



April 9, 2014

Dear Clients, Partners, and Friends,

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

	<u>Mar. 2014</u>	<u>Year to date</u>
Hong Kong Partners LP *	-0.3%	6.3%
Hang Seng Index **	-3.0%	-5.0%
Hang Seng Small Cap Index	-4.9%	-4.6%

Partners' NAV \$3.0313 after management fee, but before annual incentive fees of 15% on appreciation.

*Never count on making a good sale. Have the purchase price be so attractive that even a mediocre sale gives good results.* Warren Buffett

Our small/mid cap, Hong Kong-listed holdings of China-oriented stocks continued outperforming last month. We are pleased with these positive returns for the first quarter, in a muted trading environment.

We screen for quality companies selling at attractive risk/reward valuations. We seek long term gains with these great businesses.

This proprietary, systematic valuation method delivers a maximum price to buy, thereby mitigating risks.

An example is our holding in mid-cap, Li and Fung ("Something very interesting is going on in China comparable to 1979 when Deng Xiaoping opened up China," [William Fung told CNBC](#)), one of our top performers in March. Li and Fung reported that its earnings returned to record levels last year, after restructuring and management changes. The stock has been languishing at ½ its peak price, where we began purchasing, and shot up 21% on the report.

Small/mid cap stocks, generally, witnessed profit taking late last month and are, short-term, oversold.

For instance, one of our largest holdings, 4G smartphone casing manufacturer, Tongda Group (code 0698hk), declined sharply after the company opportunistically arranged an 11% placing of new shares.

Our poorest performer, magnesium PC/Smartphone casing manufacturer, Ka Shui Intø (code 0822hk), suffered a factory fire last December of which insurance coverage claims had yet to be received. The shares are deeply depressed, especially on the company's bright operating outlook for the coming years.

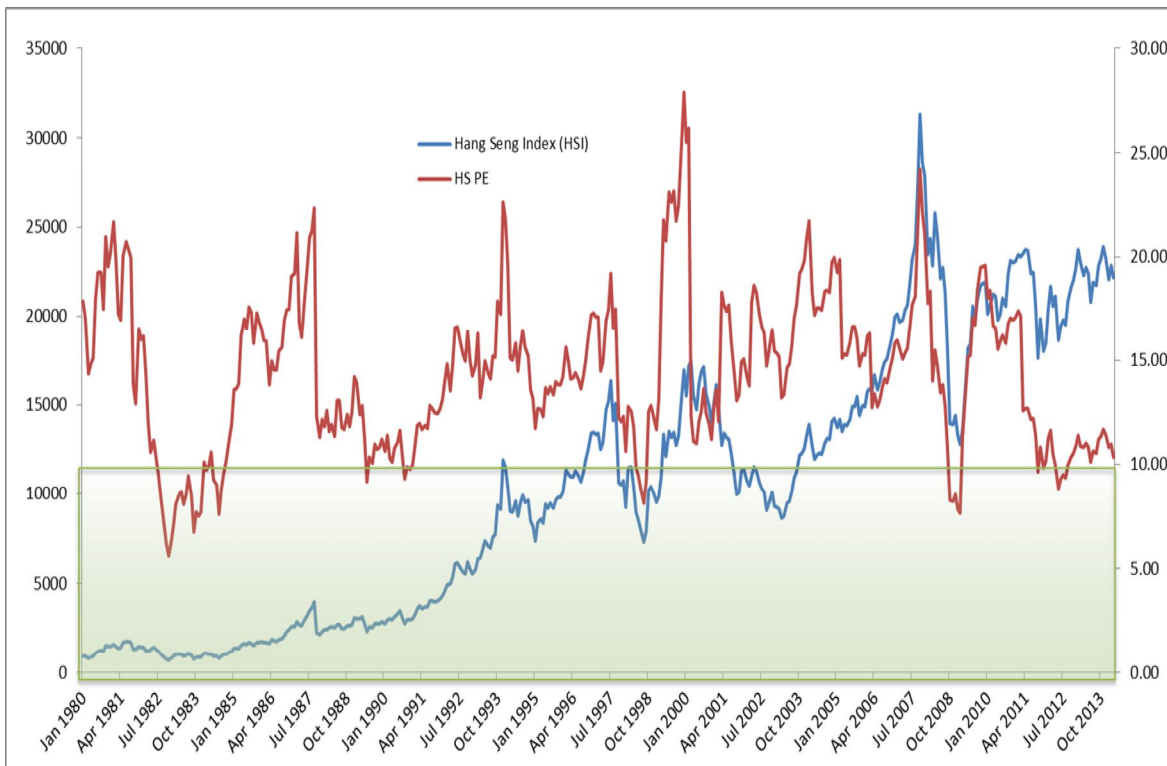
We sold Macau casino operator, Galaxy Holdings (code 0027), during the quarter after it reached our target price (TP: HK\$82), for a 130% gain in one year. Vegetable producer, Chaoda Modern Agriculture, a suspended holding, has further delayed release of its audited financials. We await further news.

A recurring theme in today's financial news is an apocalyptic bad dream about China's looming bad bank loans. As we suggested last month, with Stephen Roach's article, and more recently ([A 'Lehman moment' in China? Not quite](#)), BlackRock's Mark McCombe, chairman for Asia Pacific at BlackRock Asset Management, things that go bump in the night sometimes turn out to be less than feared.

Most of the cataclysmic headline nightmares have already been priced into the stock markets over the past 5+ years. Witness China bank stock prices trading at only 1x asset values today! China has instituted bank reforms (see our [September letter](#) regarding China's debt bubble) where higher capital adequacy ratios have already been implemented. Additionally, the PRC has recently allowed banks to issue preferred shares, thereby further increasing capital adequacy.

We are cautiously optimistic for the Mainland's macroeconomic and stock market outlook.

A chart of the Hang Seng Index overlapped with the monthly Price-Earnings ratio (right hand scale) follows. History has shown the main index has traded at a low P/E of 10 times and high of >20 times;



As we noted the end of last year, a 20 multiple on the Hang Seng's estimated earnings would equate to a 42,000 level, much higher than today's ~22,000 level.

We are fully invested in two dozen, diversified, undervalued growth stocks and, we believe, the risk/rewards remain very attractive today.

Sincerely,

Brook McConnell

President

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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](mailto: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.