

Unprecedented Activity Across Lab Medicine

► **Wow! Here are six sectors of lab medicine, and each is undergoing major transformation**

►► **CEO SUMMARY: Laboratory medicine is now considered one of the best opportunities to profit as the demand for healthcare services skyrockets, both in the United States and throughout the world. This is why a flood of investment capital is washing into the laboratory industry. Loaded with capital and eager to profit in the diagnostic gold rush, investors are paying ever higher prices for laboratories and in vitro diagnostics firms.**

By Robert L. Michel

DURING THE PAST 24 MONTHS, there has been unprecedented activity in every major sector of the laboratory medicine profession.

Below are examples that frame my point. They also provide a springboard to explore the causes and consequences of these events to clinical laboratories, pathology group practices, independent laboratory companies, and all the vendors who provide instruments, reagents, supplies, and information technology to laboratories.

MANAGED CARE CONTRACTING:

The announcement in October 2007, that **UnitedHealth Group** had granted an exclusive national contract to **Laboratory Corporation of America** and excluded **Quest Diagnostics Incorporated** as a provider set off intense competition to grab business now at risk. In many communities, regional labs and hospital outreach programs negotiated regional contracts with UnitedHealth, some for the first time ever, and began to capture new accounts from physicians with UnitedHealth patients.

Now, each major managed care contract that comes up for renewal or goes to bid is closely watched. Competition has intensified in what was a quiet sector in laboratory medicine.

CLINICAL LAB ACQUISITIONS:

During the past two years, a wave of new buyers has come into the market and bid up the price of clinical laboratory assets. In the last issue of **THE DARK REPORT**, we published data showing that **Sonic Healthcare Ltd.** of Sydney, Australia, has acquired seven labs over this period and invested about \$820 million. **Apax Partners, L.P.**, a private equity company, paid top dollar to purchase **Spectrum Laboratory Network** of Greensboro, North Carolina, in November 2005. Recently **Laboratory Partners Inc.** of Palo Alto, California, has closed the purchase of two labs, including **Terre Haute Medical Laboratory** in Terre Haute, Indiana.

Of course, the two blood brothers have not stopped their acquisitions of clinical laboratories. A number of their lab purchases, however, are not disclosed publicly, since the size of the purchase is not consid-

ered a material fact. Yet these small acquisitions, done at regular intervals, play a role in helping both national laboratories report quarterly increases in specimen volume and revenue.

ANATOMIC PATHOLOGY SERVICES:

There's hot action in this sector, but much of it is below the radar screen. Of course, Quest Diagnostics Incorporated's willingness to pay \$2 billion to acquire **AmeriPath** raised many eyebrows. Yet, that valuation is in keeping with other recent acquisitions and investments. **Pathology Partners** in Irving, Texas, was bought by equity investors and now operates as **Caris Diagnostics**. **Lakewood Pathology Associates** in Lakewood, New Jersey, was similarly acquired by equity investors last year.

Further, the list of independent anatomic pathology companies providing national services grows steadily. Despite the trend for specialist physicians to bring pathology in-house, many of these national pathology companies are growing, adding more pathologists, and expanding their services. For example, **Aurora Diagnostics** of West Beach Gardens, Florida, finished its first full year of operations and disclosed that it had done eight acquisitions and was posting about \$60 million per year in revenue.

MOLECULAR DIAGNOSTICS:

With advances in genetic medicine and molecular technology, a flood of new assays is finding clinical acceptance. The business model here is to control proprietary or patent-protected assays and be the exclusive source of such testing.

On the laboratory side, new start-ups appear regularly. **RedPath Integrated Pathology** of Pittsburgh, Pennsylvania, has shown impressive growth in specimen volume and revenues. Similarly, **Signature Genomic Laboratories** of Spokane, Washington, and **Access Genetics** of Eden Prairie, Minnesota, have found ready acceptance in the marketplace.

On the supplier side in molecular pathology, the most spectacular example is **Ventana Medical Systems, Inc.**, of Tucson, Arizona. It has enjoyed healthy growth rates in revenue and income—healthy enough to attract the attention of **Roche Holdings**. Roche is in the midst of a hostile takeover offer and is willing to pay \$3 billion to acquire Ventana and its \$282 million in annual sales! Similarly, last fall, **Vision Systems Limited** of Melbourne, Australia, attracted acquisition offers from Ventana and then **Cytc Corporation**, before selling, at a substantially higher price, to **Danaher Corporation** of Washington, DC.

IN VITRO DIAGNOSTIC FIRMS:

This same investment fever is white hot in the traditional *in vitro* diagnostics (IVD) industry. For example, the headline story in this issue is the \$7 billion agreement that will make **Siemens AG** of Erlanger, Germany, the owner of **Dade Behring, Inc.**, based in Deerfield Park, Illinois.

On page five, you will see a table that lists the world's 15 largest IVD companies, ranked by their 2005 sales. In the past 15 months, five of these 15 IVD firms have entered into acquisition agreements! This is a pace of consolidation not seen, even during the 1990s. And that won't be the end of it. Wall Street analysts predict further consolidation in the IVD sector of laboratory medicine.

HEALTH IT COMPANIES:

Healthcare continues to move toward an integrated, paperless environment where data and information can flow seamlessly between patients, physicians, hospitals, labs, and payers. Investors and healthcare's major information technology (IT) players are positioning themselves, and laboratory medicine is part of the equation.

Today's news is the sale of **Misys Healthcare Systems'** business division with most of the former **Sunquest** products, including laboratory, radiology, and pharmacy systems, to a private investment group in California.

Also, in this issue is the news that **Pathology Service Associates, LLC**, of Florence, South Carolina, the largest company in the United States devoted to billing for pathology services, has sold itself to **MED3000**, based in Pittsburgh, Pennsylvania. And it was just last year that **McKesson Corporation** scooped up **Per Se Technologies, Inc.**, itself a major provider of billing and collection services to hospital-based physicians, including pathologists. In the laboratory middle-ware space, **Data Innovations, Inc.**, of South Burlington, Vermont, recently completed its purchase of **P.G.P. s.a.**, of Brussels, Belgium.

► What Does It All Mean?

These six business and service sectors of laboratory medicine represent the full spectrum of activity across our profession. The list of noteworthy developments in each of these sectors provides incontrovertible evidence that the laboratory industry is in the midst of a remarkable period of change.

Sorting out what all these developments mean is the challenge. This intelligence briefing is designed to help you connect some dots and begin to see the larger picture unfolding in laboratory testing services today.

In my view, the laboratory industry in this country is poised for a transformational epoch unlike any seen in the past four decades. The *Mirriam-Webster Dictionary* defines epoch as “an extended period of time usually characterized by a distinctive development or by a memorable series of events.”

► Market-Shifting Activities

That definition aptly describes the past 24 months for the laboratory testing industry in the United States. In each key sector of economic activity (clinical lab and pathology lab providers, IVD manufacturers, IT vendors, payers, and bio-tech developers) you and I can identify market-shifting and memorable activities.

I believe the impact of these events will be magnified, for an overlooked reason. Our economy, our healthcare system, and our lab medicine profession is more integrated and interconnected than at any time in history. A simple example makes my point: what would happen in your laboratory or company if, even just for a single day: a) your IT network failed; or, 2) your Internet connection went down; or, 3) your wireless and cellphone services failed?

Note that I was only postulating a failure in communications or access to information. What would happen to many of your organizations if overnight delivery services ceased to operate? Or ceased to operate reliably? That's the source of daily specimens and primary work product for many labs and many vendors. Don't forget, overnight delivery services did shut down in the days following 9-11, causing widespread disruption in the ability of many labs to perform and deliver timely test results.

► Help In Developing Strategies

Laboratory directors and pathologists can use these six lab medicine activity sectors to develop a timely and accurate strategic analysis. My point in this intelligence briefing is to provide evidence and examples that demonstrate how the pace of change is accelerating across the length and breadth of laboratory medicine.

The change can be dramatic. In just 15 months, four of the 15 largest IVD suppliers to laboratories have come under new ownership. That directly affects your laboratory organization if it changes the company currently supplying you. It also reduces your product and vendor choices next time you are ready to buy.

Rapid change always creates threats, as well as opportunities. My goal is to help you anticipate and prepare for the threats, while recognizing the opportunities in time to gain competitive advantage. **TDR**

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