



December 8, 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>Nov 2014</u>	<u>Year to Date</u>
Hong Kong Partners LP	-1.4 %	4.4%
Hang Seng Index	0.0%	2.9%
Hang Seng Small Cap Index	0.0%	-4.8%

Partners' NAV \$2.9772 after management fee, but before annual incentive fees of 15% on appreciation.

Our China-focused portfolios of small/mid cap, Hong Kong-listed holdings decreased slightly in November. A surprise interest rate cut by the People's Bank of China propelled large cap stocks upwards, with a gap opening of 400+ points. As we've noted, credit conditions have been tight in China, and the authorities have room to cut further. Daily rumors of additional China stimulus measures buffeted the market all during the month.

The Occupy Central protests in Hong Kong, sadly, turned violent as court-ordered injunctions to remove street barricades resulted in baton-wielding police clashing with masses of protestors. Global news carried graphic scenes of the late night skirmishes.

Community fatigue, after 60 days of Hong Kong-government inaction, has exasperated the mounting intolerance, on both sides. The PRC Mainland government has resolutely stood firm against any change to its August 31<sup>st</sup> proclamation on Hong Kong's [suffrage](#).

Frustration with the continued unrest was cited as a possible reason for a sudden stock market retreat of 600 points on December 1 (filling in that previous gap opening). After the close on that day, the government reported Hong Kong retail sales expanded at a slow 1.4% year-on-year pace for October, likely aggravated by the Occupy movement. Investors have been avoiding local retail stocks since late summer on concerns of slower sales (a sector we have no exposure). Certainly, the Occupy situation hasn't helped market sentiment.

The anti-graft campaign in China, though, has had a greater impact on local luxury retail sales during October (than have the protests), as expensive gifts are a no-no under PRC President Xi. The new leader's unprecedented [anti-corruption campaign](#)\* in China has been ongoing for two years, but western media speculation regarding the SAR's student protests of a China-led, Tiananmen Square-like crackdown never materialized. In fact,

Beijing gave final approval on November 17<sup>th</sup> to the historic Shanghai-Hong Kong stock connect program (see my April comments on the Hong Kong/Shanghai stock connect [here](#)).

The Occupy Central impasse seems to be waning, as of this writing. Business confidence will rebound, as it did, for example, in Bangkok earlier this year after the yellow-red shirt clashes simmered down. Although it's been an inconvenience getting around town these past two months (travelling to the business district of Central takes longer in the snarled traffic), I can't complain; I have been in overall support of the students' rallying message (see my September comments [here](#)).

It's been our experience that small/mid cap stocks commonly lag sudden surges in the large, Index stocks when government policy measures or interest rate cuts are announced (and, we clearly have no way to get in front of these announcements, either). We are adding to our holdings during this period.

A year-end review will be forthcoming soon after New Year's.

A very *peaceful* and happy holiday season to all.

Sincerely,

Brook McConnell

President

Email: [brook@south-ocean.com](mailto:brook@south-ocean.com) Website: [www.south-ocean.com](http://www.south-ocean.com)

Hong Kong

### **\*Juicy scandals await as case unfolds**

**Xinhua News Agency broke the news at the stroke of midnight on Friday that former security tsar Zhou Yongkang had been expelled from the Communist Party and formally arrested on a number of serious charges.**

Mary Ma

*Monday, December 08, 2014*

Xinhua News Agency broke the news at the stroke of midnight on Friday that former security tsar Zhou Yongkang had been expelled from the Communist Party and formally arrested on a number of serious charges.

For the public, the accusation that Zhou had extramarital affairs and traded his power for sex was the juiciest.

He was said to have kept at least 29 mistresses, including many hotties at state television broadcaster CCTV.

Concerns had been raised that President Xi Jinping may have met resistance in his corruption fight, after the party's fourth plenum made no mention of the Zhou case in its communique.

Xinhua's announcement showed Xi has now cleared the hurdles in dealing with the prized "tiger."

Although much was previously rumored, the announcement was highly titillating.

It cited six sins allegedly committed by Zhou that included serious violation of party discipline.

He is further accused of taking advantage of his posts and accepting bribes, abusing his power to help relatives, mistresses and friends to make huge illicit profits resulting in serious losses of state owned assets.

Zhou also allegedly leaked party and national secrets. But as said, the most salacious accusation was committing adultery and trading power for sex and money.

In addition, investigators reportedly found evidence of other suspected crimes.

US President Barack Obama recently noted that Xi has managed to consolidate power more quickly and comprehensively than anybody since the late paramount leader Deng Xiaoping.

While, it's a matter of opinion whether this is a good or bad thing, it's nevertheless fair to say Xi has amassed the political and military muscle that his immediate predecessor Hu Jintao wanted but had failed to garner.

Without this clout, his high-profile fight against corruption would have been doomed to failure.

The arrests of Zhou and that of former central military vice chairman Xu Caihou showed Xi has arrived.

Zhou's arrest is also significant in the sense that it has broken the norm of Politburo standing committee members being immune to criminal liability.

Xi has set a new standard - that even the highest ranking officials are accountable.

That's an important breakthrough.

It's uncertain whether Zhou's trial will be held openly.

In the case of former Chongqing party secretary Bo Xilai, the public was treated to the defiant defense he staged in court. But Bo wasn't accused of leaking party and state secrets.

If Zhou is tried openly, would party and national secrets be revealed?

Xinhua said Zhou's behavior badly undermined the reputation of the party, and significantly damaged the cause of the party and people, leading to serious consequences. It's possible for the 72-year-old to face a death sentence.

The revelation by Xinhua that investigators also found clues of other suspected crimes has created room for imagination to run amok.

Could the evidence be related to rumors that Zhou was linked to the motor vehicle death of his first wife? Or could they be about something more sinister?

## **A general and his battalion of lovers**

[http://www.thestandard.com.hk/news\\_detail.asp?pp\\_cat=30&art\\_id=152127&sid=43500851&con\\_type=1&d\\_str=20141208&isSearch=1&sear\\_year=2014](http://www.thestandard.com.hk/news_detail.asp?pp_cat=30&art_id=152127&sid=43500851&con_type=1&d_str=20141208&isSearch=1&sear_year=2014)

## **Sex, money and power claims against Zhou**

[http://www.thestandard.com.hk/news\\_detail.asp?pp\\_cat=30&art\\_id=152128&sid=43500625&con\\_type=1](http://www.thestandard.com.hk/news_detail.asp?pp_cat=30&art_id=152128&sid=43500625&con_type=1)