Quest Diagnostics Inc. (DGX)

Updated August 4th, 2024 by Felix Martinez

Key Metrics

Current Price:	$150	**5 Year CAGR Estimate:**	1.6%	**Market Cap:**	$16.7 B
Fair Value Price:	$125	**5 Year Growth Estimate:**	3.0%	**Ex-Dividend Date:**	10/05/24
% Fair Value:	120%	**5 Year Valuation Multiple Estimate:**	-3.6%	**Dividend Payment Date:**	10/23/24
Dividend Yield:	2.0%	**5 Year Price Target**	$144	**Years Of Dividend Growth:**	12
Dividend Risk Score:	C	**Retirement Suitability Score:**	D	**Rating:**	Sell

Overview & Current Events

Quest Diagnostics Inc. is the world's leading provider of diagnostic information services. The company offers diagnostic testing services for cancer, cardiovascular disease, infectious disease, neurological disorders, COVID-19, and employment and court-ordered drug testing. Quest operates in the United States, Puerto Rico, Mexico, and Brazil. The company was initially founded as Metropolitan Pathology Laboratory, Inc., in 1967 by Paul A. Brown, MD. Through acquisitions and spinoffs, Quest Diagnostics Inc. was formed on December 31, 1996. Quest annually serves one in three adult Americans, half the physicians and hospitals in the United States, and nearly 50,000 employees. The company trades under the ticker DGX on the New York Stock Exchange. The company has a market cap of $16.7 billion and has twelve consecutive years of dividend growth. The most recent dividend increase was on February 1, 2024, when the company increased its dividend by 5.6%, from $0.71 per share per quarter to $0.75 per share per quarter.

On April 23rd, 2024, Quest Diagnostics reported first quarter results for Fiscal Year (FY)2024. The company reported second quarter revenues of $2.40 billion, a 2.5% increase from 2023. The company also recorded a diluted EPS of $2.03, down 1.0% from last year, while adjusted diluted EPS rose by 2.2% to $2.35. For the full year 2024, revenues are projected to range between $9.50 billion and $9.58 billion, with reported diluted EPS expected between $7.57 and $7.77, and adjusted diluted EPS between $8.80 and $9.00.

Chairman, CEO, and President Jim Davis attributed the robust performance to nearly 4% growth in base business revenue, driven by new physician and hospital customers, a favorable test mix, and strong healthcare utilization. He also highlighted improvements in operational quality and efficiency through increased automation and AI. Davis announced four strategic acquisitions, including LifeLabs, which will enhance their presence in Canada, and other acquisitions in Minnesota, Wisconsin, and Ohio to expand their footprint and partnerships with high-quality health systems.

In detailed financials, Quest Diagnostics reported a 2.4% decrease in net income attributable to the company, with diluted EPS decreasing by 1.0%. Adjusted figures showed a 2.1% increase in operating income and a 2.2% rise in diluted EPS. The company also updated its full-year 2024 guidance, projecting net revenues between $9.50 billion and $9.58 billion, and maintaining cash provided by operations and capital expenditures at approximately $1.3 billion and $420 million, respectively.

Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
EPS	$4.50	$4.77	$5.15	$5.67	$6.31	$6.56	$11.18	$14.24	$9.95	$8.71	***$8.90***	***$10.32***
DPS	$1.32	$1.52	$1.65	$1.80	$2.03	$2.12	$2.24	$2.48	$2.60	$2.79	***$2.95***	***$4.14***
Shares[1]	145.0	145.0	142.0	140.0	139.0	136.0	136.0	128.0	118.0	113.0	***113.0***	***113.0***

Quest Diagnostics has a market-leading position in several testing fields, and the company targets continued growth through Health Plan expansion, increased Hospital Health market share, advanced diagnostics, and increased shares of

[1] Share count is in millions.

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Direct-to-Consumer testing methods. However, we estimate that earnings will grow at 3% for the next five years, giving an EPS of $10.32 per share for 2029.

Valuation Analysis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
Avg. P/E	14.9	14.9	17.9	17.4	13.2	16.3	10.7	12.2	15.7	15.8	***16.9***	***14.0***
Avg. Yld.	2.0%	2.1%	1.8%	1.8%	2.4%	2.0%	1.9%	1.4%	1.7%	2.0%	***2.0%***	***2.9%***

The company has a PE of 16.9x as of this report, which is higher with its ten-year average of 14.9, and higher to its five-year average of 14.1. However, we think that a fair PE multiple of 14x is reasonable. This provides a multiple headwind compression of (3.6)%. The current dividend yield is higher than its ten-year average and the five-year average, 1.9% and 1.8%, respectively.

Safety, Quality, Competitive Advantage, & Recession Resiliency

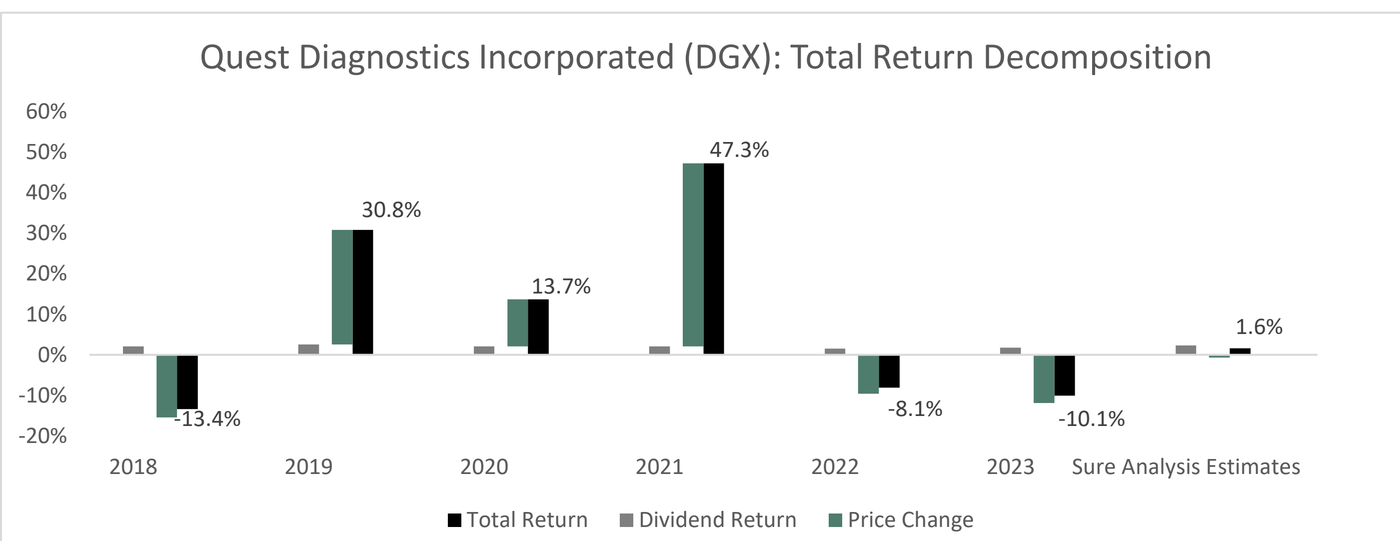
Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	29.3%	31.9%	32.0%	31.7%	32.2%	32.3%	20.0%	17.4%	26.1%	32.0%	***33%***	***40%***

Quest's competitive advantage is that it is a mature and market leader Company in the diagnostic information services industry. While this field is technically more susceptible to competition, it will require a lot of capital to build lab capacities. During the Great Recession, Quest grew earnings during that period. In 2008 EPS was $3.23 per share, and in 2009 it rose 20% to $3.88 per share. During the COVID-19 pandemic, earnings saw a tremendous growth of 70% as the company provided most of the COVID-19 tests. Quest has a BBB+ credit rating, which is an investment grade. The debt/equity ratio is 0.8, which is excellent, and the company has interest coverage of 7.1. Overall, the balance sheet is very healthy. The dividend payout ratio is low, and the company has had a dividend growth rate of 6.8% over the past five years. So, the dividend will continue to grow at a high rate.

Final Thoughts & Recommendation

Overall, Quest Diagnostic Inc. is a well-run company with a history of steady growth in earnings. The risk with purchasing shares of this company would be the post-pandemic normalization. As COVID-19 testing decreases, it will also decrease the company earnings to the 2018-2019 level. We estimate a 1.6% total annualized rate of return for the next five years. Most of it comes from earnings growth and the dividend. Thus, we rate the stock a sell.

Total Return Breakdown by Year



Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.

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Income Statement Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Revenue	7,435	7,493	7,214	7,402	7,531	7,726	9,437	10,788	9,883	9,252
Gross Profit	2,798	2,836	2,598	2,683	2,605	2,689	3,633	4,209	3,433	3,053
Gross Margin	37.6%	37.8%	36.0%	36.2%	34.6%	34.8%	38.5%	39.0%	34.7%	
SG&A Exp.	1,728	1,679	1,380	1,443	1,424	1,457	1,550	1,727	1,874	1,642
D&A Exp.	314	304	249	270	309	329	361	408	437	439
Operating Profit	983	1,065	1,159	1,165	1,101	1,231	1,971	2,381	1,428	1,262
Operating Margin	13.2%	14.2%	16.1%	15.7%	14.6%	15.9%	20.9%	22.1%	14.4%	
Net Profit	556	709	645	772	736	858	1,431	1,995	946	854
Net Margin	7.5%	9.5%	8.9%	10.4%	9.8%	11.1%	15.2%	18.5%	9.6%	
Free Cash Flow	636	558	823	923	817	843	1,587	1,830	1,314	864
Income Tax	262	373	429	241	182	247	460	597	264	248

Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Total Assets	9,857	9,962	10,100	10,503	11,003	12,843	14,026	13,611	12,837	14,020
Cash & Equivalents	192	133	359	137	135	1,192	1,158	872	315	686
Accounts Receivable	932	901	926	924	1,012	1,063	1,520	1,438	1,195	1,210
Inventories	110	84	82	95	99	123	223	208	192	190
Goodwill & Int. Ass.	7,103	6,889	6,949	7,454	7,770	7,740	8,040	8,262	8,312	8,899
Total Liabilities	5,527	5,249	5,440	5,548	5,736	7,156	7,217	7,128	6,830	7,604
Accounts Payable	257	279	231	224	222	263	446			378
Long-Term Debt	3,742	3,651	3,764	3,855	3,991	4,858	4,168	4,012	3,980	4,842
Shareholder's Equity	4,301	4,684	4,628	4,921	5,216	5,641	6,759	6,444	5,893	6,307
LTD/E Ratio	0.87	0.78	0.81	0.78	0.77	0.86	0.62	0.62	0.68	0.77

Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Return on Assets	5.9%	7.2%	6.4%	7.5%	6.8%	7.2%	10.7%	14.4%	7.2%	6.4%
Return on Equity	13.5%	15.8%	13.9%	16.2%	14.5%	15.8%	23.1%	30.2%	15.3%	13.8%
ROIC	7.2%	8.6%	7.7%	9.0%	8.1%	8.7%	13.3%	18.6%	9.2%	8.0%
Shares Out.	145.0	145.0	142.0	140.0	139.0	136.0	136.0	128.0	118.0	113.0
Revenue/Share	51.28	51.68	50.80	52.87	54.18	56.81	69.39	84.28	83.75	81.88
FCF/Share	4.39	3.85	5.80	6.59	5.88	6.20	11.67	14.30	11.14	7.65

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.