that going forward.

QUESTION ON WHAT COMPANIES TO COMPARE THE TWO ACQUISITIONS TO

Krishna Sinha
Okay, and then, just a follow-up there. I mean the margins of these companies are substantially higher than core CACI. I mean, almost double. And it sounds like the capabilities that they're bringing on the solutions side are more in line with what we would consider like the electronics portion of a defense prime. So what's the kind of the comparable set of companies we should now be comparing you to—at least this portion of the businesses—you know, the LGS and Mastodon pieces? Is that more like a Harris? Or, you know, somebody that's kind of melding software and hardware together as an integrator? Or, you know, what's really the comparable set of companies that we should be looking at to look at that part of the business?

John Mengucci
Krishna, thanks. This is John.

I'm not certain all the different product companies out there and, as you mentioned, some of the electronics parts of some of the larger A & D companies. What I can share is what we believe will differentiate our offerings within those product and solutions domains. You know, as Ken mentioned, we're not breaking out products from solutions because both of those in our terminology are actually solutions. We're really looking at disrupting what has always been a full-scale hardware marketplace with software-definable products and solutions, where we can add functionality and capability quickly. We're looking at multi-use devices, which will lessen the burden of carrying a device for a function.

Again, our business model is not to make margin on every hardware device sold. But it is very much looking to put a device in the warfighter's hands that could take on multiple missions with a simple software download, with a very different pricing and go-forward business model. With the same devices reduced training requirements, less devices, make them easier to use. And frankly, taking the high-level expertise of LGS and Mastodon in signals Intel allows us to utilize and create additional IP in this domain.

So it's tough for us to take a look at trying to compare what we're going to do with the product solutions base to what some of the other companies you mentioned are because our business model isn't a large-scale manufacturing. It's more a smaller scale assembly and test of very simply constructed devices, where the smart and the mission is really done in the software side. So we actually think bringing these two companies together with what we've talked within CACI actually provides a very differentiated and disruptive force, which was predominantly a hardware device market.

Krishna Sinha
I will be back in the queue.

Operator
The next question comes from Jon Raviv with Citi. Please go ahead.

QUESTION ON WHETHER CACI IS ADDING A MANUFACTURING FACILITY AS A RESULT OF THE TWO ACQUISITIONS

Jon Raviv
Hi, good evening, everyone, especially to Greg. I'm sorry, Greg. I don't have a question for you this time. But that happens. I hope you're well, though.

Ken Asbury
Thanks, Jon.

Jon Raviv
Sort of dovetailing on Krishna's point about this manufacturing idea—it sounds like you're adding a manufacturing facility. Do you have anything like that in the current business? And how much capacity does that—does this kind of acquisition bring? And how many of your products that you currently create today, could you—I don't know—potentially in-source, if that's even the right word from a manufacturing perspective? Thanks.

Ken Asbury
Yes, Jon. This is Ken. I'll start and John will probably want to add on to it. But we've been manufacturing things on a reasonable scale for quite some time. A lot of the work that we picked up from Six3 has sometimes a card level sort of manufacturing. We have a couple of capabilities around that in the company.

What we're talking about with Mastodon, for example, is not that. A lot of that is done with contract manufacturing and assembled in a—if you will—an assembly facility, not something that we're going to be creating a lot of things out of whole cloth other than the original design. The genius of the Mastodon people is they're really wonderful at designing. They are wonderful at fitting into certain form factors. We will have that stuff made for us and then it'll be assembled, tested, and then supported by the Mastodon team. So this is not—it's not—we're not straying into brand new territory.

In terms of this company, it actually is kind of strengthening a capability we already have and allowing us to do it across more of our, what I would call, software—our software factories that are really coming up with either signals intelligence. They're coming up with counter-UAS. They're coming up with electronic warfare, software solutions that now we can begin to give to a customer in a way that you don't have to—you don't have to always bring, for instance, your ship into shore to change out the firmware in order to upgrade your signals collection system. So think of it as, you know, your iOS upgrade is where we believe we are heading with these kinds of technologies.

John Mengucci
Hey, Jon. What I would also add is—so if we look at this from a pure cost stand, we don't believe that capex is going to materially grow here. The way to think about when we talk about products in this place is what we are growing is the number of digital signal processor engineers we have, which is sort of a software factory kind of a model versus the large-scale, unionized manufacturing facility.

So with the addition of both Mastodon and LGS, we're going to pick up hundreds of digital signal processor engineers. And the good news is, although some are in the Washington, DC, Northern Virginia area, we're going to pick up folks in New Jersey and Colorado and Rochester, New York.

As you've heard Ken and I mention over the last few years, the more we create these beach fronts of highly talented double-Es and software engineers and DSPs, that really transforms this model. So the "manufacturing" is in the software piece, not in the actual hardware.

QUESTION ON FUTURE REVENUE AND MARGIN EXPANSION GOALS

Jon Raviv
Great. Thank you. And then, as a follow-up, once these deals are done, you're going to put up a certain sales number and a certain margin number for the entire business. Is that the right base to use off of which to continue to hit those multi-year targets that, Ken, you've always laid out between outperforming the market and also the margin expansion?

Tom Mutryn
Yes, so as we get into 2020, we will provide guidance and we will think about those in terms of revenue expansion and margin expansion. But make no mistake about that, we plan to do this on

these two acquisitions. They give us a step function and we may operate of a slightly higher basis, but we still want to continue to grow and expand beyond that step function basis.

Operator
The next question comes from Joe DeNardi with Stifel, please go ahead.

QUESTION ON THE LONGER-TERM VALUATION ASSUMPTIONS OF THE TWO ACQUISITIONS

Joe DeNardi
Yes, yes. Good evening, everybody.

I think it's a question for Tom. Wondering if you could just talk about—kind of during the due diligence process and evaluation process—if you could share with us what sort of longer-term assumptions you've used on these businesses to get comfortable with valuation, whether it be sales growth or margin sustainability. Just how you thought about that over the next three or five years. Thank you.

Tom Mutryn
Yes, good. So when we look at our acquisitions, first and foremost, we look at a strategic fit in rationale, consistent with our market strategy focus. So is this the right company for us to buy? And then, once we hit that very important screen, the next step is what does the economics look like? And as a part of that we have extensive reviews of both historical financial performance as well as pipeline reviews for the forecast for the next one, two, three years that the company provides. Typically, there is a good amount of fidelity in those particular forecasts. We will use it as a basis, and we will apply our own independent judgment to that. In many cases, we have internal expertise to understand the customers and the markets and the demand for these various products. Based on that, we forecast, the best we can, revenue and profit growth for years, one, two, three, four, five. And, after that, we undertake a price and value analysis. What is the maximum we are going to pay to generate sufficient return on capital for us? And, hopefully, we will pay something less than that. So it actually has a positive present value. It exceeds our internal rates of return.

I can say that both these transactions have internal rates of return well in excess, or comfortably in excess, of our weighted-average cost of capital. And we think the transactions based on both past performance—LGS, in particular—and future prospects and funded backlog from orders in hand, support the growth, which our models are based on.

Ken Asbury
And Joe, this is Ken. I think another thing for you to consider is, we've done this with a modest amount of synergies that are really associated with reducing some of the back-office duplication that happens when you put, extend organizations together. We have also not modeled in anything related to revenue synergies, in terms of evaluating the value of this.

But we believe very firmly, because we've worked with—for instance, with LGS we've had an ongoing kind of prime sub-teaming relationship with them. We believe that strengthens some of the opportunities that we were pursuing jointly over the years. And we expect that to also offset any potential risk of something we might have missed in due diligence, which I don't think we did because we've spent a pretty good period of time taking a look at that.

QUESTION ON WHETHER MANAGEMENT VIEWS THE ACQUISITIONS AS A BENEFIT TO THE REVENUE LINE

Joe DeNardi
Yes. Thank you, Ken and Tom. Thanks for the color on the process. I guess, I'll assume from your answer that you don't want to quantify what some of your assumptions were.

Can you just talk about whether you see these businesses as more of a benefit from a top line standpoint? I guess, you could argue that it's hard for businesses with margins that high to grow as quickly as businesses with lower margin perhaps. So could you just talk about that dynamic a little bit?

Tom Mutryn
Yes, so I'll start off. So, both in terms of top line growth, we expect these companies to grow greater than base CACI. And these companies both have higher margins than base CACI. And neither of these companies are—I think you implied in the question that it's harder for high margin companies to grow. And I'm not sure, if that's the case. These are high-margin companies. But there is a huge demand—increasing demand for the types of products and solutions that our—that the customers want. So I expect them to both continue to have strong margins and expand revenue greater than core CACI.

John Mengucci
Joe, and I would also add, as we tried to explain in some of our prepared remarks, some of the capabilities and the manufacturing knowledge of both Mastodon and LGS will also play into products such as SkyTracker, that will allow us to sell that product and that solution into more customers, and potentially a lower cost of goods sold level, which would help drive our margins as well.

Operator
The next question comes from Robert Spingarn with Crédit Suisse. Please go ahead.

QUESTIONS ON THE EXPECTED CONTRIBUTIONS OF THE ACQUISITIONS, THE BUDGET TRENDS BEHIND THEIR PRODUCTS, AND DoD CUSTOMERS

Robert Spingarn
Hi guys. Congrats on your two deals here. I wanted to ask a couple of things as well on these.

First, if we could get some sense of this relative sizes or contributions. Obviously one company has got many more employees than the other, but three times the purchase price. So I wanted to reconcile that? And then, you mentioned that you are acquiring these two at a very opportune time. Maybe this is for you, John. You know, what are the budget trends behind the products that these companies make? And to that point, are these more primarily oriented toward Army and Marine Corps-type products.

John Mengucci
Okay. Let me start with the last question, first.

So budget trends. Yes, Rob, today and I'll sort of put them in two different groups. If we look at LGS—well-established company. Has been out there. Their foundations are all the way back to the Bell Labs. And the capabilities that they have are going to look at the same type of customer set that our core-CACI has across DoD, and across maybe the Intel community customers. If we look more on that the solutions, it smells more like product side.

We look at Tusk—at Mastodon—sort of gave you what our codename was there, Rob.

Robert Spingarn
So that's good to know.

John Mengucci
Yeah, great.

So, budget trends. There are clearly any of the DoD or the Intel customers that are looking for signal Intel and where electronic warfare and where this electromagnetic spectrum sits today. And budgets—Army, Marine Corps, Navy, Navy surface ships, Navy combat destroyers—all of those programs are creating additional programs to bring the actual power of signal intelligence into their large-scale products and small-scale form factor radios.

So where we see this market going is growing. We see the Army all—I am sorry—we see all DoD forces and most of the Intel Community spending quite a lot of money in these areas. This has been an area that has been neglected for decades within the US.

And you don't have to read too many global conflicts out there where electromagnetic spectrum is very important. We can talk about the Russians, talk about the Chinese and others as well as lower-level nation state actors. So, counter-UAS, cyber signals, Intel budgets are growing consistently there. And we believe that we have a software-defined way to get capability out there faster, which should allow us to grab a larger share of those budget dollars.

Ken Asbury
And Rob, this is Ken. To take it up a chunk—if you look at almost what every service is talking about—it is the Navy. It is the Army. The Air Force. They're looking at how do they improve their multi-mission domain? How do they deal with air, land, sea, cyber, space? And how do they bring those all into an integrated picture? We believe that there's going to be a lot of magic software behind that. And it's going to become less about silos of very capable hardware that do things that have to be integrated in complex ways.

We're going to see much more simpler devices. Think of everything that you have in your environment as a sensor. And you use that software then to determine what's in your environment; analyze whether it's a threat or it's a friend, decide, give you courses of action that you can take and do all this on your wristwatch. Because that's the speed of which battle is going to be fought in the future. And we're just getting to the point in…from buying…if you will, from a buying priorities, where all of the services are putting this as one of the—at the tip of where they need to be.

We've been fighting counter-insurgency, counter-terrorism missions for a long time. If you go to the National Security Policy, that is based on a large nation power again and potentially having a conflict either on land, on air, or all the above. Then you are going to need to—how to integrate all of these lethality capabilities that we have in a completely different manner than we have today. So the notion of joint is driving all of this integration. And I think we're in a really good time to be having these kinds of companies—to get these kinds of companies in our portfolio.

QUESTION ON WHEN MANAGEMENT EXPECTS ORGANIC REVENUE GROWTH TO INCREASE OVER THE PRESENT RATE

Robert Spingarn
Okay. And as the questions for Tom—just the low 2% type organic growth, 2.4%, I think it was in the quarter. And it's been kind of that way for the last several quarters. We're seeing some of the peers—and, again, I'm speaking about organic growth—more in that mid-single digit neighborhood. When do you think you might inflect up into that direction?

Tom Mutryn
Yes. Good. Thank you.

So, well, and we are in the very mid-early stage process of looking at our FY 2020 plan. And we committed to grow 1% to 4% greater than the addressable market. And we said all along that we expect the addressable market to grow approximately 3.5% as we get into 2020. So at that point in time, I would expect us to have the market potential to realize those growth levels that we committed to—again, still early in the planning process.

And I will point out that when we look at both the awards that we've been receiving and the 1.5 times book-to-bill on a trailing 12-month basis as well as a very robust set of opportunities--bids submitted, bids under review, those do support a nice quarter.

Operator
The next question comes from Cai von Rumohr with Cowen and Company.

QUESTIONS ON PERCENT OF REVENUE OF THE ACQUISITIONS ARE WITH DoD AND INTELLIGENCE COMMUNITY CUSTOMERS AND THEY COMPETE WITH

Cai von Rumohr
Yes. Thank you very much. And exciting acquisitions, guys.

Ken Asbury
Thanks, Cai.

Cai von Rumohr
So what percent of the revenues of both of these companies are with DoD and Intel customers? And can you give us some specifics of who do they compete with?

John Mengucci
Yes, Cai. Let me start off with sort of the mix of business. If I looked at Tusk—predominantly firm fixed price. Predominant customers are going to be your Special Operations Group and some of your special purpose teams. Our growth trajectory for that business, over time, is to reach more of those special units, where they were the first groups who hit some of these very unique signals that they need to: one find, then two, defend against, with a future growth strategy of getting into the Green Army and into that radio mix of multi-use devices. The work is predominately firm fixed price, as you would imagine, because they're more product-focused.

On LGS—really across DoD. Just about every Intel Community customer. Long-standing relationships, some of them two and three decades long. About 60% of their business is cost plus, Cai. But it's much more of sole source work, which is based on their deep knowledge of the domains that they serve. So when we talk about higher-margin business, even at cost plus, that type of the work in the past will continue to demand the higher fee than some of the lower level CPFF engagements. And the rest of their business is a mix of firm fixed price and time and material customers.

The other way we like to talk about our businesses—professional services, managed service and solutions work, very minimal professional services revenue. Some of it out in the field supporting products that they deliver. So just about all of the remaining revenue for both companies will today, in the future, all be considered solutions work.

QUESTIONS ON THE CULTURAL FIT OF THE ACQUISITIONS AND WHO THEY COMPETE WITH

Cai von Rumohr
Terrific, thank you. And then, so the second part of that question—who do these guys compete with? And, I mean are these guys—you mentioned that you worked with LGS. What do you view as the cultural fit—so first question.

And I think the couple have asked it. You know, it's like who are the guys—you guys really go head-to-head with to win business at these two new acquisitions? And what is the cultural fit? Because this looks like a step, kind of, even further into a product business than you have done before?

John Mengucci
Yes, so let me touch on the cultural fit, first. I think Tom mentioned earlier—our M&A strategy in what we look for in companies—that we will look at their capabilities, the customers that they serve, and not just the company "cultural fit." We believe both companies are—I can tell you Tusk is led by a management team with decades of creative and innovative leadership over a team that has the right stuff and a very innovative culture. The fact that they had many years working at other companies—solutions companies, product companies—they really saw the future being software-defined devices and a much agile and a much easier way to buy products. They are going to go in a path that, beyond serving unique customers, going into the mainstream customers.

LGS, from our view, is the "go-to" company for leading-edge wireless. Software solutions. Long years of engineering excellence. Long history of solving some of the nation's most challenging problems. Very similar to the culture set that we have today.

When you mentioned this, this is something that's going to get us further into the product side. We actually see this as the next step beyond where Six3 brought us into the solutions path. I think Ken mentioned that earlier. I mean, just as Six3 started us on our path to more highly differentiated solutions in the Intelligence Community, in the last five years, we have a taken a lot of their solutions and put those into the DoD area, and that actually created more commercial-like solutions like SkyTracker.

We honestly believe that CACI assures platform integration. Our development programs are perfect programs for both LGS and Six3 to be complementary in the signals domain and for Mastodon and Six3 to be very complimentary in some of these higher-end products.

So, pound for pound, we see the culture of both companies extending what we already began in the solutions space. Some of the solutions are going to be more FFP products and some are going to be more for fixed-price solutions business.

Ken Asbury
Yes, Cai, this is Ken. On the competitive side, we are going to see—we will probably see Harris and Thales and some of the other smaller device manufacturers that we will go up against. The LGS business is very similar to the kinds of competitions that we would have had using—from our Six3 business.

But, in the—some smaller very, very high-tech, very focused companies to some of the divisions of some of the larger businesses, we have been able to grow that side of our business at high single, low double-digit, pretty effectively for the last five or six years. We expect that and maybe even a little bit more, because now we have a little bit more of bulk. We have a few more laboratories where we can do our own work in. We have a geographic and a larger customer footprint. So I'm excited about that prospect of the LGS and Mastodon joining our business.

Operator
The next question comes from Sheila Kahyaoglu with Jefferies. Please go ahead.

QUESTION ON FACTORS BEHING THE HIGHER MARGINS IN THE SECOND QUARTER

Greg Konrad
Good evening. It's actually Greg on for Sheila.

I just wanted to apologize ahead of time for not asking about the deal but margins in the quarter trended up after having some pull-forward in Q1. Was there anything unusual in the quarter from a margin perspective and how should we think about that going forward?

Tom Mutryn
Yes, there is nothing unusual. I think it was pretty straightforward. So it's a nice margin quarter.

So I think for the core CACI business, for the full year, we are sticking through the original EBITDA margin guidance—10 to 30 basis points above 2018. 2018, I believe, was approximately 9 percentage-ish. We had some one-time effects, and so we have adjusted for that. So we should be getting margins within those particular levels over the last couple of quarters for a nice margin quarter.

QUESTION ON HOW SOON THE SALES CYCLE CAN TAKE EFFECT AND ITS LENGTH

Greg
Thank you. And then, just one follow-up, you mentioned that you don't include revenue synergies when looking at these deals. But can you maybe talk about the sales cycle? You talked about some of the synergies across the businesses. Is this something that can take effect fairly quickly? Or is the sales cycle a little bit longer?

Ken Asbury
Yes, Greg. This is Ken. The sales cycle is going to vary. Obviously, there is probably deals that we are already working on. I'm not—I couldn't name them now. And I probably wouldn't just for competitive reasons. But there is probably deals we are working on.

And then there is going to be things that, as people get to know each other, things that may have looked a little too large or too complex, or maybe beyond one group going and pursuing. That's what we've begun to see between—I mean our whole—our entire thrust in electronic warfare has come out of the—sort of the brilliant engineers and scientists at the Bits side of Six3 and some of our traditional Army folks that have been working at Aberdeen. And those guys working collaboratively are now going after much, much larger deals and being very successful in bringing our technology into being discriminators in a variety of jobs, some of those of which we won last quarter.

So, not putting revenue synergies in is akin to us having an honest appraisal on just the financials, going forward. And to tell you, or to tell the investment community, that we have done all, that's one of our screens for taking a look at whether we want to do a deal or not. Does it make sense financially? And revenue synergies, they can make that look a little better. But we don't include them for that purpose. But I mentioned them because in a deal like this, where we are beginning to work together, or have worked together, they could make a difference in reducing any forward-looking risk.

Operator
The next question comes from Tobey Sommer with SunTrust. Please go ahead.

QUESTION ON THE EFFECTS OF THE GOVERNMENT SHUTDOWN ON THE LABOR POOK IN THE WASHINGTON, DC AREA

Joseph Thomson
Hi, this is Joseph Thomson on the online for Tobey tonight. Thank you for taking my questions.

My first question is related to the shutdown. How has the shutdown affected the labor pool in the DC area? Are you seeing an increase in skilled labors with security clearance and looking to switch to the private sector? Thank you.

Ken Asbury
Yes, Joseph, we have been at it a month, and I don't know that we are going to observe anything like that.

I think there is a concern. When we went through the Budget Control Act, we drove a lot of really good talent into other parts of industry, because frankly the government being always dependable—and then you go through something like this, something like that—I'm sure that there are some folks that may have been on a cycle to go into a government job or, you know, an industry—maybe even coming to us. I haven't heard any of these reports. But, let's use it as hypothetical. All of a sudden that division is shutdown. In our case, it was less than 300 folks that were on again and off again. And from a revenue impact, it was less—it was about a million to a million and a half [dollars] a week, depending on which week you were talking about. So, it was quite de minimis.

I do believe we were on the ascendancy, again, as the budgets came back and as we had a kind of resurgence in the interest in national security, and there was a lot of spending there. So could that have an effect? I don't know one month is going to make that big of a difference. If it happens again and it lasts a long time, then maybe we ought to talk about it at some time in the future.

QUESTION ON WHETHER CACI WILL EXPAND WHERE THERE ARE EMPLOYEES IN OTHER GEOGRAPHICAL AREAS

Joseph Thomson
Okay, thank you. And then, just a quick follow-up to something you mentioned earlier. You guys mentioned that Mastodon and LGS both had employees in other regions. Do you have further plans to expand—interest in expanding where you're locating employees in other regions? Or just for those specific companies?

Ken Asbury
Well, in this case they had a footprint that are—that you know are already there. And we are not going to disturb that. We actually love that idea to be honest, so we are not—we are not always fishing in the same pond, in the Delmarva region, to trade systems engineers or digital signal processing engineers. Folks like to live in other parts of the country. And there are also some really, really smart people that love living in particular areas. And we like that because that gives us another foundation to go recruit from a different set of universities rather than the ones that are always here.

As to what CACI is thinking about—we are always thinking about that now as we want to diversify where the labor base comes from. And we want to mine locations where there are pockets. We took our Shared Services Center to Oklahoma City. And in less than two months, we hired just a fantastic group of people there that love to live in the central United States. And that helped us in a very large way.

We see doing some of that, with some of our technical resources in the future. I believe we spoken about—over the last couple of conference calls—about taking one of our agile software facilities, a classified one, and moving it maybe into Colorado to where we can do things there. We have our network capability. And the fact that we are living in the cloud now allows us to be anywhere. We don't need to be close to our servers, or any of that stuff, including for some of our development environment. So, geography is sort of a new strategy for us. It's just got to make sense, and we have got to have enough of a book of business there for us to invest in it.

John Mengucci
Joe, I would also add with the connections of LGS, you know there is a company that's got two acres of land space in New Jersey, PhD, scientists, and engineering folks, and an ever-growing university relations program was actually we will infuse into the larger CACI to be able to give us access to even a higher level of talent.

Operator
The next question comes from Josh Sullivan with Seaport Global. Please go ahead.

QUESTION ON THE ORIGIN OF THE TAX ASSETS OF THE ACQUISITIONS

Josh Sullivan
Good evening and congratulations on the deals here. Can you just give us a little background on the origin of the tax assets you are acquiring? Just trying to understand how they were created.

Tom Mutryn
Yes. So, Josh, we are not acquiring a tax asset. So these companies did not have tax-loss carry-forwards, for example. The acquisition is creating that tax asset.

So the federal tax law allows companies, when they acquire 'S' corporations or certain LLCs, to depreciate a portion of the purchase price over time, for federal tax purposes. That depreciation is straight line over 15 years. And so, with a high degree of certainty, assuming tax laws do not have material changes, we are planning to realize additional tax depreciation, which turns into tax savings for 15 years, and the present value of that is approximately $140 million. So, the structure of the transactions allows us to take advantage of those provisions in the tax code.

QUESTIONS ON CACI'S CAPACITY FOR FUTURE ACQUISITIONS AND FUTURE ACQUISITION TARGETS

Josh Sullivan
Okay, got it.

And then, just looking at the M&A strategy going forward—do you think you still have headroom to do anymore deals? Do you want to pay down the leverage? And then, do you think this commercial model of owning the IP and taking advantage of some manufacturing leverage—will that be the focus of the targets going forward do you think?

Ken Asbury
Yes, Josh, this is Ken. I think when we are done with this one, I think we will be levered at about 3.5 times, 3.6, something like that. So, we have a little bit of dry powder going forward. You know, M&A is our first priority for the deployment of capital, and that will continue. That is not going to change. We are very active in the space. As to are we going to add on to this? The answer would be yes, if the opportunity presents itself. But we have other markets that we want to fill gaps and build capabilities in.

If I look at what we have been doing with M&A over the past five or six years—since John and I have been here—it has been to evolve the company away from being a short-cycle business, where the business was more impacted by the changes in budget that we saw from the Budget Control Act. I mean, I came in eight days before that was enacted, and it really had a major effect on the business.

And, strategically, we have been moving towards a place where we wanted to be more mission-oriented, because nobody cuts a mission. They always cut the logistics. They cut training. They cut maintenance. But they are not going to cut a mission, because that's the sole reason that they get there. So moving more into mission space, moving more into spaces where we are sitting side-by-side with the customer to make sure that their value proposition gets realized has been the strategy.

So there are other elements of our business where that is resident. So if there was an opportunity—by the way, we like this space. We are by nowhere near capacity. What this does, it gives us more capability in our Space business, our Intelligence Solutions business, our Cyber and . . .

John Mengucci
Communications.

Ken Asbury
. . . Communications, and the whole notion of C4ISR…sorry John was mumbling, and I couldn't pick it up. But, if something presents itself in Business Systems, that is really a good thing. We also see that as a big business, and it has been a good business for us over the years.

So we will be acquisitive. Obviously, we have spent close to $1 billion, or slightly less because of the tax features of this one. We are incredibly happy with the two companies that we bought here, but we will have our eye out.

Operator
The next question comes from Edward Caso with Wells Fargo. Please go ahead.

QUESTION ON THE AMOUNT OF DEPRECIATION AND AMORTIZATION AND INTEREST EXPENSE FOR THE ACQUISITIONS INCLUDING IN THE REVISED FY19 GUIDANCE

Edward Caso
Hi, congrats on your deal.

Tom, thanks for the disclosure on tables 12 and 17, but if I could parse a little bit here. Instead of the forward 12-month view, how much of that D&A and how much of that interest falls, is implicit, in the annual guidance that you gave us—table 17?

Tom Mutryn
Yes, so. And just let me pull up the tables—17. I think, I know which one you are referring to…

Edward Caso
Yes, that's just the annual guide. I just want to know, if you offered it in a…over 12-month basis, I was trying to figure out how much falls this year?

Tom Mutryn
Yes, so we would just be relatively linearly prorated. So, for one transaction I would say approximately 4/12ths will fall into FY'19.

Edward Caso
Okay. Is there a…because they are off in closing by about a month on the timing, that's why.

Tom Mutryn
Yes. So, four is probably close enough. So maybe it would be like four and a half times. One company is smaller than the other. So we closed Mastodon, $200 million. $700 million, or $750 million for LGS. So that's the preponderance of the interest and intangible amortization. So 4/12th, I think, should be sufficient.

QUESTION ON WHY THE FY19 OPERATING CASH FLOW GUIDANCE WAS NOT INCREASED

Edward Caso
So you are offering…you are bringing on some nice higher margin businesses here—meaningfully higher EBITDAs. But you didn't change the operating cash flow guidance. Was that—do you think the payment thing is going to last longer? Or is that a bit of a fudge for the partial shutdown? I am just sort of curious why you didn't increase the OCF number?

Tom Mutryn
Yes, sure. What we did is, besides having the positive contribution of these two enterprises, we do have the transaction costs associated with the deal—the attorney's fees, banking fees, various employment-related one-time cost. And so, net-net, we increase our margin. But I think $5 million on the top and bottom end of the range, considering all the moving pieces. And so that was not material enough to suggest that we will increase our operating cash flow guidance.

Edward Caso
Alright, thank you.

Operator
Again, if you have a question, please press Star then "1."

The next question is a follow-up from Jon Raviv with Citi. Please go ahead.

QUESTIONS ON HOW THE ACQUISITIONS CAME TO CACI'S ATTENTION AND THE LAST TIME CACI INTEGRATED TWO ACQUISITIONS AT THE SAME TIME

Jon Raviv
Hi, guys. Thanks for going late tonight.

Ken or John, can you just offer some—or anyone—can you just offer some background on the deal and how competitive, proprietary? And then, also, some just precedent from the last time you had two near simultaneous, sizable acquisitions—to make sure that the integration of these two companies at the same time is something that you had experience and are well prepared for? Thank you.

Ken Asbury
Yes, Jon, your second questions seems like you are now picking on us.

So I can't recall when we did two deals at once. It just so happened that that was the way we have been working on these—I think, on one or close to two years. LGS, we have started—I think Kevin Kelly and I served on a panel at SOFIC two or three years ago and their engendered an interest. And with Mastodon, I think we have been looking at them for about 18 months—nine months in very, very close detail.

Neither was competitive. We were able to offer, or have a discussion in both cases, that made sense to them strategically, for that being an option. And so, that took a great deal time. But it also afforded us a great deal of deep examination of each of the businesses—the individual, you know, any of the issues associated with both of them. And I think we have a deep, rich appreciation for how good these companies are, and how good a fit they are going to be for CACI.

Jon, I lost your…remind me of your first question.

Jon Raviv
No, no, you hit both of them. Thank you.

Kenneth Asbury
Okay, very good.

Operator
Okay. Seeing no further questioners in the queue, this concludes our question-and-answer session. We would like to turn the conference back over to Ken Asbury for any closing remarks.

CEO CLOSING REMARKS

Ken Asbury
Well, thank you Phil, and thanks for all your help today on the call.

We would like to thank everybody who logged in for the webcast for their participation as well. We know that many of you will have follow-up questions. Tom Mutryn and Dan Leckburg are available immediately after this call and throughout the day tomorrow. Given that it is getting to be the witching hour, we will do as many as we can tonight. But thank you all. This concludes our call.

Thank you for your interest in CACI and we really appreciate the flexibilities that all of you have shown to us tonight to make sure that we got this message out appropriately to each of you. So thank you for that. So with that, we are done. We will see you again.

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

END