CFRA

# Quest Diagnostics Incorporated

| Recommendation | Price | 12-Mo. Target Price | Report Currency | Investment Style |
|---|---|---|---|---|
| HOLD ★★★★★ | USD 105.20 (as of Dec 13, 2019 4:00 PM ET) | USD 100.00 | USD | Mid-Cap Value |

**Equity Analyst Kevin Huang, CFA**

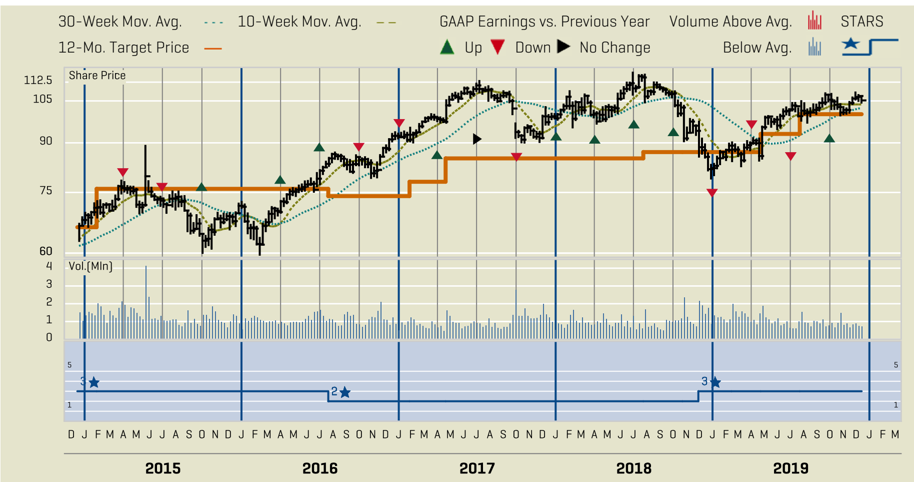
**GICS Sector** Health Care
**Sub-Industry** Health Care Services

**Summary** This company provides diagnostic testing, information and services to physicians, hospitals, managed care organizations, employers and government agencies.

## Key Stock Statistics (Source: CFRA, S&P Global Market Intelligence (SPGMI), Company Reports)

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| 52-Wk Range | **USD 108.30 - 78.95** | Oper. EPS 2019**E** | **USD 6.51** | Market Capitalization[B] | **USD 14.17** | Beta | **0.84** |
| Trailing 12-Month EPS | **USD 5.18** | Oper. EPS 2020**E** | **USD 6.79** | Yield [%] | **2.02** | 3-Yr Proj. EPS CAGR[%] | **7** |
| Trailing 12-Month P/E | **20.30** | P/E on Oper. EPS 2019**E** | **16.16** | Dividend Rate/Share | **USD 2.12** | SPGMI's Quality Ranking | **B+** |
| $10K Invested 5 Yrs Ago | **$18,361** | Common Shares Outstg.[M] | **134.70** | Institutional Ownership [%] | **91** | | |

## Price Performance




**Source: CFRA, S&P Global Market Intelligence**
**Past performance is not an indication of future performance and should not be relied upon as such.**
Analysis prepared by Equity Analyst **Kevin Huang** on Oct 22, 2019 01:57 PM, when the stock traded at **USD 102.28.**

## Highlights

- We expect 2019 sales to grow 2.5%, as DGX will likely see test volume growth, driven by its expanded partnership with UnitedHealthcare (UNH) and continued lab acquisitions, offset partially by continued reimbursement pressures. Much of DGX's recent growth has been driven by small acquisitions. In 2019, we expect at least 2% of DGX's top-line growth to be driven by M&A activity. DGX should be able to continue to enhance its growth over the next few years with lab acquisitions because we expect pricing pressures on lab tests to drive many small labs, including those owned by hospitals, out of business. DGX could also drive growth through partnerships with hospital health systems, many of which have been also feeling financial pressures.
- Since 2019, DGX has been in network for all UNH (one of the largest U.S. health insurers) plan participants, which will likely lead to increased end-user demand in 2019. In July 2019, DGX joined UNH's preferred lab network.
- We expect EBIT margins of 16.2% in 2019, down slightly from 16.3% in 2018 and 16.6% in 2017, as reimbursement pressures offset the benefits of DGX's cost cutting efforts and volume growth.

## Investment Rationale/Risk

- We think that DGX's shares, at 15.2x our next-12-month EPS estimate, are trading near fair value. We expect DGX's earnings growth to be limited by sustained industry-wide reimbursement rates declines. Under the Protecting Access to Medicare Act (PAMA), reimbursement for test prices can be cut, from 2018 to 2020, by a maximum of 10% and then by up to 15% from 2021 to 2023. CLFS (Clinical Laboratory Fee Schedule) reimbursement rates have been cut by the maximum amount for 2019; however, small labs are disproportionately affected, which could provide attractive lab acquisition opportunities for DGX. The company has also been working to offset top-line pressures by cutting costs through its Invigorate initiative, which has helped lessen margin pressures.
- Risks to our recommendation and target price include worse-than-expected pricing pressures, limited lab acquisition opportunities, poorly executed acquisition integrations and continued volume growth pressure.
- Our 12-month target of $100 is 15x our next-12-month EPS of $6.68. This multiple is below DGX's 5-year average ratio of 15.5x because we expect sustained industry-wide reimbursement pressures.

## Analyst's Risk Assessment

LOW | **MEDIUM** | HIGH

Our risk assessment reflects DGX's leadership position in the large and mature diagnostic testing industry, the company's broad geographic service area, its diverse and balanced customer mix and the growing recognition of the importance and significance of diagnostic testing, but we think regulatory uncertainties create risks for the company.

## Revenue/Earnings Data

### Revenue (Million USD)

| | 1Q | 2Q | 3Q | 4Q | Year |
|---|---|---|---|---|---|
| 2019 | 1,891 | 1,953 | 1,956 | -- | -- |
| 2018 | 1,884 | 1,919 | 1,889 | 1,839 | 7,531 |
| 2017 | 1,817 | 1,864 | 1,856 | 1,865 | 7,402 |
| 2016 | 1,863 | 1,906 | 1,885 | 1,861 | 7,214 |
| 2015 | 1,839 | 1,925 | 1,880 | 1,849 | 7,493 |
| 2014 | 1,746 | 1,902 | 1,904 | -- | 7,435 |

### Earnings Per Share (USD)

| | 1Q | 2Q | 3Q | 4Q | Year |
|---|---|---|---|---|---|
| 2020 | **E** 1.53 | **E** 1.77 | **E** 1.76 | **E** 1.73 | **E** 6.79 |
| 2019 | 1.20 | 1.51 | 1.56 | **E** 1.62 | **E** 6.51 |
| 2018 | 1.27 | 1.57 | 1.53 | 0.93 | 5.29 |
| 2017 | 1.16 | 1.37 | 1.14 | 1.83 | 5.50 |
| 2016 | 0.71 | 1.37 | 1.34 | 1.07 | 4.51 |
| 2015 | 0.42 | 0.81 | 2.35 | 1.30 | 4.87 |

Fiscal year ended Dec 31. Next earnings report expected: Early Feb. EPS Estimates based on CFRA's Operating Earnings; historical GAAP earnings are as reported in Company reports.

## Dividend Data

| Amount (USD) | Date Decl. | Ex-Div. Date | Stk. of Record | Payment Date |
|---|---|---|---|---|
| 0.53 | Nov 20 | Jan 13 | Jan 14 | Jan 29 '20 |
| 0.53 | Aug 15 | Oct 03 | Oct 04 | Oct 21 '19 |
| 0.53 | May 13 | Jul 05 | Jul 08 | Jul 22 '19 |
| 0.53 | Mar 01 | Apr 05 | Apr 08 | Apr 22 '19 |
| 0.53 | Nov 28 | Jan 14 | Jan 15 | Jan 30 '19 |

Dividends have been paid since 2004. Source: Company reports.

**Past performance is not an indication of future performance and should not be relied upon as such.**
Forecasts are not reliable indicator of future performance.

# Quest Diagnostics Incorporated

**Business Summary** April 23, 2019

CORPORATE OVERVIEW. Quest Diagnostics is a leading independent U.S. clinical lab operator. DGX offers a broad range of clinical laboratory testing services used by physicians in the detection, diagnosis and treatment of diseases and other medical conditions. Tests range from routine, such as blood cholesterol tests, to highly complex esoteric tests, such as gene-based testing and molecular diagnostics testing. At the end of 2018, DGX had a network of principal laboratories throughout the U.S., a number of smaller "rapid response" (STAT) laboratories, and more than 2,250 patient service centers, along with facilities in Mexico, Puerto Rico and England.

In 2018, DGX processed approximately 168 million requisitions (physician testing requests), up from 164 million in 2017. Routine testing generated 56% of net sales in 2018, while gene-based and esoteric testing generated 32% of net sales, and anatomic pathology testing services accounted for 8% of net sales. Diagnostic solutions accounted for the remaining 4% of net sales. Routine tests measure important health parameters such as the function of the kidney, heart, liver, thyroid and other organs. Esoteric tests are performed less frequently than routine tests and/or require more sophisticated equipment and materials, professional hands-on attention and more highly skilled personnel. As a result, they are generally priced substantially higher than routine tests.

CORPORATE STRATEGY. DGX is one of the largest companies in what we see as a mature market with limited growth potential. We foresee annual industry sales growth in the low-single digits. DGX's strategy, last updated in November 2018, has two key focal points: 1) accelerate growth and 2) drive operational excellence. DGX aims to accelerate growth through accretive, strategic acquisitions; partnerships with integrated delivery networks (IDNs); provision of broad access to diagnostic innovation; achieving recognition as a consumer-friendly provider of diagnostic information services; and support for population health initiatives. The key themes to driving operational excellence include reduction of denials and patience concessions, standardization and automation, digitization of the customer experience, and broad-based business optimization.

Under the Protecting Access to Medicare Act (PAMA), reimbursement for test prices can be cut, from 2018 to 2020, by a maximum of 10% and then by up to 15% from 2021 to 2023. CLFS (Clinical Laboratory Fee Schedule) reimbursement rates have been cut by the maximum amount for 2019, which has disproportionately affected small labs. Financially pressured labs are attractive acquisition opportunities for DGX. We think that opportunistic lab acquisitions will be a key driver of DGX's growth in the next few years. Organic growth could be achieved by increasing the number of higher-priced esoteric tests offered and achieving higher test volumes.

COMPETITIVE LANDSCAPE. The clinical lab industry is highly competitive and fragmented, with thousands of independent clinical labs, physician office labs and hospital-based labs. DGX is the largest provider of lab services; thus, it enjoys significant economies of scale over its competitors. DGX's main competitor is the publicly-traded Laboratory Corporation of America (LH).

FINANCIAL TRENDS. Sales decreased 2.3% to $7.5 billion in 2018, representing a five-year compound annual growth rate (CAGR) of 1.1%, impacted by sustained pressure on reimbursement rates. Adjusted EPS expanded 11.3% to $6.31, representing a five-year CAGR of 9.6%. DGX's debt level was moderate at 41.9% of net debt to total capital, while leverage (debt to trailing-twelve-month EBITDA) was not concerning at 2.6x. The company's free cash flow was $817 million in 2018, down from $923 million in 2017.

**Corporate Information**

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**Officers**

**Chairman, President & CEO**
S. H. Rusckowski

**Executive VP & CFO**
M. J. Guinan

**VP, Corporate Controller, Principal Accounting Officer & Chief Accounting Officer**
M. J. Deppe

**Senior VP & General Counsel**
M. E. Prevoznik

**Board Members**

D. C. Stanzione
D. M. Morrison
G. M. Pfeiffer
G. R. Wilensky
H. I. Torley
S. H. Rusckowski
T. L. Main
T. M. Ring
V. B. Gregg

**Domicile**
Delaware

**Founded**
1967

**Employees**
46,000

**Stockholders**
2,600

**Auditor**
PricewaterhouseCoopers LLP

# Quest Diagnostics Incorporated

## Quantitative Evaluations

**Fair Value Rank** 4

| 1 | 2 | 3 | 4 | 5 |
|---|---|---|---|---|
| LOWEST | | | | HIGHEST |

Based on CFRA's proprietary quantitative model, stocks are ranked from most overvalued (1) to most undervalued (5).

**Fair Value Calculation** USD 113.18 — Analysis of the stock's current worth, based on CFRA's proprietary quantitative model suggests that DGX is slightly undervalued by USD 7.98 or 7.6%.

**Volatility** LOW | AVERAGE | HIGH

**Technical Evaluation** BULLISH — Since November, 2019, the technical indicators for DGX have been BULLISH.

**Insider Activity** UNFAVORABLE | NEUTRAL | FAVORABLE

## Expanded Ratio Analysis

| | 2018 | 2017 | 2016 | 2015 |
|---|---|---|---|---|
| Price/Sales | 1.54 | 1.86 | 1.81 | 1.38 |
| Price/EBITDA | 7.55 | 8.87 | 8.84 | 6.84 |
| Price/Pretax Income | 11.93 | 12.95 | 11.60 | 9.16 |
| P/E Ratio | 15.74 | 17.91 | 20.38 | 14.61 |
| Avg. Diluted Shares Outsg.(M) | 139 | 140 | 142 | 145 |

Figures based on fiscal year-end price

## Key Growth Rates and Averages

| **Past Growth Rate (%)** | 1 Year | 3 Years | 5 Years |
|---|---|---|---|
| Sales | 1.74 | 0.17 | 1.05 |
| Net Income | -4.66 | 1.25 | -2.82 |

| **Ratio Analysis (Annual Avg.)** | | | |
|---|---|---|---|
| Net Margin (%) | NM | NM | NM |
| % LT Debt to Capitalization | 37.02 | NA | NA |
| Return on Equity (%) | 15.18 | NA | NA |

## Company Financials Fiscal year ending Dec. 31

| **Per Share Data** (USD) | 2018 | 2017 | 2016 | 2015 | 2014 | 2013 | 2012 | 2011 | 2010 | 2009 |
|---|---|---|---|---|---|---|---|---|---|---|
| Tangible Book Value | -18.92 | -18.76 | -16.94 | -15.42 | -19.46 | -18.03 | -14.21 | -19.94 | -10.92 | -10.46 |
| Free Cash Flow | 6.01 | 6.74 | 5.88 | 3.88 | 4.39 | 5.89 | 6.32 | 4.62 | 5.19 | 4.47 |
| Earnings | 5.29 | 5.50 | 4.51 | 4.87 | 3.78 | 5.31 | 3.92 | 2.85 | 3.98 | 3.88 |
| Earnings (Normalized) | 4.55 | 4.90 | 4.61 | 4.33 | 4.00 | 3.98 | 4.40 | 4.30 | 3.97 | 3.93 |
| Dividends | 2.03 | 1.80 | 1.65 | 1.52 | 1.32 | 1.20 | 0.81 | 0.47 | 0.40 | 0.40 |
| Payout Ratio (%) | 36 | 32 | 35 | 30 | 34 | 22 | 19 | 14 | 10 | 10 |
| Prices: High | 116.49 | 112.97 | 93.57 | 89.00 | 68.51 | 64.10 | 64.87 | 61.21 | 61.72 | 62.83 |
| Prices: Low | 78.95 | 90.10 | 59.66 | 60.07 | 50.46 | 52.50 | 53.25 | 45.13 | 40.80 | 42.36 |
| P/E Ratio: High | 22.0 | 20.5 | 20.7 | 18.3 | 18.1 | 12.1 | 16.5 | 21.5 | 15.5 | 16.2 |
| P/E Ratio: Low | 14.9 | 16.4 | 13.2 | 12.3 | 13.3 | 9.9 | 13.6 | 15.8 | 10.3 | 10.9 |

| **Income Statement Analysis** (Million USD) | 2018 | 2017 | 2016 | 2015 | 2014 | 2013 | 2012 | 2011 | 2010 | 2009 |
|---|---|---|---|---|---|---|---|---|---|---|
| Revenue | 7,531 | 7,402 | 7,214 | 7,493 | 7,435 | 7,146 | 7,383 | 7,392 | 7,260 | 7,455 |
| Operating Income | 1,225 | 1,284 | 1,228 | 1,204 | 1,119 | 1,156 | 1,317 | 1,298 | 1,295 | 1,346 |
| Depreciation + Amortization | 309 | 270 | 249 | 304 | 314 | 283 | 278 | 272 | 254 | 257 |
| Interest Expense | 169 | 153 | 144 | 154 | 167 | 162 | 168 | 172 | 143 | 144 |
| Pretax Income | 970 | 1,065 | 1,125 | 1,126 | 849 | 1,348 | 1,068 | 849 | 1,175 | 1,228 |
| Effective Tax Rate | 18.8 | 22.6 | 38.1 | 33.1 | 30.9 | 37.1 | 37.6 | 41.8 | 36.6 | 37.5 |
| Net Income | 736 | 772 | 645 | 709 | 556 | 849 | 556 | 471 | 721 | 729 |
| Net Income (Normalized) | 633 | 686 | 654 | 628 | 580 | 609 | 704 | 688 | 704 | 738 |

| **Balance Sheet and Other Financial Data** (Million USD) | 2018 | 2017 | 2016 | 2015 | 2014 | 2013 | 2012 | 2011 | 2010 | 2009 |
|---|---|---|---|---|---|---|---|---|---|---|
| Cash | 135 | 137 | 359 | 133 | 192 | 187 | 296 | 165 | 449 | 534 |
| Current Assets | 1,390 | 1,306 | 1,531 | 1,501 | 1,603 | 1,383 | 1,561 | 1,401 | 1,605 | 1,679 |
| Total Assets | 11,003 | 10,503 | 10,100 | 9,962 | 9,857 | 8,948 | 9,284 | 9,313 | 8,528 | 8,564 |
| Current Liabilities | 1,485 | 1,057 | 981 | 1,173 | 1,709 | 1,132 | 1,048 | 1,561 | 1,214 | 1,059 |
| Long Term Debt | 3,490 | 3,837 | 3,816 | 3,498 | 3,252 | 3,154 | 3,357 | 3,371 | 2,641 | 2,951 |
| Total Capital | 9,428 | 8,979 | 8,589 | 8,440 | 8,100 | 7,339 | 7,553 | 7,740 | 7,044 | 7,133 |
| Capital Expenditures | 383 | 252 | 293 | 263 | 308 | 231 | 182 | 161 | 205 | 167 |
| Cash from Operations | 1,200 | 1,175 | 1,116 | 821 | 944 | 652 | 1,187 | 895 | 1,118 | 997 |
| Current Ratio | 0.94 | 1.24 | 1.56 | 1.28 | 0.94 | 1.22 | 1.49 | 0.90 | 1.32 | 1.59 |
| % Long Term Debt of Capitalization | 37.0 | 42.7 | 44.4 | 41.4 | 40.1 | 43.0 | 44.4 | 43.5 | 37.5 | 41.4 |
| % Net Income of Revenue | 9.77 | 10.43 | 8.94 | 9.46 | 7.48 | 11.88 | 7.53 | 6.37 | 9.93 | 9.78 |
| % Return on Assets | 7.12 | 7.79 | 7.65 | 7.59 | 7.44 | 7.93 | 8.85 | 9.09 | 9.47 | 9.91 |
| % Return on Equity | 15.2 | 16.9 | 14.6 | 16.5 | 14.1 | 20.8 | 16.9 | 12.7 | 18.5 | 20.1 |

Source: S&P Global Market Intelligence. Data may be preliminary or restated; before results of discontinued operations/special items. Per share data adjusted for stock dividends; EPS diluted. E-Estimated. NA-Not Available. NM-Not Meaningful. NR-Not Ranked. UR-Under Review.

## Sub-Industry Outlook

Our outlook for the health care services sub-industry for the next year is positive, based on our key assumptions that: 1) the U. S. economy is currently in the late stage of the economic cycle, which means that we expect a slowdown in U.S. economic growth; 2) many of the firms within the sub-industry will likely see sustained demand for their services even in the face of weaker economic conditions; and 3) there will be no significant adverse changes to the operating and competitive environment of health care service providers. This sub-industry has recently been pressured by headline risks related to legislative and regulatory proposals, such as Medicare-For-All and Amazon's potential to disrupt the health care sector. These headlines are unlikely to evolve into real threats to the profitability of health care services firms in the near future, by our analysis.

This sub-industry has underperformed the broader market recently due to pressures unique to different businesses. For example, pharmacy benefit managers (PBMs) have been hurt by lower levels of drug price inflation and increased pressure from third party payers, which has been partially alleviated by high drug utilization. Some health care services firms, such as Mednax, have had issues finding enough qualified staff.

We see opportunities for health care services firms to address and take advantage of the recent pressures that they've been facing. For example, the major PBMs have all merged with a major insurer to offset pressures; most notably, CVS Health (CVS) acquired Aetna (AET) and Cigna (CI) acquired Express Scripts (ESRX). Lab services providers have opportunities to acquire smaller labs and gain scale as the smaller labs are likely to falter under the pressure of continued, significant reimbursement cuts.

Back to the topic of headline risks: Democrats took control of the House of Representatives in the November 2018 U.S. mid-term elections, resulting in a change to the dynamics in Washington, D.C., which had been Republican dominated for the preceding two years. A couple of key Democrat candidates for the 2020 U.S. presidential election endorse a Medicare For All (MFA) health care system. If MFA were to become law, it would likely lower average rates for health care services and, hence, substantially adversely impact firms in this sub-industry. However, we think there's an almost-zero chance of MFA becoming a reality in the near future.

Another headline risk is the potential repeal of the Affordable Care Act (ACA), instigated by a judge in Texas who ruled the ACA to be unconstitutional. Opponents are now appealing the decision. We currently expect the ACA to be upheld upon appeal, although this decision could take a couple years to reach. If the ACA were to be repealed, we expect a negative impact to health care services, which have benefited from the increased insurance coverage of the past several years under the ACA.

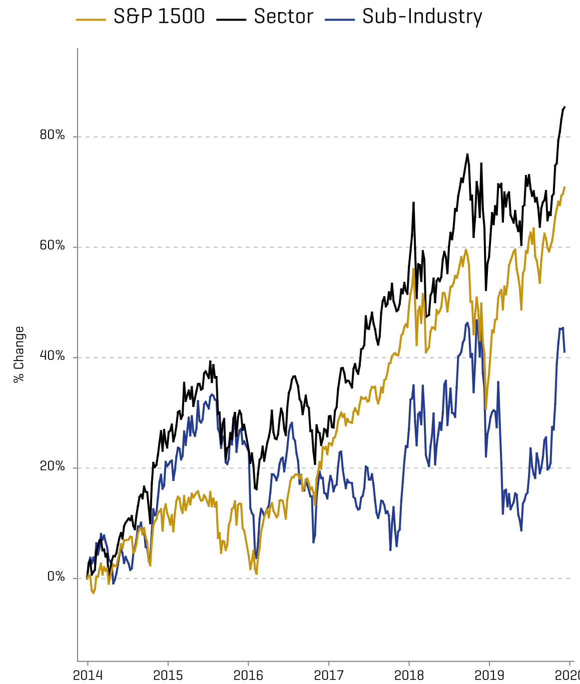
Year-to-date through September 20, the S&P Health Care Services Index declined 0.8% vs. an increase of 19.0% for the S&P Composite 1500. In 2018, the S&P Health Care Services Index increased 2.3% vs. a 6.8% decrease in the S&P 1500 Composite Index.

**/Kevin Huang, CFA**

## Industry Performance

**GICS Sector:** **Health Care**
**Sub-Industry:** **Health Care Services**

Based on S&P 1500 Indexes
Five-Year market price performance through Dec 14, 2019




NOTE: All Sector & Sub-Industry information is based on the Global Industry Classification Standard (GICS).

Past performance is not an indication of future performance and should not be relied upon as such.
**Source: S&P Global Market Intelligence**

## Sub-Industry: Health Care Services    Peer Group*: Health Care Services

| Peer Group | Stock Symbol | Exchange | Currency | Recent Stock Price | Stk. Mkt. Cap. (M) | 30-Day Price Chg. (%) | 1-Year Price Chg. (%) | P/E Ratio | Fair Value Calc. | Yield (%) | Return on Equity (%) | LTD to Cap (%) |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Quest Diagnostics Incorporated** | **DGX** | **NYSE** | **USD** | **105.20** | **14,170** | **2.8** | **19.1** | **20** | **113.18** | **2.0** | **15.2** | **37.0** |
| AMN Healthcare Services, Inc. | AMN | NYSE | USD | 59.64 | 2,786 | -0.2 | 1.6 | 23 | 64.78 | Nil | 23.6 | 40.8 |
| Amedisys, Inc. | AMED | NasdaqGS | USD | 162.30 | 5,235 | 8.1 | 25.2 | 42 | 144.25 | Nil | 24.0 | 1.2 |
| Chemed Corporation | CHE | NYSE | USD | 440.12 | 7,046 | 7.6 | 47.7 | 35 | 298.75 | 0.3 | 36.3 | 13.1 |
| DaVita Inc. | DVA | NYSE | USD | 72.71 | 9,315 | 4.9 | 22.4 | 28 | 75.90 | Nil | 14.5 | 52.3 |
| Fresenius Medical Care AG & Co. KGaA | FMS | NYSE | USD | 36.72 | 21,910 | 1.6 | 5.9 | 8 | NA | 1.8 | 37.5 | 49.0 |
| LHC Group, Inc. | LHCG | NasdaqGS | USD | 131.55 | 4,145 | 3.1 | 29.4 | 43 | 119.13 | Nil | 8.1 | 14.0 |
| Laboratory Corporation of America Holdings | LH | NYSE | USD | 166.59 | 16,176 | -0.4 | 19.2 | 22 | 164.81 | Nil | 12.8 | 45.9 |
| MEDNAX, Inc. | MD | NYSE | USD | 27.38 | 2,272 | 4.7 | -27.0 | NM | NA | Nil | 8.7 | 39.0 |
| Premier, Inc. | PINC | NasdaqGS | USD | 37.89 | 2,517 | 4.2 | -4.0 | 4 | 49.55 | Nil | -29.2 | -0.7 |
| Sonic Healthcare Limited | SKHH.Y | OTCPK | USD | 19.89 | 9,435 | -0.1 | 26.1 | 23 | NA | 2.9 | 11.4 | 25.9 |

*For Peer Groups with more than 10 companies or stocks, selection of issues is based on market capitalization.
NA-Not Available NM-Not Meaningful.
Note: Peers are selected based on Global Industry Classification Standards and market capitalization. The peer group list includes companies with similar characteristics, but may not include all the companies within the same industry and/or that engage in the same line of business.

## Analyst Research Notes and other Company News

**October 22, 2019**
12:45 pm ET... CFRA Maintains Hold Opinion on Shares of Quest Diagnostics Incorporated (101.72***): We maintain our target price at $100 based on a ratio of 15x our next-12-month EPS estimate of $6.68. This multiple is slightly below DGX's five-year average forward P/E ratio of 15.5x to reflect industry-wide reimbursement pressures. Q3 EPS of $1.76 vs. $1.68 beat our expectation by $0.05. We keep our 2019 EPS estimate at $6.51 and we lift our 2020 EPS estimate by $0.03 to $6.79. Shares traded down slightly today because the company provided full-year guidance that came in light relative to consensus expectations. Q3 net revenues grew 3.5% year-over-year to $1.96 billion, above our expectations, as requisition volumes grew 5.1% (3.7% organic), offset partially by a 1.2% decline in revenue per requisition. DGX continues to focus on delivering cost efficiencies to counter industry headwinds, such as sustained reimbursement pressure and increased payer focus on driving better value. In Q3 2019, DGX's adjusted operating margin improved to 17.9% from 17.7% in Q3 2018. /Kevin Huang, CFA

**July 23, 2019**
01:41 pm ET... CFRA Maintains Hold Opinion on Shares of Quest Diagnostics, Inc. (102.71***): We lift our target price by $7 to $100, based on a ratio of 15x our next-12-month EPS estimate of $6.64. This multiple is slightly below DGX's five-year average forward P/E ratio of 15.5x to reflect industry-wide reimbursement pressures. Q2 EPS of $1.73 vs. $1.75 exceeded our estimate by $0.01. We lift our 2019 EPS estimate to $6.51 from $6.46. Net revenues in Q2 grew 1.8% year-over-year to $1.95 billion. Despite the loss of several large-volume, low-margin capitated contracts that had a -70 basis point impact to volume growth, DGX's requisition volume growth accelerated to 4.4% (i.e. 2. 9% organic), while revenue per requisition declined 2.3%. One of DGX's competitors offered rates on said contracts that would have been unprofitable for DGX. Fortunately, the non-renewal of the contracts is expected to have an insignificant impact on DGX's top and bottom line. DGX's adjusted operating income was $352 million in Q2, reflecting an 18.0% operating margin, down from 18.9% in Q2 2018. /Kevin Huang, CFA

**April 23, 2019**
10:38 am ET... CFRA Maintains Hold Opinion on Shares of Quest Diagnostics, Inc. (91.31***): We raise our price target by $6 to $93, which is based on a ratio of 14x our next-12-month EPS estimate of $6.63. This multiple is below DGX's five-year average forward P/E ratio of 15.5x because we expect sustained reimbursement pressures on clinical laboratory companies. Q1 EPS of $1.40 vs. $1.52 was lower than our estimate of $1.45. We lift our 2019 EPS by $0.03 to $6.46 and our 2020 EPS by $0.03 to $6.76. Net revenues in Q1 rose 0.4% year-over-year to $1.89 billion, affected by a 3.6% increase in requisition volume and a 3.0% decline in revenue per requisition. On an organic basis, requisition volumes only increased 2.4%, as reported volume growth was aided by acquisitions. As a reminder, DGX expects to see $200 million of industry-wide reimbursement pressure in 2019. Although, this will be offset by accelerating volume growth, as DGX works to expand its relationships. Beginning July 2019, DGX will be a member of UnitedHealth Group's preferred lab network. /Kevin Huang, CFA

**February 14, 2019**
02:04 pm ET... CFRA Reiterates Hold Opinion on Shares of Quest Diagnostics Incorporated (85.77***): We maintain our price target of $87, which is based on a ratio of 13.6x our next-12-month EPS estimate of $6.43. This multiple is near the low-end of DGX's five-year range because we expect sustained reimbursement pressures. Q4 EPS of $1.36 vs. $1.38 was $0.04 lower than our estimate. We lower our 2019 EPS by $0.25 to $6.43 and initiate our 2020 EPS at $6.73. Net revenues in Q4 2018 declined 1.4% year-over-year to $1.84 billion, as a 5.5% decline in revenue per requisition mitigated the positive effects of a 3.4% increase in requisition volume. Volume growth was aided 230 basis points by acquisitions. We expect DGX to continue boosting its testing volumes through acquisitions of struggling small independent hospital laboratories, as PAMA-induced reimbursement pressures continue driving test prices lower. Like its main competitor, Laboratory Corporation (LH 146 ***), DGX aims to drive growth through partnerships with hospital health systems, which have been feeling financial pressures. /Kevin Huang, CFA

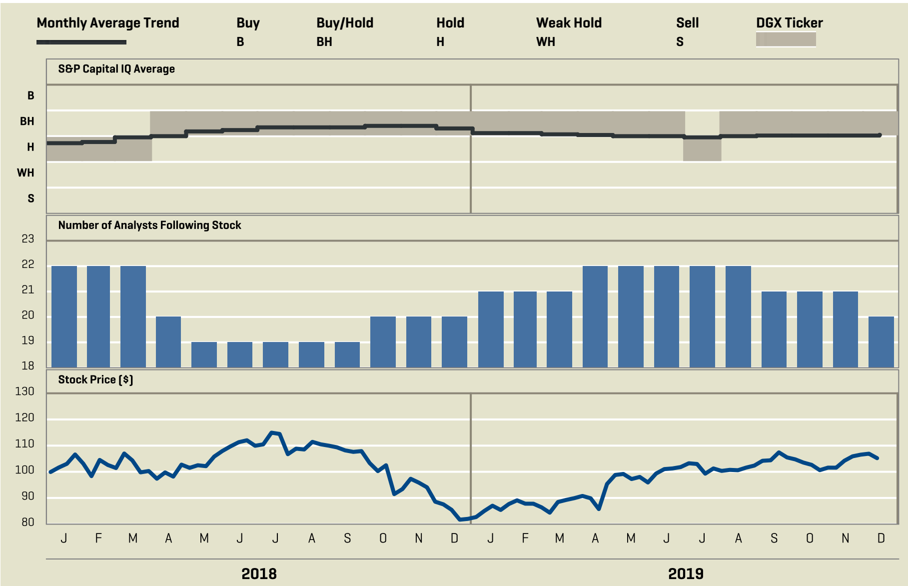
**November 29, 2018**
11:27 am ET... CFRA RAISES ITS OPINION ON SHARES OF QUEST DIAGNOSTICS TO HOLD FROM SELL (88.06***): We maintain our price target of $87, which is based on 13.6X our next-12-month EPS estimate of $6.42. In an announcement released November 28, 2018, DGX lowered both its 2018 revenue and earnings outlooks. DGX is now guiding investors towards an adjusted EPS of greater than $6.30 vs. a previous range of $6.53 - $6.60. The lower EPS outlook is primarily due to an increase in reserves associated with revenue and accounts receivable. We previously highlighted DGX's elevated accounts receivable level as a concern. We lower our 2018 EPS by $0.23 to $6.35 and our 2019 EPS by $0.25 to $6.68. Reported 2018 revenues are now expected to be $7.57 billion vs. previous expectations of $7.62 billion. Some of DGX's volume weakness has been driven by Hurricane Michael, the California wildfires, and the recent East Coast snowstorm. Because DGX lowered its revenue guidance again and increased its reserves, we now see less downside to shares of DGX; hence, we lift our opinion on shares of DGX to Hold. /Kevin Huang, CFA

**October 23, 2018**
10:30 am ET... CFRA MAINTAINS SELL OPINION ON SHARES OF QUEST DIAGNOSTICS INCORPORATED (95.42**): We maintain our 12-month target of $87 on 12.7X our next-12-month EPS estimate of $6.84. This multiple is near the low end of DGX's five-year forward PE range of 11.9X-20.0X, reflecting our expectations of sustained pressures on sales growth and margin deterioration. Q3 '18 EPS of $1.68 vs. $1.35 was $0.01 lower than our estimate. We lower our 2018 EPS outlook by $0.02 to $6.58. Q3 '18 sales increased 1.8% to $1.89 billion, driven completely by acquisitions. Requisition volume grew 2.5% in the quarter, while revenue per requisition declined 0.8%. DGX's adjusted operating margin was 16.5% in Q3 '18 compared with 17.5% in Q3 '17. We previously highlighted that Q2 '18 receivables (measured in days sales) were elevated and could pressure future revenue growth -- a pressure that has been realized as management reduced its 2018 adjusted revenue growth outlook to 3% from a previous expected growth range of 4.0%-4.5%. Q3 '18 receivables in days were still elevated compared to prior years. /Kevin Huang, CFA

Note: Research notes reflect CFRA's published opinions and analysis on the stock at the time the note was published. The note reflects the views of the equity analyst as of the date and time indicated in the note, and may not reflect CFRA's current view on the company.

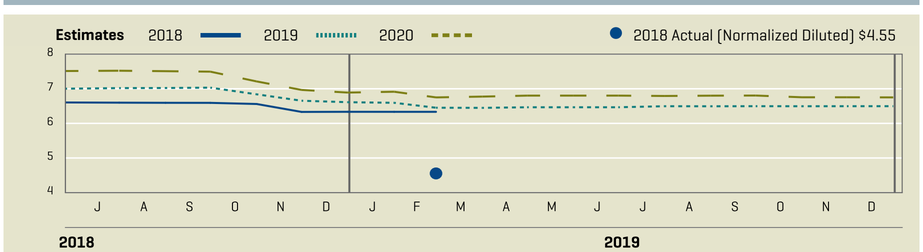
# Quest Diagnostics Incorporated

## Analysts' Recommendations




| | No. of Recommendations | % of Total | 1 Mo.Prior | 3 Mos.Prior |
|---|---|---|---|---|
| Buy | 6 | 30 | 6 | 6 |
| Buy/Hold | 2 | 10 | 2 | 2 |
| Hold | 10 | 50 | 11 | 11 |
| Weak Hold | 1 | 5 | 1 | 1 |
| Sell | 1 | 5 | 1 | 1 |
| No Opinion | 0 | 0 | 0 | 0 |
| **Total** | **20** | **100** | **21** | **21** |

## Wall Street Consensus Estimates




| Fiscal Years | Avg Est. | High Est | Low Est. | # of Est. | Est. P/E |
|---|---|---|---|---|---|
| 2020 | 6.75 | 6.90 | 6.62 | 19 | 15.6 |
| 2019 | 6.50 | 6.53 | 6.48 | 19 | 16.2 |
| **2020 vs. 2019** | **▲4%** | **▲6%** | **▲2%** | **0%** | **▼-4%** |
| | | | | | |
| Q4'20 | 1.70 | 1.84 | 1.64 | 12 | 61.9 |
| Q4'19 | 1.60 | 1.65 | 1.58 | 17 | 65.6 |
| **Q4'20 vs. Q4'19** | **▲6%** | **▲12%** | **▲4%** | **▼-29%** | **▼-6%** |

Forecasts are not reliable indicator of future performance.

Note: A company's earnings outlook plays a major part in any investment decision. S&P Global Market Intelligence organizes the earnings estimates of over 2,300 Wall Street analysts, and provides their consensus of earnings over the next two years, as well as how those earnings estimates have changed over time. Note that the information provided in relation to consensus estimates is not intended to predict actual results and should not be taken as a reliable indicator of future performance.

**Note: For all tables, graphs and charts in this report that do not cite any reference or source, the source is S&P Global Market Intelligence.**

## Wall Street Consensus Opinion

**BUY/HOLD**

## Wall Street Consensus vs. Performance

For fiscal year 2019, analysts estimate that DGX will earn USD $6.50. For the 3rd quarter of fiscal year 2019, DGX announced earnings per share of USD $1.56, representing 24% of the total revenue estimate. For fiscal year 2020, analysts estimate that DGX's earnings per share will grow by 4% to USD $6.75.

## Glossary

**STARS**
Since January 1, 1987, CFRA Equity and Fund Research Services, and its predecessor S&P Capital IQ Equity Research has ranked a universe of U.S. common stocks, ADRs (American Depositary Receipts), and ADSs (American Depositary Shares) based on a given equity's potential for future performance. Similarly, we have ranked Asian and European equities since June 30, 2002. Under proprietary STARS (Stock Appreciation Ranking System), equity analysts rank equities according to their individual forecast of an equity's future total return potential versus the expected total return of a relevant benchmark (e.g., a regional index (S&P Asia 50 Index, S&P Europe 350® Index or S&P 500® Index)), based on a 12-month time horizon. STARS was designed to meet the needs of investors looking to put their investment decisions in perspective. Data used to assist in determining the STARS ranking may be the result of the analyst's own models as well as internal proprietary models resulting from dynamic data inputs.

**S&P Global Market Intelligence's Quality Ranking**
(also known as **S&P Capital IQ Earnings & Dividend Rankings**) - Growth and stability of earnings and dividends are deemed key elements in establishing S&P Global Market Intelligence's earnings and dividend rankings for common stocks, which are designed to capsulize the nature of this record in a single symbol. It should be noted, however, that the process also takes into consideration certain adjustments and modifications deemed desirable in establishing such rankings. The final score for each stock is measured against a scoring matrix determined by analysis of the scores of a large and representative sample of stocks. The range of scores in the array of this sample has been aligned with the following ladder of rankings:

| | | | |
|---|---|---|---|
| A+ | Highest | B | Below Average |
| A | High | B- | Lower |
| A- | Above Average | C | Lowest |
| B+ | Average | D | In Reorganization |
| NR | Not Ranked | | |

**EPS Estimates**
CFRA's earnings per share (EPS) estimates reflect analyst projections of future EPS from continuing operations, and generally exclude various items that are viewed as special, non-recurring, or extraordinary. Also, EPS estimates reflect either forecasts of equity analysts; or, the consensus (average) EPS estimate, which are independently compiled by S&P Global Market Intelligence, a data provider to CFRA. Among the items typically excluded from EPS estimates are asset sale gains; impairment, restructuring or merger-related charges; legal and insurance settlements; in process research and development expenses; gains or losses on the extinguishment of debt; the cumulative effect of accounting changes; and earnings related to operations that have been classified by the company as discontinued. The inclusion of some items, such as stock option expense and recurring types of other charges, may vary, and depend on such factors as industry practice, analyst judgment, and the extent to which some types of data is disclosed by companies.

**12-Month Target Price**
The equity analyst's projection of the market price a given security will command 12 months hence, based on a combination of intrinsic, relative, and private market valuation metrics, including Fair Value.

**CFRA Equity Research**
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**Abbreviations Used in Equity Research Reports**
CAGR - Compound Annual Growth Rate
CAPEX - Capital Expenditures
CY - Calendar Year
DCF - Discounted Cash Flow
DDM - Dividend Discount Model
EBIT - Earnings Before Interest and Taxes
EBITDA - Earnings Before Interest, Taxes, Depreciation & Amortization
EPS - Earnings Per Share
EV - Enterprise Value
FCF - Free Cash Flow
FFO - Funds From Operations
FY - Fiscal Year
P/E - Price/Earnings
P/NAV - Price to Net Asset Value PEG Ratio - P/E-to-Growth Ratio PV - Present Value
R&D - Research & Development ROCE - Return on Capital Employed ROE - Return on Equity
ROI - Return on Investment
ROIC - Return on Invested Capital
ROA - Return on Assets
SG&A - Selling, General & Administrative Expenses
SOTP - Sum-of-The-Parts
WACC - Weighted Average Cost of Capital

**Dividends on American Depository Receipts (ADRs) and American Depository Shares (ADSs) are net of taxes (paid in the country of origin).**

**Qualitative Risk Assessment**
Reflects an equity analyst's view of a given company's operational risk, or the risk of a firm's ability to continue as an ongoing concern. The Qualitative Risk Assessment is a relative ranking to the U.S. STARS universe, and should be reflective of risk factors related to a company's operations, as opposed to risk and volatility measures associated with share prices. For an ETF this reflects on a capitalization-weighted basis, the average qualitative risk assessment assigned to holdings of the fund.

**STARS Ranking system and definition:**
★★★★★ **5-STARS (Strong Buy):**
Total return is expected to outperform the total return of a relevant benchmark, by a notable margin over the coming 12 months, with shares rising in price on an absolute basis.
★★★★☆ **4-STARS (Buy):**
Total return is expected to outperform the total return of a relevant benchmark over the coming 12 months, with shares rising in price on an absolute basis.
★★★☆☆ **3-STARS (Hold):**
Total return is expected to closely approximate the total return of a relevant benchmark over the coming 12 months, with shares generally rising in price on an absolute basis.
★★☆☆☆ **2-STARS (Sell):**
Total return is expected to underperform the total return of a relevant benchmark over the coming 12 months, and the share price is not anticipated to show a gain.
★☆☆☆☆ **1-STAR (Strong Sell):**
Total return is expected to underperform the total return of a relevant benchmark by a notable margin over the coming 12 months, with shares falling in price on an absolute basis.

**Relevant benchmarks:**
In North America, the relevant benchmark is the S&P 500 Index, in Europe and in Asia, the relevant benchmarks are the S&P Europe 350 Index and the S&P Asia 50 Index, respectively.

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Quantitative recommendations are determined by ranking a universe of common stocks based on 5 measures or model categories: Valuation, Quality, Growth, Street Sentiment, and Price Momentum. In the U.S., a sixth sub-category for Financial Health will also be displayed. Percentile scores are used to compare each company to all other companies in the same universe for each model category. The five (six) model category scores are then weighted and rolled up into a single percentile ranking for that company. For reports containing quantitative recommendations refer to the Glossary section of the report for detailed methodology and the definition of Quantitative rankings.

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### STARS Stock Reports:

Global STARS Distribution as of March 31, 2019

| Ranking | North America | Europe | Asia | Global |
|---|---|---|---|---|
| Buy | 35.5% | 32.4% | 39.4% | 35.4% |
| Hold | 54.8% | 54.4% | 41.7% | 53.2% |
| Sell | 9.7% | 13.2% | 18.9% | 11.3% |
| Total | 100.0% | 100.0% | 100.0% | 100.0% |

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