July 1, 2013, Mumbai

Facilities	Amount	Rating
Non Convertible Debenture (NCD) Issue*	**Rs. 50 Cr**	**SMERA AA- (SO)/Stable (reaffirmed)**
Non Convertible Debenture (NCD) Issue*	**Rs. 40 Cr**	**SMERA AA- (SO)/Stable (in-principle, assigned)**

**Credit enhancement on account of an unconditional and irrevocable guarantee given by the Government of Karnataka (GoK)*

SMERA has assigned an in-principle rating of '**SMERA AA- (SO)' -** read as **double A minus structured obligation,** to The Mysore Paper Mills (MPM) Limited's Rs. 40.0 crore NCD issue and reaffirmed its ratings on the other debt instruments. The outlook remains **'Stable'**. The ratings continue to draw core support from the GoK's unconditional and irrevocable guarantee extended towards the timely payment of principal and interest on the NCD. The ratings accordingly reflect GoK's credit risk profile.

The in-principle ratings are provisional and the final rating is subject to the execution of an unconditional and irrevocable guarantee to be extended by GoK for timely payment of interest and principal on the instrument and execution of a trust deed (with a SEBI registered trustee) which clearly outlines the payment mechanism, escrow mechanism and rights and obligations of various parties involved in the issuance.

The ratings also centrally factor in adherence to a specific, legal payment mechanism administered by the trustee of the NCD. The payment mechanism for the ten year bond (Rs. 40 cr issue with a call option at end of seven years) is as follows:

- At least seven days prior to the forthcoming due date (T) for interest or principal payment (T-7), MPM shall credit the requisite funds in the Trust & Retention Account (TRA) for servicing the bond holders on the forthcoming due date "T" or put them in a fixed deposit with a designation bank.
- If MPM fails to do so, it will inform GoK about the same.
- In case MPM fails to intimate GoK as required, the trustee shall intimate GoK.
- In shortfall in the TRA persists till three days before the due date, the trustee will invoke the guarantee.
- On invocation of the guarantee, GoK must promptly deposit clear funds, to the extent of shortfall, into the TRA

SMERA believes GoK's credit profile benefits from healthy fiscal and economic parameters. The state's deficit and indebtedness levels are within targets laid down by the Thirteenth Finance Commission (ThFC).Karnataka has successfully maintained a revenue surplus throughout the last three years despite an economic slowdown and pay commission revisions.

The state's revenue surplus increased to 1.05 percent of Gross State Domestic Product at current prices (GSDP) for 2011-12 (accounts), as compared with 0.47 percent for 2010-11. The fiscal deficit reduced to 2.68 per cent for 2011-12 as compared with 3.16 per cent respectively a year ago. The overall indebtedness (debt + guarantees) to GSDP stood at 25.25 per cent as on March 31, 2012, as compared with 24.71 per cent a year ago. For the financial year 2012-13, the revenue surplus is budgeted at 0.2 per cent (BE) and the fiscal deficit is pegged at 2.9 per cent (BE).

Karnataka also benefits from a high tax revenues (own taxes + share in central taxes and duties) to GSDP ratio. The ratio improved to 13.25 per cent for 2011-12 (accounts) as compared to 12.03 per cent a year ago. Sales tax and state excise duty accounted for over 75 per cent of total tax revenues. The state has a tertiary sector contribution of over 56 per cent of gross state domestic product (GSDP).

However, the state will find it difficult to achieve a higher level of tax buoyancy as it has reached a high tax to GSDP ratio. Also, considering only 30 per cent of the net sown area is irrigated, Karnataka's dependence on south west monsoon is high.

Outlook: Stable

In SMERA's opinion, GoK's credit profile is underscored by healthy economic parameters and sound fiscal profile. A consistent improvement or deterioration in the fiscal and economic ratios of the state could lead to a revision of its outlook to either positive or negative.

About MPM

MPM founded by Sri. Krishnaraja Wodeyar Bahadur (Maharaja of erstwhile Mysore State) in 1937. It became a government company in 1977 under Section 617 of the Companies Act, 1956. The company has its registered office at Bangalore and its plant is located at Shimoga district in Karnataka. GoK has a shareholding of 65 percent, various financial institutions 18 percent and the general public shareholding is 17 percent in the company. MPM has 4000 employees.

MPM is an ISO-14001-certified company, producing newsprint, writing, printing and packaging paper and also manufactures white sugar. The company has an installed capacity to produce 75,000 tonnes per annum (tpa) of NP and 30,000 tpa of WPP; it has sugarcane crushing capacity of 2500 tonnes per day. MPM has a sugar factory as an integrated part of a paper mill, wherein bagasse, a sugar by-product, is used as raw material for manufacturing WPP. The company also has a captive power plant.

For 2011-12 (refers to financial year ended March 31), MPM reported a net loss of Rs.76.86 crore on total income of Rs. 381.14 crore, against a net loss of Rs.84.78 crore on total income of Rs.337.50 crore for 2010-11. As on March, 31, 2012 MPM's net worth stood at a negative Rs.46 crore. During fourth quarter of 2011-12, GoK has concurred for conversion of an existing government loan of Rs.101 crores extended to MPM into equity, and further infused equity capital of Rs.5 crores in MPM. For the nine months ended December 31, 2012, MPM has reported, a net loss of Rs.49.8 crore on total income of Rs.293.3 crore, against a net loss of Rs.58.5 crore on total income of Rs.254.6 crore for the corresponding period of the previous year.

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