S&P Global
Market Intelligence

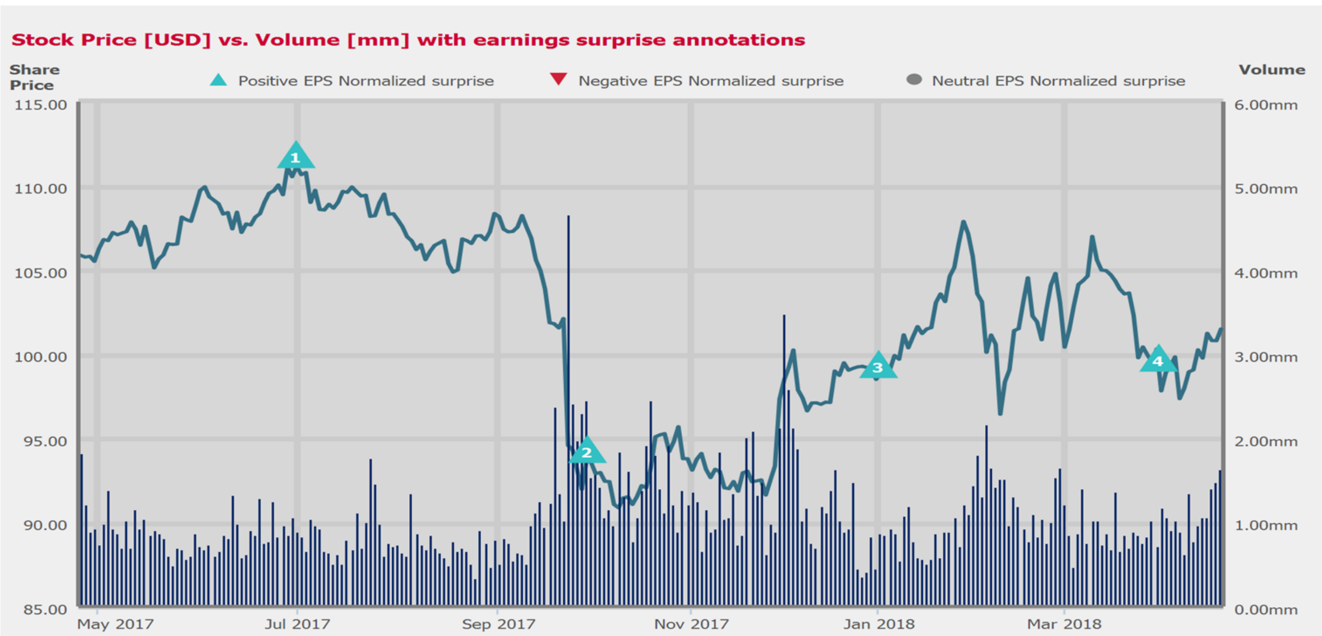
Quest Diagnostics Incorporated
NYSE:DGX
FQ2 2018 Earnings Call Transcripts

Tuesday, July 24, 2018 12:30 PM GMT

S&P Global Market Intelligence Estimates

	-FQ2 2018-			-FQ3 2018-	-FY 2018-	-FY 2019-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	1.76	1.75	▼(0.57 %)	1.69	6.61	7.00
Revenue (mm)	1953.92	1919.00	▼(1.79 %)	1944.93	7722.60	7987.14

Currency: USD
Consensus as of Jul-24-2018 12:39 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ2 2017	1.42	1.55	▲9.15 %
FQ3 2017	1.36	1.39	▲2.21 %
FQ4 2017	1.37	1.40	▲2.19 %
FQ1 2018	1.50	1.52	▲1.33 %

Table of Contents

Call Participants

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Presentation

Operator

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Now I'd like to introduce Shawn Bevec, Vice President of Investor Relations for Quest Diagnostics. Go ahead, please.

Shawn C. Bevec
Executive Director of Investor Relations

Thank you, and good morning. I'm here with Steve Rusckowski, our Chairman, President and Chief Executive Officer; and Mark Guinan, our Chief Financial Officer. During this call, we may make forward-looking statements and will discuss non-GAAP measures. Actual results may differ materially from those projected. Risks and uncertainties that may affect Quest Diagnostics future results include, but are not limited to, those described in our most recent annual report on Form 10-K and subsequently filed quarterly reports on Form 10-Q and current reports on Form 8-K. For this call, references to reported EPS refer to reported diluted EPS and references to adjusted EPS refer to adjusted diluted EPS, excluding amortization expense. As a reminder, adjusted diluted EPS excludes excess tax benefits associated with stock-based compensation. Additionally, net revenues and selling, general and administrative expenses have been restated for the basis of prior year comparisons to reflect the impact of the new revenue recognition standard that became effective January 1, 2018, and was adopted on a retrospective basis. Under the new rules, the company now reports uncollectible balances associated with patient responsibility as a reduction in net revenues, when historically these amounts were classified as bad debt expense within selling, general and administrative expenses.

Now here is Steve Rusckowski.

Stephen H. Rusckowski
Chairman, President & CEO

Thanks, Shawn, and thanks, everyone, for joining us today. This morning, I'll provide you with the highlights of the quarter and review progress on our 2-point strategy, which continues to drive results, and then Mark will provide more detail on second quarter performance. The highlight of the quarter was establishing our long-term strategic partnership with UnitedHealthcare. I'll share more on this relationship in a few minutes. We delivered strong earnings growth in the quarter driven by revenue growth and the benefits of tax reform.

Here are some key highlights from the quarters: revenues were up 3%, despite some headwinds in the marketplace; reported EPS was up more than 14% from 2017; adjusted EPS grew more than 20%. Before I describe the progress we've made, I'd like to provide an update on PAMA. We continued to support efforts by our trade association to implement a market-based laboratory reimbursement schedule. On the legal front, ACLA has sued CMS, and both sides have submitted their briefs to the court. We're awaiting the judge to rule on the briefs or set a date to hear our oral arguments. In the meantime, we continue our outreach efforts to find a legislative solution.

Earlier this month we were pleased to learn that CMS is asking stakeholders to provide comments on how to improve future data collection and reporting periods under PAMA. This is a proper step, since as we've said all along, PAMA's current reporting requirements undermine any effort to establish a sustainable market-based payment model and deliver the care that patients need. But the key will be what CMS does with their requested comments. And moreover, the need for change is now. Changing data collection for the future reporting periods does not undo the harm caused by the flawed data collection process that was used in connection with establishing the current rates.

Turning to the second quarter. We delivered on all 5 elements of our strategy to accelerate growth. The first element of our growth strategies is to grow 1% to 2% through strategically aligned accretive acquisitions. We completed our previously announced acquisition of the Outreach Laboratory Services business of Cape Cod Healthcare in Massachusetts, the leading provider of healthcare services for residents and visitors of Cape Cod. Our integrations efforts from acquisitions completed in 2017 seem to drive revenue growth and our M&A pipeline remained strong.

As we continued our conversations with hospital systems CEOs from around the country, it's clear from those discussions that there is a growing awareness of PAMA and the impact it has on their outreach laboratory business. CEOs are increasingly interested in talking more about how we could help them execute their lab strategy. As you recall, this can involve improving their hospital lab operations, working with us on reference testing and potentially selling their outreach laboratory business to us. In addition to PAMA, hospital CEOs are also seeing the trend in health plans like Aetna and UnitedHealthcare partnering with high-value providers like Quest to reduce laboratory spend and bring down the cost of care.

Under the second element of our growth strategy, we continue to expand relationships with health plans and hospital health systems. In May, we announced our long-term strategic partnership with UnitedHealthcare. Beginning on January 1, 2019, Quest will be participating as a national provider of laboratory services for all UnitedHealthcare plan participants. We're excited about this partnership as it includes a broad range of value-based programs, rewarding high quality, easily accessible laboratory services at the best value and real-time data sharing to drive more personalized care.

We are positioning ourselves to being well prepared to provide UnitedHealthcare members with a first-class customer experience. Our commercial team has already begun proactively reaching out to physician customers that elected now will be in network with UnitedHealthcare on January 1. Additionally, we'll be fielding inquiries from customers who are committed to setting us an increasingly share of their UnitedHealthcare patient specimens in 2019. We're delivering on the third element of our growth strategy, which is to offer the broadest access to diagnostic innovation. We continue to see strong growth in prescription drug monitoring, QuantiFERON, tuberculosis testing, noninvasive prenatal screening.

In the second quarter, we did experience 3 dynamics which impacted the marketplace. First, the growth we saw in prescription drug monitoring marketplace, although strong, was less than expected because of policy changes proposed by some payers to limit testing. We're engaging directly with these payers to show us the medical necessity of this testing and so far, they've had success getting at least one payer to reverse its policy change.

Second, in the hepatitis C market, we saw faster-than-expected decline in genotyping and resistance testing. This was largely due to the rapid acceptance of AbbVie's hepatitis C therapy, which works across multiple genes and does not require the same level of testing as previous therapies. We still see a tremendous opportunity in hepatitis C screening, Our screening business continues to grow, and we estimate 2/3 of more than 70 million baby boomers still have yet to be screened. Finally, on vitamin D testing, it did slow in the quarter due to increased reimbursement denials. We're working with payers and providers to ensure the appropriate testing is being performed for patients who need it.

We continue to make strong progress executing the fourth element of our growth strategy, which is to be the provider of choice for consumers. Our Walmart locations continue to see increased traffic and be well received by customers. We're now operating inside 12 Walmart locations in Florida and Texas, and will be providing more around our consumer strategies including MyQuest, our digital experience in our consumer offerings at our Investor Day in November. The fifth element of our growth strategy is to support population health with data analytics and extended care services. I'm excited about last month's launch of Quest Clinical Trial Connect, a new patient recruitment service to help pharma companies and CRO's speed the development of new therapies. We have already engaged several pharma, biotech and CRO companies with this solution.

In the area of population health, in June, we released a study on employer wellness and screening at the American Diabetes Association Scientific session showing a strong association between wellness participation and healthcare outcomes. The study showed that 1/3 of the at-risk employees identified by screening, who then participated in a behavioral health program to reduce diabetes risk, reduced glucose and hemoglobin A1c to normal levels. Also, more than 1/4 participants lost 5% or more of body weight, reducing the risk of many obesity-related conditions. This news is catching the attentions of both employers and health plans as they proactively look for opportunities to bend their healthcare cost curve. We're strengthening our already strong position in the marketplace.

The second element of our 2-point strategy is to drive operational excellence. We're continuing to drive efficiency and effectiveness within Quest to cover the cost of wage inflation and reimbursement pressure. Our efforts to digitalize our processes are improving the customer experience. So here are 2 simple, real examples of improvement opportunities in front of us. First, as we've shared previously, processing a paper requisition takes approximately 4 minutes. eEnablement allows us to improve both efficiency and quality. We are making progress in our efforts to get clients to submit electronic requisitions. Today, more than 70% of the requisitions we receive are sent electronically and this is up from approximately 60% in 2016.

Second, we have developed a client friendly application, which allows physicians and their staffs to order specimen pickups. Since the launch earlier last year, over 5,000 clients have converted to online pickup through what we call Quanum -- HCP portal, and we're adding 200 clients each week. Each day, more than 13% of routine on demand pickup requests are received electronically through our new application, and we expect that this rapid adoption will continue, while this translates into fewer calls to our call center and significantly fewer occurrences of our couriers arriving to find an empty lockbox.

Now let me turn over to Mark, who'll take you through the financial performance. Mark?

Mark J. Guinan
Executive VP & CFO

Thanks, Steve. Consolidated revenues of $1.92 billion were up 3% versus the prior year. As a reminder, we now report uncollectible balances associated with patient responsibility as a reduction of net revenues instead of bad debt due to a change in revenue recognition accounting. Revenues for Diagnostic Information Services, or DIS for short, grew 3.3% compared to the prior year, driven largely by acquisitions. Volume, measured by the number of requisitions, increased 2.5% versus the prior year, with acquisitions contributing approximately 200 basis points. Volume was softer than expected due in large part to the specific market dynamics highlighted by Steve earlier. Revenue per requisition in the second quarter grew by 20 basis points versus the prior year. As a reminder, revenue per req is not a proxy for price. It includes a number of variables such as unit price variation, business mix, test mix and test per req.

During the second quarter, unit price headwinds remained consistent with those observed in the first quarter, with a headwind of approximately 50 basis points from PAMA and less than 100 basis points from all other factors. Absent any changes to PAMA, Medicare reimbursement pressure will increase in 2019 as we've indicated previously. Beyond unit price, other risk elements remained strong in the quarter and more than offset reimbursement headwinds.

Reported operating income for the quarter was $305 million or 15.9% of revenues compared to $319 million or 17.1% of revenues a year ago. On an adjusted basis, operating income was $340 million or 17.7% of revenues compared to $343 million or 18.4% of revenues last year. The decline in operating margin was due to several factors including: investments using tax reform savings that had a 60 basis point adverse impact on operating margin, some of our larger acquisitions which are in the early stages of integration and therefore not yet delivering full margin and contribution and PAMA.

Reported EPS was $1.57 in the quarter compared to $1.37 a year ago. Adjusted EPS was $1.75, up more than 20% from $1.45 last year. During the quarter, uncollectible balances associated with patient responsibility, which we now call patient price concessions, were flat year-over-year. Cash provided by operations year-to-date was $503 million versus $490 million last year. Capital expenditures year-to-date were $151 million compared to $107 million a year ago, which is in line with the higher CapEx spend planned for 2018.

Now turning to guidance. We are narrowing our outlook for 2018 as follows: revenues now expected to be between $7.7 billion and $7.74 billion, an increase of 4% to 4.5% versus the prior year; reported diluted EPS to be between $5.50 and $5.64 and adjusted EPS to be between $6.53 and $6.67; cash provided by operation continues to be approximately $1.3 billion; and capital expenditures continue to be between $350 million and $400 million.

In addition, keep in mind that the investments in the business we are making related to tax reform savings will continue to ramp up as we progress throughout the remainder of 2018. Some of these investments are related to preparing to be a national in-network provider for UnitedHealthcare. Our narrowed revenue guidance reflects our performances through the first half. As you think about the second half of the year, consider the following: first, the actions we are taking in the areas of PBM and vitamin D testing; second, as Steve mentioned, health systems are talking to us more about how we can help them execute their lab strategy. We have a few Professional Lab Services agreements we expect to close in the second half. Taken together, we expect the benefit of these items will build as we progress through the remainder of the year. Finally, last year's severe hurricane impacts should make for easier comparison this year. The majority of the impact was in the third quarter, with some carryover in the fourth quarter as well. To sum it up, we expect growth to accelerate throughout the second half and remain confident in our ability to achieve our 2018 outlook.

I will now turn it back to Steve.

Stephen H. Rusckowski
Chairman, President & CEO

Thanks, Mark. And to summarize, we grew revenues and delivered strong earnings in the second quarter. We're excited to build on the strategic relationship that we now have with the UnitedHealthcare group. And we remain focused on executing our 2-point strategy, and, we are confident we'll meet our commitments for the remainder of 2018.
Now I'll be happy to take any questions. Operator?

Question and Answer

Operator

[Operator Instructions] Our first question comes from Patrick Donnelly with Goldman Sachs.

Patrick B. Donnelly
Goldman Sachs Group Inc., Research Division

When you think about the shifting payer contracts to nonexclusive, can you just talk through your initial discussions with United ahead of the contract opening up in January? How quickly you think you can capture share? And then just from the outside, what are the key dynamics to understand around the ramp up of business and your focus points going into January?

Stephen H. Rusckowski
Chairman, President & CEO

Yes. So Patrick, thanks for the question. We have a tremendous opportunity in front of us. When we had launched the new relationship, we talked about the opportunity to have access to over 40 million lives. And we've already started, and we've started working on this aggressively. So we have detailed out by thousands of accounts, which sales reps and which geographies will engage with customers. First of all, making of them aware of the contractual changes, talk about what we need to do to potentially serve them in a broader way. And finally is be prepared to ramp this up as quickly as possible. And so what I'll share with you is we've already left the blocks, we're off and running. We're engaging with customers throughout the United States. The receptivity of this is quite good. Been waiting for some time for us to be back on contract. And the biggest opportunity for us is for those accounts that might have had another laboratory because we were not on contract with United, now have an opportunity to continue to bring us more of their laboratory services work. And then second is, we've an opportunity just broadly in many accounts to gain more share. So we're optimistic about it and working hard at it.

Patrick B. Donnelly
Goldman Sachs Group Inc., Research Division

Okay. That's helpful. And then maybe just on the capital allocation side, pretty light quarter in terms of M&A activity, can you just update us, what you're seeing in the market? Are things developing slower than you anticipated around PAMA driving consolidation or is it more just around the processes inside of hospitals taking a long time to get deal consummated?

Stephen H. Rusckowski
Chairman, President & CEO

Yes, Patrick, just to underscore my comments, the conversations have increased. We are engaged in many more conversations today with CEOs of integrated delivery systems around their lab strategy. And in that regard, they are considering, given what's happening with PAMA and given the change they see happening with health plans, for what they should do going forward with their outreach business if they have it. So we're optimistic by the prospect. Again, there's 3 parts of our strategy. First is what we call professional laboratory services business. As Mark said, we've got a few opportunities in front of us. We're hopeful in the back half to be announcing a couple of these at least. Second is, affords us an opportunity to do more of their sophisticated testing, which we call reference testing in the hospitals. And usually, when we have those conversations, we then have a conversation around outreach. So there's more conversations today than a year ago in that funnel and that whole opportunity list continues to build for us.

Operator

Our next question comes from Ricky Goldwasser with Morgan Stanley.

Rivka Regina Goldwasser
Morgan Stanley, Research Division

So first of all, a point of clarification. When we think about the guidance for second half of the year, does that incorporate continued weakness with drug monitoring, hep C and vitamin D?

Mark J. Guinan
Executive VP & CFO

Yes. So Ricky, the hep C impact, we don't expect to be reversed. So that is kind of a permanent change. So we'll continue to have some headwinds that -- on that particular part of hep C. But as Steve mentioned, screening continues to grow. So it's still an attractive business, it's just the genotypic testing which is largely going to go away. So continued headwinds on hep C but certainly, mitigating because there will be some business that, obviously, will remain in other drugs that do require that testing. On the prescription drug monitoring, we mentioned that we've got one payer change of position. We are well down the road in discussing that with a couple of other payers, who made those changes. We're optimistic because we think that our view is the medically appropriate approach to this very necessary, important area of testing. We have some plans in place, and we're counting on not just the 1 payer being reversed, but a couple others we're feeling like we're making progress in that space. And then on vitamin D, it's really a market that has probably not always been coded appropriately. There's been changes in vitamin D that make a lot more people eligible for vitamin D testing. And there's some practices where people are still using old coding, not understanding that it's going to have an impact on the providers. So I think there's an increasing education around the appropriate use of vitamin D testing, which, of course, we support. But then ensuring that you quote it accurately as well to ensure that the providers can pay. So we're optimistic that some of that will be mitigated as well, over time, and that's why we talked about increasing momentum throughout the back half of the year.

Stephen H. Rusckowski
Chairman, President & CEO

So the guidance for the full year does contemplating, obviously, what happened in the first half but what we will address for these 3 issues that we talked about in our remarks in the second half as well. So yes, it's in.

Rivka Regina Goldwasser
Morgan Stanley, Research Division

Okay, great. And then 2 thoughts here. First of all, when we think about a step up in SG&A investment as -- in preparation for bringing on the United volume, should we think about that as incremental to the $75 million in investment that are related to tax reform savings that you talked about in the past? And should we think about this as a new SG&A base that will carry over for 2019 or are these just onetime investments? And then the second follow-up is just on unit price. In the prepared remark, you talked about the mix versus the unit price headwinds and you mentioned that 2019 reimbursement pressure will accelerate on the unit price. I know it's a little bit early, but how should we think about the mix versus the unit price in '19?

Mark J. Guinan
Executive VP & CFO

Yes, so thank you for the questions. First off, the investment that we talked about ramping up are included in that $75 million. So some incremental from the $75 million we talked about. We, in the beginning of the year, talked about a portion of that being invested in our people, in that $500 onetime bonus. We talked about some investments in the areas of accelerated growth, around advanced diagnostics and PBM. What we didn't talk about the third piece and we couldn't because that was really earmarked for United. So it's still all contained within the initial $75 million we talked about. And then importantly, though it's not all SG&A. A large portion of it is actually cost of sales. And it's investment before the volume comes, but then once the volume comes, it's just cost of sales. So as we add incremental to draw centers incremental phlebotomist, couriers and laboratory tax, ahead of that volume to ensure we're fully prepared for what we expect to come, it's in investments. But then over time, obviously, it's just the normal support you need to deliver the -- our business. And then in terms of 2019, Ricky, I'm not yet going to give any guidance for 2019. But I can assure you that when we gave the multiyear outlook, when I presented in

2016 and we reaffirmed when PAMA was announced last fall, that all of that is contemplated. So we'll give you more granularity on all those pieces at the Investor Day later in the year.

Operator

The next question comes from Amanda Murphy with William Blair.

Max Smock
William Blair & Company L.L.C., Research Division

This is actually Max on for Amanda. Just wanted to follow-up a little bit around some unit price headwinds. I know you mentioned you had a 50 basis point headwind from PAMA and 100 basis points from other factors. Can you speak around what exactly those other factors are? How transitory do you think those factors going to be moving forward? And then maybe also just some additional context around the benefit from mix in the quarter in terms of how much that contributed?

Mark J. Guinan
Executive VP & CFO

Sure. So the -- we didn't say it was 100. To clarify, it's less than 100. So that's kind of in the normal course of the last couple of years of some of the nongovernmental pricing headwinds that we've had. And it has to do with any other part of our business, whether it's extending third-party commercial contracts, whether it's the direct business in which we compete through hospital reference testing, or it can even be in the states where it's permitted, where we are actually billing physicians directly as a client who then mark-up that work and bill it to the third-party. So we have certainly competition amongst all those areas and while we've certainly turned the tide from where pricing was some years ago, as we said, there's still some degree of headwinds in the balance of our business. And that's generally going somewhere between 50 and 100 basis points over the last several years quarter-to-quarter and continues to be less than 100 basis points. Then we mentioned that when you take price and all the mix elements together, we had a favorable revenue per req of 20 basis points. So obviously, with 50 basis points of PAMA, somewhere south of 100 basis points on other pricing, we had significantly lift from the other mix elements. And then finally, we've talked about professional laboratory services, which is an increasing part of our growth. It is a business that has lower revenue per req because of the type -- the unique nature of what it is. It's basic testing done for hospital in-patient, where typically, we have fewer tests per req and more basic testing. We're not doing advanced diagnostics in that business and so on. So revenue per req tends to be lower and so that creates a mix headwind in its math in terms of our revenue per req. It doesn't in any way speak to its profitability. It's still a very attractive, profitable business. It just has a low req volume and more basic routine testing.

Stephen H. Rusckowski
Chairman, President & CEO

Yes. Just to reiterate something we always say, and Mark said in his prepared remarks, we do this calculation called revenue per requisition. But really, when you get into managing the business and understanding how that eventually yields margins, there's a lot of other considerations. Some of the slower revenue per req business actually can be more profitable than higher req -- higher dollar per requisition business. So it's not necessarily a surrogate for margins at all. So something to keep in mind. So be it in the quarter, we improved our revenue per requisition by 20 basis points, but you saw our margin were quite good in consideration for what we had to do with a lot of different moving pieces, as Mark outlined.

Max Smock
William Blair & Company L.L.C., Research Division

Got it. Appreciate the color on that. And following up on a bit of a related note. We saw a little over a week ago with the preliminary physician rules that CMS has proposed a tweak to a few thresholds to define what's an applicable labs for reporting purposes. And just wondered if there had been any discussions around what the implications can be of this internally or externally as you continue to adopt PAMA here in 2018?

Stephen H. Rusckowski
Chairman, President & CEO

Well, as I said in my prepared remarks, we're encouraged that they're asking us for input related to how to improve the data reporting. Albeit, we still believe what they did with the current Clinical Lab Fee Schedule was wrong and that needs to be corrected and we're challenging CMS in that regard. Prospective, we do need to get it right. We are pursuing a legislative solution to that. And we're engaging, as we have all along, with CMS, on how we can include more labs and how do we get the statistics to really reflect a market-based approach to laboratory services. So we're encouraged by that. Second, on the physician fee schedule, there'll be modest tweaks in that. We think it's for 2019, not necessarily that notable for our business. We have a small piece of our anatomic pathology business that get billed that way, but nothing that is material for us.

Operator

Our next question comes from A. J. Rice with Crédit Suisse.

Albert J. William Rice
Crédit Suisse AG, Research Division

First of all, just a cleanup question from some previous ones. Is there any way that we can quantify the headwind you saw from the drug testing, hep C, vitamin D in terms of maybe percentage headwind that represented?

Mark J. Guinan
Executive VP & CFO

Yes. So we have been at a pretty steady rate of organic improvements and organic growth over the last number of quarters. And then obviously, we've fallen back from that. Really, the things that we talked about are really the primary drivers of that difference, A.J. So I'm not going to give you a specific number. What I would say is those are the reconciliation between kind of the run rate organic performance we've been delivering consistently and what we delivered in the second quarter.

Stephen H. Rusckowski
Chairman, President & CEO

Yes. So we outlined the 3 areas, A.J., in our remarks. And if you look at the issues that we saw reflect what we thought we could have done versus what we really did do. So those 3, we won't quantify exactly of the 3 buckets, the total will be broken down from. But they do outline the difference between expectations of the market, our expectations and what we actually delivered.

Albert J. William Rice
Crédit Suisse AG, Research Division

Okay. And then my follow-up...

Stephen H. Rusckowski
Chairman, President & CEO

With that said, we are taking actions for a few of those to reverse it in Q3 and Q4. We mentioned the work we're doing with payers on prescription drug monitoring, the work we're doing with payers around vitamin D. As Mark said, the hep C care business, which is the genotyping resistance testing business will essentially slow down because it's no longer needed to give the new therapy for AbbVie. But the screening business continues to be a big opportunity and there's plenty of baby boomers left that need to be screened. So even though it did slow in the quarter, we're working on things to reverse that in the second half.

Albert J. William Rice
Crédit Suisse AG, Research Division

Okay. And then my follow-up, I just want to ask you about a couple of growth opportunities. We talk a lot about United, Optum is in the process of buying DaVita's Medical Group. I know lots of that medical group practice -- that volume tends to go to you. Have you looked at the opportunity that might present for you and given any sizing of that? And then is there any update on your work with HCA, I know about 1 year, 1.5 years ago, you started to work with them in Denver and the idea was just sort of exploring opportunities and that could extend. Any update on those -- that discussion?

Stephen H. Rusckowski
Chairman, President & CEO

Yes. First of all, on Optum, when we talked about our relationship with UnitedHealthcare group, it's [bought]. We clearly are now back in network in 2019 with UHC as an in-network provider laboratory services, that's big. As you know, we have partnered with them on revenue cycle management. We're one of their biggest customers. Third is, we provide their wellness services for Optum. And so we are their somewhat exclusive provider of wellness services for OptumCare when they sell those to payers. Also, we're -- they're becoming one of our biggest customers, to your specific question, in OptumCare, as you said, they're buying physicians and they're buying many of our existing customers. And the opportunity with the DaVita physician business supports is yet another opportunity. So if that closes, they'll be close to -- they will have close to 50,000 physicians, and we're actively working with them on how we can better serve all their physicians, the existing accounts but also growing -- their growing list of physicians in OptumCare. So this relationship continues to build, and we see a good growth prospect of building a bigger and better relationship with OptumCare as they consolidate those practices into their business going forward. Second part of the question...

Mark J. Guinan
Executive VP & CFO

HCA.

Stephen H. Rusckowski
Chairman, President & CEO

Second part of the question...

Mark J. Guinan
Executive VP & CFO

On HCA.

Stephen H. Rusckowski
Chairman, President & CEO

HCA. The Denver opportunity which is called the Continental Division is going well. We're optimistic that we can leverage that relationship throughout the rest of HCA. We continue to work that. And as Mark said, there'll be more professional laboratory services relationships announced in the second half. So stay posted.

Mark J. Guinan
Executive VP & CFO

Yes, I would just add, A.J., and certainly you can ask them, but I'm very confident they would tell you that we've delivered the quality and the cost savings that they were looking for target up front. So now, of course, the question is what does that mean? Could it mean you expand our sites? Obviously, at the point in time if we have something to announce or something, yes, we'd announce this, but I think the good news is that both parties are happy with what was delivered and it's worked out very well.

Operator

Our next question comes from Jack Meehan with Barclays Bank.

Jack Meehan

Barclays Bank PLC, Research Division

My first question, I was curious if you could weigh in on the Women's Health business in the quarter? Think there was some impact in the first quarter from the weather and the flu. Just what were some of the trends you were seeing in the second quarter there?

Stephen H. Rusckowski
Chairman, President & CEO

Yes. First of all, as we've mentioned in our remarks, the prenatal testing business continues to grow nicely. So we're optimistic about that. Second is if you look at just ongoing activity, and we've showed this many, many times, if you look at our existing accounts and we do the same account or same-store analysis. And if you look at activity within those accounts that we know we have, we haven't lost any share. I would say, just in general the market's stable. And I would say, just in general, that's true for let's just call it the more routine portion of our Women's Health business. We continue to actually see a continuation of the slow decline in our cap business. The change in practice guidelines back in 2013 did affect the marketplace, where women in the past used to go annually for their check, that's happening less frequently and that continues to be phased in, even though it's been about 5 years. But just in general, the general volume from our Women's Health business continues to be stable.

Jack Meehan
Barclays Bank PLC, Research Division

Great. And then I had two follow-ups on capital deployment. I caught M&A added 2% to volume, what was the total revenue contribution? And then on share repurchase, I think this is the first quarter with no repurchase since 2011. So just if you could give any color on what you think the pacing is from here and why no repurchase in the quarter?

Mark J. Guinan
Executive VP & CFO

Yes. So the contribution from M&A was similar, so there wasn't a big difference. Obviously, what we're buying, Jack, is a business that's very similar to our core business. So you wouldn't see a tremendous mix difference or a differential between the volume revenue contribution.

Jack Meehan
Barclays Bank PLC, Research Division

And then on share repurchase?

Mark J. Guinan
Executive VP & CFO

Yes. So share repurchases, we actually were quiet in the quarter. We stepped out of the market due to what we thought was the impending announcement of UnitedHealthcare. So going forward, as we said, we're going to do the minimal level to meet our 50% or at least half our commitment of cash returned to our -- or free cash flow returned to our shareholders. Certainly, you should expect that level of activity. But maybe the other share repurchases would be dependent on the amount of M&A activity we have in the back half.

Operator

Our next question comes from Brian Tanquilut with Jefferies.

Brian Gil Tanquilut
Jefferies LLC, Research Division

Steve, so I guess, as I think about the recent rule that came out of CMS, the rule proposal, and how they're still viewing, obviously, PAMA as excluding the hospitals. How do you -- assuming that holds, right, how do you view the recent changes in managed care contracting, with you getting to United, LabCorp getting to Aetna? Like, how does that impact the repricing of PAMA a few years down the road?

Stephen H. Rusckowski
Chairman, President & CEO

Well, what they used, Brian, for the majority of the data points for what we got in a refresh of the Clinical Lab Fee Schedule, the vast majority of the data points were from the 2 large nationals. So that was what was used. And we think that was incredibly flawed in its approach. Matching what CMS buys from all the laboratories and it buys from thousands of laboratories, roughly 20% of what they buy is from the nationals. So the data they collected was a distortion of what they really buy. And so this is one of the biggest points we had. We've got to collect more data from more laboratories and as you know, there's wide variation in this marketplace and the best value is from a company like Quest Diagnostics. So that was the data they collected. We're hopeful. Given this current request for more data, now they can collect more data. They obviously, by asking the question, know they got it wrong and they need to get it right in the next time they collect the data. And again, we're challenging what they did in the first time around with our lawsuit. It's still in the court. We're hopeful that, that will progress, and we'll have a favorable consideration there. But in parallel to that, we're also looking for a legislative solution. So we're currently continuing to work this because we believe, as its core, how they refreshed the Clinical Lab Fee Schedule was done wrongly. But given all that, what we've outlined in our guidance for this year, what we've outlined in our outlook for 2019 and 2020 is assuming worst case. That is if this sticks and continues to be the case then that in fact will be what we'll absorb, and we'll be able to manage the business and hit our outlook despite it. So hopefully, we'll have better news in that regard, but we're assuming the worst case. And then in the future, yes, there'll be data points gathered from payers. But again, there'll be more laboratories included in the data collection process, so therefore, that will move the needle quite a bit. So hopefully, that answers your question.

Mark J. Guinan
Executive VP & CFO

Yes. So let me just quickly comment, Brian, on its impact on PAMA. So as we've shared, we're very vocal with all the payers, not just getting United, and I certainly can't speak for our competitor. But I can tell you that when we go in there and say, "Hey, now there's full transparency," we know where the weighted volume median is amongst the national providers, we know we provide the best prices. And the fact that you already get the best prices from us and that we're going to be paying for potentially twice, with PAMA, means that you're not getting any better prices. And if anything, it's an opportunity -- has been an opportunity for us to talk about getting paid more, because even if -- getting paid more, because even if we're paid a little bit more than we have been recently or historically, it's still a much better value than the majority of the people are paying. And in fact, in the United contract, when we talked about value-based contracting, as we move volume away from those high-cost providers, part of the contract is what you'd call a bonus rate. So basically, we share the savings with our partner and that will ensure that as we're saving the healthcare system patients and the payers all money, that it doesn't damage us from a PAMA perspective, but actually, should be neutral to positive depending on how we perform and where that volume growth comes from.

Brian Gil Tanquilut
Jefferies LLC, Research Division

No. I appreciate that. And I guess the follow-up to that is, as we think about the networks built around United and Aetna, how do you think about the pace of market share shift? Not necessarily from your national competitor, but from the regionals. What is that opportunity and how hard of a lift or how heavy of a lift is that?

Stephen H. Rusckowski
Chairman, President & CEO

Well, that's the opportunity in front of us. And with this relationship with United, and we're having conversations with all the payers. Despite the 2 nationals having strong presence, there's still an opportunity to pick up share for the rest of the marketplace. We talked about the opportunity, when we talked about United, you have roughly more than 40 million lives. You go quickly through the mathematics of that, we basically have shared that their spend -- laboratory spend is north of $7 billion in that regard.

If you look at the 2 large nationals, it's still a minority. It's still the opportunity given the trend in general of healthcare is to move more of those higher cost, more expensive laboratory volumes to us. And so what we're detailing right now is precisely that. We're knocking on the doors of many -- thousands of customers, Brian. And they have many laboratories and many of those laboratories aren't the 2 large nationals, but they're many others. And in some cases, they have those laboratories because we were not in network with United. They no longer need those laboratories to serve them and therefore, those afford us a big opportunity. So we need to think about this not just between us and the other large national, but more importantly, the opportunity to really continue to gain share, particularly for the regional portion of this market.

Operator

And our next question comes from Lisa Gill with JPMorgan.

Lisa Christine Gill
JP Morgan Chase & Co, Research Division

In your prepared comments, when talking about United, you talked about value-based programs. When we think about the contracting for the new relationship, is it a traditional lab relationship when we think about being paid for the req? Or are you seeing changes in the way that you're contracting around value-based programs? That's my first question. And then secondly, if that's not the case, can you help us understand what some of the opportunities are around value-based programs, especially with United and Aetna as we think about the new contracts?

Mark J. Guinan
Executive VP & CFO

Yes, so Lisa, it is a traditional relationship. We're paid for activity. Generally, obviously, there's some portions where they're fully insured, where they have an HMO plan. But for the most part, this is a traditional fee-for-service contract. The difference is that the rate is variable dependent on our performance. So when we talk about value-based contracting, as I referenced earlier, there is incentive payments that we can earn by saving the money. When I say saving them, I'm talking about not just the United but obviously, the healthcare system and especially the patient. So there's an awful lot of work going to high-cost providers. Some of it because they have significantly higher prices, certainly talked about hospitals and physician-owned laboratories, but even some regional players. The other thing is that the payers are becoming increasingly aware that we don't all conduct ourselves in the same way. So price is one thing but the level of activity for a patient with a given condition is also a driver. So you could have some labs that might have lower pricing with same pricing as we do but they're actually charging more because there's more activity for a given condition. So really, the focus around what is the total cost per interaction with a patient in saving money on that by doing things medically appropriate at a good price. And to the extent that, that saves money for the system and overall stakeholder, some of that will come back to us. So there's an incentive for us. A lot more detail will come down the road. We believe that, around the middle of next year or maybe a little ahead of that, United will talk about their preferred network and what some of the conditions are to be a preferred provider. But also what some of the structure is, including things that we are hopeful about, including planned benefit design, where there's actually incentives for patients and other in the decision process financially to drive things towards that preferred network, because that preferred network will be at the highest quality and the best value of any of the options within the network. So that's about what we can share right now. And we're very excited about it because that is different from, historically, where we would get a network and to a large extent, it'll be kind of good luck, I hope you do well because you're great value. In this case, the United and certainly we're talking with other payers about similar relationships, actually is going to be partnering with us, working to drive that, not just sitting on the sidelines and hopping we do all of that on our own.

Lisa Christine Gill
JP Morgan Chase & Co, Research Division

Great. That's very helpful. And then just secondly, you did comment on the Walmart relationship, but is there any update on the Safeway relationship or any other retail relationship that you have in the market?

Stephen H. Rusckowski
Chairman, President & CEO

Well, first of all, Safeway continues to go very well. We've said that we're approaching 200 stores. The results in those stores have been a great. So we're very encouraged there. Second is we continue to build out the presence in Walmart. And the number will be a significantly higher than 12 stores, I can assure you of that. And yes, it's putting draw stations in, but it's also providing better healthcare, more healthcare services, with what we call extended care services. The conversation has become very broad and deep. Matter of fact, today, I'm meeting with a very senior executive from Walmart about that opportunity. Our JV and specifically Walmart is doing in healthcare. So we continue to build that out. And then third is we are testing. We're doing some pilots with some other retailers. As we mentioned in the past, we've done work with CVS in the Minute Clinics with their pending potential merger with Aetna. We have great relationship with Aetna, we have a great relationship with CVS. The opportunity that they see also is what we've been talking about here. So we're optimistic of working more proactively potentially with CVS and Aetna as they expand the potential merger with those 2 companies as well. So a lot in front of us. We have the right strategy, we're executing it and we're making a lot of progress.

Operator

And the next question comes from Kevin Ellich with Craig-Hallum.

Kevin Kim Ellich
Craig-Hallum Capital Group LLC, Research Division

Steve, just wanted to follow up on your consumer comments to Lisa's question. I guess, as we think about it big picture and holistically, over time, how much do you think all of these consumer initiatives could really add to your growth, whether it's through volume or revenue?

Stephen H. Rusckowski
Chairman, President & CEO

Well, we think -- if you take a step back and look at where we're going. Our access with United will be greater than 90%. So we want to remove the obstacles of not being in network with many of the majority of health plans throughout the United States. And in the big states, as we mentioned, when we announced the United relationship, the big states of New York, Texas, Florida and California, our access is greater than 95%. So very strong access. So when we have access, we have an opportunity to compete for laboratory services in accounts. So that's number one. So great access, it's improving every day. Second is the consumer is becoming increasingly more important, particularly as employers have pushed more of the cost of healthcare to the consumers. Consumers, patients are asking questions of what they can do to lower their out-of-pocket cost and also serve themselves in a better way. And so our consumer strategy addresses that; that is making sure that we have a great experience for that patient and consumer. So many aspects factor into that. One is what we've done with our electronic or e-tools, we call it MyQuest. We now have over 5 million registered users, the application continues to get stronger every day. You now can get your lab results, you can schedule an appointment. You can see wait times in a Patient Service Center throughout any area you're in and there will be more to come. So that's exciting. More -- looking more and more like a contemporary consumer application every day. Second, our access gets better and better. We're refreshing our Patient Service Centers. You'll see that if you go through a number of your Patient Service Centers throughout the United States. And then we augment that with the access through retailers, so we'll have more retail-like settings, making it much more physically easy for consumers to go to Quest Diagnostics. Third is we'll have products. And we have taken our experience in Arizona and also in Colorado, in Missouri with the direct-to-consumer offering. We now believe it's close to 20 states that we can go direct to consumers. We're working on broadening that solution and there'll be more to come in that regard in the fall. And with all that, you take a step back and you say when the physician eventually knows that we're in a network and they ask their patient, who would you like to go to, Quest or someone else? They remember that great experience. We have experience as far as their data. And they also know that it's not ordered by the physicians, they can order products directly from us, like a checkup on their cholesterol or their diabetes and hemoglobin A1c. So we think directionally, it's going to help us gain share in the marketplace because healthcare is becoming increasingly and more of a consumer marketplace.

Kevin Kim Ellich
Craig-Hallum Capital Group LLC, Research Division

Got you. That's super helpful, Steve. And then just a quick follow-up on the headwinds that you called out earlier on the call, hep C, drug testing, vitamin D. What -- did that have any impact on your -- or what impact did it have on your revenue per requisition, if any?

Stephen H. Rusckowski
Chairman, President & CEO

Mark?

Mark J. Guinan
Executive VP & CFO

Yes. Really not anything substantive. I mean, it's -- those businesses are within the same ZIP code as the overall revenue per req. Yes, the one difference is obviously, when you get denials, that's going to have a negative impact. So when you don't -- when the tests aren't ordered like in a hep C case, it kind of has a neutral impact. But certainly, when we do work and then get denied, obviously, that's a headwind to revenue per req.

Operator

Our next question comes from Dan Leonard with Deutsche Bank.

Daniel Louis Leonard
Deutsche Bank AG, Research Division

Just one question on the pacing of M&A. So how much of a catalyst you think the UnitedHealthcare contract is going to be by itself with its value-based components? And how quickly do you think that could accelerate the discussions you're having with health system CEOs?

Stephen H. Rusckowski
Chairman, President & CEO

Well, the first catalyst is PAMA, okay. So PAMA is a substantial change for hospitals renting outreach businesses. In many hospital system outreach business is -- their Medicare mix is 25%, 30%, so not insignificant. And when they're looking at a -- essentially a 30% cut over 3 years, it's a notable difference. That's number one. Second is they are seeing what's happening with United and also with Aetna. And they are hearing that what those 2 large nationals have done will carry over to the rest of the health insurance marketplace. So they're realizing there will be pressure on their commercial rates going forward for ancillary services and in this case, laboratory services. So with all that, it's allowing us -- we've already – always had great access throughout this concept of talking to them about their lab strategy, but it is accelerating the pace of them considering their options going forward.

Operator

Our next question comes from Mark Massaro with Canaccord Genuity.

Mark Anthony Massaro
Canaccord Genuity Limited, Research Division

So your large lab competitor will become an in-network lab provider to Aetna beginning in 2019. Is there anything your team can or need to do to defend your share of that business? And then secondly, do you expect a resolution from the PAMA lawsuit perhaps in Q3?

Stephen H. Rusckowski
Chairman, President & CEO

Yes. So first of all, we're actively detailing out account by account what we need to do. The way we broadly think about is the 3 categories. One is, we have great accounts. And an account -- a client might be using another laboratory because they had to because we weren't in network with United, and we're going directly for those accounts and we're trying to flip those as quickly as possible. So as I said earlier, we've left the blocks and we're running. And we're detailing our thousands of accounts throughout the United States with our sales force and with our regional teams. Number two, there is accounts in kind of a mixed model where they're using multiple labs. And now where we have much more significant share of their laboratory volume because we're back in network. It's an opportunity where they potentially get to a tipping point, and we potentially could become the majority of their lab service provider. So we have a number of accounts that I would categorize that way. And the third category that you've outlined is, in some cases, we are not the majority and our other national competitor has more share. And we're also detailing out those to make sure we defend what we deliver, our value that we deliver every day is quite good, our quality gets better, our service performance is outstanding, our consumer strategy is resonating. And so we think we have a very, very strong requisition -- value proposition to defend that piece of our marketplace as well.

Operator

And that comes from Ann Hynes with Mizuho Securities.

Ann Kathleen Hynes
Mizuho Securities USA LLC, Research Division

Just a couple of follow-up questions. One is, your DSOs are up year-over-year 4 or 5 days and then up sequentially, is that due to acquisitions? Or is that a lot to do with this increased denials for the vitamin D in the drug monitoring testing?

Mark J. Guinan
Executive VP & CFO

Yes, so Ann, the denials are not increasing our DSOs. The denials we don't recognize revenue. So what's really driving it is a handful of things, one of them is we're doing a significant laboratory conversion in one of our major labs and billing just ends up being a little more delayed. It's a rhythm of things that we've done over time. It's nothing to be concerned about. In fact, if you look at the aging of the DSOs, the profile has not really changed. So if you look at the key metric of what proportion of our DSOs are over 90 days, it hasn't changed even though the DSOs have gone up. So we're -- this is just a temporary spike and something that we're not concerned at all about. And very confident that we're going to hit our $1.3 billion operating cash flow guidance that we provided.

Ann Kathleen Hynes
Mizuho Securities USA LLC, Research Division

Okay. And then I think in your prepared remarks, you talked about, you think the growth will accelerate in the second half and you're confident you'll make your guidance. So is that driven by acquisitions? Or do you think that organic growth will improve from the 0.5% that you reported this quarter?

Mark J. Guinan
Executive VP & CFO

So our organic growth will markedly improve. We walked through the drivers. Obviously, it's a new year compare so that's part of it. We just want to remind everybody about that. A majority of that compare is in Q3, but we had a little bit of an impact in Q4. So each of the quarters are going to get some lift from that. We mentioned, both Steve and I, that we have some special laboratory services deals that we feel are very close. That's organic. And we're expecting to get some volume for that in the back of the year, with that accelerating sequentially. And then the actions that we talked about that we've taken around prescription drug monitoring and vitamin D denials, where we've already gotten some of those addressed, and we're optimistic that a couple others are on the cusp, that, that will help as well. And then of course, as we near the entry to the United contract, we would expect that some of that volume will flip over a little bit early. So when you put all of those pieces together, that's why we're highly confident. So we're not depending on unexecuted M&A but obviously, to the extent that we do some deals between now and the end of the year, that would just be additional upside.

Ann Kathleen Hynes
Mizuho Securities USA LLC, Research Division

Okay. Great. And just one last test, with the hepatitis C testing, I think you highlighted that the drug monitoring testing and the vitamin D should come back once you work with the payers, but the hep C won't. Can you – is that a huge percentage of volume as a percent of total hep C testing?

Mark J. Guinan
Executive VP & CFO

No. It's not a huge percent. It's a small percentage. But every several million dollars makes a difference in quarterly performance. So yes, and then a lot of that is behind us because -- we're not experts, but we believe that AbbVie has more than half the market already. And therefore, a lot of that is already behind us.

Stephen H. Rusckowski
Chairman, President & CEO

And the other part is -- there's 2 parts to what we call the hep C care, which is the testing we do if you've been prescribed the drug, that is going to decline. Second part is the screening piece of this. So we did see a small decline in the growth rate, and we're hopeful, because there's still a tremendous opportunity in front of us, that we're going to work with the pharmaceutical companies to continue to build on the awareness necessary in the marketplace. Because as I said in my prepared remarks, there's still a majority of baby boomers, the 70 million of us, that still need to be screened. So that's been slow as well in Q2. And we're hopeful, in the back half, with some of the work we're doing to build awareness with pharma, that should pick up as well.

Mark J. Guinan
Executive VP & CFO

But just to clear, it's still grow. It just didn't grow as quickly as...

Stephen H. Rusckowski
Chairman, President & CEO

Grow as fast, yes, yes.

Operator

Our final question comes from Ralph Giacobbe with Citi.

Ralph Giacobbe
Citigroup Inc, Research Division

Hopped on a little bit late, so not sure if you gave this, but do you have a baseline of how much drug monitoring, hep C and vitamin D all in make-up of total requisitions? Just a rough ballpark?

Mark J. Guinan
Executive VP & CFO

Yes. No, we haven't provided that. We have other franchises, other test segments that are obviously a lot larger. Certainly, our chemistry panels and our lipid panels and so on. I think that these are already -- obviously areas, not vitamin D as much, but the hep C and prescription monitoring have been major growth drivers for us. And prescription drug monitoring, as Steve mentioned and I did as well, continues to be a growth driver. It just slowed somewhat because of these policy changes that we, again, feel are inappropriate. It really has to do everything with -- around covering definitive testing after screening. The traditional practice has been, if you do a screen and it's positive, you move automatically or revert to the definitive on the same day with the same sample. And some of the payers, for reasons that we're pushing back on, decided they would change that and make the patient come back in for a second trial. We don't think that's medically appropriate. So that was the big headwind in PDM why we slowed our growth.

And then on hep C, certainly, we expect that to continue to grow. It's a nice business, but certainly, it's nowhere near some of the routine testing or other requisition volume that we see within our business.

Stephen H. Rusckowski
Chairman, President & CEO

Yes. So what we did is we outlined 3 areas that caused us to have less than what we had expected in Q2. We started working already in Q2 on some of the remedies for that slow down. And so the ones that we outlined particularly around prescription drug monitoring, the growth rate was strong but not nearly as strong in the past and again, when we talked about with vitamin D. So we've already started to work on these in Q2 that will carry over and will have some rebound in the portion of this. But what we want to do is provide visibility of where we thought we were going to do -- have a stronger performance in Q2, we did not. And we outlined those in the 3 that we provided to you.

Ralph Giacobbe
Citigroup Inc, Research Division

Okay. And is there anything -- separately is there anything with the timing of the UNH contract we need to be aware of? In other words, I know the contract starts Jan 1, 2019. So do you remain out-of-network for this year with UNH and sort of still charge the out-of-network rate? Or have you agreed to sort of a network rate sooner even without the open network?

Mark J. Guinan
Executive VP & CFO

Yes. So we -- I'm not going to comment on any specifics around rates, but we remain out-of-network, we'll be adjudicated out-of-network for the balance of the year. And then as we said, starting January 1, we'll be in for majority of their plans, there's still some HMO plans that we're working for the details. But for the vast majority of United, we're going to be in network as of January 1.

Ralph Giacobbe
Citigroup Inc, Research Division

Okay. Last one if I could squeeze it in. Just and I know you're not going to guide for 2019 at this point, but can you give us a directional sense of margin as we think about next year? There's a lot of moving parts, obviously, with PAMA headwinds, UNH coming on, Aetna opening up, the investments you're making. In your mind, does that mean that maybe there's sort of a revenue boost where we should think of margins as generally flat? Or do you think you can get margin expansion or vice versa? Do you think there could be some margin contraction as we think just directionally of the margin trend for 2019?

Mark J. Guinan
Executive VP & CFO

Yes. So Ralph, as I'm sure you would expect, I can't comment on 2019 in any way specifically. But what I did talk about was on a multi-year basis, that we would grow earnings, not earnings per share, but earnings faster than the top line over multiyear. So certainly, from a given year-to-year, that formula might be a little bit different. So we -- that obviously implies continued margin expansion. Now margin -- net margin, so obviously, with tax reform, we took advantage of that and made some investments, which actually reduced our before tax margin slightly this year, had some impact on that. But we would expect to continue that over multiyear look, and we'll give a update on that in November on our Investor Day.

Stephen H. Rusckowski
Chairman, President & CEO

Okay. Well, thanks, for joining us today. We appreciate your support, and have a great day.

Operator
Thank you for participating in the Quest Diagnostics Second Quarter 2018 Conference Call. A transcript of prepared remarks on this call will be posted later today on Quest Diagnostics' website at www.questdiagnostics.com. A replay of the call may be accessed online at www.questdiagnostics.com/

investor or by phone at (866) 483-9044 for domestic callers or (203) 369-1586 for international callers. Telephone replays will be available from approximately 10:30 a.m. Eastern time. Thank you.