

Edgar Filing: Chesapeake Lodging Trust - Form 10-Q

Chesapeake Lodging Trust
Form 10-Q
November 01, 2018
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2018

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____
Commission file number 001-34572

CHESAPEAKE LODGING TRUST
(Exact name of registrant as specified in its charter)

MARYLAND 27-0372343
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)
4300 Wilson Boulevard, Suite 625 22203
Arlington, Virginia
(Address of principal executive offices) (Zip Code)
(571) 349-9450
(Registrant's telephone number, including area code)

Not Applicable
(Former name, former address and former fiscal year, if changed since last report)

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

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

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

Large accelerated filer Accelerated filer
Non-accelerated filer Smaller reporting company
Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

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As of October 26, 2018, there were 60,393,791 shares of the registrant's common shares issued and outstanding.

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PART I

Item 1. Financial Statements

CHESAPEAKE LODGING TRUST
CONSOLIDATED BALANCE SHEETS

(in thousands, except share data)

| | September 30, 2018 | December 31, 2017 |
|---|-----------------------|----------------------|
| | (unaudited) | |
| ASSETS | | |
| Property and equipment, net | \$ 1,739,606 | \$ 1,823,217 |
| Intangible assets, net | 34,823 | 35,256 |
| Cash and cash equivalents | 68,865 | 44,314 |
| Restricted cash | 29,942 | 30,602 |
| Accounts receivable, net of allowance for doubtful accounts of \$145 and \$116, respectively | 32,038 | 20,769 |
| Prepaid expenses and other assets | 25,404 | 21,202 |
| Total assets | \$ 1,930,678 | \$ 1,975,360 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Long-term debt | \$ 754,599 | \$ 829,552 |
| Accounts payable and accrued expenses | 74,959 | 65,783 |
| Other liabilities | 31,219 | 31,597 |
| Total liabilities | 860,777 | 926,932 |
| Commitments and contingencies (Note 12) | | |
| Preferred shares, \$.01 par value; 100,000,000 shares authorized; no shares issued and outstanding, respectively | — | — |
| Common shares, \$.01 par value; 400,000,000 shares authorized; 60,394,154 and 59,941,088 shares issued and outstanding, respectively | 604 | 599 |
| Additional paid-in capital | 1,194,774 | 1,190,250 |
| Cumulative dividends in excess of net income | (133,463 |) (144,734) |
| Accumulated other comprehensive income | 7,986 | 2,313 |
| Total shareholders' equity | 1,069,901 | 1,048,428 |
| Total liabilities and shareholders' equity | \$ 1,930,678 | \$ 1,975,360 |
| The accompanying notes are an integral part of these consolidated financial statements. | | |

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CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data)

(unaudited)

| | Three Months Ended | | Nine Months Ended | |
|--|--------------------|-----------|-------------------|-----------|
| | September 30, | | September 30, | |
| | 2018 | 2017 | 2018 | 2017 |
| REVENUE | | | | |
| Rooms | \$122,716 | \$123,241 | \$348,846 | \$344,410 |
| Food and beverage | 25,396 | 27,172 | 83,590 | 89,620 |
| Other | 8,241 | 7,864 | 22,227 | 21,582 |
| Total revenue | 156,353 | 158,277 | 454,663 | 455,612 |
| EXPENSES | | | | |
| Hotel operating expenses: | | | | |
| Rooms | 27,865 | 28,132 | 80,623 | 80,822 |
| Food and beverage | 20,027 | 21,306 | 62,876 | 66,694 |
| Other direct | 1,369 | 1,480 | 3,721 | 4,136 |
| Indirect | 54,639 | 54,081 | 157,976 | 157,428 |
| Total hotel operating expenses | 103,900 | 104,999 | 305,196 | 309,080 |
| Depreciation and amortization | 18,621 | 19,369 | 56,934 | 57,252 |
| Air rights contract amortization | 130 | 130 | 390 | 390 |
| Corporate general and administrative | 4,419 | 4,216 | 14,522 | 13,798 |
| Total operating expenses | 127,070 | 128,714 | 377,042 | 380,520 |
| Operating income | 29,283 | 29,563 | 77,621 | 75,092 |
| Interest income | 190 | — | 228 | — |
| Interest expense | (8,445) | (9,020) | (26,203) | (24,989) |
| Gain on sale of hotel | 33,109 | — | 33,109 | — |
| Income before income taxes | 54,137 | 20,543 | 84,755 | 50,103 |
| Income tax expense | (758) | (1,590) | (1,017) | (1,470) |
| Net income | 53,379 | 18,953 | 83,738 | 48,633 |
| Preferred share dividends | — | (430) | — | (5,274) |
| Write-off of issuance costs of redeemed preferred shares | — | (4,419) | — | (4,419) |
| Net income available to common shareholders | \$53,379 | \$14,104 | \$83,738 | \$38,940 |
| Net income available per common share: | | | | |
| Basic | \$0.90 | \$0.24 | \$1.41 | \$0.65 |
| Diluted | \$0.89 | \$0.24 | \$1.39 | \$0.65 |

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

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CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(in thousands)

(unaudited)

| | Three Months | | Nine Months | |
|--|-----------------|----------|-----------------|----------|
| | Ended September | | Ended September | |
| | 30, | 30, | 30, | 30, |
| | 2018 | 2017 | 2018 | 2017 |
| Net income | \$53,379 | \$18,953 | \$83,738 | \$48,633 |
| Other comprehensive income: | | | | |
| Unrealized gains (losses) on cash flow hedge instruments | 1,063 | (215) | 5,688 | (722) |
| Reclassification of unrealized losses (gains) on cash flow hedge instruments to interest expense | (131) | 366 | (15) | 780 |
| Comprehensive income | \$54,311 | \$19,104 | \$89,411 | \$48,691 |

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

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CHESAPEAKE LODGING TRUST
CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY
(in thousands, except share data)
(unaudited)

| | Common Shares | | Additional Paid-In Capital | Cumulative Dividends in Excess of Net Income | Accumulated Other Comprehensive Income | Total |
|---|---------------|--------|----------------------------------|---|---|-------------|
| | Shares | Amount | | | | |
| Balances at December 31, 2017 | 59,941,088 | \$ 599 | \$1,190,250 | \$ (144,734) | \$ 2,313 | \$1,048,428 |
| Repurchase of common shares | (42,137) | — | (1,146) | — | — | (1,146) |
| Issuance of restricted common shares | 495,579 | 5 | (5) | — | — | — |
| Issuance of unrestricted common shares | 2,712 | — | 83 | — | — | 83 |
| Forfeiture of restricted common shares | (3,088) | — | — | — | — | — |
| Amortization of deferred compensation | — | — | 5,592 | — | — | 5,592 |
| Declaration of dividends on common shares | — | — | — | (72,467) | — | (72,467) |
| Net income | — | — | — | 83,738 | — | 83,738 |
| Other comprehensive income | — | — | — | — | 5,673 | 5,673 |
| Balances at September 30, 2018 | 60,394,154 | \$ 604 | \$1,194,774 | \$ (133,463) | \$ 7,986 | \$1,069,901 |

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

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CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)

| | Nine Months Ended September 30, | |
|---|---------------------------------------|-----------|
| | 2018 | 2017 |
| Cash flows from operating activities: | | |
| Net income | \$83,738 | \$48,633 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 56,934 | 57,252 |
| Air rights contract amortization | 390 | 390 |
| Deferred financing costs amortization | 1,211 | 1,248 |
| Gain on sale of hotel | (33,109) | — |
| Share-based compensation | 5,675 | 5,671 |
| Other | (226) | (465) |
| Changes in assets and liabilities: | | |
| Accounts receivable, net | (11,785) | (8,825) |
| Prepaid expenses and other assets | 1,212 | (1,907) |
| Accounts payable and accrued expenses | 8,801 | 5,089 |
| Other liabilities | (104) | 173 |
| Net cash provided by operating activities | 112,737 | 107,259 |
| Cash flows from investing activities: | | |
| Disposition of hotel, net of cash sold | 89,821 | — |
| Improvements and additions to hotels | (30,066) | (41,952) |
| Net cash provided by (used in) investing activities | 59,755 | (41,952) |
| Cash flows from financing activities: | | |
| Redemption of preferred shares | — | (125,000) |
| Borrowings under revolving credit facility | 55,000 | 300,000 |
| Repayments under revolving credit facility | (120,000) | (250,000) |
| Proceeds from issuance of unsecured term loan | — | 225,000 |
| Scheduled principal payments on mortgage debt | (9,604) | (134,435) |
| Payment of deferred financing costs | (1,560) | (1,771) |
| Payment of dividends to common shareholders | (71,291) | (72,168) |
| Payment of dividends to preferred shareholders | — | (7,320) |
| Repurchase of common shares | (1,146) | (1,065) |
| Net cash used in financing activities | (148,601) | (66,759) |
| Net increase (decrease) in cash, cash equivalents, and restricted cash | 23,891 | (1,452) |
| Cash, cash equivalents, and restricted cash, beginning of period | 74,916 | 79,188 |
| Cash, cash equivalents, and restricted cash, end of period | \$98,807 | \$77,736 |
| Supplemental disclosure of cash flow information: | | |
| Cash paid for interest | \$24,667 | \$23,340 |
| Cash paid for income taxes | \$860 | \$1,650 |

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

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CHESAPEAKE LODGING TRUST
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. Organization and Description of Business

Chesapeake Lodging Trust (the “Trust”) is a self-advised real estate investment trust (“REIT”) that was organized in the state of Maryland. The Trust is focused on investments primarily in upper-upscale hotels in major business and convention markets and, on a selective basis, premium select-service hotels in urban settings or unique locations in the United States of America (“U.S.”). As of September 30, 2018, the Trust owned 20 hotels with an aggregate of 6,279 rooms in eight states and the District of Columbia.

Substantially all of the Trust’s assets are held by, and all of its operations are conducted through, Chesapeake Lodging, L.P., a Delaware limited partnership, which is wholly owned by the Trust (the “Operating Partnership”). For the Trust to qualify as a REIT, it cannot operate hotels. Therefore, the Operating Partnership leases its hotels to taxable REIT subsidiaries (each, a “TRS”), which are wholly owned subsidiaries of the Operating Partnership and are treated as TRSs for federal income tax purposes. The TRSs then engage hotel management companies to operate the hotels pursuant to management agreements.

2. Summary of Significant Accounting Policies

Basis of Presentation—The interim consolidated financial statements presented herein include all of the accounts of Chesapeake Lodging Trust and its subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation. Certain reclassifications have been made to the prior year financial statements to conform to the current year presentation. These reclassifications had no effect on previously reported results of operations or retained earnings.

The information in these interim consolidated financial statements is unaudited but, in the opinion of management, reflects all adjustments necessary for a fair presentation of the results for the periods covered. All such adjustments are of a normal, recurring nature unless disclosed otherwise. These interim consolidated financial statements, including notes, have been prepared in accordance with the applicable rules of the Securities and Exchange Commission (“SEC”) and do not include all of the information and disclosures required by U.S. generally accepted accounting principles (“GAAP”) for complete financial statements. These interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and accompanying notes included in the Trust’s Form 10-K for the year ended December 31, 2017.

Cash and Cash Equivalents—The Trust considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

Restricted Cash—Restricted cash includes reserves held in escrow for normal replacements of furniture, fixtures and equipment (“FF&E”), property improvement plans (each, a “PIP”), real estate taxes, and property insurance pursuant to certain requirements in the Trust’s hotel management, franchise, and loan agreements.

Investments in Hotels—The Trust allocates the purchase prices of hotels acquired based on the fair value of the property, FF&E, and identifiable intangible assets acquired and the fair value of the liabilities assumed. In making estimates of fair value for purposes of allocating the purchase price, the Trust utilizes a number of sources of information that are obtained in connection with the acquisition of a hotel, including valuations performed by independent third parties and cost segregation studies. The Trust also considers information obtained about each hotel as a result of its pre-acquisition due diligence in estimating the fair value of the tangible and intangible assets acquired and liabilities assumed. Hotel acquisition costs, such as transfer taxes, title insurance, environmental and property condition reviews, and legal and accounting fees, are expensed in the period incurred if the acquisition of the hotel is determined to be an acquisition of a business; if the acquisition of the hotel is determined to be an acquisition of an asset, hotel acquisition costs are capitalized.

Property and equipment are depreciated using the straight-line method over the estimated useful lives of the assets, generally 15 to 40 years for buildings and building improvements and three to ten years for FF&E. Leasehold improvements are amortized over the shorter of the lease term or the useful lives of the related assets. Replacements and improvements at the hotels are capitalized, while repairs and maintenance are expensed as incurred. Upon the sale

or retirement of property and equipment, the cost and related accumulated depreciation are removed from the Trust's accounts and any resulting gain or loss is recognized in the consolidated statements of operations.

Intangible assets and liabilities are recorded on non-market contracts, including air rights, lease, management, and franchise agreements, assumed as part of the acquisition of certain hotels. Above-market and below-market contract values are based on the present value of the difference between contractual amounts to be paid pursuant to the contracts assumed and the Trust's estimate of the fair market contract rates for corresponding contracts measured over a period equal to the remaining non-cancelable term of the contracts assumed. No value is allocated to market contracts. Intangible assets and liabilities are amortized using the straight-line method over the remaining non-cancelable term of the related contracts.

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The Trust reviews its hotels for impairment whenever events or changes in circumstances indicate that the carrying values of the hotels may not be recoverable. Events or circumstances that may cause a review include, but are not limited to, adverse changes in the demand for lodging at the hotels due to declining national or local economic conditions and/or new hotel construction in markets where the hotels are located. When such conditions exist, management performs an analysis to determine if the estimated undiscounted future cash flows from operations and the proceeds from the ultimate disposition of a hotel exceed its carrying value. If the estimated undiscounted future cash flows are less than the carrying amount of the asset, an adjustment to reduce the carrying amount to the related hotel's estimated fair market value is recorded and an impairment loss is recognized. No impairment losses have been recognized related to any hotels for the three and nine months ended September 30, 2018 and 2017.

The Trust classifies a hotel as held for sale in the period in which it has made the decision to dispose of the hotel, a binding agreement to purchase the hotel has been signed under which the buyer has committed a significant amount of nonrefundable cash, and no significant financing contingencies exist which could cause the transaction not to be completed in a timely manner. If these criteria are met, depreciation and amortization of the hotel will cease and an impairment loss will be recognized if the fair value of the hotel, less the costs to sell, is lower than the carrying amount of the hotel. If the sale represents a strategic shift that has (or will have) a major effect on the Trust's operations and financial results, the Trust will classify the loss, together with the related operating results, as discontinued operations in the consolidated statements of operations and will classify the related assets and liabilities as held for sale in the consolidated balance sheets. As of September 30, 2018 and December 31, 2017, the Trust had no assets held for sale or liabilities related to assets held for sale.

Revenue Recognition—Revenues from operations of the hotels are recognized when goods and services are provided and the performance obligations are satisfied, net of any sales, occupancy, or other similar taxes collected from customers. Revenues consist of room sales, food and beverage sales, and other hotel revenues and are presented on a disaggregated basis on the consolidated statements of operations.

Room revenue is generated through short-term contracts with customers whereby customers agree to pay a daily rate for the right to use hotel rooms for one or more nights. The Trust's performance obligations are fulfilled at the end of each night that the customers are provided the rooms and room revenue is recognized daily at the contract rate in effect for each room night.

Food and beverage revenue is generated when customers agree to pay for food and beverage at a hotel's restaurant or bar outlets or for banquet and catering services at a hotel. The Trust's performance obligations are fulfilled at the time that the food and beverage is provided or when the banquet facilities and related dining and other amenities (e.g., audio visual services) are provided.

Other revenue (e.g., parking, marina, resort and cancellation fees, theater, leasing, spa, telephone, and gift shop sales) is recognized at the point in time or over the time period that the associated good or service is provided. Ancillary services (e.g., parking) at certain hotels are provided by third parties and the Trust assesses whether the Trust is the principal or agent in such arrangements. If the Trust is determined to be the agent, revenue is recognized based upon the commission earned from the third party on the provided service. If the Trust is determined to be the principal, revenue is recognized based upon the gross contract price of the provided service. Certain of the Trust's hotels have retail spaces, restaurants or other spaces which the Trust leases to third parties. Lease revenue is recognized on a straight-line basis over the life of the lease and included within other revenue.

Advance deposits are generally provided when a customer or group of customers provides a deposit for a future stay or banquet event at the Trust's hotels. Advance deposits are converted to revenue when the associated goods or services are provided to the customer or when a customer with a noncancellable reservation fails to arrive for part or all of the reservation. Conversely, advance deposits are generally refundable upon guest cancellation of the related reservation within an established period of time prior to the reservation.

Prepaid Expenses and Other Assets—Prepaid expenses and other assets consist of prepaid real estate taxes, prepaid insurance, deposits on hotel acquisitions and loan applications, deferred franchise costs, inventories, deferred tax assets, and other assets.

Deferred Financing Costs—Deferred financing costs are recorded at cost and consist of loan fees and other costs incurred in issuing debt. Amortization of deferred financing costs is computed using a method that approximates the

effective interest method over the term of the related debt and is included in interest expense in the consolidated statements of operations. Unamortized deferred financing costs are included as a direct deduction from long-term debt in the consolidated balance sheets.

Derivative Instruments—From time to time, the Trust is a party to interest rate swaps, which are considered derivative instruments, in order to manage its interest rate exposure. The Trust's interest rate risk management objective is to limit the impact of interest rate changes on earnings and cash flows. The Trust records derivative instruments at fair value as either assets or liabilities and designates them as cash flow hedging instruments at inception. The Trust evaluates the hedge effectiveness of the designated cash flow hedging instruments on a quarterly basis and records the effective portion of the change in the fair

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value of the cash flow hedging instruments as other comprehensive income (loss). Amounts reported in accumulated other comprehensive income (loss) related to cash flow hedging instruments are reclassified to interest expense as interest payments are made on the variable-rate debt being hedged. The Trust does not enter into derivative instruments for trading or speculative purposes and monitors the financial stability and credit standing of its counterparties.

Fair Value Measurements—The Trust accounts for certain assets and liabilities at fair value. In evaluating the fair value of both financial and non-financial assets and liabilities, GAAP outlines a valuation framework and creates a fair value hierarchy that distinguishes between market assumptions based on market data (observable inputs) and the reporting entity's own assumptions about market data (unobservable inputs). The three levels of the fair value hierarchy are as follows:

Level 1 – Inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that are accessible at the measurement date. An active market is defined as a market in which transactions occur with sufficient frequency and volume to provide pricing on an ongoing basis.

Level 2 – Inputs include quoted prices in active markets for similar assets and liabilities, quoted prices for identical or similar assets or liabilities in markets that are not active (markets with few transactions), inputs other than quoted prices that are observable for the asset or liability (e.g., interest rates, yield curves), and inputs that are derived principally from or corroborated by observable market data correlation or other means.

Level 3 – Unobservable inputs reflect the reporting entity's own assumptions about the pricing of an asset or liability when observable inputs are not available or when there is minimal, if any, market activity for an identical or similar asset or liability at the measurement date.

Income Taxes—The Trust has elected to be taxed as a REIT under Sections 856 through 860 of the Internal Revenue Code. As a REIT, the Trust generally will not be subject to federal income tax on that portion of its net income that does not relate to any of the Trust's TRSs, and that is currently distributed to its shareholders. The Trust's TRSs, which lease the Trust's hotels from the subsidiaries of the Operating Partnership owning them, are subject to federal and state income taxes.

The Trust accounts for income taxes using the asset and liability method under which deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Valuation allowances are provided if based upon the weight of the available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized.

Share-Based Compensation—From time to time, the Trust grants restricted share awards to employees and trustees. To date, the Trust has granted two types of restricted share awards: (1) awards that vest solely on continued employment or service (time-based awards) and (2) awards that vest based on the Trust achieving specified levels of relative total shareholder return and continued employment (performance-based awards). The Trust measures share-based compensation expense for the restricted share awards based on the fair value of the awards on the date of grant. The fair value of time-based awards is determined based on the closing price of the Trust's common shares on the measurement date, which is generally the date of grant. The fair value of performance-based awards is determined using a Monte Carlo simulation performed by an independent third party. For time-based awards, share-based compensation expense is recognized on a straight-line basis over the life of the entire award. For performance-based awards, share-based compensation expense is recognized over the requisite service period for each award. No share-based compensation expense is recognized for awards for which employees or trustees do not render the requisite service.

Earnings Per Share—Basic earnings per share is computed by dividing net income available to common shareholders, adjusted for dividends declared on and undistributed earnings allocated to unvested time-based awards, by the weighted-average number of common shares outstanding during the period. Diluted earnings per share is computed by dividing net income available to common shareholders, adjusted for dividends declared on and undistributed earnings allocated to unvested time-based awards, by the weighted-average number of common shares outstanding, plus potentially dilutive securities, such as unvested performance-based awards, during the period. The Trust's unvested time-based awards are entitled to receive non-forfeitable dividends, if declared. Therefore, unvested time-based

awards qualify as participating securities, requiring the allocation of dividends and undistributed earnings under the two-class method to calculate basic earnings per share. The percentage of undistributed earnings allocated to the unvested time-based awards is based on the proportion of the weighted-average unvested time-based awards outstanding during the period to the total of the weighted-average common shares and unvested time-based awards outstanding during the period. No adjustment is made for shares that are anti-dilutive during the period.

Segment Information—The Trust has determined that its business is conducted in one reportable segment, hotel ownership.

Use of Estimates—The preparation of the interim consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the interim consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

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Recent Accounting Pronouncements—In May 2014, the Financial Accounting Standards Board (the “FASB”) issued updated accounting guidance for recognition of revenue from contracts with customers. The comprehensive new accounting guidance supersedes previous revenue recognition guidance and requires revenue to be recognized when promised goods or services are transferred to customers in amounts that reflect the consideration to which the company expects to be entitled in exchange for those goods or services. In July 2015, the FASB delayed the effective date of the new accounting guidance to be for interim and annual periods beginning on or after December 15, 2017. The Trust adopted the new accounting guidance on January 1, 2018 on a modified retrospective basis. Based on the Trust’s completed assessment of this updated accounting guidance, it does not materially affect the amount or timing of revenue recognition for room sales, food and beverage sales, or other hotel departmental revenues because of the short-term, day to day nature of those revenues and the Trust did not recognize any cumulative-effect adjustment as a result of adopting this new accounting guidance. Furthermore, the Trust does not expect the updated accounting guidance to materially impact the recognition of or accounting for disposition of hotels, since the Trust primarily disposes of hotels to third parties in exchange for cash with few contingencies.

In November 2016, the FASB issued updated accounting guidance which requires the consolidated statements of cash flows to explain the change during the period in the total of cash, cash equivalents and restricted cash. Therefore, restricted cash should be included within cash and cash equivalents when reconciling the beginning of period and end of period total amounts shown on the consolidated statements of cash flows. The new accounting guidance is effective for interim and annual periods beginning after December 15, 2017 and is to be applied on a retrospective basis. The Trust adopted the new accounting guidance on January 1, 2018. The adoption of this guidance changed the presentation of restricted cash in the consolidated statements of cash flows; however, the Trust does not believe that the adoption of this guidance has a material impact on the consolidated financial statements.

In January 2017, the FASB issued updated accounting guidance to clarify the definition of a business. The new accounting guidance adds further guidance that assists entities in evaluating whether a transaction should be accounted for as an acquisition of (or disposal of) an asset or a business. Under the new accounting guidance, when substantially all of the fair value of the gross assets acquired (or disposed of) is concentrated in a single identifiable asset or a group of similar identifiable assets, the integrated set of assets and activities is not a business. The new accounting guidance is effective for interim and annual periods beginning after December 15, 2017 (early adoption is permitted) and is to be applied prospectively. The Trust adopted the new accounting guidance on January 1, 2018. The adoption of this guidance would result in the capitalization of hotel acquisition costs to the extent the Trust completes a future acquisition that is determined to be an acquisition of an asset rather than a business, which may have a material impact on its results of operations.

In February 2016, the FASB issued updated accounting guidance which sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract (i.e., lessees and lessors). The new accounting guidance requires lessees to apply a dual approach, classifying leases as either finance or operating leases based on whether or not the lease is effectively a financed purchase by the lessee. This classification will determine whether lease expense is recognized based on an effective interest method or on a straight line basis over the term of the lease, respectively. A lessee is also required to record a right-of-use asset and a lease liability for all leases with terms greater than 12 months regardless of their classification. Leases with terms of 12 months or less will be accounted for similarly to existing guidance for operating leases. This new accounting guidance is effective for annual periods beginning after December 15, 2018 (early adoption is permitted) and is to be applied on a modified retrospective approach. The Trust is in the process of creating an inventory of its leases and analyzing its current ground lease agreements. The Trust expects to record assets and liabilities on its consolidated balance sheets associated with the ground lease agreements under the new accounting guidance; however, the Trust is still evaluating the impact that this guidance will have on its consolidated financial statements.

3. Dispositions

On November 8, 2017, the Trust sold the 222-room The Hotel Minneapolis, Autograph Collection for \$46.3 million, including sold working capital. Net proceeds from the sale were \$46.0 million, which resulted in the recognition of a gain on sale of \$6.1 million. On July 26, 2018, the Trust sold the 200-room Hyatt Centric Santa Barbara for \$90.1

million, including sold working capital. Net proceeds from the sale were \$89.8 million, which resulted in the recognition of a gain on sale of \$33.1 million. Neither of these sales represented a strategic shift that had (or will have) a major effect on the Trust's operations and financial results, and therefore, did not qualify to be reported as discontinued operations.

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4. Property and Equipment

Property and equipment as of September 30, 2018 and December 31, 2017 consisted of the following (in thousands):

| | September 30, 2018 | December 31, 2017 |
|---|-----------------------|----------------------|
| Land and land improvements | \$286,718 | \$316,815 |
| Buildings and leasehold improvements | 1,614,896 | 1,628,945 |
| Furniture, fixtures and equipment | 230,250 | 228,492 |
| Construction-in-progress | 14,249 | 6,640 |
| | 2,146,113 | 2,180,892 |
| Less: accumulated depreciation and amortization | (406,507) | (357,675) |
| Property and equipment, net | \$1,739,606 | \$1,823,217 |

5. Intangible Assets

Intangible assets as of September 30, 2018 and December 31, 2017 consisted of the following (in thousands):

| | September 30, 2018 | December 31, 2017 |
|---------------------------------------|-----------------------|----------------------|
| Air rights contract ⁽¹⁾ | \$36,105 | \$36,105 |
| Favorable ground lease ⁽²⁾ | 3,568 | 3,568 |
| | 39,673 | 39,673 |
| Less: accumulated amortization | (4,850) | (4,417) |
| Intangible assets, net | \$34,823 | \$35,256 |

In conjunction with the acquisition of the Hyatt Regency Boston on March 18, 2010, the Trust acquired an air rights contract which expires in September 2079 and that requires no payments through maturity. The Trust recorded the fair value of the air rights contract of \$36.1 million as an intangible asset and is amortizing the value over the term of the contract.

In conjunction with the acquisition of the Hilton Denver City Center on October 3, 2011, the Trust assumed a lease agreement for a land parcel underlying a portion of the hotel with an initial term ending February 2072 that it concluded had below market terms. The Trust recorded a favorable ground lease asset of \$3.6 million associated with this lease agreement at the time. The Trust is amortizing the favorable ground lease asset over the life of the lease and including the amortization within indirect hotel operating expenses in the interim consolidated statements of operations.

6. Long-Term Debt

Long-term debt as of September 30, 2018 and December 31, 2017 consisted of the following (in thousands):

| | Origination | Original Principal Amount | Maturity | Interest Rate | Principal Amortization Period | September 30, 2018 | December 31, 2017 |
|--|---------------|---------------------------------|-------------|------------------|-------------------------------------|--------------------------|-------------------------|
| Unsecured: | | | | | | | |
| Revolving credit facility ⁽¹⁾ | July 2010 | n/a | May 2022 | Floating | n/a | \$— | \$65,000 |
| Term loan ⁽²⁾ | April 2017 | \$225,000 | April 2022 | Floating | n/a | 225,000 | 225,000 |
| Secured: | | | | | | | |
| Boston Marriott Newton | May 2013 | \$60,000 | June 2020 | 3.63% | 25 | 51,647 | 52,941 |
| Le Meridien San Francisco | July 2013 | \$92,500 | August 2020 | 3.50% | 25 | 79,864 | 81,875 |
| Hilton Denver City Center ⁽³⁾ | July 2012 | \$70,000 | August 2022 | 4.90% | 30 | 62,731 | 63,748 |
| Hilton Checkers Los Angeles | February 2013 | \$32,000 | March 2023 | 4.11% | 30 | 28,775 | 29,260 |

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| | | | | | | | |
|---|-----------|-----------|----------------|-------|----|-----------|-----------|
| W Chicago – City Center | July 2013 | \$93,000 | August 2023 | 4.25% | 25 | 81,454 | 83,320 |
| Hyatt Herald Square New York/Hyatt Place New York Midtown South | July 2014 | \$90,000 | July 2024 | 4.30% | 30 | 86,791 | 87,938 |
| Hyatt Regency Boston | June 2016 | \$150,000 | July 2026 | 4.25% | 30 | 144,382 | 146,166 |
| Unamortized deferred financing costs | | | | | | 760,644 | 835,248 |
| Long-term debt | | | | | | (6,045) | (5,696) |
| | | | | | | \$754,599 | \$829,552 |

The Trust may exercise an option to extend the maturity by one year, subject to certain customary conditions. As of (1) September 30, 2018, the interest rate in effect was 3.84%. See below for additional information related to the revolving credit facility.

The term loan bears interest equal to LIBOR plus 1.45% - 2.20% (the spread over LIBOR based on the Trust's consolidated leverage ratio). Contemporaneous with the closing of the term loan, the Trust entered into an interest rate swap to fix LIBOR at 1.86% for the five-year term (as of September 30, 2018, the effective interest rate on the term loan was 3.41%). Under the terms of this interest rate swap, the Trust pays fixed interest of

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1.86% per annum on a notional amount of \$225.0 million and receives floating rate interest equal to one-month LIBOR. The effective date of this interest rate swap was April 21, 2017 and it will mature on April 21, 2022.

(3) The loan has a term of 30 years, but is callable by the lender after 10 years, and the Trust expects the lender to call the loan at that time. The indicated maturity is based on the date the loan is callable by the lender.

Unsecured revolving credit facility and term loan

On May 31, 2018, the Trust entered into an amended and restated credit agreement with a syndicate of banks to (1) extend the maturity date to May 2022 and (2) lower the interest rate to LIBOR plus 1.45% - 2.20% (the spread over LIBOR continues to be based on the Trust's consolidated leverage ratio) for its revolving credit facility. The amended credit agreement provides for the possibility of further future increases, up to a maximum of \$450.0 million, in accordance with the terms of the amended credit agreement. The amended credit agreement also provides for an extension of the maturity date by one year, subject to satisfaction of certain customary conditions.

On April 21, 2017, the Trust obtained a \$225.0 million, five-year, unsecured term loan from a syndicate of banks. The term loan provides for the possibility of future increases, up to a maximum amount borrowed of \$375.0 million, in accordance with the terms of the term loan agreement.

The amount that the Trust can borrow in the aggregate under the revolving credit facility and the term loan is based on the value of the Trust's hotels included in the borrowing base, as defined in the amended credit agreement and the term loan agreement. As of September 30, 2018, the borrowing base included 11 of the Trust's hotels providing borrowing availability of \$300.0 million under the revolving credit facility, all of which remained available. The amended credit agreement and the term loan agreement contain financial covenants, including a leverage ratio and a minimum tangible net worth requirement, and additional financial covenants typically found in similar unsecured revolving credit facilities and term loans, including a consolidated secured debt ratio, an unsecured leverage ratio and an unsecured debt service coverage ratio.

Other

Certain of the Trust's mortgage loan agreements contain standard financial covenants relating to coverage ratios and standard provisions that require loan servicers to maintain escrow accounts for certain items, including real estate taxes, property insurance premiums, and normal replacements of FF&E.

As of September 30, 2018, the Trust was in compliance with all financial covenants under its borrowing arrangements. As of September 30, 2018, the Trust's weighted-average interest rate on its long-term debt was 3.94%.

Future scheduled principal payments of debt obligations (assuming no exercise of extension options) as of September 30, 2018 are as follows (in thousands):

| Year | Amounts |
|------------|-----------|
| 2018 | \$3,356 |
| 2019 | 13,731 |
| 2020 | 135,316 |
| 2021 | 10,233 |
| 2022 | 291,635 |
| Thereafter | 306,373 |
| | \$760,644 |

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7. Indirect Expenses

Indirect hotel operating expenses for the three and nine months ended September 30, 2018 and 2017 consisted of the following (in thousands):

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|-----------------------------------|----------------------------------|----------|---------------------------------|-----------|
| | 2018 | 2017 | 2018 | 2017 |
| Administrative and general | \$13,031 | \$13,004 | \$38,443 | \$38,843 |
| Advertising and sales | 10,872 | 10,914 | 32,657 | 32,240 |
| Repairs and maintenance | 5,325 | 5,226 | 15,956 | 15,763 |
| Utilities | 4,163 | 4,352 | 11,440 | 12,026 |
| Franchise fees | 2,526 | 2,799 | 7,563 | 7,664 |
| Management fees | 6,079 | 6,634 | 16,562 | 17,361 |
| Property and other taxes | 9,392 | 8,108 | 26,093 | 24,656 |
| Insurance, leases and other | 3,251 | 3,044 | 9,262 | 8,875 |
| Indirect hotel operating expenses | \$54,639 | \$54,081 | \$157,976 | \$157,428 |

8. Earnings Per Share

The following is a reconciliation of the amounts used in calculating basic and diluted earnings per share (in thousands, except share and per share data):

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|----------------------------------|------------|---------------------------------|------------|
| | 2018 | 2017 | 2018 | 2017 |
| Numerator: | | | | |
| Net income available to common shareholders | \$53,379 | \$14,104 | \$83,738 | \$38,940 |
| Less: Dividends declared on unvested time-based awards | (118) | (124) | (358) | (371) |
| Less: Undistributed earnings allocated to unvested time-based awards | (147) | — | (63) | — |
| Net income available to common shareholders, excluding amounts attributable to unvested time-based awards | \$53,114 | \$13,980 | \$83,317 | \$38,569 |
| Denominator: | | | | |
| Weighted-average number of common shares outstanding—basic | 59,148,764 | 59,043,425 | 59,134,264 | 59,024,497 |
| Effect of dilutive unvested performance-based awards | 726,663 | 244,387 | 687,063 | 220,306 |
| Weighted-average number of common shares outstanding—diluted | 59,875,427 | 59,287,812 | 59,821,327 | 59,244,803 |
| Net income available per common share: | | | | |
| Basic | \$0.90 | \$0.24 | \$1.41 | \$0.65 |
| Diluted | \$0.89 | \$0.24 | \$1.39 | \$0.65 |

For the three and nine months ended September 30, 2018 and 2017, 76,747 unvested performance-based awards and 371,352 unvested performance-based awards, respectively, were excluded from diluted weighted-average common shares outstanding as the awards had not achieved the specific levels of relative total shareholder return required for vesting at each period end.

9. Shareholders' Equity

Common Shares—The Trust is authorized to issue up to 400,000,000 common shares, \$.01 par value per share. Each outstanding common share entitles the holder to one vote on all matters submitted to a vote of shareholders. Holders of the Trust's common shares are entitled to receive distributions when authorized by the Trust's board of trustees out of assets legally available for the payment of distributions.

For the nine months ended September 30, 2018, the Trust issued 2,712 unrestricted common shares and 495,579 restricted common shares to its trustees and employees. For the nine months ended September 30, 2018, the Trust repurchased 42,137 common shares from employees to satisfy the minimum statutory tax withholding requirements

related to the vesting of their previously granted restricted common shares. As of September 30, 2018, the Trust had 60,394,154 common shares outstanding.

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For the nine months ended September 30, 2018, the Trust paid or its board of trustees declared the following dividends per common share:

| | Record Date | Payment Date | Dividend Per Common Share |
|---------------------|--------------------|------------------|------------------------------------|
| Fourth Quarter 2017 | December 29, 2017 | January 12, 2018 | \$ 0.40 |
| First Quarter 2018 | March 29, 2018 | April 13, 2018 | \$ 0.40 |
| Second Quarter 2018 | June 29, 2018 | July 13, 2018 | \$ 0.40 |
| Third Quarter 2018 | September 28, 2018 | October 15, 2018 | \$ 0.40 |

Preferred Shares—The Trust is authorized to issue up to 100,000,000 preferred shares, \$.01 par value per share. The Trust’s board of trustees is required to set for each class or series of preferred shares the terms, preferences, conversion or other rights, voting powers, restrictions, limitations as to dividends or other distributions, qualifications, and terms or conditions of redemption. No preferred shares were outstanding as of September 30, 2018.

10. Equity Plan

In January 2010, the Trust established the Chesapeake Lodging Trust Equity Plan (the “Plan”), which provides for the issuance of equity-based awards, including restricted shares, unrestricted shares, share options, share appreciation rights, and other awards based on the Trust’s common shares. Employees and trustees of the Trust and other persons that provide services to the Trust are eligible to participate in the Plan. The compensation committee of the board of trustees administers the Plan and determines the number of awards to be granted, the vesting period, and the exercise price, if any.

In June 2018, the Trust’s common shareholders approved an amendment to the Plan to, among other things, increase the number of shares available for issuance under the Plan by 1,250,000 shares and extend the term of the Plan to June 2028. Shares that are issued under the Plan to any person pursuant to an award are counted against the aggregate number of shares available for issuance under the Plan as one share for every one share granted. If any shares covered by an award are not purchased or are forfeited, if an award is settled in cash, or if an award otherwise terminates without delivery of any shares, then the number of common shares counted against the aggregate number of shares available under the Plan with respect to the award will, to the extent of any such forfeiture or termination, again be available for making awards under the Plan. As of September 30, 2018, subject to increases that may result in the case of any future forfeiture or termination of currently outstanding awards, 1,584,144 common shares were reserved and available for future issuances under the Plan.

The Trust will make appropriate adjustments to outstanding awards and the number of shares available for issuance under the Plan, including the individual limitations on awards, to reflect share dividends, share splits, spin-offs and other similar events. While the compensation committee can terminate or amend the Plan at any time, no amendment can adversely impair the rights of grantees with respect to outstanding awards. In addition, an amendment will be contingent on approval of the Trust’s common shareholders to the extent required by law or if the amendment would materially increase the benefits accruing to participants under the Plan, materially increase the aggregate number of shares that can be issued under the Plan, or materially modify the requirements as to eligibility for participation in the Plan. Unless terminated earlier, the Plan will terminate in June 2028, but will continue to govern unexpired awards. For the nine months ended September 30, 2018, the Trust granted 495,579 restricted common shares to certain employees and trustees, of which 133,726 shares were time-based awards and 361,853 shares were performance-based awards (the “2018 Performance-Based Awards”). The time-based awards are generally eligible to vest at the annual rate of one-third of the number of restricted shares granted commencing on the first anniversary of their issuance. The 2018 Performance-Based Awards are eligible to vest at December 31, 2020. Dividends on the 2018 Performance-Based Awards accrue, but are not paid unless the related shares vest. The fair value of the 2018 Performance-Based Awards was \$10.82 per share and was determined using a Monte Carlo simulation with the following assumptions: volatility of 24.09%; an expected term equal to the requisite service period for the awards; and a risk-free interest rate of 2.00%.

The actual number of shares under the 2018 Performance-Based Awards that vest will be based on the Trust's total shareholder return ("TSR"), as defined in the restricted share agreements, measured over a three-year performance period ending December 31, 2020, relative to the total return generated by a market-cap weighted index that includes eight lodging REITs (the "Performance Peer Group"). The payout schedule for the 2018 Performance-Based Awards is as follows, with linear interpolation for performance between 67% and 100%, and between 100% and 133% of the Performance Peer Group:

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| | |
|---|-----------------------|
| Trust TSR as % of Performance Peer Group Total Return | Payout (% of Maximum) |
| <67% | 0% |
| 67% | 25% |
| 100% | 50% |
| ≥133% | 100% |

If the Trust's TSR is negative for the performance period, no shares under the 2018 Performance-Based Awards will vest. If the Trust's TSR is positive for the performance period and the total return of the Performance Peer Group is negative, 100% of the shares subject to vesting under the 2018 Performance-Based Awards will vest.

As of September 30, 2018, there was approximately \$9.3 million of unrecognized share-based compensation expense related to restricted common shares. The unrecognized share-based compensation expense is expected to be recognized over a weighted-average period of 1.8 years.

The following is a summary of the Trust's restricted common share activity for the nine months ended September 30, 2018:

| | Number of Shares | Weighted-Average Grant-Date Fair Value |
|---|------------------|--|
| Restricted common shares as of December 31, 2017 | 895,515 | \$ 15.93 |
| Granted | 495,579 | \$ 15.45 |
| Vested | (143,782) | \$ 27.97 |
| Forfeited | (3,088) | \$ 26.98 |
| Restricted common shares as of September 30, 2018 | 1,244,224 | \$ 14.32 |

11. Fair Value Measurements and Derivative Instrument

The following table sets forth the Trust's financial assets and liabilities measured at fair value by level within the fair value hierarchy (in thousands). Assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

| | Fair Value at September 30, 2018 | | | |
|--|----------------------------------|---------|----------|---------|
| | Total | Level 1 | Level 2 | Level 3 |
| Assets: | | | | |
| Interest rate swap (included within prepaid expenses and other assets) | \$7,986 | \$ — | -\$7,986 | \$ — |
| | \$7,986 | \$ — | -\$7,986 | \$ — |

Derivative instruments are classified within Level 2 of the fair value hierarchy as they are valued using third-party pricing models which contain inputs that are derived from observable market data. Where possible, the values produced by the pricing models are verified to market prices. Valuation models require a variety of inputs, including contractual terms, market prices, yield curves, credit spreads, measures of volatility, and correlations of such inputs. The Trust's financial instruments in addition to those disclosed in the table above include cash and cash equivalents, restricted cash, accounts receivable, accounts payable and accrued expenses, and long-term debt. The carrying values reported in the consolidated balance sheets for cash and cash equivalents, restricted cash, accounts receivable, and accounts payable and accrued expenses approximate fair value. The Trust estimates the fair value of its fixed rate debt by discounting the future cash flows of each instrument using estimated market rates of debt instruments with similar maturities and credit profiles. These inputs are classified as Level 3 within the fair value hierarchy. As of September 30, 2018, the carrying value reported in the consolidated balance sheet for the Trust's long-term debt approximated its fair value.

12. Commitments and Contingencies

Management Agreements—The Trust's hotels operate pursuant to management agreements with various third-party management companies. Each management company receives a base management fee generally between 2% and 4% of hotel revenues. The management companies are also eligible to receive an incentive management fee if hotel

operating income, as defined in the management agreements, exceeds certain performance thresholds. The incentive management fee is generally calculated as a percentage of hotel operating income after the Trust has received a priority return on its investment in the hotel.

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Franchise Agreements—As of September 30, 2018, 10 of the Trust’s hotels operated pursuant to franchise agreements with hotel brand companies and 10 hotels operated pursuant to management agreements with hotel brand companies that allowed them to operate under their respective brands. Under the 10 franchise agreements, the Trust generally pays a royalty fee ranging from 3% to 6% of room revenues and up to 3% of food and beverage revenues, plus additional fees for marketing, central reservation systems, and other franchisor costs that amount to between 1% and 5% of room revenues.

Ground Lease Agreements—The Trust leases the land underlying the Hyatt Regency Mission Bay Spa and Marina pursuant to a lease agreement, which has an initial term ending January 2056. Rent due under the lease agreement is the greater of base rent or percentage rent. Base rent is currently \$2.3 million per year. Base rent resets every three years over the remaining term of the lease equal to 75% of the average of the actual rent paid over the two years preceding the base rent reset year. The next base rent reset year is 2019. Annual percentage rent is calculated based on various percentages of the hotel’s various sources of revenue, including room, food and beverage, and marina rentals, earned during the period.

The Trust also leases the land underlying the JW Marriott San Francisco Union Square pursuant to a lease agreement, which has a term ending January 2083. Rent due under the lease agreement is the greater of base rent or percentage rent. Base rent is currently \$1.7 million per year. Base rent resets every five years over the remaining term of the lease based on the level of inflation, as defined in the agreement, over the preceding five years, but in no event resulting in an increase of more than 125% of the base rent in effect immediately prior to the reset year (nor subject to any decrease). The next base rent reset year is 2019. In January 2034, base rent will reset to 10% of the fair market value of the underlying land as determined by a valuation performed by an independent third party, if such reset results in an increase over the base rent in effect immediately prior to the reset year. Annual percentage rent is calculated based on various percentages of the hotel’s various sources of revenue, including room and food and beverage, earned during the period.

FF&E Reserves—Pursuant to its management, franchise and loan agreements, the Trust is required to establish a FF&E reserve for each hotel to cover the cost of replacing FF&E. Contributions to the FF&E reserve are based on a percentage of gross revenues at each hotel. The Trust is generally required to contribute between 3% and 5% of gross revenues over the term of the agreements.

Litigation—The Trust is not involved in any material litigation nor, to its knowledge, is any material litigation threatened against the Trust.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Statements

This report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and as such may involve known and unknown risks, uncertainties and other factors which may cause our actual results, performance or achievements to be materially different from future results, performance or achievements expressed or implied by such forward-looking statements. Forward-looking statements, which are based on certain assumptions and describe our future plans, strategies and expectations, are generally identified by our use of words, such as "intend," "plan," "may," "should," "will," "project," "estimate," "anticipate," "believe," "expect," "continue," "potential," "opportunity," and similar expressions, whether negative or affirmative. We cannot guarantee that we actually will achieve these plans, intentions or expectations. All statements regarding our expected financial position, business and financing plans are forward-looking statements. Factors which could have a material adverse effect on our operations and future prospects include, but are not limited to:

- U.S. economic conditions generally and the real estate market and the lodging industry specifically;
- management and performance of our hotels;
- our plans for renovation of our hotels;
- our financing plans and the terms on which capital is available to us;
- supply and demand for hotel rooms in our current and proposed market areas;
- our ability to acquire additional hotels and the risk that potential acquisitions may not be completed or perform in accordance with expectations;
- legislative/regulatory changes, including changes to laws governing taxation of real estate investment trusts; and
- our competition.

These risks and uncertainties, together with the information contained in our Form 10-K for the year ended December 31, 2017 under the caption "Risk Factors," should be considered in evaluating any forward-looking statement contained in this report or incorporated by reference herein. All forward-looking statements speak only as of the date of this report. All subsequent written and oral forward-looking statements attributable to us or any person acting on our behalf are qualified by the cautionary statements in this section. We undertake no obligation to update or publicly release any revisions to forward-looking statements to reflect events, circumstances or changes in expectations after the date of this report, except as required by law.

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Overview

The Trust was organized as a self-advised REIT in the state of Maryland in June 2009, with a focus on investments primarily in upper-upscale hotels in major business and convention markets and, on a selective basis, premium select-service hotels in urban settings or unique locations in the U.S. We completed our IPO in January 2010 and own the following 20 hotels as of the date of this filing:

| Hotel | Location | Rooms | Acquisition Date |
|---|-------------------|-------|-------------------|
| 1 Hyatt Regency Boston | Boston, MA | 502 | March 18, 2010 |
| 2 Hilton Checkers Los Angeles | Los Angeles, CA | 193 | June 1, 2010 |
| 3 Boston Marriott Newton | Newton, MA | 430 | July 30, 2010 |
| 4 Le Meridien San Francisco | San Francisco, CA | 360 | December 15, 2010 |
| 5 Homewood Suites Seattle Convention Center | Seattle, WA | 195 | May 2, 2011 |
| 6 W Chicago – City Center | Chicago, IL | 403 | May 10, 2011 |
| 7 Hotel Indigo San Diego Gaslamp Quarter | San Diego, CA | 210 | June 17, 2011 |
| 8 Courtyard Washington Capitol Hill/Navy Yard | Washington, DC | 204 | June 30, 2011 |
| 9 Hotel Adagio San Francisco, Autograph Collection | San Francisco, CA | 171 | July 8, 2011 |
| 10 Hilton Denver City Center | Denver, CO | 613 | October 3, 2011 |
| 11 Hyatt Herald Square New York | New York, NY | 122 | December 22, 2011 |
| 12 W Chicago – Lakeshore | Chicago, IL | 520 | August 21, 2012 |
| 13 Hyatt Regency Mission Bay Spa and Marina | San Diego, CA | 429 | September 7, 2012 |
| 14 Hyatt Place New York Midtown South | New York, NY | 185 | March 14, 2013 |
| 15 W New Orleans – French Quarter | New Orleans, LA | 97 | March 28, 2013 |
| 16 Le Meridien New Orleans | New Orleans, LA | 410 | April 25, 2013 |
| 17 Hyatt Centric Fisherman’s Wharf | San Francisco, CA | 316 | May 31, 2013 |
| 18 JW Marriott San Francisco Union Square | San Francisco, CA | 344 | October 1, 2014 |
| 19 Royal Palm South Beach Miami, a Tribute Portfolio Resort | Miami Beach, FL | 393 | March 9, 2015 |
| 20 Ace Hotel and Theater Downtown Los Angeles | Los Angeles, CA | 182 | April 30, 2015 |
| | | 6,279 | |

Hotel Operating Metrics

We believe that the results of operations of our hotels are best explained by five key performance indicators: occupancy, average daily rate (“ADR”), room revenue per available room (“RevPAR”), Adjusted Hotel EBITDAre, and Adjusted Hotel EBITDAre Margin. See the “Non-GAAP Financial Measures” section for additional information on Adjusted Hotel EBITDAre and Adjusted Hotel EBITDAre Margin.

Occupancy is a major driver of room revenue, as well as other revenue categories, such as food and beverage and parking. Fluctuations in occupancy are accompanied by fluctuations in most categories of variable hotel operating expenses, such as utility costs and certain labor costs, such as housekeeping. ADR helps to drive room revenue as well; however, it does not have a direct effect on other revenue categories. Fluctuations in ADR are accompanied by fluctuations in limited categories of hotel operating expenses, such as management fees and franchise fees, since variable hotel operating expenses generally do not increase or decrease correspondingly. Thus, increases in RevPAR attributable to increases in occupancy typically result in varying levels of increases in Adjusted Hotel EBITDAre and Adjusted Hotel EBITDAre Margin, while increases in RevPAR attributable to increases in ADR typically result in greater levels of increases in Adjusted Hotel EBITDAre and Adjusted Hotel EBITDAre Margin.

Executive Summary

Our comparable 20-hotel portfolio had a RevPAR increase of 5.0% during the third quarter of 2018 as compared to the third quarter of 2017, driven by an increase in occupancy of 1.4 percentage points and an increase in ADR of 3.3%. Our hotel portfolio outperformed the U.S. industry average RevPAR growth of 1.7%, as reported by STR. Given the increase in RevPAR and as a result of the efforts of our hotel managers, working with our asset management team, to manage and control expenses, our hotel portfolio also experienced an increase in Adjusted Hotel EBITDAre of 4.3% and an increase in Adjusted Hotel EBITDAre Margin of 20 basis points during the third quarter of

2018 as compared to the third quarter of 2017. We believe the headwinds we experienced throughout 2017 (i.e., disruption resulting from significant guestroom renovations at three of our hotels and the temporary closure of the Moscone Center in San Francisco, California in the second and third quarters) have and will continue to provide tailwinds for our hotel portfolio for the coming several years.

During the third quarter of 2018, we were able to take advantage of the strong pricing seen in the hotel transaction market by selling the Hyatt Centric Santa Barbara for a sale price of \$90.0 million, recognizing a gain on sale of \$33.1 million.

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We remain committed to maximizing cash flows from our hotel portfolio by driving optimum results, increasing operational efficiencies, and investing in the physical quality and positioning of our hotels. We believe our hotel portfolio, which is concentrated in the central business districts of top U.S. lodging markets, remains well positioned for future performance and long-term real estate value appreciation.

Results of Operations

Comparison of the three months ended September 30, 2018 and 2017

Results of operations for the three months ended September 30, 2018 include the operating activity of 20 hotels for the full period and one hotel for part of the period, whereas the results of operations for the three months ended September 30, 2017 include the operating activity of 22 hotels for the full period. We use the term “comparable hotel portfolio” to refer to those hotels owned for the entirety of the two periods being compared, and the term “non-comparable hotel portfolio” to refer to those hotels not owned for the entirety of the two periods being compared. For the three months ended September 30, 2018 and 2017, the comparable hotel portfolio includes the 20 hotels owned as of September 30, 2018 and the non-comparable hotel portfolio includes the Hyatt Centric Santa Barbara, which was sold on July 26, 2018, and The Hotel Minneapolis, Autograph Collection, which was sold on November 8, 2017.

Revenues—Total revenue for the three months ended September 30, 2018 was \$156.4 million, of which \$154.7 million was contributed by the comparable hotel portfolio and \$1.7 million was contributed by the non-comparable hotel portfolio. Total revenue for the three months ended September 30, 2017 was \$158.3 million, of which \$149.2 million was contributed by the comparable hotel portfolio and \$9.1 million was contributed by the non-comparable hotel portfolio. The increase in total revenue for the comparable hotel portfolio of \$5.5 million was primarily driven by an increase in total revenue at the JW Marriott San Francisco Union Square, which was undergoing a guestroom renovation during the three months ended September 30, 2017; and increases in total revenue at our other hotels located in San Francisco, where demand from customers during the three months ended September 30, 2017 was negatively impacted by the temporary closure of the Moscone Center and the resultant decrease in citywide events, Miami, where demand from customers during the three months ended September 30, 2017 was negatively impacted by Hurricane Irma, and Boston. The aforementioned increases in total revenue were offset partially by decreases in total revenue at our hotels located in Chicago, where demand from customers was negatively impacted by a two-week labor strike, Denver, Los Angeles, Seattle and New Orleans.

Hotel operating expenses—Hotel operating expenses, excluding depreciation and amortization, for the three months ended September 30, 2018 was \$103.9 million, of which \$102.9 million was contributed by the comparable hotel portfolio and \$1.0 million was contributed by the non-comparable hotel portfolio. Hotel operating expenses, excluding depreciation and amortization, for the three months ended September 30, 2017 was \$105.0 million, of which \$99.5 million was contributed by the comparable hotel portfolio and \$5.5 million was contributed by the non-comparable hotel portfolio. The increase in hotel operating expenses for the comparable hotel portfolio of \$3.4 million was primarily a result of the increase in corresponding total revenue for the comparable hotel portfolio. Specifically driving the increase in total hotel operating expenses for the comparable hotel portfolio were rooms expense and the following indirect hotel operating expenses: administrative and general, advertising and sales, repairs and maintenance, franchise fees, property and other taxes, and insurance, leases and other. Credit card commissions (included within administrative and general) and franchise fees are both variable hotel operating expenses calculated as a percentage of revenue, and therefore, increased commensurately with the increase in total revenue for the comparable hotel portfolio. The increase in property and other taxes was primarily driven by significantly higher property tax reassessments for 2018 at our hotels located in Chicago. The increases in the aforementioned expenses were offset partially by decreases in food and beverage expense, which was primarily a result of the corresponding decrease in food and beverage revenue for the comparable hotel portfolio, and management fees, which was primarily a result of no incentive management fees being incurred at the Hilton Denver City Center during the three months ended September 30, 2018 following a change in management of the hotel that took effect on December 1, 2017.

Depreciation and amortization—Depreciation and amortization expense for the three months ended September 30, 2018 and 2017 was \$18.6 million and \$19.4 million, respectively. The decrease in depreciation and amortization expense was primarily attributable to the sales of The Hotel Minneapolis, Autograph Collection in November 2017 and the Hyatt Centric Santa Barbara in July 2018.

Air rights contract amortization—Air rights contract amortization expense associated with the Hyatt Regency Boston for each of the three months ended September 30, 2018 and 2017 was \$0.1 million.

Corporate general and administrative—Corporate general and administrative expense for the three months ended September 30, 2018 and 2017 was \$4.4 million and \$4.2 million, respectively. Included in corporate general and administrative expense for the three months ended September 30, 2018 and 2017 was \$1.9 million and \$1.8 million, respectively, of non-cash share-based compensation expense.

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Interest income—Interest income for the three months ended September 30, 2018 was \$0.2 million. There was no interest income for the three months ended September 30, 2017. The increase in interest income was primarily related to an increase in cash and cash equivalents and in short-term interest rates.

Interest expense—Interest expense for the three months ended September 30, 2018 and 2017 was \$8.4 million and \$9.0 million, respectively. The decrease in interest expense was primarily related to the decrease in average long-term debt outstanding during the three months ended September 30, 2018 as compared to the three months ended September 30, 2017, reflecting the repayment of debt with net proceeds from the sales of The Hotel Minneapolis, Autograph Collection in November 2017 and the Hyatt Centric Santa Barbara in July 2018.

Gain on sale of hotel—Gain on sale of hotel for the three months ended September 30, 2018 was \$33.1 million and related to the sale of the Hyatt Centric Santa Barbara in July 2018.

Income tax expense—Income tax expense for the three months ended September 30, 2018 and 2017 was \$0.8 million and \$1.6 million, respectively. Income tax expense is directly related to taxable income generated by our TRSs during the period. The decrease in income tax expense was partially related to a decrease in our effective income tax rate resulting from the enactment of the Tax Cuts and Jobs Act in December 2017.

Preferred share dividends—There was no preferred share dividends for the three months ended September 30, 2018.

Preferred share dividends for the three months ended September 30, 2017 was \$0.4 million. The decrease in preferred share dividends is directly related to the full redemption of the 7.75% Series A Cumulative Redeemable Preferred Shares in July 2017.

Write-off of issuance costs of redeemed preferred shares—Write-off of issuance costs of redeemed preferred shares for the three months ended September 30, 2017 of \$4.4 million related to the full redemption of the 7.75% Series A Cumulative Redeemable Preferred Shares in July 2017.

Comparison of the nine months ended September 30, 2018 and 2017

Results of operations for the nine months ended September 30, 2018 include the operating activity of 20 hotels for the full period and one hotel for part of the period, whereas the results of operations for the nine months ended September 30, 2017 include the operating activity of 22 hotels for the full period. We use the term “comparable hotel portfolio” to refer to those hotels owned for the entirety of the two periods being compared, and the term “non-comparable hotel portfolio” to refer to those hotels not owned for the entirety of the two periods being compared. For the nine months ended September 30, 2018 and 2017, the comparable hotel portfolio includes the 20 hotels owned as of September 30, 2018 and the non-comparable hotel portfolio includes the Hyatt Centric Santa Barbara, which was sold on July 26, 2018, and The Hotel Minneapolis, Autograph Collection, which was sold on November 8, 2017.

Revenues—Total revenue for the nine months ended September 30, 2018 was \$454.7 million, of which \$445.3 was contributed by the comparable hotel portfolio and \$9.4 million was contributed by the non-comparable hotel portfolio. Total revenue for the nine months ended September 30, 2017 was \$455.6 million, of which \$433.1 million was contributed by the comparable hotel portfolio and \$22.5 million was contributed by the non-comparable hotel portfolio. The increase in total revenue for the comparable hotel portfolio of \$12.2 million was primarily driven by increases in total revenue at the Boston Marriott Newton, the Hilton Denver City Center, the Hyatt Regency Mission Bay Spa and Marina and the JW Marriott San Francisco Union Square, all of which were undergoing guestroom renovations during all or a portion of the nine months ended September 30, 2017; and increases in total revenue at our other hotels located in San Francisco, where demand from customers during a portion of the nine months ended September 30, 2017 was negatively impacted by the temporary closure of the Moscone Center and the resultant decrease in citywide events, Boston, New York, and Miami. The aforementioned increases in total revenue were offset partially by decreases in total revenue at our hotels located in Chicago, Los Angeles, Denver, Seattle, and Washington D.C.

Hotel operating expenses—Hotel operating expenses, excluding depreciation and amortization, for the nine months ended September 30, 2018 was \$305.2 million, of which \$298.8 million was contributed by the comparable hotel portfolio and \$6.4 million was contributed by the non-comparable hotel portfolio. Hotel operating expenses, excluding depreciation and amortization, for the nine months ended September 30, 2017 was \$309.1 million, of which \$293.7 million was contributed by the comparable hotel portfolio and \$15.4 million was contributed by the non-comparable hotel portfolio. The increase in hotel operating expenses for the comparable hotel portfolio of \$5.1 million was

primarily a result of the increase in corresponding total revenue for the comparable hotel portfolio. Specifically driving the increase in total hotel operating expenses for the comparable hotel portfolio were rooms expense and the following indirect hotel operating expenses: administrative and general, advertising and sales, repairs and maintenance, franchise fees, property and other taxes, and insurance, leases and other. Credit card commissions (included within administrative and general) and franchise fees are both variable hotel operating expenses calculated as a percentage of revenue, and therefore, increased commensurately with the increase in total revenue for the comparable hotel portfolio. The increase in property and other taxes was primarily driven by significantly higher property tax reassessments for 2018 at our hotels located in Chicago. The increases in the aforementioned expenses were offset partially by

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decreases in food and beverage expense, which was primarily a result of the corresponding decrease in food and beverage revenue for the comparable hotel portfolio, and management fees, which was primarily a result of no incentive management fees being incurred at the Hilton Denver City Center during the nine months ended September 30, 2018 following a change in management of the hotel that took effect on December 1, 2017.

Depreciation and amortization—Depreciation and amortization expense for the nine months ended September 30, 2018 and 2017 was \$56.9 million and \$57.3 million, respectively. The decrease in depreciation and amortization expense was primarily attributable to the sales of The Hotel Minneapolis, Autograph Collection in November 2017 and the Hyatt Centric Santa Barbara in July 2018, offset partially by the guestroom renovations completed at three of our hotels during the nine months ended September 30, 2017.

Air rights contract amortization—Air rights contract amortization expense associated with the Hyatt Regency Boston for each of the nine months ended September 30, 2018 and 2017 was \$0.4 million.

Corporate general and administrative—Corporate general and administrative expense for the nine months ended September 30, 2018 and 2017 was \$14.5 million and \$13.8 million, respectively. Included in corporate general and administrative expense for each of the nine months ended September 30, 2018 and 2017 was \$5.7 million of non-cash share-based compensation expense. The increase in corporate general and administrative expense is primarily related to an increase in employee compensation expense and professional service fees.

Interest income—Interest income for the nine months ended September 30, 2018 was \$0.2 million. There was no interest income for the nine months ended September 30, 2017. The increase in interest income was primarily related to an increase in cash and cash equivalents and in short-term interest rates.

Interest expense—Interest expense for the nine months ended September 30, 2018 and 2017 was \$26.2 million and \$25.0 million, respectively. The increase in interest expense was primarily related to the increase in average long-term debt outstanding during the nine months ended September 30, 2018 as compared to the nine months ended September 30, 2017, reflecting the use of debt to fund the redemption of the 7.75% Series A Cumulative Redeemable Preferred Shares in July 2017, offset partially by repayment of debt with the net proceeds from the sales of The Hotel Minneapolis, Autograph Collection in November 2017 and the Hyatt Centric Santa Barbara in July 2018.

Gain on sale of hotel—Gain on sale of hotel for the nine months ended September 30, 2018 was \$33.1 million and related to the sale of the Hyatt Centric Santa Barbara in July 2018.

Income tax expense—Income tax expense for the nine months ended September 30, 2018 and 2017 was \$1.0 million and \$1.5 million, respectively. Income tax expense is directly related to taxable income generated by our TRSs during the period. The decrease in income tax expense was partially related to a decrease in our effective income tax rate resulting from the enactment of the Tax Cuts and Jobs Act in December 2017.

Preferred share dividends—There was no preferred share dividends for the nine months ended September 30, 2018. Preferred share dividends for the nine months ended September 30, 2017 was \$5.3 million. The decrease in preferred share dividends is directly related to the full redemption of the 7.75% Series A Cumulative Redeemable Preferred Shares in July 2017.

Write-off of issuance costs of redeemed preferred shares—Write-off of issuance costs of redeemed preferred shares for the nine months ended September 30, 2017 of \$4.4 million related to the full redemption of the 7.75% Series A Cumulative Redeemable Preferred Shares in July 2017.

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Hotel operating results

We use the term “comparable” to refer to metrics that include only those hotels owned for the entirety of the two periods being compared. As of September 30, 2018, we owned 20 hotels. Since the Hyatt Centric Santa Barbara was sold on July 26, 2018 and The Hotel Minneapolis, Autograph Collection was sold on November 8, 2017, they have been excluded from the comparable hotel portfolio metrics for the three and nine months ended September 30, 2018 and 2017. Included in the following table are comparisons of occupancy, ADR, RevPAR, Adjusted Hotel EBITDAre, and Adjusted Hotel EBITDAre Margin for the comparable 20-hotel portfolio for the three and nine months ended September 30, 2018 and 2017 (in thousands, except for ADR and RevPAR):

| | Three Months Ended | | | Nine Months Ended | | |
|---|--------------------|----------|---------|-------------------|-----------|---------|
| | September 30, | | Change | September 30, | | Change |
| | 2018 | 2017 | | 2018 | 2017 | |
| Comparable Occupancy | 89.7% | 88.3 % | 140 bps | 86.5% | 83.8 % | 270 bps |
| Comparable ADR | \$234.51 | \$226.97 | 3.3% | \$230.09 | \$227.18 | 1.3% |
| Comparable RevPAR | \$210.28 | \$200.33 | 5.0% | \$199.11 | \$190.48 | 4.5% |
| Comparable Adjusted Hotel EBITDAre | \$51,665 | \$49,537 | 4.3% | \$146,245 | \$138,988 | 5.2% |
| Comparable Adjusted Hotel EBITDAre Margin | 33.4% | 33.2 % | 20 bps | 32.8% | 32.1 % | 70 bps |

Non-GAAP Financial Measures

Non-GAAP financial measures are measures of our historical financial performance that are different from measures calculated and presented in accordance with U.S. generally accepted accounting principles. We report the following seven non-GAAP financial measures that we believe are useful to investors as key measures of our operating performance: (1) EBITDAre, (2) Adjusted Corporate EBITDAre, (3) Adjusted Hotel EBITDAre, (4) Adjusted Hotel EBITDAre Margin, (5) Funds from operations (FFO), (6) FFO available to common shareholders, and (7) Adjusted FFO (AFFO) available to common shareholders. Effective January 1, 2018, we report EBITDAre in accordance with standards established by the National Association of Real Estate Investment Trusts (“NAREIT”). Adjusted Corporate EBITDAre, Adjusted Hotel EBITDAre, and Adjusted Hotel EBITDAre Margin are equivalent to our previously reported Adjusted Corporate EBITDA, Adjusted Hotel EBITDA, and Adjusted Hotel EBITDA Margin measures, respectively.

EBITDAre—We calculate EBITDAre in accordance with standards established by NAREIT, which defines EBITDAre as net income (calculated in accordance with GAAP) before interest, income taxes, depreciation and amortization, gains (losses) from sales of real estate, impairment charges of depreciated real estate, and adjustments for unconsolidated partnerships and joint ventures. We believe that EBITDAre provides investors a useful financial measure to evaluate our operating performance, excluding the impact of our capital structure (primarily interest expense) and our asset base (primarily depreciation and amortization).

Adjusted Corporate EBITDAre—We further adjust EBITDAre for certain additional recurring and non-recurring items that are not in NAREIT’s definition of EBITDAre. Specifically, we adjust for hotel acquisition costs and non-cash amortization of intangible assets and liabilities, deferred franchise costs, and deferred key money, all of which are recurring items. We believe that Adjusted Corporate EBITDAre provides investors another financial measure of our operating performance that provides for greater comparability of our core operating results between periods.

Adjusted Hotel EBITDAre—We further adjust Adjusted Corporate EBITDAre for corporate general and administrative expenses, which is a recurring item. We believe that Adjusted Hotel EBITDAre provides investors a useful financial measure to evaluate our hotel operating performance by excluding the impact of corporate-level expenses.

Adjusted Hotel EBITDAre Margin—Adjusted Hotel EBITDAre Margin is defined as Adjusted Hotel EBITDAre as a percentage of total revenues. We believe that Adjusted Hotel EBITDAre Margin provides investors another useful financial measure to evaluate our hotel operating performance.

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The following table reconciles net income to EBITDAre, Adjusted Corporate EBITDAre, Adjusted Hotel EBITDAre, and Adjusted Hotel EBITDAre Margin for the three and nine months ended September 30, 2018 and 2017 (in thousands):

| | Three Months Ended | | Nine Months Ended | | |
|---|--------------------|-----------|-------------------|-----------|---|
| | September 30, | | September 30, | | |
| | 2018 | 2017 | 2018 | 2017 | |
| Net income | \$53,379 | \$18,953 | \$83,738 | \$48,633 | |
| Add: Interest expense | 8,445 | 9,020 | 26,203 | 24,989 | |
| Income tax expense | 758 | 1,590 | 1,017 | 1,470 | |
| Depreciation and amortization | 18,621 | 19,369 | 56,934 | 57,252 | |
| Less: Interest income | (190) | — | (228) | — | |
| Gain on sale of hotel | (33,109) | — | (33,109) | — | |
| EBITDAre | 47,904 | 48,932 | 134,555 | 132,344 | |
| Add: Non-cash amortization ⁽¹⁾ | 54 | (25) | 164 | (76) | |
| Adjusted Corporate EBITDAre | 47,958 | 48,907 | 134,719 | 132,268 | |
| Add: Corporate general and administrative | 4,419 | 4,216 | 14,522 | 13,798 | |
| Adjusted Hotel EBITDAre | 52,377 | 53,123 | 149,241 | 146,066 | |
| Less: Adjusted Hotel EBITDAre of hotels sold ⁽²⁾ | (712) | (3,586) | (2,996) | (7,078) | |
| Comparable Adjusted Hotel EBITDAre | \$51,665 | \$49,537 | \$146,245 | \$138,988 | |
| | | | | | |
| Total revenue | \$156,353 | \$158,277 | \$454,663 | \$455,612 | |
| Less: Total revenue of hotels sold ⁽²⁾ | (1,662) | (9,121) | (9,411) | (22,492) | |
| Comparable total revenue | \$154,691 | \$149,156 | \$445,252 | \$433,120 | |
| | | | | | |
| Comparable Adjusted Hotel EBITDAre Margin | 33.4 | % 33.2 | % 32.8 | % 32.1 | % |

(1) Reflects non-cash amortization of ground lease asset, deferred franchise costs, deferred key money, unfavorable contract liability, and air rights contract.

(2) Reflects results of operations for the Hyatt Centric Santa Barbara, which was sold on July 26, 2018, and The Hotel Minneapolis, Autograph Collection, which was sold on November 8, 2017.

FFO—We calculate FFO in accordance with standards established by NAREIT, which defines FFO as net income (calculated in accordance with GAAP), excluding depreciation and amortization, gains (losses) from sales of real estate, impairment charges of depreciated real estate, adjustments for unconsolidated partnerships and joint ventures, and the cumulative effect of changes in accounting principles. Historical cost accounting for real estate assets implicitly assumes that the value of real estate assets diminishes predictably over time. Since real estate values instead have historically risen or fallen with market conditions, most industry investors consider presentations of operating results for real estate companies that use historical cost accounting to be insufficient by themselves. By excluding the effect of depreciation and amortization and gains (losses) from sales of real estate, both of which are based on historical cost accounting and which may be of lesser significance in evaluating current performance, we believe that FFO provides investors a useful financial measure to evaluate our operating performance.

FFO available to common shareholders—We reduce FFO for preferred share dividends, write-off of issuance costs of redeemed preferred shares, and dividends declared on and earnings allocated to unvested time-based awards (consistent with adjustments required by GAAP in reporting net income available to common shareholders and related per share amounts). FFO available to common shareholders provides investors another financial measure to evaluate our operating performance after taking into account the interests of holders of our preferred shares and unvested time-based awards.

AFFO available to common shareholders—We further adjust FFO available to common shareholders for certain additional recurring and non-recurring items that are not in NAREIT's definition of FFO. Specifically, we adjust for hotel acquisition costs and non-cash amortization of intangible assets and liabilities, deferred franchise costs, and

deferred key money, all of which are recurring items. We believe that AFFO available to common shareholders provides investors another financial measure of our operating performance that provides for greater comparability of our core operating results between periods.

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The following table reconciles net income to FFO, FFO available to common shareholders, and AFFO available to common shareholders for the three and nine months ended September 30, 2018 and 2017 (in thousands, except per share amounts):

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--|--|----------|------------------------------------|-----------|
| | 2018 | 2017 | 2018 | 2017 |
| Net income | \$53,379 | \$18,953 | \$83,738 | \$48,633 |
| Add: Depreciation and amortization | 18,621 | 19,369 | 56,934 | 57,252 |
| Less: Gain on sale of hotel | (33,109) | — | (33,109) | — |
| FFO | 38,891 | 38,322 | 107,563 | 105,885 |
| Less: Preferred share dividends | — | (430) | — | (5,274) |
| Write-off of issuance costs of redeemed preferred shares | — | (4,419) | — | (4,419) |
| Dividends declared on unvested time-based awards | (118) | (124) | (358) | (371) |
| Undistributed earnings allocated to unvested time-based awards | (147) | — | (63) | — |
| FFO available to common shareholders | 38,626 | 33,349 | 107,142 | 95,821 |
| Add: Write-off of issuance costs of redeemed preferred shares | — | 4,419 | — | 4,419 |
| Non-cash amortization ⁽¹⁾ | 54 | (25) | 164 | (76) |
| AFFO available to common shareholders | \$38,680 | \$37,743 | \$107,306 | \$100,164 |
| FFO available per common share: | | | | |
| Basic | \$0.65 | \$0.56 | \$1.81 | \$1.62 |
| Diluted | \$0.65 | \$0.56 | \$1.79 | \$1.62 |
| AFFO available per common share: | | | | |
| Basic | \$0.65 | \$0.64 | \$1.81 | \$1.70 |
| Diluted | \$0.65 | \$0.64 | \$1.79 | \$1.69 |

⁽¹⁾ Reflects non-cash amortization of ground lease asset, deferred franchise costs, deferred key money, unfavorable contract liability, and air rights contract.

None of EBITDAre, Adjusted Corporate EBITDAre, Adjusted Hotel EBITDAre, Adjusted Hotel EBITDAre Margin, FFO, FFO available to common shareholders, or AFFO available to common shareholders represent cash generated from operating activities as determined by GAAP, nor shall any of these measures be considered as an alternative to GAAP net income (loss), as an indication of our financial performance, or to GAAP cash flow from operating activities, as a measure of liquidity. In addition, EBITDAre, Adjusted Corporate EBITDAre, Adjusted Hotel EBITDAre, Adjusted Hotel EBITDAre Margin, FFO, FFO available to common shareholders, and AFFO available to common shareholders are not indicative of funds available to fund cash needs, including the ability to make cash distributions.

Sources and Uses of Cash

For the nine months ended September 30, 2018, net cash flows from operating activities were \$112.7 million; net cash flows provided by investing activities were \$59.8 million, including proceeds of \$89.8 million from the disposition of the Hyatt Centric Santa Barbara, offset partially by \$30.1 million for improvements and additions to our hotels; and net cash flows used in financing activities were \$148.6 million, including \$71.3 million in dividend payments to common shareholders, a net repayment of \$65.0 million under our revolving credit facility, and \$9.6 million in scheduled principal payments on mortgage debt. As of September 30, 2018, we had cash and cash equivalents of \$68.9 million and restricted cash of \$29.9 million.

Liquidity and Capital Resources

We expect our primary source of cash to meet operating requirements, including payment of dividends in accordance with the REIT requirements of the U.S. federal income tax laws, payment of interest on any borrowings and funding of any capital expenditures, will be from our hotels' results of operations and existing cash and cash equivalent balances. We currently expect that our operating cash flows will be sufficient to fund our continuing operations. We also expect to use existing restricted cash balances and borrowings under our revolving credit facility to partially fund any capital expenditures. We intend to incur indebtedness to supplement our investment capital and to maintain flexibility to respond to industry conditions and opportunities. We are targeting an overall debt level not to exceed 40% of the aggregate value of all of our hotels, as calculated in accordance with our revolving credit facility; as of September 30, 2018, our overall debt level was 33.9% under this calculation.

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We expect to meet long-term liquidity requirements, such as new hotel acquisitions and scheduled debt maturities, through additional secured and unsecured borrowings and the issuance of equity securities. Our ability to raise funds through the issuance of equity securities depends on, among other things, general market conditions for hotel companies and REITs and market perceptions about us. We will continue to analyze alternative sources of capital in an effort to minimize our capital costs and maximize our financial flexibility.

We expect to continue declaring distributions to shareholders, as required to maintain our REIT status, although no assurances can be made that we will continue to generate sufficient income to distribute similar aggregate amounts in the future. The per share amounts of future distributions will depend on the number of our common and preferred shares outstanding from time to time and will be determined by our board of trustees following its periodic review of our financial performance and capital requirements, and the terms of our existing borrowing arrangements.

As of the date of this filing, we have approximately \$55.0 million of cash and cash equivalents, approximately \$30.0 million of restricted cash, and \$300.0 million available to borrow under our revolving credit facility. See Note 6, "Long-Term Debt," to our interim consolidated financial statements for additional information relating to our revolving credit facility and other long-term debt.

Capital Expenditures

We maintain each hotel in good repair and condition and in conformity with applicable laws and regulations and in accordance with the franchisor's standards and the agreed-upon requirements in our management and loan agreements. The cost of all such routine improvements and alterations will be paid out of FF&E reserves, which will be funded by a portion of each hotel's gross revenues. Routine capital expenditures will be administered by the management companies. However, we will have approval rights over the capital expenditures as part of the annual budget process. From time to time, certain of our hotels may be undergoing renovations as a result of our decision to upgrade portions of the hotels, such as guestrooms, meeting space, and/or restaurants, in order to better compete with other hotels in our markets. As of September 30, 2018, none of our hotels were undergoing comprehensive renovations. In addition, often after we acquire a hotel, we are required to complete a PIP in order to bring the hotel up to the respective franchisor's standards. If permitted by the terms of the management agreement, funding for a renovation will first come from the FF&E reserve. To the extent that the FF&E reserve is not adequate to cover the cost of the renovation, we will fund the remaining portion of the renovation with cash and cash equivalents or available borrowings under our revolving credit facility.

Contractual Obligations

The following table sets forth our contractual obligations as of September 30, 2018, and the effect such obligations are expected to have on our liquidity and cash flow in future periods (in thousands). There were no other material off-balance sheet arrangements at September 30, 2018.

| Contractual Obligations | Payments Due by Period | | | | |
|--|------------------------|--------------------|--------------------|---------------------|----------------------|
| | Total | Less Than One Year | One to Three Years | Three to Five Years | More Than Five Years |
| Revolving credit facility, including interest ⁽¹⁾ | \$— | \$— | \$— | \$— | \$— |
| Term loan, including interest ⁽¹⁾ | 253,358 | 7,788 | 15,598 | 229,972 | — |
| Secured loans, including interest | 641,589 | 35,772 | 183,912 | 197,480 | 224,425 |
| Corporate office lease | 1,146 | 294 | 614 | 238 | — |
| Ground leases ⁽²⁾ | 202,412 | 4,101 | 8,201 | 8,221 | 181,889 |
| | \$1,098,505 | \$47,955 | \$208,325 | \$435,911 | \$406,314 |

Assumes no additional borrowings and interest payments are based on the interest rate in effect at September 30, (1)2018. Also assumes that no extension options, if any, are exercised. See Note 6, "Long-Term Debt," to our interim consolidated financial statements for additional information relating to our revolving credit facility and term loan.

(2)

The ground leases for the Hyatt Regency Mission Bay Spa and Marina and the JW Marriott San Francisco Union Square provide for the greater of base or percentage rent, subject to potential increases over the term of the leases. Amounts assume only base rent for all periods presented and do not assume any adjustments for potential increases.

Inflation

Operators of hotels, in general, possess the ability to adjust room rates daily to reflect the effects of inflation. However, competitive pressures may limit the ability of our management companies to raise room rates.

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Seasonality

Demand in the lodging industry is affected by recurring seasonal patterns. For non-resort properties, demand is generally lower in the winter months due to decreased travel and higher in the spring and summer months during the peak travel season. For resort properties, demand is generally higher in the winter months. We expect that our operations will generally reflect non-resort seasonality patterns. Accordingly, we expect that we will have lower revenue, operating income and cash flow in the first and fourth quarters and higher revenue, operating income and cash flow in the second and third quarters. These general trends are, however, expected to be greatly influenced by overall economic cycles.

Critical Accounting Policies

Our interim consolidated financial statements have been prepared in conformity with GAAP, which requires management to make estimates and assumptions that affect the reported amount of assets and liabilities at the date of our interim consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. While we do not believe the reported amounts would be materially different, application of these policies involves the exercise of judgment and the use of assumptions as to future uncertainties and, as a result, actual results could differ from these estimates. We evaluate our estimates and judgments on an ongoing basis. We base our estimates on experience and on various other assumptions that are believed to be reasonable under the circumstances. All of our critical accounting policies are disclosed in our Form 10-K for the year ended December 31, 2017.

Recent Accounting Pronouncements

See Note 2, "Summary of Significant Accounting Policies," to our interim consolidated financial statements for additional information relating to recent accounting pronouncements, if any.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

We earn interest income primarily from cash and cash equivalent balances. Based on our cash and cash equivalents as of September 30, 2018, if interest rates increase or decrease by 1.00%, our interest income will increase or decrease by approximately \$0.7 million annually.

Amounts borrowed under our revolving credit facility currently bear interest at variable rates based on LIBOR plus 1.45% - 2.20% (the spread over LIBOR based on our consolidated leverage ratio). If prevailing LIBOR on any outstanding borrowings under our revolving credit facility were to increase or decrease, our interest expense on those outstanding borrowings would increase or decrease future earnings and cash flows. As of September 30, 2018, we had no outstanding borrowings under our revolving credit facility.

Item 4. Controls and Procedures

The Chief Executive Officer and Chief Financial Officer of the Trust have evaluated the effectiveness of the disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")), as required by paragraph (b) of Rules 13a-15 and 15d-15 under the Exchange Act, and have concluded that as of the end of the period covered by this report, the Trust's disclosure controls and procedures were effective at a reasonable assurance level.

There was no change in the Trust's internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Rules 13a-15 and 15d-15 under the Exchange Act during the Trust's most recent fiscal quarter that materially affected, or is reasonably likely to materially affect, the Trust's internal control over financial reporting.

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PART II

Item 1. Legal Proceedings

We are not involved in any material litigation nor, to our knowledge, is any material litigation threatened against us.

Item 1A. Risk Factors

There have been no material changes from the risk factors disclosed under the caption "Risk Factors" in the Trust's Form 10-K for the year ended December 31, 2017.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Not applicable.

Item 3. Defaults Upon Senior Securities

Not applicable.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

The following exhibits are filed as part of this Form 10-Q:

Exhibit Number Description of Exhibit

31.1 Rule 13a-14(a)/15d-14(a) Certification of President and Chief Executive Officer

31.2 Rule 13a-14(a)/15d-14(a) Certification of Executive Vice President and Chief Financial Officer

32.1 Section 1350 Certification of President and Chief Executive Officer

32.2 Section 1350 Certification of Executive Vice President and Chief Financial Officer

101.INS XBRL Instance Document

101.SCH XBRL Taxonomy Extension Schema Document

101.CAL XBRL Taxonomy Extension Calculation Linkbase Document

101.DEF XBRL Taxonomy Extension Definition Linkbase Document

101.LAB XBRL Taxonomy Extension Label Linkbase Document

101.PRE XBRL Taxonomy Extension Presentation Linkbase Document

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SIGNATURES

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

CHESAPEAKE LODGING TRUST

Date: November 1, 2018 By: /S/ DOUGLAS W. VICARI

Douglas W. Vicari

Executive Vice President and Chief Financial Officer

(Principal Financial Officer)

/S/ GRAHAM J. WOOTTEN

Graham J. Wootten

Senior Vice President and Chief Accounting Officer (Principal Accounting Officer)