

Cardinal Health: Capital Priorities After the CVS LOI

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Student strategy case

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The decision

On October 1, Cardinal Health announced a binding letter of intent to extend its pharmaceutical distribution agreement with CVS Health through June 30, 2032, on the current distribution-service scope. That same day, McKesson announced an agreement in principle to extend its own CVS distribution partnership through June 2032. Cardinal's announcement reaffirmed its FY27 earnings guidance, but neither company disclosed contract economics.

You are preparing a capital-allocation recommendation for a **hypothetical Cardinal Health leadership discussion**. The public record does not disclose a pending board vote, a new CVS award, or an unallocated pool of cash. Your assignment is to set a decision rule for the next incremental dollar and management attention **beyond Cardinal's disclosed FY27 plan**. How should Cardinal balance its planned investment and shareholder returns against possible additional specialty or at-Home growth and the need to preserve financial flexibility?

Recommend a hurdle and pacing policy. State what the company should do if cash flow or investment opportunities come in above or below plan, which evidence should release further commitments, and what would cause you to pause. You may recommend a combination of approaches. Do not assume all forecast capex is discretionary, that the CVS LOI changes contract economics, or that guidance is a fixed cash commitment. Do not invent an acquisition target, budget, or board proposal.

The company and its businesses

Cardinal is a large pharmaceutical and medical-products distributor. In FY26 it reported two segments: Pharma/Specialty and Global Medical Products and Distribution (GMPD). It separately reported an "Other" grouping containing Nuclear and Precision Health Solutions, at-Home Solutions, and OptiFreight. "Other" is not an at-Home-only result. The company also sells specialty products and services through multiple businesses; reported segment profit is a company-defined measure, not consolidated GAAP operating earnings. [P01, MD&A pp. 7-10; P02]

The CVS relationship is significant. CVS represented 28% of Cardinal's FY26 revenue and 22% of gross trade receivables at June 30. Cardinal described its LOI as binding and limited to the current scope. McKesson's same-day announcement was an agreement in principle covering retail, mail-order and specialty pharmacies and distribution centers. The announcements establish that both distributors expect to continue serving CVS; they do not reveal comparative

price, volume, margin, service, or investment terms. Do not infer that Cardinal won new business or gained a relative advantage. [P01, HTML lines 1023-31 and 1442-45; P03, SEC Ex. 99.1 lines 8-10; P07]

FY27 plan and capital constraints

Cardinal's August outlook called for FY27 non-GAAP diluted EPS of \$12.40-\$12.60, 13-15% growth from an adjusted FY26 base excluding a one-time tariff-refund benefit. It expected Pharma/Specialty revenue growth of 3-5% and segment-profit growth of 8-11%; GMPD revenue growth of 2-4% and segment profit of \$200-\$220 million; and Other revenue growth of 11-13% and profit growth of 15-18%. Management included the recently completed Strive Medical tuck-in and announced, then pending, Diabetes Health acquisition in the outlook. The two July agreements totaled about \$360 million cash, subject to working-capital adjustment; public materials do not allocate the amount between the businesses. [P02, lines 239-66; P04]

The same guidance included approximately \$700 million of capex, about \$1 billion of share repurchases, and \$3.5-\$4.0 billion of adjusted free cash flow. Cardinal's board had authorized \$6.4 billion of repurchases; authorization is permission, not a requirement to spend. FY26 operating cash flow was \$5.174 billion and company-defined adjusted FCF was \$5.0 billion. Adjusted FCF is calculated after PPE additions under the company definition, but excludes specified litigation-settlement cash flows and other significant or non-recurring items; it is not net of dividends, repurchases, acquisitions, or debt payments. It is not a pool left over after every use. [P02, lines 92-103, 239-66 and Schedule 6]

Settlement obligations and financing matter too. Cardinal reported \$4.3 billion accrued for certain national opioid settlements at June 30 and said most remaining payments were expected through 2038. It paid \$374 million under the National Opioid Settlement in July. In August it replaced three facilities with a \$4.0 billion revolver due in 2031. The credit agreement's leverage limit is generally 4.00x; after a qualifying Material Acquisition, the company may elect a notified leverage holiday allowing 4.50x for the first four test dates on or after closing. The filings do not disclose current covenant headroom or establish that the full facility is available for a new acquisition. [P01, HTML lines 472-545; P06, §6.12]

Exhibit 1. Operating and financial baseline

FY26 / FY27 disclosure	Figure	What it measures
FY26 revenue	\$254.248bn	Consolidated reported revenue
FY26 GAAP consolidated operating earnings	\$2.613bn	Includes corporate, acquisition, impairment and other effects
Pharma/Specialty FY26 revenue / segment profit	\$234.833bn / \$2.783bn	Reportable segment; segment profit is not GAAP operating earnings
GMPD FY26 revenue / segment profit	\$12.719bn / \$258m	Reportable segment
Other FY26 revenue / profit	\$6.792bn / \$707m	NPHS, at-Home and OptiFreight combined
FY26 operating cash flow / adjusted FCF	\$5.174bn / \$5.0bn	Adjusted FCF is company-defined and non-GAAP
FY27 capex / repurchase guidance	~\$700m / ~\$1bn	Management outlook, not a disclosed discretionary surplus
FY27 adjusted FCF guidance	\$3.5-\$4.0bn	Management estimate using its definition
Opioid settlement accrual at June 30	\$4.3bn	Certain national settlements; majority of remaining payments expected through 2038

Sources: Cardinal FY26 Form 10-K and FY26 results/FY27 outlook release [P01, pp. 7-14; P02, lines 239-66 and Schedule 6]. Figures rounded where shown. FY26 included a roughly \$100m net operating-earnings benefit from an IEEPA refund after a corresponding customer-repayment expense; FY27 EPS growth is against an adjusted FY26 base. Do not compare headline EPS without that qualification.

Exhibit 2. Possible uses and limits of capital

Use or constraint	Publicly disclosed position by cutoff	Decision implication
Base operating investment	~\$700m FY27 capex guidance, primarily manufacturing/distribution infrastructure and technology	Do not assume it is fully movable or that additional capacity is available
Shareholder return	~\$1bn FY27 buyback guidance; \$6.4bn total authorization	Guidance and authorization are not identical; authorization does not compel repurchases
At-Home growth	Strive recently completed; Diabetes Health announced/pending; about \$360m combined July transaction value	Integration and target-level economics are not disclosed in the combined amount
CVS relationship	Cardinal binding LOI through June 2032, current service scope; McKesson agreement in principle through same date	Duration visibility, but price, volume, margins and required investment remain unknown
Opioid settlements	\$4.3bn accrued at June 30; \$374m paid in July	Cash schedule is material but future annual payments vary by settlement terms
Revolver	\$4.0bn facility; 4.00x general leverage limit, conditional 4.50x holiday	Facility size is not proof of availability or headroom

Sources: [P01-P07]. “Other” segment growth is not a stand-in for at-Home growth.

Your recommendation

Prepare a two-page capital-allocation memo and a five-minute oral defense. Address:

1. Which uses should receive priority within the disclosed plan, and what rule applies to any verified capacity beyond it?
2. What minimum return, strategic-fit, integration, and liquidity tests should a new specialty or at-Home investment pass?
3. Under what conditions would you slow discretionary repurchases, retain additional liquidity, or reduce debt instead?
4. What CVS-related information would you request before committing relationship-specific investment? How does McKesson’s same-day announcement affect your interpretation?
5. Identify one fact that would make you change your recommendation.

Separate public facts from your assumptions. If you introduce numeric hurdle rates or liquidity floors, label them as classroom assumptions and show how they influence the rule. No candidate deal returns, CVS economics, Q1 FY27 balances, or unreported board decisions are available at the cutoff.

Sources

- P01 - FY26 Form 10-K
- P02 - FY26 results and FY27 outlook
- P03 - Cardinal binding CVS LOI, SEC Exhibit 99.1
- P04 - July at-Home tuck-in announcements
- P05 - FY27 Q1 results scheduled for Nov. 5
- P06 - Aug. 7 replacement credit facility
- P07 - McKesson's Oct. 1 CVS announcement