Can This Small Cap Continue to Outperform in 2017?

Description

Collectively, small-cap businesses can grow at a tremendous rate far greater than the average market. However, **CRH Medical Corp.'s** (TSX:CRH)(NYSE:CRHM) performance has been off the charts, despite its pullback of 16% on Monday.

How much has CRH Medical outperformed? What's the cause of the drop? Is the pullback a buying opportunity? Can the company continue to outperform in the New Year? Here are the answers.

CRH Medical outperforms

CRH Medical has appreciated a little over 70% year to date. In the same period, the **Vanguard Small-Cap Growth ETF** (NYSEARCA:VBK) has returned about 12%, the **Health Care SPDR** (NYSEARCA:XLV), which holds companies such as **Johnson & Johnson**, **Unitedhealth Group**, **Amgen**, and **Celgene** as its largest holdings, has returned about -2%.

In other words, CRH Medical has been a rising star in its industry. So, what was the cause of the drop of 16%?

The 16% drop

The shares had a big drop on Monday, but there was no news released by the company. A possible explanation is that investors were taking profits.

Before the fall, the shares had appreciated more than 100% for the year. On Monday, the trading volume for the stock was 4.3 times that of the average volume.

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smiling female doctor
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Business overview

CRH Medical's hemorrhoid-treating business has done well and has started to mature. So, the company has started investing in the related business of anesthesia for higher growth. Since 2014, it has acquired nine anesthesia companies.

Recent results

In the first three quarters, CRH Medical generated US$52.5 million of revenue, which was 64% higher than it was in the same period in the previous year.

Likewise, its operating earnings before interest, taxes, depreciation, and amortization (EBITDA) were nearly US$27 million–61% higher.

In the third quarter, its anesthesia services generated 111% higher revenues than they did a year ago. This is thanks partially to the acquisitions of three anesthesia companies in the quarter located in Texas, Massachusetts, and Colorado. CRH Medical owns a majority and controlling interest in each company.

Is the pullback a buying opportunity?

Although CRH Medical's shares had a seemingly big drop on Monday, it doesn't necessarily mean it's priced at a bargain.

At about $7 per share, the company trades at a forward multiple of 25 based on the fiscal 2017 estimated earnings, which is a reasonable valuation for CRH Medical's growth potential.

However, it could experience further volatility in the near term. Cautious investors should wait for some sort of consolidation or a meaningful dip before buying.

Conclusion

Since CRH Medical is a small cap, it can experience higher volatility than the average stock. So, conservative investors would probably prefer to invest in a small-cap exchange-traded fund or diversify across multiple small caps.

Whether CRH Medical will outperform in 2017 or not depends on management's execution on the anesthesia business, which is where most of its growth is coming from.

If management executes well and the shares decline further before year end, then it's likely that the stock can outperform in the New Year barring the occurrence of a market-wide crash.

CATEGORY

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