July 11, 2013

Dear Clients, Partners, and Friends,

The results for South Ocean Managementôs Delaware LP, Kong Partnersô L.P., before incentive fees, were as follows:

	Jun 2013	Year-to-Date
Hong Kong Partners LP (net)	-10.8%	-0.8%*
Hang Seng Index	-7.1%	-8.2%
Hang Seng C S C	-9.1%	-3.9%

Partnersô NAV $2.4881 after management fees and March 2013 provisions, but before annual incentive fees of 15% on appreciation. *after provisions March 31, 2013

"Ben Graham's favorite allegory is that of Mr. Market, a fellow who turns up every day at the stock holder's door offering to buy or sell his shares at a different price. Usually, the price quoted by Mr. Market seems plausible, but occasionally it is ridiculous..." Benjamin Graham, From Wikipedia

Hong Kong Partners LP, our China-oriented fund of well-managed, Hong Kong-listed growth stocks, increased 3.74% vs. - 6.5 % for the Hang Seng Index for the second quarter ending June 2013.

For Hong Kong market overall, The TR (Thomson Reuters) index of all Hong Kong stocks (a weighted index covering close to 90% of the total market capitalization), declined 7.497% in the first half this year.

Investor sentiment has remained subdued in the Greater China region. For the record, The World ex-US was down for both the Q2 and year-to-date periods.

The last weeks of June were rough as investors fled from Fed interest rate tightening scares along with the China interbank rate surge that sent markets reeling. The Hong Kong market broke out in sweat and convulsions, like a junkie who had lost his needle.

Technically, the selling momentum was as intense as any period since the late 2007 market collapse (which was after the Hang Seng Index had surged from 20,000 to over 30,000 in matter of weeks. I suspect there may have been some weak hands in the market recently, wrong players, such as non-equity fixed income or retail investors, chasing yields. Ben Grahamôs Mr. Market decided to shake them off, emblematically, and take them to the cleaners).

Individual stocks we had been following became cheap in the late June sell-off and we added to our portfolios using sidelined cash. The following chart is the path of the Hang Seng Index in 2013.

That late sell-off: Ridiculous?

Our cash holding is now below 10% of total market value.

The Hong Kong market is a volatile animal, with traumatic declines over the past. Since we arrived in Hong Kong, we have witnessed 20% or greater declines every year (since 1993). That's the nature of the animal, even in good markets we have declines, and trying to predict its direction over the near term is an exercise in futility. We do not claim any special gift in ducking or predicting these events, as we are bottom up, individual stock shareholders, not market momentum investors.

We have outperformed, nevertheless, over these volatile cycles (see our fact sheet www.south-ocean.com)

Actually, in the first six months this year of actively employing our unique new *Warren Buffett-style* investment proprietary software system (South Oceanοs *Banquet System*) of screening for great businesses to own at (incredibly) reasonable prices, we have out-performed the market. This performance is even after an 11% provision made on two (temporarily) suspended holdings in our fund made at the end of the first quarter.

With the new system, we have identified and fortified our portfolios by diversifying into an expanded list of companies to own (we own 27 holdings in over a dozen differing industry sectors). Notably, in formulating intrinsic values with our Banquet System, we demand a margin of safety to buy, and require a 20 % minimum annual.

And, because our holdings have strong balance sheets, many with net cash positions, the liquidity crunch in China should not be an issue.

Though the late quarter sell-off was tumultuous, we stuck to our outstanding holdings, even adding in the decline. Importantly, we have yet seen (nor expect at this juncture) any major contraction/reduction in earnings estimates in this already cheap selling market.

Speaking of momentum market players, a Barclayôs bank survey recently noted an interesting point: "Asian investors are usually momentum-driven. They cash the assets (in) when the market goes down, and buy when it goes up," The bank commented ñé there are more bottom fishers in the developed markets, where investors are more sophisticated and have more experience.ò This inefficiency creates bountiful hunting grounds for sizable ten baggers for our portfolios in Hong Kong.

We are fully invested in China-oriented, growth stocks today. For example, we invested during the last quarter in a company that makes aseptic packaging in China, Greatview Aseptic Packaging (GA PAK, code 468hk, HK$6.4billion market cap, US$831 million, 3.1% dividend yield, no long term debt and net cash gearing).

A little background and description of the businessé

> Tetra pak was invented by a Swedish company 40 years ago. The aseptic packaging technology made possible a cold chain supply, substantially facilitating distribution and storage. In 1943, the Åkerlund & Rausing lab started to work on developing the milk carton package and, in 1944, came up with the idea of constructing a tetrahedron shaped package out of a tube of paper. In aseptic processing the product and the package are sterilized separately and then combined and sealed in a sterile atmosphere, as compared to canning, where product and package are combined and then sterilized. When filled with ultra-heat treated (UHT) foodstuffs (liquids like milk and juice or processed food like vegetables and preserved fruits), the aseptic packages can be preserved without chilling for up to one year, with the result that distribution and storage costs, as well as the environmental impact, is greatly reduced and product shelf life expanded.

GA PAK started manufacturing in 1996 in the Inner Mongolia milk producing region of China, garnering a 13% market share today. Listed in December 2010, its top customers include the major dairy operators in China, Mengniu and Yili. It has captured market share from privately-owned giant, Tetra Pak, with its lower pricing strategy (former Tetra Pak execs make up GA PAKôs management). The company is expanding internationally, setting up a German plant to operate in the European theater with production just starting.

Revenues have grown 27.1% compounded annually for the past 5 years. Bain Capital was an early backer and owns ~30% today. As dairy products in China represent a fast growing, yet still small per capita consumption ratio in the Chinese market, we believe Greatview Aseptic Packaging's growth prospects are strong.

Our overall portfolio's weighted average P/E on this year's estimated earnings is 8.1 times with a 3.1% dividend yield. As we have said, we expect the best returns are yet to come.

Sincerely,

Brook McConnell
President
Email*:* *brook@south-ocean.com* Website: *www.south-ocean.com*
Hong Kong