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

October 16, 2018

Dear Clients, Partners, and Friends,

The results for South Ocean Management's Delaware LP, Hong Kong Partners' L.P., before incentive fees, were as follows:

	Sep 2018	Year-to-date
Hong Kong Partners LP	-0.7%	-19.4%
Hang Seng Index	-0.4%	-15.5%
Hang Seng Small Cap Index	-2.6%	-16.6%
MSCI HK Small Cap Index	-2.5%	-24.8%
HS Mid Cap Index	-0.5%	-21.6%

Partners' NAV $2.6517 after management fee and provisions, but before annual incentive fees of 15% on appreciation.

Continued US/China trade news and fears of a slowing China economy and currency devaluation kept pressuring Hong Kong stocks last month. In mid-month, there was elation that trade talks might be re-started, but hopes were soon dashed. Bearish economists' commentaries have jolted investors, driving the Hong Kong market to oversold levels.

As shown in this chart, buyers have been concentrated in the US and very little elsewhere:

The MSCI ACWI index covers approximately 85% of the global equity opportunity set outside the US.

We are finding some extraordinary values evolving in the wake of the adverse investment sentiment. Our weighted average price-earnings ratio is quite low today:

	Price/Book	2017 PE	2018 PE	Yield	Earn Yield
South Ocean Holdings	1.0	6.8	6.2	4.3%	20.0%
Hang Seng Index	1.5	10.5	10.8	3.8%	9.5%

Our strategy, since our founding in 1992, has been to uncover unrealized values in small/mid-capitalized shares of companies listed in Hong Kong with businesses benefiting from operations in China.

We developed an in-house intrinsic value-oriented screen more than 5 years ago, using bottom-up analysis. Our system ranks companies (A, B or C) based on 5 fundamental inputs and calculates a maximum price to pay for the stock. We demand a low enough price to return 20% per year for our long-term holding period. Usually, these are leading, top rated businesses that are out of favor and selling below a reasonably estimated intrinsic value.

We further enhanced our in-house stock selection process with a method used by Peter Lynch (famed mutual fund manager of Magellan Fund at Fidelity). This analysis aligns well with our Warren Buffett-like intrinsic value screen, (called The Banquet System) with some added features.

Lynch would chart the stock price and the earnings per share together and aligned the value of $1 in earnings per share to $15 in stock price. He wrote in his book, One Up on Wall Street:

> "A quick way to tell if a stock is overpriced is to compare the price line to the earnings line. If you bought familiar growth companies when the stock price fell well below the earnings line, and sold them when the stock price rose dramatically above it, the chances are you'd do pretty well."

Lynch defaulted his earnings line multiple to 15x for all growth stocks. The tweak for our screen is to be flexible with the multiple. We can use an individual stock's lowest annual PE multiple over the last 5 years, (similar to our Banquet System process), and we can draw the earnings line using any meaningful multiple assumed, as well.

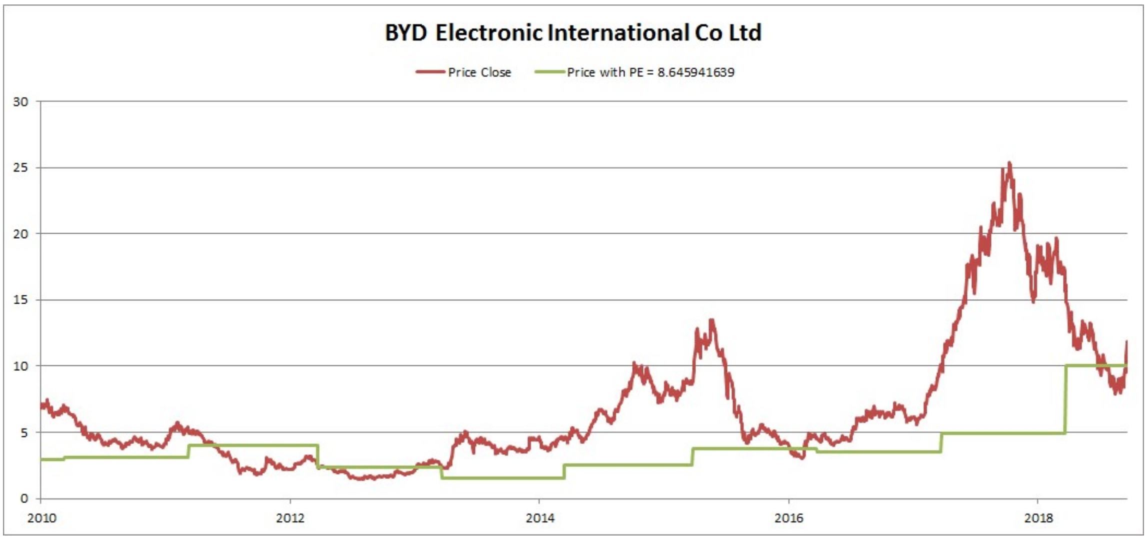
For example, Beijing Enterprise Water Group (BEWG, code 371hk) has normally sold at ~20x its earnings annually over the past 5 years. The lowest the shares sold relative to its annual earnings was 15x.

Today, the share price of BEWG is selling below the (green) earnings line, which makes the risk reward of owning this growth stock attractive.

BEWG is also rated a buy on our intrinsic value Banquet System screen. As shown by the red line above, the share price today is selling below the earnings line.

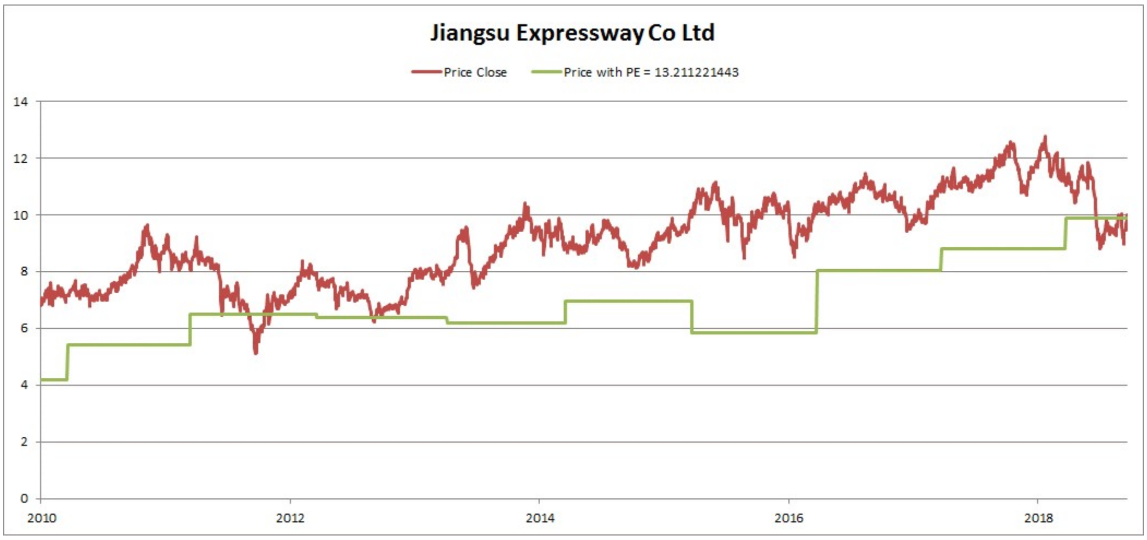
We added to this long time holding of ours after the company announced above average earnings growth in August.

The following is an example of an initial purchase in the 3rd quarter this year of BYD Electronic, a leading manufacturer of smart phone casings. The ranking on our Banquet System intrinsic screen of the company's fundamentals was favorable and the company has enjoyed consistent earnings growth over the past consecutive 4 years. The balance sheet has net cash with no long-term debt. The share price had fallen from a 52-week high of HK$25 to HK$8 where we began buying:

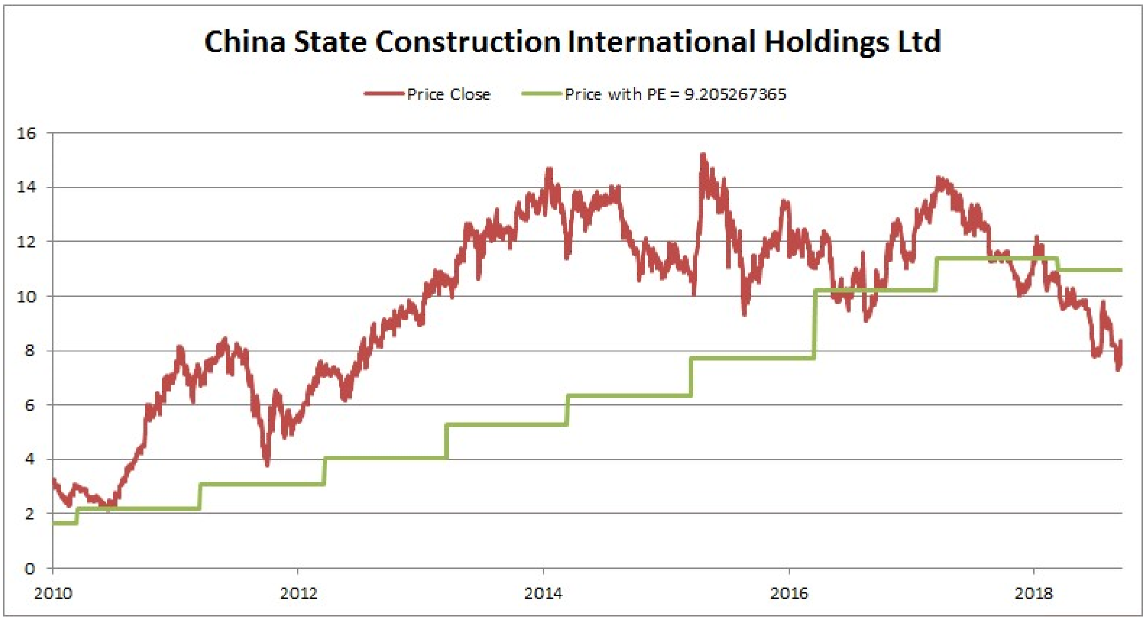


Another example is A-rated toll road and bridge operator, Jiangsu Expressway (code 0177hk, Market cap HK$12.3 billion, US$1.6 billion). The Shandong Province-based company, in the busy Yangtze River delta area, has seen steadily rising earnings from increased toll revenues and is expanding its portfolio of toll roads and bridges in the Province. The company pays a generous 5.4% dividend. With an expected 6% long term growth rate, the shares were attractively priced based on our Banquet System screen.

The share price dipped below the green earnings line (earnings per share times lowest annual 5-year price earnings ratio) last month, where we began buying.



We also added to our position in A-rated China State Construction (code 3311hk, HK$18 billion market cap, US$2.3 billion) on recent weakness at a price close to $7.40/share.



Our combined processes further pin-points the risk/reward, overpriced/under-valued areas of the market. As we fine tune our processes, we are able to identify many opportunities in the less-followed small/mid cap stock sectors in Hong Kong.

Lastly, with all the volatile weather (and stock market) conditions around the world (two hurricanes in the US and super Typhoon Manghut in Hong Kong), we hope all our friends were not affected and safe from all the tumult.

Sincerely,

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