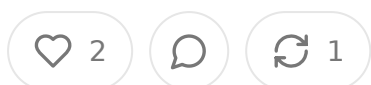


The Lab Wrapper Trap: Why Betting on Quest and Labcorp Beats Betting Against Them

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Abstract

This essay examines the investment thesis behind consumer health companies built on service layers atop Quest Diagnostics and Labcorp's laboratory infrastructure, arguing that direct investment in the underlying lab giants offers superior risk-adjusted returns. While wrapper companies like Function Health demonstrate impressive marketing execution and create genuine consumer value through improved UX and care coordination, their business models face structural disadvantages including margin compression, limited pricing power, challenging unit economics, and vulnerability to disintermediation. Analysis of Q3 2025 earnings from both Quest and Labcorp reveals robust organic growth, expanding margins, and strategic positioning that captures value across multiple customer channels. For health tech angels, this comparison illustrates why infrastructure ownership typically generates more durable returns than service-layer businesses in healthcare, particularly when the underl

infrastructure players are actively moving upmarket into the same consumer segment that wrappers target.

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The Wrapper Economy in Healthcare Diagnostics

There's a recurring pattern in healthcare investing where entrepreneurs look at incumbents with bad UX, identify a specific customer segment being underserved and build a consumer-friendly layer on top of existing infrastructure. Sometimes it works spectacularly. Oscar Health went public. Hims became a real business. Ro built something sustainable. But for every success story, there are dozens of companies that discovered they were renting someone else's infrastructure on terms that made profitability impossible.

The current wave of direct-to-consumer lab testing companies represents the latest iteration of this pattern. Function Health, Everlywell before its struggles, the proliferation of longevity clinics ordering comprehensive panels through aggregators. All of them are fundamentally in the business of making Quest and Labcorp easy to use for consumers who are willing to pay cash. The value prop is real. Going to a

Quest patient service center feels like visiting a DMV in 1987. The paperwork is insane, the results come back in formats designed for physicians not patients, and the whole experience screams “this was built for insurance billing not human beings; there’s obvious room for someone to add a layer that makes this tolerable.

But here’s the thing about building on someone else’s infrastructure in healthcare: The infrastructure owner has all the leverage, captures most of the economics, and is probably already thinking about moving into whatever adjacent market you’re creating. And when you look at what Quest and Labcorp are actually doing based on their recent earnings, it becomes pretty clear they’re not sitting still while wrap-up companies try to capture the consumer diagnostics opportunity.

What Quest and Labcorp’s Q3 Numbers Actually Tell Us

Quest just reported Q3 2025 revenue of \$2.82 billion, up 13.1% year over year with 6.8% organic growth. Their adjusted operating margin hit 16.3%, up 80 basis points from prior year. Labcorp posted \$3.56 billion in revenue, up 8.6% with organic growth of 6.2%, and adjusted operating margin of 14.4%. These aren’t mature businesses that need disruption. These are companies growing mid-to-high single digits organically and expanding margins while doing it.

The composition of Quest’s growth is particularly telling. They saw roughly 17% revenue growth in their physician channel with organic growth in high single digits driven by what they describe as “broad-based adoption of clinical innovations” and “expanded health plan access in several states.” Their hospital channel grew low single digits but Co-Lab Solutions is scaling aggressively. The Corewell Health deal alone is expected to generate approximately \$1 billion in annual Co-Lab Solutions revenue once fully implemented. And then there’s the consumer channel, where Quest explicitly called out “increasing momentum” as they position themselves as “the preferred lab engine inside top wellness brands.”

That last point is critical. Quest isn’t sitting back watching Function and other consumer businesses on top of their infrastructure. They’re actively partnering

WHOOP, Oura, and other wearable/wellness brands to be the lab provider inside those platforms. They're seeing strong double-digit growth from [questhealth.cc (<http://questhealth.com>)], their own consumer-initiated test platform. They're moving upstream into the exact customer experience layer that wrapper companies thought was their defensible territory.

Labcorp's doing similar things. Their diagnostics business grew 8.5% with strong performance in what they call their "gene-based and esoteric testing services," which includes their advanced diagnostics portfolio. They're not breaking out consumer specifically but they're clearly investing in specialty testing areas like oncology, neurology, and women's health that have strong consumer pull. The Invitae integration gives them genetic testing capabilities that appeal directly to the longevity and wellness crowds. Their Alzheimer's blood tests more than doubled in Q3 following new clinical guidelines.

Both companies are also printing cash. Quest generated \$1.42 billion in operating cash flow through nine months, up 63% year over year. Labcorp did \$1.03 billion through nine months, up 27%. They're using this cash to acquire strategic assets, invest in technology platforms, and return capital to shareholders. Quest raised full year guidance again. Labcorp did the same. These are businesses operating in positions of strength, not incumbents ripe for disruption.

The Structural Problem with Lab Wrappers

Let's talk about what happens when you build a business that depends on Quest or Labcorp as your primary vendor. Every customer you acquire represents a transaction where you're the middleman between that customer and the lab. The lab knows exactly what those tests cost them to run. They know what margin they need. They know you need them more than they need you. Yes, you can negotiate volume discounts. But those discounts are still subject to the lab's pricing power and cost structure.

Function is charging customers around \$500 annually for comprehensive panel tests done twice per year. They're using Quest for the actual lab work. Let's be generous and assume Function negotiated really aggressive pricing and they're paying Quest \$150 per panel, so \$300 per customer per year in direct lab costs. That leaves \$200 gross margin before any other costs. Now you have to pay for the phlebotomy visit, customer dashboard and technology, care coordination, customer support, and most importantly customer acquisition.

The customer acquisition cost question is where this gets brutal. Function has done an incredible job building brand through content marketing and community, but they're still spending heavily to acquire customers. Let's say they're achieving the best-in-class CAC of \$200 per customer through efficient digital marketing. At \$200 gross margin and \$200 CAC, you need a customer to stay for at least one year just to break even, and multiple years to achieve acceptable payback.

But retention in wellness products is historically terrible. Year one, you're excited about your numbers. Year two, assuming nothing dramatic changed, the novelty wears off. Year three, you start asking whether you really need comprehensive biomarker monitoring when you feel fine. Function might beat industry averages because of their community and content, but they're still fighting against the fundamental dynamic that most people don't naturally engage with health data when asymptomatic. This business needs constant customer acquisition to grow, which means marketing spend never decreases as a percentage of revenue. That's a treadmill.

Compare this to Quest's unit economics. They own the labs, the collection network, the logistics infrastructure, the IT systems, the relationships with physicians and health systems. When a physician orders a test, Quest captures the full reimbursement from the payer minus their own cost of goods. When a health system signs a Co-Lab Solutions deal, Quest gets infrastructure fees plus testing volume and supply chain revenue. When a consumer orders through [questhealth.com] (<http://questhealth.com>), Quest gets direct revenue without paying a middleman. This margin structure is just fundamentally better when you own the infrastructure.

Where Value Actually Accrues in Diagnostic Value Chains

There's a broader principle here about where value accumulates in healthcare value chains. In general, value accrues to whoever owns the scarcest or most difficult-to-replicate asset. In diagnostics, that asset is the lab infrastructure itself. Running CLIA-certified lab is hard. You need significant capital for equipment and facilities. You need specialized technical staff. You need quality control systems that meet regulatory requirements. You need scale to make the economics work because fixed costs are high. You need relationships with physicians who trust your results. You need integration with EHR systems and payer billing infrastructure.

All of that creates massive barriers to entry. There's a reason the lab industry consolidated into two dominant players (Quest and Labcorp) plus a handful of specialists like Exact Sciences and Guardant in specific niches. Once you've built infrastructure, the incremental cost of running additional tests is relatively low, creates operating leverage as volume grows. Quest's adjusted operating margin expanded 80 basis points year over year in Q3 even while they're investing in growth initiatives. That's what happens when you own infrastructure that scales.

Now compare that to what a wrapper company owns. They have a consumer brand, a decent dashboard, some care coordination processes, maybe some proprietary patient engagement tactics. But none of that is particularly hard to replicate. Another well-funded competitor can build an equally good consumer experience with enough capital. The underlying labs can decide to build their own consumer interfaces, they're actively doing. The barriers to entry for the service layer are orders of magnitude lower than the barriers to building lab infrastructure.

This dynamic plays out across healthcare. Telemedicine companies discovered that they were renting physician networks and pharmacy infrastructure on terms that made profitability elusive. Digital health companies built on top of EHR data found that EHR vendors captured most of the value and could cut them out anytime. Care navigation companies learned that self-insured employers would only pay so much for a service layer when they could contract directly with providers. The pattern is

consistent: service layers built on someone else's infrastructure tend to get squeezed over time unless they develop genuine moats beyond just having better UX.

Why the Giants Are Better Positioned for the Consumer

The conventional wisdom in health tech is that incumbents are slow and bad at consumer experiences, creating opportunities for startups to win consumer segments through superior product and marketing. Sometimes this is true. But it's worth examining whether Quest and Labcorp are actually that disadvantaged in consumer

Quest has 2,200 patient service centers. That's real physical infrastructure in communities across America. Yes, the experience currently isn't great. But they can improve that experience if they prioritize it. They're already investing in digital front doors, appointment scheduling, and result delivery through partnerships with Epic and other platforms. Project Nova, their multi-year order-to-cash transformation using Epic's technology stack, is specifically designed to modernize patient and provider experiences. They're not technologically incapable of building good consumer products, they just historically haven't prioritized it because physician and health system relationships drove their business.

But now they are prioritizing it, because they see the consumer opportunity. The partnerships with WHOOP and Oura are telling. These wearable companies have already done the hard work of acquiring engaged wellness consumers who are thinking about their health data daily. Quest is providing the lab infrastructure and platforms needed to offer diagnostic testing to their user bases. This is a much better distribution strategy than trying to acquire consumers one by one through direct marketing. Quest gets to tap into audiences that are pre-qualified as health-engaged without having to bear the customer acquisition cost themselves.

Labcorp has similar advantages. They processed over 700 million tests annually. Their network includes relationships with 75% of the new drugs approved by FDA in 2022 through their biopharma services business, which gives them early visibility into therapeutic trends that create testing demand. Their acquisition of Invitae gives

genetic testing capabilities that are highly relevant to consumer wellness and far planning markets. Their Alzheimer's blood tests more than doubled in Q3 as guidelines changed to recognize blood-based biomarkers. They're not sleeping through the consumer opportunity, they're actively building capabilities to serve

The key insight is that winning in consumer diagnostics isn't just about having an app and good marketing. It's about having infrastructure that can deliver reliable results at scale, scientific credibility that makes physicians comfortable recommending your tests, and distribution that reaches customers cost-effectively. Quest and Labcorp have the first two in spades. They're actively building the third through platform partnerships rather than trying to outspend startups on direct consumer marketing. That's probably the smarter approach.

The Capital Efficiency Mirage

One argument for wrapper businesses is that they're supposedly more capital efficient than infrastructure businesses. You don't have to build labs or buy expensive equipment. You can scale revenue by acquiring customers digitally and outsourcing fulfillment to existing labs. In theory, this should allow for faster growth and better returns on invested capital.

But this framing ignores several realities. First, customer acquisition in competitive consumer categories is expensive and getting more expensive as digital advertising costs increase. Function might have achieved efficient customer acquisition early through content marketing and word-of-mouth, but as they scale they'll need to move more on paid channels where costs are determined by auction dynamics, not by how clever their marketing is. The CAC that worked at 10,000 customers probably doesn't hold at 100,000 or 1,000,000 customers.

Second, the capital you're not spending on infrastructure you're spending on customer acquisition, and unlike infrastructure investments, customer acquisition spend has to be repeated continuously. Quest's investment in lab infrastructure depreciates over time but generates cash flow for years. Function's investment in acquiring a customer generates cash flow only as long as that customer remains

subscribed, which historically isn't that long in wellness categories. The payback periods are completely different.

Third, as mentioned earlier, when you don't own infrastructure you're vulnerable whoever does own it. Quest and Labcorp can change pricing whenever contracts up for renewal. They can decide to compete directly in consumer and use their infrastructure cost advantage to price aggressively. They can partner with your potential distribution partners and cut you out. Infrastructure ownership create optionality and defensive positioning that service layers lack.

The capital efficiency argument only holds if you assume perfect competitive dynamics where the wrapper business can maintain pricing power, control CAC, ensure strong retention, and avoid getting squeezed by infrastructure providers. In practice, none of those assumptions hold reliably over time. The seemingly capital efficient business model often turns out to be more fragile than the capital-intensive infrastructure model once you account for competitive dynamics and customer economics.

What This Means for Angel Investors

So what does all this mean if you're an angel investor looking at opportunities in diagnostic testing and wellness? The thesis is pretty straightforward: unless a consumer diagnostics company has something genuinely differentiated beyond "UX on top of Quest/Labcorp infrastructure," you're probably better off just buying Quest or Labcorp stock.

Quest trades at roughly 17x forward earnings with mid-single-digit organic revenue growth and expanding margins. Labcorp is similar. These aren't expensive multiples for businesses with strong competitive positions, significant operating leverage, multiple growth vectors. They're both returning cash to shareholders through dividends and buybacks. The risk-adjusted returns from owning these businesses probably better than the risk-adjusted returns from owning a consumer wrapper company that depends on them, unless that wrapper company achieves truly exceptional scale and retention.

The scenarios where the wrapper company wins typically require some combination of: perfect execution on growth and unit economics, the underlying labs remaining passive and not moving into consumer, no well-funded competitors emerging to up CAC, and strong retention that drives LTV well above what wellness categories historically achieve. That's a lot of things that all need to go right. Meanwhile the scenario where Quest or Labcorp continues doing well just requires them to keep executing their current strategy of organic growth, strategic M&A, margin expansion and selective moves into higher-growth segments like consumer and advanced diagnostics. The bar for success is much lower.

There might be exceptions. A diagnostic company with proprietary hardware like Siphox (which we've discussed previously) has real differentiation because they control technology Quest and Labcorp don't have. A company with unique clinical capabilities or biomarker discovery might have defensibility through IP and scientific expertise. A business that creates genuine behavior change and has evidence of strong retention might overcome the unit economics challenges. But a company whose primary value proposition is "we made Quest easier to use for consumers willing to pay cash" is going to have a hard time generating venture-scale returns because Quest can capture that value themselves anytime they prioritize it.

For angels specifically, this matters because early-stage investors are taking concentrated bets with long time horizons. If you're investing at a \$50 million price tag in a consumer lab testing business, you need a path to that company reaching \$500 million to \$1 billion in value to generate a meaningful return. That requires either very large scale (hundreds of thousands of retained subscribers) or successful exit to a strategic acquirer. The scale path is hard because of the unit economics and competition discussed above. The acquisition path is hard because the most logical acquirers (Quest, Labcorp, and potentially large health systems) can build similar capabilities themselves rather than paying a premium for a customer base that churns after acquisition.

Compare that to the risk profile of just owning Quest or Labcorp stock. You get exposure to the entire diagnostic testing market including the consumer segment as it grows. You benefit from their infrastructure advantages and scale economies. You

collect dividends and benefit from buybacks. You're not making 10x your money you're also not losing your entire investment if execution stumbles. For most investors, the risk-adjusted return of the boring infrastructure play is probably higher than the apparently exciting growth company built on top of that infrastructure.

The broader pattern here applies beyond diagnostics. Healthcare is full of opportunities where entrepreneurs see incumbents with bad UX and think "I can do better." Often they can do better on the product experience. But doing better on product doesn't automatically translate to building a valuable business if you don't own the underlying infrastructure that delivers the service. The infrastructure owner has structural advantages in unit economics, pricing power, competitive defense, and optionalities that are really hard to overcome just by being better at marketing and product design.

This doesn't mean no one should build service layer businesses in healthcare. It just means you need to be really honest about whether you're building something defensible or just making an incumbent's offering more accessible until they decide to do that themselves. And as an investor, you need to assess whether the wrapper is likely to generate better returns than the infrastructure it wraps. In the case of consumer diagnostic testing built on Quest and Labcorp infrastructure, the honest answer is probably no unless something genuinely differentiated is happening.

Quest and Labcorp aren't perfect companies. They have challenges around reimbursement pressure, competition from specialty labs in high-value niches, and the ongoing need to modernize technology platforms. But they're growing, profit-generating cash, and have durable competitive positions in businesses that benefit from scale and scope. If you believe consumer diagnostic testing is a big opportunity, the straightforward way to bet on that is to own the companies that will process the results of those tests regardless of which consumer brand ends up winning the front-end relationship.

The wrapper economy in healthcare creates real value for consumers and serves markets poorly addressed by incumbents. But that doesn't mean wrappers create proportionate value for investors. In diagnostics specifically, the weight of evidence

suggests that value accrues primarily to infrastructure owners, and wrapper companies face structural challenges that make consistent profitability difficult. angels deploying capital in this space, betting on Quest and Labcorp either direct through public equity or indirectly by focusing on diagnostic businesses with ge technical differentiation makes more sense than betting on better UX layers built on rented infrastructure. Sometimes the boring answer is the right answer.



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