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

9 Aug 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:

	July 2015	Year-to-date
Hong Kong Partners LP	-10.4%	14.3%
Hang Seng Index	- 6.1%	4.4%
Hang Seng Small Cap Index	-18.4%	-0.4%
MSCI HK Small Cap Index	-11.1%	-5.5%

Partnersô NAV $3.2367 after management fees, but before annual incentive fees of 15% on appreciation.

Our holdings of Hong Kong listed small/mid capitalized stocks, with earnings geared towards China, witnessed increased volatility due to the China market sell-down.

The sharp correction in Hong Kong during June and July has now settled into much slower trading volumes as the mid-summer doldrums have set in. As of this writing, investors await financial earnings releases for the first half ending June before making any commitments.

To recap recent events, Shanghai stocks lost a third of their value in the three weeks to July 9. Conflicting central bank signals were partially to blame. In early June, the Peopleôs Bank of China (PBOC) drained funds from the countryôs financial system in the heat of the stock rally. That led investors to believe the central bank was tightening monetary policy.

Heavily leveraged China investors started selling. The official data of total margin borrowing from brokerages did not include money borrowed by investors from unofficial channels such as banks and Internet finance firms. As the selloff worsened in early July, triggered by heavily indebted investors rushing for the exit, the central bank had to step in to make cash available to brokers to expand margin lending to investors.

The sell-off forced the PBOC to announce ¼ point interest rate cut coupled with a loosening of some banksô reserve requirements on June 27 to spur lending. In the two weeks to July 20th, Beijing announced further initiatives to stem the downturn. The China Securities Finance Corp lent US$ 42 billion to 21 brokerages to buy stocks. The Commission further promoted bank lending to companies in order to buy their own shares.

Financial experts in the media were panic-stricken, claiming China was about to crash the world economy. But worries about the stock market rout causing a hard landing on the mainland are overblown.

Stocks account for about 9 percent of total household wealth in China, and major market indices are still higher on the year, so relatively few Chinese have been severely affected. Household income, wages and consumption are going up at a vigorous rate, and banks do not look seriously exposed to the rout.

There are certain areas in Chinaôs economy, such as in the industrial sectors, that are witnessing flat growth. Other sectors are strong, such as insurance, transportation and utilities. While we have no idea when the massive reform measures taking place in China today (moving from a central controlled economy to a market-led economy, recent interest rate cuts) will kick in, there certainly are reasons to believe the economy is seeing some improvements in this rough environment: China housing prices have turned up this year, the Caixin Services PMI, a measure of the service sector, hit an 11 month high in July (service sectors accounted for 51.6% of total GDP in the first quarter of this year, up from 46.9% in 2013 and 48.2% in 2014) and retail sales grew 10.6% in June versus 10.2% in May. (Interestingly, mobile e-commerce in China is expected to make up 11% of total retail sales next year and over half of total online retail shopping. This phenomena is only just beginning as the huge number of Chinese in the rural market has yet to be tapped. China is currently 22% of world Internet usage versus 8% in India and 10% in the U.S.)

Leading economic indicator, The Baltic Dry Index, is up 54% year-to-date.

The sell-off in China has unsettled investors, globally. Foreign ownership of China shares has dropped dramatically. There were 9 consecutive days in July of net money outflows from China, through the Shanghai Hong Kong stock connect, amounting to more than US$8 billion. Miss-steps by China authorities/regulators are unlikely to be repeated in Hong Kong. Hong Kong is not China. Hong Kong has an independent securities regulator (SFC) and a self-regulating, listed stock exchange. The PRC securities market loopholes and miss-steps by the regulators are part of the learning curve for China to create a fully functioning market.

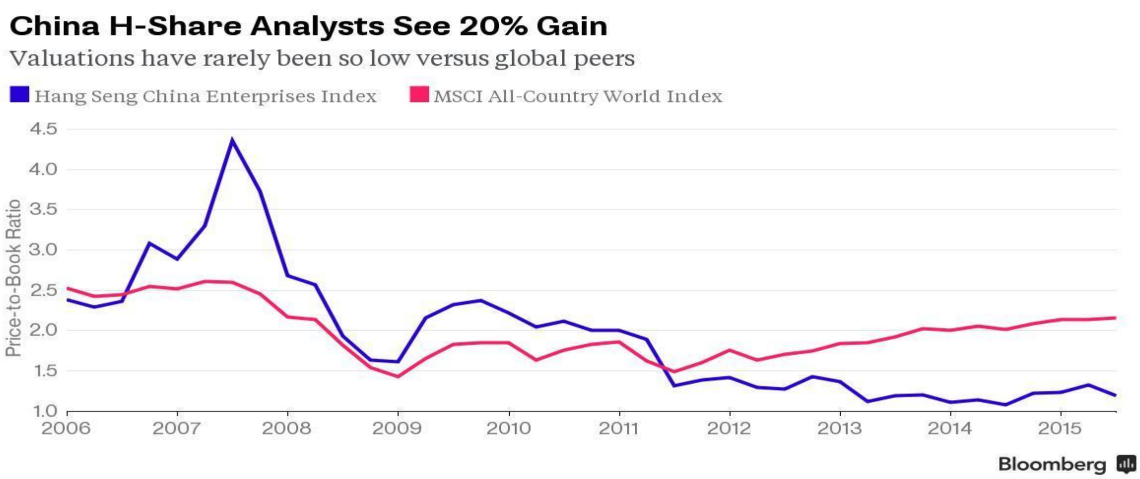
An in-depth review of the China equity markets in Institutional Investor is reported here. Nevertheless, the Chinese authorities (as Europeôs central banking once said) are doing ñwhatever it takesò to stem the rout. The Peopleôs Bank of China is essentially pledging unlimited credit support to keep buying battered shares and lending to securities firms.

With Hong Kong stock prices sold down this far, Hong Kong stocks, along with China shares traded in Hong Kong, are the cheapest in the world today, using Price to Earnings and Price to Book valuations.

The following chart from Reuters shows world index valuations:

Americas 03-Aug-2015							
Name	**Last**	**Div Yld %**	**PE**	**PE FY1**	**PE FY2**	**PBook**	**Mcap USD**
S&P 500	2,103.84	2.4	19.39	17.39	15.86	2.72	19.40T
DJI	17,689.86	2.49	16.01	15.92	14.65	3.07	5.42T
NASDAQ 100	4,588.91		21.49	19.55	18.43	4.8	5.47T
S&P/TSX	14,468.44	3.39	16.94	16.57	14.61	1.87	1.55T
BOVESPA	50,864.77	4.66	12.72	11.85	10.41	1.29	504.98B
MXSE IPC	44,752.93	1.9	23.87	20.57	16.94	3.53	313.56B
Europe							
Name	**Last**	**Div Yld %**	**PE**	**PE FY1**	**PE FY2**	**PBook**	**Mcap USD**
STXE 600	396.37	3.28	17.63	16.6	15.07	1.94	11.27T
FTSE 100	6,696.28	4.15	15.93	16.04	14.71	1.81	2.90T
DAX	11,308.99	2.63	16.9	14.07	12.89	1.85	1.20T
CAC 40	5,082.61	3.02	20.06	16.12	14.52	1.62	1.53T
FTSE MIB	23,538.03	2.73	26.07	17.43	14.61	1.25	537.97B
SMI	9,428.17	2.94	17.01	18.51	16.99	2.92	1.24T
AEX	495.23	2.73	17.67	17.96	15.76	1.71	611.86B
IBEX	11,180.70	5	17.39	16.29	14.18	1.62	709.53B
OMXS 30	1,615.64	3.72	15.05	16.78	15.5	2.42	602.63B
Asia							
Name	**Last**	**Div Yld %**	**PE**	**PE FY1**	**PE FY2**	**PBook**	**Mcap USD**
NIKKEI 225	20,492.53	1.43	20.69	19.62	17.66	1.92	3.06T
S&P/ASX 200	5,680.40	5.95	14.33	15.97	14.94	1.78	1.13T
HANG SENG	24,502.49	3.27	11.53	12.94	11.82	1.45	1.96T
H-Share	11,038.13	3.62	8.33	8.14	7.33	1.21	767.87B

China shares traded in Hong Kong have witnessed almost panic selling the past month and today sell at historic relative discounts.



China H-Share Strategists See 20% Gain on Cheap Valuations
http://www.bloomberg.com/news/articles/2015-07-16/china-h-share-analysts-see-20-gain-on-valuations-rarely-so-low

On a 5-10 year outlook, the US stock and bond markets are priced for low returns. China will remain the worldôs largest source of economic growth during the next five years and the risk gain ratio of buying and owning Hong Kong stocks at these levels are compelling today.

For instance, we are buying shares in a retail operator in China listed in Hong Kong with a market capitalization of US$810 million and revenues last year of US$715 million. The seasoned company has closed loss making stores on the mainland, a market that has witnessed an extremely challenging retailing environment since the 2008 Beijing Olympics. Huge operating leverage will benefit the bottom line when the retailing cycle turns. The companyøs balance sheet is clean with ~HK$900 million net cash. Its management is very shareholder friendly, producing an annual report that is one of the most transparent descriptions of any companyøs operations Iøve read here in Hong Kong. The dividend yield is over 6%, return on equity is a decent 14%. The stock is selling at 2.5x book, which is low for a retailer. Our 10 year price target, assuming a modest 6.3% compound annual growth in earnings per share, is calculated, using our proprietary Banquet System intrinsic value analysis program, at HK$28 per share. We started buying at $4.01 or 14.3 times this yearøs estimated earnings.

Our concentrated portfolios of small/mid cap, Hong Kong listed stocks have an average ROE of 15.8%, sell at a weighted average 8.8 times expected earnings, 1.8 times book value, with an average 4.7% dividend yield and strong balance sheets.

Sincerely,

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Here is an eye-opening clip of Chinaøs ambitions; **China opens world's largest single structure**. http://youtu.be/tn9hoo6cZFc).