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THE SCOTT LETTER is intended to educate global investors about closed-end funds. Closed-end funds can be a valuable and profitable investment tool. To learn about closed-end funds, visit our web site, www.CEFAdvisors.com, and in particular, read our article, *What Are Closed-End Funds*. Feel free to forward this newsletter to anyone who you believe could benefit from information on closed-end funds or global portfolios.

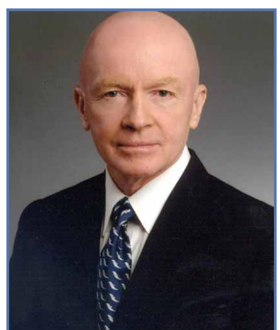
– George Cole Scott
Editor-in-Chief

IN THIS ISSUE:

Interview with Dr. Mark Mobius of Franklin Templeton Investments: Templeton Emerging Markets Fund Has Record Year

In 1987, Dr. Mark Mobius became a pioneer of emerging markets investing. He is managing director of Templeton Asset Management Limited and, as of September 30 2005, is responsible for over $20 billion of assets under management. He currently directs the analysts in Templeton's emerging markets offices.

Dr. Mobius and his developing markets team have professionals in 28 countries, including South Korea, China, Singapore, Poland, Russia, Turkey, India, South Africa, Brazil and Argentina. They typically venture to some 40 countries a year, visiting nearly 1,200 companies. Most of the analysts are natives of the areas they cover, and they provide a unique perspective on opportunities for investments.



Dr. J. Mark Mobius

Dr. Mobius has spent over 38 years working in Asia and other parts of the emerging markets world. He manages both mutual funds and closed-end funds, including Templeton Emerging Markets Fund (EMF-NYSE), Templeton Dragon Fund (TDF-NYSE) and Templeton Russia and Eastern European Fund (TRF-NYSE).

[Note: For more information on the geographical breakdown of these closed-end funds, see table on page 2. Clients of Closed-End Fund Advisors hold shares in TDF and EMF, including the accounts of George Cole Scott and his family.]

Dr. Mobius, who holds Bachelor and Masters degrees from Boston University and a Ph.D. in economics and political science from MIT, is the author of three books: *The Investors Guide to Emerging Markets, Mobius on Emerging Markets* and *Passport to Profits.*

We interviewed Dr. Mobius by telephone on December 14, 2005. He had been traveling in Asia and was in Bangkok when we reached him.

SL: Good day, Mark. It is wonderful to talk with you again. What time is it there?

Mobius: It is 8:00 in the evening. I just arrived here late last night from Hong Kong.

SL: We will talk about the WTO meeting Hong Kong in a few minutes. My first question regards your views on the value of company visits, something you do often, in order to keep up with economic and political changes in emerging markets countries.

Mobius: Traveling to foreign nations and visiting companies is one of the most valuable ways to gain reliable information about a firm. It is very helpful to get an inside view of companies on the ground and also to see what problems and opportunities these companies are facing in person.

SL: We don't know of anyone else who does it the way you do. That is "The Templeton Way." Now, tell us if you see the world as more or less secure as we approach the year 2006 versus your view when we spoke a year ago?

Mobius: I see a world that is a lot more secure because the political instability in many countries we visit seems to be getting better and better with wealth coming into play. As per capita income increases, people feel more secure than they did many years ago.

SL: That's good to hear. Now, what kinds of economic changes do you see for 2006? What is the upside and downside?

Mobius: The big change is the tremendous increase in foreign reserves in the emerging markets countries. The trade balances are much better. This has led to better credit ratings. The interest rate spread between emerging markets debt and U.S. Treasuries is even narrower than last year, which is the most significant thing in the last few years. It is directly and inversely correlated to the Emerging Markets Stock Index. As that spread comes down, indicating that people are more confident, they are willing to put more money into the stock market. So, a lower spread means higher emerging markets stocks.

The downside is that there is (more) risk in investing in emerging markets. There could be backtracking. One good example is the WTO negotiations that took place this week in Hong Kong. If these negotiations are not successful over the long term, emerging markets (nations) could be hit since their growth is dependent on a free trade environment, while there is a lessening of protectionism and subsidies. If this does not succeed, it will be a problem going forward.

SL: We agree that free trade must replace all forms of protectionism. This reminds me of the time I visited Sir John Templeton at his home in Nassau and asked him about free trade. His reply was: "That helps everybody."

A recent *Wall Street Journal* report says that Russia, Ukraine and Vietnam hoped to join the WTO this year but are pushing back their targets until next year at the earliest because of frustration over the process of joining. Anger is building in these nations as they say it is unfair. How about that?

Mobius: It goes with the territory and will take time. I have no doubt that Russia will join and Ukraine will do the same, but I doubt that anything can be done soon.

That is why it is so distressing to see the Hong Kong protestors who don't realize that free trade does help everyone. People have to adjust. It is a "win-win" situation.

SL: In the emerging markets, we have seen large rises for three years now in the markets you cover. How long do you think this will continue? If so, why?

Mobius: That is a very good and very significant question. When people see these kinds of rises, they have to ask how long will this go on? The answer comes when you have to look at the fundamentals: the price-earnings ratios, price-to-book-value ratios and price-to-cash flow (value investing measurements). The indicators that we are seeing show that these markets are still cheap as earnings have kept up with the growth. The emerging markets still have about half of the price-earnings ratios of the book value of the U.S. where book values are higher.

It is difficult to see if the markets are topping out. There will be corrections along the way, but what is keeping the markets at a level – not moving up at a crazy pace – is the fact that many are issuing new initial public offerings, especially in China. We estimate that the number of IPO's in the emerging markets will be at least four times the pace of last year. This should mop-up all the new money that is coming in and keep prices at reasonable levels.

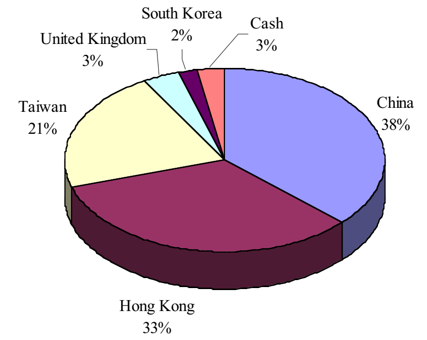
SL: Very interesting. What about the various projections we have seen over the years of emergence of the rising middle classes around the world? Where does this appear to be growing the fastest?

Mobius: The most significant thing is this: The most populous countries in the world, China and India, are growing the fastest of any major countries. In these countries, population growth is about 1%, whereas the real GDP growth is running at 7% to 9%. This is very significant as per capita income is growing very fast. The rising population will be consuming more and will be building a better life for their children. China and India are both great exporters and importers. Growth in Asia has been driven by the Chinese engine, as China is a great importer from all over Asia. So, this is how China and India are the great engines for middle class growth.

[On December 20, China announced that the world's fastest growing major economy is even bigger than previously known. This is because the service sector is a larger part of the economy. This might prompt economists to revise their forecasts for the date when China might surpass the U.S. as the world's largest economy, according to media reports. For foreign investors, the Beijing government also announced that foreign investors will now be exempt from capital gains taxes. This puts Chinese regulations in line with sophisticated, successful markets in Asia such as in Hong Kong, Singapore and

Templeton Dragon Fund (As of 11/30/05)

Geographic Breakdown

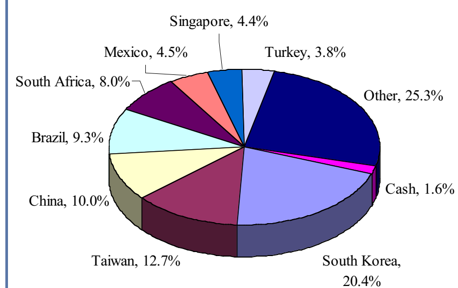


Performance

	NAV	Market Price
1-Year	17.25%	13.76%
3-Years	34.19%	32.84%
5-Years	22.00%	26.75%

Templeton Emerging Markets Fund (As of 11/30/05)

Geographic Breakdown



Performance

	NAV	Market Price
1-Year	29.02%	13.76%
3-Years	32.39%	32.84%
5-Years	19.56%	26.75%

Malaysia which don't tax capital gains on stocks.)

SL: When you take your profits in stocks that have reached your targets, are you able to see others that are undervalued in the same area?

Mobius: Yes, but the bottom line is that most of the stocks that we own have not reached our selling limits, so we are hanging onto a lot of them. In some cases, we are disposing of stocks that are up and beyond our targets. In those cases, we are able to find good substitutes. It hasn't been much of a problem as in previous years, when things got out of control. That is not happening now.

SL: That's good to hear. Have you shifted your focus in your search for bargains this year?

Mobius: No, because we are able to find good bargains with large and liquid stocks. That is quite significant. In the past, we have had to increase the number of stocks in our portfolios since the number of large-cap stocks got too expensive, so we had to move over into the small caps. Now, that is not the case. We are finding many opportunities among large-cap stocks. In the past, we had as many as 600 stocks in our portfolios; now it is about 120 to 130. That is a big change.

SL: Why is that?

Mobius: Simply because these companies have been able to increase their earnings nicely, and corporate governance has improved so we can concentrate our investments. One of the things we found in talking to companies around the world is their sensitivity to shareholders, a big improvement. They talk more about shareholder value and how they can serve their shareholders better.

SL: As you know, there have been many disruptions in 2005 caused by climate change, floods, earthquakes, typhoons, etc. Has this been a problem for you?

Mobius: No. We have the usual disruptions, but people are more concerned about the possibility of a flu "pandemic" that may be caused by the spread of the bird flu. But this time, there has been a lot of preparation. This had affected some markets, but it has been largely discounted by the markets. The World Health Organization has raised warning signals, but there is not much of a threat of it spreading like the previous flu.

[A recent report in the *Wall Street Journal* confirms this by saying that China has declared initial success in controlling the spread of bird flu, but there is still a chance of outbreaks during the winter and spring. China has embarked on a massive program culling 22 million birds and vaccinated 6.85 million domestic fowl in 2005 to prevent the outbreak. We have become aware that the flu has spread into Turkey, however. – Editor]

SL: Have you seen more concern in your travels for such things as energy and water conservation, and if so, where?

Mobius: China is facing a real shortage of energy and water. There is a pollution problem due to coal plants and their rushing to industrialize as well as the huge growth in the number of automobiles. They are using a lot more coal, which is creating all kinds of problems. China will have to work hard to solve this problem. There is a big improvement in cutting down pollution in Beijing because of the 2008 Olympics, but not yet in the other cities.

In India, the problem is their infrastructure. They are building roads, but the Indians have to move faster in this area.

SL: We see that your largest exposure in The Templeton Emerging Markets Fund has been in Korea. Do you have any concerns about this market going forward?

Mobius: We have some concerns about their "chaebols" (family-controlled conglomerates), their banks and possible changes in capital gains taxes. However, we remain fully invested in Korea because of the so-called "Korean discount," which exists because of the perception that the big chaebols may transfer assets from one group company to the other without knowledge of the minority investors. However, attitudes have changed. There is a move towards reform in the system.

[The Korean Ministry of Commerce, Industry and Energy announced on January 2, 2006 that growth in South Korea's exports slowed in 2005, and the trade surplus narrowed because of the rise in international oil prices. However, oil prices have now declined, and China has increased its purchases of Korean products by 24.8% in the January 1, 2006-December 20, 2006 period, a trend that is expected to continue. – Editor]

SL: Turning to another region, there has been a lot of concern that Brazil may be overvalued and whether they will succeed in their growth plans under President Lula. What is your assessment of this market now? Your allocation to the country is still large (8.8%) relative to the others.

Mobius: There is concern, but President Lula has done better than anyone expected. The main interest was to ensure that inflation did not rise. They were willing to raise interest rates to cut inflation and have succeeded. A lot of fears didn't come true. In addition, the Brazilian companies are doing well. The market is not overvalued yet, and their companies are on a par with other major emerging markets companies. They are, therefore, in great shape.

[The Brazilian treasury has just announced that Brazil will pay-off its remaining $2.6 billion debt to the Paris Club, an informal group of creditors who coordinate plans for debtor nations to resolve their payment difficulties, in January 2006, a year earlier than planned. This will improve the country's debt ratings. – Editor]

SL: Good. We may be adding to our exposure there, using regional rather than single country funds for the investment. We have also noticed that your exposure to Mexico appears to have lessened. Is that related to the upcoming election in July?

Mobius: We have reached some of our price limits, but there has been no reduction (in our investments). As some of our markets came up, it looked like a reduction in percentage terms, but we didn't really reduce (our holdings). Politically, there is concern about the reforms, but I don't see them going backwards, so there is a general move in that direction, which is good. Regarding the election, it will be important if the candidate, Mr. Obidor, keeps up his lead for President; and if elected, he will shake-up the status quo, but this may pose a hazard for fiscal discipline. Everyone is convinced that Mexico needs a new path of growth. It will be very interesting to see how it develops.

[Mexico's stock market has hit highs more than 40 times in 2005 and rose 37.81% by year-end, tripling in value since President Vincent Fox took office in 2000. But, reports show that this is at odds with economic growth, which has dropped to 3% in 2005 from 3.5% in 2004. The government's forecast is predicting a return to 3.5% in 2006 although it may be insufficient to create enough jobs for millions of Mexicans entering the work force. – Editor]

SL: Turning to Eastern and Central Europe, we read in a business report that outsourcing in this region is growing faster there than in any country besides in China and India. The report says India in particular is slowing down. The Eastern Europeans are a highly-educated and hard working class of people. Do you have any thoughts on this?

Mobius: Yes, in fact, Franklin/Templeton has some outsourcing in Poland. The region is growing, but it is not anywhere what the Indians are doing where the outsourcing is incredible. Nevertheless, the East Europeans are doing much more work for the Western European which has wages about a quarter of what they are in Europe.

SL: What about the merging of the Eastern European countries into the European Union? Do you see it moving forward in 2006?

Mobius: The new members have been good and bring fresh air to what is happening. Ukraine and even Turkey are right in line to join, in spite of some problems. Whether Turkey gets into the European Union or not is not relevant. What is important is they do the reforms that the European Union is asking them to do. That will make a tremendous difference to their country. They will have all the benefits of these reforms. That is very critical, in my view.

SL: Is there much outsourcing in Russia?

Mobius: In Russia they are good at computer software work. It is not huge, but it is growing. The reason why the stock markets in Russia have done so well is because they have produced good managers and good profits (for shareholders).

SL: I remember that you have had a long interest in concern for minority shareholders and other corporate governance issues. What is your latest assessment of the progress of the corporate reforms in Russia?

Mobius: The oil industry has produced tremendous wealth for Russia so they have built-up very large oil reserves, taking a lot of pressure off the economy. The big question is where to go next in terms of government control of the oil industry. Up to now, it seems that they will keep control of Gazprom and the pipelines, but it will probably not be going much further than that. If so, that would be very good. They have built pipelines to the Caspian and the Mediterranean. They also want to build a pipeline under the sea to Germany. With its huge land mass, large population and abundant natural resources, Russia could become one of the fastest-developing economies, attracting a great deal of long-term capital.

SL: A final question: Are you expanding your investments into any new areas such as the Middle East?

Mobius: In fact, I am heading to Dubai next, where we have an office, and Kuwait to see if there is anything of interest in those countries.

SL: This has been very interesting and informative. We hope that it will help our rapidly growing number of readers understand the emerging markets better. Now, it is time to wrap it all up. What are your summary thoughts about the emerging world?

Mobius: I think it is going very well. People have begun to economize. More supply is coming in, and the bottlenecks are being fixed so things are shaping up very well for 2006.

SL: Thank you for your always excellent insights into the emerging markets.

For more information on Franklin Templeton Funds, call 1-800-342-5236 or visit www.franklintempleton.com. ■

A Better Way To Go Abroad

"With U.S. Stocks stuck in low gear for two years now, traders have had little choice but to search the globe for opportunities," says a recent report in *Business Week.* The Dow Jones World Index (ex-U.S.) jumped 20.14%% in 2005, while the S&P 500 Index only gained 3% (36 points) for the same period.

During the same period, the international indexes in the Asia-Pacific region increased 21.6%, (54% in Korea alone), 37.8% in Mexico, 27.7% in Brazil and 101.4% in Russia. As a result, we expect to achieve better returns.

Despite the recent rally in foreign stocks, especially in the emerging markets, the foreign markets are still cheaper than the U.S., according to analysts. This has been confirmed by our interview with Dr. Mobius.

The magazine says there are only three ways to invest globally. (They ignore closed-end funds.) First, there are proxies for foreign stocks called American Depository Receipts or ADRs. However, these only cover a small fraction of publicly traded companies around the world because of strict listing requirements.

Secondly, mutual funds mostly target broad regions, are priced just once daily and have redemption problems where local blow-ups spread quickly.

Finally, there are the fast growing exchange-traded funds or ETFs, which are baskets of stocks that typically trade close to market indexes and are bought and sold throughout the day. They have low expenses, can be sold short and are growing dramatically, much faster than closed-end funds. The downside for ETF traders is the high transaction costs, they rarely trade at discounts to net asset value and, unlike closed-end funds, they pay out little in distributions.

On the other hand, "sales" of closed-end funds cannot be tracked, because they are publicly-traded like stocks. Our position remains that we may find a place for ETFs in our portfolios at times where we cannot find an equivalent CEF selling at a discount, but ETFs still have limitations for investors. When one of our funds rises to a premium over 5%, we are likely to put the assets into a mutual fund at net asset value with the same manager rather than choose an ETF. Enough said. ■

H&Q Healthcare Investors Reports Record Year

To the Shareholders of H&Q Healthcare Investors:

On September 30, 2005, the net asset value ("NAV") per share of the Fund was $19.65. During the twelve month period ending September 30, 2005, total return at net asset value of your fund was 17.54%. During the most recent six month period ended September 30, 2005, total return at net asset of your fund was 17.62%. The total investment return at market was 11.56% during the twelve month period ended September 30, 2005 and was 19.12% during the six month period ended September 30, 2005.

A number of positive developments occurred in the healthcare/biotechnology sector during the six month period ending September 30, 2005. These events included clinical results, such as those reported by Genentech for its Herceptin, Avastin and Lucentis drugs as well as financial results reported by Genentech at the end of the second calendar quarter. Merger and acquisition activities such as the acquisition of Vicuron by Pfizer also buoyed the sector.

These positive events helped to offset negative sentiment that had developed in the prior period after health care sector-related events such as the removal of Vioxx and Tysabri from the market. We believe that these more recent positive events helped to catalyze the upward movement that has occurred in the biotech sector over the last six months.

Despite uncertainties (at the FDA and in the Gulf Coast area), we continue to be impressed by a general trend demonstrating the benefits that new drugs appear to be having on patients with a wide range of diseases including cancer, diabetes and hypertension. In the immediate and longer term, we are in an age where we are continuing to see that individual drugs or combinations of agents have an impressive impact on the course of a number of diseases.

– Daniel R. Olmstead
President

Portfolio Manager's Review

As the New Year 2006 begins, the financial press and TV media deluge the public with stock market predictions, mostly by journalists who don't manage public money. As a former financial writer for newspapers, I remember that they always try to make predictions about the course of stock markets, a futile job at best.

We never make predictions about markets, instead we just look for value for our clients and, influenced by John Templeton, we continue to diversify into the world markets to reduce investment risk. This approach has paid-off as we have outperformed the U.S. benchmarks in 2005 again by a wide margin.

We use the interview with portfolio managers to help us pick superior investments for our clients. In October, we decided to reduce the U.S. portion of client portfolios to 25% from 30%, increasing the foreign sectors, both in the international equity funds to 35% and the real estate sector to 25%.

In December, we sold funds according to our annual re-balancing process. The funds realized are being re-allocated into funds showing better value. As a result, the U.S. sectors will be more concentrated into the older funds that have consistently performed over the years, while increasing the foreign and real estate allocations.

We also will be dividing the foreign equity funds into two categories: the first in the developed markets, which in 2004 were limited to two European funds, The Europe Fund and the now more diversified European Equity Fund. The rest of the global portfolios will be concentrated in the emerging markets. For performance purposes, however, the Dow Jones World Index (ex-U.S.) will be maintained as a benchmark for all the foreign equity investments.

At year-end, we decided to take what tax losses were significant enough. However, as in past years, very few of our investments in closed-end funds showed losses, due to another good year of overall performance. An exception was TCW Convertible Growth and Income Fund, which stretched their dividends too far and may have had to pay a return of capital in the 2005's weak bond market environment in which its net asset value declined significantly. The other sales were in redeeming some shares of the Cohen & Steers Realty Shares Fund, a mutual fund, in order to buy the Cohen & Steers Worldwide Realty Income Fund (RWF-NYSE) as well as adding some of the Cohen & Steers domestic funds. We also reduced the positions in Lazard Global Total Return & Income Fund (LGI-NYSE).

As the year ended, we held over 5% in cash for investment opportunities. We also have been getting new money from old clients, and new ones are joining us. We always tell new clients that we may take as long as six months waiting for the best prices before fully investing their funds.

Our investment focus in 2006: the emerging markets. We now have nearly every client in The Templeton Emerging Markets Fund and will continue to buy it when a discount appears as well as adding to other funds that are in the emerging markets. One example is The Templeton Developing Markets Trust (TDMTX), a load fund which can be to purchased at net asset value, choosing the "C" shares. The expense ratio is higher, but when EMF again trades at a discount, as it did earlier in 2005, it may be prudent to switch back into this fund.

Long-term readers remember that we have focused on a new region each year: Asia, Latin America and last year Western Europe. Even though many of these markets have appreciated significantly, we still are adding to their shares on weakness. Our focus will, therefore, not be confined to one region in 2006 but will emphasize funds in the emerging markets where opportunities arise.

In the next few months, we plan to interview the managers of the three closed-end funds managed by the Deutsche Bank Group: (1) The European Equity Fund, which invests primarily in companies domiciled in European countries that utilize the Euro currency; (2) the New Germany Fund and (3) the Central Europe and Russia Fund, which invests in Central European and Russian companies.

We also plan to again interview the manager of the Asia Pacific Fund, one of our top performers. We see these manager interviews as the best way to help us pick the right funds by speaking directly to their portfolio managers. They also help us to understand the markets or regions in which to invest.We find that there are many investment opportunities for 2006. ■

George Cole Scott

2005 Distributions of Closed-End Funds Portfolios Being Paid in 2006

A number of closed-end funds have declared their year-end distributions, but the payments are not being made until 2006. They are taxable in 2005, however. This is something all shareholders of closed-end funds need to watch. The following list contains funds that were held in CEFA portfolios on the ex-dividend dates: Allied Capital, Asia Pacific Fund, Latin America Discovery Fund, Latin America Equity Fund, Templeton Dragon Fund, and Templeton Emerging Markets Fund. ■

Questions Or Comments?

The editor of The Scott Letter is interested in any questions from you, especially now that we have so many new readers. Please e-mail your questions or comments to us at CEFA@CEFAdvisors, or write to us at P. O. Box 1100, Richmond, VA 23218. We cannot promise that your questions will be published in ***The Scott Letter,*** but we may find room for portions of them. We look forward to any comments that may help us serve you better as well as help you in your investment portfolio. ■

The closer one gets to the top, the more one finds there is no "top."

– Nancy Barcus

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