

Holloway Lodging Real Estate Investment Trust

Unaudited Consolidated Financial Statements
June 30, 2009

August 10, 2009

Management's Report

The accompanying unaudited interim consolidated financial statements of Holloway Lodging Real Estate Investment Trust are the responsibility of management. The unaudited interim consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles. The unaudited interim consolidated financial statements include some amounts and assumptions based on management's best estimates which have been derived with careful judgement.

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 financial statements. The Board of Trustees have reviewed and approved these unaudited interim consolidated financial statements.

(signed) "Glenn Squires"
Chief Executive Officer

(signed) "Tracy Sherren"
Chief Financial Officer

Holloway Lodging Real Estate Investment Trust

Unaudited Consolidated Balance Sheet

As at June 30, 2009

	June 30, 2009 \$	December 31, 2008 \$
Assets		
Current assets		
Cash and cash equivalents (note 10)	1,254,781	4,991,951
Capital reserve	1,116,533	1,552,737
Restricted cash	616,075	653,504
Accounts receivable	3,519,028	3,376,048
Inventories	270,073	303,465
Prepaid expenses and deposits	2,442,956	2,238,765
Current portion of mezzanine loans receivable (note 4)	—	3,000,000
	<u>9,219,446</u>	<u>16,116,470</u>
Capital reserve – restricted	3,954,563	2,975,289
Loans receivable from related parties (note 3)	6,508,910	6,508,910
Mezzanine loans and advances receivable (note 4)	6,304,419	10,174,065
Investments in hotel properties	2,966,730	2,688,334
Property and equipment (note 5)	346,092,843	352,035,190
Other assets	1,002,333	1,123,944
Future income taxes	3,873,000	1,764,000
	<u>379,922,244</u>	<u>393,386,202</u>
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	9,298,796	9,418,698
Distributions payable	684,866	684,866
Accrued interest on convertible debentures	674,600	674,600
Current portion of obligations under capital leases (note 6)	319,637	338,249
Current portion of mortgages and loans payable (note 7)	14,132,999	5,155,110
	<u>25,110,898</u>	<u>16,271,523</u>
Obligations under capital leases (note 6)	373,147	528,132
Mortgages and loans payable (note 7)	149,139,984	159,665,899
Promissory notes payable (note 8)	3,386,662	3,368,334
Convertible debentures (note 9)	64,658,728	63,457,890
	<u>242,669,419</u>	<u>243,291,778</u>
Unitholders' Equity	<u>137,252,825</u>	<u>150,094,424</u>
	<u>379,922,244</u>	<u>393,386,202</u>

Holloway Lodging Real Estate Investment Trust

Unaudited Consolidated Statement of Unitholders' Equity

For the six-month periods ended June 30, 2009 and 2008

	Units \$	Class B LP units \$	Contributed surplus \$	Equity component of convertible debentures \$	Accumulated income (losses) \$	Accumulated distributions \$	Total \$
Balance, December 31, 2007	180,231,026	667,000	804,890	9,596,225	312,428	(17,806,019)	173,805,550
Unit-based compensation related to options	–	–	342,194	–	–	–	342,194
Units repurchased and cancelled	(239,424)	–	52,193	–	–	–	(187,231)
Issuance costs	(2,500)	–	–	–	–	–	(2,500)
Units issued to trustees	67,828	–	–	–	–	–	67,828
Net loss	–	–	–	–	(958,345)	–	(958,345)
Distributions	–	–	–	–	–	(10,563,758)	(10,563,758)
Balance, June 30, 2008	180,056,930	667,000	1,199,277	9,596,225	(645,917)	(28,369,777)	162,503,738
Unit-based compensation related to options	–	–	129,279	–	–	–	129,279
Exercise of options	84,268	–	(57,601)	–	–	–	26,667
Units repurchased and cancelled	(53,360)	–	24,239	–	–	–	(29,121)
Net loss	–	–	–	–	(4,122,125)	–	(4,122,125)
Distributions	–	–	–	–	–	(8,414,014)	(8,414,014)
Balance, December 31, 2008	180,087,838	667,000	1,295,194	9,596,225	(4,768,042)	(36,783,791)	150,094,424
Unit-based compensation related to options	–	–	33,333	–	–	–	33,333
Net loss	–	–	–	–	(8,765,735)	–	(8,765,735)
Distributions	–	–	–	–	–	(4,109,197)	(4,109,197)
Balance, June 30, 2009	180,087,838	667,000	1,328,527	9,596,225	(13,533,777)	(40,892,988)	137,252,825

Holloway Lodging Real Estate Investment Trust

Unaudited Consolidated Statement of Operations and Comprehensive Loss
For the three and six-month periods ended June 30, 2009 and 2008

	Three months ended		Six months ended	
	June 30, 2009	June 30, 2008	June 30, 2009	June 30, 2008
	\$	\$	\$	\$
Hotel revenues				
Rooms	16,360,560	20,416,685	32,943,368	39,992,305
Other	2,556,481	3,252,364	5,301,500	6,384,657
	<u>18,917,041</u>	<u>23,669,049</u>	<u>38,244,868</u>	<u>46,376,962</u>
Hotel expenses				
Operating expenses	11,873,776	13,697,785	24,322,284	27,179,931
Property taxes and insurance	1,145,064	1,345,481	2,430,816	2,459,424
Management fees	543,338	593,415	1,038,152	1,182,693
	<u>13,562,178</u>	<u>15,636,681</u>	<u>27,791,252</u>	<u>30,822,048</u>
Hotel operating income	<u>5,354,863</u>	<u>8,032,368</u>	<u>10,453,616</u>	<u>15,554,914</u>
Other (income) expenses				
Interest on mortgages and other debt and accretion of deferred financing fees	2,882,984	2,877,514	5,772,644	5,753,432
Convertible debentures interest and accretion	1,862,321	1,792,884	3,708,267	3,601,236
Corporate and administrative	532,995	762,811	1,111,446	1,629,554
Interest income	(224,899)	(695,320)	(483,509)	(1,403,338)
Unrealized foreign exchange loss (gain)	(436,924)	(31,111)	(243,690)	128,735
Depreciation and amortization	3,373,509	3,300,429	6,763,193	6,561,640
Provision for impairment of mezzanine loans and advances	4,700,000	—	4,700,000	—
	<u>12,689,986</u>	<u>8,007,207</u>	<u>21,328,351</u>	<u>16,271,259</u>
Income (loss) before income taxes	<u>(7,335,123)</u>	<u>25,161</u>	<u>(10,874,735)</u>	<u>(716,345)</u>
Provision for (recovery of) future income taxes	<u>(1,049,000)</u>	<u>(203,000)</u>	<u>(2,109,000)</u>	<u>242,000</u>
Net loss and comprehensive loss for the periods	<u>(6,286,123)</u>	<u>(177,839)</u>	<u>(8,765,735)</u>	<u>(958,345)</u>
Basic and diluted loss per unit	(0.16)	(0.01)	(0.22)	(0.02)

Holloway Lodging Real Estate Investment Trust

Unaudited Consolidated Statement of Cash Flows

For the three and six-month periods ended June 30, 2009 and 2008

	Three months ended		Six months ended	
	June 30, 2009 \$	June 30, 2008 \$	June 30, 2009 \$	June 30, 2008 \$
Cash provided by (used in)				
Operating activities				
Net loss and comprehensive loss for the periods	(6,286,123)	(177,839)	(8,765,735)	(958,345)
Charges (credits) to income not involving cash				
Unit-based compensation	15,416	118,250	33,333	342,194
Depreciation and amortization	3,373,509	3,300,429	6,763,193	6,561,640
Accretion of mortgages and convertible debentures	614,167	537,683	1,211,773	1,058,451
Unrealized foreign exchange (gain) loss	(436,924)	(31,111)	(243,690)	128,735
Provision for impairment of mezzanine loans and advances	4,700,000	–	4,700,000	–
Provision for (recovery of) future income taxes	(1,049,000)	203,000	(2,109,000)	242,000
	931,045	3,950,412	1,589,874	7,374,675
Net change in non-cash working capital balances related to operations (note 10)	409,166	346,041	(482,806)	(1,594,290)
Cash flow from operating activities	1,340,211	4,296,453	1,107,068	5,780,385
Investing activities				
Decrease in restricted cash	49,023	1,170,082	37,429	1,768,323
Increase in capital reserves	(259,152)	(504,370)	(543,070)	(1,104,047)
Issuance of mezzanine loans and advances	(421,966)	–	(830,354)	–
Proceeds from repayment of mezzanine loans	–	–	3,000,000	–
Issuance of loan to a related party	–	–	–	(6,350,000)
Investment in hotel properties	(5,081)	–	(278,396)	–
Additions to property and equipment	(383,375)	(880,196)	(669,462)	(1,338,744)
Increase in other assets	–	(7,515)	–	(7,515)
Cash flow from (used in) investing activities	(1,020,551)	(221,999)	716,147	(7,031,983)
Financing activities				
Repayment of capital lease obligations	(88,753)	(106,055)	(173,596)	(230,232)
Proceeds from mortgages and loans, net of financing fees	(33,511)	(8,364)	1,129,038	(40,388)
Repayment of mortgages and loans payable	(1,208,851)	(1,012,555)	(2,406,630)	(2,023,838)
Units repurchased and cancelled	–	–	–	(187,231)
Issuance costs	–	–	–	(2,500)
Distributions paid to unitholders	(2,054,598)	(5,279,557)	(4,109,197)	(10,565,255)
Cash flow used in financing activities	(3,385,713)	(6,406,531)	(5,560,385)	(13,049,444)
Net change in cash and cash equivalents during the periods	(3,066,053)	(2,332,077)	(3,737,170)	(14,301,042)
Cash and cash equivalents – Beginning of periods	4,320,834	10,925,474	4,991,951	22,894,439
Cash and cash equivalents – End of periods	1,254,781	8,593,397	1,254,781	8,593,397

Holloway Lodging Real Estate Investment Trust

Notes to Unaudited Consolidated Financial Statements

For the six-month periods ended June 30, 2009 and 2008

1 Basis of presentation and nature of operations

Holloway Lodging Real Estate Investment Trust (“Holloway Lodging REIT” or the “REIT”) is an open-ended real estate investment trust that was formed under the laws of the Province of Ontario pursuant to its Declaration of Trust on March 28, 2006.

The objectives of the REIT are: (a) to expand its asset base and increase its funds from operations through accretive acquisitions and internal growth initiatives; (b) to enhance the value of its assets to maximize long-term unit value through active management of its assets; and (c) to increase cashflow from operations in order to resume distributions to unitholders at the appropriate time (note 14).

As at June 30, 2009, the REIT owned 21 hotels in Canada and 1 hotel in the United States with 2,423 guest rooms and suites and held minority ownership interests in nine hotels.

2 Significant accounting policies

The accompanying unaudited consolidated financial statements have been prepared in accordance with the requirements of the Canadian Institute of Chartered Accountants (CICA) Handbook Section 1751, “Interim Financial Statements”. Accordingly, certain information and note disclosure normally included in annual financial statements prepared in accordance with Canadian generally accepted accounting principles have been omitted or condensed. These unaudited interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements of the REIT for the year ended December 31, 2008.

In the opinion of management, the unaudited interim consolidated financial statements include all adjustments considered necessary by management to present a fair statement of the results of operations, financial position and cash flows. Except as otherwise noted hereunder, these unaudited interim consolidated financial statements were prepared using the same policies and methods of computation as the audited consolidated financial statements of the REIT for the year ended December 31, 2008.

Changes in accounting standards

In the first quarter of 2009, the REIT adopted the following new Handbook Sections issued by CICA.

Goodwill and Intangible Assets

Section 3064 Goodwill and Intangible Assets establishes new standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. Section 1000 Financial Statement Concepts was also amended to provide consistency with Section 3064. These new standards have no impact on the REIT’s 2009 financial statements.

Holloway Lodging Real Estate Investment Trust

Notes to Unaudited Consolidated Financial Statements

For the six-month periods ended June 30, 2009 and 2008

3 Loans receivable from related parties

The REIT has a \$6.35 million loan, advanced February 1, 2008 receivable from Pacrim Hospitality Services Inc., a company in which a member of management and trustee has a significant ownership interest. The loan is unsecured, has a ten-year term, is repayable at any time without penalty and bears interest at the lesser of 13% and the trailing three-month yield plus 1% on Holloway's units.

The REIT has a \$158,910 loan receivable from Winport Developments Inc., a company in which a member of management and trustee has a significant ownership interest. The loan is secured by 55,555 units of Holloway and a guarantee by 3475425 Canada Inc., is repayable at any time without penalty and bears interest at 12% per annum.

4 Mezzanine loans and advances receivable

The REIT provides mezzanine loans on hotel projects being developed by Winport Developments Inc., Winport Developments Limited Partnership and its partners.

	June 30, 2009	December 31, 2008
	\$	\$
Winport Developments Limited Partnership, a related party, and Pacrim North York Limited Partnership, principal balance due November 3, 2011, with \$8.0 million bearing interest at 12% and \$1.5 million bearing interest at 11%	9,500,000	9,500,000
Winport Development Limited Partnership, a related party, and Pacrim North York Limited Partnership, principal balance due January 13, 2009, bearing interest at 12%	1,250,000	1,250,000
RegWin Hotel Ltd., principal balance due January 19, 2012, bearing interest at 12%, repaid on February 5, 2009	—	3,000,000
Windsor 8 Motel Limited, principal balance due January 19, 2012, bearing interest at 12%	1,913,000	1,913,000
Accrued interest on loans to Winport Developments Limited Partnership and Pacrim North York Limited Partnership to December 31, 2008	511,065	511,065
Additional advances to Winport Developments Limited Partnership and Pacrim North York Limited Partnership, non-interest bearing with no set terms of repayment and other expenses	790,344	—
Additional advances to Windsor 8 Motel Limited, non-interest bearing with no set terms of repayment	40,010	—
	<hr/>	<hr/>
	14,004,419	16,174,065
Less: Current portion	—	3,000,000
Less: Provision for impairment	7,700,000	3,000,000
	<hr/>	<hr/>
	6,304,419	10,174,065

Holloway Lodging Real Estate Investment Trust

Notes to Unaudited Consolidated Financial Statements

For the six-month periods ended June 30, 2009 and 2008

4 Mezzanine loans and advances receivable (continued)

The REIT believes that the loans to Winport Development Limited Partnership and Pacrim North York Limited Partnership are impaired. The loans are in default and the REIT has issued a demand notice for payment. On August 6, 2009, a court-appointed receiver for the property was named, with a mandate to sell the property and maximize the return to the debt-holders. The REIT's loans have been written down to the estimated fair value of the REIT's underlying security. During the three months ended June 30, 2009, the REIT recorded an additional provision for impairment of \$4.7 million. Significant judgment was exercised by management in making this estimate. As such, actual losses will differ from the estimate and the differences could be material.

5 Property and equipment

	June 30, 2009		
	Cost \$	Accumulated amortization \$	Net \$
Land	32,216,832	—	32,216,832
Land lease	500,000	35,890	464,110
Buildings	304,885,697	17,092,092	287,793,604
Renovations in progress	349,926	—	349,926
Furniture, fixtures, equipment and other	30,473,413	9,769,022	20,704,391
Paving	3,619,378	824,740	2,794,638
Landscaping	22,984	3,756	19,228
Signage	1,036,130	225,700	810,430
Computer equipment and website	1,787,193	1,164,362	622,831
Vehicles	353,467	202,619	150,849
Tenant inducements	211,920	45,916	166,004
	375,456,940	29,364,097	346,092,843

	December 31, 2008		
	Cost \$	Accumulated amortization \$	Net \$
Land	32,216,832	—	32,216,832
Land lease	500,000	30,037	469,963
Buildings	304,904,833	13,282,864	291,621,969
Renovations in progress	220,541	—	220,541
Furniture, fixtures and equipment	29,940,422	7,549,543	22,390,879
Paving	3,619,378	644,063	2,975,315
Landscaping	22,984	1,656	21,328
Signage	1,008,114	173,139	834,975
Computer equipment and websites	1,759,212	870,297	888,915
Vehicles	353,467	146,190	207,277
Tenant inducements	211,920	24,724	187,196
	374,757,703	22,722,513	352,035,190

Holloway Lodging Real Estate Investment Trust

Notes to Unaudited Consolidated Financial Statements

For the six-month periods ended June 30, 2009 and 2008

6 Obligations under capital leases

The REIT has various capital lease obligations to acquire computer equipment, signs, furniture and hotel equipment.

	June 30, 2009	December 31, 2008
	\$	\$
Present value of future minimum lease payments	692,784	866,381
Less: Current portion	319,637	338,249
	<u>373,147</u>	<u>528,132</u>

Estimated future repayments over the next five years are as follows:

	\$
Reminder of 2009	199,423
Year ending December 31, 2010	325,117
Year ending December 31, 2011	143,981
Year ending December 31, 2012	85,461
Year ending December 31, 2013	20,712
Thereafter	<u>20,574</u>
Future minimum lease payments	795,268
Less: Amounts representing interest at a weighted average rate of 10.47%	<u>102,484</u>
Present value of future minimum lease payments	<u>692,784</u>

Holloway Lodging Real Estate Investment Trust

Notes to Unaudited Consolidated Financial Statements

For the six-month periods ended June 30, 2009 and 2008

7 Mortgages and loans payable

	June 30, 2009 \$	December 31, 2008 \$
Mortgages payable, bearing interest at a weighted average rate of 6.78% (December 31, 2008 - 6.76%) and maturing on various dates from April, 2010 to July, 2017. Individual first charges on most of the hotel properties have been pledged as security for individual mortgages	164,363,883	165,919,967
Vehicle loans payable, bearing interest at a weighted average rate of 7.63% (December 31, 2008 - 7.62%) and maturing on various dates from April, 2010 to April, 2011	69,231	98,834
	<u>164,433,114</u>	<u>166,018,801</u>
Less: Deferred financing fees	1,160,131	1,197,792
Less: Current portion	14,132,999	5,155,110
	<u>149,139,984</u>	<u>159,665,899</u>

Estimated future principal repayments over the next five years are as follows:

	\$
Reminder of 2009	2,624,963
Year ending December 31, 2010	13,934,479
Year ending December 31, 2011	36,519,112
Year ending December 31, 2012	18,811,101
Year ending December 31, 2013	2,912,766
Thereafter	89,630,693

The current portion of long-term debt on the balance sheet is based on the twelve months ending June 30, 2010, whereas the repayment schedule above reflects the fiscal year. The current portion of long-term debt on the balance sheet includes \$8.9 million of the principal for two mortgages that mature on April 1, 2010. The REIT is in the process of refinancing these mortgages.

8 Promissory notes payable

On December 22, 2008, the REIT issued two promissory notes for \$3.0 million and \$551,613, respectively, payable to Winport Developments Limited Partnership to finance the acquisition of the investments in hotel properties. The \$3.0 million promissory note bears interest at 6% per year until December 22, 2011 and 12% per year, thereafter. The \$551,613 note does not bear interest and therefore has been discounted by \$183,279, representing the net present value of the implicit interest. The discount is being accreted to interest expense over five years, the expected term of the promissory notes. The principal of the notes is repayable on the sale of Holloway's ownership interests or the sale of the underlying properties.

Holloway Lodging Real Estate Investment Trust

Notes to Unaudited Consolidated Financial Statements

For the six-month periods ended June 30, 2009 and 2008

9 Convertible debentures

On August 1, 2006, the REIT issued \$20,238,000 in convertible, redeemable debentures. The debentures bear interest at 8%, payable semi-annually on February 1st and August 1st, and mature in five years. The convertible debentures can be converted into units of the REIT at \$5.40 per unit at any time commencing two years and one day from the issuance date and ending on the date that is 15 days prior to the maturity date.

On June 21, 2007, the REIT issued \$45,000,000 in convertible, redeemable debentures. The debentures bear interest at 6.5%, payable semi-annually on June 30th and December 31st, and mature in five years. The convertible debentures can be converted into units of the REIT at \$6.15 per unit at any time commencing two years and one day from the issuance date and ending on the date that is 15 days prior to the maturity date. On July 18, 2007, the REIT issued an additional \$6,844,000 in convertible, redeemable debentures with the same terms as the June 21, 2007 debentures, pursuant to the underwriters exercising their over-allotment option.

In the event, the REIT gives notice of redemption, the debenture holders have 30 days to elect to convert their debentures into units.

The convertible debentures have been valued at their estimated fair value at the time of issuance, according to the terms and conditions in place at the time. The difference between the gross proceeds and the estimated fair value of the debt of \$5,300,000 on the August 1, 2006 8% debentures, \$4,150,000 on the June 21, 2007 6.5% debentures and \$644,000 on the July 18, 2007 6.5% debentures represents the value of the conversion feature of the debentures and accordingly, has been recorded as a component of equity. The difference between the recorded value of the debt component of the debentures and their face value has been accounted for as a discount on the issuance of the debt and is being accreted to interest expense, using the effective interest rate method, over the terms of the debentures.

The debt component of the convertible debentures is recorded as a liability. The accretion of the discount on the issuance of the debentures increases the debt component to their face value over the term of the debentures.

	June 30, 2009	December 31, 2008
	\$	\$
Debt component	61,988,000	61,988,000
Accretion of convertible debentures	4,285,662	3,336,996
Deferred financing fees	(1,614,934)	(1,867,106)
	<u>64,658,728</u>	<u>63,457,890</u>

Holloway Lodging Real Estate Investment Trust

Notes to Unaudited Consolidated Financial Statements

For the six-month periods ended June 30, 2009 and 2008

10 Supplemental cash flow information

Net change in non-cash working capital balances related to operations:

	Three months ended		Six months ended	
	June 30, 2009 \$	June 30, 2008 \$	June 30, 2009 \$	June 30, 2008 \$
Accounts receivable	175,144	40,631	(142,980)	(1,658,591)
Inventories	10,408	34,152	33,392	111,981
Prepaid expenses and deposits	197,952	13,766	(204,191)	176,427
Accounts payable and accrued liabilities	463,367	695,197	(169,027)	(224,107)
Accrued interest on convertible debentures	(437,705)	(437,705)	—	—
	<u>409,166</u>	<u>346,041</u>	<u>(482,806)</u>	<u>(1,594,290)</u>

Cash and cash equivalents are comprised of the following:

	June 30, 2009 \$	December 31, 2008 \$
Cash on hand and balances with banks	<u>1,254,781</u>	<u>4,991,951</u>

11 Seasonality

Revenues from hotel operations tend to fluctuate throughout the year, with greater demand in the second and third quarters of the calendar year.

12 Capital management

The REIT defines capital as the aggregate of unitholders' equity and interest-bearing debt. The objectives of the REIT's capital management program are to maintain a level of capital that complies with the investment and debt restrictions according to the REIT's Declaration of Trust, complies with existing debt covenants, optimizes the cost of capital, funds its business strategies and builds long-term unitholder value.

In managing its capital structure, the REIT monitors performance throughout the year to ensure anticipated working capital requirements and capital expenditures are funded from operations, available cash on deposit and, where applicable, bank borrowings. The REIT will make adjustments to its capital structure to meet the objectives of the broader corporate strategy or in response to changes in economic conditions and risk. In order to maintain or adjust the capital structure, the REIT may issue debt and/or issue or redeem units.

Holloway Lodging Real Estate Investment Trust

Notes to Unaudited Consolidated Financial Statements

For the six-month periods ended June 30, 2009 and 2008

12 Capital management (continued)

The REIT monitors capital using the following financial metrics, including (but not limited to):

- a Debt Service coverage ratio defined as earnings before interest, income taxes, depreciation, amortization, non-cash accretion of deferred financing fees and unit-based compensation (Earnings base) to mortgage, loans, promissory notes and capital lease interest and principal payments (Debt Service); and
- a Debt to Gross Book Value (Debt to GBV) ratio defined as mortgages and loans payable, obligations under capital leases, promissory notes and the face value of the convertible debentures (Debt) divided by total assets plus accumulated depreciation and amortization (GBV). This ratio cannot exceed 60% based on the REIT's Declaration of Trust.

	June 30, 2009	December 31, 2008
	\$	\$
Capital structure		
Obligations under capital leases	692,784	866,381
Mortgages and loans payable	163,272,983	164,821,009
Convertible debentures	64,658,728	63,457,890
Promissory notes	3,386,662	3,368,334
Total debt	232,011,157	232,513,614
Unitholders' equity	137,252,825	150,094,424
Total capital	369,263,982	382,608,038
Ratios		
Total debt	232,011,157	232,513,614
Adjustment of convertible debentures to face value	7,423,272	8,624,110
Adjustment of promissory notes to face value	164,951	183,279
Debt	239,599,380	241,321,003
Gross book value	409,681,250	416,447,047
Debt to GBV	58.5%	57.9%
Trailing 12 months ended		
	June 30, 2009	December 31, 2008
	\$	\$
Earnings base	26,195,512	32,019,577
Debt service	21,391,941	21,093,105
Debt service ratio	1.22	1.52

Holloway Lodging Real Estate Investment Trust

Notes to Unaudited Consolidated Financial Statements

For the six-month periods ended June 30, 2009 and 2008

12 Capital management (continued)

The REIT is also subject to financial covenants on its mortgages payable, which are measured on an annual basis and include customary terms and conditions for borrowings of this nature. These include the Debt Service ratio presented above. The REIT is in compliance with, or has obtained waivers for, all its financial covenants.

For 2008 and the current quarter, cash distributions to unitholders exceeded the REIT's distributable income, as defined in the REIT's Declaration of Trust. On November 13, 2008, the REIT reduced its distributions to \$0.21 per unit on an annual basis. On July 21, 2009, the REIT suspended distributions (note 14).

13 Financial instruments

i) Fair value of financial instruments

The REIT's financial instruments consist of cash and cash equivalents, restricted cash, accounts receivable, mezzanine loans and advances receivable, capital reserves, loans receivable from related parties, accounts payable and accrued liabilities, distributions payable, accrued interest on convertible debentures, obligations under capital leases, mortgages and loans payable, promissory notes payable and convertible debentures. The REIT's cash and cash equivalents, restricted cash, accounts receivable, capital reserves, accounts payable and accrued liabilities, distributions payable and accrued interest on convertible debentures are carried at amortized cost, which approximates fair value due to the immediate or short-term maturities of these financial instruments.

The fair value of the REIT's obligations under capital leases and mortgages and loans payable is based on discounted future cashflows using discount rates that reflect current market conditions for instruments with similar terms and risks. The fair values do not necessarily represent amounts the REIT might pay in actual market transactions. The fair value of the convertible debentures is the trading value at June 30, 2009 and December 31, 2008, respectively.

Holloway Lodging Real Estate Investment Trust

Notes to Unaudited Consolidated Financial Statements

For the six-month periods ended June 30, 2009 and 2008

13 Financial instruments (continued)

	June 30, 2009		December 31, 2008	
	Carrying value \$	Fair value \$	Carrying value \$	Fair value \$
Held for trading (cash, restricted cash and capital reserve)	6,941,952	6,941,952	10,173,481	10,173,481
Loans and receivables (accounts receivable)	3,519,028	3,519,028	3,376,048	3,376,048
Other financial liabilities (accounts payable and accrued liabilities, distributions payable and accrued interest on convertible debentures)	10,658,262	10,658,262	10,778,164	10,778,164
Obligations under capital leases	692,784	692,784	866,381	866,381
Mortgages and loans payable	163,272,983	171,534,978	164,821,009	179,289,428
Convertible debentures	74,254,953	36,782,273	73,054,115	43,832,469

ii) Risk management

The REIT, through its financial assets and liabilities, has exposure to the following risks from its use of financial instruments: interest rate risk, credit risk, liquidity risk and currency risk. Senior management is responsible for setting acceptable levels of risk and reviewing risk management activities as necessary.

Interest rate risk

The REIT is exposed to interest rate risk on its lending and borrowing activities. It manages its exposure to interest rate risk by using fixed rate debt so that cashflow is not impacted significantly by a change in interest rates. The REIT does not have any mortgages to be re-financed in 2009 and \$8.9 million to be re-financed in 2010. The weighted average interest rate on its mortgages payable is 6.78% (December 31, 2008 - 6.76%) with a weighted average maturity of 5.7 years (December 31, 2008 - 6.2 years). The convertible debentures have a weighted average interest rate of 6.9% (December 31, 2008 - 6.9%) and a weighted average maturity of 2.74 years (December 31, 2008 - 3.2 years).

At June 30, 2009, the REIT had no long-term debt at floating rates and thus, for the three and six months ended June 30, 2009, a 1% change in interest rates would not change the net loss.

Holloway Lodging Real Estate Investment Trust

Notes to Unaudited Consolidated Financial Statements

For the six-month periods ended June 30, 2009 and 2008

13 Financial instruments (continued)

Credit risk

In accordance with its investment policy, the REIT invests excess cash in Government of Canada treasury bills, short-term Canadian and provincial government debt, bankers' acceptance notes and term deposits of Schedule 1 Banks. The credit risk on cash and cash equivalents is limited because the counter-parties are governments and banks with high credit-ratings assigned by international credit-rating agencies.

The amount of accounts receivable disclosed in the balance sheet of \$3,519,028 is net of allowances for bad debts, estimated by management based on prior experience and their assessment of the current economic environment.

Historically, there have been no collection issues and the REIT does not believe it is subject to any significant concentration of credit risk. The REIT assesses the credit worthiness of customers requesting credit and listings of accounts receivable are reviewed by management on a monthly basis.

The following table sets forth details of accounts receivable and the related allowance for doubtful accounts:

	June 30, 2009	December 31, 2008
	\$	\$
Accounts receivable under 30 days aged	2,566,679	2,111,945
Accounts receivable over 30 days aged	1,254,421	1,349,345
Less: Allowance for doubtful accounts	(302,072)	(85,242)
	<u>3,519,028</u>	<u>3,376,048</u>

The REIT is exposed to credit risk on its loans receivable from related parties and mezzanine loans receivable. The mezzanine loans are secured by a second or third charge on the property. Management reviews the results and cashflows of these entities on a monthly basis and will take steps to enforce its security when this is deemed appropriate.

Currency risk

The REIT incurs revenue and expenses in U.S. and Canadian currency, and as such, is subject to fluctuations as a result of foreign exchange rate variation. The REIT manages its exposure to currency risk by billing for its services in the U.S. in the underlying currency related to the expenditure. As this natural hedging effectively matches the revenue and expenses, the REIT's management considers there to be little currency risk. However, a \$0.01 change in the US dollar exchange rate will change the unrealized foreign exchange gain or loss by \$44,493 (December 31, 2008 - \$44,735).

Holloway Lodging Real Estate Investment Trust

Notes to Unaudited Consolidated Financial Statements

For the six-month periods ended June 30, 2009 and 2008

13 Financial instruments (continued)

Liquidity risk

The REIT's objective is to have sufficient liquidity to meet liabilities when due, as well as to maintain compliance with liquidity covenants on financing contracts and its capital management requirements and objectives. In November 2008, distributions were reduced to \$0.0175 per unit per month (\$0.21 per unit annually) and on July 21, 2009, the REIT suspended distributions (note 14) in order to conserve cash and satisfy its operating obligations, including principal repayments. The REIT monitors and forecasts its cash balances and cash flows generated from operations to meet its requirements. Based on overall cash generation capacity and overall financial position, while there can be no assurance, management believes the REIT will be able to meet financial obligations as they come due while maintaining compliance with all financial covenants.

14 Subsequent events

On July 21, 2009, the REIT suspended distributions to unitholders.

On August 5, 2009, the REIT entered into a binding agreement for the conditional sale of its Wingate by Wyndham property in Calgary, Alberta to an arm's length purchaser for \$16.5 million, representing a gain of approximately \$2.0 million. Net proceeds, after repayment of the mortgage on the property, are expected to be approximately \$9.3 million. The sale is conditional upon, among other things, the purchaser completing its due diligence by August 17, 2009. The transaction is expected to close in early September 2009.