Q1/2007
CONFERENCE CALL SCRIPT
Thursday, April 19, 2007, 8:30 am ET

Laure Park: Thank you and good morning. I am here with Surya Mohapatra, our chairman and chief executive officer, and Bob Hagemann, our chief financial officer.

Some of our commentary and answers to questions may contain forward-looking statements that are based on current expectations and involve risks and uncertainties that could cause actual results and outcomes to be materially different. Certain of these risks and uncertainties may include, but are not limited to, competitive environment, changes in government regulations, changing relationships with customers, payers, suppliers and strategic partners and other factors described in the 2006 Quest Diagnostics Incorporated Form 10-K and subsequent SEC filings.

A copy of our earnings press release is available, and the text of our prepared remarks will be available later today in the "quarterly updates" section of our website at www.questdiagnostics.com.

A downloadable spreadsheet with our results and supplemental analysis are also available on the website.

Now, here is Surya Mohapatra.

Surya Mohapatra: Thank you, Laure.

During the first quarter we reported:

- Revenues of $1.5 billion;
- Earnings per share of $0.55; and
- Cash from operations of $152 million.

As expected, during the first quarter, we experienced significant attrition of the UnitedHealthcare business.

Over the last six months our marketplace has experienced a major disruption.

A large payer is attempting to turn laboratory testing into a commodity. At the same time, a large competitor has offered a significant price reduction and also guaranteed hundreds of millions of dollars of leakage.

UnitedHealthcare is taking unprecedented and inappropriate actions, including threatening doctors with penalties for selecting Quest Diagnostics.

This has created confusion among doctors and patients. During this time, we have taken action to defend our market position, and have maintained high levels of service.

And we have validated our value proposition, which differentiates us from our competitors.

As a result, we have significantly minimized the potential loss of pull-through business associated with United physicians.

Additionally, our access, quality and cost-effective service enabled us to renew our agreement with Aetna. We also renewed our agreement with Wellpoint Anthem in New England.

Our focus now is on growing our business, and we are gaining momentum.

I will speak more about our efforts to drive growth. But first Bob will review our financial performance and 2007 guidance. Bob?

Bob Hagemann: Thanks, Surya.

While our first quarter performance is behind where we would like it to be, we have gained better visibility on a number of uncertainties, which we had entering the year, and are clearly gaining momentum.

Revenues from continuing operations were $1.5 billion, 1.7% below the prior year. Revenues in our clinical testing business, which accounts for over 90% of our total revenues, were 3% below the prior year, on a 7% volume decrease and a 4% increase in revenue per requisition. The increase in revenue per requisition was primarily driven by a positive mix shift and an increase in the number of tests ordered per requisition. We estimate that revenues declined approximately 5% due to our change in status with United, with volume reduced by approximately 6%, partially offset by a positive impact to revenue per requisition of about 1%.

The positive impact to revenue per requisition is associated with higher reimbursement on the retained United work, although some of the benefit is offset by higher bad debt expense associated with having to bill patients directly. The United volume moved to other contracted providers somewhat faster than we had forecasted, with about 70% having moved by the end of March. So far that rate has not changed significantly since March 1, the date by which United has threatened to impose financial penalties on physicians. However, United is continuing to go to great lengths to move volume, and we continue to expect that additional volume will move to contracted providers as the year progresses.

While the United volume may have moved faster than we anticipated, we have retained more of the discretionary work from physicians than we initially estimated. We believe this is due to our outstanding service levels, which we improved during the quarter, and the efforts of our sales force to retain business. In addition, we worked to inform patients and their physicians that they do have a choice in selecting their laboratory provider, and that there are important differences among providers.

While the net revenue impact associated with the United change was generally somewhat less than we had estimated, we saw roughly 2% slower growth than we had anticipated due to focusing our sales force on customer retention, and clarifying significant misinformation that had circulated about the United situation during the fourth quarter and most of this first quarter. However, as we exited the quarter, we were beginning to see underlying improvement in revenue growth as our sales force began to refocus on winning new accounts and selling additional tests. Our new agreement with Aetna, which goes into effect July 1, will certainly help us continue that momentum; but remember, today we are already Aetna's largest laboratory provider, by a wide margin.

Also, impacting revenue growth in the quarter, were severe storms in the central part of the country during the month of February, which reduced revenues and volumes by about 1%.

Organic revenues in our non-clinical testing businesses as a group, which include our Clinical Trials testing business and the Risk Assessment business acquired as part of LabOne, were comparable to the prior year.

The acquisitions of Focus Diagnostics, Enterix and HemoCue contributed about 2% to consolidated revenue growth.

Operating income as a percentage of revenues was 13.2% for the quarter, compared to 16.7% in the prior year. We estimate that the net revenue loss associated with United impacted margin comparisons by just over 3%. As we indicated when we provided guidance in January, the profit impact associated with lost business will be greatest during the first six months following its loss, due to the time it takes to align the cost structure with volume levels. And, as I mentioned earlier, during the first quarter we actually increased certain expenditures to maintain and improve service levels, and inform physicians and patients of the facts regarding their choice of laboratory providers.

In addition, during the quarter we recorded charges of $11 million associated with workforce reductions, which reduced margins by almost 1%.

Bad debt expense as a percentage of revenues was 4.4% compared to 4.1% last year. The increase was principally driven by higher bad debt expense associated with billing patients directly for a portion of the United volume.

The acquisitions of Focus, Enterix and HemoCue combined to reduce margins by about a quarter of a percent after the amortization of intangibles.

As required by the accounting rules for acquisitions, we recorded a pretax charge of $4 million, or $0.01 per share, to expense in-process R&D in connection with the HemoCue acquisition. The charge is recorded in other operating expense, net.

Diluted earnings per share from continuing operations were $0.55 compared to $0.77 in the prior year. The decrease was associated principally with the change in contract status with United, and the various other items I just discussed. Included in footnote 7 to the earnings release is a table, which summarizes the impact to various measures for each of the items.

Cash from operations was $152 million, compared to $241 million in the prior year, with the change driven principally by the various factors already discussed. During the quarter we made capital expenditures of $40 million, repurchased $105 million of common stock, and invested $450 million in the HemoCue acquisition. Days sales outstanding (DSO's) were 47 days, down one day from year-end. For the most part, the work we have performed for United members is being reimbursed on a timely basis. As a result, the several day increase in DSO's we were anticipating was avoided.

Turning to full-year 2007 guidance.

While we have gained better visibility on a number of questions we had coming into the year, as we explained to you in January, developing estimates for the full year will remain challenging, through at least the second quarter.

Our current guidance for results from continuing operations is as follows:

- We expect revenues to approximate \$6.1 – \$6.2 billion. The increase from previous guidance is principally due to the HemoCue acquisition.

- We expect operating income as a percentage of revenues to be between 16 and 17%. This is about half a percent below our previous guidance principally due to the first quarter results. However, we continue to expect to exit the year with margins similar to our earlier estimates.

- We continue to expect cash from operations to approximate \$800 million and capital expenditures of approximately \$200 million.

- And lastly, we expect diluted earnings per share, adjusted to exclude the \$0.04 in Q1 charges, to be between \$2.75 and \$2.95, the midpoint unchanged from earlier estimates.

- These estimates exclude the impact of the planned acquisition of AmeriPath and any additional charges related to potential restructuring activities.

The first quarter was particularly challenging, and we expect there will be challenges for the remainder of the year. However, we are gaining momentum and are excited by the opportunities we see, and expect to exit the year as strong, or stronger than, we anticipated at the start of the year. Now I will turn it back to Surya.

Surya Mohapatra: Thanks, Bob.

We continue to leverage sales, service and science to drive organic growth. And we are clearly focused on all three fronts.

It was our access, quality and cost effective service that led to our new agreement with Aetna. We are pleased to have the opportunity to continue to serve their members, and we are working with Aetna to communicate the contract change to physicians.

We continue to enhance the overall patient experience. We are seeing the results of training we are providing to our phlebotomists. Nine out of ten patients surveyed in our Patient Service Centers rated their experience “outstanding” and 98% said they would return to a Quest Diagnostics PSC.

Patients and managed care organizations are excited about our electronic appointment scheduling for patients. We have accelerated the deployment and most of our PSC’s across the country will be live by the end of the summer.

Our emphasis on introducing new tests, services and technologies is helping to improve patient care and to drive growth. Our recent acquisition of HemoCue expands our near patient testing capabilities. Technology is enabling testing to be performed closer to the patient, whether in the physician's office or at the patient's bedside. We want Quest Diagnostics to be the trusted source for testing both in the central lab and near the patient.

We continue to build on our healthcare information technology offerings. We are excited that the province of British Columbia has selected our Care360 physician portal and our "Data Hub" to be an integral part of their comprehensive electronic healthcare system. This system is expected to transform the way laboratory results and other essential patient information is securely shared among healthcare practitioners.

We also see increased opportunities to bring our experience and expertise in diagnostic testing to international markets. In the U.K., the National Health Service recently selected us to manage the laboratory testing needs of the West Middlesex Hospital and Hounslow Primary Care Trust. This is further recognition of the quality and service we provide in the U.S. and abroad.

We have been building our cancer testing capabilities. Earlier this week we announced a definitive agreement to acquire AmeriPath, which will establish us as the leader in cancer diagnostics. This acquisition will create long-term value for our shareholders by accelerating revenue and earnings growth. It is expected to close in the current quarter.

In closing:

- Our focus on our value proposition – putting patients first, providing superior service to physicians and payers, and bringing innovative science and medicine to the marketplace—has served us well in the past and will drive growth in the future.
- Bob provided you with guidance for the full-year 2007. Looking beyond this current year, we remain fully committed to our longer-term goals – to grow revenues organically, at or above the industry growth rate; to pursue selective acquisitions; to expand margins to 20%; and to further strengthen our leadership position.
- I am excited about the prospects for our company.

We will now take your questions. Operator?

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