

Labcorp - How to Screen the Next Laboratory Partnerships?

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Decision scope: A hypothetical process for screening and sequencing future laboratory partnerships

Case convention: The decision exercise is hypothetical. It does not imply an undisclosed mandate, fixed capital pool or dispute at Labcorp.

The question

Imagine joining Labcorp's strategy group on March 1, 2024. The company has publicly emphasized becoming a partner of choice for health systems and local and regional laboratories. How should the group screen and sequence additional opportunities?

The group could continue broad partnership expansion; stage new opportunities behind integration, service and financial evidence; or put more emphasis on organic specialty-testing and patient-access capabilities while existing partnerships mature. The choice concerns potential future opportunities. Signed or completed arrangements are part of the historical record, not decisions to reverse. [P1] [P2]

Labcorp says partnership opportunities should be accretive in the first year, return the transaction's cost of capital within three years and have a clear path to margin improvement. Yet reported growth and margins combine multiple effects, and public filings do not provide partner-level economics or service outcomes. What should a useful screening process require beyond the company's stated criteria? [P1]

A post-spin company

Labcorp completed the spin-off of Fortrea on June 30, 2023. The company recast its historical segments to exclude the former clinical development and commercialization services business. Its two continuing reportable segments are Diagnostics Laboratories (Dx) and Biopharma Laboratory Services (BLS). Dx serves physicians, health systems, laboratories, patients and other customers with clinical testing; BLS provides laboratory and related services to pharmaceutical, biotechnology and medical-device customers. Their revenue and demand drivers differ. [P1, Item 1, printed pp. 9-11; Item 7, printed pp. 54-56]

A partnership strategy with several paths

Labcorp describes two near-term growth opportunities across Dx and BLS: becoming the partner of choice for health systems and local and regional laboratories, and developing, licensing and scaling specialty tests, including companion diagnostics. The company says a broad pipeline of partnership opportunities exists; that is management's characterization, not a disclosed deal list. [P1, Item 1, printed p. 10]

The company said six health-system collaboration transactions were signed or completed in 2023. Its February results release also described six new laboratory partnerships during the year. Those descriptions may refer to the same activity and should not be added together. Labcorp said it closed its Legacy Health transaction at year end, acquiring select outreach laboratory assets and beginning to manage Legacy's inpatient hospital laboratories in Oregon and southwest Washington. [P1, Item 1, printed p. 10; P2, release pp. 1-2]

Labcorp also describes consumer-centric capabilities as a longer-term growth priority. Through Labcorp OnDemand, it offered more than 50 health and wellness tests, and the company cited investments in its patient portal and patient-service-center network. These statements show strategic options; they do not report consumer uptake or returns. [P1, Item 1, printed pp. 10-11]

What the reported results show

For 2023, Labcorp reported continuing-operations revenue of \$12.162 billion, up 2.5%. Dx revenue was \$9.415 billion, up 2.3%; BLS revenue was \$2.774 billion, up 2.9%. Intercompany eliminations were \$27.7 million. Companywide growth reflected acquisitions, organic revenue and foreign exchange; it did not isolate partnership performance. [P1, Item 7, printed pp. 54-56]

Exhibit 1. FY2023 continuing-operations revenue

Reporting scope	Revenue (\$bn)	Year-over-year change
Diagnostics Laboratories (Dx)	9.415	+2.3%
Biopharma Laboratory Services (BLS)	2.774	+2.9%
Intercompany eliminations	(0.028)	-
Labcorp enterprise	12.162	+2.5%

Source: P1, Item 7, printed pp. 54-56. Figures may not add due to rounding. Enterprise revenue is net of intercompany eliminations. Segment growth rates and enterprise growth have different scopes.

In Dx, management attributed the annual 2.3% revenue increase to acquisitions (+2.3 percentage points), organic growth (+0.2%) and unfavorable foreign exchange (−0.2%). Within organic revenue, growth in the company-defined base business was largely offset by declining COVID-19 testing. For the fourth quarter, Dx revenue grew 2.6%; acquisitions contributed 1.8% and organic revenue 0.8%. The company reported 5.3% growth in the quarter's base business, partly offset by a 4.5% decrease in COVID testing. "Base business" excludes COVID-19 testing. [P1, Item 7, printed p. 55; P2, segment results, pp. 6-7]

Q4 Dx adjusted operating margin was 15.1%, compared with 16.9% a year earlier. Labcorp attributed the decline to lower COVID testing and the mix impact of recently closed hospital partnerships; it also cited higher personnel costs, partly offset by higher organic demand,

acquisitions and LaunchPad savings. The result does not show whether any particular partnership met the company’s financial criteria. [P2, segment results, p. 6]

Exhibit 2. Selected Q4 Diagnostics Laboratories measures

Measure	Q4 2023	Q4 2022
Revenue	\$2.35bn	\$2.29bn
Revenue growth	+2.6%	-
Adjusted operating margin	15.1%	16.9%

Source: P2, Q4 segment results, HTML ¶¶84-89. Adjusted operating results exclude impairment charges, amortization, restructuring charges, special items and unallocated corporate expenses. The company attributed margin pressure to lower COVID testing and the mix impact from recently closed hospital partnerships; this does not identify a causal effect for any individual deal.

The operating side of partnership value

Labcorp presents scale, a national testing portfolio, specialty tests, data and analytics, and integration experience as reasons health systems may choose it. The company also discloses risks from failing to integrate acquisitions, including customer or employee loss, difficulty consolidating facilities and systems, service-quality problems, unexpected costs and disruption to ongoing operations. [P1, Item 1, printed pp. 10-11; Item 1A, printed pp. 36-37]

A partnership may involve more than buying a local laboratory. The parties may have to determine which tests remain on site, which move to a reference lab, how specimens and results travel, how information systems connect, who pays for equipment or upgrades, and how local clinicians participate. A broader menu and network may support new services; centralization or outsourcing may change turnaround time, consultation access and control over test selection. The 10-K does not disclose the specific terms or performance of Labcorp’s individual partnerships.

Competition and the 2024 outlook

Quest Diagnostics reported 2023 revenue down 6.4%, while its company-defined base-business revenue, excluding COVID-19 testing, rose 7.1%; COVID testing fell 84.7%. Quest’s management also cited expanded health-system relationships and an M&A pipeline. Labcorp and Quest report different business mixes and measure “base business” under their own definitions, so their figures do not form a direct market-share comparison. They do show that the largest competitors faced pandemic-related comparisons while pursuing growth through relationships. [P3]

Labcorp’s 2024 guidance projected revenue growth of 4.7%-6.5% for the enterprise, 3.2%-4.8% for Dx and 5.5%-7.5% for BLS. The ranges include stated foreign-exchange assumptions, and the enterprise measure is net of intersegment eliminations. Guidance is a forecast, not an outcome or a partnership-level target. [P2, guidance table]

Decision prompt

Recommend a screening and sequencing process for potential future health-system and local/regional laboratory partnerships. State whether Labcorp should continue expanding, stage opportunities behind additional integration and service evidence, or emphasize organic specialty-testing and patient-access capabilities while it learns. Identify the evidence and governance terms you would require, define what would trigger expansion or pause, and give the strongest counterargument to your approach.

Separate disclosed facts, management statements and your assumptions. Do not infer partnership returns from consolidated revenue growth, segment margins or the number of transactions. No fixed budget or financial model is supplied.

Sources and conventions

Information is limited to material available through February 29, 2024. Revenue is reported in U.S. dollars. Dx and BLS are separate segments; enterprise figures include intercompany eliminations. Management's 2024 guidance and explanations are labeled as such. No later outcomes are included.

- **P1:** Labcorp FY2023 Form 10-K, filed February 26, 2024; Item 1, printed pp. 9-11; Item 7, pp. 54-56; Item 1A, pp. 36-37; accession 0000920148-24-000014.
- **P2:** Labcorp Q4 and FY2023 results, Exhibit 99.1 to Form 8-K, issued February 15, 2024; Q4 Dx segment results and FY2024 guidance.
- **P3:** Quest Diagnostics FY2023 results, issued February 1, 2024; full-year revenue and company-defined base-business measures.