April 12, 2011

Dear Clients, Partners, and Friends,

The results for the South Ocean Management composite and Hong Kong Partners L.P. before management fees, were as follows:

	Mar 2011	Year-to-Date
Hong Kong Partners *	-1.9%	-6.1%
Hang Seng Index**	0.8%	2.1%
BNP Peregrine Greater China Index	4.5%	1.9%
MSCI HK Small Cap Index	3.1%	-2.3%

Partnersø NAV for Mar was 3.2844 after management fee, but before annual incentive fees of 15% on appreciation.

Hong Kong stocks were hit by a barrage of unexpected events last month that rattled investors. Small/mid cap growth stocks of China-oriented companies de-rated and are becoming better values today than at the bottom of the market in March 2009.

We extend our heart-felt condolences to all our friends who were personally affected by the Japanese earthquake. In fact, the quake was so big, some claim they felt a jolt here on March 11.th Though the ensuing tsunami did not reach Hong Kong shores, fears of radiation did, landing in the supermarkets.

We are fully invested in small/mid cap, China-geared Hong Kong listings of companies with strong balance sheets and fast growing earnings benefiting from operations in China. Several recent purchases to our diversified list of holdings are illustrated below.

Sincerely,

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

Shortly after the earthquake, our media was dominated with ÷expertsø explaining the potential consequences of the troubled Japanese nuclear plants. Naturally, people worried. For example, Hong Kong parents began stocking Japanese baby formula, a trusted Japanese import.

Hong Kong investors also panicked during the month.

Even before the mid-month alarmist news reports began, headlines were downbeat, such as **China Exports Grew in February…well short of forecasts**, and, **Brace for $200 oil if unrest hits Saudi Arabia.** Stock prices, in general, were directionless for most of the first quarter.

Hong Kong, it seems, is particularly susceptibility to rumor, speculation, superstition and gossip stories. This was evident one week after the disastrous earthquake when headlines in local paper read: **Salt shame**

Panicked shoppers stripped stores of table salt in Hong Kong - and in cities across the mainland - amid internet claims that it can ward off radiation exposure from Japan.

Ionized salt and iodine tablets? Other than the fact 85 percent of table salt is not iodized and "í one has to take about 2.5 to five kilograms of [iodized] table salt a day in order to absorb the dose of iodine that is contained in an iodine tablet," it didnøt stop pandemonium in the stores. Hong Kong people emptied supermarket shelves of all salt. When all salt products were gone, they next went after soy sauce.

Characteristically, an elderly Hong Kong woman, who had queued for half an hour, reportedly said "I don't know what the salt can be used for. But people are snatching, so I'd better hurry."

Thankfully, the events 2,000 miles away didnøt cause any direct impact to Hong Kong. While the ongoing concerns from the earthquake still prevail, they are under a less hyped-up atmosphere. And although the salt episode clearly demonstrates a deep-seated terror about radioactivity, the same stricken behavior is evident in investment decisions made locally as well. Smaller capitalized, less followed stocks, typically owned by retail investors in Hong Kong, were sold indiscriminately after the earthquake.

The markets, at times, operate extremely inefficiently in Hong Kong. As one prominent money manager observed, õí players in China-related stock marketsí are quite õuneducatedö in the true sense of the word. The idea is that you make money by taking money from stupid (sic) people who shouldnøt be in the market; that is the truthí ö

We see the currently depressed environment of small/mid cap sectors today as temporary and an opportunity for our client portfolios. We have 27 positions of well managed companies, which are growing rapidly and sport single digit price/earnings ratiosí what a combination of value and growth!

We invested in several new holdings; a property stock, an oil exploration company, and a pharmaceutical company, as well as added to two existing positions.

Most of the steel used in the Beijing Olympic stadium, known as the õBirdøs Nest,ö came from fast growing steel manufacturer, China Oriental (stock code 0581hk). China Oriental is the only private, non-State-Owned steel maker listed in Hong Kong, the second largest private steel company in China.

Its strategic and major shareholder is the worldøs largest steel company, Indiaøs ArcelorMittal. ArcelorMittal became a strategic partner and major shareholder, with a 29% stake, in 2007. This partnership provides advanced steel production, global distribution and sourcing networks, supply chain management and, perhaps most important, management expertise for the company. The joint venture also nurtures an

incentivized workforce, a concrete investment factor and leap over other operating steel enterprises in China today.

We met with the profit-oriented management on several occasions in Hong Kong and learned insights into Chinaøs burgeoning steel industry.

China requires increasing amounts of steel for its urbanization. In 2009, the PRC produced 567 million tons of steel versus 58 million tons produced in the USA Have not come across 2010 numbers as of this writing). China Orientaløs total production capacity of 11 million tonnes of crude steel will rise to 15 million tonnes in 2015. The companyøs factories are strategically located in Hubei Province, the largest iron ore and steel producing province in China. It ranks among the top five non-SOE steelmakers in the country.

China Oriental is not making steel for the property market, an area of concern in China. It produces steel for infrastructure, where there is still a huge push by the China government to build more roads, bridges and tunnels. Most state-owned steel factories will produce all out just to keep employment steady. China Oriental, with all new factories, has a cost structure 4 times lower than that of larger steel maker, Maanshan Steel. Though the company makes the same profit as Angang Steel, which has 3.4x more revenue, this low cost producer spends just Rmb49 per tonne on sales and administrative expenses, Rmb50-200 lower than its peers.

China Oriental reported HK$0.43 earnings per share for FY 2010 for a 6.0 P/E when we added to our position. The stock trades at 4.2X FY11E P/E on street estimates, well below the averages for Angang and Maanshan Iron & Steel of 18.8X and 13.6X.
One caveat: the shares are illiquid and, consequently, are volatile.

Sino Union Energy Investment Group (stock code 0346hk) has transformed its business at the hand of its new chairman from China, US-educated Dr. Zhuo Zefan. Dr. Zhuo has brought in a seasoned management team and owns 27.2%, along with two other significant shareholders; Yangchang Petroleum, Chinaøs fourth largest oil company, with a 14.5% ownership, and Hong Kong and China Gas Company (Towngas) with 5%.

The company has two promising oilfields being drilled in Madagascar, the island off the coast of Africa. Reputed international reserve consultant, Netherland Sewell & Associates, estimates the companyøs first oil field will contain not less than 2 billion barrels of oil. At US$100 per barrel, that equates to US$200,000,000,000. Sino Union Energy (with a HK$4.2 billion or US$530 million market cap), has a 43.42% stake in the project.

Drilling results on three wells will be announced this summer. The company expects full production by the end of 2012. The cash rich company will need further funding to expand drilling after the results have been concluded, but will not do any placing less than 50% above the current price. The risk/gain ratio appears quite appealing and we are patient holders of this undiscovered stock recently purchased.

We also bought a new position last quarter in shares listed on the GEM board in Hong Kong.

One advantage to owning a GEM-listed stock is the fact shareholders receive quarterly versus semi-annual financial reports. There is no question a higher valuation (i.e., price/earnings ratio) can be achieved with more frequent correspondence and higher transparency from company management.

Hospital management, pharmaceutical producer Hua Xia Health (stock code 8143) was created in 2005 from a reverse takeover. It reported its third quarter, nine month results on Valentineøs Day. Those results suggest an improving outlook and a stock selling at a significant discount to peer company valuations.

The Company has three segments: provision of general hospital management services, pharmaceutical wholesale/distribution and pharmaceutical retail chain business. Early last year, the company bought (from its Chairman) the pharmaceutical distribution business in Fujian Province (encompassing over 7,000 drugs to 200 different hospitals). Its retail division owns 85 pharmacies in Fujian Province (population: 35 million) which derives 1/3rd of the companyøs overall business. Its wholesale to government business is seeing significant improvement on new government tendering policies. The company raised HK$90mn last October in a rights issue at HK$.62 to partially pay for the distribution business.

Chinaøs health care overhaul is now starting to cover the medical costs for all its citizens. In the past two years, insurance cards were issued to all Chinese enabling prescription medical drugs (versus just Chinese herb remedies) to be purchased and covered.

The newly acquired pharmaceutical distribution business will likely contribute 90% to the companyøs overall business. It seems few analysts comprehend the magnitude and far reaching implications of Chinaøs new healthcare policies. Hua Xia stands to be a major beneficiary of these new government procedures.

Revenues rose more than eleven-fold for the nine months through December to approximately HK$1.1 billion (2009: approximately HK$98.5 million). Profits of approximately HK$44 million compared to a small net loss in 2009. Earnings per share were HK4.46 cents, or, 5.9 cents annualized. The HK$350mn market capitalized company currently trades at 7.1 times estimated full year results.

Mid-sized property developer Capital Strategies (stock code 0497) is severely ignored by the market, based on several factors.

This company has a knack at spotting the potential of HK properties that they buy, renovate and sell. Their holding period is generally two to three years. The past six months has witnessed large returns. It sold a ten-storey building, AXA Centre in Wan Chai, in Kowloonøs Tsim Sha, they sold Tsui Mohan House, a shopping mall, and the International Building Shanghai, all expected to generate HK$4.7 billion in cash and gross profit of nearly HK$2.1 billion. The current market value of the company is only HK$1.85 billion, therefore, the gross profit of these four transactions is already more than the total market value of the company!

(B) From rental income and the sale proceeds from these four transactions, for fiscal years March 2011and March 2012, we conservatively estimate earnings per share of 8.6 cents and 12.2 cents, which is only a 2.6 and 1.9 PE.

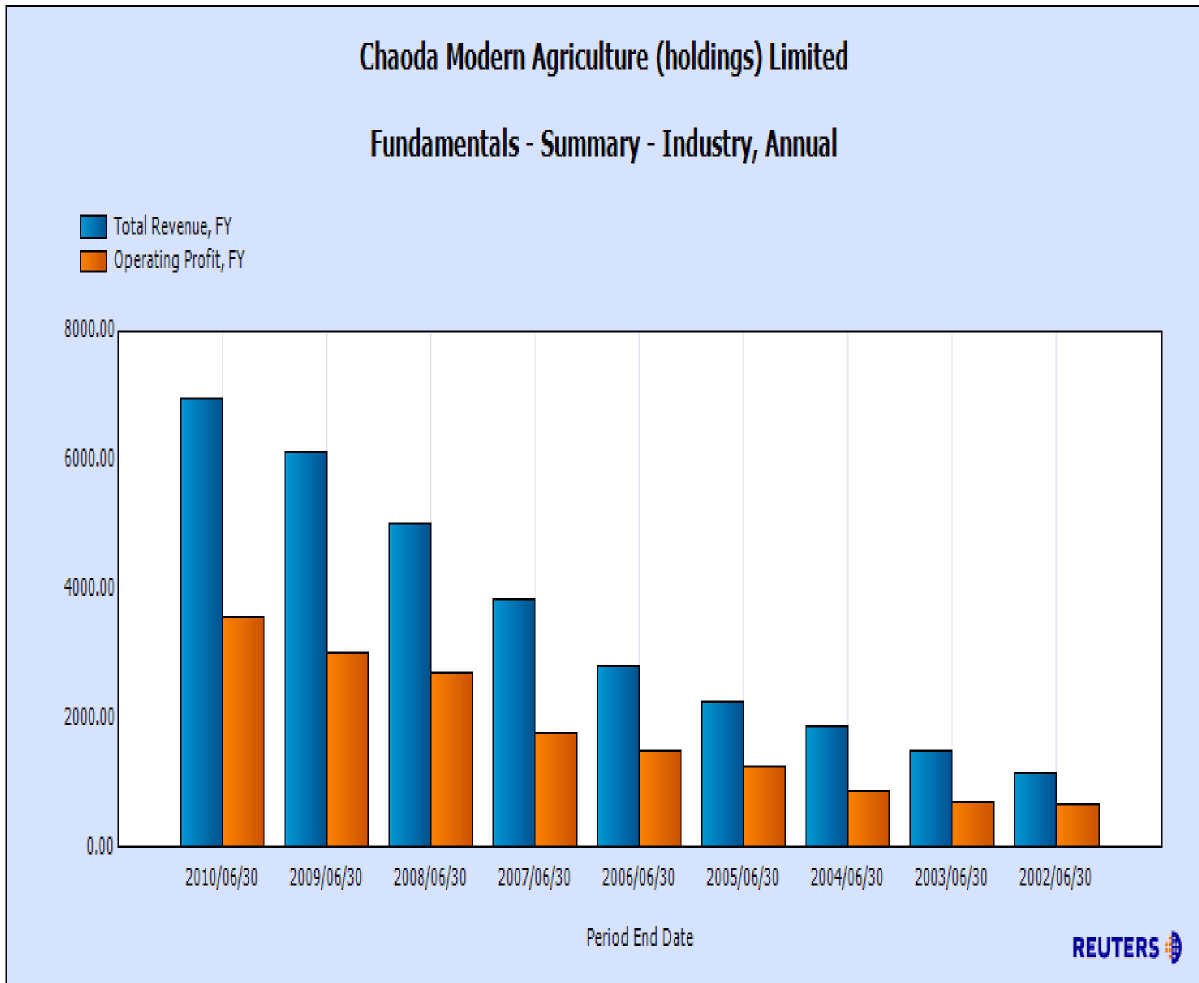
C) In the past, the companyøs policy has been to use 20% of cash profits for the dividend payout (excluding derivative instruments such as convertible debt-related gain, etc.). This should calculate out, for the next two years, dividends of 1.7 cents and 2.4 cents, or a potential dividend yield 7.5% and 10.6%.

D) The propertiesö held for saleö on the books are only recorded at cost or HK$ 0.43 book value per share. We estimate the present value of all properties to be about HK$0.90 per share. The current share price is a discount of 75% to that value! We bought at approximately HK$.23 per share.

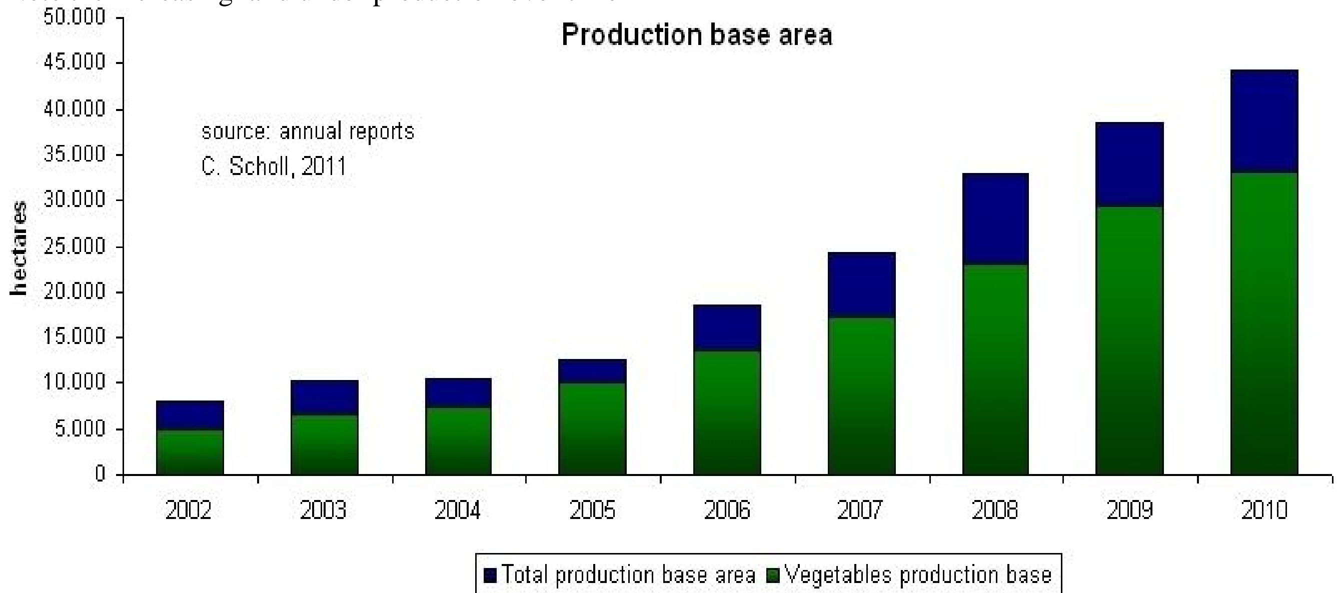
(E) The President, Zhongchu Yi, is from a local real estate family and has strong investment banking experience and background running a public company. He is a former PCCW (8) executive director for many years (now remains non-executive director) and brings a great deal of property investment and financial skill sets to a smaller, medium-sized real estate company.

We added to our largest holding, vegetable producer Chaoda Modern Agriculture, during the panic selloff, buying in at a low valuation of 2.6 times estimated June fiscal year-end earnings.

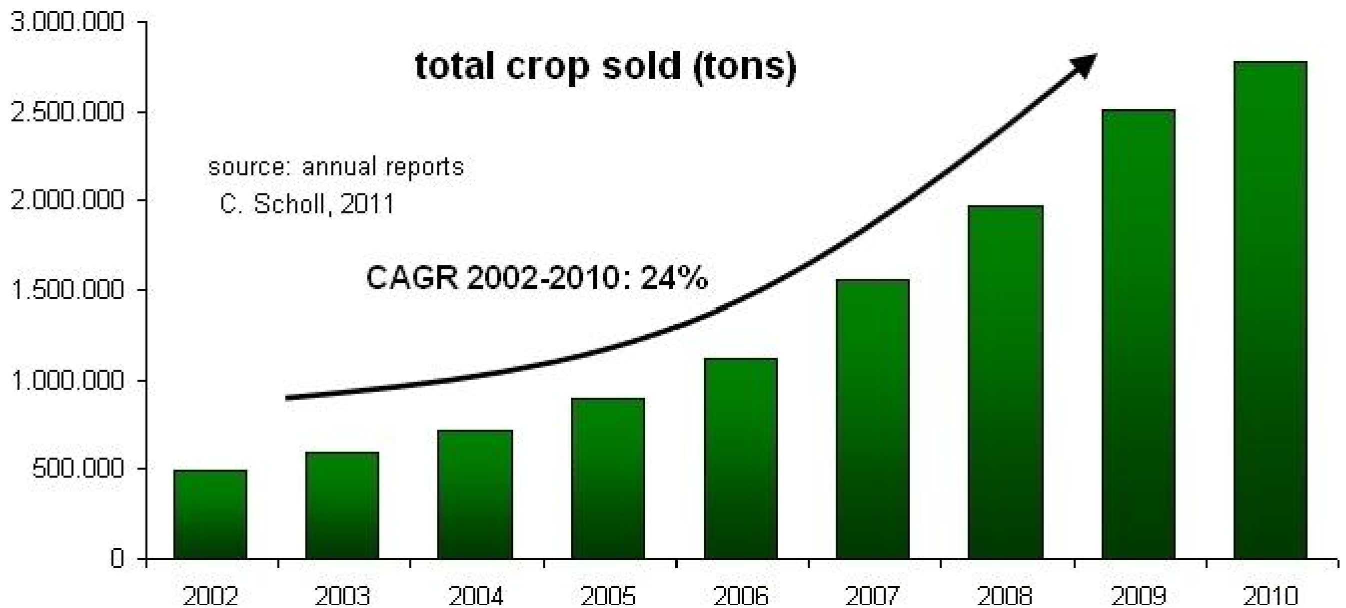
To illustrate our decision to acquire more shares, observe the progress of the company over timeí



Note the increasing land under production over timeí



The amount of production each year of crops sold has been audited over timeí



These are solid results. Chaoda continues to be a core holding in South Ocean Management portfolios. Chaodaøs two largest independent shareholders, Janus and Blackrock, were reported buying during last monthøs sell-off as well.

We realized a 30% long term profit in furniture maker, Samson, after the company posted lower net profits last year. The less than expected results left the shares selling at 16.4x trailing earnings, not a cheap ratio. The companyøs biggest market, in the US, is not vigorous for the most part (new home sales in the US for February were 443k vs. 500K+ estimated) and we are finding many single digit P/E growth stocks today to reinvest our profits.

Overall, we try to understand the underlying fundamentals of each of our companies. We get out and visit management frequently, hopefully gaining insights and convictions that can otherwise be easily lost in the ÷noiseø in the market. From our work, we believe todayøs values are more attractive than even at the bottom in 2009. Recall, just two years ago, there was zero earnings visibility and little confidence of any growth prospects.

Today, the Hang Seng Index P/E of 13 times estimated earnings this year compares to our weighted average 2011 P/E of 5 times.

We remain confident in the outlook, yet fully aware of the salty risks that sometimes prevail.

Brook McConnell
Hong Kong

*Hong Kong Partners LP risk disclaimer:

- Hong Kong Partners LP (The "Fund") primarily invests in the Hong Kong equity market with a Greater China focus.
- The Fund invests in China-related companies which involve certain risks not typically associated with investment in more developed markets, such as greater political, tax, economic, foreign exchange, liquidity and regulatory risks.
- The Fund is also subject to concentration risk due to its concentration in Hong Kong, particularly China-related companies. The value of the Fund can be extremely volatile and could go down substantially within a short period of time. It is possible that a substantial value of your investment could be lost.
- You should not make investment decision on the basis of this material alone. Please read the explanatory private placement memorandum for details and risk factors.

**Index Descriptions: The Hang Seng Indexes are a widely recognized capitalization-weighted indexes that measures the performance of the three largest-capitalization sectors of the Hong Kong stock market in descending order. The Hang Seng Index measures the largest 52 market capitalized listed companies in Hong Kong's stock market. The Hang Seng Mid Cap Index represents the next 193 largest capitalized listed companies, the Hang Seng Small Cap Index represents the next 187 largest capitalized listed companies in Hong Kong.
The MSCI HK Small Cap Index is a free float-adjusted market cap weighted index designed to measure the performance of small cap equity securities in the bottom 15% of equity market capitalization in Hong Kong. With 69 constituents, the index represents approximately 14% of the free float-adjusted market capitalization of the Hong Kong equity universe.
The Hong Kong Partners LP (HKP) is benchmark agnostic and its corresponding portfolio may have significant noncorrelation to any index. The portfolios may invest in all sectors (within and/or on other stock markets) and the composition of securities in the portfolio may change periodically depending on market conditions at the time. Securities in the portfolio will not match those in any index.
Index returns are generally provided as an overall market indicator. You cannot invest directly in an index. Although reinvestment of dividend and interest payments is assumed, no expenses are netted against an index's returns. Index performance information was furnished by sources deemed reliable and is believed to be accurate, however, no warranty or representation is made as to the accuracy thereof and the information is subject to correction.
Before investing you should carefully consider the Partnership's investment objectives, risks, charges and expenses. This and other information are in the prospectus, a copy for Accredited Investors may be obtained by inquiring to info@south-ocean.com. Please read the prospectus carefully before you invest.
The principal risks of investing in HKP: Equity Securities Risk. The value of the equity securities the Fund holds may fall due to general market and economic conditions. Foreign Securities Risk. Investments in the securities of foreign issuers involve risks beyond those associated with investments in U.S. securities. Industrials Sector Risk. Companies in the industrials sector may be adversely affected by changes in government regulation, world events, economic conditions, environmental damages, product liability claims and exchange rates. Consumer Discretionary Risk. Companies in this sector may be adversely impacted by changes in domestic/international economies, exchange/interest rates, social trends and consumer preferences. Information Technology Sector Risk. Information technology companies face intense competition, both domestically and internationally, which may have an adverse effect on profit margins. Detailed information regarding the specific risks of Hong Kong Partners LP can be found in the prospectus. Additional risks of investing in HKP include equity, market, management and non-diversification risks, as well as fluctuations in market value and NAV. An investment in a private limited partnership is subject to risks and you can lose money on your investment in the limited partnership.
There can be no assurance that HKP will achieve its investment objective. The LP's portfolio is more volatile than broad market averages. Shares of HKP cannot be bought or sold publicly, there is no active market in the Units and there are restrictions imposed on Limited Partnership unit transfers. Partnership redemptions are handled by Authorized Administrators of the Partnership.