SOUTH OCEAN 南海管理有限公司

MANAGEMENT, LTD.

HONG KONG

June 9, 2015

Dear Clients, Partners, and Friends,

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

	May 2014	Year-to-date
Hong Kong Partners LP *	4.0%	35.1%
Hang Seng Index **	-2.5%	16.2%
Hang Seng Small Cap Index	3.2%	37.5%
MSCI HK Small Cap Index	2.4%	16.3%

Partnersô NAV $3.8267 after management fees, but before annual incentive fees of 15% on appreciation.

South Oceanôs portfolios of quality, small/mid cap, Hong Kong-listed companies, with earnings geared towards Chinaôs growth, continued to advance last month. We use an intrinsic value investment approach similar to Warren Buffett/Charlie Munger which enhances and systematizes our original price to growth (PEG) investment strategy that South Ocean has used since our 1992 founding in Hong Kong. Our investible universe has expanded and, by setting a maximum price limit to buy, we can sleep soundly. Since launching this internally-developed, software program, the results have been gratifying;

Period 12/31/2012 through 5/30/2015*

Hong Kong Partners LP (after March 2013 write-downs)	+52.6%
Hang Seng Index	+21.0%
Hang Seng Small Cap Index	+42.6%

Chinaôs stock markets have witnessed extraordinary gains this year, yet, Hong Kong still lags. Part of this yearôs stock rallies has been the anticipation of economic stimulative policies by the Peopleôs Bank of China (PBOC). We believe there are more enduring, major supports to the long term sustainability of the markets and economy even in the absence of any further imminent lowering of interest costs.

Chinaôs bull market in also driven by a myriad of financial reforms and deregulation as the government wants a ôhealthyô stock market. As highlighted a year ago (See April 2014 client letter; Itôs Different This Time), China is structurally under-owned by foreign investors and, now, the floodgates are opening. Recently, the FTSE Russell, one of the worldôs largest index providers, has launched two indexes that include China A-shares. The MSCIôs inclusion of China A-shares will see long-lasting capital inflows of passive liquidity into the mainland market.

But, we envision a far more promising outlook, even after China completely opens its capital account.

From this Americanós perspective, the environment today in China is reminiscent of the US in the early 80s (see [last monthós](#) commentary on the 1982 US bull market). Common stocks were shunned just as the long bear market in US equities came to an end, despite concerns of inflation-ravaged corporate balance sheets, stag-flation, an energy crisis, 20% interest rates and dire economists, such as Henry Kaufman.

The early 80ós hatched an era of considerable financial innovations and productivity. Banking regulations were eased to relieve dying savings banks (Glass-Steagull Act/Gramm-Leach-Bliley Act) as newfangled money market funds caused ódisintermediationô. ñNeutronò Jack Welch took over GE and instituted managerial reforms to the stodgy, bureaucratic Dow Jones Index company. Between 1981 and 2001, during his tenure at GE, the company's value rose 4,000%. Michael Eisner was brought in as CEO of the Walt Disney Company in 1984. Disney was revitalized as Eisner re-invigorated the Disney brands and ómonetizedô the vast assets of the Disney library.

Mike Milken, (the óJunk Bond Kingô)

> "…was a key source of the organizational changes that have impelled economic growth over the last twenty years, "stated George Gilder in *Telecosm* 2000. "Most striking was the productivity surge in capital, as Milken...and others took the vast sums trapped in old-line businesses and put them back into the markets."

Ted Turner of Turner Network News (now, CNN) was just one of the recipients of Milkenós financing who built an empire through high-yield bonds (together with the National Geographic Jacques Cousteau series).

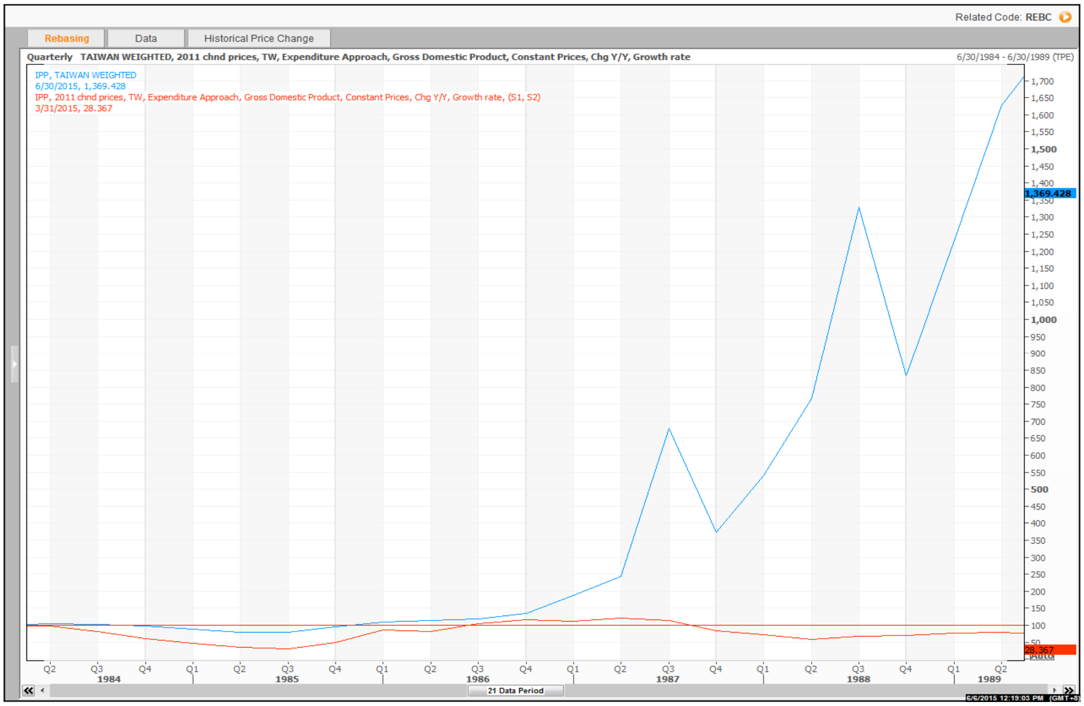
Those ripe conditions are prevalent in China today. Entrepreneurs will appear (already, such names today as Jack Ma of Alibaba/Alipay, Peony Ma of Tencent and Guo Guangchang of Fosun have emerged) and will transform Chinaós vast industrial complex and New Economy to heights previously thought unattainable.

The PRCós monumental reforms taking place are all brand new:

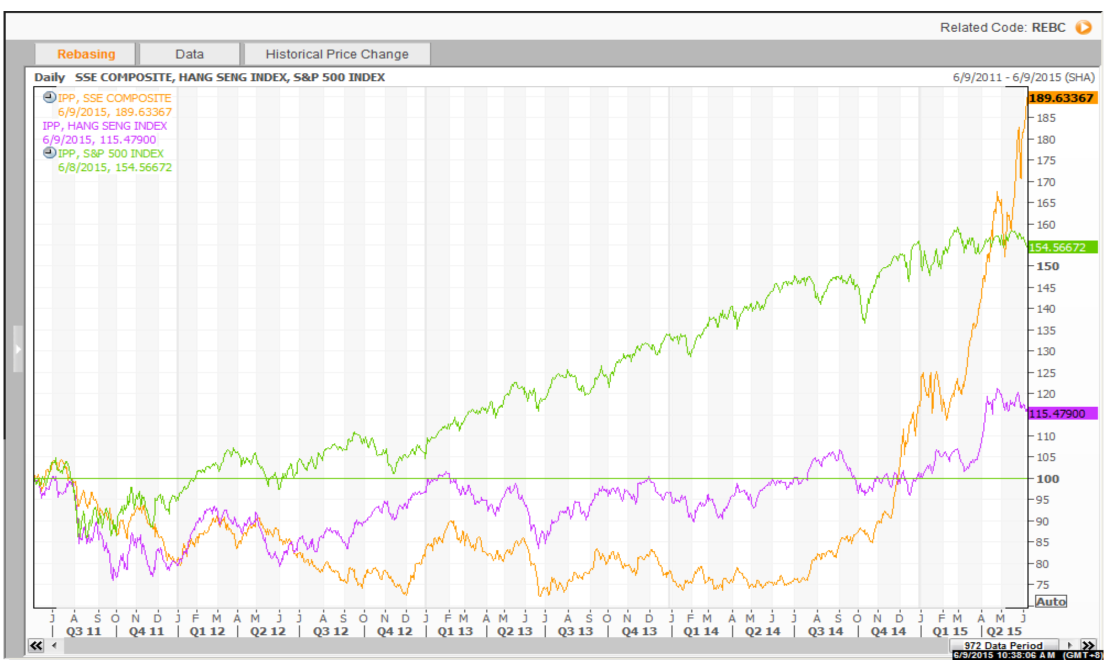
> "Made in China 2025" (explained in more detail **here**, transforming China from a manufacturing giant into the world's leading manufacturing superpower),
>
> The Silk Road Economic Belt, The Maritime Silk Road (see our September 2014 client letter),
>
> The China-led Asian Infrastructure Investment Bank,
>
> The "One Belt and One Road", (China's Marshall Plan, a far-reaching initiative concerning 65 countries and 4.4 billion people and is one of China's most important and strategic initiatives).

The deep-seated, outdated PRC centralized mindset is being radically overhauled. The reform programs have yet to be digested and are vastly under-rated by investors. Just imagine the efficiencies that could be brought to bear in Chinaós old enterprises coupled with the powerful emergence of Chinaôs New Economy (technology, robotics, biotech/healthcare)! The forward looking stock market is just beginning to react.

Economists today continuously fret that the stock markets have advanced too much and point out that Chinaôs economy has been slowing. But, note what happened to Taiwanôs stock market (blue line) in the 1980s as its economy (orange line) slowed:



The Hang Seng Index has yet to reflect the positive events and changes occurring today. It has underperformed both the S&P 500 (green line) and Shanghai Composite (yellow line) in the past 4 yearsé and needs to advance higher over the coming months just to catch up:



Granted, we hold a positive outlook. Pessimism always sounds more sophisticated than optimism: the end of the Adam and Eve mythos and Armageddon forecast over and over again (just pick up any paper today and read the ominous headlines!).

However, look at where China has come in the past 30 yearsé   the most colossal increase in living standards in the history of mankindé and, if that is a sign of a collapse, then letôs have more of it.

We reiterate points in our May 14th, inter-month email:

We think this bull-run in China will last longer than most analyst suspect, with far better RISK/REWARD fundamentals than at any time we have perceived in our 23 years investing here. Why?

1) Valuations in Hong Kong remain cheap as the Hang Seng Index sells at 13 times trailing earnings.

2) The economy is weak and inflation is subdued, especially in the past bubbly property sector, which is positive for stocks, because;

3) After three decades of tight money, monetary policy is stimulative (China's PBOC has been fighting inflation since June 1989, Tiananmen Square, which was primarily about rampant inflation);

4) Beijing authorities seek to channel savings (household savings of US$7 trillion) into investment and not just real estate, to allow further privatization of state assets, via IPOs, venture capital, merger activities.   This will channel capital to productive, private companies and allow bad companies to wither (China's reformers are mostly officials aged 28-45 who have attended Western business and economic programs, and they DO have reasonable outlines by which to direct this capital. President Xi Jinping is a comprehensive, pragmatic reformer: China benefits);

5) The stock connect between Hong Kong and Shanghai and Shenzhen exchanges is a dramatic step in this structural change; Beijing aims to brand the Yuan, the fifth most-used payment legal-tender, a reserve-currency status, an epic event, which could occur sooner than expected by investors.

6) As we've been citing for years, global investors are non-existent in China indexes, and are EXTREMELY underweight China. As the government (central and municipal) sells down its ownership stakes in companies, free floats will rise, increasing China's percentage of global benchmarks, further forcing foreign investors to 'chase' the indices higher. This has happened time and again, in emerging markets, such as Japan in the 80's.

7) Higher equity valuations permit companies to pare down borrowings. Margin debt in China is roughly 2-3% of total market capitalization, about the same percentage as with the NYSE.

The countdown has finished, thereôs an ignition, and this space shuttle launch is finally set for outer space.

Please consider joining (or adding to) our investment program to invest alongside myself and our limited partners, which is available for US and non-US accredited investors (ask Joyce for material on Hong Kong Partners LP at joyce@south-ocean.com before making any decision).

All aboard.

Sincerely,

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

PS: The importance of the China reforms taking place has even been overlooked in this community.

The front page of the local English paper, Saturday, 23 May, 2015, displayed this exuberant group photo:

"The anticipated launch of the Shenzhen-Hong Kong Stock Connect will spur the inclusion of A shares in the widely tracked MSCI index series and trigger billions of dollars of global fund flows into mainland equity markets, ***experts*** told the *South China Morning Post's* Redefining Hong Kong seminar yesterday…"

A year ago, there was nary a word from these œexpertsô when the stock connect program and major reforms were being introduced. In fact, the Hong Kong monetary authority warned inflows of money into Hong Kong (stock market) could turn quickly to outflows last August. The Financial Secretary (John Tsang) warned at that time of a "perfect financial and economic storm," for Hong Kong.

Despondent yesterday, giddy today. Sentiment changes on a dime in Hong Kong. Short-sighted œexpertsô are the norm in Hong Kong, and is an advantage to perceptive investors.

*- Past performance, as the regulators maintain we must emphasize, is no guarantee of future performance.

*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.