



Axel Merk On The Broader Impact Of An Activist Investor's Approach

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Chuck Jaffe, in this episode of The NAVigator podcast interviewed Axel Merk, chief investment officer of the ASA Gold and Precious Metals. Read the Q&A below as Axel and Chuck discuss the impact that Saba Capital Management is having on the fund and on shareholders as it entered the fund as an activist, moving to change the board as it pushes for a double-digit discount to be narrowed. Merk discusses the challenge of dealing with activist investors in a junior mining fund, the potential for the fund to be liquidated, the possible outcomes, and the impact of the



Axel Merk

action on shareholders.

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CHUCK JAFFE: We're talking about how closed-end funds manage activist investors with Axel Merk, whose closed-end fund is squaring off with them now, this is an unusual episode of 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's going to point you in the right direction. And today, well, we're looking into the impact of

shareholder activism on a closed-end fund, and we're doing it with Axel Merk, who's probably best known as president and chief investment officer at the Merks Funds, but who also runs the ASA Gold and Precious Metals Fund, that's an old line closed-end fund that's based in Bermuda – by the way, that location will become important here – and it was started in 1958, but Axel took it over in 2019. It's ticker symbol ASA, and you can learn about the fund at ASALtd.com. And I couldn't help but notice that if you sound that out phonetically, it comes out as Assaulted.com, which is kind of how Axel might be feeling right now because ASA Gold and Precious Metals is facing an activist investor in Saba Capital Management. So as much as we like hearing about gold and precious metals from Axel who's been here as a guest several times, today we're going to try to let you see how complex and complicated a proxy fight with an activist investor can be from the side of fund management, and maybe it'll give you a different perspective on, "Hey, I buy the discounts." Before we get there, a quick reminder that you can learn about closed-end funds, interval funds, and business-development companies generally by going to AICAlliance.org, the website for the Active Investment Company Alliance. Axel Merk, it's great to have you back on The NAVigator.

AXEL MERK: Chuck, what an introduction. Good morning, or good day.

CHUCK JAFFE: Well, a lot to get through because there is a perception, we've had plenty of managers on The NAVigator who are discount buyers, and there is always a perception that buy closed-end funds at a discount, and if the discount gets too wide an activist investor will come in and they will narrow the discount or they'll open-end the fund, and then we go up to net asset value and, "Look, I bought it at a discount, it got back to its net asset value and I profited." And that sounds great from an investment standpoint, but for somebody running a fund it's a very different experience to suddenly have people coming into your backyard and doing this. And more to the point, one of the things that people should learn here is that not every activist case is the same, many activist cases are doing what closed-end funds do best, which is things like fixed-income funds and the rest, but you run a junior mining fund. Gold and precious metals, different kind of beast, and the impact this can have on shareholders is different. But I'm getting ahead of myself, first thing's first, help us understand, Saba came in when, and where do things stand now in terms of what they want versus what you think is possible?

AXEL MERK: Sure, how many hours do we have? In December 2022, Saba started buying shares in ASA, we saw that in filings early in 2023, and then pretty quickly afterwards we reached out to them. We reach out to all our investors, we appreciate investors large and small whether they are activists or not, to try to establish a dialog, and as we did that we took months to get a call established with them, and once we did they did not have any demands. We asked them in numerous ways whether they have any requests, any demands, whether they would like to talk to the board directly, and all they said is they're following their investment process. They also indicated once they do their filing, that they become activists, it really only means that a market-based exit is less likely, not that they have any demands. But then in December, on December 1 they sent us a demand that a slate of their director nominees be added to the proxy because our board has been incapable of closing the discount, meaning that they turned aggressive without engaging with us in a discussion. That I think is very important context for what was then to come, because in that context the board has a responsibility to think about, well, how do we react to that? And as a board we believe that all shareholders should have a say in the future of ASA, and I think we'll touch on it, but ASA has various unique facets that make what I would call their traditional playbook difficult if not impossible to implement, notably it might be detrimental to all shareholders, including Saba if they actually were to do what they're planning to do.

CHUCK JAFFE: That is a key part of this, because again saying, "I want to narrow the discount," well, in your case narrowing the discount creates different issues because you're doing junior miners and if they open end the fund there become other issues. Your investment strategy kind of blows up in the face of this, right?

AXEL MERK: Well, you mentioned numerous issues. The first one may be that when we didn't take over the fund as you mentioned earlier, we had shareholders approve us as managers and there was a process involved and various reasons, but when we took over the management as you say, we shifted the fund towards junior mining companies, and there were two reasons. One is we believe that space is a good place to invest in, the other one though is we want to differentiate ourselves from an open-end product. In an open-end product, in an ETF or a mutual fund you can only invest in these less liquid companies on a very limited basis, and the last big bear market we had in the space, that caused significant issues for the mutual fund space when they had outflows because they had to sell their liquid

holdings and they got stuck with these small holdings, and so they've been very reluctant to engage in that. If we were index hugging, then by all means, there probably shouldn't be a closed-end fund because an open-end product is less expensive to run, and so there is that side of it. The other side of it is that over 70% of the stocks are small cap companies, and so it is just not feasible in the current environment to open end the fund. And then maybe most importantly, you mentioned in the introduction that this is a Bermuda-based fund, that's rather unusual in this space. This fund was launched in 1958 in South Africa, re-incorporated in Bermuda in 2004, and the reason it was incorporated in South Africa in the 1950s was because it was almost impossible to invest in gold at the time. In order then to act as an investment fund, you get a special permission, a so-called exemptive order from the SEC, that comes with a whole bunch of strings attached that amongst others make managing a fund more expensive, but that we believe would make it tremendously expensive to even try to open-end the fund and quite likely would not succeed. And the reason we don't think it will succeed is in the 1980s there were several European mutual funds that tried to list their mutual funds in the US, the industry lobby in the US fought that tooth and nail, and eventually they gave up. We don't think that it would be easy, and it certainly wouldn't be inexpensive to do it, and I think that effort would well fail if one tried to open-end this fund.

CHUCK JAFFE: Let's ask a slightly different question in here, which is rather than turning it into an open-end fund, if they couldn't do that, and I'm not asking you to make their case, but would they simply say, "Okay, fine. Then we reach net asset value by, can't keep the fund going, but liquidate it and give us full value." Wouldn't that be the logical conclusion for them to reach?

AXEL MERK: If Saba gains control of the fund, we believe liquidation may well be the end game, that's simply because the sort of alternatives they typically consider might not make sense. At the same time, of course you have the same issue, you have all these liquid holdings, so you cannot just sell them and give everybody the money back because we would sell them at a substantial discount. It would probably be a protracted liquidation including in-kind redemptions, for the larger investors at least, and if that's what investors want, then the board is more than willing to pursue that. We happen to believe that the current board is far better suited to execute that if that is what investors want. Now that said, we believe that most investors are in this fund because they like investing in mining companies. Now clearly

different investors have different priorities, some investors like to trade the discount, and obviously Saba has its own plans and those need to be reconciled. As a board, we have to think about what do all investors want and make sure that their voices get heard.

CHUCK JAFFE: Saba is of course the biggest of activist investors, you're not alone in the companies that they are doing this with, though as we point out, your situation is very different. Let's talk about something else, which is you don't believe the fund can be run, and you don't believe that Saba can reach its ends, because again even if it's liquidation, it's not like you're liquidating a bond portfolio, you cash out and you're all done, that's not happening here. So that being the case, there is a cost here that current shareholders are paying, Saba's now a shareholder, they're paying it too, but what is this doing for the investors who are riding along watching how this plays out?

AXEL MERK: Well, a so-called proxy battle is expensive, we don't like it, investors don't like it. Had Saba engaged constructively this would have not have been necessary. Again, we have, and this board even before I came on board, has been very open to investors, when investors have requests they have come to the board, demanding to close the discount have not been part of that, right? And so similarly, Saba did not engage with the board, and so we had to work with what we had. We had an investor aggressively buying shares, not communicating, indicating they want to kick out the board of directors, and then we of course have to see what is Saba's track record? What do they historically do? And your audience knows what they typically do, they do these tender offers amongst others, and they have by the way increasingly taken over the management contract, and that may well be because they have grown bigger and it does make economic sense from their point of view. But of course, they don't have any expertise in the mining sector, so they might repurpose this fund into a fixed-income product. If that's what investors want, sure, but again we happen to think that most investors want this fund to be investing in the mining sector, and indeed one of the items we have on the proxy list is to move to a slight super majority to change the investment objective of the fund to be at 60% or more of shares outstanding. And we believe that given the history of ASA, that that is warranted, and so we're asking investors for direct feedback as to, "Is that what you want?" Because again, if you want this to become a fixed-income product, by all means, go for it. That said, there are probably less costly ways than running a fixed-income product, and it might not make sense to do that with ASA.

CHUCK JAFFE: Doesn't sound like there's any quick resolution coming here. I mean, how long does this drag on? Does this drag on until they get enough proxies to beat you or you get enough proxies to beat them back? Is there any sort of interim solution, and does this hurt the fund while it's ongoing? In other words, will your performance be damaged at all while you go through this?

AXEL MERK: There are a few things. First of all, one of the things we didn't touch on, because we don't want to talk about mining too much, but this is a very volatile space, far more volatile definitely than the fixed-income space. And indeed, the 10% or let the discount be 15%, you can just wait a week and this fund can move 5% or even more, sometimes it does move more than 5% in a day, which is very consistent with the sort of space that we are in, and so that's just one thing I'd like to throw out there as a side note. In the short term, we have a shareholder meeting coming up at the end of April, we are confident that we will prevail and send a very strong message to the community, including to Saba. That said, Saba is known to be very patient, and so if our shareholders don't send a strong message they may well stick around, and so we have to take it a step at a time. We are of course very much focused on managing the fund, we have not changed the strategy in how we invest in the fund, and we're very excited about the strategy. So as much of an issue this is for the fund structure, we continue to be focused on what we believe we're good at, which is managing this product.

CHUCK JAFFE: Axel, it's a really interesting story, it's a really interesting case. We're out of time here, but I'm sure we will discuss this with you again down the line. Thanks for joining me 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 yes, that's me, check out my show on your favorite podcast app or by going to MoneyLifeShow.com. To learn more about interval funds, closed-end funds, and business-development companies go to 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 president of the Merk Funds, he also serves as chief investment officer for the ASA Gold and Precious Metals Fund. Learn more about the firm and the fund at ASALtd.com. Yeah, again, phonetically, Assaulted.com, too funny. Axel is on

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