



KARL KAPITAL

1Q'26 Newsletter

"Blackstone may have 300 people dedicated to the wealth channel, but I have 2.1 million followers on X." – Bill Ackman

"Americans can always be counted on to do the right thing, after they have exhausted all other possibilities." – Winston Churchill

"What the wise man does in the beginning, the fool does in the end." – old market proverb

	Year-to-Date March 31, 2026	Inception-to-Date March 31, 2026
P2 NEXXT FUND II LP¹ (pro forma net)	(5.9) %	96.3 %
<i>Standard & Poor's 500 Index (SPX)</i>	<i>(4.4) %</i>	<i>142.1 %</i>
<i>Financial Select Sector SPDR (XLF)</i>	<i>(9.4) %</i>	<i>99.4 %</i>
<i>Russell 2000 (RTY)²</i>	<i>0.9 %</i>	<i>78.6 %</i>
P2 NEXXT OFFSHORE MASTER FUND LP³ (pro forma net)	(5.6) %	54.2 %
<i>Standard & Poor's 500 Index (SPX)</i>	<i>(4.4) %</i>	<i>116.0 %</i>
<i>Financial Select Sector SPDR (XLF)</i>	<i>(9.4) %</i>	<i>127.9 %</i>
<i>Russell 2000 (RTY)</i>	<i>0.9 %</i>	<i>74.3 %</i>

Nexxt II had a negative return of 5.9% net in 1Q26, in line with the overall market. This was our first quarterly decline in two years. Financials, the sector in which we primarily invest, was the worst-

¹ The returns listed above for **P2 Nexxt Fund II LP** (a 3(c)(1) fund; the "Fund") are unaudited estimates generated by Karl Kapital which are subject to modification by our independent administrator and/or auditors. The Fund performance figures are net of all fees and expenses, including management fees (1.5%) and the performance allocation (20% if applicable). Fund returns are inclusive of the reinvestment of dividends and other earnings, including income from new issues. The Year to Date and Inception to Date performance figures have been calculated using a hypothetical investor that made an initial investment on day 1, October 1, 2019, and pays full fees, (1.5%/20%) with no intra-year contributions or withdrawals. The performance statistics from October 2019 to October 2020 are from a proprietary account which was not subject to any administrative/operating expenses, management fees or performance allocation and did not participate in new issues. A model 20% performance allocation and 1.5% management fee, representing the expected fees applicable to typical fund investors, has been applied retrospectively. The performance of the Fund, which may pay possibly differing fees and expenses and participate in new issues, may differ, perhaps materially, from the performance shown and does not reflect the performance of any other funds or accounts managed by Karl Kapital. Individual investor returns may vary based on the timing of their contributions, withdrawals and/or varying fee arrangements. Please note that this table contains unverified performance estimates and may be subject to change. Past performance is not a guarantee of future returns. This is not an offer or a solicitation to invest in P2 Nexxt Fund II LP. All indices comparison returns are shown with dividends reinvested.

² Indices cannot be invested in directly. Unmanaged index returns assume reinvestment of any and all distributions and do not reflect fees or expenses. Past performance does not indicate future performance and there is a possibility of a loss.

³ The returns listed above for **P2 Nexxt Offshore Master Fund LP** (a 3(c)(7) fund; the "Fund") are unaudited estimates generated by Karl Kapital which are subject to modification by our independent administrator and/or auditors. The Fund performance figures are net of all fees and expenses (excluding direct feeder funds operating expenses), including management fees (1.5%) and the performance allocation (20% if applicable). Fund returns are inclusive of the reinvestment of dividends and other earnings, including income from new issues. Inception to Date performance figures have been calculated using a hypothetical investor that made an initial investment on day 1, November 1, 2020, and pays full fees, (1.5%/20%) with no intra-year contributions or withdrawals. The returns only reflect the performance of Fund and do not reflect the performance of any other funds or accounts managed by Karl Kapital, including, as applicable, that of any onshore or offshore feeder fund of a specified portfolio. Individual investor returns may vary based on the timing of their contributions, withdrawals and/or varying fee arrangements. Please note that this table contains unverified performance estimates and may be subject to change. Past performance is not a guarantee of future returns. This is not an offer or a solicitation to invest in P2 Nexxt Offshore Master Fund LP. All indices comparison returns are shown with dividends reinvested. P2 Nexxt Fund II LP and P2 Nexxt Offshore Master Fund LP ordinarily invest in parallel, however, the performance of each of the funds may differ, perhaps materially, due to a number of factors including without limitation that each may pay differing fees and expenses or participate in new issues. Karl Kapital, LLC began managing the Funds effective as of January 1, 2025. Prior to this date, the Funds were managed by Phase 2 Partners, LLC.



performing sector to start the year (even worse than AI threatened info services), and our hedged portfolio (as it should) significantly outperformed the 9.4% decline in the financial sector ETF. Most of our losses were experienced in March as the Iran war negatively impacted all financials, especially those in Europe. Historically, Europe has been a meaningful contributor to our performance.

Last 12-Months Performance												
Apr-25	May-25	Jun-25	Jul-25	Aug-25	Sep-25	Oct-25	Nov-25	Dec-25	Jan-26	Feb-26	Mar-26	Total
3.8%	3.5%	1.8%	0.8%	2.4%	2.4%	(0.1%)	3.7%	2.7%	(0.9%)	(0.9%)	(4.1%)	15.4%

P2 Nexxt II LP returns net of fees. See first page for full disclosures.

The battle for headlines in the first quarter was fought between concerns about the Iran war and concerns about private credit. (Iran war headlines slightly edged out private credit). Sorry, but we have no insights to add on the Iran war other than to say that we maintain a hedged portfolio designed to reduce volatility and generate uncorrelated returns. However, we do have opinions and concerns on private credit. No, we do not believe private credit is the next crisis, nor should it be compared to mortgages in the Global Financial Crisis. But we do believe there is a risk that private credit losses will be worse than modeled (primarily on lower recovery rates) and investor gates will continue to be a problem. Our concern is the vehicles that were marketed to unsuspecting retail investors. The glossy marketing materials highlighted quarterly liquidity, low loan-to-value ratios, high stated dividend yields, and “senior secured” loans. However, the legal documents filed with the SEC disclosed portfolios of illiquid junk bonds with double-digit debt/EBITDA ratios, misaligned management fee structures, sometimes liquidity, and if that’s not enough, an extra turn of leverage at the fund level, just as a cherry on top. It should not be a surprise that large-scale Evergreen funds are running at a nearly 100% failure rate (defined by the investor experience, not the manager's success at raising assets). In March, we were asked by the Securities & Exchange Commission to discuss the state of the private credit industry. We presented a 40-page report on the current challenges and possible solutions to senior members of the commission, with significant follow-up dialogue since. If any of our investors would like a copy of this presentation, please reach out to Rachael (Rachael@karlkapital.com). Thematically, little has changed in our portfolio. The Iran war has caused significant volatility and price moves, but we do not see it changing any of our longer-term views that we see in our individual names or subsectors. The war has just seemed to have placed a pause on the market for now.

Nexxt II was unprofitable in five of its seven subsectors that we track. The two profitable sectors were specialty finance and non-financials. The specialty finance sector was hard hit in 1Q26, beginning with the Trump administration’s threat to cap credit card rates, followed by fears of future AI capabilities causing unemployment, and finally, higher oil prices straining the consumer. Despite these fears, our biggest winner in specialty finance was a long position in a debt collection company, Encore Capital Group Inc. (ECPG). Brokerage/asset management and banks were nearly tied for the worst-performing sectors. Brokerage was primarily dragged down by our theme to be long retail trading firms. The losses in banks were driven by our European bank exposure. The Iran war hit European stocks and especially banks on the energy price shock as investors priced in recessionary fears from the potential GDP slowdown.



First Quarter 2026 Sector Performance*		
Sectors	Gross	Net
Specialty Finance	1.9 %	1.8 %
Non-Financial	0.4 %	0.3 %
Financial Technology	(0.5) %	(0.5) %
Insurance	(0.8) %	(0.8) %
Mortgage Finance / Homebuilders	(0.9) %	(0.9) %
Banks	(2.9) %	(2.9) %
Brokerage / Asset Management	(3.0) %	(3.0) %

Total	(5.7) %	(5.9) %
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*P2 Nexxt II LP

Note: Sector net performance= (fund net performance/fund gross performance) x sector gross performance.

The sector gross returns are based off raw stock performance.

By individual names, the funds' largest winner for the quarter was surprisingly a long, despite the significant decline in financial stocks. Encore Capital, a name we have probably discussed in these letters far too many times, was the funds' largest winner. Encore's underlying core profitability from accelerated purchases in recent years is starting to show through to investors. Frustrated with the Street continuously underestimating earnings power, Encore broke from its standard of withholding guidance and delivered a 'minimum' EPS guide 50% above consensus forecasts. We believe Encore will continue to exceed expectations and see its earnings mix shift to higher multiple recurring revenues, while buying back significant stock, driving further multiple expansion. The second largest winner for the funds was a mid-sized investment bank. In the 1990s and 2000s there was a saying, "if there is a problem in financial markets, Merrill Lynch will find a way to be involved". Merrill is gone, but this company seems to have assumed the mantle of always finding the problem. Disclosure is poor, but we suspect the company has outsized exposure to private credit on its balance sheet, and with several 'one-time' write-offs, our suspicions have been correct. A short in a European private equity manager was our third largest winner. We believe this firm is mismarking its portfolio to mask fund performance that is worse than reported. The fourth-largest winner was a short on an M&A advisory firm. In our last letter, we highlighted that the M&A advisor firms once again seemed to be ahead of themselves and we were correct. Rapid fire headlines are bad for CEO confidence and thus M&A activity. Finally, a short on a financial technology/business services company that specializes in making metal credit cards was the funds' fifth largest winner. The company has recently made a business combination in a non-core industry (injection molding) using extremely aggressive accounting assumptions in a new holding vehicle structure with a dubious incentive framework. We remain short as we see further issues underlying the company.

On the losing side of the ledger, unsurprisingly, all of our top five losers were longs. Eurazeo SE (RF.FP) was the largest loser in the quarter. The combination of being Europe + private equity weighed on the shares, while a disappointing buyback guide (only 4% of shares vs 10% in 2025) outweighed the strong trends in fundraising and profitability. Capital One Financial Group (COF) was the second largest loser as the shares were hit by the previously mentioned Trump administration's threat to cap credit card



interest rates, along with employment fears from AI and higher oil prices. A surprise acquisition of fintech company Brex, specializing in enterprise level spend management, was negatively received. We believe the share reaction to Brex, which represented just 3% of market cap, was overstated and further pushes the company down its path of becoming a four-sided network (like American Express), driving higher profitability and a multiple re-rating in the future. Wealthfront Corp (WLTH) was the third largest loser. We like the business (its AI investing before AI was all the buzz), but we underappreciated their exposure to rate chasing cash sweep. We bought the shares too soon and sold too early. UWM Holdings Corp (UWMC) was the fourth largest loser. We initially started the position following the acquisition of Two Harbors in December. We believed the acquisition would improve capital and earnings stability. The Trump administration’s push to lower mortgage rates early in the year boosted shares, but rising rates from the Iran war reversed shares later in the quarter. Skyward Specialty Insurance Group Inc. (SKWD) was the fifth largest loser, which declined due to overarching fears of negative pricing cycles and increasing competition across the entire insurance industry. We believe that Skyward plays in niche segments that are much more resilient to the competitive fears, which will be born out in solid execution.

First Quarter 2026 Winners & Losers*	
Winners	Losers
Encore Capital	Eurazeo
Financial Advisory Short	Capital One
Alternative Asset Manager Short	Wealthfront
Financial Advisory Short	United Wholesale Mortgage
Transaction Hardware Short	Skyward Specialty Insurance

*P2 Nexxt II LP

Outlook: 2026

Despite the market’s rocky start to the year, we see many tailwinds within the economy and broader financial sector. The consumer remains well positioned with strong balance sheets that have been supported in the near term by elevated tax returns from last year’s OBBB. This consumer strength is driving solid credit and healthy spending levels. Our data shows early signs of stabilization in the employment environment with hiring trends beginning to improve (It is still quite early on this trend, but we are monitoring as an emerging theme as it is one we played in the opposite direction for the past few years!). Capex spending is accelerating, while broader corporate loan demand and credit remain strong despite the issues that we see present in the private credit sector. Though we expect the Trump administration to continue to create headlines and volatility, as we look to the remainder of 2026, we believe Trump will recognize that volatility is not good for his chances at the midterms, leading to tempering on some of the extreme uncertainty allowing company fundamentals to re-emerge as the key driver within our coverage universe.

Within capital markets, the remainder of 2026 is expected to have three of the largest IPOs in US history (four if Bill Ackman can get his 2m followers to pony up for his proposed \$10B fund offering). Hey, if Trump can govern via Tweet, why can’t Ackman build an IPO orderbook via Tweet? We believe calmer headlines out of Washington, combined with a record IPO calendar, not only in dollars raised but in investor interest, could provide an excellent backdrop for retail excitement and activity. So, we may get



a short-term boost to our longer-term investment thesis on retail investing platforms (Or if you were born before 1970, they were called discount brokers. If born before 1980, they were called online brokers.).

Our top five positions currently are: Flywire (FLYW), Encore Capital, and Skyward that have each been discussed in previous letters. Affirm Holdings (AFRM) and Banca Monte dei Paschi di Siena (BMPS.IM) round out the top five. While BMPS is not a new name for the funds, we have held a position for the better part of two years, it is new to the top five, so highlights are below:

- 1) Affirm— a new position on the long side for the fund, was purchased late in the quarter following market fears around consumer credit, AI, and the company’s ability to fund loan sales (private credit). As mentioned, our data shows consumer credit is continuing to be strong, and the company has recently executed some of its strongest ABS issuances in company history. These fears were overblown. We believe AFRM is a highly scalable consumer-led fintech company, akin to the credit card lenders in the 1990s. Covered primarily by tech investors, while we believe the market understands the growth potential and TAM of Affirm, our analysis shows that consensus significantly underestimates the inherent operating leverage in the model as the business scales. While the buy-now-pay-later product continues to gain share, the company’s recent launch of its Affirm card (2024) has seen strong adoption with a 14% attach rate, currently up from under 10% a year ago. This product expands their reach beyond the online checkout into physical locations and has a higher attach rate of the much more profitable interest-bearing product. We believe this will continue to drive an underlying mix shift to higher RLTC (a proxy for AFRM’s gross profit), and ultimately profitability. In the near term, we believe this could drive earnings estimates up 20-30%, while the shares trade at just 6-7x our longer-term GAAP EPS forecast. The company has also recently applied for an ILC bank charter, which would materially lower funding costs and add further upside to our estimates. We believe the company’s upcoming investor day in May will shine further light on these initiatives and continue to see over 50% upside in the shares.
- 2) Banca Monte dei Paschi – We have held a position in BMPS IM for the better part of two years as the company emerged strongly from a recapitalization in 2022 and was able to significantly reduce government ownership in 2024. More recently, the company acquired rival Mediobanca, leading to drama and CEO uncertainty, which weighed on the shares as one shareholder moved to oust the CEO (Luigi Lovaglio) because they wanted control of the Generali stake that came with the Mediobanca acquisition. This shareholder pressured the board to oust Mr. Lovaglio and proposed an alternative CEO (with limited banking experience) at the recent AGM. Despite proxy companies aligning with the board against Mr. Lovaglio, another shareholder supported his re-election, and ultimately Luigi won over 50% to be reappointment as CEO. Are you still following with us? We are not surprised by the majority of shareholders supporting Mr. Lovaglio, who became CEO in 2022, as he has done an impeccable job navigating the company from the recapitalization to the highly profitable business that it is today. We have the utmost confidence in Mr. Lovaglio’s leadership of the company and voiced our support for him in a press release ahead of the meeting ([here](#)). Moving forward, with Mr. Lovaglio back at the helm, we believe there is significant strategic optionality at BMPS to offload the Generali stake (worth ~30% of market cap) and free up significant excess capital. Further the company sits in prime position to help form the third banking pillar of Italy, which has been much discussed in recent years. We believe that given the capital flexibility, diversification following the MB acquisition, and strong geographies the company would make an excellent merger target. In fact, many had



speculated this to be the case in 2024 as Banco BPM and Anima (now owned by Banco BPM) took large stakes in the government's secondary sale. We continue to see meaningful upside along with an >10% dividend yield for the shares.

Operational

There were no material changes to operations during the quarter. We are on track to launch our market-neutral product in June with a large anchor investor. We will have more details once the product is live, but if you have any questions or interest, please contact rachael@karlkapital.com. By now, all investors should have received their K-1s. Similarly, if there are any questions, please reach out to Rachael.

In other interesting news, late last year the Securities & Exchange Commission charged the CEO of Triterras (TRIT) with fraud. You may recall that in 2021 we published research on Triterras showing the company was hiding its revenue dependence on related parties. Following our report, the auditor resigned the next day, the company accused us of hacking their computer systems, and shares were soon delisted. The wheels of justice may move slowly, but we are glad we hopefully helped protect some investors from this fraud. <https://www.sec.gov/enforcement-litigation/litigation-releases/lr-26429>

Thank you for all the support,

Karl Kapital



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