SOUTH OCEAN 南海管理有限公司
MANAGEMENT, LTD.
HONG KONG

January 9, 2014

Dear Clients, Partners, and Friends,

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

	Dec 2013	Year-to-Date
Hong Kong Partners LP (net)	2.7%	13.6%*
Hang Seng Index	-2.4%	2.9%
Hang Seng Small Cap Index	-0.2%	12.3%

Partnersô NAV $2.8506 after management fees and March 2013 provisions, but before annual incentive fees of 15% on appreciation. *after provisions March 31, 2013

The dynamics behind our small/mid cap holdings of Hong Kong-listed, China-geared stocks became evident in the fourth quarter last year.

Our portfolios rose 6.9% versus 2.2% for the blue chip Hang Seng Index in the October through December period.

Our strategy, using a proprietary, Warren Buffett-like software screening system, provides a maximum price to pay for stocks. Our intent is to find great growth businesses at a reasonable price.

We seek 20% annual appreciation for each purchase, with companies that have solid balance sheets and managements we have visited.

Our core know-how is produced by being based in Hong Kong, near the principle offices of our holdings (itôs very difficult to follow fast moving events in the volatile markets here from London or New York).

For the year, our performance was penalized by provisions made in March 2013 on two large, China-oriented holdings: we wrote to zero the values of Chaoda Modern Agriculture (~7% holding), and China Metal Recycle (~5%).

Had we not written down, our portfolio performance would have shown a net increase of 25.0% for the year (we expect to realize a write-back on these two holdings at some future date, as well).

It is gratifying our 20% performance target was principally met last year, utilizing our fundamental investment approach.

In the last quarter, our best performers were Beijing Enterprise Water Group (BEWG, 5.1% holding, code 0371hk, an under-owned, leading water treatment enterprise in the PRC), which secured a US$240 million long-term loan from Asian Development Bank, and gained 49.5%.

China Metal (2.1% holding, code 0319hk), gained 34.8% and Macau casino operator Galaxy Entertainment (2.0% holding, code 0027hk) gained 26.7%.

Both BEWG and Galaxy are experiencing rapid earnings growth. China Metal, a 20 year PRC manufacturer and supplier of parts to Caterpillar and John Deere, sells at just 5.4 next yearôs expected earnings.

Our laggard was orange grove company, Asian Citrus (code 0073hk, 2.0% holding), down 25%, on local media news of a relatively small amount of dyed navel oranges being sold in Southern China (not by the company), which affected customer confidence in the domestic orange market as a whole. We added to our holding in sourcing giant, Li and Fung (1.9% holding, code 0494hk), on price weakness in December.

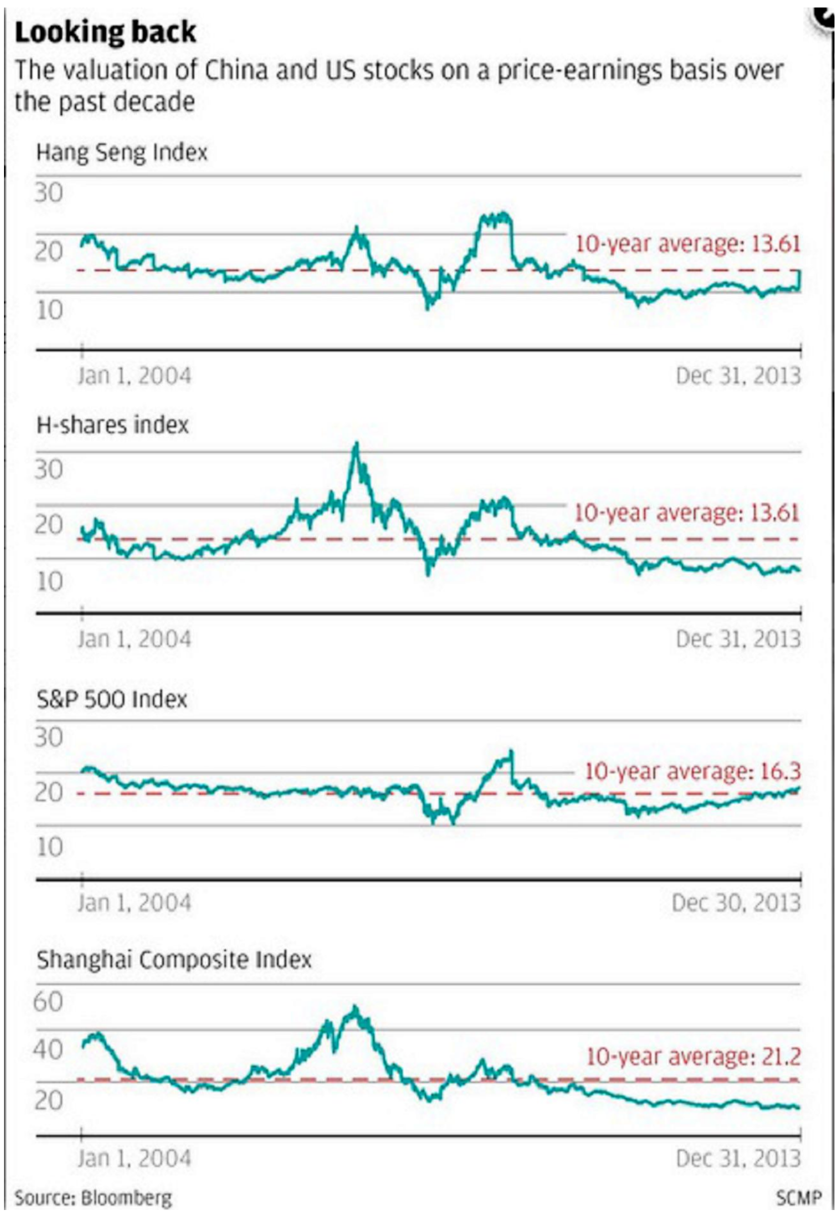
Last year, the Hang Seng Index barely moved.

Investors have neglected China shares, with the MSCI China index trading today at a 40% discount to the MSCI India on a forward price-earnings basis (according to I.B.E.S).

The Hong Kong Hang Seng Index sells at 10.4 times trailing earnings, with a 3.5% dividend yield and a 1.5 times price to book value.

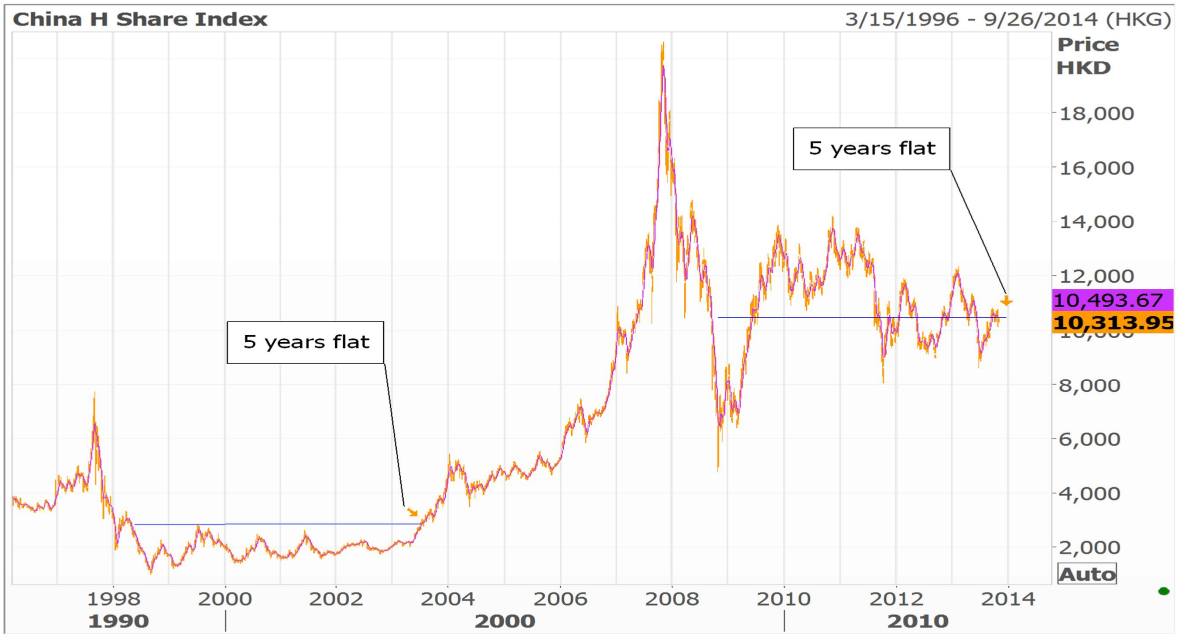
The Hang Seng China H share index sells at 7.9 times trailing earnings (according to Reuters), with a 4.0% dividend yield and 1.3 times book value.

These valuation levels are below historic 10 year averages (see the following South China Morning Post table);



The last time China H shares (Chinese enterprises listed in Hong Kong) sold this cheap was in 2003 when the index was at 2,000:

Why now?



(Note the rise from 2,000 to 20,000 by late 2007é quite a move!).

Essentially, the China index has traded flat, for the past 5 years.

With pessimism this intense and pervasive, we contemplate what might the flip side look like (should pessimism be replaced by optimism)?

How about the Hang Seng Index, (currently trading at ~23,000), rising to 38,000 in two years?

Laughable?

Consider a simple equation: with (depressed) 2014 consensus earnings projections for the Hang Seng Index of 2,119, a 20 price-earnings multiple (which is below historic levels the Index has sold) would equate to a ~42,000 level.

(Fibonacci, the mathematician from the 13th century, constructed some basic numeric sequences. The following projection is generated from those sequences).

38,000! Ridiculous? Preposterousé maybe, but not out of the realm of possibility. Of course, no guarantee our contrarian outlook materializes.

Nonetheless, we expect our small/mid cap holdings of companies, profiting from operations in China, to benefit.

Sincerely,

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