Holloway Lodging Corporation

Interim Consolidated Condensed Financial Statements
(Unaudited)
June 30, 2015
(in thousands of Canadian dollars)

August 12, 2015

Management's Report

The accompanying unaudited interim consolidated condensed financial statements of **Holloway Lodging Corporation** (the "Company") have been prepared by the Company's management. The unaudited interim consolidated condensed financial statements have been prepared in accordance with International Financial Reporting Standards and contain estimates based on management's judgment. The unaudited interim consolidated condensed 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 consolidated condensed financial statements. The Board of Directors have reviewed and approved these unaudited interim consolidated condensed financial statements.

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

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

Holloway Lodging Corporation

Interim Consolidated Statements of Financial Position

(Unaudited)

As at June 30, 2015

(in thousands of Canadian dollars)

	June 30, 2015 $	December 31, 2014 $
Assets		
Current assets		
Cash	1,375	3,473
Restricted cash	371	347
Trade and other receivables	5,078	5,697
Inventories	474	597
Prepaid expenses and deposits	3,828	2,258
Current portion of loans receivable (note 6)	1,925	–
	13,051	12,372
Non-current assets		
Property and equipment (note 4)	320,864	330,307
Franchise business (note 5)	–	14,700
Minority interest investments in hotel properties	–	190
Capital reserve – restricted	2,674	2,304
Loans receivable (note 6)	4,996	–
Other assets	514	616
Deferred income tax assets	23,530	21,800
Funds held on behalf of franchisees	–	167
	352,578	370,084
Total assets	365,629	382,456
Liabilities		
Current liabilities		
Trade payables and accrued liabilities	11,711	12,210
Accrued interest on convertible debentures	1,309	1,309
Current portion of secured credit facilities	9,576	9,007
Current portion of mortgages and loan payable	13,204	6,248
Share-based payment liability	689	–
	36,489	28,774
Non-current liabilities		
Secured credit facilities	–	18,000
Mortgages and loan payable	118,634	129,510
Convertible debentures	88,627	88,061
Funds to be spent on behalf of franchisees	–	167
	207,261	235,738
Total liabilities	243,750	264,512
Equity		
Equity attributable to shareholders of the Company	119,831	115,913
Non-controlling interest	2,048	2,031
Total equity	121,879	117,944
Total liabilities and equity	365,629	382,456

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

Holloway Lodging Corporation

Interim Consolidated Statements of Income (Loss)

(Unaudited)

For the three and six months ended June 30, 2015 and 2014

(in thousands of Canadian dollars)

	For the three months ended		For the six months ended	
	June 30, 2015	June 30, 2014	June 30, 2015	June 30, 2014
	$	$	$	$
Hotel revenues				
Rooms	24,582	13,150	48,456	27,113
Food and beverage	2,817	927	5,627	1,977
Franchising	–	–	412	–
Other	1,164	308	2,546	647
	28,563	14,385	57,041	29,737
Hotel expenses				
Operating expenses	18,175	8,051	37,685	16,710
Property taxes and insurance	1,595	841	3,376	1,671
Management fees	–	314	121	642
Depreciation and amortization	3,464	2,267	7,147	4,557
	23,234	11,473	48,329	23,580
Income before the following	5,329	2,912	8,712	6,157
Other (income) and expenses				
Interest and accretion on debt	4,004	1,796	8,359	3,574
Corporate and administrative	575	400	1,433	892
Share-based compensation	67	75	141	151
Investment income	(149)	(100)	(149)	(161)
Gain on disposals of property and equipment, franchise business, minority interest investment in hotel property and repurchase of convertible debentures	(58)	(45)	(8,113)	(7)
Fair value adjustment and amounts reclassified to profit and loss on minority interest investments in hotel properties	–	(689)	–	(689)
Impairment (reversal of impairment) of hotel property	2,700	–	2,700	(1,217)
Acquisition costs	–	639	135	649
	7,139	2,076	4,506	3,192
Income (loss) before income taxes	(1,810)	836	4,206	2,965
Provision for (recovery of) deferred income taxes (note 7)	(930)	230	(1,730)	800
Net income (loss) for the period	(880)	606	5,936	2,165
Attributable to:				
Shareholders of the Company	(907)	606	5,919	2,176
Non-controlling interest	27	–	17	(11)
	(880)	606	5,936	2,165
Basic earnings (loss) per share (note 8)	(0.05)	0.03	0.31	0.12
Diluted earnings (loss) per share (note 8)	(0.05)	0.03	0.30	0.12

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

Holloway Lodging Corporation

Interim Consolidated Statements of Comprehensive Income (Loss)

(Unaudited)

For the three and six months ended June 30, 2015 and 2014

(in thousands of Canadian dollars)

	For the three months ended		For the six months ended	
	June 30, 2015 $	June 30, 2014 $	June 30, 2015 $	June 30, 2014 $
Net income (loss) for the period	(880)	606	5,936	2,165
Other comprehensive income (loss)				
Items that may be subsequently reclassified to profit or loss				
Cumulative translation adjustments	(26)	(66)	159	5
Fair value adjustments of minority interest investment in hotel properties	–	–	–	80
Items reclassified in the period to profit or loss				
Previously recognized fair value adjustment of minority interest investments in hotel properties	–	(390)	–	(390)
Other comprehensive income (loss)	(26)	(456)	159	(305)
Comprehensive income (loss) for the period	(906)	150	6,095	1,860
Comprehensive income (loss) attributable to:				
Shareholders of the Company	(933)	150	6,078	1,871
Non-controlling interest	27	–	17	(11)
	(906)	150	6,095	1,860

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

Holloway Lodging Corporation

Interim Consolidated Statements of Changes in Equity

(Unaudited)

For the six months ended June 30, 2015 and 2014

(in thousands of Canadian dollars)

	Common shares $	Contributed surplus $	Deficit $	Accumulated other comprehensive income (loss) $	Equity attributable to shareholders of the Company $	Non-controlling interest $	Total equity $
Balance, January 1, 2014	223,713	2,327	(140,683)	28	85,385	22	85,407
Net income for the period	–	–	2,176	–	2,176	(11)	2,165
Other comprehensive income for the period	–	–	–	(305)	(305)	–	(305)
Comprehensive income for the period	–	–	2,176	(305)	1,871	(11)	1,860
Non-controlling interest arising on acquisition of subsidiary	–	–	–	–	–	2,739	2,739
Acquisition of non-controlling interest in subsidiary	–	(90)	–	–	(90)	(11)	(101)
Dividends paid to shareholders	–	–	(1,255)	–	(1,255)	–	(1,255)
Share-based compensation	–	151	–	–	151	–	151
Repurchase of common shares	(22)	–	–	–	(22)	–	(22)
Balance, June 30, 2014	223,691	2,388	(139,762)	(277)	86,040	2,739	88,779
Balance, January 1, 2015	229,859	2,544	(116,386)	(104)	115,913	2,031	117,944
Net income for the period	–	–	5,919	–	5,919	17	5,936
Other comprehensive income for the period	–	–	–	159	159	–	159
Comprehensive income for the period	–	–	5,919	159	6,078	17	6,095
Dividends paid to shareholders	–	–	(1,356)	–	(1,356)	–	(1,356)
Share-based compensation	–	119	–	–	119	–	119
Reclassification of share-based compensation from equity-settled to cash-settled liability (note 3)	–	(816)	–	–	(816)	–	(816)
Exercise of stock options	22	(5)	–	–	17	–	17
Repurchase of common shares	(124)	–	–	–	(124)	–	(124)
Balance, June 30, 2015	229,757	1,842	(111,823)	55	119,831	2,048	121,879

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

Holloway Lodging Corporation

Interim Consolidated Statements of Cash Flows

(Unaudited)

For the six months ended June 30, 2015 and 2014

(in thousands of Canadian dollars)

	For the six months ended June 30, 2015 $	June 30, 2014 $
Cash provided by (used in)		
Operating activities		
Net income for the period	5,936	2,165
Adjustments for non-cash items (note 9)	1,067	3,705
	7,003	5,870
Changes in items of working capital (note 9)	(3,030)	43
Net cash generated from operating activities	3,973	5,913
Investing activities		
Decrease (increase) in capital reserves and restricted cash	(394)	262
Purchase of loan receivable	(1,925)	–
Proceeds from sales of property and equipment, net of costs	17,523	9,216
Proceeds from sale of franchise business, net of costs	15,758	–
Proceeds from disposal of minority interest investment in hotel property	155	–
Acquisition and additions to property and equipment	(13,716)	(10,546)
Acquisition of subsidiaries, net of cash acquired	–	(1,848)
Additions to other assets	(38)	–
Net cash provided by (used in) investing activities	17,363	(2,916)
Financing activities		
Repayment of secured credit facilities	(17,431)	(1,004)
Funds drawn on secured credit facility	–	16,000
Increase in funds held in trust	–	(16,380)
Proceeds from mortgages and loan payable, net of deferred financing fees	–	5,845
Repayment of mortgages payable	(4,361)	(2,000)
Proceeds from exercise of options	17	–
Settlement of share-based payment liability	(149)	–
Repurchase of common shares	(124)	(22)
Repurchase of convertible debentures	(30)	–
Dividends paid to shareholders	(1,356)	(1,255)
Net cash provided by (used in) financing activities	(23,434)	1,184
Increase (decrease) in cash	(2,098)	4,181
Cash – Beginning of period	3,473	852
Cash – End of period	1,375	5,033
Supplemental cash flow information		
Interest paid	7,718	3,470

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

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

(in thousands of Canadian dollars)

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 June 30, 2015, the Company owned and operated 33 hotels in Canada, one hotel in the United States and a 62% interest in another hotel in Canada, with a total of 3,967 guest rooms. The address of its registered office is 6009 Quinpool Road, 10th Floor, Halifax, Nova Scotia.

The results of operations for the six months ended June 30, 2015 represent the operations of 34 hotels for the full period and 3 hotels for part of the period as the Company:

- sold the Ramada® in Trenton, ON on January 23, 2015;
- acquired the Days Inn® in Whitehorse, YT on January 30, 2015; and
- sold the Travelodge® in Toronto, ON on February 4, 2015.

The results of operations for the six months ended June 30, 2014 represent the operations of 17 hotels for the full period and 3 hotels for part of the period as the Company:

- sold the Holiday Inn Express® in Kamloops, BC on April 1, 2014;
- acquired the Days Inn® in Whitecourt, AB on June 6, 2014; and
- acquired a controlling interest in the partnership that owns Super 8® St. John's, NL on June 25, 2014, which is now consolidated.

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 with the other three quarters being comparable to each other.

2 Basis of preparation

These unaudited interim consolidated condensed financial statements ("condensed financial statements") have been prepared in accordance with generally accepted accounting principles in Canada ("GAAP") as set out in the CPA Canada Handbook – Accounting – Part 1 ("CPA Canada Handbook") which incorporates International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"), and in accordance with IAS 34 – *"Interim Financial Reporting"*.

These condensed financial statements were approved by the Board of Directors on August 12, 2015.

3 Significant accounting policies and critical accounting estimates

Significant accounting polices

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, 2014 except as noted below. These condensed financial statements should be read in conjunction with the Company's audited annual financial statements for the year ended December 31, 2014.

(in thousands of Canadian dollars)

3 Significant accounting policies and critical accounting estimates (continued)

Cash-settled options

In the second quarter of 2015, the Company settled stock options for cash. As a result, effective May 29, 2015, the stock option obligation changed from an equity settled obligation to a cash settled obligation, recognized in the consolidated statement of financial position. The share-based payment liability is remeasured to fair value based on the number of options expected to vest at each reporting date up to and including the settlement date. Changes to the share-based payment liability are included in share-based compensation expense in the consolidated statement of income (loss).

Critical accounting estimates

Property and equipment

On June 30, 2015, the Company decreased the carrying value of one CGU by $2,700. The fair value of the CGU was based on its value in use and was determined by an internal model. A CGU is reviewed at the individual hotel level, the lowest level for which identifiable cash flows are largely independent when measuring the fair value of property and equipment. The fair value is determined based on the discounted future cash flows expected to be received from the CGU. The fair value has been determined using cash flow projections and a capitalized terminal value calculation and made maximum use of observable inputs and outputs. For periods beyond the initial budget period, cash flows were extrapolated using growth rates determined to be reasonable for the specific CGU and market in which it operates and does not exceed the anticipated long-term average growth rates for the Company's portfolio. Key factors of estimation uncertainty include:

Pre-tax discount rate	11.75%
Capitalization rate	10.50%
Growth rate	Consistent with industry and market/hotel outlook

The fair value may not reflect the realizable value in the event a particular CGU is sold by the Company.

The amount of the impairment is the amount by which the CGU's carrying value exceeds its fair value. The future cash flows expected from the use and eventual disposition involve assumptions of occupancy, room rates, revenues, expenses, the residual or terminal value for the CGU and the discount rate. In addition to these estimates, management assesses the effect of new competition in the individual markets and the hotel industry predictions of hotel demand and supply. These estimates and assumptions are subject to change. Based on this information, management estimated that the range of reasonably possible values for the asset would be between $6,836 and $8,344 for the CGU that was decreased in value using an internal model. The final value for the CGU decreased in value was $7,530.

4 Acquisition and disposals of property and equipment

Royal Host Inc.

The Company has finalized the purchase price allocation to the assets acquired and liabilities assumed. There have been no changes to the purchase price allocation since December 31, 2014.

(in thousands of Canadian dollars)

4 Acquisition and disposals of property and equipment (continued)

Ramada®, Trenton, ON

On January 23, 2015, the Company sold the Ramada® in Trenton, ON for gross proceeds of $3,950. After closing costs, the net cash proceeds were $3,760. A portion of the proceeds were used to repay a $3,000 secured credit facility in full. The Company recognized a gain on disposal of property and equipment of $116 in the consolidated statement of income (loss).

Days Inn®, Whitehorse, YT

On January 30, 2015, the Company acquired the Ramada® in Whitehorse, YT for a gross purchase price of $8,228 which was paid in cash. The property has been rebranded as a Days Inn®.

The following table summarizes the fair value of assets acquired and consideration paid at the acquisition date:

	$
Assets acquired	
Land	2,470
Building and components	4,372
Furniture, fixtures and equipment	1,250
Paving	100
Signage	11
Computer equipment	25
	8,228

The fair values and allocation to the various assets was based on the purchase and sale agreement for the property.

Included in the condensed financial statements at June 30, 2015 is revenue of $1,068 and a net income of $191. Costs of acquisition of $135 were recognized in the consolidated statement of income (loss).

Travelodge®, Toronto, ON

On February 4, 2015, the Company sold the Travelodge® in Toronto, ON for gross proceeds of $13,000. A portion of the proceeds were used to repay a $2,000 secured credit facility in full. After closing costs, the net cash proceeds were $12,715. The Company recorded a gain on disposal of property and equipment of $1,672 in the consolidated statement of income (loss).

Land, Orillia, ON

On April 15, 2015, the Company sold a vacant parcel of land in Orillia, ON for gross proceeds of $1,084. After closing costs, the net cash proceeds were $1,048. The Company recorded a gain on disposal of property and equipment of $88 in the consolidated statement of income (loss).

(in thousands of Canadian dollars)

5 Disposal of franchise business

On March 31, 2015, the Company sold the franchise business which owned the master franchise rights to the Travelodge® and Thriftlodge® hotel brands in Canada for gross proceeds of $21,030. The purchase price was satisfied with the issuance of a $4,000 USD senior secured note (note 6) and a cash payment of $15,758, net of closing costs, which was applied to a $16,000 secured credit facility which has been repaid in full. The Company recognized a gain on disposal of franchise business of $6,260 in the consolidated statement of income (loss).

6 Loans receivable

	June 30, 2015 $	December 31, 2014 $
Senior secured note receivable	4,996	–
Mortgages receivable	1,925	–
	6,921	–
Less: Current portion	1,925	–
	4,996	–

The senior secured note receivable is denominated in US dollars (US$4,000) and bears interest at 12.0%. Interest and principal payments are due semi-annually. The maturity date of the note is April 30, 2027 although the anticipated amortization period for the principal amount of the note is approximately eight years.

The mortgages receivable consist of first and second mortgages on the same property. The mortgages bear interest at 6.5% and were due on May 1, 2015. At the date of acquisition, the mortgages were in default due to non-payment of principal, interest and property taxes and the Company has commenced foreclosure proceedings against the borrower.

(in thousands of Canadian dollars)

7 Income taxes

The following table is a reconciliation of the expected deferred income tax provision (recovery) at the statutory rate to the amounts recognized in the consolidated statement of income (loss) for the three and six months ended June 30, 2015 and 2014:

	For the three months ended		For the six months ended	
	June 30, 2015 $	June 30, 2014 $	June 30, 2015 $	June 30, 2014 $
Income (loss) before income taxes	(1,810)	836	4,206	2,965
Combined statutory income tax rate	26.76%	25.87%	26.76%	25.87%
Income tax expense (recovery) at the combined statutory income tax rate	(484)	216	1,126	767
Non-taxable portion of gains	(47)	–	(2,690)	–
Non-deductible share-based compensation	18	20	38	39
Non-taxable capital gains	–	(178)	–	(178)
Non-deductible expenses	(62)	168	40	168
Change in tax rates	(469)	–	(469)	–
Other	114	4	225	4
Provision for (recovery of) deferred income taxes	(930)	230	(1,730)	800

The statutory tax rate was 26.76% for the three and six months ended June 30, 2015 (for the three and six months ended June 30, 2014 – 25.87%).

(in thousands of Canadian dollars, except share amounts)

8 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 six months ended	
	June 30, 2015 $	June 30, 2014 $	June 30, 2015 $	June 30, 2014 $
Net income (loss) attributable to shareholders of the Company	(907)	606	5,919	2,176
Weighted average number of shares outstanding	19,355,287	17,927,847	19,356,594	17,928,919
Basic earnings (loss) per share	(0.05)	0.03	0.31	0.12

Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of shares outstanding to assume conversion of all potentially dilutive instruments convertible into shares. 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, options and warrants. During the three and six months ended June 30, 2015, the Company had two categories of potentially dilutive instruments – convertible debentures and options. During the three and six months ended June 30, 2014, the Company had two categories of potentially dilutive instruments – options and warrants. For the three and six months ended June 30, 2014 and the three months ended June 30, 2015, the options and warrants were anti-dilutive. Accordingly, diluted earnings per share for the three and six months ended June 30, 2014 and the three months ended June 30, 2015 is equal to basic earnings per share.

For the six months ended June 30, 2015, the convertible debentures are anti-dilutive. Diluted earnings per share for the six months ended June 30, 2015 is presented below:

	For the six months ended
	June 30, 2015 $
Diluted income attributable to shareholders of the Company	5,919
Weighted average number of diluted shares	19,438,905
Diluted earnings per share	0.30

At June 30, 2015, there were 19,353,666 common shares outstanding. During the six months ended June 30, 2015, the Company repurchased and cancelled 23,700 shares at a cost of $124 (average price of $5.25 per share).

(in thousands of Canadian dollars)

9 Supplemental cash flow information

Adjustments for non-cash items:

	For the six months ended June 30, 2015 $	For the six months ended June 30, 2014 $
Accretion on debt, change in fair value of embedded derivative and unrealized foreign exchange loss	869	81
Share-based compensation	141	151
Depreciation and amortization	7,200	4,586
Fair value adjustment and amounts reclassified to profit and loss on minority interest investments in hotel properties	–	(689)
Gain on disposals of property and equipment, franchise business, minority interest investment in hotel property and repurchase of convertible debentures	(8,113)	(7)
Impairment (reversal of impairment) of hotel property	2,700	(1,217)
Provision for (recovery of) deferred income taxes	(1,730)	800
	1,067	3,705

Changes in items of working capital:

	For the six months ended June 30, 2015 $	For the six months ended June 30, 2014 $
Trade and other receivables	571	(279)
Inventories	123	29
Prepaid expenses and deposits	(1,570)	114
Funds held on behalf of franchisees	167	–
Trade payables and accrued liabilities	(2,154)	179
Funds to be spent on behalf of franchisees	(167)	–
	(3,030)	43

(in thousands of Canadian dollars)

10 Financial instruments and fair values

Financial assets and liabilities have been classified into categories that determine their basis of measurement and, for items measured at fair value, whether changes in fair value are recognized in the consolidated statement of income (loss) or comprehensive income (loss). Those categories are: fair value through profit or loss; loans and receivables; available-for-sale assets; and for liabilities, amortized cost. With the exception of the items noted below, all financial instruments have fair values that approximate their carrying values due to their short-term nature.

The Company's financial instruments consist of cash, restricted cash, trade and other receivables, capital reserve – restricted, loans receivable, trade payables and accrued liabilities, accrued interest on convertible debentures, secured credit facilities, mortgages and loan payable and convertible debentures.

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

	June 30, 2015	
	Carrying value $	Fair value $
Mortgages and loan payable	131,838	137,918
Convertible debentures	88,627	88,929

The methods and assumptions used in estimating the fair values are as follows:

Loans receivable, secured credit facilities and mortgages and loan payable: The fair values are determined using internal valuation techniques which incorporate the discounted future cash flows using discount rates that reflect current market conditions for instruments with similar interest rates, terms and risk. The fair values do not necessarily represent the amounts the Company might pay or receive in actual market transactions.

Convertible debentures: The fair value of the convertible debentures is based on the quoted market price for the debentures.