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10 Outperformers Nobody Knows About Yet

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"*Most leading brokers cannot spare the time and money to research smaller stocks. You are therefore more likely to find a bargain in this relatively under-exploited area of the stock market.*"
-- James D. Slater, the master investor who invented the PEG ratio.

I certainly agree.

I've shown in the past exactly why Wall Street is always behind the game in finding the small stock winners that build fortunes; since Wall Street talks in billions, stocks worth millions are just too small to move their needles ... this isn't the case for you and me.

I've also documented how Warren Buffett used these very same small-cap stocks to start *his* fortune.

Today, though, I want to share some of these small-but-mighty outperformers that are flying under the radar of most investors.

The outperformers
Before I show you these outperformers, let me clarify what I mean by an outperformer.

By outperformer, I do not necessarily mean a company whose stock has rocketed up in price. No, I'm talking about companies that have outperformed *operationally*; companies that have substantially grown their earnings ... and done so profitably. And we want these growing earnings at reasonable prices (before Wall Street catches on).

Using my Capital IQ institutional software package, I screened for the following criteria:

- Five-year trailing earnings growth above 10% (annualized).
- Five-year return on capital above 10% (average) vs. the S&P's five-year return on capital of just over 1%.
- Forward P/E ratio below 20.

I found both larger companies you've likely heard of and smaller companies you probably haven't. I'm going to share the ones you've heard of first for two reasons:

1. They provide a basis of comparison for the companies you're not familiar with.

2. Larger stocks are an important part of any portfolio -- I'm merely saying that there are compelling (read: profitable) reasons to look at smaller, underfollowed companies. More on that shortly.

Here they are (in order of growth):

Company	5-Year Earnings Growth	5-Year Return on Capital	Forward P/E
Apple	62.2%	29.4%	18.3
Google	40.4%	16%	19.1
Mastercard	36.6%	53.3%	15.9
Medtronic	19.3%	14.3%	9.6
McDonald's	18.2%	17.1%	16.7

Honeywell	13.9%	12%	16.8
Colgate-Palmolive	13.4%	36.7%	15.5
Pepsico	11.6%	17.9%	14.9
Accenture	11.3%	54.9%	15.0
Nike	10.2%	16.1%	18.0

Source: Capital IQ, a division of Standard & Poor's.

All of these companies appear to be kicking some serious butt without the corresponding ultra-high price tag.

If you're looking to buy some solid larger-cap stocks, these are good research candidates. But I promised you another compelling reason to look deeper, at the smaller companies other investors don't know about yet.

The reason? The biggest returns in the market come from identifying a growth story before the market catches on. The companies above are all huge in size. Though they've got impressive five-year growth, their size makes it harder for them to keep up that growth. Not so with the small companies I'm about to show you.

That's why Buffett exploited these kinds of small bargain stock opportunities in the past, before he got too big to do so.

So here you go (in order of growth):

Company	5-Year Earnings Growth	5-Year Return on Capital	Forward P/E
GrafTech International (NYSE: GTI)	77.2%	14.3%	13.3
Ebix (Nasdaq: EBIX)	61.2%	15.1%	17.3
Medifast (NYSE: MED)	54.9%	23.2%	15.9
Cubic (NYSE: CUB)	32.7%	12.3%	16.3
Immucor (Nasdaq: BLUD)	25.4%	19.6%	15.3
Tower Group	22.1%	11.1%	7.2
PetMed Express (Nasdaq: PETS)	22%	28.6%	14.1
ManTech International	18.2%	13.9%	11.6
VCA Antech	14.9%	11.2%	14.6
Synaptics (Nasdaq: SYNA)	11.6%	14.8%	10.8

Source: Capital IQ, a division of Standard & Poor's.

Very few investors are taking the time to look into these stocks -- which is a very good thing if you're trying to beat the market.

Of course, these kinds of stocks should be part of a balanced stock portfolio -- allocating between smaller companies like these and larger companies like the ones we discussed earlier. You'll also want to make sure to diversify among sectors, countries, and company life cycles.

If you want help with your asset allocation, our *Million Dollar Portfolio* service builds a real money portfolio with the Motley Fool's own money. If you'd like to learn more about *Million Dollar Portfolio*, simply click here.

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