

Unaudited Consolidated Financial Statements of

ALLIED HOTEL PROPERTIES INC.

Six months ended June 30, 2004 and 2003

ALLIED HOTEL PROPERTIES INC.

Under National Instrument 51-102, "*Continuous Disclosure Obligations*", Part 4, subsection 4.3(3)(a), if an auditor has not performed a review of the interim financial statements, they must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor.

Allied Hotel Properties Inc.'s external auditors, KPMG LLP, have not performed a review of these interim financial statements.

"Peter Y.L. Eng" (signed)

Peter Y.L. Eng
Chief Executive Officer

"John R. Ellen" (signed)

John R. Ellen, CA
Chief Financial Officer

August 18, 2004

ALLIED HOTEL PROPERTIES INC.

Consolidated Balance Sheets
June 30, 2004 and December 31, 2003
(in thousands of dollars)

	June 2004	December 2003
	Unaudited	Audited
Assets		
Current assets:		
Accounts receivable	\$ 2,999	\$ 1,983
Inventories	427	453
Prepaid expenses	737	759
Future income taxes	180	98
	<u>4,343</u>	<u>3,293</u>
Income-producing properties	106,608	107,990
Investment	2,131	2,190
Deferred costs, net of amortization	308	324
Future income taxes	3,238	3,227
	<u>\$ 116,628</u>	<u>\$ 117,024</u>

Liabilities and Shareholders' Deficiency

Current liabilities:		
Bank indebtedness	\$ 2,960	\$ 2,412
Demand loan (note 4)	7,750	3,000
Accounts payable and accrued liabilities	13,305	12,369
Deferred revenue	268	266
Mortgage payable (note 4)	12,943	17,140
Long-term debt	489	486
Due to related parties	7,678	5,306
Capital lease obligation	152	266
Long-term demand loans	70,208	71,854
	<u>115,753</u>	<u>113,099</u>
Deferred revenue	1,747	1,842
Long-term debt	2,458	2,663
Capital lease obligation	162	216
	<u>120,120</u>	<u>117,820</u>
Shareholders' deficiency:		
Share capital	29,868	29,868
Deficit	(33,360)	(30,664)
	<u>(3,492)</u>	<u>(796)</u>
	<u>\$ 116,628</u>	<u>\$ 117,024</u>

See accompanying notes to unaudited consolidated financial statements.

"Peter Y.L. Eng" (signed) Director
Peter Y.L. Eng

"Michael Chan" (signed) Director
Michael Chan

ALLIED HOTEL PROPERTIES INC.

Unaudited Consolidated Statements of Operations
(in thousands of dollars, except per share amounts)

	Three months ended June 30		Six months ended June 30	
	2004	2003	2004	2003
Revenues:				
Rooms	\$ 8,576	\$ 6,901	\$ 14,569	\$ 12,289
Food and beverage	4,728	4,071	8,105	7,289
Other	1,039	1,076	2,118	2,102
	14,343	12,048	24,792	21,680
Cost of sales:				
Rooms	2,815	2,326	5,063	4,439
Food and beverage	3,700	3,291	6,687	6,235
Other	342	362	716	726
	6,857	5,979	12,466	11,400
Gross profit	7,486	6,069	12,326	10,280
Operating expenses:				
Selling, general and administrative	4,320	4,116	8,223	7,956
Management fees	115	185	236	369
Taxes and insurance	938	988	1,885	1,914
Depreciation and amortization	755	766	1,510	1,519
	6,128	6,055	11,854	11,758
Operating income (loss)	1,358	14	472	(1,478)
Other expenses (income):				
Interest on long-term demand loans and long-term debt	1,301	1,483	2,661	2,899
Interest – other	250	229	490	454
Equity in loss (income) of investee	16	(84)	59	(161)
	1,567	1,628	3,210	3,192
Loss before income taxes	209	1,614	2,738	4,670
Income taxes (recovery):				
Current	35	14	51	34
Future	(127)	17	(93)	(132)
	(92)	31	(42)	(98)
Loss for the period	\$ 117	\$ 1,645	\$ 2,696	\$ 4,572
Basic and diluted loss per share	\$ 0.00	\$ 0.02	\$ 0.03	\$ 0.04

See accompanying notes to unaudited consolidated financial statements

ALLIED HOTEL PROPERTIES INC.

Unaudited Consolidated Statements of Deficit
Six months ended June 30, 2004 and 2003
(in thousands of dollars)

		2004		2003
Net loss	\$	2,696	\$	4,572
Deficit, beginning of period		30,664		29,108
Deficit, end of period	\$	33,360	\$	33,680

See accompanying notes to unaudited consolidated financial statements

ALLIED HOTEL PROPERTIES INC.

Unaudited Consolidated Statements of Cash Flows

(in thousands of dollars)

	Three months ended June 30		Six months ended June 30	
	2004	2003	2004	2003
Cash provided by (used in):				
Operations:				
Loss for the period	\$ (117)	\$ (1,645)	\$ (2,696)	\$ (4,572)
Adjustments for:				
Depreciation and amortization	755	766	1,510	1,519
Future income taxes	(127)	17	(93)	(132)
Equity in loss (income) of investee	16	(84)	59	(161)
Amortization of deferred revenue	(46)	(45)	(93)	(91)
Funds from operations	481	(991)	(1,313)	(3,437)
Changes in non-cash operating working capital (note 6)	16	(1,545)	(32)	(637)
	497	(2,536)	(1,345)	(4,074)
Financing:				
Proceeds from demand loan	4,750	–	4,750	–
Proceeds from long-term demand loans	–	6,000	–	6,000
Principal repayments on long-term demand loans	(838)	(677)	(1,646)	(1,373)
Principal repayments on long-term debt	(86)	(122)	(202)	(252)
Principal repayments on mortgage payable	(4,087)	(3,135)	(4,197)	(3,252)
Due to related parties	(156)	1,326	2,372	2,172
Repayment of obligations under capital leases	(80)	(130)	(168)	(230)
	(497)	3,262	909	3,065
Investments:				
Additions to income-producing properties	(90)	(96)	(112)	(370)
Net proceeds from sale of investments	–	–	–	659
	(90)	(96)	(112)	289
(Decrease) increase in cash and cash equivalents	(90)	630	(548)	(720)
Cash and cash equivalents, beginning of period	(2,870)	(3,442)	(2,412)	(2,092)
Cash and cash equivalents, end of period	\$ (2,960)	\$ (2,812)	\$ (2,960)	\$ (2,812)

See accompanying notes to unaudited consolidated financial statements

Supplemental information (note 6)

ALLIED HOTEL PROPERTIES INC.

Notes to Unaudited Consolidated Financial Statements
Six months ended June 30, 2004 and 2003
(in thousands of dollars, except per share amounts)

1. Future operations:

Allied Hotel Properties Inc. (the "Company") was incorporated in 1982. The primary business activity of the Company is hotel and real estate acquisition, holding and management.

The application of the going concern basis of presentation in accordance with Canadian generally accepted accounting principles assumes that the Company will continue in operation for the foreseeable future and be able to realize its assets and discharge its liabilities and commitments in the normal course of business. These financial statements have been prepared on the going concern basis notwithstanding conditions which cast doubt on the Company's ability to continue in such a manner. At June 30, 2004 and December 31, 2003, the Company had a significant working capital deficiency. In addition, the Company has experienced losses and negative cash flow from operations in the six months ended June 30, 2004 and 2003. Further, based on management's current projections, the Company will likely experience a significant cash flow deficiency through the balance of the 2004 fiscal year.

The Company is subject to certain debt service ratio ("DSR") and other covenants pertaining to long-term demand loans. At June 30, 2004 the Company was in breach of certain of its covenants. The Company's lenders are aware of these breaches. Further, based on management's current projections, the Company believes it is unlikely that it will be in compliance throughout 2004 with the DSR covenant applicable to \$59,575 of long-term demand loans, unless it is modified. Although the Company expects the breached covenants to be modified, if they are not, such violations could result in a requirement to immediately repay a portion of the applicable long-term demand loans sufficient to bring the Company into compliance with the covenants, to sell certain income-producing properties, or to take other measures as determined by the lenders.

Although the Company's majority shareholder has provided a pledge of continued financial support to the Company, there is no certainty that the shareholder will be able to perform under its pledge, nor that such financial support, if forthcoming, will be sufficient to permit the Company to meet its liabilities and commitments as they become payable. If the going concern basis was not appropriate for these financial statements, then adjustments would be necessary in the carrying value of assets and liabilities, the reported revenues and expenses, and the balance sheet classifications used.

2. Significant accounting policies:

a. *General*

The Company's accounting policies and its standards of financial disclosure are in accordance with Canadian generally accepted accounting principles ("GAAP") and are substantially in accordance with the recommendations of the Canadian Institute of Public and Private Real Estate Companies.

ALLIED HOTEL PROPERTIES INC.

Notes to Unaudited Consolidated Financial Statements
Six months ended June 30, 2004 and 2003
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2. Significant accounting policies (cont'd):

a. General (cont'd)

The Company's standards of financial disclosure in these interim financial statements are in accordance with the recommendations in The Canadian Institute of Chartered Accountants' ("CICA") standard on Interim Financial Statements. Certain note disclosures do not fully conform to Canadian GAAP disclosure requirements for annual financial statements, and these financial statements should be read in conjunction with the Company's audited financial statements for the year ended December 31, 2003 (the "Annual Financial Statements"). These interim financial statements follow the same accounting policies as the Annual Financial Statements, except for note 3.

b. Cyclical Business

The nature of the hotel business is inherently cyclical such that, in prior years, approximately 60% of the Company's annual revenues are generated in the second and third quarters of the year. With a significant investment in income-producing properties, the Company has high fixed costs, particularly for depreciation and interest expense. As a result, the first and fourth quarters have historically recorded lower net operating income than the second and third quarters. These seasonal factors should be considered when reviewing the Company's quarterly operating results.

3. Change in accounting policy:

Effective January 1, 2004, the Company changed its accounting policy with respect to the basis of calculating depreciation on buildings within income-producing properties. The Company had used the sinking fund method. Following the issuance of Section 1100 of the CICA Handbook the sinking fund method is no longer acceptable under GAAP. Accordingly, effective January 1, 2004, the Company calculates depreciation of buildings using the straight-line method. The change in accounting policy has been applied prospectively and has resulted in an increase to depreciation expense and net loss of \$724 for the six months ended June 30, 2004 (\$362 for the three months ended June 30, 2004).

4. Demand loan and mortgage payable:

Effective April 1, 2004 the Company entered into an agreement with the lender of the mortgage payable to refinance \$13,000, repayable in blended monthly installments of \$101, bearing interest at a rate of 6.8% per annum for the first year and 4.25% above one-year Canadian bond yields for the second year, with principal due April 1, 2006. Concurrent with this refinancing the Company refinanced the demand loan of \$3,000 with a new facility of \$7,750 on which interest only is payable monthly at a rate of prime plus 2.5% per annum, with the principal due April 1, 2007. Proceeds from the new demand loan facility were used to pay down the mortgage payable and to pay loan fees associated with both refinancings.

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5. Per share information:

	2004	2003
Weighted average number of common shares outstanding	106,327,268	106,327,268

6. Supplementary cash flow information:

Changes in non-cash operating working capital consist of the following:

	Three months ended June 30		Six months ended June 30	
	2004	2003	2004	2003
Accounts receivable	\$ (1,362)	\$ (879)	\$ (1,016)	\$ (537)
Inventories	(30)	(10)	26	16
Prepaid expenses	96	227	22	160
Accounts payable and accrued liabilities	1,312	(883)	936	(276)
	\$ 16	\$ (1,545)	\$ (32)	\$ (637)

Supplemental disclosures related to the statements of cash flows consist of the following:

	Three months ended June 30		Six months ended June 30	
	2004	2003	2004	2003
Supplemental information:				
Interest paid	\$ 1,512	\$ 1,705	\$ 3,068	\$ 3,243
Taxes paid	2	1	2	1
Non-cash investing and financing activities:				
Acquisition of equipment under capital lease	–	239	–	239
Refinancing of demand loan	3,000	–	3,000	–
Refinancing of mortgage payable	13,000	17,488	13,000	17,488