Holloway Lodging Corporation

Interim Condensed Consolidated Financial Statements
(Unaudited)
September 30, 2017
(in thousands of Canadian dollars)

November 9, 2017

Management's Report

The accompanying unaudited interim condensed consolidated financial statements of **Holloway Lodging Corporation** (the "Company") have been prepared by the Company's management. The unaudited interim condensed consolidated financial statements have been prepared in accordance with International Financial Reporting Standards and contain estimates based on management's judgment. The unaudited interim condensed consolidated financial statements include some amounts and assumptions based on management's best estimates which have been derived with careful judgment.

In fulfilling its responsibilities, management has developed and maintains a system of internal accounting controls. These controls are designed to ensure that the financial records are reliable for preparation of the unaudited interim condensed consolidated financial statements. The Board of Directors have reviewed and approved these unaudited interim condensed consolidated financial statements.

(signed) *"Felix Seiler"*
Acting Chief Executive Officer

(signed) *"Jane Rafuse"*
Chief Financial Officer

Holloway Lodging Corporation

Interim Condensed Consolidated Statements of Financial Position

(Unaudited)

As at September 30, 2017

(in thousands of Canadian dollars)

	September 30, 2017 $	December 31, 2016 $
Assets		
Current assets		
Cash	1,387	1,183
Trade and other receivables	5,387	3,580
Insurance proceeds receivable (note 8)	817	–
Capital reserve - restricted	–	3,371
Inventories	488	533
Prepaid expenses and deposits	1,921	2,819
	10,000	11,486
Non-current assets		
Property and equipment (notes 4 and 8)	286,244	305,624
Loan receivable	4,992	5,371
Other assets	715	746
Deferred income tax assets	25,760	28,172
	317,711	339,913
Total assets	327,711	351,399
Liabilities		
Current liabilities		
Secured credit facilities (note 5)	30,239	17,630
Trade payables and accrued liabilities	11,215	9,640
Accrued interest on convertible debentures	1,348	1,304
Current portion of mortgages payable (note 5)	8,792	94,166
Share-based liability (note 7)	480	709
	52,074	123,449
Non-current liabilities		
Mortgages payable (note 5)	77,162	33,130
Convertible debentures (note 6)	90,345	89,815
	167,507	122,945
Total liabilities	219,581	246,394
Equity		
Equity attributable to shareholders of the Company	106,165	103,118
Non-controlling interest	1,965	1,887
Total equity	108,130	105,005
Total liabilities and equity	327,711	351,399

The accompanying notes are an integral part of these unaudited interim condensed consolidated financial statements.

Holloway Lodging Corporation

Interim Condensed Consolidated Statements of Income

(Unaudited)

For the three and nine months ended September 30, 2017 and 2016

(in thousands of Canadian dollars)

	For the three months ended		For the nine months ended	
	September 30, 2017 $	September 30, 2016 $	September 30, 2017 $	September 30, 2016 $
Revenues				
Rooms	27,790	28,345	68,677	69,808
Food and beverage	2,192	2,482	7,477	8,352
Rental	291	345	951	1,030
Other	1,713	1,042	3,699	2,627
	31,986	32,214	80,804	81,817
Hotel expenses				
Operating expenses	17,804	18,669	50,982	53,143
Property taxes and insurance	1,495	1,498	4,701	4,934
Depreciation and amortization	3,828	4,016	11,562	11,530
	23,127	24,183	67,245	69,607
Income before the following	8,859	8,031	13,559	12,210
Other (income) and expenses				
Interest and accretion on debt	3,269	4,026	11,042	12,054
Corporate and administrative	671	537	1,956	1,236
Share-based expense (recovery)	(12)	217	269	180
Investment income	(155)	(157)	(484)	(478)
Management services income	(27)	(49)	(156)	(49)
Insurance proceeds, net of clean-up and other costs (note 8)	(1,228)	–	(1,476)	–
Loss (gain) on disposals of property and equipment and repurchase of convertible debentures (note 8)	920	(2,834)	(6,562)	(2,685)
Reversal of impairment of hotel properties	–	–	–	(1,100)
Acquisition and redevelopment costs	–	4	10	634
Unrealized foreign exchange loss (gain)	207	(75)	395	(93)
Realized foreign exchange loss	–	–	–	926
	3,645	1,669	4,994	10,625
Income before income taxes	5,214	6,362	8,565	1,585
Provision for income taxes (note 9)	1,486	1,580	2,412	391
Net income for the period	3,728	4,782	6,153	1,194
Attributable to:				
Shareholders of the Company	3,658	4,834	6,075	1,258
Non-controlling interest	70	(52)	78	(64)
	3,728	4,782	6,153	1,194
Basic earnings per share (note 10)	0.19	0.26	0.32	0.07
Diluted earnings per share (note 10)	0.19	0.25	0.32	0.07

The accompanying notes are an integral part of these unaudited interim condensed consolidated financial statements.

Holloway Lodging Corporation

Interim Condensed Consolidated Statements of Comprehensive Income

(Unaudited)

For the three and nine months ended September 30, 2017 and 2016

(in thousands of Canadian dollars)

	For the three months ended		For the nine months ended	
	September 30, 2017 $	September 30, 2016 $	September 30, 2017 $	September 30, 2016 $
Net income for the period	3,728	4,782	6,153	1,194
Other comprehensive income				
Items that may be subsequently reclassified to profit or loss				
Cumulative translation adjustments	–	–	–	21
Items reclassified to profit or loss				
Cumulative translation adjustments	–	–	(337)	–
Other comprehensive income	–	–	(337)	21
Comprehensive income for the period	3,728	4,782	5,816	1,215
Comprehensive income attributable to:				
Shareholders of the Company	3,658	4,834	5,738	1,279
Non-controlling interest	70	(52)	78	(64)
	3,728	4,782	5,816	1,215

The accompanying notes are an integral part of these interim condensed consolidated financial statements.

Holloway Lodging Corporation

Interim Condensed Consolidated Statements of Changes in Equity

(Unaudited)

For the nine months ended September 30, 2017 and 2016

(in thousands of Canadian dollars)

	Common shares $	Contributed surplus $	Deficit $	Accumulated other comprehensive income $	Equity attributable to shareholders of the Company $	Non-controlling interest $	Total equity $
Balance, January 1, 2016	228,169	1,842	(122,890)	316	107,437	2,151	109,588
Net income for the period	–	–	1,258	–	1,258	(64)	1,194
Other comprehensive income for the period	–	–	–	21	21	–	21
Comprehensive income for the period	–	–	1,258	21	1,279	(64)	1,215
Dividends paid to shareholders	–	–	(1,983)	–	(1,983)	–	(1,983)
Repurchase of common shares	(1,755)	1,104	–	–	(651)	–	(651)
Balance, September 30, 2016	226,414	2,946	(123,615)	337	106,082	2,087	108,169
Balance, January 1, 2017	226,414	2,946	(126,579)	337	103,118	1,887	105,005
Net income for the period	–	–	6,075	–	6,075	78	6,153
Other comprehensive income for the period	–	–	337	(337)	–	–	–
Comprehensive income for the period	–	–	6,412	(337)	6,075	78	6,153
Dividends paid to shareholders	–	–	(1,979)	–	(1,979)	–	(1,979)
Repurchase of common shares	(2,410)	1,361	–	–	(1,049)	–	(1,049)
Balance, September 30, 2017	224,004	4,307	(122,146)	–	106,165	1,965	108,130

The accompanying notes are an integral part of these unaudited interim condensed consolidated financial statements.

Holloway Lodging Corporation

Interim Condensed Consolidated Statements of Cash Flows

(Unaudited)

For the nine months ended September 30, 2017 and 2016

(in thousands of Canadian dollars)

	For the nine months ended September 30, 2017 $	September 30, 2016 $
Cash provided by (used in)		
Operating activities		
Net income for the period	6,153	1,194
Adjustments for non-cash items (note 11)	9,152	9,257
	15,305	10,451
Changes in items of working capital (note 11)	(1,698)	(1,382)
Net cash generated from operating activities	13,607	9,069
Investing activities		
Decrease (increase) in capital reserves and additions to other assets	3,344	(909)
Acquisition of hotel properties and additions to property and equipment	(11,106)	(17,371)
Proceeds from sales of hotel properties and equipment, net of costs (note 4)	26,437	8,729
Net cash provided by (used in) investing activities	18,675	(9,551)
Financing activities		
Proceeds from (repayment of) secured credit facilities (note 5)	12,609	(2,007)
Proceeds from mortgages, net of deferred financing fees (note 5)	56,158	11,896
Repayment of mortgages and loan payable (note 5)	(97,604)	(7,526)
Repurchase of common shares	(1,049)	(651)
Repurchase of convertible debentures	(213)	(106)
Dividends paid to shareholders	(1,979)	(1,983)
Net cash used in financing activities	(32,078)	(377)
Increase (decrease) in cash	204	(859)
Cash – Beginning of period	1,183	2,059
Cash – End of period	1,387	1,200
Supplemental cash flow information		
Interest paid	10,280	11,013

Cash is comprised of cash on hand and balances with banks.

The accompanying notes are an integral part of these unaudited interim condensed consolidated financial statements.

(in thousands of Canadian dollars, except shares, share prices and earnings per share)

1 General information

Holloway Lodging Corporation, together with its subsidiaries ("Holloway" or the "Company") is a hospitality company that owns and operates hotels. As at September 30, 2017, the Company owned and operated 32 hotels and held a 62% interest in another hotel in Canada, with a total of 3,764 confirmed guest rooms. The address of its registered office is 6009 Quinpool Road, 10th Floor, Halifax, Nova Scotia.

The results of operations for the nine months ended September 30, 2017 represent the operations of 33 hotels for the full period and 2 hotels for part of the period as the Company:

- sold the Holiday Inn® in Oakville, ON on January 16, 2017; and
- sold the Travelodge® in Belleville, ON on March 17, 2017.

The results of operations for the nine months ended September 30, 2016 represent the operations of 34 hotels for the full period and 2 hotels for part of the period as the Company:

- acquired the Westmark® Whitehorse Hotel and Conference Center in Whitehorse, YT on April 8, 2016; and
- sold the Travelodge® hotel in Barrie, ON on September 26, 2016.

The Company's financial results for an individual quarter are not necessarily indicative of results to be expected for the full year. Revenue from hotel operations tends to fluctuate throughout the year. The Company's third quarter revenues are generally the strongest of the year.

2 Basis of preparation and critical accounting estimates

These unaudited interim condensed consolidated financial statements ("condensed financial statements") have been prepared in accordance with generally accepted accounting principles in Canada as set out in the CPA Canada Handbook – Accounting – Part 1 which incorporates International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board and in accordance with IAS 34 – *"Interim Financial Reporting"*. The accounting policies followed in these condensed financial statements are the same as those applied in the Company's audited annual financial statements for the year ended December 31, 2016. These condensed financial statements should be read in conjunction with the Company's audited annual financial statements for the year ended December 31, 2016.

These condensed financial statements were approved for issue by the Board of Directors on November 9, 2017.

Critical accounting estimates

Property and equipment

During the nine months ended September 30, 2016, the Company increased the carrying value of two hotels or cash generating units ("CGUs") by reversing previously recorded impairments by $1,100. The recoverable amount of the CGUs was determined by independent third party appraisals.

(in thousands of Canadian dollars, except shares, share prices and earnings per share)

3 New standards and interpretations not yet adopted

IFRS 15, Revenue from Contracts and Customers

IFRS 15, "*Revenue from Contacts and Customers*" ("IFRS 15") is effective for annual periods beginning on or after January 1, 2018, with early adoption permitted. IFRS 15 establishes a new control-based revenue recognition model and replaces IAS 18, "*Revenue*" and IAS 11, "*Construction Contracts*", and some revenue related interpretations. The underlying principle is that an entity will recognize revenue to depict the transfer of goods and services to customers at an amount the entity expects to be entitled to in exchange for those goods and services. The Company is currently evaluating the new standard and does not expect there to be a material impact on its consolidated financial statements. The Company has selected the modified retrospective approach as its transition method for this standard.

IFRS 9, Financial Instruments

IFRS 9, "*Financial Instruments*" ("IFRS 9") will replace IAS 39, "*Financial instruments: recognition and measurement*". The standard is effective for annual periods beginning on or after January 1, 2018. IFRS 9 includes requirements for recognition and measurement, impairment, derecognition and general hedge accounting. The Company is currently evaluating the impact of this new standard on its consolidated financial statements.

IFRS 16, Leases

IFRS 16, "*Leases*" ("IFRS 16"), will replace IAS 17, "*Leases*". The new standard results in substantially all leases being recorded on the consolidated statement of financial position of the lessee. IFRS 16 is effective for annual periods beginning on or after January 1, 2019, with early adoption permitted. The Company is currently evaluating the impact of this new standard on its consolidated financial statements.

4 Disposals of property and equipment

Holiday Inn®, Oakville, ON

On January 16, 2017, the Company sold the Holiday Inn® hotel in Oakville, ON for gross proceeds of $19,438. After closing costs, the net cash proceeds were $19,196. The Company recognized a gain on disposal of property and equipment of $7,832 in the interim condensed consolidated statements of income.

Travelodge®, Belleville, ON

On March 17, 2017, the Company sold the Travelodge® hotel in Belleville, ON for gross proceeds of $7,000. After repayment of the existing mortgage and closing costs, the net cash proceeds were $3,453. The Company recognized a loss on disposal of property and equipment of $144 in the interim condensed consolidated statements of income.

(in thousands of Canadian dollars, except shares, share prices and earnings per share)

5 Secured credit facilities and mortgages payable

In May, 2017, the Company repaid eleven mortgages totaling $90,385 which were to mature in May and July 2017. The Company secured financing with a new lender through a loan consisting of a $50,000 mortgage and a $30,000 secured credit facility. The mortgage bears interest at prime plus 1.50%, has an option to convert the interest to a fixed rate, an amortization period of seventeen years and a five year term. The secured credit facility bears interest at prime plus 1.50%. The Company drew $15,000 on the secured credit facility in May 2017, of which $5,000 was repaid in July 2017. Both the mortgage and secured credit facility are secured by ten hotels.

In July, 2017, the Company drew $6,866 on a mortgage secured by two hotels. The mortgage with a maximum principal amount of $17,500, bears interest at 4.45%, has a fifteen year amortization period and a five year term. The Company drew $5,634 on this mortgage in October 2017 (note 14).

6 Convertible debenture

In August, 2017, the Company obtained approval to amend the Series C Debentures as follows: (1) extend the maturity of the Series C Debentures by three years to September 30, 2021; (2) amend the conversion price to $12.50 per common share; and (3) provide holders with the option to exchange their Series C Debentures for a new series of debentures upon receiving an exchange notice from the Company. The Company also obtained approval to amend the Series B Debentures to provide holders with the option to exchange their Series B Debentures for a new series of debentures upon receiving an exchange notice from the Company. The amendment has been accounted for as a modification.

7 Share-based liability

On March 29, 2017, the Company granted a total of 285,000 options to purchase common shares to directors and certain employees with an exercise price of $5.36 per share. The options vest equally over three years commencing on March 29, 2018 and expire after seven years. On March 18, 2016, the Company granted a total of 200,000 options to purchase common shares to directors and certain employees with an exercise price of $4.80 per share. The options vest equally over three years commencing on March 18, 2017 and expire after seven years. The fair value of the options were measured at the grant date using the Black-Scholes option pricing model with the following assumptions (not in thousands of dollars):

	Option grant March 2017	Option grant March 2016
Exercise price	$5.36	$4.80
Closing price on grant date	$5.35	$4.76
Volatility	44.3%	46.9%
Annual dividend yield	2.6%	2.9%
Expected option life	7 years	7 years
Annual risk-free interest rate	1.3%	1.1%
Fair value per option	$1.86	$1.61

(in thousands of Canadian dollars, except shares, share prices and earnings per share)

8 Insurance proceeds

On March 17, 2017, the Super 8® in Grande Prairie, AB was damaged due to a significant release of water into the hotel. This event resulted in an insurance claim under the Company's insurance policy. The hotel re-opened on October 1, 2017.

The Company has spent $1,443 on capital improvements to the hotel and has recorded $632 in business interruption insurance (included in other revenues) and $1,452 in property and contents insurance, net of clean-up and other costs. The Company recorded a loss on disposal of $1,055 on the write-off of the building components and equipment that were damaged.

9 Income taxes

The following table is a reconciliation of the expected deferred income tax expense at the statutory rate to the amounts recognized in the interim consolidated statement of income:

	For the three months ended		For the nine months ended	
	September 30, 2017 $	September 30, 2016 $	September 30, 2017 $	September 30, 2016 $
Income before income taxes	5,214	6,362	8,565	1,585
Combined statutory income tax rate	27.54%	27.27%	27.54%	27.27%
Income tax expense at the combined statutory income tax rate	1,436	1,735	2,359	432
Non-taxable portion of losses (gains)	37	(198)	(457)	(102)
Non-deductible expenses	2	64	90	64
Change in tax rates	–	(5)	(13)	6
Other	11	(16)	433	(9)
Provision for income taxes	1,486	1,580	2,412	391

The statutory tax rate was 27.54% for the nine months ended September 30, 2017 (for the nine months ended September 30, 2016 - 27.27%). The income tax provision will not require an outlay of cash due to available non-capital loss carry forwards.

(in thousands of Canadian dollars, except shares, share prices and earnings per share)

10 Share capital and earnings per share

Basic

Basic earnings per share is calculated by dividing the net income attributable to shareholders of the Company by the weighted average number of shares outstanding during the period.

	For the three months ended		For the nine months ended	
	September 30, 2017 $	September 30, 2016 $	September 30, 2017 $	September 30, 2016 $
Net income attributable to shareholders of the Company	3,658	4,834	6,075	1,258
Weighted average number of shares outstanding	18,819,405	18,889,066	18,864,615	18,896,757
Basic earnings per share	0.19	0.26	0.32	0.07

Diluted

Diluted earnings per share for the three and nine months ended September 30, 2017 and 2016 is calculated by adjusting the weighted average number of shares outstanding to assume conversion of all potentially dilutive instruments convertible into shares. During the three and nine months ended September 30, 2017 and 2016, the Company had two categories of potentially dilutive instruments – convertible debentures and options. This calculation is done to determine the number of shares that could have been acquired at fair value based on the subscription rights of the convertible debentures and options. For the three and nine months ended September 30, 2017 and 2016, the convertible debentures were anti-dilutive.

Diluted earnings per share for the three and nine months ended September 30, 2017 is presented below:

	For the three months ended		For the nine months ended	
	September 30, 2017 $	September 30, 2016 $	September 30, 2017 $	September 30, 2016 $
Diluted income arrtibutable to shareholders of the Company	3,658	4,834	6,075	1,258
Weighted average number of diluted shares	18,850,656	18,960,213	18,896,669	18,954,610
Diluted earnings per share	0.19	0.25	0.32	0.07

At September 30, 2017, there were 18,694,566 common shares outstanding. During the nine months ended September 30, 2017, the Company repurchased and cancelled 194,500 shares at a cost of $1,049 (average price of $5.39 per share).

(in thousands of Canadian dollars, except shares, share prices and earnings per share)

11 Supplemental cash flow information

Adjustments for non-cash items:

	For the nine months ended	
	September 30, 2017 $	September 30, 2016 $
Depreciation and amortization	11,583	11,590
Accretion on debt and unrealized foreign exchange loss	1,450	881
Share-based expense	269	180
Gain on disposals of property and equipment and repurchase of convertible debentures	(6,562)	(2,685)
Reversal of impairment of hotel properties	–	(1,100)
Provision for income taxes	2,412	391
	9,152	9,257

Changes in items of working capital:

	For the nine months ended	
	September 30, 2017 $	September 30, 2016 $
Trade, insurance proceeds and other receivables	(2,656)	(2,184)
Inventories	45	(115)
Prepaid expenses and deposits	898	(638)
Trade payables and accrued liabilities	(29)	1,502
Accrued interest on convertible debentures	44	53
	(1,698)	(1,382)

12 Related party transactions

Clarke Inc. and the Clarke Pension Plan are considered related parties of Holloway. During the first quarter of 2016, the Company repaid a mortgage of $2,429 from the Clarke Pension Plan. No related party mortgages remain outstanding.

13 Financial instruments and fair values

The following table shows the financial instruments which have fair values that differ from their carrying values:

	September 30, 2017		December 31, 2016	
	Carrying value $	Fair value $	Carrying value $	Fair value $
Mortgages payable	85,894	86,421	127,296	126,172
Convertible debentures	90,345	89,148	89,815	88,207

The methods and assumptions used in estimating the fair values are consistent with those applied in the Company's audited annual financial statements for the year ended December 31, 2016.

(in thousands of Canadian dollars, except shares, share prices and earnings per share)

14 Subsequent events

On October 2, 2017, the Company extended a mortgage on one of its hotels with a principal amount of $4,902 which was to mature in April 2018. The interest rate was reduced from 4.81% to 4.29%. The mortgage has a fifteen year amortization period and a five-year term.

On October 6, 2017, the Company drew $5,634 on a mortgage secured by two hotels (note 5). The proceeds were used to reduce its secured credit facilities.