John Templeton, aged 95, passed away yesterday. He will be greatly missed. Templeton was a legendary contrarian investor and a tireless philanthropist.

In February of 1987, the Templeton Emerging Markets Fund debuted on the New York Stock Exchange. Very few investors in those days cared to dabble in emerging market stocks. And after the stock market crash in October of that year, even fewer investors cared to dabble in emerging market stocks. The Templeton Emerging Markets Fund, which traded around $14 at the end of its first trading day, slumped to $6 by the end of the year.

Sir John Templeton would not have had it any other way. This uber-contrarian seemed to relish adversity. He built a career – and a fortune – by investing during what he called "the moment of maximum pessimism." Your editor's father embraced this same philosophy with a passion. In the nervous days of late 1987, he purchased a few hundred shares of the Emerging Markets Fund and gave them to his son, your editor.

Although delighted to receive a gift of cash in any form, your editor was not so sure he wanted to continue holding this quirky, and somewhat boring, stock. So he held it long enough to make a few bucks, then sold the stock to purchase the shares of a small drug company that eventually went bankrupt. And so began your editor's costly education in the art, science, misery and luck of investing.

But fortunately, the early days of this education began with John Templeton. Your editor may have abandoned the Emerging Markets Fund a bit too early, as the nearby chart painfully illustrates, but he did not abandon the principles of John Templeton, at least not intentionally. In fact, he tried to get a job working for the man...
Sometime during the late 1980s, your editor was studying theology at Pepperdine University, but he was also actively investing in the stock market "for fun." Not knowing therefore, whether he wished to pursue a career that focused on God or mammon, he endeavored to do both at once. So he sent an awkwardly worded letter to John Templeton asking for some kind of job somewhere in Templeton's organization, whether on the charitable side or the investing side.

A few days later, a handwritten letter arrived from Sir John Templeton himself. I don't remember exactly what the letter said. But I remember that the letter contained genuine words of encouragement, even though it did not contain the words, "You're hired." Mostly, I remember the utter shock of receiving a handwritten letter from one of the world's most successful investors.

Sir John could never have known how that one little handwritten note would influence the recipient. That one little handwritten note inspired me to pursue a future that resembled John Templeton's. I would not suggest that I have succeeded. But I have managed to purchase a handful of exotic foreign stocks during the last twenty years and I have learned a thing or two about buying stocks when nobody else wants them. As for the "billionaire philanthropist" component of the John Templeton story, I'm still working on that.

In 1972, Sir John established the Templeton Prize to honor "a living person who has made an exceptional contribution to affirming life's spiritual dimension, whether through insight, discovery, or practical works." The Prize aims, in
Templeton's words, to identify "entrepreneurs of the spirit." Mother Teresa was the very first recipient…six years before she won the Nobel Peace Prize. "What we say about investing," Templeton once remarked, "isn't as lasting as what we say about spiritual matters."

So you tell me, was John Templeton a legendary investor…or simply a legend? Our colleague, Chris Mayer, offers a few additional remarks about Sir John Templeton:

"When I think of Templeton's influence on me, I think of two things: his willingness to invest abroad and his belief that people focus too little on the opportunities problems create. Templeton was perfectly comfortable exploring the stock exchanges of South Africa, Japan, Switzerland, Australia and plenty of others too. He helped drive home the idea that quality investments don't have to mean well-known, large, blue chip, U.S. companies. He sort of prided himself on people not knowing a third of the names in his portfolio.

"He was sometimes seen as an optimist, because he had a strong belief that investors generally pay little attention to the opportunities problems create. In a recent foreword, which must be the last thing he published, he called the present time one of "great hope and glorious promise, perhaps a new golden age of opportunity…" which seems remarkable given all the bad developments in recent years. But, it's perfectly understandable given Templeton's worldview. I think this is a very important idea, more so now than ever. It's easy to get scared out of the market, but times like this are when you plant the seeds for your next big winners.

"Finally, I also think his own story is an inspiring one. He grew up relatively poor in Winchester, Tenn. He was studying at Yale when his father could no longer afford to pay to keep him there (this was the Great Depression) and so he worked, earned scholarships and – so legend has it – played lots of winning poker to put himself through school. He also made a famous big bet on U.S. stocks in 1939, buying $100 worth over every stock on the major exchanges selling for less than $1 per share. He turned $10,000 into $40,000 in 4 years. He kept on winning, compiling a great and long track record.

"One of the best of all time."

Just two weeks ago, as faithful Rude readers may recall, Chris shared one of Sir John's final investment ideas. For those who may have missed this excellent column the first time around, we offer it up a second time…

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God Bless John Templeton
By Chris Mayer
"I'm approaching my 95th birthday," Sir John Templeton, the great old investor writes in the foreword to a new book about his methods put together by his great-niece (Investing the Templeton Way). The short foreword has some words of advice. One that stuck with me: "Throughout history, people have focused too little on the opportunities that problems present in investing and in life in general."

I think that is true. Water crisis, energy crisis, food crisis, whatever... There are always opportunities on the other side of these things. That's why I started my investment letter, Capital & Crisis 2004, and that's the idea I had in my head when I came up with the newsletter's name.

A crisis is an opportunity for you to put your capital to work. At least, that's what the greatest investors have always done.

If anyone knows about the relationship between trouble and profits, it's Templeton.

Templeton spent in his young adult years in the Great Depression, which surely left its marks on his psyche - as it did on many others'. Templeton, for instance, paid cash for his first house. He never had a mortgage and never borrowed money to buy a car. These thrifty attitudes carried over to his investing style. He gravitated toward cheap stocks. As a result, he was a buyer during the Great Depression, when most people wanted nothing to do with stocks.

Templeton picked up many steals. For instance, he bought shares of Missouri Pacific Railroad for 12.5 cents per share, selling them some years later for $5 per share. He had many other successes.

But out of all that, Templeton’s fame may rest more on the fact that he was something of a pioneer when it came to investing overseas. The early success of his Templeton Growth Fund in the 1950s was, in part, due to his early identification of overseas opportunities.

Among those opportunities was Japan, a market he rode to great riches - and which he also exited before it all fell apart in the late 1980s. He first invested there after World War II.

Today, Japan is an economy with lots of problems. It is not at all like the war-torn nation of the 1950s, but it's suffered through years of bear markets and other economic setbacks. Today, reflecting all that ill sentiment, the Japanese market hovers near two-year lows.

That's just the way a Templeton-style investor likes it. Templeton liked to invest when there were few interested buyers, during times of "maximum pessimism,"
as he liked to say. Japan must fit the bill. And there are interesting opportunities here…

Japanese small caps trade at price-to-earnings ratios not seen since 2003. And about 53% sell for less than book value. About 15% sell for less than net current assets, a rare financial sight not seen in great numbers on our shores since the Great Depression. The so-called Jasdaq, a Japanese equivalent to our own Nasdaq, trades for only 12 times next year's earnings.

Cat Fund AG, in a recent note on Japan, opines, "Balance sheets of companies are the healthiest they have been in the past 40 years." Cat also points out that the dividend yield on stocks is now higher than the 10-year Japanese government bond yield. This has, in the past, signaled a bottom. "This situation," Cat notes, "[also] occurred in 1998, 2003, 2005 and was usually followed by a rising market in the following months."

Japanese management teams seem to realize their shares are awfully cheap. Companies are buying back stock. For the 12 months ending March 2008, there was some $46 billion in stock buybacks. This is something Japanese companies don't usually do much of, preferring to sit on cash or waste it on uneconomic projects.

Perhaps more important than the lively buyback market is the anecdotal evidence from investors working that market. Symphony Financial Partners has found even more compelling values than the surface statistics indicate. Witness the case of Nippon Ceramics. Symphony reports that at one point in March, it traded for 90% of cash in the bank and half book value. All while still earning 20% pretax profit margins. Again, you just don't find those kinds of values in the U.S. markets.

There are a variety of ways to play the small caps in Japan. One is to buy the Japan Smaller Capitalization Fund or the Russell/Nomura Small Cap Japan ETF. Both of these funds can get you exposure to cheap Japanese shares. In my investment service, Mayer’s Special Situations, we’ve had some success in Japan. We own Kurita Water, which is up 87% for us - even though the Japanese market hasn't done much. We also recently picked up a cheap Japanese real estate company.

"The 21st century offers great hope and glorious promise," Templeton predicts, "perhaps a new golden age of opportunity." He can say that because where he sees problems, he also sees opportunity. I see lots of problems today, too… and many opportunities. Japan's small-cap market is just one interesting possibility.
[Rude Endnote: Lastly today, this is the final time we'll bother you with reminders about your chance to grab your $1,500 one-time dividend check from Agora Financial H.Q. The offer expires today at high noon.

Interested? Click Here. Not interested? You won't hear about it again after today.

Until next time...

Cheers,

Joel Bowman

The Rude Awakening

Attitude

At some time almost anything is likely to become a bargain, if you are in a position to evaluate the neglected factor that will change things for the better. To perceive this factor you have to wear glasses different from those worn by other who don’t like what they see. Templeton thinks that the investor needs this ability to recognize unfamiliar values more than any other skill. He calls it flexibility.

A flexible viewpoint is the professional investor’s greatest need, and will be increasingly needed in the future.

Always ask yourself whether a company is in an industry that is a natural candidate to be socialized.

Debt ridden real estate companies are good specs in an inflationary period.

Templeton removed himself from the hustle and bustle of Wall Street.

He has developed primary sources of information on companies and investments.

He studies the portfolios of other great investors.

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Everything has its season, which does not last forever. The world changes its spots, and the investor must change his. Change your approach, especially after a long run of excellent performance.
The cardinal rule is flexibility. You must get ready to change when everything seems to be working particularly well; when the cycle is perfectly in gear with your expectation, prepare to jump.

Don’t trust rules and formulas. Nothing replaces thinking.