Current Trends in the Anatomic Pathology Market

Overview of Competitive Business Strategies

HAVERFORD HEALTHCARE ADVISORS

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Introduction

• Size and Growth Characteristics of the AP Market
• AP Industry Dynamics
• Market Participants
• Recent Industry Developments
• Competitive Strategies
Size of the AP Market

Overall Clinical Lab Testing Market

Clinical Lab Testing
$29.5 Billion
82%

Anatomic Pathology
$6.5 Billion
18%

$36 Billion Total Market
Size of the AP Market (cont.)

Anatomic Pathology Market

- Outpatient: $3.1 Billion (48%)
- Hospital Inpatient: $2.5 Billion (38%)
- Hospital Outpatient: $0.9 Billion (14%)

* Haverford Healthcare Advisors estimates
Size of the AP Market (cont.)

Outpatient Anatomic Pathology Market - $3.1 Billion

- Cervical: $620 Million (20%)
- GI: $170 Million (5%)
- Skin: $680 Million (22%)
- Prostate: $230 Million (7%)
- Pap Smears: $1.13 Billion (37%)
- Other: $280 Million (9%)

* Haverford Healthcare Advisors estimates
Industry Growth Characteristics

*Outpatient AP market is the place to be!*

- Overall independent lab testing market growing at 5% to 6% annually (2% price growth and 3% to 4% volume growth)

- Overall AP market growing at 6% to 7% annually

- Outpatient AP market growing at 8% to 10% annually
Factors Driving Industry Growth

- Aging Population
- Increased Incidence of Cancer
- Advances in Medicine and Technology
- Shift to Outpatient Surgical Settings
- Reimbursement Improvements – Technical Component
- Managed Care Threat Diminished
Anatomic Pathology is a fragmented industry consisting of over 3,200 practices.

Size of Pathology Practices by Number of Pathologists in Group

- 21+ pathologists: 7%
- Solo practice: 7%
- 5 to 6 pathologists: 18%
- 7 to 10 pathologists: 17%
- 11 to 20 pathologists: 19%
- 2 to 4 pathologists: 32%

Source: 2002 Practice Characteristics Survey Report - CAP

Small practices cannot match the resources of the larger players
# Market Participants

## Total Anatomic Pathology Market Share Based on 2001 Revenue

<table>
<thead>
<tr>
<th>Total Anatomic Pathology Market</th>
<th>Rev ($M)</th>
<th>Share</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>AmeriPath</strong>*</td>
<td>387.9</td>
<td>6.0%</td>
</tr>
<tr>
<td>Quest Diagnostics</td>
<td>355.0</td>
<td>5.5%</td>
</tr>
<tr>
<td>LabCorp</td>
<td>250.0</td>
<td>3.8%</td>
</tr>
<tr>
<td>Impath, Inc.</td>
<td>189.6</td>
<td>2.9%</td>
</tr>
<tr>
<td>Dianon (assumes full year UCOR impact)</td>
<td>177.0</td>
<td>2.7%</td>
</tr>
<tr>
<td><strong>Others (about 3,200 practices)</strong></td>
<td>5,140.5</td>
<td>79.1%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>6,500.0</td>
<td>100%</td>
</tr>
</tbody>
</table>

*AmeriPath revenue excludes management services revenue.

Source: Company filings and Haverford Healthcare Advisors’ estimates
### Outpatient Anatomic Pathology Market Share Based on 2001 Revenue (cont.)

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<th>Outpatient Market</th>
<th>Rev ($M)</th>
<th>Share</th>
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<td>Quest Diagnostics</td>
<td>355.0</td>
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<td>LabCorp</td>
<td>250.0</td>
<td>8.1%</td>
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<tr>
<td>AmeriPath*</td>
<td>192.6</td>
<td>6.2%</td>
</tr>
<tr>
<td>Dianon (assumes full year UCOR impact)</td>
<td>177.0</td>
<td>5.7%</td>
</tr>
<tr>
<td>Others (about 3,200 practices)</td>
<td>2,125.4</td>
<td>68.6%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>3,100.0</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
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AmeriPath revenue excludes management services revenue.

Source: Company filings and Haverford Healthcare Advisors’ estimates
Industry Developments

Top Three Pure-Play AP Companies Acquired:

Dianon: *Acquired by LabCorp effective January 17, 2003*
  Purchase price of $598.4 million

AmeriPath: *Acquired by Welsh Carson on April 30, 2003*
  Purchase price of $792.3 million

Impath: *Acquired by Genzyme Genetics on May 3, 2004*
  Purchase price of $215 million for Physician Services business unit.
Competitive Strategies

• Market Specialization
• Branding Pathology
• Affiliation with Prominent Experts
• Sales and Marketing Organizations
• Informative Diagnostic Reporting
• Centralized Operating Model
• Full Service Menu Including Clinical and Genetic Tests
• Payor Relationships
Competitive Strategies (cont.)

- Market Specialization - Providing Sub-Specialist Review
  - Preferred by physician specialists, if given a choice
  - Results in higher levels of productivity
  - Results in lower rate of uncertain diagnoses

Anatomic Pathology Sub-Specialties

<table>
<thead>
<tr>
<th>Sub-Specialty</th>
<th>Typically Referred by</th>
<th>Common Test</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cytopathology</td>
<td>OB/Gyn</td>
<td>Pap Smear</td>
</tr>
<tr>
<td>Dermatopathology</td>
<td>Dermatologist</td>
<td>Skin Biopsy</td>
</tr>
<tr>
<td>Hematopathology</td>
<td>Hematologist/Oncologist</td>
<td>Bone Marrow</td>
</tr>
<tr>
<td>Surgical Pathology</td>
<td>Primary Care Physician</td>
<td>Tissue Biopsy</td>
</tr>
<tr>
<td>Urologic Pathology</td>
<td>Urologist</td>
<td>Prostate Biopsy</td>
</tr>
<tr>
<td>Gastrointestinal Pathology</td>
<td>Gastroenterologist</td>
<td>Endoscopic Biopsy</td>
</tr>
</tbody>
</table>

Source: Banc of America Securities LLC and industry data.
Competitive Strategies (cont.)

• Market Specialization - Providing Sub-Specialist Review
  – Dianon has mastered this particular competitive strategy.
  – Each of Dianon’s 55 pathologists is a board certified, fellowship-trained, sub-specialist.
  – High level of productivity - e.g. 100+ derm path cases per day
  – Departmental review for suspicious cases
  – Sales staff and marketing materials oriented toward particular types of referring physician specialists
  – LIS and reporting is specially tailored to support sub-specialty review
Competitive Strategies (cont.)

- “Branding” Pathology
Competitive Strategies (cont.)

• “Branding” Pathology (cont.)
  – Branding helps to remove the personal link to a particular pathologist
  – Makes it easier emotionally to send the specimen out of town
  – Brand image is enhanced through advertising and promotional material
  – Brand image appears on reports - providing daily reinforcement
  – Branding will lead to patient awareness (and influence) over referral decision
Competitive Strategies (cont.)

• Affiliation with Prominent Experts
  – Creates the perception of a world-class reputation for excellence
  – Leverages the teacher-student relationship to establish a referral base
  – AmeriPath has used this strategy:
    • Established the “Ackerman Academy of Dermatopathology” in July, 1999
    • Neal S. Penneys, M.D., a leading dermatopathologist, joined AmeriPath in 2001
    • Robert E. Petras, M.D. joined AmeriPath in January, 2002, and now heads AmeriPath’s “Institute of Gastrointestinal Pathology and Digestive Diseases”
Competitive Strategies (cont.)

• Sales and Marketing Organizations
  – **Status quo for practice-based pathology today:**
    • Rely upon the professional reputations and individual efforts of pathologists
  – **AmeriPath’s Strategy:**
    • Employs approximately 100 field sales people focused on the outpatient AP market
    • Sales force divided between the *Dermpath Diagnostics Division* and the *General Anatomic Division*
    • Sales force calls on physicians, hospital and ASC administrators, the national clinical labs, and managed care companies
    • Expand on base of over 200 hospital contracts to penetrate surrounding outpatient markets
Competitive Strategies (cont.)

- Informative, **Attractive** Diagnostic Reporting
  - Attractive, color reports that include a photomicrograph, disease mapping, and prognostic data
  - Disease related information for *both* the doctor and patient
  - Dianon’s *CarePath™* has taken reporting to the next level by including reports for its physician client, the patient, and the patient’s managed care plan
Competitive Strategies (cont.)

• Centralized Operating Model
  – AP labs have substantial fixed costs that can be leveraged
  – Economies of scale are available in AP
  – Centralized model more applicable to Outpatient AP
  – Local physician resistance to sending specimens out-of-town has been overcome
  – Higher volumes support leading-edge technologies
• Centralized Operating Model (cont.)
  – Dianon’s Stratford, CT Laboratory
    • Approximately 35 pathologists
    • 64,300 square foot lab facility
    • Full service menu offered: AP, genetic testing, clinical testing
  – AmeriPath’s Center for Advanced Diagnostics ("CAD") in Orlando, FL
    • Captive specialty pathology laboratory offering:
      – Cytogenetics, Flow Cytometry, Immunohistochemistry, Image Analysis, and Molecular Studies
Competitive Strategies (cont.)

• Payor Relationships
  – AmeriPath and Dianon have been successful in establishing state-wide and regional contracts to provide pathology services with Aetna U.S. Healthcare, UnitedHealthcare, and hundreds of other insurance providers.
  – With increasing frequency, these insurers are granting these national pathology companies preferred provider status.
  – Such contracts are an effective way to extend the reach of these companies into more physician offices, resulting in pull-through volume.