

XERIUM TECHNOLOGIES INC
Form 10-Q
November 06, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended September 30, 2013

Or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from _____ to _____
Commission File Number 001-32498

Xerium Technologies, Inc.
(Exact name of registrant as specified in its charter)

DELAWARE
(State or other jurisdiction of incorporation or organization)

42-1558674
(I.R.S. Employer Identification No.)

14101 Capital Boulevard
Youngsville, North Carolina
(Address of principal executive offices)
(919) 526-1400
(Registrant's telephone number, including area code)

27596
(Zip Code)

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input checked="" type="checkbox"/>

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

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Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes No

The number of shares of the registrant's common stock, \$0.001 par value, outstanding as of November 1, 2013 was 15,380,507.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Xerium Technologies, Inc.
 Consolidated Balance Sheets
 (Dollars in thousands)

	September 30, 2013 (Unaudited)	December 31, 2012
ASSETS		
Current assets:		
Cash and cash equivalents	\$48,782	\$34,777
Accounts receivable, net	92,985	84,456
Inventories, net	81,417	77,391
Prepaid expenses	7,531	9,386
Other current assets	13,436	14,839
Total current assets	244,151	220,849
Property and equipment, net	292,957	308,806
Goodwill	66,060	61,127
Intangible assets	15,203	18,678
Other assets	8,535	9,383
Total assets	\$626,906	\$618,843
LIABILITIES AND STOCKHOLDERS' DEFICIT		
Current liabilities:		
Notes payable	\$8,120	\$7,911
Accounts payable	31,298	36,884
Accrued expenses	74,191	59,757
Current maturities of long-term debt	2,139	2,397
Total current liabilities	115,748	106,949
Long-term debt, net of current maturities	432,910	434,684
Deferred and long-term taxes	16,061	16,582
Pension, other post-retirement and post-employment obligations	81,252	83,949
Other long-term liabilities	6,304	5,740
Commitments and contingencies (Note 9)		
Stockholders' deficit		
Preferred stock, \$0.001 par value, 1,000,000 shares authorized; no shares outstanding as of September 30, 2013 and December 31, 2012	—	—
Common stock, \$0.001 par value, 20,000,000 shares authorized; 15,380,507 and 15,309,717 shares outstanding as of September 30, 2013 and December 31, 2012, respectively	15	15
Stock warrants	13,532	13,532
Paid-in capital	414,151	413,124
Accumulated deficit	(413,128	) (413,839
Accumulated other comprehensive loss	(39,939	) (41,893
Total stockholders' deficit	(25,369	) (29,061
Total liabilities and stockholders' deficit	\$626,906	\$618,843
See accompanying notes.		

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Xerium Technologies, Inc.

Consolidated Statements of Operations and Comprehensive Income (Loss) (Unaudited)

(Dollars in thousands, except per share data)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2013	2012	2013	2012
Net Sales	\$ 135,042	\$ 134,231	\$ 413,171	\$ 404,973
Costs and expenses:				
Cost of products sold	81,656	85,079	252,628	258,396
Selling	17,242	18,546	53,349	57,104
General and administrative	15,278	15,650	45,418	47,509
Research and development	2,382	2,700	7,634	8,531
Restructuring	3,034	5,840	8,454	10,943
	119,592	127,815	367,483	382,483
Income from operations	15,450	6,416	45,688	22,490
Interest expense, net	(9,378	) (9,777	) (31,697	) (28,494
Loss on extinguishment of debt	—	—	(3,123) —
Foreign exchange (loss) gain	(905	) (202	) (1,102	) 157
Income (loss) before provision for income taxes	5,167	(3,563	) 9,766	(5,847
Provision for income taxes	(3,063	) (94	) (9,055	) (3,105
Net income (loss)	\$ 2,104	\$ (3,657	) \$ 711	\$ (8,952
Comprehensive income (loss)	\$ 9,182	\$ (1,781	) \$ 2,665	\$ (15,490
Net income (loss) per share:				
Basic	\$ 0.14	\$ (0.24	) \$ 0.05	\$ (0.59
Diluted	\$ 0.13	\$ (0.24	) \$ 0.05	\$ (0.59
Shares used in computing net income (loss) per share:				
Basic	15,375,728	15,257,617	15,352,352	15,215,752
Diluted	16,044,291	15,257,617	15,791,597	15,215,752
See accompanying notes.				

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Xerium Technologies, Inc.
 Consolidated Statements of Cash Flows—(Unaudited)
 (Dollars in thousands)

	Nine Months Ended September 30,	
	2013	2012
Operating activities		
Net income (loss)	\$711	\$(8,952)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Stock-based compensation	1,141	1,574
Depreciation	26,051	28,513
Amortization of intangibles	1,368	1,729
Deferred financing cost amortization	2,293	2,707
Foreign exchange loss on revaluation of debt	1,626	879
Deferred taxes	1,339	(383)
Asset impairment	1,078	1,600
Gain (loss) on disposition of property and equipment	154	(656)
Loss on extinguishment of debt	3,123	—
Provision for doubtful accounts	543	463
Change in assets and liabilities which provided (used) cash:		
Accounts receivable	(10,599)	) 2,954
Inventories	(5,195)	) 2,338
Prepaid expenses	1,714	(4,021)
Other current assets	(1,026)	) 1,385
Accounts payable and accrued expenses	7,436	1,945
Deferred and other long-term liabilities	(1,326)	) (1,158)
Net cash provided by operating activities	30,431	30,917
Investing activities		
Capital expenditures, gross	(15,562)	) (13,222)
Proceeds from disposals of property and equipment	2,235	1,378
Net cash used in investing activities	(13,327)	) (11,844)
Financing activities		
Net increase in notes payable	—	7,365
Proceeds from borrowings	199,000	—
Principal payments on debt	(198,848)	) (27,965)
Payment of deferred financing fees	(3,030)	) (1,782)
Net cash used in financing activities	(2,878)	) (22,382)
Effect of exchange rate changes on cash flows	(221)	) (680)
Net increase (decrease) in cash	14,005	(3,989)
Cash and cash equivalents at beginning of period	34,777	43,566
Cash and cash equivalents at end of period	\$48,782	\$39,577

See accompanying notes.

Xerium Technologies, Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
(Dollars in thousands, except per share data)

1. Description of Business and Significant Accounting Policies

Description of Business

Xerium Technologies, Inc. (the "Company") is a leading global provider of industrial consumables and mechanical services used in the production of paper, paperboard, building products and nonwoven materials. Its operations are strategically located in the major paper-making regions of the world, including North America, Europe, South America and Asia-Pacific.

Basis of Presentation

The accompanying unaudited condensed consolidated interim financial statements at September 30, 2013 and for the three and nine months ended September 30, 2013 and 2012 include the accounts of the Company and its wholly-owned subsidiaries and have been prepared in conformity with U.S. Generally Accepted Accounting Principles ("GAAP") for interim financial reporting and pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). Accordingly, such financial statements do not include all of the information and footnotes required by GAAP for complete financial statements. GAAP requires the Company's management to make estimates and assumptions that affect the amounts reported in the financial statements. Actual results could differ from those estimates. The interim results presented herein are not necessarily indicative of the results to be expected for the entire year. In management's opinion, these unaudited condensed consolidated interim financial statements contain all adjustments of a normal recurring nature necessary for a fair presentation of the financial statements for the interim periods presented. Certain reclassifications have been made to prior year amounts to conform to the presentation of current year amounts. These unaudited consolidated interim financial statements should be read in conjunction with the Company's audited consolidated financial statements for the year ended December 31, 2012 as reported on the Company's Annual Report on Form 10-K filed on March 11, 2013.

Accounting Policies

Inventories, net

Inventories are generally valued at the lower of cost or market using the first-in, first-out (FIFO) method. Raw materials are valued principally on a weighted average cost basis. The Company's work in process and finished goods are specifically identified and valued based on actual inputs to production. Provisions are recorded as appropriate to write-down obsolete and excess inventory to estimated net realizable value. The process for evaluating obsolete and excess inventory often requires management to make subjective judgments and estimates concerning future sales levels, quantities and prices at which such inventory will be able to be sold in the normal course of business, while considering the general aging of inventory and factoring in any new business conditions.

The components of inventories, net of allowances are as follows at:

	September 30, 2013	December 31, 2012
Raw materials	\$20,378	\$16,924
Work in process	24,744	23,681
Finished goods (includes consigned inventory of \$8,620 at September 30, 2013 and \$8,726 at December 31, 2012)	36,295	36,786
	\$81,417	\$77,391

In the second quarter of 2013, in connection with the closure of the Spain clothing facility, the Company reserved \$692 of obsolete inventory. This charge is included in cost of products sold expense in the Consolidated Income Statement for the nine months ended September 30, 2013.

Goodwill

The Company accounts for goodwill and other intangible assets in accordance with ASC Topic 350, Intangibles—Goodwill and Other Intangible Assets ("Topic 350"). Topic 350 requires that goodwill and intangible assets

that have indefinite lives not be amortized, but instead, must be tested for impairment at least annually or whenever events or business conditions warrant. During the nine months ended September 30, 2013, the Company evaluated events and business conditions to

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determine if a test for an impairment of goodwill was warranted. No such events or business conditions took place during this period, therefore no test was determined to be warranted at September 30, 2013.

Warranties

The Company offers warranties on certain rolls products that it sells. The specific terms and conditions of these warranties vary depending on the product sold, the country in which the product is sold and arrangements with the customer. The Company estimates the costs that may be incurred under its warranties and records a liability for such costs. Factors that affect the Company's warranty liability include the number of units sold, historical and anticipated rates of warranty claims, cost per claim and new product introduction. The Company periodically assesses the adequacy of its recorded warranty claims and adjusts the amounts as necessary. The table below represents the changes in the Company's warranty liability for the nine months ended September 30, 2013:

	Balance at December 31, 2012	Charged to Cost of Sales	Effect of Foreign Currency Translation	Deduction from Reserves	Balance at September 30, 2013
For the nine months ended September 30, 2013	\$ 1,848	\$ 1,254	\$ 48	\$(1,378	) \$ 1,772

Net Income (Loss) Per Common Share

Net (loss) income per common share has been computed and presented pursuant to the provisions of ASC Topic 260, Earnings per Share ("Topic 260"). Net income (loss) per share is based on the weighted-average number of shares outstanding during the period. As of September 30, 2013 and 2012, the Company had outstanding restricted stock units ("RSUs"), deferred stock units ("DSUs"), warrants and options.

The following table sets forth the computation of basic and diluted weighted-average shares:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Weighted-average common shares outstanding—basic	15,375,728	15,257,617	15,352,352	15,215,752
Dilutive effect of stock-based compensation awards outstanding	668,563	—	439,245	—
Weighted-average common shares outstanding—diluted	16,044,291	15,257,617	15,791,597	15,215,752

Dilutive securities aggregating approximately 1.8 million were outstanding for the three and nine months ended September 30, 2012, but were not included in the computation of diluted earnings per share for the three months and nine months ended September 30, 2012 because the impact of including such shares would be anti-dilutive to the earnings per share calculations.

Impairment

The Company reviews its long-lived assets that have finite lives for impairment in accordance with ASC Topic 360, Property, Plant, and Equipment ("Topic 360"). This topic requires that companies evaluate the fair value of long-lived assets based on the anticipated undiscounted future cash flows to be generated by the assets when indicators of impairment exist to determine if there is impairment to the carrying value. Any change in the carrying amount of an asset as a result of the Company's evaluation has been recorded in either restructuring expense, if it was a result of the Company's restructuring activities, or general and administrative expense for all other impairments in the consolidated statements of operations. Impairment charges associated with restructuring are discussed in Note 7 "Restructuring Expense".

In 2013, the Company determined there was an impairment of \$0.7 million to the carrying value of a vacant facility held for sale and certain other assets at March 31, 2013. This impairment charge is included in general and administrative expense in the Consolidated Statements of Operations for the nine months ended September 30, 2013. The facility and related assets were sold during the third quarter of 2013.

New Accounting Standards

In July of 2013, FASB issued ASU 2013-11 Income Taxes (Topic 740), Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists (a consensus of the FASB Emerging Issues Taskforce) ("ASU 2013-11"). Beginning January 1, 2014, the effective date of this regulation, the Company will adopt the provisions of ASU 2013-11 related to presentation of an unrecognized tax benefit when a net operating loss

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carryforward, a similar tax loss, or a tax credit carryforward exists. Adoption of ASU 2013-11 is not expected to have a material impact to the consolidated financial statements.

2. Derivatives and Hedging

As required by ASC Topic 815, Derivatives and Hedging (“Topic 815”), the Company records all derivatives on the balance sheet at fair value. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative, whether the Company has elected to designate a derivative in a hedging relationship and apply hedge accounting and whether the hedging relationship has satisfied the criteria necessary to apply hedge accounting. Derivatives designated and qualifying as a hedge of the exposure to changes in the fair value of an asset, liability or firm commitment attributable to a particular risk are considered fair value hedges. Derivatives designated and qualifying as a hedge of the exposure to variability in expected future cash flows, or other types of forecasted transactions, are considered cash flow hedges. Derivatives may also be designated as hedges of the foreign currency exposure of a net investment in a foreign operation. Hedge accounting generally provides for the matching of the timing of gain or loss recognition on the hedging instrument with the recognition of the changes in the fair value of the hedged asset or liability that are attributable to the hedged risk in a fair value hedge or the earnings effect of the hedged forecasted transactions in a cash flow hedge.

Risk Management Objective of Using Derivatives

The Company is exposed to certain risks arising from both its business operations and economic conditions. The Company principally manages its exposures to a wide variety of business and operational risks through management of its core business activities. From time to time, the Company enters into derivative financial instruments to manage exposures that arise from business activities that result in the receipt or payment of future known cash amounts, the value of which are determined by interest rates or foreign exchange rates.

Cash Flow Hedges of Interest Rate Risk

The Company’s objectives in using interest rate derivatives are to add stability to interest expense and to manage its exposure to interest rate movements. To accomplish this objective, the Company uses interest rate caps as part of its interest rate risk management strategy. Interest rate caps designated as cash flow hedges protect the Company from increases in interest rates above the strike rate of the interest rate cap. However, the Company’s financial statements are exposed to the effects of interest rate fluctuations below the strike rate negotiated in the interest rate cap agreements, which could have a material impact on its results of operations.

On August 8, 2011, the Company entered into two interest rate cap agreements with certain financial institutions, in notional amounts totaling \$114,400, whereby the Company limits its variable interest rate exposure to the strike rate of the interest rate cap agreements. During the second quarter of 2013, in connection with the refinancing of its credit facility, the Company paid off its Euro-denominated debt, resulting in the termination of one of the interest rate cap agreements and accelerated amortization of \$322 to interest expense. At September 30, 2013, the notional amount of the remaining agreement was \$42,800. Under the terms of this interest rate cap agreement, the Company will receive payments based on the spread in rates if the three-month LIBOR rate increases above the negotiated cap rate of 3.0%. The interest rate cap is considered a designated hedging instrument and classified as Level 2 in the fair value hierarchy. Changes in fair value will be deferred in accumulated other comprehensive income (loss) and the cap purchase price will be reclassified from accumulated comprehensive loss into earnings as interest expense over the life of the agreement. The following represents the fair value of the interest rate cap and unrecognized losses included in accumulated other comprehensive loss at September 30, 2013 and December 31, 2012:

	September 30, 2013	December 31, 2012
Fair value of interest rate rate cap included in other assets in the Consolidated Balance Sheets	\$4	\$16
Unrecognized losses included in accumulated other comprehensive loss	\$(257	) \$(644
The Company expects to reclassify \$108 from other comprehensive income (loss) to interest expense over the next twelve months.		

Non-designated Hedges of Foreign Exchange Risk

Derivatives not designated as hedges are not speculative and are used to manage the Company’s exposure to foreign exchange rates, but do not meet the strict hedge accounting requirements of Topic 815. Changes in the fair value of

derivatives not designated in hedging relationships are recorded directly to earnings.

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The Company, from time to time, may enter into foreign exchange forward contracts to fix currencies at specified rates based on expected future cash flows to protect against the fluctuations in cash flows resulting from sales denominated in foreign currencies. Additionally, to manage its exposure to fluctuations in foreign currency on intercompany balances and certain purchase commitments, the Company from time to time may use foreign exchange forward contracts.

As of September 30, 2013 and December 31, 2012, the Company had outstanding derivatives that were not designated as hedges in qualifying hedging relationships. The value of these contracts is recognized at fair value based on market exchange forward rates and is recorded in other assets or other liabilities on the Consolidated Balance Sheets. The following represents the fair value of these derivatives at September 30, 2013 and December 31, 2012 and the change in fair value included in foreign exchange gain for the three and nine months ended September 30, 2013 and 2012:

	September 30, 2013	December 31, 2012
Fair value of derivatives	\$(287	) \$357
	Three Months Ended	Three Months Ended
	September 30, 2013:	September 30, 2012:
Change in fair value included in foreign exchange (loss) gain for the three months ended September 30, 2013 and September 30, 2012	\$(836	) \$155
	Nine months ended	Nine months ended
	September 30, 2013	September 30, 2012
Change in fair value included in foreign exchange gain for the nine months ended September 30, 2013 and September 30, 2012	\$706	\$438

The following represents the notional amounts of foreign exchange forward contracts at September 30, 2013:

	Notional Sold	Notional Purchased
Non-designated hedges of foreign exchange risk	\$25,812	\$ (14,706
Fair Value of Derivatives Under ASC Topic 820)

ASC Topic 820, Fair Value Measurements and Disclosures (“Topic 820”), emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair value measurements, Topic 820 establishes a fair value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity (observable inputs that are classified within Levels 1 and 2 of the hierarchy) and the reporting entity’s own assumptions about market participant assumptions (unobservable inputs classified within Level 3 of the hierarchy). Level 1 inputs utilize quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access. Level 2 inputs are inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs may include quoted prices for similar assets and liabilities in active markets, as well as inputs that are observable for the asset or liability (other than quoted prices), such as interest rates, foreign exchange rates, and yield curves that are observable at commonly quoted intervals. Level 3 inputs are unobservable inputs including fair value of investments that do not have the ability to redeem at net asset value as of the measurement date, or during the first quarter following the measurement date. The derivative assets or liabilities are typically based on an entity’s own assumptions, as there is little, if any, market activity. In instances where the determination of the fair value measurement is based on inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety. The Company’s assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and the Company considers factors specific to the asset or liability. The Company determined that its derivative valuations, which are

based on market exchange forward rates, fall within Level 2 of the fair value hierarchy.

3. Long-term Debt

At September 30, 2013 and December 31, 2012, long-term debt consisted of the following:

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	September 30, 2013	December 31, 2012
New senior secured term loan facility, payable quarterly, U.S. Dollar denominated–LIBOR (minimum 1.25%) plus 5.00% (6.25%) as of September 30, 2013, net of \$1.0 million discount	\$ 198,500	\$—
Prior first lien debt, payable quarterly, U.S. Dollar denominated–LIBOR (minimum 1.25%) plus 5.00% (6.25%) as of December 31, 2012	—	104,557
Prior first lien debt, payable quarterly, Euro denominated–EURIBOR (minimum 1.25%) plus 5.00% (6.25%) as of December 31, 2012	—	95,979
	198,500	200,536
Senior Notes (Unsecured), payable semi-annually–U.S. Dollar denominated interest rate fixed at 8.875%, matures June of 2018	236,410	236,410
Unsecured, interest rate fixed at 2.00%, Euro denominated	139	135
	435,049	437,081
Less current maturities	2,139	2,397
Total	\$432,910	\$434,684

On May 17, 2013, the Company entered into a Credit and Guaranty Agreement for a \$200 million term loan credit facility (the “New Term Credit Facility”), net of a discount of \$1.0 million, among the Company, certain direct and indirect U.S. subsidiaries of the Company as guarantors and certain financial institutions. The Company also entered into a Revolving Credit and Guaranty Agreement for a \$40.0 million asset-based revolving credit facility subject to a borrowing base (the “ABL Facility,” and collectively with the New Term Credit Facility, the “New Credit Facility”) among the Company, Xerium Canada Inc., as Canadian borrower, certain direct and indirect U.S. subsidiaries of the Company as guarantors and certain financial institutions.

The New Term Credit Facility provides for:

a six-year \$200 million senior secured term loan facility, provided the facility would mature in March 2018 if any of the Company's senior notes due 2018 ("Senior Notes") remain outstanding at that time; and
an uncommitted accordion option (the “Incremental Facility”) allowing for increases for borrowings under the New Term Credit Facility with the same terms, and borrowing of new tranches of term loans, up to an aggregate principal amount equal to (i) \$75 million plus (ii) an additional amount (the “Facility Increase”) provided, if after giving effect to such Facility Increase (as well as any other additional term loans), on a pro forma basis, the Senior Secured Leverage Ratio (as defined in the New Term Credit Facility) for the most recent four consecutive fiscal quarters does not exceed 2.25:1.

The ABL Facility provides for a \$40 million senior secured revolving credit facility with a \$20 million sub-limit on letters of credit. Availability under the ABL Facility is subject to a borrowing base that is based on a specified percentage of eligible accounts receivable and inventory. The term of the ABL Facility is five years, provided that if any of the Senior Notes remain outstanding in March 2018, the ABL Facility would mature at that time.

The Company used the borrowings under the New Term Credit Facility to refinance all of its outstanding indebtedness under its previously existing senior secured term loan and revolving credit facility entered into in 2011 (the "2011 Credit Facility"). The Company intends to draw upon the ABL Facility from time-to-time for working capital and general corporate purposes.

The New Term Credit Facility will require the Company to make amortization payments (payable in quarterly installments) equal to 1% of principal per annum with respect to the Term Loans with the remaining amount due at final maturity. Voluntary prepayments will be permitted, in whole or in part, subject to minimum prepayment requirements; provided that prepayments made prior to the date that is six months after the Closing Date of the New Term Credit Facility for the purpose of repricing or effectively repricing the term loan facilities must include a 1.0% prepayment premium; provided, further, that voluntary prepayments of loans bearing interest at the London Interbank Offered Rate (“LIBOR”) on a date other than the last day of the relevant interest period will be subject to the payment of

customary breakage costs.

If the total amount of advances outstanding under the ABL Facility exceed either \$40 million or the borrowing base, the Company must repay an amount equal to the excess borrowing. If obligations under all outstanding letters of credit exceeds \$20 million, the Company must cash collateralize its letters of credit in an amount equal to the excess obligations outstanding.

The interest rates under the New Term Credit Facility will be calculated, at the Company's option, at either the base rate or LIBOR, plus a margin of 4.00% and 5.00%, respectively. Each of the base rate and LIBOR shall be subject to a minimum of 2.25% and 1.25%, respectively. If the Company's Senior Secured Leverage Ratio (as defined in the \$200 million New Credit

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Facility) is less than 2.00:1 at any quarterly determination date, then the margins over the base rate and LIBOR will be 3.50% and 4.50%, respectively.

Depending on whether advances are made in U.S. Dollars or Canadian Dollars, interest rates under the ABL Facility will be calculated, at the Company's option, at either a U.S.-based or Canadian-based base rate ("Base Rate Loans") or LIBOR or the Canadian Dealer Offered Rate ("CDOR") (each, "Fixed Rate Loans"), respectively, plus a margin of 1.25% for Base Rate Loans and a margin of 2.25% for Fixed Rate Loans. If the Company draws advances on the ABL Facility that are greater than 33.3% but less than or equal to 66.7% of the \$40 million limit, then the margins on Base Rate Loans and Fixed Rate Loans drop to 1.00% and 2.00%, respectively. The margins drop to 0.75% and 1.75%, respectively, if advances under the ABL Facility are greater than 66.7% of the \$40 million limit. In addition to paying interest on outstanding advances under the ABL Facility, the Company will be required to pay a commitment fee to the lenders in respect of the unutilized commitments at a rate equal to 0.50% per annum if advances under the ABL Facility are less than or equal to 50% of the commitments or a rate equal to 0.375% per annum if advances under the ABL are more than 50% of the commitments.

The obligations under the New Credit Facility will be guaranteed by all of the Company's existing and future direct and indirect subsidiaries that are organized in the United States (subject to certain exceptions in the case of immaterial subsidiaries and joint ventures) and, in the case of the ABL Facility, by Xerium Canada Inc. and any future Canadian subsidiaries, provided that non-U.S. guarantors will only be liable for obligations of Xerium Canada Inc. and any other Canadian borrowers. The New Term Credit Facility is secured by a first-priority perfected security interest in substantially all of the assets of the Company, Xerium Canada Inc. and such subsidiary guarantors (collectively, the "Loan Parties"), in each case, now owned or later acquired, except with respect to the Loan Parties' accounts receivables and inventory, which are secured by a second-priority interest. The ABL Facility is secured by a first-priority perfected security interest in the Loan Parties' accounts receivables and inventory, and a second-priority interest in substantially all of the Loan Parties' other assets.

The New Credit Facility contains certain customary covenants that, subject to exceptions, restrict the Company's ability to, among other things:

- declare dividends or redeem or repurchase equity interests;
- prepay, redeem or purchase debt;
- incur liens and engage in sale-leaseback transactions;
- make loans and investments;
- incur additional indebtedness;
- amend or otherwise alter debt and other material agreements;
- make capital expenditures in excess of \$42 million per fiscal year, subject to adjustment;
- engage in mergers, acquisitions and asset sales;
- transact with affiliates; and
- engage in businesses that are not related to the Company's existing business.

The New Credit Facility eliminates the interest coverage and leverage coverage ratio maintenance tests that were contained in the Company's 2011 Credit Facility. However, the ABL Facility contains a springing Fixed Charge Coverage Ratio (as defined in the ABL Facility), which must be not less than 1.00:1 during periods in which our Global Excess Availability (as defined in the ABL Facility) falls below certain minimum thresholds.

The New Credit Facility contains certain customary representations and warranties, affirmative covenants and events of default, including payment defaults, breaches of representations and warranties, covenant defaults, cross-defaults and cross-acceleration to certain indebtedness, certain events of bankruptcy, certain triggering events under U.S. and, in the case of the ABL Facility, Canadian employee benefit plans, material judgments, actual or asserted failures of any guarantee or security document supporting the New Credit Facility to be in full force and effect and a change of control. If an event of default occurs, the lenders under the New Credit Facility would be entitled to take various enforcement actions, including acceleration of amounts due under the New Credit Facility and all actions permitted to be taken by a secured creditor. The material risks associated with the New Credit Facility are substantially similar to the material risks regarding the 2011 Credit Facility identified in the section entitled "Risks Relating to Our Capital Structure" under "Item 1A - Risk Factors" of our Form 10-K for the year-ended December 31,

2012.

The Company has \$236.4 million aggregate principal amount of 8.875% senior unsecured notes (the "Notes"). The Notes contain customary covenants that, subject to certain exceptions, restrict its ability to enter into certain transactions and engage in certain activities.

As of September 30, 2013, the outstanding balance of the Company's term debt under its New Term Credit Facility and Notes was \$435.0 million, which is net of a \$1.0 million discount. In addition, as of September 30, 2013, the Company had no outstanding borrowings under its current ABL Facility and had an aggregate of \$22.2 million available for additional borrowing. The borrowing availability represents the borrowing base under the ABL Facility less commitments on outstanding

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letters of credit. Additionally, at September 30, 2013, the Company had \$5.2 million available for borrowings from other credit facilities.

As of September 30, 2013 and December 31, 2012, the carrying value of the Company's long-term debt was \$435.0 million and \$437.1 million, respectively, and its fair value was approximately \$447.1 million and \$410.1 million, respectively. The Company determined the fair value of its debt utilizing significant other observable inputs (Level 2 of the fair value hierarchy).

4. Income Taxes

The Company utilizes the asset and liability method for accounting for income taxes in accordance with ASC Topic 740, Income Taxes ("Topic 740"). Under Topic 740, deferred tax assets and liabilities are determined based on the difference between their financial reporting and tax basis. The assets and liabilities are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. The Company reduces its deferred tax assets by a valuation allowance if, based upon the weight of available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized. In making this determination, the Company evaluates all available information including the Company's financial position and results of operations for the current and preceding years, as well as any available projected information for future years.

For the three and nine months ended September 30, 2013, the provision for income taxes was \$(3,063) and \$(9,055) as compared to \$(94) and \$(3,105) for the three and nine months ended September 30, 2012. The increase in tax expense was primarily attributable to the geographic mix of earnings in the three and nine months ended September 30, 2013 as compared to the three and nine months ended September 30, 2012, as well as tax expense due to the increase in unrecognized tax benefit in the three and nine months ended September 30, 2013. The provision for income taxes is primarily impacted by income earned in tax paying jurisdictions relative to income earned in non-tax paying jurisdictions. The majority of income recognized for purposes of computing the effective tax rate is earned in countries where the statutory income tax rates range from 25% to 39%; however, permanent income adjustments recorded against pre-tax earnings may result in an effective tax rate that is higher or lower than the statutory tax rate in these jurisdictions. The Company generates losses in certain jurisdictions for which no tax benefit is received, as the deferred tax assets in these jurisdictions (including the net operating losses) are fully reserved in the valuation allowance. For this reason, the Company recognizes minimal income tax expense or benefit in these jurisdictions, of which the most material jurisdictions are the United States, the United Kingdom and Australia. Due to these reserves, the geographic mix of the Company's pre-tax earnings has a direct correlation with how high or low its annual effective tax rate is relative to consolidated earnings. As the Company continues to reorganize and restructure its operations, it is possible that deferred tax assets, for which no income tax benefit has previously been provided, may more likely than not become realized. The Company continues to evaluate future operations and will record an income tax benefit in the period where it believes it is more likely than not that the deferred tax asset will be able to be realized. We estimate the resulting potential income tax benefit to be up to \$7,197.

As of September 30, 2013, the Company had a gross amount of unrecognized tax benefit of \$4,375, exclusive of interest and penalties. The unrecognized tax benefit increased by approximately \$1,100 during the nine months ended September 30, 2013, as a result of foreign currency effects, statute expirations, ongoing changes in currently reserved positions as a result of new facts or information, and the effects of income tax audits. Developments in ongoing tax audits related to the deductibility of a write down of an investment in a subsidiary and transfer pricing transactions increased the unrecognized tax benefit by \$816 during the three and nine months ended September 30, 2013. The Company's policy is to recognize interest and penalties related to income tax matters as income tax expense, which were immaterial for the nine months ended September 30, 2013 and 2012. The tax years 2000 through 2012 remain open to examination in a number of the major taxing jurisdictions to which the Company and its subsidiaries are subject. The Company believes that it has made adequate provisions for all income tax uncertainties.

In November of 2011, the Federal Revenue Department of the Ministry of Finance of ("FRD") issued a tax assessment against the Company's indirect subsidiary, Xerium Technologies Brasil Indústria e Comércio S.A. ("Xerium Brazil"), challenging the goodwill recorded in the 2005 acquisition of Wangner Itelpa and Huyck Indústria e Comércio S.A. by

Robec Brasil Participações Ltda., a predecessor to Xerium Brazil. This assessment denied the amortization of that goodwill against net income for the years 2006 through 2010 and sought payment of approximately \$40,592 (subject to currency exchange rates) in tax, penalties and interest as of September 30, 2013. The Company believes the transactions in question (i) complied with Brazilian tax and accounting rules, (ii) were effected for a legitimate business purpose, to consolidate the Company's operating activities in Brazil into one legal entity, and (iii) were properly documented and declared to Brazilian tax and corporate authorities. Based on the foregoing, Xerium Brazil filed a response disputing the tax assessment. In December of 2012 an administrative panel at the first administrative appeals level within the FRD rendered a decision upholding the original assessment, but reducing the claimed penalties by 50%. This decision reduced the total assessed amount as of September 30,

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2013 by approximately \$10,892 to \$29,700 (subject to currency exchange rates). On January 18, 2013, Xerium Brazil appealed the decision of the first administrative panel to the second of three administrative appeals courts potentially available to it within the FRD.

Although there can be no assurances, as of September 30, 2013, the Company believes it is more likely than not that it would prevail on every tax position under examination and therefore it did not accrue any amounts related to this assessment. The Company cannot assure a favorable outcome and cannot currently estimate the timing of the final resolution of this matter. The Company believes it has meritorious defenses and will vigorously contest this matter, and if the administrative courts of the FRD do not rule in the Company's favor, the Company intends to appeal its case to the Brazilian judicial courts. However, if management's views of the Company's position and the probable outcome of the assessment changes or the FRD's initial position is sustained by Brazilian judicial courts, the amount accrued would adversely impact the Company's financial condition and results of operations in the period in which any such determination or decision is made.

5. Pensions, Other Post-retirement and Post-employment Benefits

The Company accounts for its pensions, other post-retirement and post-employment benefit plans in accordance with ASC Topic 715, Compensation—Retirement Benefits (“Topic 715”). The Company has defined benefit pension plans covering substantially all of its U.S. and Canadian employees and employees of certain subsidiaries in other countries. Benefits are generally based on the employee's years of service and compensation. These plans are funded in conformity with the funding requirements of applicable government regulations. The Company does not fund certain plans, as funding is not required. The Company plans to continue to fund its U.S. defined benefit plans to comply with the Pension Protection Act of 2006. In addition, the Company also intends to fund its U.K. and Canadian defined benefit plans in accordance with local regulations.

As required by Topic 715, the following tables summarize the components of net periodic benefit cost:

Defined Benefit Plans

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Service cost	\$934	\$898	\$2,873	\$2,671
Interest cost	1,497	1,855	4,605	5,523
Expected return on plan assets	(1,356)	(1,392)	(4,169)	(4,142)
Amortization of prior service cost	7	4	10	11
Amortization of net loss	547	640	1,690	1,906
Net periodic benefit cost	\$1,629	\$2,005	\$5,009	\$5,969

6. Comprehensive Income (loss) and Accumulated Other Comprehensive Loss

Comprehensive income (loss) for the three and nine months ended September 30, 2013 and 2012 is as follows (net of taxes):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Net income (loss)	\$2,104	\$(3,657)	\$711	\$(8,952)
Foreign currency translation adjustments	7,462	2,571	(650)	(5,828)
Pension liability changes under Topic 715	(398)	(683)	2,217	(593)
Change in value of derivative instruments	14	(12)	387	(117)
Comprehensive income (loss)	\$9,182	\$(1,781)	\$2,665	\$(15,490)

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The components of accumulated other comprehensive loss for the three months ended September 30, 2013 are as follows (net of taxes):

	Foreign Currency Translation Adjustment	Pension Liability Changes Under Topic 715	Change in Value of Derivative Instruments	Accumulated Other Comprehensive (Loss) Income
Balance at June 30, 2013	\$ (4,859)	\$ (41,887)	\$ (271)	\$ (47,017)
Other comprehensive income (loss) before reclassifications	7,462	(902)	—	6,560
Amounts reclassified from other comprehensive (loss) income				
Amortization of actuarial losses	—	504	14	518
Amortization of interest expense	—	—	—	—
Net current period other comprehensive (loss) income	7,462	(398)	14	7,078
Balance at September 30, 2013	\$ 2,603	\$ (42,285)	\$ (257)	\$ (39,939)

The components of accumulated other comprehensive loss for the nine months ended September 30, 2013 are as follows (net of taxes):

	Foreign Currency Translation Adjustment	Pension Liability Changes Under Topic 715	Change in Value of Derivative Instruments	Accumulated Other Comprehensive (Loss) Income
Balance at December 31, 2012	\$ 3,253	\$ (44,502)	\$ (644)	\$ (41,893)
Other comprehensive (loss) income before reclassifications	(650)	685	14	49
Amounts reclassified from other comprehensive (loss) income				
Amortization of actuarial losses	—	1,532	—	1,532
Amortization of interest expense	—	—	373	373
Net current period other comprehensive (loss) income	(650)	2,217	387	1,954
Balance at September 30, 2013	\$ 2,603	\$ (42,285)	\$ (257)	\$ (39,939)

For the three and nine months ended September 30, 2013, the amortization of actuarial losses is included in cost of products sold and general and administrative expenses in the Consolidated Statements of Operations and Comprehensive Income (loss).

7. Restructuring and Impairment Expense

During the nine months ended September 30, 2013, the Company recorded restructuring and impairment expenses of approximately \$8,454. These included charges relating to the reduction of base costs via previously announced headcount reductions, the closure of two clothing facilities in Spain and Argentina and the closure of a roll cover facility in Charlotte, NC. During the nine months ended September 30, 2012, the Company recorded restructuring and impairment expenses of approximately \$10,943. These charges were primarily related to the voluntary redundancy program in Argentina, the relocation of a rolls cover facility in France, the transfer of certain equipment from a downsized location and the termination of various sales agency arrangements in Europe.

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The following table sets forth the significant components and activity under restructuring programs for the nine months ended September 30, 2013 and 2012:

	Balance at December 31, 2012	Charges (1)	Currency Effects	Cash Payments	Balance at September 30, 2013
Severance and other benefits	\$15,577	\$5,743	\$(53)	\$(11,028)	\$10,239
Facility costs and other	335	2,302	103	(1,880)	860
Total	\$15,912	\$8,045	\$50	\$(12,908)	\$11,099

	Balance at December 31, 2011	Charges (2)	Currency Effects	Cash Payments	Balance at September 30, 2012
Severance and other benefits	\$800	\$4,888	\$9	\$(2,405)	\$3,292
Facility costs and other	452	4,455	(117)	(4,456)	334
Total	\$1,252	\$9,343	\$(108)	\$(6,861)	\$3,626

(1) Amount excludes \$409 impairment charges.

(2) Amount excludes \$1,600 impairment charges.

Restructuring and impairment expense by segment, which is not included in Segment Earnings (Loss) in Note 8, is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Clothing	\$2,888	\$2,572	\$6,875	\$7,338
Roll Covers	86	3,223	1,518	3,402
Corporate	60	45	61	203
Total	\$3,034	\$5,840	\$8,454	\$10,943

8. Business Segment Information

The Company is a global manufacturer and supplier of consumable products used primarily in the production of paper and is organized into two reportable segments: Clothing and Roll Covers. The Clothing segment represents the manufacture and sale of synthetic textile belts used to transport paper along the length of papermaking machines. The Roll Covers segment primarily represents the manufacture and refurbishment of covers used on the steel rolls of papermaking machines and the servicing of those rolls. The Company manages each of these operating segments separately.

Management evaluates segment performance based on earnings before interest, taxes, depreciation and amortization and before allocation of corporate charges. Such measure is then adjusted to exclude items that are of an unusual nature and are not used in measuring segment performance or are not segment specific ("Segment Earnings (Loss)"). The accounting policies of these segments are the same as those for the Company as a whole. Inter-segment net sales and inter-segment eliminations are not material for any of the periods presented.

Summarized financial information for the Company's reportable segments is presented in the tables that follow for the three and nine months ended September 30, 2013 and 2012.

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	Clothing	Roll Covers	Corporate	Total
Three Months Ended September 30, 2013:				
Net Sales	\$87,980	\$47,062	\$—	\$135,042
Segment Earnings (Loss)	\$20,109	\$11,140	\$(4,332)	
Three Months Ended September 30, 2012:				
Net Sales	\$88,873	\$45,358	\$—	\$134,231
Segment Earnings (Loss)	\$17,429	\$9,914	\$(2,942)	
Nine months ended September 30, 2013:				
Net Sales	\$267,331	\$145,840	\$—	\$413,171
Segment Earnings (Loss)	\$58,319	\$35,802	\$(11,162)	
Nine months ended September 30, 2012:				
Net Sales	\$265,671	\$139,302	\$—	\$404,973
Segment Earnings (Loss)	\$48,051	\$29,930	\$(9,364)	

Provided below is a reconciliation of Segment earnings income (loss) to income (loss) before provision for income taxes for the three and nine months ended September 30, 2013 and 2012, respectively.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Segment Earnings (loss):				
Clothing	\$20,109	\$17,429	\$58,319	\$48,051
Roll Covers	11,140	9,914	35,802	29,930
Corporate	(4,332)	(2,942)	(11,162)	(9,364)
Stock-based compensation	(547)	(820)	(1,141)	(1,574)
Inventory write-off	—	—	(692)	—
Impairment expense	—	—	(667)	—
Legal fees related to term debt amendment	—	(30)	—	(115)
Non-recurring expenses related to CEO retirement	—	(1,600)	—	(3,096)
Interest expense, net	(9,378)	(9,777)	(31,697)	(28,494)
Depreciation and amortization	(8,791)	(9,897)	(27,419)	(30,242)
Loss on debt extinguishment	—	—	(3,123)	—
Restructuring expense	(3,034)	(5,840)	(8,454)	(10,943)
Income (loss) before provision for income taxes	\$5,167	\$(3,563)	\$9,766	\$(5,847)

9. Commitments and Contingencies

The Company is involved in various legal matters which have arisen in the ordinary course of business as a result of various immaterial labor claims, taxing authority reviews and other routine legal matters. As of September 30, 2013, the Company accrued an immaterial amount in its financial statements for these matters for which the Company believed the possibility of loss was probable and was able to estimate the damages. The Company does not believe that the ultimate resolution of these matters will have a material adverse effect on its financial position, results of operations or cash flow. The Company believes that any additional liability in excess of amounts provided which may result from the resolution of legal matters will not have a material adverse effect on the financial condition, liquidity or cash flow of the Company.

See Note 4 for a discussion of Xerium Brazil's proceeding with the FRD.

10. Stock-Based Compensation and Stockholders' Deficit

The Company records stock-based compensation expense in accordance with ASC Topic 718, Accounting for Stock Compensation and has used the straight-line attribution method to recognize expense for time-based restricted stock

units ("RSUs") and deferred stock units ("DSUs"). The Company recorded stock-based compensation expense during the three and nine months ended September 30, 2013 and September 30, 2012 as follows:

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	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2013	2012	2013	2012
RSU, Options and DSU Awards (1)	\$547	\$820	\$1,141	\$1,574

- (1) Related to RSUs, Options and DSUs awarded to certain employees and non-employee directors.

Summary of Activity under the Long-Term Incentive Plans

On September 22, 2010, the Board approved the Company's 2010 Long-Term Incentive Plan (the "2010 LTIP") under the 2010 Equity Incentive Plan (the "2010 Plan"). Awards under the 2010 LTIP are both time-based and performance-based. Awards will be paid in the form of RSUs or shares of common stock of the Company. Time-based awards under the 2010 LTIP were approved in the form of 131,010 time-based RSUs granted on October 29, 2010 under the Company's 2010 Plan. As of March 31, 2013, all of the time-based RSUs had vested in accordance with the 2010 LTIP and were converted to common stock. Performance-based awards under the 2010 LTIP in the amount of 20,709 vested on December 31, 2012, upon meeting various criteria, as included in the Company's 2012 Annual Report on Form 10-K, and were converted into common stock, net of applicable tax withholdings.

On May 8, 2012, the Board approved the 2012 Executive Long-Term Incentive Plan (the "2012 Executive LTIP") under the 2010 Plan. Awards under the 2012 Executive LTIP are both time-based and performance-based. A specific target share award is set for each participant in the 2012 Executive LTIP. Awards will be paid in the form of RSUs or shares of common stock of the Company. Time-based awards, or 50% of the total target award, were granted in the form of 54,750 time-based RSUs under the Company's 2010 Plan. As of March 31, 2013, 16,582 time-based RSUs vested in accordance with the 2012 Executive LTIP and were converted to common stock, net of applicable tax withholdings. The remaining time-based RSUs will vest in equal installments on March 31, 2014, and March 31, 2015, and convert into shares of common stock as they vest. Performance-based awards, which constitute 50% of the total award, will be determined based on the Company's performance against a three-year cumulative Adjusted EBITDA metric, adjusted for currency fluctuations during the term of the 2012 – 2014 Executive LTIP. The performance-based awards will convert into shares of the Company's common stock and be paid after the close of the three-year performance period. The amount of the payment will be based on a sliding scale ranging from 50% if the metric is achieved at 85% of the target up to 200% if the metric is achieved at or above 115% of the target.

On June 13, 2013, at the 2013 Annual Meeting of Stockholders of Xerium Technologies, Inc., the stockholders of the Company approved an amendment to the Company's 2010 Equity Incentive Plan, which increased the aggregate number of shares of the Company's common stock that may be delivered under or in satisfaction of awards under such plan from 913,525 to 1,663,525, increased the number of shares that may be subject to option and stock appreciation right grants and that may be granted as stock awards to any one participant in a calendar year from 150,000 to 500,000, and set a maximum cash award that may be granted to any one participant in a calendar year at \$2,000. This amendment was approved by the Company's Board of Directors on March 12, 2013.

On June 13, 2013, after the stockholders had approved the amendment to the Company's 2010 Equity Incentive Plan, the Board approved the granting of awards under the 2013 Executive Long-Term Incentive Plan (the "2013 Executive LTIP") under the 2010 Plan. Awards under the 2013 Executive LTIP are both time-based and performance-based and will be paid in the form of RSUs or shares of common stock of the Company. Time-based awards, or 50% of the total target award, were granted in the form of 179,571 time-based RSUs under the Company's 2010 Plan. These time-based awards will cliff vest on March 11, 2016, and will be converted to common stock, net of applicable tax withholdings.

Performance-based awards, which constitute the remaining 50% of the total award, will vest depending on the Company's stock price performance during the three year participant service period from March 11, 2013 through March 10, 2016. If the awards vest, they will convert into shares of the Company's common stock and be paid after the close of the three-year performance period.

Other Stock Compensation Plans

On August 15, 2012, in connection with the previously announced anticipated retirement of Stephen R. Light, the Board of Directors of the Company appointed Harold C. Bevis to the position of President and Chief Executive Officer, effective immediately, and Mr. Light notified the Company of his resignation, effective as of that date, as the Company's

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Chairman, President and Chief Executive Officer. The Company granted Mr. Bevis a sign-on award of 204,208 restricted stock units and options to acquire 781,701 shares of the Company's Common Stock, par value \$0.001 per share. Both the restricted stock units and the options will vest over a three year period, beginning on the second anniversary of the August 15, 2012 grant date. The options have a 10-year term and an exercise price of \$4.00 per share, the August 15, 2012 closing price of the Company's common stock on the New York Stock Exchange. In addition, on August 15, 2012, the Company accelerated the vesting of Mr. Light's remaining 50,000 restricted stock units, issuing 27,900 shares of common stock, upon vesting, net of certain tax withholdings.

Directors' Deferred Stock Unit Plan

Under the 2011 non-management directors stock plan ("2011 DSU Plan"), each director receives an annual retainer of \$112, to be paid on a quarterly basis in arrears. Half of the annual retainer is payable in deferred stock units ("DSUs"), with the remaining half payable in cash. The non-management directors were awarded an aggregate of 7,247 DSUs under the 2011 DSU Plan for service during the quarter ended September 30, 2013. In addition, in accordance with the 2011 DSU Plan, 4,831 DSUs were settled in Common Stock during the quarter ended September 30, 2013.

11. Supplemental Guarantor Financial Information

On May 26, 2011, the Company closed on the sale of its Notes. The Notes are unsecured obligations of the Company and are fully and unconditionally guaranteed on a senior unsecured basis by all of the domestic wholly owned subsidiaries of the Company (the "Guarantors"). In accordance with Rule 3-10 of Regulation S-X promulgated under the Securities Act of 1933, the following condensed consolidating financial statements present the financial position, results of operations and cash flows of Xerium Technologies, Inc. (referred to as "Parent" for the purpose of this note only) on a stand-alone parent-only basis, the Guarantors on a Guarantors-only basis, the combined non-Guarantor subsidiaries and elimination entries necessary to arrive at the information for the Parent, the Guarantors and non-Guarantor subsidiaries on a consolidated basis.

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Xerium Technologies, Inc.
 Consolidating Balance Sheet—(Unaudited)
 At September 30, 2013
 (Dollars in thousands)

	Parent	Total Guarantors	Total Non Guarantors	Other Eliminations	The Company
ASSETS					
Current assets:					
Cash and cash equivalents	\$13,614	\$(9)	\$35,177	\$—	\$48,782
Accounts receivable, net	—	23,969	69,016	—	92,985
Intercompany receivables	(104,241)	110,566	(6,325)	—	—
Inventories, net	—	16,729	65,459	(771)	81,417
Prepaid expenses	353	1,717	5,461	—	7,531
Other current assets	134	3,412	9,890	—	13,436
Total current assets	(90,140)	156,384	178,678	(771)	244,151
Property and equipment, net	4,778	58,553	229,626	—	292,957
Investments	685,672	268,312	—	(953,984)	—
Goodwill	—	17,737	48,323	—	66,060
Intangible assets	11,406	3,478	319	—	15,203
Other assets	4	—	8,531	—	8,535
Total assets	\$611,720	\$504,464	\$465,477	\$(954,755)	\$626,906
LIABILITIES AND STOCKHOLDERS'					
(DEFICIT) EQUITY					
Current liabilities:					
Accounts payable	\$1,181	\$7,558	\$22,559	\$—	\$31,298
Accrued expenses	14,110	8,416	51,665	—	74,191
Current notes payable	—	—	8,120	—	8,120
Current maturities of long-term debt	2,000	—	139	—	2,139
Total current liabilities	17,291	15,974	82,483	—	115,748
Long-term debt, net of current maturities	432,910	—	—	—	432,910
Deferred and long-term taxes	291	2,335	13,435	—	16,061
Pension, other post-retirement and post-employment obligations	21,643	1,154	58,455	—	81,252
Other long-term liabilities	88	—	6,216	—	6,304
Intercompany loans	225,604	(342,537)	116,933	—	—
Total stockholders' (deficit) equity	(86,107)	827,538	187,955	(954,755)	(25,369)
Total liabilities and stockholders' equity	\$611,720	\$504,464	\$465,477	\$(954,755)	\$626,906

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Xerium Technologies, Inc.
 Consolidating Balance Sheet
 At December 31, 2012
 (Dollars in thousands)

	Parent	Total Guarantors	Total Non Guarantors	Other Eliminations	The Company
ASSETS					
Current assets:					
Cash and cash equivalents	\$6,471	\$ 36	\$ 28,270	\$—	\$ 34,777
Accounts receivable, net	—	20,964	63,492	—	84,456
Intercompany receivables	(102,407)	107,944	(5,537)	—	—
Inventories, net	—	15,672	62,569	(850)	77,391
Prepaid expenses	159	1,693	7,534	—	9,386
Other current assets	—	2,970	11,869	—	14,839
Total current assets	(95,777)	149,279	168,197	(850)	220,849
Property and equipment, net	734	62,157	245,915	—	308,806
Investments	596,891	149,134	—	(746,025)	—
Goodwill	—	17,737	43,390	—	61,127
Intangible assets	10,034	4,776	3,868	—	18,678
Other assets	44	—	9,339	—	9,383
Total assets	\$511,926	\$ 383,083	\$ 470,709	\$(746,875)	\$ 618,843
LIABILITIES AND STOCKHOLDERS' (DEFICIT) EQUITY					
Current liabilities:					
Accounts payable	\$502	\$ 8,629	\$ 27,753	\$—	\$ 36,884
Accrued expenses	6,005	6,579	47,173	—	59,757
Current notes payable	—	—	7,911	—	7,911
Current maturities of long-term debt	1,250	—	1,147	—	2,397
Total current liabilities	7,757	15,208	83,984	—	106,949
Long-term debt, net of current maturities	339,717	—	94,967	—	434,684
Deferred and long-term taxes	—	2,335	14,247	—	16,582
Pension, other post-retirement and post-employment obligations	21,677	1,000	61,272	—	83,949
Other long-term liabilities	31	—	5,709	—	5,740
Intercompany loans	229,239	(358,187)	128,948	—	—
Total stockholders' (deficit) equity	(86,495)	722,727	81,582	(746,875)	(29,061)
Total liabilities and stockholders' equity	\$511,926	\$ 383,083	\$ 470,709	\$(746,875)	\$ 618,843

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Xerium Technologies, Inc.

Consolidating Statement of Operations and Comprehensive Income (Unaudited)

For the three months ended September 30, 2013

(Dollars in thousands)

	Parent	Total Guarantors	Total Non Guarantors	Other Eliminations	The Company	
Net sales	\$—	\$44,922	\$102,702	\$(12,582	) \$135,042
Costs and expenses:						
Cost of products sold	(421	) 31,008	63,730	(12,661	) 81,656
Selling	—	5,048	12,194	—	17,242	
General and administrative	2,485	1,528	11,265	—	15,278	
Research and development	—	1,874	508	—	2,382	
Restructuring and impairment	60	37	2,937	—	3,034	
	2,124	39,495	90,634	(12,661	) 119,592
(Loss) income from operations	(2,124	) 5,427	12,068	79	15,450
Interest (expense) income, net	(8,898) 1,408	(1,888) —	(9,378)
Foreign exchange loss	(538) (126) (241) —	(905)
Equity in subsidiaries income	13,992	6,139	—	(20,131) —	
Income (loss) before provision for income taxes	2,432	12,848	9,939	(20,052	) 5,167
Provision for income taxes	(328) (23) (2,712) —	(3,063)
Net income	\$2,104	\$12,825	\$7,227	\$(20,052	) \$2,104
Comprehensive income	\$2,563	\$12,975	\$13,696	\$(20,052	) \$9,182

Xerium Technologies, Inc.

Consolidating Statement of Operations and Comprehensive (Loss) Income-(Unaudited)

For the three months ended September 30, 2012

(Dollars in thousands)

	Parent	Total Guarantors	Total Non Guarantors	Other Eliminations	The Company	
Net sales	\$—	\$45,119	\$100,831	\$(11,719	) \$134,231
Costs and expenses:						
Cost of products sold	(342	) 31,821	65,442	(11,842	) 85,079
Selling	—	5,393	13,153	—	18,546	
General and administrative	3,489	1,725	10,436	—	15,650	
Research and development	—	2,105	595	—	2,700	
Restructuring and impairment	45	19	5,776	—	5,840	
	3,192	41,063	95,402	(11,842	) 127,815
(Loss) income from operations	(3,192	) 4,056	5,429	123	6,416
Interest (expense) income, net	(6,973) 1,490	(4,294) —	(9,777)
Foreign exchange loss	(193) (3) (6) —	(202)
Equity in subsidiaries income (deficit)	5,093	(13,056	) —	7,963	—
Dividend income	1,656	18,904	—	(20,560) —	
(Loss) Income before provision for income taxes	(3,609) 11,391	1,129	(12,474) (3,563)
Provision for income taxes	(48) (35) (11) —	(94)
Net (loss) income	\$(3,657) \$11,356	\$1,118	\$(12,474) \$(3,657)

Comprehensive (loss) income	\$(3,598)	\$11,464	\$2,827	\$(12,474)	\$(1,781)
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Xerium Technologies, Inc.

Condensed Consolidating Statement of Operations and Comprehensive (Loss) Income -(Unaudited)

For the nine months ended September 30, 2013

(Dollars in thousands)

	Parent	Total Guarantors	Total Non Guarantors	Other Eliminations	The Company
Net sales	\$—	\$138,303	\$311,319	\$(36,451)	) \$413,171
Costs and expenses:					
Cost of products sold	(1,270)	94,341	196,087	(36,530)	) 252,628
Selling	—	15,239	38,110	—	) 53,349
General and administrative	6,766	4,072	34,580	—	) 45,418
Research and development	—	5,924	1,710	—	) 7,634
Restructuring and impairment	61	831	7,562	—	) 8,454
	5,557	120,407	278,049	(36,530)	) 367,483
(Loss) income from operations	(5,557)	17,896	33,270	79	) 45,688
Interest (expense) income, net	(23,715)	4,219	(12,201)	) —	) (31,697)
Foreign exchange loss	(442)	(130)	(530 )	) —	) (1,102)
Equity in subsidiaries income	33,970	9,124	—	(43,094)) —
Loss on extinguishment of debt	(3,123 )	—	—	—	) (3,123)
Dividend income	—	1,555	—	(1,555)) —
Income (loss) before provision for income taxes	1,133	32,664	20,539	(44,570)	) 9,766
Provision for income taxes	(422)	45	(8,678)	) —	) (9,055)
Net income	\$711	\$32,709	\$11,861	\$(44,570)	) \$711
Comprehensive income	\$(632)	\$32,815	\$15,052	\$(44,570)	) \$2,665

Xerium Technologies, Inc.

Condensed Consolidating Statement of Operations and Comprehensive (Loss) Income-(Unaudited)

For the nine months ended September 30, 2012

(Dollars in thousands)

	Parent	Total Guarantors	Total Non Guarantors	Other Eliminations	The Company
Net sales	\$—	\$134,970	\$305,628	\$(35,625)	) \$404,973
Costs and expenses:					
Cost of products sold	(1,150)	97,245	198,291	(35,990)	) 258,396
Selling	—	16,725	40,379	—	) 57,104
General and administrative	8,753	5,492	33,264	—	) 47,509
Research and development	—	6,258	2,273	—	) 8,531
Restructuring and impairment	203	182	10,558	—	) 10,943
	7,806	125,902	284,765	(35,990)	) 382,483
(Loss) income from operations	(7,806)	9,068	20,863	365	) 22,490
Interest (expense) income, net	(21,419)	5,035	(12,110)	) —	) (28,494)
Foreign exchange loss	(501)	(7)	665	—	) 157
Equity in subsidiaries income	19,221	(10,668)	) —	(8,553)) —
Dividend income	1,656	18,904	—	(20,560)) —
(Loss) income before provision for income taxes	(8,849)	22,332	9,418	(28,748)) (5,847)

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Provision for income taxes	(103)	(108)	(2,894)	—	(3,105)
Net (loss) income	\$(8,952)	\$22,224	\$6,524	\$(28,748)	\$(8,952)
Comprehensive income	\$(8,261)	\$22,860	\$(1,341)	\$(28,748)	\$(15,490)

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Xerium Technologies, Inc.
 Consolidating Statement of Cash Flows-(Unaudited)
 For the nine months ended September 30, 2013
 (Dollars in thousands)

	Parent	Total Guarantors	Total Non Guarantors	Other Eliminations	The Company
Operating activities					
Net income	\$711	\$32,709	\$11,861	\$ (44,570)	\$711
Adjustments to reconcile net income to net cash (used in) provided by operating activities:					
Stock-based compensation	1,120	—	21	—	1,141
Depreciation	94	5,599	20,358	—	26,051
Amortization of intangibles	—	1,298	70	—	1,368
Deferred financing cost amortization	(1,466)	—	3,759	—	2,293
Foreign exchange loss on revaluation of debt	(410)	(45)	2,081	—	1,626
Deferred taxes	291	—	1,048	—	1,339
Asset impairment	17	341	720	—	1,078
Loss on disposition of property and equipment	132	17	5	—	154
Loss on extinguishment of debt	3,123	—	—	—	3,123
Provision for doubtful accounts	—	155	388	—	543
Undistributed equity in earnings of subsidiaries	(33,970)	(9,124)	—	43,094	—
Change in assets and liabilities which provided (used) cash:					
Accounts receivable	25	(3,151)	(7,473)	—	(10,599)
Inventories	—	(1,057)	(4,059)	(79)	(5,195)
Prepaid expenses	(194)	(23)	1,931	—	1,714
Other current assets	(151)	47	(922)	—	(1,026)
Accounts payable and accrued expenses	8,667	55	(2,841)	1,555	7,436
Deferred and other long-term liabilities	93	153	(1,572)	—	(1,326)
Intercompany loans	1,834	(2,635)	801	—	—
Net cash (used in) provided by operating activities	(20,084)	24,339	26,176	—	30,431
Investing activities					
Capital expenditures, gross	(4,274)	(2,166)	(9,122)	—	(15,562)
Intercompany property and equipment transfers, net	3	88	(91)	—	—
Proceeds from disposals of property and equipment	—	4	2,231	—	2,235
Net cash used in investing activities	(4,271)	(2,074)	(6,982)	—	(13,327)
Financing activities					
Proceeds from borrowings	199,000	—	—	—	199,000
Principal payments on debt	(105,057)	—	(93,791)	—	(198,848)
Payment of deferred financing fees	(3,030)	—	—	—	(3,030)
Intercompany loans	(59,415)	(22,310)	81,725	—	—
Net cash provided by (used in) financing activities	31,498	(22,310)	(12,066)	—	(2,878)
Effect of exchange rate changes on cash flows	—	—	(221)	—	(221)
Net increase (decrease) in cash	7,143	(45)	6,907	—	14,005
Cash and cash equivalents at beginning of period	6,471	36	28,270	—	34,777
Cash and cash equivalents at end of period	\$13,614	\$(9)	\$35,177	\$—	\$48,782

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Xerium Technologies, Inc.
 Consolidating Statement of Cash Flows-(Unaudited)
 For the nine months ended September 30, 2012
 (Dollars in thousands)

	Parent	Total Guarantors	Total Non Guarantors	Other Eliminations	The Company
Operating activities					
Net (loss) income	\$(8,952)	\$22,224	\$6,524	\$(28,748)	\$(8,952)
Adjustments to reconcile net (loss) income to net cash (used in) provided by operating activities:					
Stock-based compensation	1,574	—	—	—	1,574
Depreciation	135	5,932	22,446	—	28,513
Amortization of intangibles	—	1,659	70	—	1,729
Deferred financing cost amortization	1,885	—	822	—	2,707
Foreign exchange loss on revaluation of debt	—	—	879	—	879
Deferred taxes	—	—	(383)	—	(383)
Asset impairment	—	—	1,600	—	1,600
Gain on disposition of property and equipment	—	24	(680)	—	(656)
Intercompany dividend	(1,656)	(18,904)	—	20,560	—
Provision for doubtful accounts	—	(150)	613	—	463
Undistributed equity in (earnings) loss of subsidiaries	(19,221)	10,668	—	8,553	—
Change in assets and liabilities which provided (used) cash:					
Accounts receivable	8	852	2,094	—	2,954
Inventories	—	3,107	(404)	(365)	2,338
Prepaid expenses	122	(671)	(3,472)	—	(4,021)
Other current assets	—	1,799	(414)	—	1,385
Accounts payable and accrued expenses	4,781	(2,106)	(730)	—	1,945
Deferred and other long-term liabilities	244	(622)	(780)	—	(1,158)
Intercompany loans	1,891	(394)	(1,497)	—	—
Net cash (used in) provided by operating activities	(19,189)	23,418	26,688	—	30,917
Investing activities					
Capital expenditures, gross	(22)	(1,895)	(11,305)	—	(13,222)
Intercompany property and equipment transfers, net	344	(317)	(27)	—	—
Proceeds from disposals of property and equipment	—	298	1,080	—	1,378
Net cash provided by (used in) investing activities	322	(1,914)	(10,252)	—	(11,844)
Financing activities					
Increase in notes payable	—	—	7,365	—	7,365
Principal payments on debt	(13,846)	—	(14,119)	—	(27,965)
Payment of deferred financing fees	(1,047)	—	(735)	—	(1,782)
Dividends paid	1,656	—	(1,656)	—	—
Intercompany loans	31,091	(21,778)	(9,313)	—	—
Net cash provided by (used in) financing activities	17,854	(21,778)	(18,458)	—	(22,382)
Effect of exchange rate changes on cash flows	—	2	(682)	—	(680)
Net decrease in cash	(1,013)	(272)	(2,704)	—	(3,989)
Cash and cash equivalents at beginning of period	11,548	280	31,738	—	43,566
Cash and cash equivalents at end of period	\$10,535	\$8	\$29,034	\$—	\$39,577

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Quarterly Report on Form 10-Q contains "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995 that are subject to the safe harbor created by that Act. These statements relate to future events or to our future financial performance and involve known and unknown risks, uncertainties, and other factors that may cause our actual results, levels of activity, performance, or achievements to be materially different from any future results, levels of activity, performance, or achievements expressed or implied by these forward-looking statements. In some cases, forward-looking statements can be identified by the use of words such as "may," "could," "expect," "intend," "plan," "seek," "anticipate," "believe," "estimate," "predict," "potential," or "continue" or the negative of these words or other comparable terminology. Undue reliance should not be placed on forward-looking statements because they involve known and unknown risks, uncertainties, and other factors that are, in some cases, beyond our control and that could materially affect actual results, levels of activity, performance, or achievements. Factors that could materially affect our actual results, levels of activity, performance or achievements include the following items:

- we are subject to the risk of a weaker global economy that influences the paper industry as well as local economic conditions in the areas around the world where we conduct business;
- structural shifts in the demand for paper, for instance the shift away from newsprint, printing and writing paper in favor of digital media, may adversely impact our financial results;
- our strategy to lower our costs in response to market changes in the paper industry by reorganizing and restructuring our operations will require us to incur significantly higher costs and may not provide the cost reductions and results we anticipate;
- we are subject to execution risk related to the startup of our proposed new facility in China;
- our strategies and plans, including, but not limited to, those relating to developing and successfully marketing new products, enhancing our operational efficiencies and reducing costs, may not result in the anticipated benefits;
- our financial results could be adversely affected by fluctuations in interest rates and currency exchange rates;
- our manufacturing facilities may be required to quickly increase or decrease production capacity, which could negatively affect our production, customer order lead time, product quality, labor relations or gross margin;
- we may not be successful in developing and marketing new technologies or in competing against new technologies developed by competitors;
- variations in demand for our products, including our new products, could negatively affect our net sales and profitability;
- we are subject to fluctuations in the price of our component supply costs;
 - due to our high degree of leverage and significant debt service obligations, we need to generate substantial operating cash flow to fund growth and unexpected cash needs;
- we are subject to the risk of terrorist attacks or an outbreak or escalation of any insurrection or armed conflict involving the United States or any other country in which we conduct business, or any other domestic or international calamity, including natural disasters;
- we are subject to the impact of changes in the policies, laws, regulations and practices of the United States and any foreign country in which we operate or conduct business, including changes regarding taxes and the repatriation of earnings; and
- anti-takeover provisions could make it more difficult for a third-party to acquire us.

Other factors that could materially affect our actual results, levels of activity, performance or achievements can be found in our "Risk Factors" section in our Annual Report on Form 10-K for the year ended December 31, 2012, filed with the SEC on March 11, 2013, our Quarterly Report for the quarter ended March 31, 2013 on Form 10-Q filed with the SEC on May 7, 2013, our Quarterly Report for the quarter ended June 30, 2013 on Form 10-Q filed with the SEC on August 1, 2013 and this Quarterly Report on Form 10-Q. If any of these risks or uncertainties materialize, or if our underlying assumptions prove to be incorrect, actual results may vary significantly from what we project. Any

forward-looking statement in this Quarterly Report on Form 10-Q reflects our current views with respect to future events and is subject to these and other risks, uncertainties, and assumptions relating to our operations, results of operations, growth strategy, and liquidity. We assume no obligation to publicly update or revise these forward-looking statements for any reason, whether as a result of new information, future events, or otherwise, except as required by law.

All references in this Quarterly Report to “Xerium”, “the Company”, “we”, “our” and “us” means Xerium Technologies, Inc. and its subsidiaries.

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Company Overview

We are a leading global manufacturer and supplier of two types of consumable products used primarily in the production of paper—clothing and roll covers. Our operations are strategically located in the major paper-producing regions of North America, Europe, South America and Asia-Pacific. Our products play key roles in the formation and processing of paper along the length of a paper-making machine. Paper producers rely on our products and services to help improve the quality of their paper, differentiate their paper products, operate their paper-making machines more efficiently and reduce production costs.

We operate in two principal business segments: clothing and roll covers. In our clothing segment, we manufacture and sell highly engineered synthetic textile belts that transport paper as it is processed in a paper-making machine. Clothing plays a significant role in the forming, pressing and drying stages of paper production. Because paper-making processes and machine specifications vary widely, the clothing size, form, material and function is custom engineered to fit each individual paper-making machine and process. For the nine months ended September 30, 2013, our clothing segment represented 65% of our net sales.

Our roll cover products provide a surface with the mechanical properties necessary to process the paper sheet in a cost-effective manner that delivers the sheet qualities desired by the paper producer. Roll covers are tailored to individual paper-making machines and processes, using different materials, treatments and finishings. In addition to manufacturing and selling new roll covers, we also provide refurbishment services for previously installed roll covers and we manufacture new and rebuilt spreader rolls. We also provide various related products and services to our customers, both directly and through third party providers, as a growing part of our overall product offering through our roll covers sales channels. For the nine months ended September 30, 2013, our roll cover segment represented 35% of our net sales.

Industry Trends and Outlook

Historically, demand for our products has been driven primarily by the volume (tonnage) of paper produced on a worldwide basis, which in turn is affected by global economic conditions. Since 2000, paper producers have taken actions that seek to structurally improve the balance between the supply of, and demand for, paper in response to the industry's highly cyclical swings in profitability driven by the oversupply of paper during periods when paper producers have more aggregate capacity than the market requires. As part of these efforts, they have permanently shut down many paper-making machines or entire manufacturing facilities.

Beginning about the same time the paper industry began to address the structural balance between the supply and demand for paper, the widespread adoption of e-commerce and digitalization of traditionally printed material has resulted in a prolonged decline in newsprint and printing and writing grades of paper. This longer term decline has been partially offset by increases in the production of packaging grades, both as a consequence of globalization of manufacturing and as a result of the increase of tissue/personal care products which have increased as global GDP has risen, particularly in the developing world. In 2010 and 2011, global paper and board production began to recover from the economic recession and show growth, particularly in developing countries. As international shipments of manufactured goods increased, containerboard production recovered particularly strongly, contributing over 50% of the total global improvement. The paper and board production recovery, however, stalled in the second half of 2011 and remained weak throughout 2012, particularly in Europe and South America. For the full year of 2013, we still expect that global paper and board manufacturers' operating rates will remain near their 2012 levels, while industry forecasters predict the growth of global paper production from 2013 to 2015 to be between approximately 2% and 4% per annum. Generally, and over time, we expect growth in paper production to be greater in Asia-Pacific, South America and Eastern Europe than in the more mature North American and Western European regions, where demand may decline.

Despite projected growth, many paper producers continue to experience low levels of profitability. Any anticipated global paper production growth would be moderated by further consolidation among papermakers, reduction in the

number of paper producers, and shutdowns of paper-making machines or facilities, which we believe will continue, particularly in Europe and North America, until there is a better balance between supply and demand for paper and the profit levels of paper producers improve.

Also affecting machine curtailments are structural productivity gains from new paper machine designs that have fewer rolls and from improved products that we and our competitors supply, which enable paper producers to manufacture more paper with fewer machines. In particular, market recognition of the extended life of our roll cover products has, and will likely continue to, negatively impact demand for these products and their volume potential. Additionally, we are seeing a trend that paper producers are placing an increasing emphasis on maintenance cost reduction and, as a result, are extending the life of roll

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covers through additional maintenance cycles before replacing them. However, we believe volume declines would be at least partially offset by our introduction of new products with the extended life qualities that our customer's desire and increasing market share of proprietary products such as our SmartRoll™.

In response to this, we expect to continue to focus our research and development efforts on new products that deliver increased value to our customers and for which they will pay increased prices. In addition, we intend to continue to enhance and deploy our value added selling approach as part of our strategy to differentiate our products, while at the same time we remain focused on cost reduction and efficiency programs.

The negative paper industry trends described above are likely to continue. We believe that the paper industry will continue to experience an increased emphasis on cost reduction and continued paper-machine shutdown activity. These underlying industry dynamics could negatively impact our business, results of operations and financial condition and are the key drivers behind our strategy to reduce our cost structure, align our geographic footprint with anticipated growth in the South America and Asia-Pacific regions and grow our non-paper business revenue streams.

Net Sales and Expenses

Net sales in both our clothing and roll covers segments are primarily driven by the following factors:

- The volume (tonnage) of worldwide paper production;
- Our ability to introduce new products that our customers value and will pay for;
- Advances in technology of our products, which can provide value to our customers by improving the efficiency of paper-making machines and reduce their manufacturing costs;
- Growth in developing markets, particular in Asia;
- The mix of paper grades being produced;
- Our ability to enter and expand our business in non-paper products; and
- The impact of currency fluctuations.

Net sales in our roll covers segment include our mechanical services business. We have expanded this business in response to demand from paper producers that we perform work on the internal mechanisms of their rolls while we refurbish or replace a roll cover. In our clothing segment, a small portion of our business has been conducted pursuant to consignment arrangements; for these, we do not recognize a sale of a product to a customer until the customer places the product into use, which typically occurs some period after the product is shipped to the customer or to a warehouse location near the customer's facility. As part of the consignment agreement, we deliver the goods to a location designated by the customer. In addition, we agree to a "sunset" date with the customer, which represents the date by which the customer must accept all risks and responsibilities of ownership of the product and payment terms begin. For consignment sales, revenue is recognized on the earlier of the actual product installation date or the "sunset" date.

Our operating cost levels are impacted by total sales volume, raw material costs, the impact of inflation, foreign currency fluctuations and the success of our cost reduction programs.

The level of our cost of products sold is primarily attributable to labor costs, raw material costs, product shipping costs, plant utilization and depreciation, with labor costs constituting the largest component. We invest in facilities and equipment that enable innovative product development and improve production efficiency and costs. Recent examples of capital spending for such purposes include faster weaving looms and seaming machines with accurate electronic controls, automated compound mixing equipment and computer-controlled lathes and mills.

The level of research and development spending is driven by market demand for technology enhancements, including both specific customer needs and general market requirements, as well as by our own analysis of applied technology opportunities. With the exception of purchases of equipment and similar capital items used in our research and development activities, all research and development is expensed as incurred. Research and development expenses were \$2.4 million and \$2.7 million for the three months ended September 30, 2013 and 2012, respectively.

Foreign Exchange

We have a geographically diverse customer base. In the nine months ended September 30, 2013 we generated approximately 38% of our net sales in North America, 32% in Europe, 8% in South America, 20% in Asia-Pacific and 2% in the rest of the world.

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A substantial portion of our net sales is denominated in Euros or other currencies. As a result, changes in the relative values of U.S. Dollars, Euros and other currencies affect our reported levels of net sales and profitability as the results are translated into U.S. Dollars for reporting purposes. In particular, decreases in the value of the U.S. Dollar relative to the value of the Euro and these other currencies positively impact our levels of revenue and profitability because the translation of a certain number of Euros or units of such other currencies into U.S. Dollars for financial reporting purposes will represent more U.S. Dollars than it would have prior to the relative decrease in the value of the U.S. Dollar. Conversely, a decline in the value of the Euro will result in a lower number of U.S. Dollars for financial reporting purposes.

For certain transactions, our net sales are denominated in U.S. Dollars but all or a substantial portion of the associated costs are denominated in a different currency. As a result, changes in the relative values of U.S. Dollars, Euros and other currencies can affect the level of the profitability of these transactions. The largest proportion of such transactions consists of transactions in which the net sales are denominated in or indexed to the U.S. Dollar and all or a substantial portion of the associated costs are denominated in Brazilian Reals or other currencies.

Currency fluctuations have a greater effect on the level of our net sales than on the level of our income (loss) from operations. For example, in the nine months ended September 30, 2013 as compared to the nine months ended September 30, 2012, the change in the value of the U.S. Dollar against most of the currencies we conduct our business in resulted in net currency decreases in net sales of \$0.9 million, yet income from operations currency effects increased by \$2.8 million.

During the nine months ended September 30, 2013, we conducted business in nine foreign currencies. The following table provides the average exchange rate for the nine months ended September 30, 2013 and the nine months ended September 30, 2012 of the U.S. Dollar against each of the four foreign currencies in which we conduct the largest portion of our operations.

Currency	Average exchange rate of the U.S. Dollar in the nine months ended September 30, 2013	Average exchange rate of the U.S. Dollar in the nine months ended September 30, 2012
Euro	\$1.32 = 1 Euro	\$1.28 = 1 Euro
Brazilian Real	\$0.47 = 1 Brazilian Real	\$0.52 = 1 Brazilian Real
Canadian Dollar	\$0.98 = 1 Canadian Dollar	\$1.00 = 1 Canadian Dollar
Australian Dollar	\$0.98 = 1 Australian Dollar	\$1.04 = 1 Australian Dollar

In the nine months ended September 30, 2013, we conducted approximately 36% of our operations in Euros, approximately 11% in the Australian Dollar, approximately 7% in the Brazilian Real (although a significant portion of Brazil net sales are in U.S. Dollars) and approximately 5% in the Canadian Dollar.

To mitigate the risk of transactions in which a sale is made in one currency and associated costs are denominated in a different currency, we may utilize forward currency contracts in certain circumstances to lock in exchange rates with the objective that the gain or loss on the forward contracts will approximate the loss or gain that results from the transaction or transactions being hedged. We determine whether to enter into hedging arrangements based upon the size of the underlying transaction or transactions, an assessment of the risk of adverse movements in the applicable currencies and the availability of a cost effective hedge strategy. To the extent we do not engage in hedging or such hedging is not effective, changes in the relative value of currencies can affect our profitability.

Domestic and Foreign Operating Results:

The following is an analysis of our domestic and foreign operations during the three and nine months ended September 30, 2013 and September 30, 2012 and a discussion of the results of operations during those periods (in thousands):

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	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Domestic income from operations	\$3,303	\$864	\$12,339	\$1,262
Foreign income from operations	12,147	5,552	33,349	21,228
Total income from operations	\$15,450	\$6,416	\$45,688	\$22,490

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During the three and nine months ended September 30, 2013, domestic income from operations was lower than foreign income from operations primarily due to product mix, market differences and various unallocated corporate expenses. Excess cash generated from operations will typically remain permanently reinvested in most foreign subsidiaries. If cash does not remain permanently reinvested, income tax would need to be recorded. However, there are no legal restrictions or material adverse consequence for repatriating the excess cash to the domestic subsidiaries to assist in debt repayment, capital expenditures and other expenses of our operations.

Cost Reduction Programs

An important part of our strategy is to seek to reduce our overall costs and improve our competitiveness. As a part of this effort, we engage in cost reduction programs, which are designed to improve the cost structure of our global operations in response to changing market conditions. These cost reduction programs include headcount reductions throughout the world as well as plant closures that are intended to rationalize production among our facilities to better enable us to match our cost structure with customer demand. Cost savings have been realized and are expected to be realized in labor costs and other production overhead, other components of costs of products sold, general and administrative expenses and facility costs. The majority of cost savings begin at the time of the headcount reductions and plant closure with remaining cost savings recognized over subsequent periods. Cost savings from headcount reductions have not been and are not expected to be offset by related increases in other expenses. Cost savings related to plant closures have been and are expected to be partially offset by additional costs incurred in the facilities that assumed the operations of the closed facility.

During the nine months ended September 30, 2013, we recorded restructuring expenses of approximately \$8.5 million. These included charges relating to the reduction of base costs via previously announced headcount reductions, the closure of two clothing facilities in Spain and Argentina and the closure of a roll cover facility in Charlotte, NC. During the nine months ended September 30, 2012, we recorded restructuring expenses of approximately \$10.9 million, primarily related to the voluntary redundancy program in Argentina, the relocation of a rolls cover facility in France, the transfer of certain equipment from a downsized location and the termination of various sales agency arrangements in Europe.

Results of Operations

The table that follows sets forth for the periods presented certain consolidated operating results.

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2013	2012	2013	2012
	(in thousands)		(in thousands)	
Net Sales	\$135,042	\$134,231	\$413,171	\$404,973
Costs and expenses:				
Cost of products sold	81,656	85,079	252,628	258,396
Selling	17,242	18,546	53,349	57,104
General and administrative	15,278	15,650	45,418	47,509
Research and development	2,382	2,700	7,634	8,531
Restructuring	3,034	5,840	8,454	10,943
	119,592	127,815	367,483	382,483
Income from operations	15,450	6,416	45,688	22,490
Interest expense, net	(9,378)	) (9,777)	) (31,697)	) (28,494)
Loss on extinguishment of debt	—	—	(3,123)) —
Foreign exchange (loss) gain	(905)	) (202)	) (1,102)	) 157
Income (loss) before provision for income taxes	5,167	(3,563)) 9,766	(5,847)
Provision for income taxes	(3,063)) (94)) (9,055)) (3,105)

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Net income (loss)	\$2,104	\$(3,657)	\$711	\$(8,952)
Comprehensive income (loss)	\$9,182	\$(1,781)	\$2,665	\$(15,490)

Three Months Ended September 30, 2013 Compared to the Three Months Ended September 30, 2012

Net Sales. Net sales for the three months ended September 30, 2013 increased by \$0.8 million, or 0.6%, to \$135.0 million from \$134.2 million for the three months ended September 30, 2012. For the three months ended September 30, 2013, approximately 65% of our net sales were in our clothing segment and approximately 35% were in our roll covers segment.

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In our clothing segment, net sales for the three months ended September 30, 2013 decreased by \$0.9 million, or 1.0%, to \$88.0 million from \$88.9 million for the three months ended September 30, 2012, primarily due to decreased sales volume of \$0.8 million in South America, \$0.5 million in North America and \$0.5 million in Europe, partially offset by a increase in sales volume of \$1.0 million in Asia Pacific.

In our roll covers segment, net sales for the three months ended September 30, 2013 increased by \$1.7 million or 3.7%, to \$47.1 million from \$45.4 million for the three months ended September 30, 2012. The increase was primarily due to increased sales volume of \$1.5 million in North America and \$0.2 million in Europe and favorable currency effects of \$0.7 million, partially offset by decreases in sales volume of \$0.6 million in Asia Pacific and \$0.2 million in South America.

Cost of Products Sold. Cost of products sold for the three months ended September 30, 2013 decreased by \$3.4 million, or 4.0% to \$81.7 million from \$85.1 million for the three months ended September 30, 2012.

In our clothing segment, cost of products sold decreased \$3.4 million in the current quarter compared to the third quarter of 2012 as a result of lower cost of products sold as a percentage of sales. Cost of products sold, as a percentage of net sales decreased by 3.2% to 59.9% in the three months ended September 30, 2013 from 63.1% in the three months ended September 30, 2012. This decrease was primarily due to reduced costs as a result of restructuring savings and operational efficiencies, partially offset by unfavorable regional and product sales mix.

In our roll covers segment, cost of products sold increased \$0.1 million in the current quarter compared to the third quarter of 2012. However, cost of products sold, as a percentage of net sales decreased by 2.1% to 62.5% for the three months ended June 30, 2013 from 64.6% for the three months ended June 30, 2012. This decrease was primarily due to restructuring savings and operational efficiencies and favorable factory overhead absorption.

Selling Expenses. For the three months ended September 30, 2013, selling expenses decreased by \$1.3 million, or 7.0% to \$17.2 million from \$18.5 million for the three months ended September 30, 2012, primarily as a result of restructuring savings.

General and Administrative Expenses. For the three months ended September 30, 2013, general and administrative expenses decreased by \$0.4 million, or 2.5% to \$15.3 million from \$15.7 million for the three months ended September 30, 2012, primarily as a result of our cost reduction activities, a decrease of \$1.6 million due to charges recorded in 2012 related to CEO transition costs, partially offset by an increase of \$1.3 million in management incentive expense in 2013, \$0.6 million in professional fees and \$0.3 million of China press felt plant startup costs.

Restructuring Expenses. For the three months ended September 30, 2013, we incurred restructuring expenses of \$3.0 million. These included charges relating to the reduction of base costs via previously announced headcount reductions and the closure of a clothing facility in Spain. In 2012, we incurred restructuring expenses of \$5.8 million, primarily related to the voluntary redundancy program in Argentina and the relocation of a rolls cover facility in France. See Note 7 to the Consolidated Financial Statements for further discussion on these restructuring activities.

Interest Expense, Net. Net interest expense for the three months ended June 30, 2013 decreased by \$0.4 million or 4.1%, to \$9.4 million from \$9.8 million for the three months ended September 30, 2012. The decrease was primarily due to lower average debt balances during the third quarter of 2013 versus the third quarter of 2012.

Provision for Income Taxes. For the three months ended September 30, 2013 and September 30, 2012, the provision for income taxes was \$3.1 million and \$0.1 million. The increase in income tax expense was primarily attributable to increased earnings and the geographic mix of earnings in the third quarter of 2013 as compared to the third quarter of 2012. Our provision for income taxes is primarily impacted by income we earn in tax paying jurisdictions relative to income we earn in non-tax paying jurisdictions. The majority of income recognized for purposes of computing our effective tax rate is earned in countries where the statutory income tax rates range from 25% to 39%. However, permanent income adjustments recorded against pre-tax earnings may result in an effective tax rate that is higher or lower than the statutory tax rate in these jurisdictions. We generate losses in certain jurisdictions for which we receive no tax benefit as the deferred tax assets in these jurisdictions (including net operating losses) are fully reserved in our valuation allowance. For this reason, we recognize minimal income tax expense or benefit in these jurisdictions, of which the most material jurisdictions are the United States, the United Kingdom and Australia. Due to these reserves, the geographic mix of our pre-tax earnings has a direct correlation with how high or low our annual effective tax rate

is relative to consolidated earnings.

Nine Months Ended September 30, 2013 Compared to the Nine Months Ended September 30, 2012

Net Sales. Net sales for the nine months ended September 30, 2013 increased by \$8.2 million, or 2.0%, to \$413.2 million from \$405.0 million for the nine months ended September 30, 2012. For the nine months ended September 30, 2013, approximately 65% of our net sales were in our clothing segment and approximately 35% were in our roll covers segment.

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In our clothing segment, net sales for the nine months ended September 30, 2013 increased by \$1.6 million, or 0.6%, to \$267.3 million from \$265.7 million for the nine months ended September 30, 2012, primarily due to increased sales volume of \$4.4 million in Asia Pacific, \$1.5 million in North America and \$0.6 million in Europe, partially offset by unfavorable currency effects of \$1.8 million and a decrease in sales volume of \$3.0 million in South America.

In our roll covers segment, net sales for the nine months ended September 30, 2013 increased by \$6.5 million or 4.7%, to \$145.8 million from \$139.3 million for the nine months ended September 30, 2012. The increase was primarily due to increased sales volume of \$3.3 million in North America, \$2.2 million in Europe and \$0.4 million in South America and favorable currency effects of \$0.9 million.

Cost of Products Sold. Cost of products sold for the nine months ended September 30, 2013 decreased by \$5.8 million, or 2.2%, to \$252.6 million from \$258.4 million for the nine months ended September 30, 2012.

In our clothing segment, cost of products sold decreased \$4.6 million or 2.8% in the nine months ended September 30, 2013 compared to the nine months ended September 30, 2012 as a result of lower cost of products sold as a percentage of sales. Cost of products sold, as a percentage of net sales decreased by 2.1% to 61.1% in the nine months ended September 30, 2013 from 63.2% in the nine months ended September 30, 2012. This decrease was primarily due to reduced costs as a result of restructuring savings and operational efficiencies, partially offset by unfavorable regional and product mix.

In our roll covers segment, cost of products sold decreased \$1.0 million or 1.1% in the nine months ended June 30, 2013 compared to the nine months ended September 30, 2012 as a result of lower cost of products sold as a percentage of sales. Cost of products sold, as a percentage of net sales decreased by 3.5% to 62.1% in the nine months ended September 30, 2013 from 65.6% in the nine months ended September 30, 2012. This decrease was due to restructuring savings, operational efficiencies and favorable factory overhead absorption.

Selling Expenses. For the nine months ended September 30, 2013, selling expenses decreased by \$3.8 million, or 6.7% to \$53.3 million from \$57.1 million for the nine months ended September 30, 2012 primarily as a result of restructuring savings.

General and Administrative Expenses. For the nine months ended September 30, 2013, general and administrative expenses decreased by \$2.1 million, or 4.4% to \$45.4 million from \$47.5 million for the nine months ended September 30, 2012. This decrease is largely comprised of our cost reduction activities, a decrease of \$3.1 million due to charges recorded in 2012 related to CEO transition costs, a gain of \$0.7 million related to insurance recovery from a plant fire and favorable currency effects of \$0.6 million. These decreases were partially offset by an increase of \$4.4 million in management incentive costs, the reversal of \$1.0 million related to a favorable tax contingency settlement in 2012 and an impairment charge of \$0.7 million related to an idle facility sold in the third quarter of 2013.

Restructuring Expenses. For the nine months ended September 30, 2013, we incurred restructuring expenses of \$8.5 million. These included charges relating to the reduction of base costs via previously announced headcount reductions, the closure of two clothing facilities in Spain and Argentina and the closure of a roll cover facility in Charlotte, NC. During the nine months ended September 30, 2012, we recorded restructuring expenses of approximately \$10.9 million, primarily related to the voluntary redundancy program in Argentina, the relocation of a rolls cover facility in France, the transfer of certain equipment from a downsized location and the termination of various sales agency arrangements in Europe. See Note 7 to the Consolidated Financial Statements for further discussion on these restructuring activities.

Interest Expense, Net. Net interest expense for the nine months ended September 30, 2013 increased by \$3.2 million or 11.2%, to \$31.7 million from \$28.5 million for the nine months ended September 30, 2012. The increase was primarily due to the \$3.7 million in financing fees paid in connection with our May 2013 debt refinancing that were charged to interest expense.

Loss on Extinguishment of Debt. The loss on extinguishment of debt of \$3.1 million in the nine months ended September 30, 2013 represents the write-off of deferred financing costs resulting from our previous credit facility. (See Note 3 of the Consolidated Financial Statements and "Liquidity and Capital Resources-Credit Facility and Notes" for further discussion on the refinancing.)

Provision for Income Taxes. For the nine months ended September 30, 2013 and September 30, 2012, the provision for income taxes was \$9.1 million and \$3.1 million respectively. The increase in income tax expense was primarily attributable to increased earnings and the geographic mix of earnings in the nine months ended September 30, 2013 as compared to the nine months ended September 30, 2012. Our provision for income taxes is primarily impacted by income we earn in tax paying jurisdictions relative to income we earn in non-tax paying jurisdictions. The majority of income recognized for purposes of computing our effective tax rate is earned in countries where the statutory income tax rates range from 25% to 39%. However, permanent income adjustments recorded against pre-tax earnings may result in an effective tax rate that is higher or lower than the statutory tax rate in these jurisdictions. We generate losses in certain jurisdictions for which we receive no tax benefit as the

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deferred tax assets in these jurisdictions (including net operating losses) are fully reserved in our valuation allowance. For this reason, we recognize minimal income tax expense or benefit in these jurisdictions, of which the most material jurisdictions are the United States, the United Kingdom and Australia. Due to these reserves, the geographic mix of our pre-tax earnings has a direct correlation with how high or low our annual effective tax rate is relative to consolidated earnings.

Liquidity and Capital Resources

Our principal liquidity requirements are for debt service, working capital and capital expenditures. We plan to use cash on hand, cash generated by operations and, should it become necessary, access to our revolving credit facility, as our primary sources of liquidity. Our operations are highly dependent upon the paper production industry and the degree to which the paper industry is affected by global economic conditions and the availability of credit. Demand for our products could decline if paper manufacturers are unable to obtain required financing or if economic conditions cause additional mill closures. In addition, the impact of the most recent global economic recession and the continued lack of availability of credit may affect our customers' ability to pay their debts.

Net cash provided by operating activities was \$30.4 million for the nine months ended September 30, 2013 and \$30.9 million for the nine months ended September 30, 2012. The \$0.5 million decrease was due to increased in working capital, partially offset by an increase in cash earnings.

Net cash used in investing activities was \$13.3 million for the nine months ended September 30, 2013 and \$11.8 million for the nine months ended September 30, 2012. The increase of \$1.5 million was primarily due to the increase in capital expenditures of \$2.3 million, partially an increase of \$0.9 million in proceeds from disposals of property and equipment.

Net cash used in financing activities was \$2.9 million and \$22.4 million for the nine months ended September 30, 2013 and September 30, 2012, respectively. The decrease of \$19.5 million was primarily the result of the decrease of \$20.7 million in net principal payments made on debt in 2013, partially offset by an increase of \$1.2 million in financing fees paid in 2013.

As of September 30, 2013, the outstanding balance of our term debt under our New Term Credit Facility and Notes was \$435.0 million. In addition, as of September 30, 2013, we had no outstanding borrowings under our current ABL Facility and had an aggregate of \$22.2 million available for additional borrowing. The borrowing availability represents the borrowing base under the ABL Facility less commitments on outstanding letters of credit. Additionally, at September 30, 2013, we had \$5.2 million available for borrowings from other credit facilities.

We expect to incur expense of approximately \$4.6 million related to the continuation of our restructuring initiatives in the fourth quarter of 2013. We have incurred \$8.5 million in the nine months ended September 30, 2013. Actual restructuring costs for 2013 may substantially differ from estimates at this time, depending on the timing of the restructuring activities and the required actions to complete them.

Capital Expenditures

For the nine months ended September 30, 2013 and 2012, we had capital expenditures of \$15.6 million and \$13.2 million. We are currently targeting capital expenditures for 2013 to exceed our earlier estimate of \$33.0 million by \$5.0 to \$10.0 million due to the acceleration of certain capital projects. We analyze our planned capital expenditures based on investment opportunities available to us and our financial and operating performance, and accordingly, actual capital expenditures may be more or less than this amount. We intend to use existing cash and cash from operations to fund our capital expenditures.

See "Credit Facility and Notes" below for a description on limitations on capital expenditures imposed by our Credit Facility.

Credit Facility and Notes

On May 17, 2013, we entered into a Credit and Guaranty Agreement for a \$200 million term loan credit facility (the "New Term Credit Facility") among us, certain direct and indirect U.S. subsidiaries of the Company as guarantors and

certain financial institutions. We also entered into a Revolving Credit and Guaranty Agreement for a \$40 million asset-based revolving credit facility subject to a borrowing base (the “ABL Facility,” and collectively with the New Term Credit Facility, the “New Credit Facility”) among us, Xerium Canada Inc., as Canadian borrower, certain direct and indirect U.S. subsidiaries of the Company as guarantors and certain financial institutions.

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The New Term Credit Facility provides for:

a six-year \$200 million senior secured term loan facility, provided the facility would mature in March 2018 if any of the Company's senior notes due 2018 ("Senior Notes") remain outstanding at that time; and an uncommitted accordion option (the "Incremental Facility") allowing for increases for borrowings under the New Term Credit Facility with the same terms, and borrowing of new tranches of term loans, up to an aggregate principal amount equal to (i) \$75 million plus (ii) an additional amount (the "Facility Increase") provided, if after giving effect to such Facility Increase (as well as any other additional term loans), on a pro forma basis, the Senior Secured Leverage Ratio (as defined in the New Term Credit Facility) for the most recent four consecutive fiscal quarters does not exceed 2.25:1.

The ABL Facility provides for a \$40 million senior secured revolving credit facility with a \$20 million sub-limit on letters of credit. Availability under the ABL Facility is subject to a borrowing base that is based on a specified percentage of eligible accounts receivable and inventory. The term of the ABL Facility is five years, provided that if any of the Senior Notes remain outstanding in March 2018, the ABL Facility would mature at that time.

We used the borrowings under the New Term Credit Facility to refinance all of our outstanding indebtedness under our previously existing senior secured term loan and revolving credit facility entered into in 2011 (the "2011 Credit Facility"). We intend to draw upon the ABL Facility from time-to-time for working capital and general corporate purposes.

The New Term Credit Facility will require us to make amortization payments (payable in quarterly installments) equal to 1% of principal per annum with respect to the Term Loans with the remaining amount due at final maturity. Voluntary prepayments will be permitted, in whole or in part, subject to minimum prepayment requirements; provided that prepayments made prior to the date that is six months after the Closing Date of the New Term Credit Facility for the purpose of repricing or effectively repricing the term loan facilities must include a 1.0% prepayment premium; provided, further, that voluntary prepayments of loans bearing interest at the London Interbank Offered Rate ("LIBOR") on a date other than the last day of the relevant interest period will be subject to the payment of customary breakage costs.

The interest rates under the New Term Credit Facility will be calculated, at our option, at either the base rate or LIBOR, plus a margin of 4.00% and 5.00%, respectively. Each of the base rate and LIBOR shall be subject to a minimum of 2.25% and 1.25%, respectively. If our Senior Secured Leverage Ratio (as defined in the \$200 Million New Credit Facility) is less than 2.00:1 at any quarterly determination date, then the margins over the base rate and LIBOR will be 3.50% and 4.50%, respectively.

Depending on whether advances are made in U.S. Dollars or Canadian Dollars, interest rates under the ABL Facility will be calculated, at our option, at either a U.S.-based or Canadian-based base rate ("Base Rate Loans") or LIBOR or the Canadian Dealer Offered Rate ("CDOR") (each, "Fixed Rate Loans"), respectively, plus a margin of 1.25% for Base Rate Loans and a margin of 2.25% for Fixed Rate Loans. If we draw advances on the ABL Facility that are greater than 33.3% but less than or equal to 66.7% of the \$40 million limit, then the margins on Base Rate Loans and Fixed Rate Loans drop to 1.00% and 2.00%, respectively. The margins drop to 0.75% and 1.75%, respectively, if advances under the ABL Facility are greater than 66.7% of the \$40 million limit. In addition to paying interest on outstanding advances under the ABL Facility, we will be required to pay a commitment fee to the lenders in respect of the unutilized commitments at a rate equal to 0.50% per annum if advances under the ABL Facility are less than or equal to 50% of the commitments or a rate equal to 0.375% per annum if advances under the ABL are more than 50% of the commitments.

The obligations under the New Credit Facility will be guaranteed by all of our existing and future direct and indirect subsidiaries that are organized in the United States (subject to certain exceptions in the case of immaterial subsidiaries and joint ventures) and, in the case of the ABL Facility, by Xerium Canada Inc. and any future Canadian subsidiaries, provided that non-U.S. guarantors will only be liable for obligations of Xerium Canada Inc. and any other Canadian borrowers. The New Term Credit Facility is secured by a first-priority perfected security interest in substantially all of the assets of the Company, Xerium Canada Inc. and such subsidiary guarantors (collectively, the "Loan Parties"), in each case, now owned or later acquired, except with respect to the Loan Parties' accounts receivables and inventory, which are secured by a second-priority interest. The ABL Facility is secured by a first-priority

perfected security interest in the Loan Parties' accounts receivables and inventory, and a second-priority interest in substantially all of the Loan Parties' other assets. In each case, the security interests are subject to certain exceptions and legal and tax considerations and requirements, including that only 65% of the voting capital stock of the domestic Loan Parties' "first-tier" non-U.S. subsidiaries is required to be pledged in respect of the obligations of the Company and the U.S. guarantors under the New Credit Facility.

The New Credit Facility contains certain customary covenants that, subject to exceptions, restrict our ability to, among other things:

- declare dividends or redeem or repurchase equity interests;
- prepay, redeem or purchase debt;
- incur liens and engage in sale-leaseback transactions;

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- make loans and investments;
- incur additional indebtedness;
- amend or otherwise alter debt and other material agreements;
- make capital expenditures in excess of \$42 million per fiscal year, subject to adjustment;
- engage in mergers, acquisitions and asset sales;
- transact with affiliates; and
- engage in businesses that are not related to the Company's existing business.

The New Credit Facility eliminates the interest coverage and leverage coverage ratio maintenance tests that were contained in the 2011 Credit Facility. However, the ABL Facility contains a springing Fixed Charge Coverage Ratio (as defined in the ABL Facility), which must be not less than 1.00:1 during periods in which our Global Excess Availability (as defined in the ABL Facility and generally, equal to our borrowing base less outstanding borrowings under the ABL Facility and trade payables at least 60 days past due) falls below certain minimum thresholds.

The New Credit Facility contains certain customary representations and warranties, affirmative covenants and events of default, including payment defaults, breaches of representations and warranties, covenant defaults, cross-defaults and cross-acceleration to certain indebtedness, certain events of bankruptcy, certain triggering events under U.S. and, in the case of the ABL Facility, Canadian employee benefit plans, material judgments, actual or asserted failures of any guarantee or security document supporting the New Credit Facility to be in full force and effect and a change of control. If an event of default occurs, the lenders under the New Credit Facility would be entitled to take various enforcement actions, including acceleration of amounts due under the New Credit Facility and all actions permitted to be taken by a secured creditor.

On May 26, 2011, we completed a refinancing transaction, which replaced certain of our then outstanding indebtedness with \$240 million aggregate principal amount of 8.875% senior unsecured notes (the "Notes"). The Notes contain customary covenants that, subject to certain exceptions, restrict our ability to enter into certain transactions and engage in certain activities.

We are in compliance with all covenants under the Notes and New Credit Facility at September 30, 2013.

Critical Accounting Policies

The condensed consolidated financial statements are prepared in conformity with accounting principles generally accepted in the United States ("GAAP"). The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses. Actual results could differ from those estimates.

Our significant policies are described in the notes to the condensed consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2012. Judgments and estimates of uncertainties are required in applying our accounting policies in many areas. There have been no material changes to the critical accounting policies affecting the application of those accounting policies as noted in our Annual Report on Form 10-K for the year ended December 31, 2012.

Non-GAAP Financial Measures

We use EBITDA and Adjusted EBITDA (each as defined in the New Term Credit Facility) as supplementary non-GAAP liquidity measures to assist us in evaluating our liquidity and financial performance, specifically our ability to service indebtedness and to fund ongoing capital expenditures. Neither EBITDA nor Adjusted EBITDA should be considered in isolation or as a substitute for income (loss) from operations or cash flows (as determined in accordance with GAAP).

EBITDA is defined as net income (loss) before interest expense, income tax provision (benefit) and depreciation (including non-cash impairment charges) and amortization.

"Adjusted EBITDA" means, with respect to any period, the total of (A) the consolidated net income for such period, plus (B) without duplication, to the extent that any of the following were deducted in computing such consolidated net

income for such period: (i) provision for taxes based on income or profits, including, without limitation, federal, state, provincial, franchise and similar taxes, including any penalties and interest relating to any tax examinations, (ii) consolidated interest expense, (iii) consolidated depreciation and amortization expense, (iv) reserves for inventory in connection with plant closures, (v) consolidated operational restructuring costs, subject to annual limitations provided for in the Credit Facility, (vi) non-cash charges resulting from the application of purchase accounting, including push-down accounting, (vii) non-cash expenses

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resulting from the granting of common stock, stock options, restricted stock or restricted stock unit awards under equity compensation programs solely with respect to common stock, and cash expenses for compensation mandatorily applied to purchase common stock, (viii) non-cash items relating to a change in or adoption of accounting policies, (ix) non-cash expenses relating to pension or benefit arrangements, (x) expenses incurred as a result of the repurchase, redemption or retention of common stock earned under equity compensation programs solely in order to make withholding tax payments, (xi) amortization or write-offs of deferred financing costs, (xii) any non-cash losses resulting from mark to market hedging obligations (to the extent the cash impact resulting from such loss has not been realized in such period) and (xiii) other non-cash losses or charges (excluding, however, any non-cash loss or charge which represents an accrual of, or a reserve for, a cash disbursement in a future period), minus (C) without duplication, to the extent any of the following were included in computing consolidated net income for such period, (i) non-cash gains with respect to the items described in clauses (vi), (vii), (ix), (xi), (xii) and (xiii) (other than, in the case of clause (xiii), any such gain to the extent that it represents a reversal of an accrual of, or reserve for, a cash disbursement in a future period) of clause (B) above and (ii) provisions for tax benefits based on income or profits. Notwithstanding the foregoing, Adjusted EBITDA, as defined in the credit facility and calculated below, may not be comparable to similarly titled measurements used by other companies.

Consolidated net income is defined as net income (loss) determined on a consolidated basis in accordance with GAAP; provided, however, that the following, without duplication, shall be excluded in determining consolidated net income: (i) any net after-tax extraordinary or non-recurring gains, losses or expenses (less all fees and expenses relating thereto), (ii) the cumulative effect of changes in accounting principles, (iii) any fees and expenses incurred during such period in connection with the issuance or repayment of indebtedness, any refinancing transaction or amendment or modification of any debt instrument, in each case, as permitted under the Credit Facility and (iv) any cancellation of indebtedness income.

The following table provides reconciliation from net (loss) income and operating cash flows, which are the most directly comparable GAAP financial measures, to EBITDA and Adjusted EBITDA.

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	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2013	2012	2013	2012
Net income (loss)	\$2,104	\$(3,657)	) 711	\$(8,952)
Stock-based compensation	547	820	1,141	1,574
Depreciation	8,384	9,321	26,051	28,513
Amortization of intangibles	407	576	1,368	1,729
Deferred financing cost amortization	675	971	2,293	2,707
Foreign exchange loss on revaluation of debt	(1,296)	) 344	1,626	879
Deferred taxes	591	(22)	) 1,339	(383)
Asset impairment	—	1,600	1,078	1,600
Gain (loss) on disposition of property and equipment	161	(40)	) 154	(656)
Loss on extinguishment of debt	—	—	3,123	—
Net change in operating assets and liabilities	4,986	7,053	(8,453)	) 3,906
Net cash provided by operating activities	16,559	16,966	30,431	30,917
Interest expense, excluding amortization	8,703	8,806	29,404	25,787
Net change in operating assets and liabilities	(4,986)	) (7,053)	) 8,453	(3,906)
Current portion of income tax expense	2,472	116	7,716	3,488
Stock-based compensation	(547)	) (820)	) (1,141)	) (1,574)
Foreign exchange loss on revaluation of debt	1,296	(344)	) (1,626)	) (879)
Asset impairment	—	(1,600)	) (1,078)	) (1,600)
(Loss) gain on disposition of property and equipment	(161)	) 40	(154)	) 656
Loss on extinguishment of debt	—	—	(3,123)) —
EBITDA	23,336	16,111	68,882	52,889
Loss on extinguishment of debt	—	—	3,123	—
Stock-based compensation	547	820	1,141	1,574
Operational restructuring expenses	3,034	5,840	8,454	10,943
Inventory write off	—	—	692	—
Non-restructuring impairment expense	1	—	667	—
Legal fees related to term debt amendment	—	30	—	115
Non-recurring CEO retirement expenses	—	1,600	—	3,096
China plant startup costs	296	—	296	—
Adjusted EBITDA	\$27,214	\$24,401	\$83,255	\$68,617

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our foreign currency exposure and interest rate risks as of September 30, 2013 have not materially changed from December 31, 2012 (see Item 7A of our Annual Report on Form 10-K for the year ended December 31, 2012). As of September 30, 2013, we had outstanding long-term debt with a carrying amount of \$435.0 million with an approximate fair value of \$447.1 million.

ITEM 4. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures. We have carried out an evaluation, as of September 30, 2013 under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Act"). Based upon that evaluation, our principal executive officer and principal financial officer concluded that our disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed by us

in the reports that we file or submit under the Act is (i) recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms; and (ii) accumulated and communicated to our management, including our principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosures. No evaluation of

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disclosure controls and procedures can provide absolute assurance that these controls and procedures will operate effectively under all circumstances. However, our disclosure controls and procedures are designed to provide reasonable assurance of achieving their objectives, and our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures are effective at the reasonable assurance level as set forth above.

(b) Changes in Internal Control over Financial Reporting. No change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Act) occurred during the quarter ended September 30, 2013 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

There have been no material developments to the legal proceedings described in our Annual Report on Form 10-K for the year ended December 31, 2012. See Notes 4 and 9 to our Unaudited Condensed Consolidated Financial Statements for a discussion of our Brazilian operating subsidiary's proceedings before the Federal Reserve Department of Brazil and other routine litigation to which we are subject.

ITEM 1A. RISK FACTORS

The risks described in our Annual Report on Form 10-K for the year ended December 31, 2012 have not materially changed.

ITEM 6. EXHIBITS

See the exhibit index following the signature page to this Quarterly Report on Form 10-Q.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

XERIUM TECHNOLOGIES, INC.
(Registrant)

November 6, 2013

By: /s/Clifford E. Pietrafitta
Clifford E. Pietrafitta
Executive Vice President and CFO
(Principal Financial Officer)

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EXHIBIT INDEX

Exhibit Number	Description of Exhibits
10.1	Employment Agreement of William Butterfield
31.1	Certification Statement of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification Statement of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification Statement of the Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification Statement of the Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document