



ASA Gold's Merk On How Precious Metals Will Respond In A Coming Recession

Friday, December 1, 2023

Chuck Jaffe, in this episode of The NAVigator podcast interviewed Axel Merk, chief investment officer for the ASA Gold and Precious Metals fund. Read the Q&A below as Axel says that gold prices are most tightly correlated to "the confidence the market has in the central bank to manage inflation over time," so gold's rally over the last six weeks, as well as its path forward, is "favorable because we might be entering a recession, most notably a recession that is more severe than is currently priced into the market." Merk says he does not foresee a soft landing for the economy, he sees a decline that is more significant than most observers are expecting, which is why he does not think "we are going to have the trajectory [for gold] that is priced in right now."



Axel Merk

The podcast can be found on AICA's website by clicking here: <https://aicalliance.org/alliance-content/pod-cast/>

CHUCK JAFFE: Axel Merk, chief investment officer at the ASA Gold and Precious Metals Fund is here, one thing we know he'd say about himself, "I love gold!" Oh yeah, and we're talking about that now on The NAVigator. Welcome to The NAVigator, where we talk about all-weather active investing and plotting a course to financial success with the help of closed-end funds. The NAVigator is brought to you by the Active Investment Company Alliance, a unique industry organization that represents all facets of the closed-end fund industry from

users and investors to fund sponsors and creators. If you're looking for excellence beyond indexing, The NAVigator is going to point you in the right direction. And today it points us in the direction of Axel Merk, who is chief investment officer at the ASA Gold and Precious Metals Fund. It is a closed-end fund that, oh, by the way, started in the 1950s, that Axel got involved with a few years ago, and you can learn all about it at ASALtd.com. Axel is also the president of Merk Investments and the Merk Funds, and by the way, he will rejoin us on Money Life next week where we will have him in for a big interview and talk about much more than just gold. Beyond checking out ASALtd.com, if you want to learn more about closed-end funds, business-development companies, and interval funds go to AICAlliance.org, the website for the Active Investment Company Alliance. Alex Merk, great to chat with you again.

AXEL MERK: Great to be with you. What an introduction.

CHUCK JAFFE: Well, let's talk about gold and where you see things headed right now, because we've been in this high-inflation environment where gold has not worked as an inflation hedge, but it has worked a little bit as a socioeconomic/political hedge. And so here we are entering into a time where inflation is starting to calm down, at least a little, and folks are expecting some changes in rates going forward, but yet we're also going into political turmoil and an election year in this country, and we've got political turmoil around the globe. So what is the role that you think gold should be playing, and how well is it playing that role now?

AXEL MERK: First, let's take a step back. Gold does not change, it's the world around it that changes, and one of the beauties about gold is that there is fairly little industrial use and so it just is. And I sometimes say it reflects the mania of policy makers, it reflects what happens around the world. And so if you're asking me, "Oh, what's going to happen with the price of gold?" we have to look at you're talking about inflation, right? Just like any asset, it is not priced on what is happening, it is priced on the perception of what will or might be happening. Might might be the better term, because even if you're right of what will happen tomorrow, tomorrow's price is going to be what people think will happen the day after. And so when you talk to me about whether gold and inflation have a relationship, gold isn't really correlated to most things, the one thing it is more correlated to other things over time is real rates, and not about short-term rates but long-term real rates. Now before all the gold bugs pile in and say, "We have no idea what long-term real rates are," that's [inaudible] by the

way, on a 10-year basis what will inflation be in 10 years? It doesn't matter what rates will be in 10 years, it matters what the market's perception will be. And to talk a little bit less abstractly, it is a reflection of the confidence the market has in the central bank to manage inflation over time, so that is what the price of gold is reflecting with regard to inflation. And so when the Federal Reserve says, "Hey, I'm gonna beat up everybody and we're going to be hawkish," then that has an impact on inflation more so than what today's CPI is.

CHUCK JAFFE You started that answer talking about how gold kind of reflects the mania of politics and all the rest. Given the situation that we have right now, do you believe that gold is properly priced for the situations we're facing around the world?

AXEL MERK: Being humble, I first like to understand why it's priced a certain way, and indeed I just talked about real rates, indeed real rates have been going up and for that gold has actually held up quite well. So based on that framework, there must be other drivers, and other drivers might be the typical gold buyer is concerned about the purchasing power of the dollar. So why would the dollar potentially weaken, and inflation is one reason, future interest rate path is another one, deficits is another one, and we are in an economic time where usually it would have less of a deficit, so that's one. Then you also have a different type of buyer of gold sometimes, most of the time actually, that is the diversification buyer. In 2022, diversification in very few assets worked, but this year gold has worked as a diversifier, and most of the time it does. That buyer has been active. You have a speculator sometimes active in gold, that type of buyer has been absent, they are in meme stocks in the like. But then somebody unique to gold is central banks, central banks have been buying, in part because central banks are a little more reluctant to buy the US dollar when they are part of countries that are not all that friendly to the US, and so that's been pushing it higher. I'm mostly a humble observer of the price of gold, I do think that we're currently in a phase where the path of gold in the coming months is favorable because we might be entering a recession, most notably a recession that's more severe than is currently priced into the market, which if that is the case, would be potentially favorable to the price of gold.

CHUCK JAFFE: You also run the VanEck Merk Gold Trust ETF, that's OUNX, and of course one is gold equities and one is gold. Right now would you rather be owning the precious metal or would rather be holding the equities in gold companies?

AXEL MERK: They're different dynamics. Let's talk about here the ASA since you started out with that, in the gold mining space, that is of course different. The gold miners have done far worse than the price of gold, at least in the context of what you might think gold miners should do. And part of the reason is, and ASA in particular focuses more on the junior sector, we help institutionalize some of the exploration companies and provide funding to them, and in some ways those companies are credit plays. And so aside from the price of gold, the availability of credit in the market is relevant for these, they need to get financing rounds done once a year, once every other year, and anybody's who'd paid attention to the market knows that financing conditions have been tight. And what's unique about the gold space is that historically when a recession starts, even though general financing conditions are tight, those junior gold miners have access to funding. And the reason is that there's the assumption, and often the reality, that the Federal Reserve will lower rates quite sharply, and that will first give money to the gold miners and then they get into disproportionate gains. What's unique about this turn of course, is that we are in this quote/unquote "higher for longer" environment, and so it remains to be seen whether we have the cuts that are priced in or more severe ones. So if you think we'll have a more severe recession, then the gold mining space in my view is going to do very well. If you think we're going to have a super subtle soft landing, then the market may look through that and the gold miners might not get the sort of boost that they typically get in a recession.

CHUCK JAFFE: And I want to make it clear, you do not think that we're going to have this super soft, subtle landing?

AXEL MERK: I cannot see how that is possible. The argument in favor of that is this immense stimulus we have, and the system is evidenced by the deficits. That said, we have most of the parameters that are part of a slowdown showing their face, delinquencies are going up. You have for example college loans, the repayments starting October 1st, which has an impact on especially the low income group. And in particular you have the tightness in the credit conditions, where the Federal Reserve committed to staying tight, and because Fed policy acts with a lag, at the time when they start lowering rates you're still going to have ripple effects going forward. And so there is going to be a further downward momentum, most people, not everybody agrees that we are in somewhat tight conditions right now. And so if you just extrapolate from that, I don't think how we're going to have the trajectory that's

priced in right now, but obviously the market is always right and what am I to say? And then of course the thing is everybody thinks we're going to have a soft landing until we have a hard landing, so I'm not predicting a 2008 equivalent but I do think this is going to be far more significant a downturn than what the market as a whole is thinking right now.

CHUCK JAFFE: Axel, I have a lot of follow-up questions. Unfortunately I don't have time, at least not here. I have some time next week where we'll be talking on Money Life, I look forward to that one already. Thanks so much for joining me today on The NAVigator.

AXEL MERK: My pleasure.

CHUCK JAFFE: The NAVigator is a joint production of the Active Investment Company Alliance and Money Life with Chuck Jaffe. And yeah, that's me, why don't you check out my hour-long weekday show on your favorite podcast app or by going to MoneyLifeShow.com. And if you want to learn more about interval funds, closed-end funds, and business-development companies be sure to check out AICAlliance.org, the website for the Active Investment Company Alliance. They're on Facebook and LinkedIn @AICAlliance. Thanks to my guest Axel Merk, he's chief investment officer at the ASA Gold and Precious Metals Fund, that's a closed-end fund that you can learn more about at ASALtd.com. He's also the president of Merk Investments and the Merk Funds. The NAVigator podcast is new every Friday, be sure not to miss an episode by subscribing or following along on your favorite podcast app. And if you like this podcast, please leave a review for us and tell your friends, because that stuff really does help. We'll be back next week, and until then, happy investing, everybody.

Recorded on December 1, 2023

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