

The Scott Letter: *Closed-End Fund Report*®

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George Cole Scott, Editor

The Scott Letter Online is intended to educate closed-end fund investors. [What are closed-end funds?](#) Closed-end funds are a valuable and profitable tool for many of our clients and colleagues. Please feel free to forward this newsletter to anyone who you believe could benefit from information on closed-end funds or go to our website (www.CEFAdvisors.com) Please call (800) 356-3508 or email: cefa@CEFAdvisors.com to learn about or get started with one of our managed portfolios. For more information on closed-end funds, please visit the [Investor Resources](#) section on our website or the Closed-End Fund Association's website (closed-endfunds.com). As always, we encourage feedback from our readers so we can continue to serve you better. Please make a note of our new website: www.CEFAdvisors.com we are currently revamping our website to better serve our clients.

We currently have back issues of *The Scott Letter Online*. They include interviews with [Adams Express \(2\)](#), [General American Investors](#), [Ellsworth & Bancroft Convertible Funds \(2\)](#), [The Royce Funds](#), [The Templeton Funds\(2\)](#), [Renaissance Capital](#), [Tri-Continental Corp](#), [Allied Capital](#), [Pan Pacific Realty](#), [Central European Equity Fund](#), [The Asia Pacific Fund](#) and [H & Q Healthcare Investors](#).

Interview with Dr. Mark Mobius of Franklin Templeton Investments

Mark Mobius is one of the world's leading emerging markets equity investors and is managing director of Templeton Asset Management Limited. He is responsible for over \$11 billion of assets under management.

Dr. Mobius joined Templeton in 1987 as President of Templeton Emerging Markets Fund in Hong Kong. He currently directs the analysts in Templeton's eleven emerging markets offices and manages the emerging markets portfolios, including many mutual funds and three closed-end funds for Franklin Templeton Investments. Dr. Mobius has spent over 30 years working in Asia and other parts of the emerging markets world. As a result of his experience, in 1999 Dr. Mobius was appointed joint chairman of the World Bank and OECD's (Organization for Economic Cooperation and Development) Global Corporate Governance Forum's Investor Responsibility Taskforce.

In 1999, Dr. Mobius was named one of the "Ten Top Money Managers of the 20th Century" in a survey by the Carson Group, a leading global capital markets intelligence-consulting firm. For the second year in a row, Dr. Mobius was named the number one global emerging markets fund manager in the 1998 Reuters Survey. CNBC named him "1994 First in Business Money Manager of the Year". Morningstar in the U.S. awarded him the "Closed-End Fund Manager of the Year" for 1993. In 1992, Dr. Mobius was

named “Investment Trust Manager of the Year” by the Sunday Telegraph in the United Kingdom.

Dr. Mobius holds bachelor and master’s degrees from Boston University, and a Ph.D. in economics and political science from the Massachusetts Institute of Technology. He also studied at the University of Wisconsin, University of New Mexico and Kyoto University in Japan. Dr. Mobius is the author of the books, The Investor’s Guide to Emerging Markets, Mobius on Emerging Markets and Passport to Profits.

NOTE: Closed-End Fund Advisors uses the Templeton Emerging Markets Fund (EMF) and Templeton Dragon Fund (TDF) in its portfolios.

The performance of EMF and TDF is as follows: (to December 31, 2003)

<u>Performance at NAV</u>	<u>6 months</u>	<u>1 year</u>	<u>3 year</u>	<u>5 year</u>	<u>10 year</u>
Templeton Emerging Markets Fund	32.23%	59.72%	34.73%	68.95%	52.33%
Templeton Dragon Fund	35.35%	74.72%	94.27%	188.54%	NA
<u>Performance at Market Price</u>					
Templeton Emerging Markets Fund	25.15%	64.72%	50.29%	44.75%	23.29%
Templeton Dragon Fund	45.52%	87.24%	137.07%	257.67%	NA
Templeton Developed Markets Trust	32.05%	60.10%	35.24%	65.21%	26.46%

We telephoned Dr. Mobius on February 5 in southern Brazil. Matthew Walsh, senior PR coordinator for Franklin Templeton Investments, joined us from in San Mateo, California.

S.L: Where are you exactly, Mark?

Mobius: I am in a car in Iguassu in Southern Brazil. The name means “singing rock”. Here is one of the largest hydroelectric power plants in the world located on the Parana River that crosses between Paraguay and Brazil. It is called Itaipu Dam and is unique as it is equally owned by Paraguay and Brazil and now produces about 22% of Brazil’s energy. We also visited Copel, another power company in the Parana State.

S.L: Is the dam as large as the one in China?

Mobius: The capacity of the Twin Gorges in China is greater. This dam produces 14,000 megawatts whereas the one in China will produce 18,000 plus megawatts. The average production is greater here because the Parana River flows faster so more water passes through it. Both dams are enormous engineering feats costing billions of dollars.

S.L: That's interesting. Regarding the two closed-end funds you manage, **Templeton Emerging Markets Fund** and Templeton Dragon funds, we have been selling-off some of these closed-end fund shares because they have been selling at premiums to net asset value. The proceeds are then employed to buy the open-end fund, **Templeton Developing Markets Trust**, which has the same portfolio and we can buy its shares cheaply at NAV. We think this is a good strategy.

Have you merged **Templeton China World Fund** into **Templeton Dragon Fund**?

Mobius: Templeton China World is now an open-end fund. Dragon is still a closed-end fund as China is very popular now.

SL: Last year when I talked to you, you were invested in 33 countries and were able to invest in 55 countries. How many are you in now?

Mobius: I haven't counted, but I would guess that it is more in the twenties. We were in more African countries, but are out of many of the smaller ones now. In Africa, we are a tiny bit in South Africa and Egypt. In Eastern Europe, we have invested in the Baltic countries such as Latvia, but aren't now. There has to be a trade-off between liquidity and value.

S.L: Does your home office track worldwide flows of funds in any way? We are interested in this now to try to see how much money is flowing into Latin America as we see the potential there. I saw in the February issue of "Latin Finance" that you wrote that Latin American equities last year returned, according to the MSCI Latin America index, over 67% last year, led by Brazil where the index returned 103% in dollar terms. Chile, Argentina and Peru also posted strong performances. Chile, you wrote, has become the regional model for structural reforms, especially in trade and market liberalization. Would you tell us what you can about the flow of funds into Latin America?

Mobius: All that is true, but tracking money flows is very difficult to come-by, and I will tell you why. On the one hand, you have fixed-income flows and on the other, equity flows so it is difficult to track. I think equity flows are a little easier to track. You have to be careful because you may have an institution with money offshore, say from Korea to Taiwan, which might not be recorded. I don't know about money flows into Latin America. However, there is a lot more interest in Latin America now, a natural consequence of the return to popularity of the emerging markets. Here in Brazil, portfolio flows have increased, while Chile has a very active fund business.

S.L: Brazil President Lula da Silva's first year has been a success because he has pursued traditional macro-economic policies, has stabilized the economy and dropped inflation from about 17% to 10%. This has moved the equity markets up 140% in 2003. Do you still think there now is value in Brazil?

Mobius: That is exactly what we talk about with our analysts every day here. We find that the price-earnings ratios are still low, earnings are outstanding and increasing. However, you look at the way prices have appreciated 100% or 200% and begin to wonder if it will last. We have become more cautious and are looking for companies that have not appreciated much where there is still value. We definitely want to stay involved.

S.L: Does that include Argentina?

Mobius: We are pretty much out of Argentina with one exception. The market has appreciated, but on

very low volume so we don't like it because you can't control it. We don't want to be in countries where there is any possibility that we can't get the money out again. Since Argentina has refused to pay its debt, the consequence is its foreign reserves are building up. I expect they will return to the bond market soon.

S.L.: Regarding Brazil, I read in the Financial Times that the current epidemic of bird flu in Asia is a marketing opportunity for Brazil, as the country is the world's largest chicken exporter, \$1.8 billion in 2003. The newspaper wonders how long it will last.

Mobius: Brazil is a powerhouse when it comes to exports. In fact, we visited two of the biggest poultry companies last week. One of the breeders told us that they have resisted raising prices because they want to keep the relationship going with long-standing customers. I think Thailand will have a hard time exporting chickens for sometime. It is interesting how these things work: the Europeans have tried to put restrictive tariffs on chickens by driving the prices of frozen chicken down and ironically taking jobs away from their own people.

S.L.: While we are on the effects of diseases, what do you think of the possibility of SARS coming back into China and Hong Kong?

Mobius: I think flu will always be with us and won't disappear anytime soon. When the SARS came in last year, I was very sanguine about it. I arrived in Hong Kong from China to see everyone in masks. I said this is not a serious disease, nor a very big thing. Sure, tourism suffered, but the actual deaths from the illness were low in terms of the psychological impact which was very big. The disease plummeted, but now has returned. I think we will see the same thing with chicken flu or whatever you have. As we get more and more of these diseases, the health authorities will catch them sooner and the World Health Organization will be more on top of it.

S.L.: I also saw in the press today that South African companies are responding to the growing threat to their profit margins posed by HIV/AIDS. Are you aware of this? Does it affect your investments in this area at all?

Mobius: I am very much aware of the question. While in South Africa two weeks ago, I talked to them about this and found that the impact is far less than people imagined. One example: while having lunch with a gentleman from the giant company, Anglo-American Gold, who is in charge of their coal operations, he said that when HIV came up, they thought they would be affected badly. So, they instituted a drug program for the workers. Other companies are starting the same program. They, therefore, really have mitigated the disease. The executive, who previously was against the drug program, changed his mind. It costs about a dollar a day per person. So, I think they are beginning to lick that problem. If you look at it from a hard, cold point of view, the supply of workers for the mines is there and the cost of labor isn't a problem. So, I do not see that their profit margins are suffering from labor problems, but from the appreciation of the currency, the Rand, which raises the costs of exports.

S.L.: Do you ever read the publication, "State of the World", which is published annually by The Worldwatch Institute of Washington, DC ?

Mobius: No, but I would like to get it. Matthew, would you take a note of that so it can be sent to me? (Matthew told me later the book was on its way by Fed-Ex to Dr. Mobius).

S.L: The 2004 issue also has an article on “The State of Consumption Today”. It says that consumerism is spreading too quickly all over the world, especially in China because of rising prosperity. Throughout the twentieth century, the streets of China, formally filled with literally millions of bicycles, are now filled with over 10 million private cars, particularly in Beijing and Shanghai. They added four million new private cars in 2003 alone. I was in Shanghai in 1997 and saw some of this. The book also says that almost half of the growing consumer class now lives in the developing nations. How much of this have you noticed in your travels?

Mobius: That’s interesting because in our investments in the last few years we have concentrated on three themes: consumers, commodities and conversion. Consumerism is right at the top and we see that exploding in many countries such as Brazil, China and India. It is incredible. Yesterday, I walked into a Wal-Mart here just like anything you would see in America. The retail revolution is definitely here in every emerging country. That is exciting, because what it means is that these countries are not only going to be dependent on exports, but also will be generating their own consumer demand which is very important.

S.L: Aren’t we talking about a rising middle class? However, many Americans are concerned about its environmental consequences.

Mobius: Yes, but mind you there’s a great mass of very poor people who are aspiring to move-up the ladder. Their governments are under pressure to find jobs to lower unemployment rates and inflation as well.

S.L: Would you tell us more about why there has been so much prosperity, which must explain why so many emerging stock markets are doing so well?

Mobius: Absolutely. The cost of money has come down dramatically. That is why so many companies are restructuring their debt. Here in Brazil, I see companies which a few years ago would be happy with two-year money. Now they are getting 10, 12 even 15 year money from dollar accounts to reduce debt. So, it is looking a lot better. The interesting thing I find when I talk to the banks here and in other parts of the world, is that they are focusing on consumer rather than corporate lending as they see big money to be made in consumer loans. Companies like GE have been everywhere, even going into the banks and buying-out their consumer loans at discounts. That is something we have to watch carefully.

S.L: Have you spent much time in India lately? We have seen much about the rising prosperity there in our press.

Mobius: I was there six months ago and will go back next month. India has been booming, with lots of optimism. An interesting sidelight is that our own mutual fund business in India is now managing \$3.5 billion, up 50 percent from two years ago. We see the same thing in South Korea, about \$3 billion worth. A lot of the hot stocks in India have been in software because of outsourcing from the U.S. We find that they are building the same culture as in the U.S. including many shopping centers.

S.L: Last year when I talked to you, you told us that you were more and more emphasizing corporate governance. Have you seen improvements in this area since then?

I noticed in a recent issue of “Latin Finance”, you wrote:

“Despite some improvement in corporate governance standards in the last couple of years, a tremendous

amount of work has to be done to develop an equity culture in Latin America.” Any comments?

Mobius: Yes, there have been improvements, but they have been slow. Here in Brazil, they have had some regulations that require companies to have “tag-along-rights” i.e. if the majority shareholders sell shares they will have to bring along the others at the same price. That is a giant step for Brazil as many times minority shareholders get a short shrift when a company is sold and the majority shareholders sellout at big premiums and the minority shareholders were left “holding the bag” at a lower price.

S.L: That sounds not too far from what has been happening in the U.S. in the last few years. Have you seen that happening worldwide?

Mobius: Yes, but I have seen changes. The most important thing is that the whole issue has become more salient, as people have become more aware of this corporate governance issue. Now, when you go into a company, the first thing they talk about is what they are doing about corporate governance.

S.L: Fascinating! The Worldwatch Institute writers also express a lot of concern about dwindling supplies of fresh water around the world, particularly water used for agriculture. Do you see much of this in your travels?

Mobius: Yes, water is definitely an issue. That is why in China the Three Gorges Project is an irrigation project as well as a power project. The water issue is global.

S.L: Has anyone been fighting any wars over it yet?

Mobius: Yes, it’s possible. In the Middle East, Turkey controls the source of the Tigris and Euphrates running into Syria. They haven’t come to blows yet but have been close. These are very touchy issues.

S.L: We have been trying to follow the steady proliferation of cell phones around the world. My research finds that in just 10 years these devices have rocketed from less than 1 percent to 18 percent or 1.4 billion total. This is more than 1.10 billion with a conventional phone line and more than 90 percent of countries now have a network, led by the Philippines which leads the world with text messaging via cell phone. In Africa, cell phones outnumber fixed line phones more than on any other continent. The small size of the phones makes them easier to discard than computers. Are you aware of this as you go around the world?

Mobius: Yes, one of our largest investments is China Mobile. We see that everywhere. Often a first phone is a mobile phone rather than a fixed-line phone as cell phones are getting cheaper and with pre-paid cards so they can easily reach the poorest people. This is especially true in China and India where you will see a hawker on the street pulling out his cell phone. They are definitely becoming a universal status symbol.

S.L: As they are not disposable, they are plugging-up the environment. Are you aware of that problem?

Mobius: Yes, it is getting that way as people are changing their cell phones every year. I have worked my way through four or five in three years. The worst environmental fear will be the replacement of the cathode ray tubes from old TV sets as they are converted to flat panel sets worldwide.

S.L: Very true. To change the subject, we have been concerned about some of our investments in Russia because there is so much dependence on oil there. Do you think they will be able to diversify away from that dependence?

Mobius: Slowly, but surely. The problem is that oil is so profitable. It is not only the oil, but they also have diamonds, iron, nickel, and so forth. It is difficult to get away from this when they are making so much money, but I think what you are seeing now is a gradual shift in the composition in the industrial sector in Russia towards more consumer products. We have invested in a few companies such as in those making tires, one in fruit juice, dairy products and a beer company—companies growing at a pretty good pace and will continue to do so as the consumer market expands. However, when you compare them to the oil companies, there is not much comparison.

S.L: Do you have any new or more promising countries or regions where you are investing?

Mobius: I wouldn't say new, but if you look at the whole situation, you would have to focus on Brazil, China, India, South Africa and Russia. Those five are the countries that we should be focusing on from a long-range point of view. The emerging markets are back but will continue to be volatile. I would say that they are like teenage countries; you have to be ready for the bumps and problems along the way, but generally speaking, things are looking very good.

S.L: That is the Templeton way. Thank you for your time, Mark

(Worldwatch publications are available at www.worldwatch.org and The Franklin/Templeton Investments website www.franklintempleton.com).

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