

NexPoint Residential Trust, Inc.
Form 10-K
February 19, 2019

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington D.C. 20549

FORM 10-K

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 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 001-36663

NexPoint Residential Trust, Inc.

(Exact Name of Registrant as Specified in Its Charter)

Maryland 47-1881359
(State or other Jurisdiction of (I.R.S. Employer
Incorporation or Organization) Identification No.)

300 Crescent Court, Suite 700, Dallas, Texas 75201
(Address of Principal Executive Offices) (Zip Code)

(972) 628-4100

(Telephone Number, Including Area Code)

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Securities registered pursuant to Section 12(b) of the Securities Exchange Act of 1934:

Title of each class	Name of each exchange on which registered
Common Stock, par value \$0.01 per share	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Securities Exchange Act of 1934:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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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The aggregate market value of the shares of common stock of the registrant held by non-affiliates of the registrant, based upon the closing price of such shares on June 29, 2018, was approximately \$459,930,000.

As of February 15, 2019, the registrant had 23,575,826 shares of its common stock, par value \$0.01 per share, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the proxy statement for the registrant's 2019 Annual Meeting of Stockholders are incorporated by reference in Part III of this Form 10-K.

NEXPOINT RESIDENTIAL TRUST, INC.

Form 10-K

Year Ended December 31, 2018

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Cautionary Statement Regarding Forward-Looking Statements

This annual report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 that are subject to risks and uncertainties. In particular, statements relating to our liquidity and capital resources, the performance of our properties and results of operations contain forward-looking statements. Furthermore, all of the statements regarding future financial performance (including market conditions and demographics) are forward-looking statements. We caution investors that any forward-looking statements presented in this annual report are based on management's current beliefs and assumptions made by, and information currently available to, management. When used, the words "anticipate," "believe," "expect," "intend," "may," "might," "plan," "estimate," "project," "should," "will," "would," "result" and similar expressions that do not relate solely to historical matters are intended to identify forward-looking statements. You can also identify forward-looking statements by discussions of strategy, plans or intentions.

Forward-looking statements are subject to risks, uncertainties and assumptions and may be affected by known and unknown risks, trends, uncertainties and factors that are beyond our control. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those anticipated, estimated or projected. We caution you therefore against relying on any of these forward-looking statements.

Some of the risks and uncertainties that may cause our actual results, performance, liquidity or achievements to differ materially from those expressed or implied by forward-looking statements include, among others, the following:

- unfavorable changes in market and economic conditions in the United States and globally and in the specific markets where our properties are located;
- risks associated with ownership of real estate;
- limited ability to dispose of assets because of the relative illiquidity of real estate investments;
- our multifamily properties are concentrated in certain geographic markets in the Southeastern and Southwestern United States, which makes us more susceptible to adverse developments in those markets;
- increased risks associated with our strategy of acquiring value-enhancement multifamily properties rather than more conservative investment strategies;
- potential reforms to the Federal Home Loan Mortgage Corporation ("Freddie Mac") and the Federal National Mortgage Association ("Fannie Mae");
- competition could limit our ability to acquire attractive investment opportunities, which could adversely affect our profitability and impede our growth;
- competition and any increased affordability of residential homes could limit our ability to lease our apartments or increase or maintain rents;
- the relatively low residential mortgage rates may result in potential renters purchasing residences rather than leasing them, and as a result, cause a decline in our occupancy rates;
- the risk that we may fail to consummate future property acquisitions;
- failure of acquisitions to yield anticipated results;
- risks associated with increases in interest rates and our ability to issue additional debt or equity securities in the future;
- risks associated with selling apartment communities, which could limit our operational and financial flexibility;
 - contingent or unknown liabilities related to properties or businesses that we have acquired or may acquire;
 - lack of or insufficient amounts of insurance;
- the risk that our environmental assessments may not identify all potential environmental liabilities and our remediation actions may be insufficient;

- high costs associated with the investigation or remediation of environmental contamination, including asbestos, lead-based paint, chemical vapor, subsurface contamination and mold growth;
- high costs associated with the compliance with various accessibility, environmental, building and health and safety laws and regulations, such as the Americans with Disabilities Act of 1990 (the “ADA”) and the Fair Housing Act (the “FHA”);
- risks associated with limited warranties we may obtain when purchasing properties;

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• exposure to decreases in market rents due to our short-term leases;

• risks associated with operating through joint ventures and funds;

• our dependence on information systems;

• risks associated with breaches of our data security;

• risks associated with our reduced public company reporting requirements as an “emerging growth company”;

• costs associated with being a public company, including compliance with securities laws;

• the risk that our business could be adversely impacted if there are deficiencies in our disclosure controls and procedures or internal control over financial reporting;

• risks associated with our substantial current indebtedness and indebtedness we may incur in the future;

• risks associated with derivatives or hedging activity;

• the relative lack of experience of NexPoint Real Estate Advisors, L.P. (our “Adviser”) and property manager in operating under the constraints imposed on us as a real estate investment trust (“REIT”) may hinder the achievement of our investment objectives;

• loss of key personnel of Highland Capital Management, L.P. (our “Sponsor” or “Highland”), our Adviser and our property manager;

• the risk that we may not replicate the historical results achieved by other entities managed or sponsored by affiliates of our Adviser, members of our Adviser’s management team or by our Sponsor or its affiliates;

• risks associated with our Adviser’s ability to terminate the Advisory Agreement (as defined below);

• our ability to change our major policies, operations and targeted investments without stockholder consent;

• the substantial fees and expenses we pay to our Adviser and its affiliates;

• risks associated with any potential internalization of our management functions;

• conflicts of interest and competing demands for time faced by our Adviser, our Sponsor and their officers and employees;

• the risk that we may compete with other entities affiliated with our Sponsor or property manager for properties and tenants;

• failure to maintain our status as a REIT;

• failure of our operating partnership to be taxable as a partnership for federal income tax purposes, possibly causing us to fail to qualify for or to maintain REIT status;

• compliance with REIT requirements, which may limit our ability to hedge our liabilities effectively and cause us to forgo otherwise attractive opportunities, liquidate certain of our investments or incur tax liabilities;

• risks associated with our ownership of interests in taxable REIT subsidiaries;

• the recognition of taxable gains from the sale of properties as a result of the inability to complete certain like-kind exchanges (“1031 Exchanges”) in accordance with Section 1031 of the Internal Revenue Code of 1986, as amended (the “Code”);

• the risk that the Internal Revenue Service (the “IRS”) may consider certain sales of properties to be prohibited transactions, resulting in a 100% penalty tax on any taxable gain;

• the ineligibility of dividends payable by REITs for the reduced tax rates available for some dividends;

• risks associated with the stock ownership restrictions of the Code for REITs and the stock ownership limit imposed by our charter;

• the ability of our board of directors (the “Board”) to revoke our REIT qualification without stockholder approval;

• recent and potential legislative or regulatory tax changes or other actions affecting REITs;

• risks associated with the market for our common stock and the general volatility of the capital and credit markets;

• failure to generate sufficient cash flows to service our outstanding indebtedness or pay distributions at expected levels;

risks associated with limitations of liability for and our indemnification of our directors and officers; and any other risks included under the heading “Risk Factors” in this annual report.

While forward-looking statements reflect our good faith beliefs, they are not guarantees of future performance. They are based on estimates and assumptions only as of the date of this annual report. We undertake no obligation to update or revise any forward-looking statement to reflect changes in underlying assumptions or factors, new information, data or methods, future events or other changes, except as required by law.

PART I

ITEM 1. BUSINESS

General

NexPoint Residential Trust, Inc. (the “Company”, “we”, “our”) was incorporated in Maryland on September 19, 2014, and has elected to be taxed as a REIT. The Company is focused on “value-add” multifamily investments primarily located in the Southeastern and Southwestern United States. Substantially all of the Company’s business is conducted through NexPoint Residential Trust Operating Partnership, L.P. (the “OP”), the Company’s operating partnership. The Company owns its properties (the “Portfolio”) through the OP and its wholly owned taxable REIT subsidiary (“TRS”). The OP owns approximately 99.9% of the Portfolio; the TRS owns approximately 0.1% of the Portfolio. The Company’s wholly owned subsidiary, NexPoint Residential Trust Operating Partnership GP, LLC (the “OP GP”), is the sole general partner of the OP. As of December 31, 2018, there were 23,819,402 common units in the OP (“OP Units”) outstanding, of which 23,746,169, or 99.7%, were owned by the Company and 73,233, or 0.3%, were owned by a noncontrolling limited partner (see Note 10 to our consolidated financial statements).

The Company began operations on March 31, 2015 as a result of the transfer and contribution by NexPoint Strategic Opportunities Fund (fka NexPoint Credit Strategies Fund) (“NHF”) of all but one of the multifamily properties owned by NHF through its wholly owned subsidiary NexPoint Real Estate Opportunities, LLC (fka Freedom REIT, LLC) (“NREO”). We use the term “predecessor” to mean the carve-out business of NREO. On March 31, 2015, NHF distributed all of the outstanding shares of the Company’s common stock held by NHF to holders of NHF common shares. We refer to the distribution of our common stock by NHF as the “Spin-Off.”

The Company is externally managed by the Adviser through an agreement dated March 16, 2015, as amended, and renewed on February 13, 2019 for a one-year term set to expire on March 16, 2020 (the “Advisory Agreement”), by and among the Company, the OP and the Adviser. The Adviser conducts substantially all of the Company’s operations and provides asset management services for its real estate investments. The Company expects it will only have accounting employees while the Advisory Agreement is in effect. All of the Company’s investment decisions are made by the Adviser, subject to general oversight by the Adviser’s investment committee and the Board. The Adviser is wholly owned by NexPoint Advisors, L.P., which is an affiliate of the Sponsor.

The Company’s investment objectives are to maximize the cash flow and value of properties owned, acquire properties with cash flow growth potential, provide quarterly cash distributions and achieve long-term capital appreciation for its stockholders through targeted management and a value-add program. Consistent with the Company’s policy to acquire assets for both income and capital gain, the Company intends to hold at least majority interests in its properties for long-term appreciation and to engage in the business of directly or indirectly acquiring, owning, and operating well-located multifamily properties with a value-add component in large cities and suburban submarkets of large cities primarily in the Southeastern and Southwestern United States consistent with its investment objectives. Economic and market conditions may influence the Company to hold properties for different periods of time. From time to time, the Company may sell a property if, among other deciding factors, the sale would be in the best interest of its stockholders.

The entities through which we own the properties in the Portfolio have entered into management agreements with BH Management Services, LLC (“BH”). Pursuant to these agreements, BH operates and leases the underlying properties in the Portfolio and provides construction management services. BH has significant experience operating and leasing multifamily properties, having begun business in 1993 and currently operating and leasing approximately 90,000 multifamily units across the country. The Company pays BH a management fee of approximately 3% of the monthly gross income from each property managed, as well as construction supervision fees and certain other fees. BH is an

affiliate of the noncontrolling limited partner of the OP. See Notes 10 and 11 to our consolidated financial statements for additional information.

The Company may also participate with third parties in property ownership through limited liability companies (“LLCs”), funds or other types of co-ownership or acquire real estate or interests in real estate in exchange for the issuance of common stock, OP Units, preferred stock or options to purchase stock. These types of investments may permit the Company to own interests in larger assets without unduly restricting diversification, which provides flexibility in structuring the Company’s portfolio.

The Company may allocate up to 30% of the portfolio to investments in real estate-related debt and securities with the potential for high current income or total returns. These allocations may include first and second mortgages and subordinated, bridge, mezzanine, construction and other loans, as well as debt securities related to or secured by multifamily real estate and common and preferred equity securities, which may include securities of other REITs or real estate companies.

As of December 31, 2018, the Company, through the OP and the wholly owned TRS, owned 35 properties representing 12,555 units in seven states, as further described under Item 2, “Properties” and Notes 3, 4 and 5 to our consolidated financial statements.

2018 Highlights

Key highlights and transactions completed in 2018 include the following:

2018 Offering: On November 14, 2018, we issued 2,702,500 shares of common stock, par value \$0.01 per share, at a public offering price of \$33.00 per share (before underwriters' discounts and offering costs) for gross proceeds of approximately \$89.2 million (the "2018 Offering"). We contributed the net proceeds from the 2018 Offering to the OP in exchange for 2,702,500 OP Units, and the OP in turn used a majority of the net proceeds to repay the \$50.0 million outstanding under a credit facility with KeyBank National Association ("KeyBank") (the "\$60 Million Credit Facility") and the \$30.0 million outstanding under a bridge facility with KeyBank (the "\$30 Million Bridge Facility"). The following table contains summary information of the 2018 Offering:

Gross proceeds	\$89,182,500
Common shares sold (1)	2,702,500
Public offering price per share	\$33.00
Offering costs	876,800
Underwriters' discounts	3,523,500
Net proceeds	84,782,200
Average price per share	\$31.37

(1) Affiliates of our Adviser purchased 207,971 shares in the 2018 Offering. No underwriters' discount applied to the purchase of such shares.

Acquisitions: We completed three acquisitions, which increased our presence in two markets. Details of the acquisitions are in the table below (dollars in thousands):

Property Name	Location	Date of Acquisition	Purchase Price	Mortgage Debt (1)	# Units	Effective Ownership
Cedar Pointe	Antioch, Tennessee	August 24, 2018	\$26,500	\$17,300	210	100 %
Crestmont Reserve	Dallas, Texas	September 26, 2018	24,680	12,061	242	100 %
Brandywine I & II (2)	Nashville, Tennessee	September 26, 2018	79,800	43,835	632	100 %
			\$130,980	\$73,196	1,084	

(1) For additional information regarding our debt, see Note 6 to our consolidated financial statements.

(2) Brandywine I & II are two separate properties that we combined and operate as a single property.

Disposition: We sold one property totaling 304 units. Details of the disposition are in the table below (in thousands):

Property Name	Location	Date of Sale	Sales Price	Outstanding Principal (1)	Net Cash Proceeds (2)	Gain on Sale of Real Estate
Timberglen	(3) Dallas, Texas	January 31, 2018	\$30,000	\$17,226	\$29,553	\$13,742

(1) Represents the outstanding principal balance when the loan was repaid.

(2) Represents sales price, net of closing costs.

(3)

We completed the reverse portion of the 1031 Exchange of Atera Apartments with the sale of Timberglen, at which time legal title to Atera Apartments transferred to us.

Renovations: For the properties in our Portfolio as of December 31, 2018, we completed full and partial renovations on 1,432 units at an average cost of \$4,703 per renovated unit. Since inception, for the properties in our Portfolio as of December 31, 2018, we have completed full and partial renovations on 5,661 units at an average cost of \$4,909 per renovated unit that has been leased as of December 31, 2018. We have achieved average rent growth of 10.6%, or a \$93 average monthly rental increase per unit, on all units renovated and leased as of December 31, 2018, resulting in a return on investment on capital expended for interior renovations of 22.7%.

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Dividends: We declared dividends totaling \$22.6 million, or \$1.025 per share. During the fourth quarter of 2018, we increased our quarterly dividend for the third time since the Spin-Off to \$0.275 per share, which was an increase of \$0.025 per share, or a 10.0% increase, over our previous quarterly dividends declared in 2018. The increase in our quarterly dividend to \$0.275 per share is an increase of \$0.069 per share, or a 33.5% increase, over our historical quarterly dividends declared since the Spin-Off through the third quarter of 2016. Our fourth quarter dividend equates to a 3.1% annualized yield based on our closing share price of \$35.05 on December 31, 2018.

Results of Operations and Non-GAAP Measures: We reported the following increases (decreases) in net income (loss), net operating income (“NOI”), funds from operations (“FFO”), core funds from operations (“Core FFO”) and adjusted funds from operations (“AFFO”) for the year ended December 31, 2018 as compared to the year ended December 31, 2017 (dollars in thousands):

	For the Year Ended December 31,			
	2018	2017	\$ Change	% Change
Net income (loss)	\$(1,614)	\$56,359	\$(57,973)	(1) -102.9 %
NOI	(2) 80,175	76,578	3,597	4.7 %
FFO attributable to common stockholders	(2) 32,018	25,051	6,967	27.8 %
Core FFO attributable to common stockholders	(2) 35,081	30,147	4,934	16.4 %
AFFO attributable to common stockholders	(2) 40,753	34,772	5,981	17.2 %

(1) The change in our net income (loss) between the periods primarily relates to a decrease in gain on sales of real estate of \$64.6 million, and was partially offset by an increase in total revenues of \$2.4 million and decreases in total property operating expenses of \$1.4 million, depreciation and amortization expense of \$1.3 million and loss on extinguishment of debt and modification costs of \$2.1 million.

(2) See Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations” for a discussion regarding the non-GAAP measures of NOI, FFO, Core FFO and AFFO provided above, including reconciliations to net income (loss) in accordance with U.S. generally accepted accounting principles (“GAAP”).

Same Store Growth: There are 29 properties encompassing 10,123 units of apartment space in our same store pool for the years ended December 31, 2018 and 2017 (our “2017-2018 Same Store” properties). For our 2017-2018 Same Store properties, we recorded the following operating metrics for the year ended December 31, 2018 as compared to the year ended December 31, 2017:

Operating Metric	2018	2017	% Change
Occupancy	(1) 94.5 %	93.9 %	0.6 %
Average Effective Monthly Rent Per Unit	(2) \$963	\$925	4.1 %
Rental income (in thousands)	\$107,312	\$102,643	4.5 %
Other income (in thousands)	\$16,273	\$15,827	2.8 %

(1) Occupancy is calculated as the number of units occupied as of December 31 for the respective year, divided by the total number of units, expressed as a percentage.

(2) Average effective monthly rent per unit is equal to the average of the contractual rent for commenced leases as of December 31 for the respective year minus any tenant concessions over the term of the lease, divided by the number of units under commenced leases as of December 31 for the respective year.

Cash Position: At December 31, 2018, we had \$43.1 million of cash on our balance sheet, of which \$2.0 million was reserved for future renovations, \$3.2 million for green improvements (see Note 6 to our consolidated financial statements) and \$18.1 million for lender required escrows and security deposits. We believe we have adequate cash on

hand, in addition to our expected excess cash flows from operations, to meet our near term obligations, service our debt, pay distributions and make opportunistic acquisitions.

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Refinancings: We refinanced mortgages on seven properties, as detailed in the table below (dollars in thousands). See Note 6 to our consolidated financial statements for additional information.

Property Name	Date of Refinance	Accounting Treatment	Write-off	Prepayment		Debt		Reduction in Spread (in basis points)
			Deferred Financing Costs (1)	Capitalized Deferred Financing Costs (3)	Penalties and Defeasance Costs (1)	Modification and Other Extinguishments Costs (1)		
Belmont at Duck Creek	6/1/2018	Extinguishment	\$ —	(3)\$ 293	\$ —	\$ —	79	(4)
Sabal Palm at Lake Buena Vista	8/20/2018	Extinguishment	228	442	371	—	51	
Abbingtion Heights	8/21/2018	Extinguishment	—	105	446	202	4	(4)
Beechwood Terrace	8/31/2018	Extinguishment	405	100	202	196	24	
Timber Creek	9/28/2018	Extinguishment	151	296	191	—	56	
Radbourne Lake	9/28/2018	Extinguishment	144	266	189	—	52	
Hollister Place	9/28/2018	Modification	—	141	135	87	90	
			\$ 928	\$ 1,643	\$ 1,534	\$ 485	50	(5)

(1) Included in loss on extinguishment of debt and modification costs on the accompanying consolidated statements of operations and comprehensive income.

(2) For previous floating rate mortgages, represents the reduction in the borrowing spread from the previous mortgage to the current mortgage. For previous fixed-rate mortgages, represents the reduction in the borrowing rate from the previous mortgage to the current mortgage (using one-month LIBOR as of December 31, 2018).

(3) There were no existing deferred financing costs related to the prior fixed rate mortgage. We wrote-off the unamortized fair market value adjustment as of June 1, 2018, a premium of less than \$0.1 million, related to the prior fixed rate mortgage, which is recorded in loss on extinguishment of debt and modification costs on the accompanying consolidated statements of operations and comprehensive income.

(4) Previous mortgage was an assumed fixed-rate loan.

(5) Represents the weighted average reduction in the borrowing spreads.

Our Real Estate Portfolio

As of December 31, 2018, we owned 35 properties representing 12,555 units in seven states that were approximately 94.6% occupied with a weighted average monthly effective rent per occupied apartment unit of \$985. For additional information regarding our Portfolio, see Item 2, "Properties" and Notes 3, 4 and 5 to our consolidated financial statements.

We evaluate our operating performance on an individual property level and view our real estate assets as one industry segment and, accordingly, our properties are aggregated into one reportable segment.

Our Business Objectives and Strategies

Our primary business objectives are to:

- deliver stable, attractive yields and long-term capital appreciation to our stockholders;
- acquire multifamily properties in markets with attractive job growth and household formation fundamentals primarily in the Southeastern and Southwestern United States;
- acquire assets at discounts to replacement cost;

implement a value-add program to increase returns to our stockholders;
own assets that provide lifestyle amenities and upgraded living spaces to low and moderate income renters; and
recycle capital from dispositions when economic and market conditions present opportunities that we believe are in the best interest of our stockholders.

We intend to accomplish these objectives by:

Focusing on Acquiring Class B Properties in Our Core Markets. We will continue to seek opportunities to acquire primarily Class B multifamily properties at prices that we believe represent discounts to replacement cost, provide the potential for significant long-term value appreciation and that we expect will generate attractive yields for our stockholders. We will focus on these types of opportunities in our core markets, which we consider to be primarily major metropolitan areas in the Southeastern and Southwestern United States.

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Focusing on Multifamily Properties with a Value-Add Component. We will continue to seek opportunities to acquire multifamily properties that have a value-add component. Due to a lack of reinvestment by many prior owners, we believe these types of properties provide us the opportunity to make relatively modest capital expenditures that result in a significant increase in rents, thereby generating NOI growth, and thus higher yields and capital appreciation for our stockholders.

Prudently Using Leverage to Increase Stockholder Value. We will typically finance new property acquisitions at a target leverage level of approximately 50-60% loan-to-value (outstanding principal balance to enterprise value). Given that we intend for the majority of our acquisitions to have a value-add component in the first three years of ownership, we will generally seek leverage with the optionality to refinance (such as floating rate debt). In the management team's experience, this leverage strategy allows for the opportunity to maximize returns for our stockholders while providing maximum flexibility. We are currently targeting to reduce our leverage to 40-45% loan-to-value (outstanding principal balance to enterprise value) over time by increasing the value of our properties, refinancing properties we intend to hold longer term and strategically paying down debt with excess cash flows from operations or future equity offerings.

Our Adviser's investment approach combines its management team's experience with a structure that emphasizes thorough market research, local market knowledge, underwriting discipline and risk management in evaluating potential investments with a goal of maximizing long-term stockholder value and a philosophy of thoughtful capital allocation and balance sheet management.

Acquisition and Operating Strategy

We seek primarily Class B multifamily properties that are priced at a discount to replacement cost. We believe that through the implementation of our value-add program we will be able to grow the NOI of these types of properties significantly in the first three years of ownership and thus these types of acquisitions will be accretive over the long-term to our FFO, Core FFO and AFFO. As we progress through the real estate life cycle, these opportunities will become more difficult to find. However, we will continue to take a disciplined approach to acquisitions by primarily pursuing these types of opportunities. Our Adviser's investment approach includes active management of each property acquired. Our Adviser believes that active management is critical to creating value. Prior to the purchase of a property, BH and our Adviser generally tour each property and develop a business strategy for the property. This includes a forecast of the action items to be taken and the capital needed to achieve the anticipated returns. Our Adviser reviews such property-level business strategies on an ongoing basis to anticipate changes or opportunities in the market. In an effort to keep properties in compliance with our underwriting standards and management strategies, our Adviser remains involved throughout the investment life cycle of each acquired property and actively consults with BH throughout the holding period.

We may also allocate up to 30% of our Portfolio to investments in real estate-related debt, mezzanine and other loans and preferred equity and other securities in situations where the risk-return profile is more attractive than investments in common equity. This strategy would be focused on the multifamily property type and would be designed to minimize potential losses during market downturns and maximize risk adjusted total returns to our stockholders in all market cycles.

Value-Add Strategy

We will continue to implement our value-add strategy at our properties where we believe we can achieve a significant increase in rents above what would otherwise be the case with purely organic market increases. Our value-add program has three components: 1) improvement of exteriors and common areas, 2) improvement of interiors and 3) management and cost improvements.

We invest in exterior and common areas improvements at our properties in an effort to enhance asset quality, to improve “curb appeal”/market positioning, and expand or enhance our amenity offerings, all of which we believe will improve tenant retention and modestly drive rent and NOI growth. Renovations to the exteriors and common areas include structural improvements that enhance the physical condition, value and/or useful life of our properties, as well as aesthetic improvements to, among others, landscape and signage. We also seek to improve our competitive positioning by adding to, redecorating or otherwise enhancing our common areas and amenity offerings. As of December 31, 2018, with the exception of the properties we acquired in 2018, we have renovated the exteriors and common areas at a majority of the properties in our Portfolio.

We expect interior renovations, along with organic growth in rents, to be the primary drivers of rent and NOI growth at our properties. Our interior renovations include: 1) aesthetic design enhancements such as kitchen and/or bath remodeling, 2) replacement of outdated appliances, equipment and fixtures, 3) addition of washer/dryer appliances, 4) private yards and 5) smart technologies such as Bluetooth locks, networked climate control systems and USB electrical outlets. We also seek to achieve cost improvements through investment in longer-lived materials, energy conservation projects, and other strategic initiatives. For the properties in our Portfolio as of December 31, 2018, we have completed full and partial renovations on 5,661 units out of our 12,555 total units with an average monthly rental increase per unit of \$93 and an average cost of \$4,909 per renovated unit that has been leased as of December 31, 2018. In cases where we believe rents will grow significantly in a market organically, we will implement the value-add program

more strategically in order to capture significant rent and NOI growth without expending additional capital. Additionally, to the extent we believe rents at a property are maximized regardless of the level of additional renovations, we may opt not to further renovate units at that property. As of December 31, 2018, we had reserved approximately \$2.0 million for our planned capital expenditures and other expenses to implement our value-add program, which will complete approximately 325 planned interior rehabs, eliminating the need for us to raise additional capital in order to carry out our currently planned value-add program.

Disposition Strategy

In general, we intend to hold our multifamily properties for production of rental income for a period of at least three years from the date of acquisition. Economic and market conditions may influence us to hold our investments for different periods of time. From time to time, we may sell an asset before the end of the expected holding period, particularly if we receive a bona fide unsolicited offer with attractive terms, have an upcoming liquidity need, such as a debt maturing, are strategically exiting a certain market or sub-market or the sale of the asset would otherwise be in the best interest of our stockholders. When reviewing whether a sale is in the best interest of our stockholders, we take into consideration whether market conditions and asset positioning have maximized the value of the property to us and any potential adverse tax consequences of a sale.

Financing Strategy

We intend to use leverage in making our investments with an objective of maintaining a strong balance sheet and providing liquidity to grow our Portfolio. We are currently targeting to reduce our leverage to 40-45% loan-to-value (outstanding principal balance to enterprise value) over time by increasing the value of our properties and refinancing properties we intend to hold longer-term. However, we are not subject to any limitations on the amount of leverage we may use, and, accordingly, the amount of leverage we use may be significantly less or greater than what we currently anticipate. We are currently meeting our short-term liquidity needs through our cash and cash equivalents and cash flows from operations.

When interest rates are high or financing is otherwise unavailable on a timely basis, we may purchase certain properties and other assets for cash with the intention of obtaining a loan for a portion of the purchase price at a later time. We will refinance properties during the term of a loan only under certain circumstances, such as when a decline in interest rates makes it beneficial to prepay an existing mortgage, an existing mortgage matures, the value of the property has increased significantly and we can obtain more attractive terms through refinancing the property, or an attractive investment becomes available and the proceeds from the refinancing can be used to purchase such investment.

We typically use floating rate debt with interest rate swaps and interest rate caps as opposed to using fixed rate debt. We believe this is a more sensible and flexible way to utilize leverage, while limiting our interest rate risk in our strategy as we attempt to increase the value of each property over the course of three years after acquisition through our value-add program. Fixed rate financing is typically more expensive and less flexible since there are typically high prepayment penalties, yield maintenance payments and/or defeasance penalties when refinancing the debt prior to maturity. To the extent we intend to hold a property long-term, we will reassess the use of refinancing with fixed rate debt.

Property Management Strategy

We seek to achieve long-term earnings growth through superior property management. To achieve this, we have partnered with BH to manage all of our properties as an external manager. In order to align our property manager's interests with those of our stockholders, BH (through an affiliate) is a noncontrolling limited partner of the OP. We

believe BH provides the following benefits:

- manages approximately 90,000 multifamily units in 20 states and has managed multifamily communities for 26 years;
 - brings a scale of operations we could not otherwise achieve for approximately 3% of gross income, which is the contracted amount we pay for its property management services;
- has operations in all of our current and desired markets, allowing us greater scale when entering new markets or make investments in non-core markets without making substantial investments in management infrastructure in those markets;
- has a construction management operation and substantial experience in renovating Class B multifamily units;
- its scale allows it to obtain highly competitive pricing as it pertains to the costs of our value-add program, increasing our return on investment for renovations;
- helps us source and underwrite opportunities as well as assist in due diligence of properties prior to closing;
- assists in locating potential buyers for our properties;

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its size, scale and experience allows it to keep costs low and maximize rents and occupancy; and has proved successful in driving other revenue growth at properties it manages.

Our Structure

The following chart shows our ownership structure.

*An affiliate of BH Equities, LLC is the property manager for all of our properties.

Our Adviser

We are externally managed by our Adviser pursuant to the Advisory Agreement, by and among the OP, our Adviser, and us. Our Adviser was organized on September 5, 2014 and is an affiliate of Highland. Our Adviser has contractual and fiduciary responsibilities to us and our stockholders as further described under “—Our Advisory Agreement” below. The members of our Adviser’s management team are Jim Dondero, Brian Mitts, Matt McGraner and Matthew Goetz, all of whom are employed by our Adviser or its affiliates.

Our Adviser has also entered into a shared services agreement with Highland, pursuant to which Highland or its affiliates provide research and operational support to our Adviser, including services in connection with the due diligence of actual or potential investments, the execution of investment transactions approved by our Adviser and certain back office and administrative services.

Our Advisory Agreement

Below is a summary of the terms of our Advisory Agreement:

Duties of Our Adviser. Our Advisory Agreement provides that our Adviser manage our business and affairs in accordance with the policies and guidelines established by our Board and that our Adviser be under the supervision of our Board. The agreement requires our Adviser to provide us with all services necessary or appropriate to conduct our business, including the following:

- locating, presenting and recommending to us real estate investment opportunities consistent with our investment policies, acquisition and disposition strategies and objectives, including our conflicts of interest policies;
- structuring the terms and conditions of transactions pursuant to which acquisitions and dispositions of properties will be made;
- acquiring and disposing properties on our behalf in compliance with our investment objectives, strategies and applicable tax regulations;
- arranging for the financing and refinancing of properties;
- administering our bookkeeping and accounting functions;
- serving as our consultant in connection with policy decisions to be made by our Board, managing our properties or causing our properties to be managed by another party;
- monitoring our compliance with regulatory requirements, including the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and the rules and regulations promulgated thereunder, New York Stock Exchange (“NYSE”) rules and regulations of the Code to maintain our status as a REIT;
- performing administrative services; and
- rendering other services as our Board deems appropriate.

Our Adviser is required to obtain the prior approval of our Board in connection with:

- any investment for which the portion of the consideration paid out of our equity equals or exceeds \$50,000,000;
- any investment that is inconsistent with the publicly disclosed investment guidelines as in effect from time to time, or, if none are then publicly disclosed, as otherwise adopted by our Board from time to time; or
- any engagement of affiliated service providers on behalf of us or the OP, which engagement terms will be negotiated on an arm’s length basis.

For these purposes, “equity” means the purchase price of the investment, exclusive of the proceeds of any debt financing incurred or to be incurred in connection with the relevant investment and anticipated closing and other acquisition costs.

Our Adviser will be prohibited from taking any action, in its sole judgment, or in the sole judgment of our Board, that:

- would adversely affect our qualification as a REIT under the Code, unless our Board had determined that REIT qualification is not in the best interest of us and our stockholders;
- would subject us to regulation under the Investment Company Act of 1940 (the “1940 Act”), except to the extent that we and our Adviser have undertaken in the Advisory Agreement and our charter to comply with Section 15 of the 1940 Act in connection with the entry into, continuation of, or amendment of the Advisory Agreement or any advisory agreement;
- is contrary to or inconsistent with our investment guidelines; or
- would violate any law, rule, regulation or statement of policy of any governmental body or agency having jurisdiction over us or our shares of common stock, or otherwise not be permitted by our charter or bylaws.

Advisory Fee. Our Advisory Agreement requires that we pay our Adviser an annual advisory fee of 1.00% of our Average Real Estate Assets.

“Average Real Estate Assets” means the average of the aggregate book value of Real Estate Assets (see below) before reserves for depreciation or other non-cash reserves, computed by taking the average of the book value of real estate assets at the end of each month (1) for which any fee under the Advisory Agreement is calculated or (2) during the year for which any expense reimbursement under the Advisory Agreement is calculated. “Real Estate Assets” is defined broadly in the Advisory Agreement to include, among other things, investments in real estate-related securities and mortgages and reserves for capital expenditures (the value-add program).

In calculating the advisory fee, we categorize our Average Real Estate Assets into either “Contributed Assets” or “New Assets.” The advisory fee on Contributed Assets may not exceed \$4.5 million in any calendar year. This cap is intended to limit the fees paid to our Adviser on the Contributed Assets following the Spin-Off to the fees that would have been paid by NHF to its adviser had the Spin-Off not occurred. The advisory fee on New Assets is not subject to this limitation but is subject to the expense cap mentioned below.

“Contributed Assets” means all of the real estate assets we owned upon the completion of the Spin-Off and is not reduced for dispositions of such assets subsequent to the Spin-Off.

“New Assets” means all of the Average Real Estate Assets other than Contributed Assets. New Assets includes proceeds from the sale of a Contributed Asset that are used to purchase a new investment.

The advisory fee is payable monthly in arrears in cash, unless our Adviser elects, in its sole discretion, to receive all or a portion of such fee in shares of our common stock, subject to the limitations set forth below under “—Limitations on Receiving Shares.” The number of shares issued to our Adviser as payment for the advisory fee will be equal to the dollar amount of the portion of such fee that is payable in shares divided by the volume-weighted average closing price of shares of our common stock for the ten trading days prior to the end of the month for which such fee will be paid, which we refer to as the fee VWAP. Our Adviser computes each installment of the advisory fee as promptly as possible after the end of the month with respect to which such installment is payable.

The accrued fees are payable monthly as promptly as possible after the end of each month during which the Advisory Agreement is in effect. A copy of the computations made by our Adviser to calculate such installment is delivered to our Board for informational purposes only.

Administrative Fee. Our Advisory Agreement requires that we pay our Adviser an annual administrative fee of 0.20% of the Average Real Estate Assets.

In calculating the administrative fee, we categorize our Average Real Estate Assets into either Contributed Assets or New Assets. The administrative fee on Contributed Assets may not exceed \$890,000 in any calendar year. This cap is intended to limit the fees paid to our Adviser on the Contributed Assets following the Spin-Off to the fees that would have been paid by NHF to its adviser had the Spin-Off not occurred. The administrative fee on New Assets is not subject to this limitation but is subject to the expense cap described below.

The administrative fee is payable monthly in arrears in cash, unless our Adviser elects, in its sole discretion, to receive all or a portion of such fee in shares of our common stock, subject to the limitations set forth below under “—Limitations on Receiving Shares.” The number of shares issued to our Adviser as payment for the administrative fee will be equal to the dollar amount of the portion of such fee that is payable in shares divided by the fee VWAP. Our Adviser computes each installment of the administrative fee as promptly as possible after the end of each month with respect to which such installment is payable. The accrued fees are payable monthly as promptly as possible after the end of

each month during which the Advisory Agreement is in effect. A copy of the computations made by our Adviser to calculate such installment is delivered to our Board for informational purposes only.

Reimbursement of Expenses. Our Advisory Agreement requires that we reimburse our Adviser for all of its out-of-pocket expenses in performing its services, including legal, accounting, financial, due diligence and other services performed by our Adviser that outside professionals or outside consultants would otherwise perform and also pay our pro rata share of rent, telephone, utilities, office furniture, equipment, machinery and other office, internal and overhead expenses of our Adviser required for our operations (“Adviser Operating Expenses”). Adviser Operating Expenses do not include expenses for the advisory and administrative services provided under the Advisory Agreement. We will also reimburse our Adviser for any and all expenses (other than underwriters’ discounts) in connection with an offering, including, without limitation, legal, accounting, printing, mailing and filing fees and other documented offering expenses.

When applicable, our Adviser prepares a statement documenting all expenses incurred during each month, and delivers such statement to us within 15 business days after the end of each month. When submitted for reimbursement, such expenses are reimbursed by us no later than the 15th business day immediately following the date of delivery of such statement of expenses to us. All expenses payable by us or reimbursable to our Adviser pursuant to the agreement will not be in amounts greater than those which would be payable to outside professionals or consultants engaged to perform such services pursuant to agreements negotiated on an arm's length basis. Our Adviser may, at its discretion and at any time, waive its right to reimbursement for eligible out-of-pocket expenses paid on our behalf. Once waived, these expenses are considered permanently waived and become non-recoupable in the future.

Expense Cap. Reimbursement of Adviser Operating Expenses under the Advisory Agreement, advisory and administrative fees paid to our Adviser and corporate general and administrative expenses such as audit, legal, listing and Board fees and equity-based compensation expense recognized under a long-term incentive plan will not exceed 1.5% of Average Real Estate Assets per calendar year (or part thereof that the Advisory Agreement is in effect (the "Expense Cap")). The Expense Cap does not limit the reimbursement by us of expenses related to securities offerings paid by our Adviser. The Expense Cap also does not apply to legal, accounting, financial, due diligence and other service fees incurred in connection with mergers and acquisitions, extraordinary litigation or other events outside our ordinary course of business or any out-of-pocket acquisition or due diligence expenses incurred in connection with the acquisition or disposition of real estate assets.

Term of the Advisory Agreement. The Advisory Agreement has a one-year term. The Advisory Agreement shall continue in full force and effect so long as the Advisory Agreement is approved at least annually by our Board. On February 13, 2019, our Board, including the independent directors, unanimously approved the renewal of the Advisory Agreement with the Adviser for a one-year term that expires on March 16, 2020.

The Advisory Agreement may be terminated at any time, without payment of any penalty to our Adviser, by vote of our Board or stockholders, or by our Adviser, in each case on not more than 60 days' nor less than 30 days' prior written notice to the other party. The Advisory Agreement shall automatically and immediately terminate in the event of its "assignment" (as defined in the 1940 Act).

Amendment. The Advisory Agreement may only be amended, waived, discharged or terminated in writing signed by the party against which enforcement of the amendment, waiver, discharge or termination is sought.

Limitations on Receiving Shares. The ability of our Adviser to receive shares of our common stock as payment for all or a portion of the advisory and administrative fees due under the terms of our Advisory Agreement will be subject to the following limitations: (1) the ownership of shares of common stock by our Adviser may not violate the ownership limitations set forth in our charter, after giving effect to any exception from such ownership limitations that our Board may grant to our Adviser or its affiliates and (2) compliance with all applicable restrictions under the U.S. federal securities laws and the NYSE rules. To the extent that payment of any fee in shares of our common stock would result in a violation of the ownership limits set forth in our charter (taking into account any applicable waiver or any restrictions imposed under the U.S. federal securities laws or NYSE rules), all or a portion of such fee payable to our Adviser will be payable in cash to the extent necessary to avoid such violation.

Registration Rights. We entered into a registration rights agreement with our Adviser with respect to any shares of our common stock that our Adviser receives as payment for any fees owed under our Advisory Agreement. These registration rights will require us to file a registration statement with respect to such shares. We agreed to pay all of the expenses relating to registering these securities. The costs associated with registering these securities will not be deducted from the compensation owed to our Adviser.

Liability and Indemnification of our Adviser. Under the Advisory Agreement, we are also required to indemnify our Adviser and to pay or reimburse reasonable expenses in advance of final disposition of a proceeding with respect to certain of our Adviser's acts or omissions.

Other Activities of our Adviser and its Affiliates. Our Adviser and its affiliates expect to engage in other business ventures, and as a result, their resources will not be dedicated exclusively to our business. However, pursuant to the Advisory Agreement, our Adviser will be required to devote sufficient resources to our administration to discharge its obligations.

Potential Acquisition of our Adviser. Many REITs that are listed on a national stock exchange are considered "self-managed" or "internally managed," since the employees of such REITs perform all significant management functions. In contrast, REITs that are not self-managed, like us, are referred to as "externally managed" and typically engage a third party, such as our Adviser, to perform management functions on its behalf. Our independent directors may determine that we should become self-managed through the acquisition of our Adviser, which we refer to as an internalization transaction. See "Risk Factors—If we internalize our management functions, the percentage of our outstanding common stock owned by our other stockholders could be reduced, and we could incur other significant costs associated with being self-managed."

Our Property Manager

The entities through which we own the properties in our Portfolio have entered into management agreements with BH. Pursuant to these agreements, BH operates and leases the underlying properties in our Portfolio. In addition to property management and leasing services, BH also provides us with market research, acquisition advice, a pipeline of investment opportunities and construction management services. We utilize BH for property and construction management services and leasing, paying BH a management fee of approximately 3% of the monthly gross income from each property managed, as well as construction supervision fees and certain other fees described under “—Property Management Agreements” below.

Property Management Agreements

Under these agreements, BH operates, coordinates and supervises the ordinary and usual business and affairs pertaining to the operation, maintenance, leasing, licensing, and management of each property. The following summarizes the terms of the management agreements.

Term. The terms of the management agreements will continue until the last day of the calendar month following the second anniversary of the agreement. Upon the expiration of the original term, the agreements will automatically renew on a month-to-month basis until terminated. The agreements may be terminated at any time with 60 days written notice.

Proposed Management Plans. Each management agreement requires that BH prepare and submit a proposed management plan and operating budget for the marketing, operation, repair and maintenance, and renovation of the property for the year the agreement is entered into. BH must submit subsequent proposed management plans 45 days prior to the beginning of the next year.

Amounts Payable under the Management Agreements. The entities that own the properties pay BH monthly for its services. Pursuant to the management agreements, BH may pay itself out of each property’s operating account. Any sums not paid within 10 days after becoming due bear interest at the rate of 18% per annum. Compensation under the management agreements consists of the following components:

• **Management Fee.** The management fee is approximately 3% of the monthly gross income from each property. For the purposes of calculating the management fee, “monthly gross income” is defined as all receipts of every kind and nature actually collected from the operation of the property, determined on a cash basis, including, without limitation, rental or lease payments, late charges, service charges, forfeited security deposits, proceeds of vending machine collections, resident utility payment collections, and all other forms of miscellaneous income (but excluding the collection of any insurance or condemnation awards).

• **Set-Up/Inspection Fees.** BH receives a one-time set-up/inspection fee per unit upon commencement of management of each property.

• **Construction Supervision Fee.** BH receives a construction supervision fee of 5-6% of total project costs if BH performs these services.

• **Renter’s Insurance Program Fee; Other Fees.** In the event that the entities that own the properties direct BH to implement a renter’s insurance program at a property, the entities pay BH a fee in connection with running such program. In consideration for any additional services other than the services required under the management agreements, the entities pay BH an hourly rate.

Additionally, BH also acts as a paymaster for the properties and is reimbursed at cost for various operating expenses it pays on behalf of the properties.

Termination. A management agreement will terminate automatically in the event that the entity that owns the property is sold or if all or substantially all of the property to which the agreement applies is otherwise disposed of.

Additionally, a management agreement may be terminated if certain other events occur, including:

- a default by BH or the entity that owns the property that is not cured prior to the expiration of any applicable cure periods;
- upon written notice by either party if a petition for bankruptcy, reorganization or arrangement is filed by the other party, or if any such petition shall be filed against the other party and is not dismissed within 60 days of the date of such filing, or in the event the other party shall make an assignment for the benefit of creditors, or take advantage of any insolvency statute or similar law;

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• upon 15 days written notice in the event that all or substantially all of the property is destroyed by a casualty, or taken by means of eminent domain or condemnation; or
• upon 60 days written notice by either party.

If a management agreement is terminated by the entity that owns the property for any reason, or if it is terminated by BH due to our default or due to the destruction, condemnation or taking by eminent domain of a property, the entity that owns the property will be required to pay damages to BH. Such damages will be equal to the management fee earned by BH for the calendar month immediately preceding the month in which the notice of termination is given, multiplied by the number of months and/or portions thereof remaining from the termination date until the end of the initial term or term year in which the termination occurred.

Additionally, for the month or the partial month after the date of the termination of BH's on-site property management responsibilities, BH will be paid a close-out management fee equivalent to 50% of the last month's full management fee.

Insurance. The entities that own the properties are required to maintain property and liability insurance for each property, and its liability insurance policy must include BH as an "Additional Insured." BH is required to maintain, at the entities' expense, workers' compensation insurance covering all employees of BH employed in, on, or about each property so as to provide statutory benefits required by state and federal laws.

Assignment. BH may not assign the management agreements without the prior written consent of the entities that own the properties.

Indemnification. The entities that own the properties are required to indemnify, defend and hold harmless BH and its agents and employees from and against all claims, liabilities, losses, damages, and/or expenses arising out of (1) BH's performance under the management agreements, or (2) facts, occurrences, or matters first arising before the date of the management agreements. The entities that own the properties are not required to indemnify BH against damages or expenses suffered as a result of the gross negligence, willful misconduct, or fraud on the part of BH, its agents, or employees.

BH is required to indemnify, defend, and hold harmless the entities that own the properties and their agents and employees from and against all claims, liabilities, losses, damages, and/or expenses arising out of the gross negligence, willful misconduct, or fraud on the part of BH, its agents, or employees, and shall at its own cost and expense defend any action or proceeding against us arising therefrom.

Our Sponsor

Highland is a registered investment adviser with the U.S. Securities and Exchange Commission ("SEC"), which, together with its affiliates, including our Adviser, had approximately \$9.9 billion in assets under management as of December 31, 2018. Highland is one of the most experienced global alternative credit managers. The firm invests in various credit and equity strategies through hedge funds, long-only funds, separate accounts, collateralized loan obligations, non-traded funds, publicly traded funds, closed-end funds, mutual funds and ETFs, and manages strategies such as distressed-for-control private equity, oil and gas, direct real estate, real estate credit and originated or structured real estate credit investments. The members of Highland's real estate team, both during their tenure at Highland and in their previous roles before joining Highland, and employees of BH have a long history of investing in real estate and debt related to real estate properties.

Regulation

Multifamily properties are subject to various laws, ordinances and regulations, including regulations relating to common areas, such as swimming pools, activity centers, and recreational facilities. We believe that each of our properties has the necessary permits and approvals to operate its business.

Americans with Disabilities Act

The properties in our Portfolio must comply with Title III of the ADA, to the extent that such properties are “public accommodations” as defined by the ADA. The ADA may require removal of structural barriers to access by persons with disabilities in certain public areas of our properties where such removal is readily achievable. We believe that our properties are in substantial compliance with the ADA and that we will not be required to make substantial capital expenditures to address the requirements of the ADA. However, noncompliance with the ADA could result in imposition of fines or an award of damages to private litigants. The obligation to make readily accessible accommodations is an ongoing one, and we will continue to assess our properties and make alterations as appropriate in this respect.

Fair Housing Act

The FHA, its state law counterparts and the regulations promulgated by the U.S. Department of Housing and Urban Development and various state agencies, prohibit discrimination in housing on the basis of race or color, national origin, religion, sex, familial status (including children under the age of 18 living with parents or legal custodians, pregnant women and people securing custody of children under 18) or handicap (disability) and, in some states, financial capability or other bases. A failure to comply with these laws in our operations could result in litigation, fines, penalties or other adverse claims, or could result in limitations or restrictions on our ability to operate, any of which could materially and adversely affect us. We believe that we operate our properties in substantial compliance with the FHA.

Environmental Matters

Under various federal, state and local laws and regulations relating to the environment, as a current or former owner or operator of real property, we may be liable for costs and damages resulting from the presence or discharge of hazardous or toxic substances, waste or petroleum products at, on, in, under, or migrating from such property, including costs to investigate and clean up such contamination and liability for natural resources. Such laws often impose liability without regard to whether the owner or operator knew of, or was responsible for, the presence of such contamination, and the liability may be joint and several. These liabilities could be substantial and the cost of any required remediation, removal, fines, or other costs could exceed the value of the property and/or our aggregate assets. In addition, the presence of contamination or the failure to remediate contamination at our properties may expose us to third-party liability for costs of remediation and/or personal or property damage or materially adversely affect our ability to sell, lease or develop our properties or to borrow using the properties as collateral. In addition, environmental laws may create liens on contaminated sites in favor of the government for damages and costs it incurs to address such contamination. Moreover, if contamination is discovered on our properties, environmental laws may impose restrictions on the manner in which property may be used or businesses may be operated, and these restrictions may require substantial expenditures.

Independent environmental consultants have conducted Phase I Environmental Site Assessments at all of the properties in our Portfolio using the American Society for Testing and Materials Standard E 1527-05. A Phase I Environmental Site Assessment is a report that identifies potential or existing environmental contamination liabilities. Site assessments are intended to discover and evaluate information regarding the environmental condition of the assessed property and surrounding properties. These assessments do not generally include soil samplings, subsurface investigations or an asbestos survey. None of the site assessments identified any known past or present contamination that we believe would have a material adverse effect on our business, assets or operations. However, the assessments are limited in scope and may have failed to identify all environmental conditions or concerns. A prior owner or operator of a property or historic operations at our properties, or operations and conditions at nearby properties, may have created a material environmental condition that is not known to us or the independent consultants preparing the site assessments. Material environmental conditions may have arisen after the review was completed or may arise in the future, and future laws, ordinances or regulations may impose material additional environmental liability. Moreover, conditions identified in environmental assessments that did not appear material at that time, may in the future result in material liability.

Environmental laws also govern the presence, maintenance and removal of hazardous materials in building materials (e.g., asbestos and lead), and may impose fines and penalties for failure to comply with these requirements or expose us to third-party liability (e.g., liability for personal injury associated with exposure to asbestos). Such laws require that owners or operators of buildings containing hazardous materials properly manage and maintain certain hazardous materials, adequately notify or train those who may come into contact with certain hazardous materials, and undertake special precautions, including removal or other abatement, if certain hazardous materials would be disturbed during

renovation or demolition of a building. In addition, the properties in our Portfolio are subject to various federal, state, and local environmental and health and safety requirements, such as state and local fire requirements.

When excessive moisture accumulates in buildings or on building materials, mold growth may occur, particularly if the moisture problem remains undiscovered or is not addressed over a period of time. Some molds may produce airborne toxins or irritants. Indoor air quality issues can also stem from inadequate ventilation, chemical contamination from indoor or outdoor sources, and other biological contaminants such as pollen, viruses and bacteria. Indoor exposure to airborne toxins or irritants above certain levels can be alleged to cause a variety of adverse health effects and symptoms, including allergic or other reactions. As a result, the presence of significant mold or other airborne contaminants at any of our properties could require us to undertake a costly remediation program to contain or remove the mold or other airborne contaminants from the affected property or increase indoor ventilation. In addition, the presence of significant mold or other airborne contaminants could expose us to liability from our tenants or others if property damage or personal injury occurs. We are not presently aware of any material adverse indoor air quality issues at our properties.

The cost of future environmental compliance may materially and adversely affect us. See “Risk Factors—We may face high costs associated with the investigation or remediation of environmental contamination, including asbestos, lead-based paint, chemical vapor, subsurface contamination and mold growth.”

Insurance

We carry comprehensive general liability coverage on the properties in our Portfolio, with limits of liability customary within the industry to insure against liability claims and related defense costs. Similarly, we are insured against the risk of direct physical damage in amounts necessary to reimburse us on a replacement-cost basis for costs incurred to repair or rebuild each property, including loss of rental income during the reconstruction period. The majority of our property policies for all U.S. operating and development communities include coverage for the perils of flood and earthquake shock with limits and deductibles customary in the industry and specific to the project. We will also obtain title insurance policies when acquiring new properties, which insure fee title to the properties in our Portfolio. We have obtained coverage for losses incurred in connection with both domestic and foreign terrorist-related activities. These policies include limits and terms we consider commercially reasonable. There are certain losses (including, but not limited to, losses arising from environmental conditions, acts of war or certain kinds of terrorist attacks) that are not insured, in full or in part, because they are either uninsurable or the cost of insurance makes it, in our belief, economically impractical to maintain such coverage. Should an uninsured loss arise against us, we would be required to use our own funds to resolve the issue, including litigation costs. In addition, for the properties in our Portfolio, we could self-insure certain portions of our insurance program and therefore, use our own funds to satisfy those limits. We believe the policy specifications and insured limits are adequate given the relative risk of loss, the cost of the coverage and industry practice. In the opinion of our management team, the properties in our Portfolio are adequately insured.

Competition

In attracting and retaining residents to occupy the properties in our Portfolio, we compete with numerous other housing alternatives. The properties in our Portfolio compete directly with other rental apartments as well as condominiums and single-family homes that are available for rent or purchase in the sub-markets in which our properties are located. Principal factors of competition include rent or price charged, attractiveness of the location and property and quality and breadth of services and amenities. If our competitors offer leases at rental rates below current market rates, or below the rental rates that the tenants of the properties in our Portfolio pay, we may lose potential tenants and we may be pressured to reduce rental rates below those currently charged or to offer more substantial rent abatements, tenant improvements, early termination rights or below-market renewal options in order to retain tenants when the tenants' leases expire.

The number of competitive properties relative to demand in a particular area has a material effect on our ability to lease apartment units at our properties and on the rents we charge. In addition, we compete with numerous other investors for suitable properties. This competition affects our ability to acquire properties and the price that we pay in such acquisitions.

Employees

Our Adviser conducts substantially all of our operations and provides asset management for our real estate investments. We expect we will only have accounting employees while the Advisory Agreement is in effect. As of December 31, 2018, we had two employees.

Corporate Information

Our Adviser's offices are located at 300 Crescent Court, Suite 700, Dallas, Texas 75201. Our Adviser's telephone number is (972) 628-4100. We maintain a website at www.nexpointliving.com. We make our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) available on our website as soon as reasonably practicable after we file

such material with, or furnish it to, the SEC. Information contained on, or accessible through our website, is not incorporated by reference into and does not constitute a part of this annual report or any other report or documents we file with or furnish to the SEC. These documents may also be found on the SEC's website at www.sec.gov.

Item 1A. Risk Factors

You should carefully consider the following risks and other information in this annual report in evaluating us and our common stock. Any of the following risks, as well as additional risks and uncertainties not currently known to us or that we currently deem immaterial, could materially and adversely affect our business, financial condition or results of operations, and could, in turn, impact the trading price of our common stock.

Risks Related to Our Business and Industry

Unfavorable market and economic conditions in the United States and globally and in the specific markets or submarkets where our properties are located could adversely affect occupancy levels, rental rates, rent collections, operating expenses and the overall market value of our assets, and impair our ability to sell, recapitalize or refinance our assets.

Unfavorable market conditions in the areas in which we operate and unfavorable economic conditions in the United States and globally may significantly affect our occupancy levels, our rental rates, rent collections, operating expenses, the market value of our properties and our ability to strategically acquire, dispose, recapitalize or refinance our multifamily properties on economically favorable terms or at all. Our ability to lease our properties at favorable rates is adversely affected by increases in supply of multifamily communities in our markets and is dependent upon overall economic conditions, which are adversely affected by, among other things, job losses and unemployment levels, a recession, personal debt levels, a downturn in the housing market, stock market volatility and uncertainty about the future. Some of our major expenses, including debt service and real estate taxes, generally do not decline when related rents decline. We expect that any declines in our occupancy levels, rental revenues and/or the values of our multifamily properties would cause us to have less cash available to pay our indebtedness, fund necessary capital expenditures and to make distributions to our stockholders, which could negatively affect our financial condition and the market value of our assets. Factors that may affect our occupancy levels, our revenues, our NOI and/or the value of our properties include the following, among others:

- downturns in global, national, regional and local economic conditions;
- declines in the financial condition of our residents, which may make it more difficult for us to collect rents from these residents;
- the inability or unwillingness of our residents to pay rent increases;
- a decline in household formation;
- a decline in employment or lack of employment growth;
- an oversupply of, or a reduced demand for, apartment homes;
- changes in market rental rates in our core markets;
- our ability to renew leases or re-lease space on favorable terms;
 - the timing and costs associated with property improvements, repairs and renovations;
- declines in mortgage interest rates, making home and condominium ownership more affordable;
- changes in home loan lending practices, including the easing of credit underwriting standards, increasing the availability of home loans and thereby reducing demand for apartment homes;
- government or builder incentives which enable first-time homebuyers to put little or no money down, making alternative housing options more attractive;
- rent control or rent stabilization laws, or other laws regulating housing, that could prevent us from raising rents to offset increases in operating costs; and
- economic conditions that could cause an increase in our operating expenses, such as increases in property taxes (particularly as a result of increased local, state and national government budget deficits and debt and potentially reduced federal aid to state and local governments), utilities, insurance, compensation of on-site associates and

routine maintenance.

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We are subject to risks inherent in ownership of real estate.

Real estate cash flows and values are affected by a number of factors, including competition from other available properties and the ability to provide adequate property maintenance and insurance and to control operating costs. Real estate cash flows and values are also affected by such factors as government regulations (including zoning, usage and tax laws) limitations on rent and rent increases, interest rate levels, the availability of financing, property tax rates, utility expenses, potential liability under environmental and other laws and changes in environmental and other laws.

Real estate investments are relatively illiquid and may limit our flexibility.

Equity real estate investments are relatively illiquid, which tends to limit our ability to react promptly to changes in economic or other market conditions. Our ability to dispose of assets in the future will depend on prevailing economic and market conditions. Our inability to sell our properties on favorable terms or at all could have a material adverse effect on our sources of working capital and our ability to satisfy our debt obligations. In addition, real estate can at times be difficult to sell quickly at prices we find acceptable. These potential difficulties in selling real estate in our markets may limit our ability to change or reduce the number of multifamily properties in our Portfolio promptly in response to changes in economic or other conditions.

Our multifamily properties are concentrated in certain geographic markets, which makes us more susceptible to adverse developments in those markets.

Our most significant geographic investment concentrations are primarily in the Southeastern and Southwestern United States. We are, therefore, subject to increased exposure from economic and other competitive factors specific to markets within these geographic areas. To the extent general economic conditions worsen in one or more of these markets, or if any of these areas experience a natural disaster, the value of our Portfolio and our market rental rates could be adversely affected. As a result, our results of operations, cash flow, cash available for distribution, including cash available to pay distributions to our stockholders, and our ability to satisfy our debt obligations could be materially adversely affected.

Our strategy for acquiring value-enhancement multifamily properties involves greater risks than more conservative investment strategies.

Our primary strategy is a value-add strategy. Therefore, for a majority of our Portfolio, we intend to execute a “value-enhancement” strategy whereby we will acquire under-managed assets in high-demand neighborhoods, invest additional capital, and reposition the properties to increase both average rental rates and resale value. Our strategy for acquiring value-enhancement multifamily properties involves greater risks than more conservative investment strategies. The risks related to these value-enhancement investments include risks related to delays in the repositioning or improvement process, higher than expected capital improvement costs, the additional capital needed to execute our value-add program, including possible borrowings or raising additional equity necessary to fund such costs, and ultimately that the repositioning process may not result in the higher rents and occupancy rates anticipated. In addition, our value-enhancement properties may not produce revenue while undergoing capital improvements. Furthermore, we may also be unable to complete the improvements of these properties and may be forced to hold or sell these properties at a loss. For these and other reasons, we cannot assure you that we will realize growth in the value of our value-enhancement multifamily properties, and as a result, our ability to make distributions to our stockholders could be adversely affected.

Potential reforms or changes to Freddie Mac and Fannie Mae could adversely affect our business.

As of December 31, 2018, we had approximately \$830.2 million and \$15.5 million of outstanding consolidated indebtedness under our Freddie Mac and Fannie Mae mortgage loans, respectively. We rely on national and regional institutions, including Freddie Mac and Fannie Mae, to provide financing for our acquisitions and permanent financing on properties we may develop in the future. Currently, there is significant uncertainty regarding the futures of Freddie Mac and Fannie Mae. Should Freddie Mac and Fannie Mae have their mandates changed or reduced, be disbanded or reorganized by the government, privatized or otherwise discontinue providing liquidity to our sector, it could significantly reduce our access to debt capital and/or increase borrowing costs and could significantly reduce our sales of assets and/or the values realized upon sale.

Competition could limit our ability to acquire attractive investment opportunities, which could adversely affect our profitability and impede our growth.

We compete with numerous real estate companies and other owners of real estate in seeking multifamily properties for acquisition and pursuing buyers for dispositions. We expect that other real estate investors, including insurance companies, private equity funds, sovereign wealth funds, pension funds, other REITs and other well-capitalized investors, will compete with us to acquire existing properties and to develop new properties, and many of these investors will have greater sources of capital to acquire properties. This competition could increase prices for properties of the type we would likely pursue and adversely affect our profitability and impede our growth.

Competition and any increased affordability of residential homes could limit our ability to lease our apartments or increase or maintain rents.

Our multifamily properties compete with other housing alternatives to attract residents, including other rental apartments, condominiums and single-family homes that are available for rent, as well as new and existing condominiums and single-family homes for sale. All of our multifamily properties are located in developed areas that include other multifamily properties and/or condominiums. The number of competitive multifamily properties and/or condominiums in a particular area, and any increased affordability of owner occupied single and multifamily homes caused by declining housing prices, low mortgage interest rates and government programs to promote home ownership, could have a material adverse effect on our ability to lease our apartments and the rents we are able to obtain. In addition, single-family homes and other residential properties provide housing alternatives to residents and potential residents of our multifamily properties.

The relatively low residential mortgage rates may result in potential renters purchasing residences rather than leasing them, and as a result, cause a decline in occupancy rates.

The relatively low residential mortgage interest rates currently available and government-sponsored programs to promote home ownership have resulted in a record high level on the National Association of Realtor's Housing Affordability Index, an index used to measure whether or not a typical family could qualify for a mortgage loan on a typical home. The foregoing factors may encourage potential renters to purchase residences rather than lease them, thereby causing a decline in the occupancy rates of our properties.

We may fail to consummate future property acquisitions, and we may not be able to find suitable alternative investment opportunities.

When acquiring properties in the future, we may be subject to various closing conditions, and there can be no assurance that we can satisfy these conditions or that the acquisitions will close. If we fail to consummate future acquisitions, there can be no assurance that we will be able to find suitable alternative investment opportunities.

Acquisitions may not yield anticipated results, which could negatively affect our financial condition and results of operations.

We intend to actively acquire multifamily properties for rental operations as market conditions, including access to the debt and equity markets, dictate. We may also acquire multifamily properties that are unoccupied or in the early stages of lease-up. We may be unable to lease-up these multifamily properties on schedule, resulting in decreases in expected rental revenues and/or lower yields as the result of lower occupancy and rental rates as well as higher than expected concessions. We may underestimate the costs necessary to bring an acquired property up to standards established for its intended market position or to complete a development project. We may be unable to integrate the existing operations of newly acquired multifamily properties and over time such communities may not perform as well as existing communities or as we initially anticipated in terms of occupancy and/or rental rates. Additionally, we expect that other major real estate investors with significant capital will compete with us for attractive investment opportunities or may also develop properties in markets where we focus our development efforts. This competition may increase acquisition costs for multifamily properties. We may not be in a position or have the opportunity in the future to make suitable property acquisitions on favorable terms.

Variable rate debt is subject to interest rate risk, which could increase our interest expense, increase the cost to refinance and increase the cost of issuing new debt.

As of December 31, 2018, approximately \$808.0 million of our total debt outstanding bears interest at variable rates, and we may also borrow additional money at variable interest rates in the future. As of December 31, 2018, seven interest rate swap agreements, with a combined notional amount of \$650.0 million and terms expiring in 2021 and 2022, effectively fix the interest rate on \$650.0 million, or 80%, of our \$808.0 million of floating rate mortgage debt outstanding. As of December 31, 2018, the interest rate cap agreements we have entered into effectively cap one-month LIBOR on \$255.2 million of our floating rate mortgage debt outstanding at a weighted average rate of 5.82% for the term of the agreements, which is generally 3-4 years. Except to the extent we have arrangements in place that hedge against the risk of rising interest rates, increases in interest rates would increase our interest expense under these instruments and would increase the cost of refinancing these instruments and issuing new debt. As a result, our cash flow and our ability to service our indebtedness and to make distributions to our stockholders would be adversely affected, which could adversely affect the market price of our common stock.

We have a substantial amount of variable rate debt and interest rate swaps indexed to LIBOR. We may be adversely affected upon the transition away from LIBOR after 2021.

In July 2017, the Financial Conduct Authority (the authority that regulates LIBOR) announced it intends to stop compelling banks to submit rates for the calculation of LIBOR after 2021. The Alternative Reference Rates Committee (“ARRC”) has proposed that the Secured Overnight Financing Rate (“SOFR”) is the rate that represents best practice as the alternative to USD-LIBOR for use in derivatives and other financial contracts that are currently indexed to USD-LIBOR. ARRC has proposed a paced market transition plan to SOFR from USD-LIBOR and organizations are currently working on industry wide and company specific transition plans as it relates to derivatives and cash markets exposed to USD-LIBOR. We have material contracts that are indexed to USD-LIBOR and are monitoring this activity and evaluating the related risks.

We are subject to certain risks associated with selling apartment communities, which could limit our operational and financial flexibility.

We periodically dispose of apartment communities that no longer meet our strategic objectives, but adverse market conditions may make it difficult to sell apartment communities like the ones we own. We cannot predict whether we will be able to sell any property for the price or on the terms we set, or whether any price or other terms offered by a prospective purchaser would be acceptable to us. We also cannot predict the length of time needed to find a willing purchaser and to close the sale of a property. Furthermore, we may be required to expend funds to correct defects or to make improvements before a property can be sold. These conditions may limit our ability to dispose of properties and to change our portfolio promptly in order to meet our strategic objectives, which may in turn have a material adverse effect on our financial condition and the market value of our assets. We are also subject to the following risks in connection with sales of our apartment communities:

- a significant portion of the proceeds from our overall property sales may be held by intermediaries in order for some sales to qualify as 1031 Exchanges so that any related capital gain can be deferred for federal income tax purposes. As a result, we may not have immediate access to all of the cash proceeds generated from our property sales; and
- federal tax laws limit our ability to profit on the sale of communities that we have owned for less than two years, and this limitation may prevent us from selling communities when market conditions are favorable.

We may be subject to contingent or unknown liabilities related to properties or business that we have acquired or may acquire for which we may have limited or no recourse against the sellers.

The properties or businesses that we have acquired or may acquire, may be subject to unknown or contingent liabilities for which we have limited or no recourse against the sellers. Unknown liabilities might include liabilities for, among other things, cleanup or remediation of undisclosed environmental conditions, liabilities under the Employee Retirement Income Security Act of 1974, as amended (“ERISA”), claims of residents, vendors or other persons dealing with the entities prior to the acquisition of such property, tax liabilities, and accrued but unpaid liabilities whether incurred in the ordinary course of business or otherwise. Because many liabilities, including tax liabilities, may not be identified within the applicable contractual indemnification period, we may have no recourse against any of the owners from whom we acquire such properties for these liabilities. The existence of such liabilities could significantly and adversely affect the value of the property subject to such liability. As a result, if a liability were asserted against us based on ownership of any of such properties, then we might have to pay substantial sums to settle it, which could adversely affect our cash flows.

We are subject to losses that are either uninsurable, not economically insurable or that are in excess of our insurance coverage.

There are certain types of losses (including, but not limited to, losses arising from environmental conditions, earthquakes and hurricanes, acts of war or certain kinds of terrorist attacks) that are not insured, in full or in part, because they are either uninsurable or the cost of insurance makes it, in our belief, economically impractical to maintain such coverage. We carry commercial general liability insurance, property insurance and terrorism insurance with respect to our communities with limits and on terms we consider commercially reasonable. If an uninsured loss or liability were to occur, whether because of a lack of insurance coverage or a loss in excess of insured limits, we could lose our capital invested in a community, as well as the anticipated future revenues from such community. We would also continue to be obligated to repay any mortgage indebtedness or other obligations related to the community. If an uninsured liability to a third party were to occur, we would incur the cost of defense and settlement with, or court ordered damages to, that third party. A significant uninsured property or liability loss could materially and adversely affect our business and our financial condition and results of operations.

Our environmental assessments may not identify all potential environmental liabilities and our remediation actions may be insufficient.

Properties being considered for potential acquisition by us are subjected to at least a Phase I or similar environmental assessment prior to closing, which generally does not involve invasive techniques such as soil or ground water sampling. A Phase II assessment is conducted if recommended in the Phase I report. These assessments, together with subsurface assessments conducted on some properties, have not revealed, and we are not otherwise aware of, any environmental conditions that we believe would have a material adverse effect on our business, assets, financial condition or results of operations. However, such environmental assessments may not identify all potential environmental liabilities. Moreover, we may in the future discover adverse environmental conditions at our communities, including at communities we acquire in the future, which may have a material adverse effect on our business, assets, financial condition or results of operations. In connection with our ownership, operation and selective development of communities, from time to time we undertake substantial remedial action in response to the presence of subsurface or other contaminants, including contaminants in soil, groundwater and soil vapor beneath or affecting our buildings. In some cases, an indemnity exists upon which we may be able to rely if environmental liability arises from the contamination, or if remediation costs exceed estimates. We can provide no assurance, however, that all necessary remediation actions have been or will be undertaken at our communities or that we will be indemnified, in full or at all, in the event that environmental liability arises.

We may face high costs associated with the investigation or remediation of environmental contamination, including asbestos, lead-based paint, chemical vapor, subsurface contamination and mold growth.

We are subject to various federal, state and local environmental and public health laws, regulations and ordinances. Under various federal, state and local environmental and public health laws, regulations and ordinances, we may be required, regardless of knowledge or responsibility, to investigate and remediate the effects of hazardous or toxic substances or petroleum product releases at our properties (including in some cases natural substances such as methane and radon gas) and may be held liable under these laws or common law to a governmental entity or to third parties for property, personal injury or natural resources damages and for investigation and remediation costs incurred as a result of the contamination. These damages and costs may be substantial and may exceed any insurance coverage we have for such events. The presence of such substances, or the failure to properly remediate the contamination, may adversely affect our ability to borrow against, sell or rent the affected property. In addition, some environmental laws create or allow a government agency to impose a lien on the contaminated site in favor of the government for damages and costs it incurs as a result of the contamination.

We face risks relating to asbestos.

Certain federal, state and local laws, regulations and ordinances govern the removal, encapsulation or disturbance of asbestos containing materials (“ACMs”) when such materials are in poor condition or in the event of renovation or demolition of a building. These laws and the common law may impose liability for release of ACMs and may allow third parties to seek recovery from owners or operators of real properties for personal injury associated with exposure to ACMs. ACMs may have been used in the construction of a number of the communities that we acquired and may have been used in the construction of communities we acquire in the future. We will implement an operations and maintenance program at each of the communities at which we discover ACMs. We can provide no assurance that we will not incur any material liabilities as a result of the presence of ACMs at our communities.

We face risks relating to lead-based paint.

Some of our communities may have lead-based paint and we may have to implement an operations and maintenance program at some of our communities. Communities that we acquire in the future may also have lead-based paint. We

can provide no assurance that we will not incur any material liabilities as a result of the presence of lead-based paint at our communities.

We face risks relating to chemical vapors and subsurface contamination.

We are also aware that environmental agencies and third parties have, in the case of certain communities with on-site or nearby contamination, asserted claims for remediation, property damage or personal injury based on the alleged actual or potential intrusion into buildings of chemical vapors (e.g., radon) or volatile organic compounds from soils or groundwater underlying or in the vicinity of those buildings or on nearby properties. We can provide no assurance that we will not incur any material liabilities as a result of vapor intrusion at our communities.

We face risks relating to mold growth.

Mold growth may occur when excessive moisture accumulates in buildings or on building materials, particularly if the moisture problem remains undiscovered or is not addressed over a period of time. Although the occurrence of mold at multifamily and other structures, and the need to remediate such mold, is not a new phenomenon, there has been increased awareness in recent years that certain molds may in some instances lead to adverse health effects, including allergic or other reactions. To help limit mold growth, we educate residents about the importance of adequate ventilation and include a lease requirement that they notify us when they see

mold or excessive moisture. We have established procedures for promptly addressing and remediating mold or excessive moisture when we become aware of its presence regardless of whether the resident believes or we believe a health risk is present. However, we can provide no assurance that mold or excessive moisture will be detected and remediated in a timely manner. If a significant mold problem arises at one of our communities, we could be required to undertake a costly remediation program to contain or remove the mold from the affected community and could be exposed to other liabilities that may exceed any applicable insurance coverage.

Compliance with various laws and regulations, including accessibility, building and health and safety laws and regulations, may be costly, may adversely affect our operations or expose us to liability.

In addition to compliance with environmental regulations, we must comply with various laws and regulations such as accessibility, building, zoning, landlord/tenant and health and safety laws and regulations, including, but not limited to, the ADA and the FHA. Some of those laws and regulations may conflict with one another or be subject to limited judicial or regulatory interpretations. Under those laws and regulations, we may be liable for, among other things, the costs of bringing our properties into compliance with the statutory and regulatory requirements. Noncompliance with certain of these laws and regulations may result in liability without regard to fault and the imposition of fines and could give rise to actions brought against us by governmental entities and/or third parties who claim to be or have been damaged as a consequence of an apartment not being in compliance with the subject laws and regulations. As part of our due diligence procedures in connection with the acquisition of a property, we typically conduct an investigation of the property's compliance with known laws and regulatory requirements with which we must comply once we acquire a property, including a review of compliance with the ADA and local zoning regulations. Our investigations and these assessments may not have revealed, and may not with respect to future acquisitions reveal, all potential noncompliance issues or related liabilities and we can provide no assurance that our development properties have been, or that our future development projects will be, designed and built in accordance with all applicable legal requirements.

The development, construction and operation of our communities are subject to regulations and permitting under various federal, state and local laws, regulations and ordinances, which regulate matters including wetlands protection, storm water runoff and wastewater discharge. Noncompliance with such laws and regulations may subject us to fines and penalties. We can provide no assurance that we will not incur any material liabilities as a result of noncompliance with these laws.

We may obtain only limited warranties when we acquire a property and may only have limited recourse if our due diligence did not identify any issues that may subject us to unknown liabilities or lower the value of our property, which could adversely affect our financial condition and ability to make distributions to you.

The seller of a property often sells the property in its "as is" condition on a "where is" basis and "with all faults," without any warranties of merchantability or fitness for a particular use or purpose. In addition, purchase agreements may contain only limited warranties, representations and indemnifications that will survive for only a limited period after the closing. The acquisition of, or purchase of, properties with limited warranties increases the risk that we may lose some or all of our invested capital in the property, lose rental income from that property or may be subject to unknown liabilities with respect to such properties.

Short-term apartment leases expose us to the effects of declining market rent, which could adversely affect our ability to make cash distributions to our stockholders.

Substantially all of our apartment leases are for a term of one year or less. Because these leases generally permit the residents to leave at the end of the lease term without penalty, our rental revenues may be impacted by declines in market rents more quickly than if our leases were for longer terms.

We may be subject to risks involved in real estate activity through joint ventures.

We may acquire properties through joint ventures when we believe circumstances warrant the use of such structures. Joint venture investments involve risks, including: the possibility that joint venture partners might refuse to make capital contributions when due; that we may be responsible to joint venture partners for indemnifiable losses; that joint venture partners might at any time have business or economic goals which are inconsistent with ours; and that joint venture partners may be in a position to take action or withhold consent contrary to our recommendations, instructions or requests. In some instances, joint venture partners may have competing interests in our markets that could create conflicts of interest. Further, joint venture partners may fail to meet their obligations to the joint venture as a result of financial distress or otherwise, and we would be forced to make contributions to maintain the value of the property. To the extent joint venture partners do not meet their obligations to the joint venture or they take action inconsistent with the interests of the joint venture, we could be adversely affected.

If we acquire properties through joint ventures, we may be required to make decisions jointly with the other investors who have interests in the respective joint ventures. We might not have the same interests as the other investors in relation to these decisions or transactions. Accordingly, we might not be able to favorably resolve any of these issues, or we might have to provide financial or other inducements to the other investors to obtain a favorable resolution.

In addition, various restrictive provisions and third-party rights, including consent rights to certain transactions, may apply to sales or transfers of interests in joint ventures. Consequently, decisions to buy or sell interests in a property or properties relating to joint ventures may be subject to the prior consent of other investors. These restrictive provisions and third-party rights would potentially preclude us from achieving full value of the properties because of our inability to obtain the necessary consents to sell or transfer the interests.

We depend on information systems, and systems failures could significantly disrupt our business, which may, in turn, negatively affect our ability to pay dividends to our stockholders.

Our business depends on the communications and information systems of Highland, to which we have access through our Adviser. In addition, certain of these systems are provided to Highland by third-party service providers. Any failure or interruption of such systems, including as a result of the termination of an agreement with any such third-party service provider, could cause delays or other problems in our activities. This, in turn, could have a material adverse effect on our operating results and negatively affect our ability to pay dividends to our stockholders.

Breaches of our data security could materially harm our business and reputation.

We collect and retain certain personal information provided by our tenants. While security measures to protect the confidentiality of this information are in place, we can provide no assurance that we will be able to prevent unauthorized access to this information. Any breach of our data security measures and/or loss of this information may result in legal liability and costs (including damages and penalties), as well as damage to our reputation, that could materially and adversely affect our business and financial performance.

We are an “emerging growth company” under the federal securities laws and will be subject to reduced public company reporting requirements.

We are an “emerging growth company,” as defined in the Jumpstart Our Business Startups Act (the “JOBS Act”), and are eligible to take advantage of certain exemptions from, or reduced disclosure obligations relating to, various reporting requirements that are normally applicable to public companies.

We could remain an “emerging growth company” until the earliest of (1) the last day of the fiscal year following the fifth anniversary of becoming a public company, (2) the last day of the first fiscal year in which we have total annual gross revenue of \$1.07 billion or more, (3) the date on which we are deemed to be a “large accelerated filer” as defined in Rule 12b-2 under the Exchange Act (which would occur if the market value of our common stock held by non-affiliates exceeds \$700 million, measured as of the last business day of our most recently completed second fiscal quarter, and we have been publicly reporting for at least 12 months) or (4) the date on which we have, during the preceding three year period, issued more than \$1.0 billion in non-convertible debt. Under the JOBS Act, emerging growth companies are not required to, among others, (1) provide an auditor’s attestation report on management’s assessment of the effectiveness of internal control over financial reporting, pursuant to Section 404 of the Sarbanes-Oxley Act of 2002 (“Sarbanes-Oxley Act”), (2) provide certain disclosures relating to executive compensation generally required for larger public companies or (3) hold stockholder advisory votes on executive compensation. We intend to take advantage of the JOBS Act exemptions that are applicable to us. Some investors may find our common stock less attractive as a result.

Additionally, the JOBS Act provides that an “emerging growth company” may take advantage of an extended transition period for complying with new or revised accounting standards that have different effective dates for public and private companies. This means an “emerging growth company” can delay adopting certain accounting standards until such standards are otherwise applicable to private companies. We have elected to take advantage of this extended transition period. As a result of this election, our financial statements may not be comparable to companies that comply with public company effective dates for such new or revised standards. We may elect to comply with public company effective dates at any time, and such election would be irrevocable pursuant to Section 107(b) of the JOBS Act.

Although we are an Emerging Growth Company, the requirements of being a public company, including compliance with the reporting requirements of the Exchange Act and the requirements of the Sarbanes-Oxley Act, may strain our resources, increase our costs and place additional demands on management, and we may be unable to comply with these requirements in a timely or cost-effective manner.

As a public company with listed equity securities, we are required to comply with new laws, regulations and requirements, certain corporate governance provisions of the Sarbanes-Oxley Act, related regulations of the SEC, including compliance with the reporting requirements of the Exchange Act and the requirements of the NYSE, with which we were not required to comply with as a private company. Complying with these statutes, regulations and requirements occupies a significant amount of time of our Board and management and requires us to incur significant costs and expenses. As a result of becoming a public company, we are required to:

- institute a more comprehensive compliance function;
- design, establish, evaluate and maintain a system of internal controls over financial reporting in compliance with the requirements of Section 404 of the Sarbanes-Oxley Act and the related rules and regulations of the SEC and the Public Company Accounting Oversight Board;
 - comply with rules promulgated by the NYSE;
- prepare and distribute periodic public reports in compliance with our obligations under federal securities laws;
- establish new internal policies, such as those relating to disclosure controls and procedures and insider trading;
- involve and retain to a greater degree outside counsel and accountants in the above activities; and
- maintain an investor relations function.

If our profitability is adversely affected because of these additional costs, it could have a negative effect on the trading price of our common stock.

Our business could be adversely impacted if there are deficiencies in our disclosure controls and procedures or internal control over financial reporting.

The design and effectiveness of our disclosure controls and procedures and internal control over financial reporting may not prevent all errors, misstatements or misrepresentations. While management will continue to review the effectiveness of our disclosure controls and procedures and internal control over financial reporting, there can be no guarantee that our internal control over financial reporting will be effective in accomplishing all control objectives all of the time. Deficiencies, including any material weakness, in our internal control over financial reporting which may occur in the future could result in misstatements of our results of operations, restatements of our financial statements, a decline in our stock price, or otherwise materially adversely affect our business, reputation, results of operations, financial condition or liquidity.

We may incur mortgage indebtedness and other borrowings, which we have broad authority to incur, that may increase our business risks and decrease the value of your investment.

We expect that in most instances, we will acquire real properties by using either existing financing or borrowing new funds. In addition, we may incur mortgage and other secured debt and pledge all or some of our real properties as security for that debt to obtain funds to acquire additional real properties. We may borrow if we need funds to satisfy the REIT tax qualification requirement that we generally distribute annually to our stockholders at least 90% of our REIT taxable income (which does not equal net income as calculated in accordance with GAAP), determined without regard to the deduction for dividends paid and excluding net capital gain. We also may borrow if we otherwise deem it necessary or advisable to assure that we maintain our qualification as a REIT.

If there is a shortfall between the cash flow from a property and the cash flow needed to service the related debt, then the amount available for distributions to stockholders may be reduced. In addition, incurring secured debt increases the risk of loss since defaults on indebtedness secured by a property may result in lenders initiating foreclosure actions. In that case, we could lose the property securing the loan that is in default, thus reducing the value of your investment. For U.S. federal income tax purposes, a foreclosure of any of our properties would be treated as a sale of the property for a purchase price equal to the outstanding balance of the debt secured by the mortgage. If the outstanding balance of the debt secured by the mortgage exceeds our tax basis in the property, we would recognize taxable income on foreclosure, but would not receive any cash proceeds. In such event, we may be unable to pay the amount of distributions required in order to maintain our REIT status. We may give full or partial guarantees to lenders of mortgage and other secured debt to the entities that own our properties. When we provide a guaranty on behalf of an entity that owns one of our properties, we will be responsible to the lender for satisfaction of the debt if it is not paid by such entity. If any mortgages or other secured debt contain cross-collateralization or cross-default provisions, a default on a single property could affect multiple properties. If any of our properties are foreclosed upon due to a default, our ability to pay cash distributions to our stockholders will be adversely affected, which could result in losing our REIT status and would result in a decrease in the value of your investment.

We have a substantial amount of indebtedness, which may limit our financial and operating activities and may adversely affect our ability to incur additional debt to fund future needs.

As of December 31, 2018, there was \$845.7 million of mortgage debt outstanding related to our Portfolio.

Payments of principal and interest on borrowings may leave us with insufficient cash resources to operate our properties, fully implement our capital expenditure, acquisition and development activities, or pay the dividends necessary to maintain our REIT qualification. Our level of debt and the limitations imposed on us by our debt agreements could have significant adverse consequences, including the following:

- require us to dedicate a substantial portion of cash flow from operations to the payment of principal, and interest on, indebtedness, thereby reducing the funds available for other purposes;
- make it more difficult for us to borrow additional funds as needed or on favorable terms, which could, among other things, adversely affect our ability to meet operational needs;
- force us to dispose of one or more of our properties, possibly on unfavorable terms (including the possible application of the 100% tax on income from prohibited transactions, discussed below in “—Risks Related to Our Structure”) or in violation of certain covenants to which we may be subject;
- subject us to increased sensitivity to interest rate increases;
- make us more vulnerable to economic downturns, adverse industry conditions or catastrophic external events;
- limit our ability to withstand competitive pressures;
- limit our ability to refinance our indebtedness at maturity or the refinancing terms may be less favorable than the terms of our original indebtedness;
- reduce our flexibility in planning for or responding to changing business, industry and economic conditions; and/or
- place us at a competitive disadvantage to competitors that have relatively less debt than we have.

If any one of these events were to occur, our financial condition, results of operations, cash flow and trading price of our common stock could be adversely affected. Furthermore, foreclosures could create taxable income without accompanying cash proceeds, which could hinder our ability to meet the REIT distribution requirements imposed by the Code.

We may be unable to refinance current or future indebtedness on favorable terms, if at all.

We may not be able to refinance existing debt on terms as favorable as the terms of existing indebtedness, or at all, including as a result of increases in interest rates or a decline in the value of our Portfolio or portions thereof. If principal payments due at maturity cannot be refinanced, extended or paid with proceeds of other capital transactions, such as new equity capital, our operating cash flow will not be sufficient in all years to repay all maturing debt. As a result, certain of our other debt may default, we may be forced to postpone capital expenditures necessary for the maintenance of our properties, we may have to dispose of one or more properties on terms that would otherwise be unacceptable to us or we may be forced to allow the mortgage holder to foreclose on a property. Foreclosure on mortgaged properties or an inability to refinance existing indebtedness would likely have a negative impact on our financial condition and results of operations and could adversely affect our ability to make distributions to our stockholders.

Our debt agreements include restrictive covenants, which could limit our flexibility and our ability to make distributions.

Our debt agreements, including our lines of credit, contain customary negative covenants that, among other things, limit our ability, without the prior consent of the lender, to further mortgage the property, to reduce or change insurance coverage or to engage in material asset sales, mergers, consolidations and acquisitions. Our debt agreements require certain mandatory prepayments upon disposition of underlying collateral. Early repayments of certain debt are

subject to prepayment penalties. Failure to comply with these covenants could cause a default under the agreements and result in a requirement to repay the indebtedness prior to its maturity, which could have an adverse effect on our cash flow and ability to make distributions to our stockholders. In addition, loan documents may limit our ability to replace a property's property manager or terminate certain operating or lease agreements related to a property. These or other limitations would decrease our operating flexibility and our ability to achieve our operating objectives.

If we are required to make payments under any “bad boy” carve out guarantees that we have provided in connection with certain mortgages and related loans, our business and financial results could be materially adversely affected.

In obtaining certain non-recourse loans, we have provided our lenders with standard carve out guarantees. These guarantees are only applicable if and when the borrower directly, or indirectly through an agreement with an affiliate, joint venture partner or other third party, voluntarily files a bankruptcy or similar liquidation or reorganization action or takes other actions that are fraudulent or improper (commonly referred to as “bad boy” guarantees). Although we believe that “bad boy” carve out guarantees are not guarantees of payment in the event of foreclosure or other actions of the foreclosing lender that are beyond the borrower’s control, some lenders in the real estate industry have recently sought to make claims for payment under such guarantees. In the event such a claim were made against us under a “bad boy” carve out guarantee, following foreclosure on mortgages or related loans, and such claim were successful, our business and financial results could be materially adversely affected.

Derivatives and hedging activity could adversely affect cash flow.

In the normal course of business, we use derivatives to manage our exposure to interest rate volatility on debt instruments, including hedging for future debt issuances. At other times, we may utilize derivatives to increase our exposure to floating interest rates. However, these hedging arrangements may not have the desired beneficial impact. Hedging arrangements, which can include a number of counterparties, may expose us to additional risks, including failure of any of our counterparties to perform under these contracts, and may involve extensive costs, such as transaction fees or, if we terminate them, breakage costs. No strategy can completely insulate us from the risks associated with interest rate fluctuations.

Risks Related to Our Structure

The relative lack of experience of our Adviser and property manager in operating under the constraints imposed on us as a REIT may hinder the achievement of our investment objectives.

Our ability to achieve our investment objectives will depend on our ability to manage and grow our business. This will depend, in turn, on our Adviser’s ability to identify, invest in and monitor properties that meet our investment criteria. The achievement of our investment objectives on a cost-effective basis will depend upon our Adviser’s execution of our investment process, its ability to provide competent, attentive and efficient services to us and our access to debt and/or equity financing on acceptable terms. Our Adviser has substantial responsibilities under the Advisory Agreement. The personnel of our Adviser are engaged in other business activities, which could distract them and divert their time and attention such that they can no longer dedicate a significant portion of their time to our businesses or otherwise slow our rate of investment. Any failure to manage our business and our future growth effectively could have a material adverse effect on our business, financial condition, results of operations and cash flows.

The Code imposes numerous constraints on the operations of REITs that do not apply to other investment vehicles managed by Highland and its affiliates. Our qualification as a REIT depends upon our ability to meet requirements regarding our organization and ownership, distributions of our income, the nature and diversification of our income and assets and other tests imposed by the Code. Any failure to comply could cause us to fail to satisfy the requirements associated with maintaining REIT status. Our Adviser and property manager have relatively limited experience operating under these constraints, which may hinder our ability to take advantage of attractive investment opportunities and to achieve our investment objectives. As a result, we cannot assure you that our Adviser or property manager will be able to operate our business under these constraints. If we fail to qualify as a REIT for any taxable year, we will be subject to federal income tax on our taxable income at corporate rates. In addition, we would generally be disqualified from treatment as a REIT for the four taxable years following the year of losing our REIT

status. Losing our REIT status would reduce our net earnings available for investment or distribution to stockholders because of the additional tax liability. In addition, distributions to stockholders would no longer qualify for the dividends-paid deduction, and we would no longer be required to make distributions. If this occurs, we might be required to borrow funds or liquidate some investments in order to pay the applicable tax.

We depend upon key personnel of Highland, our Adviser and its affiliates and our property manager.

We are an externally managed REIT and therefore we do not have any internal management capacity and only have accounting employees. We also depend on BH for our property management and construction services. We depend to a significant degree on the diligence, skill and network of business contacts of the management team and other key personnel of our Adviser and of our property manager to achieve our investment objectives, including Messrs. Dondero, Mitts, McGraner and Goetz, all of whom may be difficult to replace. We expect that our Adviser will evaluate, negotiate, structure, close and monitor our investments in accordance with the terms of the Advisory Agreement.

We also depend upon the senior professionals of our Adviser and our property manager to maintain relationships with sources of potential investments, and we rely upon these relationships to provide us with potential investment opportunities. We cannot assure you that these individuals will continue to provide indirect investment advice to us. If these individuals, including the members of the management team of our Adviser, do not maintain their existing relationships with our Adviser, maintain existing relationships or develop new relationships with other sources of investment opportunities, we may not be able to grow our investment portfolio. In addition, individuals with whom the senior professionals of our Adviser and our property manager have relationships are not obligated to provide us with investment opportunities. Therefore, we can offer no assurance that such relationships will generate investment opportunities for us.

Our Adviser relies on Highland, a registered investment adviser under common control with our Adviser, to provide investment research and operational support to our Adviser, including services in connection with research, due diligence of actual or potential investments, the execution of investment transactions approved by our Adviser and certain back office services and administrative services. If Highland does not provide such services to our Adviser, there can be no assurance that our Adviser would be able to find a substitute service provider with the same experience or on the same terms as Highland.

We may not replicate the historical results achieved by other entities managed or sponsored by affiliates of our Adviser, members of our Adviser's management team or by Highland or its affiliates.

Our primary focus in making investments generally differs from that of existing investment funds, accounts or other investment vehicles that are or have been managed by affiliates of our Adviser, members of our Adviser's management team or sponsored by Highland or its affiliates. In addition, the previously sponsored investment programs by Highland were significantly different from us in terms of targeted assets, regulatory structure and limitations, investment strategy and objectives and investment personnel. Past performance is not a guarantee of future results, and there can be no assurance that we will achieve comparable results of those Highland affiliates. We also cannot assure you that we will replicate the historical results achieved by members of the management team, and we caution you that our investment returns could be substantially lower than the returns achieved by them in prior periods. Additionally, all or a portion of the prior results may have been achieved in particular market conditions which may never be repeated.

Our Adviser can resign on 30 days' notice from its role as adviser, and we may not be able to find a suitable replacement within that time, resulting in a disruption in our operations that could adversely affect our financial condition, business, and results of operations and cash flows.

The Advisory Agreement gives our Adviser the right to resign after giving not more than 60 nor less than 30 days' written notice, whether we have found a replacement or not. If our Adviser resigns, we may not be able to find a new adviser or hire internal management with similar expertise and ability to provide the same or equivalent services on acceptable terms within 30 to 60 days, or at all. If we are unable to do so quickly, our operations are likely to experience a disruption and our financial condition, business and results of operations, as well as our ability to pay distributions, are likely to be adversely affected. In addition, the coordination of our internal management and investment activities is likely to suffer if we are unable to identify and reach an agreement with a single institution or group of executives having the experience possessed by our Adviser and its affiliates. Even if we are able to retain comparable management, the integration of such management and its lack of familiarity with our investment objectives may result in additional costs and time delays that may adversely affect our business, financial condition, results of operations and cash flows.

You will have limited control over changes in our policies and operations, which increases the uncertainty and risks you face as a stockholder.

Our Board determines our major policies, including our policies regarding financing, growth, debt capitalization, REIT qualification and distributions. Our Board may amend or revise these and other policies without your vote. Our Board's broad discretion in setting policies and your inability to exert control over those policies increases the uncertainty and risks you face as a stockholder.

We may change our targeted investments without stockholder consent.

We expect our portfolio of investments in commercial real estate to consist primarily of multifamily properties. Though this is our current target portfolio, we may make adjustments to our target portfolio based on real estate market conditions and investment opportunities, and we may change our targeted investments and investment guidelines at any time without the consent of our stockholders. Any such change could result in us making investments that are different from, and possibly riskier than, the investments described in this annual report. These policies may change over time. A change in our targeted investments or investment guidelines, which may occur without notice to you or without your consent, may increase our exposure to interest rate risk, default risk and real estate market fluctuations, all of which could adversely affect the value of our common stock and our ability to make distributions to you. We intend to disclose any changes in our investment policies in our next required periodic report, if any.

We pay substantial fees and expenses to our Adviser and its affiliates and to our property manager, which payments increase the risk that you will not earn a profit on your investment.

Pursuant to the Advisory Agreement, we pay significant fees to our Adviser and its affiliates. Those fees include advisory and administrative fees and obligations to reimburse our Adviser and its affiliates for expenses they incur in connection with providing services to us, including certain personnel services.

Additionally, pursuant to the management agreements we have entered into with BH, we pay significant fees to BH. These fees include property management fees, construction management and other customary property manager fees.

If we internalize our management functions, the percentage of our outstanding common stock owned by our other stockholders could be reduced, and we could incur other significant costs associated with being self-managed.

In the future, our Board may consider internalizing the functions performed for us by our Adviser by, among other methods, acquiring our Adviser's assets. The method by which we could internalize these functions could take many forms. There is no assurance that internalizing our management functions will be beneficial to us and our stockholders. An acquisition of our Adviser could result in a dilution of your interests as a stockholder and could reduce earnings per share and FFO, Core FFO and AFFO per share. Additionally, we may not realize the perceived benefits, we may not be able to properly integrate a new staff of managers and employees or we may not be able to effectively replicate the services provided previously by our Adviser, property manager or their affiliates. Internalization transactions, including without limitation, transactions involving the acquisition of affiliated advisers or property managers have also, in some cases, been the subject of litigation. Even if these claims are without merit, we could be forced to spend significant amounts of money defending claims that would reduce the amount of funds available for us to invest in properties or other investments and to pay distributions. All of these factors could have a material adverse effect on our results of operations, financial condition and ability to pay distributions.

There are significant potential conflicts of interest that could affect our investment returns.

As a result of our arrangements with Highland and our Adviser, there may be times when Highland, our Adviser or their affiliates have interests that differ from those of our stockholders, giving rise to a conflict of interest.

Our directors and management team serve or may serve as officers, directors or principals of entities that operate in the same or a related line of business as we do, or of investment funds managed by our Adviser or its affiliates. Similarly, our Adviser or its affiliates may have other clients with similar, different or competing investment objectives, including NexPoint Real Estate Advisors IV, L.P. In serving in these multiple capacities, they may have obligations to other clients or investors in those entities, the fulfillment of which may not be in the best interest of us or our stockholders. For example, the management team of our Adviser has, and will continue to have, management responsibilities for other investment funds, accounts or other investment vehicles managed or sponsored by our Adviser or its affiliates. Our investment objectives may overlap with the investment objectives of such affiliated investment funds, accounts or other investment vehicles. As a result, those individuals may face conflicts in the allocation of investment opportunities among us and other investment funds or accounts advised by or affiliated with our Adviser. Our Adviser will seek to allocate investment opportunities among eligible accounts in a manner consistent with its allocation policy. However, we can offer no assurance that such opportunities will be allocated to us fairly or equitably in the short-term or over time.

Additionally, under the Advisory Agreement, our Adviser does not assume any responsibility to us other than to render the services called for under that agreement, and it will not be responsible for any action of our Board in following or declining to follow our Adviser's advice or recommendations. In addition, we have agreed to indemnify our Adviser and each of its officers, directors, members, managers and employees from and against any claims or

liabilities, including reasonable legal fees and other expenses reasonably incurred, arising out of or in connection with our business and operations or any action taken or omitted on our behalf pursuant to authority granted by the Advisory Agreement, except where attributable to gross negligence, willful misconduct, bad faith or reckless disregard of such person's duties under the Advisory Agreement. These protections may lead our Adviser to act in a riskier manner when acting on our behalf than it would when acting for its own account.

Our Adviser faces conflicts of interest relating to the fee structure under our Advisory Agreement, which could result in actions that are not necessarily in the long-term best interest of our stockholders.

Under our Advisory Agreement, our Adviser or its affiliates is entitled to fees that are structured in a manner intended to provide incentives to our Adviser to perform in our best interest and in the best interest of our stockholders. However, because our Adviser is entitled to receive substantial compensation regardless of performance, our Adviser's interests are not wholly aligned with those of our stockholders. In that regard, our Adviser could be motivated to recommend riskier or more speculative investments that would entitle our Adviser to the highest fees. For example, because advisory and administrative fees payable to our Adviser are based on our total real estate assets, including any form of investment leverage, our Adviser may have an incentive to incur a high level of leverage or to acquire properties on less than favorable terms in order to increase the total amount of real estate assets under management. In

addition, our Adviser's ability to receive higher fees and reimbursements depends on our continued investment in real properties. Therefore, the interest of our Adviser and its affiliates in receiving fees may conflict with the interest of our stockholders in earning income on their investment in our common stock.

Our Adviser, Sponsor and their officers and employees face competing demands relating to their time, and this may cause our operating results to suffer.

Our Adviser, our Sponsor and their officers and employees and their respective affiliates are key personnel, general partners, sponsors, managers, owners and advisers of other real estate investment programs, including Highland-sponsored investment products, some of which have investment objectives and legal and financial obligations similar to ours and may have other business interests as well. Because these persons have competing demands on their time and resources, they may have conflicts of interest in allocating their time between our business and these other activities. If this occurs, the returns on our investments may suffer.

We may compete with other entities affiliated with our Sponsor and property manager for tenants.

Neither our Sponsor and its affiliates nor BH and its affiliates is prohibited from engaging, directly or indirectly, in any other business or from possessing interests in any other business venture, including ventures involved in the acquisition, development, ownership, management, leasing or sale of real estate, including properties in the vicinity of the properties in our Portfolio. Our Sponsor and/or its affiliates and BH and its affiliates may own and/or manage properties in the same geographical areas in which we currently own and expect to acquire real estate assets. Therefore, our properties may compete for tenants with other properties owned and/or managed by our Sponsor and its affiliates and BH and its affiliates. Our Sponsor and BH may face conflicts of interest when evaluating tenant opportunities for our properties and other properties owned and/or managed by our Sponsor and its affiliates and BH and its affiliates, and these conflicts of interest may have a negative impact on our ability to attract and retain tenants.

Our failure to qualify as a REIT for federal income tax purposes would reduce the amount of income we have available for distribution and limit our ability to make distributions to our stockholders.

Our qualification as a REIT depends upon our ability to meet requirements regarding our organization and ownership, distributions of our income, the nature and diversification of our income and assets and other tests imposed by the Code. The REIT qualification requirements are extremely complex and interpretation of the U.S. federal income tax laws governing qualification as a REIT is limited. Furthermore, future legislative, judicial or administrative changes to the federal income tax laws could be applied retroactively, which could result in our disqualification as a REIT. We believe we have been and are organized and qualify as a REIT, and we intend to operate in a manner that will permit us to continue to qualify as a REIT. However, we cannot assure you that we have qualified as a REIT, or that we will remain qualified as a REIT in the future.

If we were to fail to qualify as a REIT for any taxable year, we would be subject to federal income tax on our taxable income at regular corporate rates, and dividends paid to our stockholders would not be deductible by us in computing our taxable income. Any resulting corporate tax liability could be substantial and would reduce the amount of cash available for distribution to our stockholders, which in turn could have an adverse impact on the value of shares of our common stock. Unless we were entitled to relief under certain Code provisions, we also would be disqualified from taxation as a REIT and would not be allowed to re-elect REIT status for the four taxable years following the year in which we failed to qualify as a REIT.

The rule against re-electing REIT status following a loss of such status would also apply to us if NREO failed to qualify as a REIT for its taxable years ending on or before December 31, 2015, because we are treated as a successor to NREO for U.S. federal income tax purposes. Although NREO has represented to us that it has no knowledge of any

fact or circumstance that would cause us to fail to qualify as a REIT, and covenanted in the agreement between us and our Adviser to use its reasonable best efforts to maintain its REIT status for each of NREO's taxable years ending on or before December 31, 2015, no assurance can be given that such representation and covenant would prevent us from failing to qualify as a REIT. Although, in the event of a breach, we may be able to seek damages from NHF and NREO, there can be no assurance that such damages, if any, would appropriately compensate us.

If our operating partnership failed to qualify as a partnership or is not otherwise disregarded for U.S. federal income tax purposes, we would cease to qualify as a REIT.

Our OP intends to qualify as a partnership for federal income tax purposes, and intends to take that position for all income tax reporting purposes. If classified as a partnership, our OP generally will not be a taxable entity and will not incur federal income tax liability. However, our OP would be treated as a corporation for federal income tax purposes if it was a "publicly traded partnership," unless at least 90% of its income was qualifying income as defined in the Code. A "publicly traded partnership" is a partnership whose partnership interests are traded on an established securities market or are readily tradable on a secondary market (or the substantial equivalent thereof). Although our OP's partnership units are not traded on an established securities market, because of the redemption rights of its outside limited partner, the OP's units held by such limited partner could be viewed as readily tradable on a secondary market (or the substantial equivalent thereof), and our OP may not qualify for one of the "safe harbors" under the applicable tax regulations. Qualifying income for the 90% test generally includes passive income, such as real property rents, dividends and interest.

The income requirements applicable to REITs and the definition of qualifying income for purposes of this 90% test are similar in most respects. Our OP may not meet this qualifying income test. If our OP were to be taxed as a corporation, it would incur substantial tax liabilities, and we would then fail to qualify as a REIT for federal income tax purposes, unless we qualified for relief under certain statutory savings provisions, and our ability to raise additional capital and pay distributions to our stockholders would be impaired.

Complying with REIT requirements may force us to liquidate otherwise attractive investments.

To qualify as a REIT, we must ensure that at the end of each calendar quarter, at least 75% of the value of our assets consists of cash, cash items, government securities and qualified REIT real estate assets, including certain mortgage loans and mortgage-backed securities. The remainder of our investment in securities (other than government securities and qualified real estate assets) generally cannot include more than 10% of the outstanding voting securities of any one issuer or more than 10% of the total value of the outstanding securities of any one issuer. In addition, in general, no more than 5% of the value of our assets (other than government securities and qualified real estate assets) can consist of the securities of any one issuer, and no more than 20% of the value of our total assets can be represented by securities of one or more TRSs. If we fail to comply with these requirements at the end of any calendar quarter, we must correct the failure within 30 days after the end of the calendar quarter or qualify for certain statutory relief provisions to avoid losing our REIT qualification and suffering adverse tax consequences. As a result, we may be required to liquidate otherwise attractive investments from our Portfolio. These actions could have the effect of reducing our income and amounts available for distribution to our stockholders.

Complying with REIT requirements may limit our ability to hedge our liabilities effectively and may cause us to incur tax liabilities.

The REIT provisions of the Code may limit our ability to hedge our liabilities. Any income from a hedging transaction we enter into to manage risk of interest rate changes, price changes or currency fluctuations with respect to borrowings made or to be made to acquire or carry real estate assets, if properly identified under applicable Treasury Regulations, does not constitute "gross income" for purposes of the 75% or 95% gross income tests. For taxable years beginning after December 31, 2015, certain income from hedging transactions entered into to hedge existing hedging positions after any portion of the hedged indebtedness or property is extinguished or disposed of, will not be included in income for purposes of the 75% and 95% gross income tests. To the extent that we enter into other types of hedging transactions, the income from those transactions will likely be treated as non-qualifying income for purposes of both of the gross income tests. As a result of these rules, we may need to limit our use of advantageous hedging techniques or implement those hedges through a TRS. This could increase the cost of our hedging activities because our TRSs would be subject to tax on gains or expose us to greater risks associated with changes in interest rates than we would otherwise want to bear. In addition, losses in a TRS generally will not provide any tax benefit, except for being carried forward against future taxable income of such TRS.

Despite our qualification as a REIT for federal income tax purposes, we may be subject to other tax liabilities that reduce our cash flow and our ability to make distributions to you.

Despite our qualification as a REIT for federal income tax purposes, we may be subject to some federal, state and local taxes on our income or property. For example, net income from a "prohibited transaction" will be subject to a 100% tax. We may not be able to make sufficient distributions to avoid excise taxes applicable to REITs. We may also decide to retain income we earn from the sale or other disposition of our real estate assets and pay income tax directly on such income. We may also be subject to state and local taxes on our income or property, either directly or at the level of the companies through which we indirectly own our assets. In addition, our TRS or any TRS we form will be subject to federal income tax and applicable state and local taxes on their net income. Any federal or state taxes we pay will reduce our cash available for distribution to you.

Our ownership of interests in TRSs raises certain tax risks.

A TRS is a corporation other than a REIT in which a REIT directly or indirectly holds stock, and that has made a joint election with such REIT to be treated as a TRS. A TRS also includes any corporation other than a REIT with respect to which a TRS owns securities possessing more than 35% of the total voting power or value of the outstanding securities of such corporation. Other than some activities relating to lodging and health care facilities, a TRS may generally engage in any business, including the provision of customary or non-customary services to tenants of its parent REIT. A TRS is subject to income tax as a regular C corporation. We currently own interests in a TRS and may acquire securities in additional TRSs in the future.

We will be required to pay a 100% tax on any “redetermined rents,” “redetermined deductions,” “excess interest” or “redetermined TRS service income.” In general, redetermined rents are rents from real property that are overstated as a result of services furnished to any of our tenants by a TRS of ours. Redetermined deductions and excess interest generally represent amounts that are deducted by a TRS of ours for amounts paid to us that are in excess of the amounts that would have been deducted based on arm’s length negotiations. Redetermined TRS service income generally represents amounts by which the gross income of a TRS attributable to its services for or on behalf of us (other than to a tenant of ours) would be increased based on arm’s length negotiations.

Our TRS is and any TRS we acquire in the future will be subject to corporate income tax at the federal, state and local levels, (including on the gain realized from the sale of property held by it, as well as on income earned while such property is operated by the TRS). This tax obligation, if material, would diminish the amount of the proceeds from the sale or operation of such property, or other

income earned through the TRS that would be distributable to our stockholders. Federal, state and local corporate income tax rates may be increased in the future, and any such increase would reduce the amount of the net proceeds available for distribution by us to our stockholders from the sale of property or other income earned through a TRS after the effective date of any increase in such tax rates. We do not anticipate material income tax obligations in connection with our ownership of interests in TRSs.

As a REIT, the value of non-mortgage securities we may hold in our TRSs generally may not exceed 20% of the total value of our assets at the end of any calendar quarter. If the IRS were to determine that the value of our interests in all of our TRSs exceeded this limit at the end of any calendar quarter, then we would fail to qualify as a REIT. If we determine it to be in our best interest to own a substantial number of our properties through one or more TRSs, then it is possible that the IRS may conclude that the value of our interests in our TRSs exceeds 20% of the value of our total assets at the end of any calendar quarter and therefore cause us to fail to qualify as a REIT. Additionally, as a REIT, no more than 25% of our gross income with respect to any year may, in general, be from sources other than certain real estate-related assets. Dividends paid to us from a TRS are typically considered to be non-real estate income. Therefore, we may fail to qualify as a REIT if dividends from all of our TRSs, when aggregated with all other non-real estate income with respect to any one year, are more than 25% of our gross income with respect to such year.

The sale of certain properties could result in significant tax liabilities unless we are able to defer the taxable gain through 1031 Exchanges.

In general, we structure asset sales for possible inclusion in 1031 Exchanges. The ability to complete a 1031 Exchange depends on many factors, including, among others, identifying and acquiring suitable replacement property within limited time periods, and the ownership structure of the properties being sold and acquired. Therefore, we are not always able to sell an asset as part of a 1031 Exchange. When successful, a 1031 Exchange enables us to defer the taxable gain on the asset sold. If we cannot defer the taxable gain resulting from the sales of certain properties, our business, financial condition, results of operations and cash flow, the market price per share of our common stock and our ability to satisfy our debt service obligations and make distributions to our stockholders could be materially and adversely affected.

Certain of our business activities are potentially subject to the prohibited transaction tax, which could reduce the return on your investment.

For so long as we qualify as a REIT, our ability to dispose of property during the first few years following its acquisition may be restricted to a substantial extent as a result of our REIT qualification. Under applicable provisions of the Code regarding prohibited transactions by REITs, while we qualify as a REIT, we will be subject to a 100% penalty tax on any gain recognized on the sale or other disposition of any property (other than foreclosure property) that we own or hold an interest in, directly or indirectly through any subsidiary entity, including our operating partnership, but generally excluding TRSs, that is deemed to be inventory or property held primarily for sale to customers in the ordinary course of a trade or business. Whether property is inventory or otherwise held primarily for sale to customers in the ordinary course of a trade or business depends on the particular facts and circumstances surrounding each property. During such time as we qualify as a REIT, we intend to avoid the 100% prohibited transaction tax by (1) conducting activities that may otherwise be considered prohibited transactions through a TRS (but such TRS will incur corporate rate income taxes with respect to any income or gain recognized by it), (2) conducting our operations in such a manner so that no sale or other disposition of an asset we own or hold an interest in, directly or through any subsidiary, will be treated as a prohibited transaction, or (3) structuring certain dispositions of our properties to comply with the requirements of the prohibited transaction safe harbor available under the Code for properties that, among other requirements, have been held for at least two years. No assurance can be given that any particular property that we own or hold an interest in, directly or through any subsidiary entity, including our operating partnership, but generally excluding TRSs, will not be treated as inventory or property held

primarily for sale to customers in the ordinary course of a trade or business.

To continue qualifying as a REIT, we must meet annual distribution requirements, which may force us to forgo otherwise attractive opportunities or borrow funds during unfavorable market conditions. This could delay or hinder our ability to meet our investment objectives and reduce your overall return.

In order to qualify as a REIT, we must distribute annually to our stockholders at least 90% of our REIT taxable income (which does not equal net income as calculated in accordance with GAAP), determined without regard to the deduction for dividends paid and excluding net capital gain. We will be subject to U.S. federal income tax on our undistributed REIT taxable income and net capital gain and to a 4% nondeductible excise tax on any amount by which distributions we pay with respect to any calendar year are less than the sum of (1) 85% of our ordinary income, (2) 95% of our capital gain net income and (3) 100% of our undistributed income from prior years. These requirements could cause us to distribute amounts that otherwise would be spent on investments in real estate assets and it is possible that we might be required to borrow funds, possibly at unfavorable rates, or sell assets to fund these distributions. It is possible that we might not always be able to make distributions sufficient to meet the annual distribution requirements and to avoid U.S. federal income and excise taxes on our earnings while we qualify as a REIT.

Dividends payable by REITs generally do not qualify for the reduced tax rates available for some dividends.

Currently, the maximum tax rate applicable to qualified dividend income payable to U.S. stockholders that are individuals, trusts and estates is 20%. Dividends payable by REITs, however, generally are not eligible for this reduced rate. Distributions from REITs that are treated as dividends but are not designated as qualified dividends or capital gain dividends are treated as ordinary income. Under recently passed tax legislation commonly referred to as the Tax Cuts and Jobs Act (the "TCJA"), the rate brackets for non-corporate taxpayers' ordinary income are adjusted, the top tax rate is reduced from 39.6% to 37%, and ordinary REIT dividends are taxed at even lower effective rates. Under the TCJA, for taxable years beginning after December 31, 2017 and before January 1, 2026, distributions from REITs that are treated as dividends but are not designated as qualified dividends or capital gain dividends are taxed as ordinary income after deducting 20% of the amount of the dividend in the case of non-corporate stockholders. At the maximum ordinary income tax rate of 37% applicable for taxable years beginning after December 31, 2017 and before January 1, 2026, the maximum tax rate on ordinary REIT dividends for non-corporate stockholders is 29.6%. Although this does not adversely affect the taxation of REITs or dividends payable by REITs, the more favorable rates applicable to regular corporate qualified dividends could cause investors who are individuals, trusts and estates to perceive investments in REITs to be relatively less attractive than investments in the stocks of non-REIT corporations that pay dividends, which could adversely affect the value of the shares of REITs, including our common stock. In addition, certain U.S. stockholders may be subject to a 3.8% Medicare tax on dividends payable by REITs. Tax rates could be changed in future legislation.

The share ownership restrictions of the Code for REITs and the 6.2% share ownership limit in our charter may inhibit market activity in shares of our stock and restrict our business combination opportunities.

In order to qualify as a REIT, five or fewer individuals, as defined in the Code, may not own, actually or constructively, more than 50% in value of our issued and outstanding shares of stock at any time during the last half of each taxable year, other than the first year for which a REIT election is made. Attribution rules in the Code determine if any individual or entity actually or constructively owns shares of our common stock under this requirement. Additionally, at least 100 persons must beneficially own shares of our common stock during at least 335 days of a taxable year for each taxable year, other than the first year for which a REIT election is made. To help insure that we meet these tests, among other purposes, our charter restricts the acquisition and ownership of shares of our common stock.

Our charter, with certain exceptions, authorizes our directors to take such actions as are necessary and desirable to preserve our qualification as a REIT while we so qualify. Unless exempted by our Board (prospectively or retroactively), for so long as we qualify as a REIT, our charter prohibits, among other limitations on ownership and transfer of shares of our stock, any person from beneficially or constructively owning (applying certain attribution rules under the Code) more than 6.2% in value of the aggregate of the outstanding shares of our capital stock and more than 6.2% (in value or in number of shares, whichever is more restrictive) of the outstanding shares of our common stock. Our Board may not grant an exemption from these restrictions to any proposed transferee whose ownership in excess of the 6.2% ownership limit would result in our failing to qualify as a REIT. Our Board granted a waiver from the ownership limits for Highland, and may grant additional waivers in the future. These waivers will be subject to certain initial and ongoing conditions designed to protect our status as a REIT. These restrictions on transferability and ownership will not apply, however, if our Board determines that it is no longer in our best interest to qualify as a REIT or that compliance with the restrictions is no longer required in order for us to so qualify as a REIT.

These ownership limits could delay or prevent a transaction or a change in control that might involve a premium price for our common stock or otherwise be in the best interest of the stockholders.

The ability of the Board to revoke our REIT qualification without stockholder approval may cause adverse consequences to our stockholders.

Our charter provides that our Board may revoke or otherwise terminate our REIT election, without the approval of our stockholders, if it determines that it is no longer in our best interest to continue to qualify as a REIT. If we cease to be a REIT, we will not be allowed a deduction for dividends paid to stockholders in computing our taxable income and will be subject to U.S. federal income tax at regular corporate rates and state and local taxes, which may have adverse consequences on our total return to our stockholders.

Legislative or regulatory tax changes or other actions affecting REITs could have a negative effect on us, including our ability to qualify as a REIT or the federal income tax consequences of such qualification, and could adversely affect you.

On December 22, 2017, the TCJA was signed into law. The TCJA makes significant changes to the U.S. federal income tax rules for taxation of individuals and corporations, generally effective for taxable years beginning after December 31, 2017. In addition to reducing corporate and individual tax rates, the TCJA eliminates or restricts various deductions. Most of the changes applicable to individuals are temporary and apply only to taxable years beginning after December 31, 2017 and before January 1, 2026. The TCJA makes numerous large and small changes to the tax rules that do not affect REITs directly but may affect our stockholders and may indirectly affect us.

While the changes in the TCJA generally appear to be favorable with respect to REITs, the extensive changes to non-REIT provisions in the Code may have unanticipated effects on us or our stockholders. Moreover, Congressional leaders have recognized that the process of adopting extensive tax legislation in a short amount of time without hearings and substantial time for review is likely to have led to drafting errors, issues needing clarification and unintended consequences that will have to be revisited in subsequent tax legislation. At this point, it is not clear when Congress will address these issues or when the IRS will issue administrative guidance on the changes made in the TCJA.

At any time, the federal income tax laws governing REITs or the administrative interpretations of those laws or regulations may be amended. The rules dealing with federal income taxation are constantly under review by persons involved in the legislative process and by the IRS and the U.S. Department of the Treasury. Therefore, changes in tax laws, regulations or administrative interpretations or any amendments thereto could diminish the value of shares of our common stock or the value or the resale potential of our properties. We cannot predict how changes in the tax laws might affect our investors or us.

We urge you to consult with your own tax advisor with respect to the status of the TCJA and any other legislative, regulatory or administrative developments and proposals and their potential effect on an investment in shares of our common stock.

U.S. Federal Income Tax Consequence of the TCJA--Legislative or Other Actions Affecting REITs

Income Tax Rates. Under the TCJA, the corporate income tax rate is reduced from a maximum marginal rate of 35% to a flat 21% rate, a 40% reduction. The reduced corporate income tax rate, which is effective for taxable years beginning after December 31, 2017, reduces some of the tax advantages that REITs have had relative to C corporations, however, this reduced corporate income tax rate applies to income earned by our TRS. The rate of U.S. federal withholding tax on distributions made to non-U.S. shareholders by a REIT that are attributable to gains from the sale or exchange of U.S. real property interests was also reduced from 35% to 21%. The TCJA also permanently eliminates the corporate alternative minimum tax.

The TCJA also reduces the highest marginal income tax rate applicable to individuals to 37% (excluding the 3.8% Medicare tax on net investment income), a 6.6% reduction. Individuals continue to pay a maximum 20% rate on long-term capital gains and qualified dividend income. However, the TCJA also allows non-corporate U.S. shareholders to deduct 20% of their dividends from REITs, excluding capital gain dividends and qualified dividend income (which continue to be subject to the maximum 20% rate). As a result, the qualified REIT dividends received by an individual or other non-corporate U.S. shareholder in a REIT are subject to a maximum effective federal income tax rate of 29.6%, compared with the previously effective rate of 39.6% (plus, in each case, the 3.8% Medicare tax on net investment income). The income tax rate changes applicable to individuals apply for taxable years beginning after December 31, 2017 and before January 1, 2026.

Net Operating Loss Modifications. Net operating loss ("NOL") provisions are modified by the TCJA. The TCJA limits the NOL deduction to 80% of taxable income (before the deduction). It also generally eliminates NOL carrybacks for individuals and non-REIT corporations (NOL carrybacks did not apply to REITs under prior law), but allows indefinite NOL carryforwards. The new NOL rules apply to losses arising in taxable years beginning in 2018.

Depreciation of Real Property. The TCJA reduces the recovery period under the modified accelerated cost recovery system ("MACRS") for qualified improvement property to 15 years. Qualified improvement property is any improvement to the interior portion of a building which is non-residential real property if such improvement is placed in service after the date the building was first placed in service. The TCJA made no change to the MACRS recovery period for non-residential real property (39 years) and residential real property (27.5 years). Under the TCJA, the

alternative depreciation system lives are as follows: 30 years for residential real property (previously 40 years), 40 years for non-residential property (no change), and 20 years for qualified improvement property (previously 40 years).

Like-Kind Exchanges. The TCJA modifies the like-kind exchange provisions by restricting the preferential tax treatment applicable to like-kind exchanges to exchanges of real property not held primarily for sale. Previously, the like-kind exchange provisions also applied to personal property not held for sale. Accordingly, any personal property included in a real property exchange no longer qualifies for deferred treatment under these provisions. This change applies to exchanges completed after December 31, 2017. We believe that relatively little gain from dispositions of our real estate properties would be attributable to personal property and thus this change will not have material impact on us.

Other Provisions. The TCJA makes other significant changes to the Code. These changes include provisions limiting the ability to offset dividend and interest income with partnership or S corporation net active business losses. These provisions are effective beginning in 2018, but without further legislation, will sunset after 2025.

Foreign investors may be subject to U.S. federal withholding tax and may be subject to U.S. federal income tax on distributions received from us and upon disposition of shares of our common stock.

Subject to certain exceptions, distributions received from us will be treated as dividends of ordinary income to the extent of our current or accumulated earnings and profits. Such dividends paid to a non-U.S. stockholder ordinarily will be subject to U.S. withholding tax at a 30% rate, or such lower rate as may be specified by an applicable income tax treaty, unless the distributions are treated as “effectively connected” with the conduct by the non-U.S. stockholder of a U.S. trade or business. Pursuant to the Foreign Investment in Real Property Tax Act of 1980 (“FIRPTA”), capital gain distributions attributable to sales or exchanges of “U.S. real property interests” (“USRPIs”), generally will be taxed to a non-U.S. stockholder as if such gain were effectively connected with a U.S. trade or business. However, a capital gain dividend will not be treated as effectively connected income if (1) the distribution is received with respect to a class of stock that is regularly traded on an established securities market located in the United States and (2) the non-U.S. stockholder does not own more than 10% of the class of our stock at any time during the one-year period ending on the date the distribution is received.

Gain recognized by a non-U.S. stockholder upon the sale or exchange of our common stock generally will not be subject to U.S. federal income taxation unless such stock constitutes a USRPI under FIRPTA. Our common stock will not constitute a USRPI so long as we are a “domestically-controlled” REIT. A REIT is “domestically controlled” if less than 50% of the REIT’s stock, by value, has been owned directly or indirectly by persons who are not qualifying U.S. persons during a continuous five-year period ending on the date of disposition or, if shorter, during the entire period of the REIT’s existence. We cannot assure you that we will qualify as a “domestically controlled” REIT. If we were to fail to so qualify, gain realized by foreign investors on a sale of shares of our stock would be subject to FIRPTA tax, unless the shares of our stock were traded on an established securities market and the foreign investor did not at any time during a specified testing period directly or indirectly own more than 10% of the value of our outstanding common stock.

Risks Related to the Ownership of our Common Stock

Our common stock is listed on the NYSE and broad market fluctuations could negatively affect the market price of our stock.

We have listed shares of our common stock on the NYSE under the symbol “NXRT.” The price of NXRT common stock may fluctuate significantly. Further, the market price of our common stock may be volatile. In addition, the trading volume in our common stock may fluctuate and cause significant price variations to occur. We cannot assure you that the market price of our common stock will not fluctuate or decline significantly in the future. Some of the factors that could affect our stock price or result in fluctuations in the price or trading volume of our common stock include:

- actual or anticipated variations in our quarterly operating results;
- changes in our operations or earnings estimates or publication of research reports about us or the real estate industry;
- changes in market valuations of similar companies;
- increases in market interest rates that lead purchasers of our shares to demand a higher yield;
- adverse market reaction to any increased indebtedness we incur in the future;
- additions or departures of key management personnel;
- actions by institutional stockholders;
- speculation in the press or investment community;
- the realization of any of the other risk factors presented in this annual report;
- the extent of investor interest in our securities;

the general reputation of REITs and the attractiveness of our equity securities in comparison to other equity securities, including securities issued by other real estate-based companies;

- our underlying asset value;
- investor confidence in the stock and bond markets, generally;
- changes in tax laws;
- future equity issuances;
- failure to meet income estimates;

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failure to meet and maintain REIT qualifications; and
general market and economic conditions.

In the past, class-action litigation has often been instituted against companies following periods of volatility in the price of their common stock. This type of litigation could result in substantial costs and divert our management's attention and resources, which could have an adverse effect on our financial condition, results of operations, cash flow and trading price of our common stock.

The form, timing and/or amount of dividend distributions in future periods may vary and be impacted by economic and other considerations.

The form, timing and/or amount of dividend distributions will be declared at the discretion of our Board and will depend on actual cash flows from operations, our financial condition, capital requirements, the annual distribution requirements under the REIT provisions of the Code and other factors as our Board may consider relevant. Our Board may modify our dividend policy from time to time at its discretion.

We may be unable to make distributions at expected levels, which could result in a decrease in the market price of our common stock.

If sufficient cash is not available for distribution from our operations, we may have to fund distributions from working capital, borrow to provide funds for such distributions, reduce the amount of such distributions, or issue stock dividends. To the extent we borrow to fund distributions, our future interest costs would increase, thereby reducing our earnings and cash available for distribution from what they otherwise would have been. If cash available for distribution generated by our assets is less than we expect, our inability to make the expected distributions could result in a decrease in the market price of our common stock. In addition, if we make stock dividends in lieu of cash distributions, it may have a dilutive effect on the holdings of our stockholders.

All distributions are made at the discretion of our Board and are based upon, among other factors, our historical and projected results of operations, financial condition, cash flows and liquidity, maintenance of our REIT qualification and other tax considerations, capital expenditure and other expense obligations, debt covenants, contractual prohibitions or other limitations, applicable law and such other matters as our Board may deem relevant from time to time. We may not be able to make distributions in the future, and our inability to make distributions, or to make distributions at expected levels, could result in a decrease in the market price of our common stock.

Our charter permits the Board to issue stock with terms that may subordinate the rights of our common stockholders or discourage a third party from acquiring us in a manner that could otherwise result in a premium price to our stockholders.

Our Board may classify or reclassify any unissued shares of common stock or preferred stock and establish the preferences, conversion or other rights, voting powers, restrictions, limitations as to distributions, qualifications and terms or conditions of redemption of any such stock. Thus, our Board could authorize the issuance of preferred stock with terms and conditions that could have priority as to distributions and amounts payable upon liquidation over the rights of the holders of our common stock. Such preferred stock could also have the effect of delaying, deferring or preventing a change in control of us, including an extraordinary transaction (such as a merger, tender offer or sale of all or substantially all of our assets) that might provide a premium price to holders of our common stock.

Future issuances of debt securities and equity securities may negatively affect the market price of shares of our common stock and, in the case of equity securities, may be dilutive to existing stockholders and could reduce the overall value of your investment.

In the future, we may issue debt or equity securities or incur other financial obligations, including stock dividends and shares that may be issued in exchange for common units and equity plan shares/units. Upon liquidation, holders of our debt securities and other loans and preferred stock will receive a distribution of our available assets before common stockholders. We are not required to offer any such additional debt or equity securities to existing stockholders on a preemptive basis. Therefore, additional common stock issuances, directly or through convertible or exchangeable securities (including common units and convertible preferred units), warrants or options, will dilute the holdings of our existing common stockholders and such issuances or the perception of such issuances may reduce the market price of shares of our common stock. Any convertible preferred units would have, and any series or class of our preferred stock would likely have, a preference on distribution payments, periodically or upon liquidation, which could eliminate or otherwise limit our ability to make distributions to common stockholders.

Existing stockholders do not have preemptive rights to any shares we issue in the future. Our charter authorizes us to issue 600 million shares of capital stock, of which 500 million shares are designated as common stock and 100 million shares are designated as preferred stock. Our Board may increase the number of authorized shares of capital stock without stockholder approval. Our Board may elect to (1) sell additional shares in future public offerings; (2) issue equity interests in private offerings; (3) issue shares of our common stock under a long-term incentive plan to our directors, officers and other key employees (and those of our Adviser or its affiliates and our subsidiaries), our non-employee directors, and potentially certain non-employees who perform employee-type functions; (4) issue shares to our Adviser, its successors or assigns, in payment of an outstanding fee obligation or as consideration in a related-party transaction; or (5) issue shares of our common stock to sellers of properties we acquire in connection with an exchange of OP Units. To the extent we issue additional equity interests, your percentage ownership interest in us will be diluted. Further, depending upon the terms of such transactions, most notably the offering price per share, existing stockholders may also experience a dilution in the book value of their investment in us.

Our rights and the rights of our stockholders to recover claims against our independent directors are limited, which could reduce your and our recovery against them if they negligently cause us to incur losses.

Maryland law provides that a director has no liability in the capacity as a director if he or she performs his or her duties in good faith, in a manner he or she reasonably believes to be in the company's best interest and with the care that an ordinarily prudent person in a like position would use under similar circumstances. As permitted by the Maryland General Corporation Law (the "MGCL"), our charter limits the liability of our directors and officers to us and our stockholders for money damages, except for liability resulting from:

- actual receipt of an improper benefit or profit in money, property or services; or
- a final judgment based upon a finding of active and deliberate dishonesty by the director or officer that was material to the cause of action adjudicated.

In addition, our charter authorizes us, and our bylaws require us, to indemnify our directors and officers for actions taken by them in those capacities and to pay or reimburse their reasonable expenses in advance of final disposition of a proceeding to the maximum extent permitted by Maryland law. We have entered into indemnification agreements with our directors and executive officers. As a result, we and our stockholders may have more limited rights against our directors and officers than might otherwise exist under common law. Accordingly, in the event that actions taken by any of our directors or officers are immune or exculpated from, or indemnified against, liability but which impede our performance, our stockholders' ability to recover damages from that director or officer will be limited.

Our charter and bylaws contain provisions that may delay, defer or prevent an acquisition of our common stock or a change in control.

Our charter and bylaws contain a number of provisions, the exercise or existence of which could delay, defer or prevent a transaction or a change in control that might involve a premium price for our stockholders or otherwise be in their best interest, including the following:

◆ **Our Charter Contains Restrictions on the Ownership and Transfer of Our Stock.** In order for us to qualify, and elect to be taxed, as a REIT, no more than 50% of the value of outstanding shares of our stock may be owned, beneficially or constructively, by five or fewer individuals at any time during the last half of each taxable year other than the first year for which we elect to be taxed as a REIT. Subject to certain exceptions, our charter prohibits any stockholder from owning beneficially or constructively more than 6.2% in value or in number of shares, whichever is more restrictive, of the outstanding shares of our common stock, or 6.2% in value of the aggregate of the outstanding shares of all classes or series of our stock. We refer to these restrictions collectively as the “ownership limits.” The constructive ownership rules under the Code are complex and may cause the outstanding stock owned by a group of related individuals or entities to be deemed to be constructively owned by one individual or entity. As a result, the acquisition of less than 6.2% of our outstanding shares of common stock or the outstanding shares of all classes or series of our stock by an individual or entity could cause that individual or entity or another individual or entity to own constructively in excess of the relevant ownership limits. Our charter also prohibits any person from owning shares of our stock that would result in our being “closely held” under Section 856(h) of the Code or otherwise cause us to fail to qualify as a REIT. Any attempt to own or transfer shares of our common stock or of any of our other capital stock in violation of these restrictions may result in the shares being automatically transferred to a charitable trust or may be void. These ownership limits may prevent a third party from acquiring control of us if our Board does not grant an exemption from the ownership limits, even if our stockholders believe the change in control is in their best interest. Our Board granted a waiver from the ownership limits applicable to holders of our common stock to Highland and may grant additional waivers in the future. These waivers will be subject to certain initial and ongoing conditions designed to protect our status as a REIT.

◆ **Our Board Has the Power to Cause Us to Issue Additional Shares of Our Stock without Stockholder Approval.** Our charter authorizes us to issue additional authorized but unissued shares of common or preferred stock. In addition, our Board may, without stockholder approval, amend our charter to increase the aggregate number of shares of our common stock or the number of shares of stock of any class or series that we have authority to issue and classify or reclassify any unissued shares of common or preferred stock and set the preferences, rights and other terms of the classified or reclassified shares. As a result, our Board may establish a series of shares of common or preferred stock that could delay or prevent a transaction or a change in control that might involve a premium price for our shares of common stock or otherwise be in the best interest of our stockholders.

Certain provisions of Maryland law may limit the ability of a third party to acquire control of us.

Certain provisions of the MGCL may have the effect of inhibiting a third party from acquiring us or of impeding a change of control under circumstances that otherwise could provide our common stockholders with the opportunity to realize a premium over the then-prevailing market price of such shares, including:

◆ “business combination” provisions that, subject to limitations, prohibit certain business combinations between an “interested stockholder” (defined generally as any person who beneficially owns 10% or more of the voting power of our outstanding shares of voting stock or an affiliate or associate of the corporation who, at any time within the two-year period immediately prior to the date in question, was the beneficial owner of 10% or more of the voting power of the then outstanding stock of the corporation) or an affiliate of any interested stockholder and us for five years after the most recent date on which the stockholder becomes an interested stockholder, and thereafter imposes two super-majority stockholder voting requirements on these combinations; and

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“control share” provisions that provide that holders of “control shares” of us (defined as voting shares of stock that, if aggregated with all other shares of stock owned or controlled by the acquirer, would entitle the acquirer to exercise one of three increasing ranges of voting power in electing directors) acquired in a “control share acquisition” (defined as the direct or indirect acquisition of issued and outstanding “control shares”) have no voting rights except to the extent approved by our stockholders by the affirmative vote of at least two-thirds of all of the votes entitled to be cast on the matter, excluding all interested shares.

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Pursuant to the Maryland Business Combination Act, our Board by resolution exempted from the provisions of the Maryland Business Combination Act all business combinations (1) between our Adviser, our Sponsor or their respective affiliates and us and (2) between any other person and us, provided that such business combination is first approved by our Board (including a majority of our directors who are not affiliates or associates of such person). Our bylaws contain a provision exempting from the Maryland Control Share Acquisition Act any and all acquisitions by any person of shares of our stock. There can be no assurance that these exemptions or resolutions will not be amended or eliminated at any time in the future.

Additionally, Title 3, Subtitle 8 of the MGCL permits our Board, without stockholder approval and regardless of what is currently provided in our charter or bylaws, to implement certain takeover defenses, such as a classified board, some of which are not currently provided for in our charter or bylaws.

Risks Related to Our Spin-Off

Potential indemnification liabilities pursuant to the Separation and Distribution Agreement could materially adversely affect us.

The Separation and Distribution Agreement between us and NHF provided for, among other things, the principal corporate transactions required to effect the separation, certain conditions to the Spin-Off and provisions governing the relationship between us and NHF with respect to and resulting from the Spin-Off.

Among other things, the Separation and Distribution Agreement also provided for indemnification obligations designed to make us financially responsible for substantially all liabilities that may exist relating to or arising out of our business. If we are required to indemnify NHF under the circumstances set forth in the Separation and Distribution Agreement, we may be subject to substantial liabilities.

In connection with our separation from NHF, NHF will indemnify us for certain liabilities. However, there can be no assurance that these indemnities will be sufficient to insure us against the full amount of such liabilities, or that NHF's ability to satisfy its indemnification obligation will not be impaired in the future.

Pursuant to the Separation and Distribution Agreement, NHF has agreed to indemnify us for certain liabilities, including certain tax liabilities. However, third parties could seek to hold us responsible for any of the liabilities that NHF has agreed to retain, and there can be no assurance that NHF will be able to fully satisfy its indemnification obligations. Moreover, even if we ultimately succeed in recovering from NHF any amounts for which we are held liable, we may be temporarily required to bear these losses while seeking recovery from NHF.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

As of December 31, 2018, our Portfolio consisted of 35 properties representing 12,555 units in seven states. The following table provides a summary of the properties in our Portfolio as of December 31, 2018:

Properties by State	Location	Number of Units	Date Acquired	Purchase Price (in thousands)	As of December 31, 2018			
					Average Monthly Rent per Occupied Unit (1)	Effective Date	Number of Units Rented (2)	Average Effective Rent per Unit (3)
2017-2018 Same Store Properties								
Texas								
Arbors on Forest Ridge	Bedford, Texas	210	1/31/2014	\$12,805	\$870	95.2%	190	\$3,027
Cutter's Point	Richardson, Texas	196	1/31/2014	15,845	1,109	95.4%	165	4,185
Eagle Crest	Irving, Texas	447	1/31/2014	27,325	922	94.9%	118	2,623
Silverbrook	Grand Prairie, Texas	642	1/31/2014	30,400	835	94.9%	449	3,022
Belmont at Duck Creek	Garland, Texas	240	9/30/2014	18,525	1,030	92.1%	193	3,670
Heatherstone	Dallas, Texas	152	2/26/2015	9,450	874	94.7%	157	4,227
The Ashlar	Dallas, Texas	264	2/26/2015	16,235	859	94.3%	296	3,732
Versailles	Dallas, Texas	388	2/26/2015	26,165	884	96.4%	446	3,761
Venue at 8651	Fort Worth, Texas	333	10/30/2015	19,250	875	92.8%	277	4,238
Old Farm	Houston, Texas	734	12/29/2016	84,721	1,176	92.9%	—	—
Stone Creek at Old Farm	Houston, Texas	190	12/29/2016	23,332	1,173	96.8%	—	—
Florida								
The Summit at Sabal Park	Tampa, Florida	252	8/20/2014	19,050	955	94.4%	184	4,485
Courtney Cove	Tampa, Florida	324	8/20/2014	18,950	895	95.7%	129	4,738
Sabal Palm at Lake Buena Vista	Orlando, Florida	400	11/5/2014	49,500	1,255	96.5%	200	646
Cornerstone	Orlando, Florida	430	1/15/2015	31,550	1,007	94.2%	219	5,411
Seasons 704 Apartments	West Palm Beach, Florida	222	4/15/2015	21,000	1,130	96.8%	134	5,885
Parc500	West Palm Beach, Florida	217	7/27/2016	22,421	1,254	94.9%	106	13,936
Georgia								
Edgewater at Sandy Springs	Atlanta, Georgia	760	7/18/2014	58,000	950	94.1%	401	7,503
The Preserve at Terrell Mill	Marietta, Georgia	752	2/6/2015	58,000	921	94.8%	407	8,600
Tennessee								
Beechwood Terrace	Antioch, Tennessee	300	7/21/2014	21,400	933	93.7%	226	4,663
Willow Grove	Nashville, Tennessee	244	7/21/2014	13,750	960	95.1%	136	5,337

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Woodbridge	Nashville, Tennessee	220	7/21/2014	16,000	1,028	94.1%	95	5,231
Abbingtion Heights Arizona	Antioch, Tennessee	274	8/1/2014	17,900	889	92.0%	183	4,632
Madera Point	Mesa, Arizona	256	8/5/2015	22,525	866	94.5%	143	3,998
The Pointe at the Foothills	Mesa, Arizona	528	8/5/2015	52,275	859	95.1%	63	1,867
The Colonnade North Carolina	Phoenix, Arizona	415	10/11/2016	44,600	719	93.3%	74	10,674
Radbourne Lake	Charlotte, North Carolina	225	9/30/2014	24,250	1,082	96.0%	267	906
Timber Creek Virginia	Charlotte, North Carolina	352	9/30/2014	22,750	847	92.6%	72	5,664
Southpoint Reserve at Stoney Creek	Fredericksburg, (5) Virginia	156	12/18/2014	17,000	1,093	98.1%	55	7,240
Total 2017-2018 Same Store Properties		10,123		\$814,974	\$963	94.5%	5,385	\$4,765
Non-Same Store Properties								
Texas								
Hollister Place	Houston, Texas	260	2/1/2017	\$24,500	\$984	93.5%	118	\$7,349
Atera Apartments	Dallas, Texas	380	10/25/2017	59,200	1,232	97.4%	71	3,318
Crestmont Reserve	Dallas, Texas	242	9/26/2018	24,680	914	94.6%	—	—
Georgia								
Rockledge Apartments	Marietta, Georgia	708	6/30/2017	113,500	1,186	94.6%	87	11,571

Tennessee								
Cedar Pointe	Antioch, Tennessee	210	8/24/2018	26,500	1,051	95.7%	—	—
Brandywine I & II	Nashville, Tennessee	632	9/26/2018	79,800	957	93.8%	—	—
Total Non-Same Store Properties		2,432		\$328,180	\$1,074	94.8%	276	\$8,467
Total		12,555		\$1,143,154	\$985	94.6%	5,661	\$4,909

(1) Average effective monthly rent per unit is equal to the average of the contractual rent for commenced leases as of December 31, 2018 minus any tenant concessions over the term of the lease, divided by the number of units under commenced leases as of December 31, 2018.

(2) Percent occupied is calculated as the number of units occupied as of December 31, 2018, divided by the total number of units, expressed as a percentage.

(3) Inclusive of all full and partial interior upgrades completed.

(4) Inclusive of all full and partial interior upgrades completed and leased as of December 31, 2018.

(5) Property was classified as held for sale as of December 31, 2018.

For additional information regarding our Portfolio, see Notes 3, 4 and 5 to our consolidated financial statements.

Item 3. Legal Proceedings

From time to time, we are party to legal proceedings that arise in the ordinary course of our business. Management is not aware of any legal proceedings of which the outcome is reasonably likely to have a material adverse effect on our results of operations or financial condition, nor are we aware of any such legal proceedings contemplated by government agencies.

Item 4. Mine Safety Disclosures

Not applicable.

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Stockholder Information

On February 15, 2019, we had 23,575,826 shares of common stock outstanding held by a total of approximately 1,062 record holders. The number of record holders is based on the records of American Stock Transfer & Trust Company, LLC, who serves as our transfer agent. The number of holders does not include individuals or entities who beneficially own shares but whose shares are held of record by a broker or clearing agency, but does include each such broker or clearing agency as one record holder.

On March 15, 2017, we filed a registration statement on Form S-3 (the "Registration Statement"), registering an indeterminate aggregate principal amount and number of securities of each identified class of securities therein up to a proposed aggregate offering price of \$200,000,000, which may be offered from time to time in unspecified numbers and at indeterminate prices, as may be issued upon conversion, redemption, repurchase, exchange or exercise of any securities registered thereunder, including under any applicable anti-dilution provisions. The Registration Statement also covers an indeterminate number of securities that may become issuable as a result of stock splits, stock dividends or similar transactions relating to the securities registered thereunder.

On November 14, 2018, in connection with the 2018 Offering, we issued 2,702,500 shares of common stock, par value \$0.01 per share, at a public offering price of \$33.00 per share (before underwriters' discounts and offering costs) for gross proceeds of approximately \$89.2 million. The common stock was offered and sold pursuant to a prospectus supplement, dated November 14, 2018, and a base prospectus, dated April 24, 2017, relating to the Registration Statement. We contributed the net proceeds from the 2018 Offering to the OP in exchange for 2,702,500 OP Units, and the OP in turn used a majority of the net proceeds to repay the \$50.0 million outstanding under the \$60 Million Credit Facility and the \$30.0 million outstanding under the \$30 Million Bridge Facility. See Notes 6 and 8 to our consolidated financial statements for additional information.

Market Information

Our common stock trades on the NYSE under the ticker symbol "NXRT."

PERFORMANCE GRAPH

On April 1, 2015, our common stock commenced trading on the NYSE. The following graph compares the index of the cumulative total stockholder return on our common shares for the measurement period commencing March 31, 2015 and ending December 31, 2018 with the cumulative total returns of the Russell 3000 Index, the MSCI U.S. REIT Index (^RMZ), the Standard & Poor's U.S. REIT Index and the National Association of Real Estate Investment Trusts (NAREIT) Equity REIT Index. The following graph assumes an investment of \$100 on the initial day of the relevant measurement period and that all dividends were reinvested.

Distribution Activity

At present, we expect to continue our policy of paying regular quarterly cash dividends and to target a payout ratio that is less than Core FFO. However, the form, timing and/or amount of dividends will be declared at the discretion of our Board and will depend on actual cash flows from operations, our financial condition, capital requirements, the annual distribution requirements under the REIT provisions of the Code, any contractual limitations and other factors as our Board may consider relevant. Our Board may modify our dividend policy from time to time.

The following table shows the regular dividends declared for each quarter during the two most recent fiscal years (in thousands, except per share amounts):

	2017	
	Dividends Declared	
	Dividends Declared	Per Share
First Quarter	\$4,724	\$ 0.220
Second Quarter	4,724	0.220
Third Quarter	4,712	0.220
Fourth Quarter	5,342	0.250
Total	\$19,502	\$ 0.910

	2018	
	Dividends Declared	
	Dividends Declared	Per Share
First Quarter	\$5,380	\$ 0.250
Second Quarter	5,316	0.250
Third Quarter	5,315	0.250
Fourth Quarter	6,590	0.275
Total	\$22,601	\$ 1.025

During 2018, our dividends were classified as follows for federal income tax purposes:

	2018
Ordinary income	29 %
Capital gains	— %
Section 1250 recapture capital gains	— %
Return of capital	71 %
Total	100 %

Issuer Purchases of Equity Securities – Common stock

The following table provides information on our purchases of equity securities during the three months ended December 31, 2018:

Period	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares	Approximate Dollar Value of Shares that may yet be
			Purchased as Part of Publicly Announced Plans or Programs	Purchased under the Plans or Programs (in millions)
Beginning Balance	737,458	\$ 22.64	737,458	\$ 23.3
October 1 – October 31	—	—	—	23.3
November 1 – November 30	—	—	—	23.3
December 1 – December 31	—	—	—	23.3
Balance as of December 31, 2018	737,458	\$ 22.64	737,458	\$ 23.3

Item 6. Selected Financial Data

The following table summarizes selected financial data about the Company. The following selected financial data information should be read in conjunction with Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” and our consolidated financial statements, including the notes thereto, included elsewhere herein. The selected financial data presented below has been derived from our audited consolidated financial statements (in thousands, except per share amounts):

	As of December 31,				
	2018	2017	2016	2015	2014
Balance Sheet Data					
Net real estate investments (1)	\$1,087,542	\$991,156	\$963,037	\$902,882	\$628,526
Total assets	1,161,210	1,055,375	1,035,397	970,060	692,725
Mortgage debt, net (1)	838,020	754,405	423,138	676,324	482,344
Credit and bridge facilities, net	—	38,419	340,366	28,805	—
Total debt, net (1)	838,020	792,824	763,504	705,129	482,344
Total liabilities	862,615	813,796	779,295	721,122	495,201
Redeemable noncontrolling interests in the Operating Partnership	2,567	2,135	—	—	—
Noncontrolling interests	—	—	24,558	27,390	21,281
Stockholders' equity	296,028	239,444	231,544	221,548	176,243
	For the Year Ended December 31,				
	2018	2017	2016	2015 (2)	2014 (2)
Operating Data					
Total revenues	\$146,597	\$144,235	\$132,848	\$117,658	\$43,150
Net income (loss)	(1,614)	56,359	25,888	(10,992)	(17,533)
Net income (loss) attributable to common stockholders	(1,609)	53,374	21,882	(10,832)	(15,601)
Earnings (loss) per weighted average common share - basic	(0.08)	2.53	1.03	(0.51)	(0.73)
Earnings (loss) per weighted average common share - diluted	(0.08)	2.49	1.03	(0.51)	(0.73)
Weighted average common shares outstanding - basic	21,189	21,057	21,232	21,294	21,294
Weighted average common shares outstanding - diluted	21,667	21,399	21,314	21,294	21,294
Cash Flow Data					
Cash flows provided by operating activities	\$41,743	\$37,506	\$33,776	\$34,514	\$10,070
Cash flows provided by (used in) investing activities	(136,954)	2,324	(51,904)	(283,000)	(599,078)
Cash flows provided by (used in) financing activities	95,092	(51,843)	10,294	251,102	647,262
Other Data					
Dividends declared per common share	\$1.025	\$0.910	\$0.838	\$0.618	\$—
FFO attributable to common stockholders (3)	\$32,018	\$25,051	\$31,016	\$25,639	\$3,549
FFO per share - basic	1.51	1.19	1.46	1.20	0.17

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FFO per share - diluted	1.48	1.17	1.46	1.20	0.17
Core FFO attributable to common stockholders (3)	\$35,081	\$30,147	\$31,485	\$28,944	\$11,162
Core FFO per share - basic	1.66	1.43	1.48	1.36	0.52
Core FFO per share - diluted	1.62	1.41	1.48	1.36	0.52
AFFO attributable to common stockholders (3)	\$40,753	\$34,772	\$33,593	\$29,933	\$11,460
AFFO per share - basic	1.92	1.65	1.58	1.41	0.54
AFFO per share - diluted	1.88	1.62	1.58	1.41	0.54

(1) Includes amounts classified as held for sale, where applicable.

(2) We began operations on March 31, 2015, as described above, and therefore we had no operating activities or earnings (loss) per share before March 31, 2015. However, for purposes of the consolidated statements of operations and comprehensive income (loss), we have presented basic and diluted earnings (loss), FFO, Core FFO and AFFO per share as if the operating activities of our predecessor were those of us and assuming the shares outstanding at the date of the Spin-Off were outstanding for all periods prior to the Spin-Off.

(3)FFO, Core FFO and AFFO are non-GAAP measures. For definitions of these non-GAAP measures, as well an explanation of why we believe these measures are useful and reconciliations to the most directly comparable GAAP financial measures, see Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations” below.

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Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following is a discussion and analysis of our financial condition and our historical results of operations. The following should be read in conjunction with our financial statements and accompanying notes. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those projected, forecasted, or expected in these forward-looking statements as a result of various factors, including, but not limited to, those discussed below and elsewhere in this annual report. See "Cautionary Statement Regarding Forward-Looking Statements" and "Risk Factors" in this annual report. Our management believes the assumptions underlying the Company's financial statements and accompanying notes are reasonable. However, the Company's financial statements and accompanying notes may not be an indication of our financial condition and results of operations in the future.

Overview

As of December 31, 2018, our Portfolio consisted of 35 multifamily properties primarily located in the Southeastern and Southwestern United States encompassing 12,555 units of apartment space that was approximately 94.6% leased with a weighted average monthly effective rent per occupied apartment unit of \$985. Substantially all of our business is conducted through the OP. We own the Portfolio through the OP and our TRS. The OP owns approximately 99.9% of the Portfolio; our TRS owns approximately 0.1% of the Portfolio. The OP GP is the sole general partner of the OP. As of December 31, 2018, there were 23,819,402 OP Units outstanding, of which 23,746,169, or 99.7%, were owned by us and 73,233, or 0.3%, were owned by an unaffiliated limited partner (see Note 10 to our consolidated financial statements).

We are primarily focused on directly or indirectly acquiring, owning, and operating well-located multifamily properties with a value-add component in large cities and suburban submarkets of large cities, primarily in the Southeastern and Southwestern United States. We generate revenue primarily by leasing our multifamily properties. We intend to employ targeted management and a value-add program at a majority of our properties in an attempt to improve rental rates and the NOI at our properties and achieve long-term capital appreciation for our stockholders. We are externally managed by the Adviser through the Advisory Agreement, by and among the OP, the Adviser and us. The Advisory Agreement was renewed on February 13, 2019 for a one-year term set to expire on March 16, 2020. The Adviser is wholly owned by NexPoint Advisors, L.P., which is an affiliate of our Sponsor.

We began operations on March 31, 2015 as a result of the transfer and contribution by NHF of all but one of the multifamily properties owned by NHF through its wholly owned subsidiary NREO in exchange for 100% of its outstanding common stock. We use the term "predecessor" to mean the carve-out business of NREO, which owned all or a majority interest in the multifamily properties transferred or contributed to us by NHF through NREO. On March 31, 2015, NHF distributed all of the outstanding shares of our common stock held by NHF to holders of NHF common shares. We refer to the distribution of our common stock by NHF as the "Spin-Off." Substantially all of our operations were conducted by our predecessor prior to March 31, 2015. With the exception of a nominal amount of initial cash funded at inception, we did not own any assets prior to March 31, 2015. Our predecessor included all of the properties in our Portfolio that were held indirectly by NREO prior to the Spin-Off. Our predecessor was determined in accordance with the rules and regulations of the SEC. References throughout this report to the "Company," "we," or "our," include the activity of the predecessor defined above.

On November 14, 2018, in connection with the 2018 Offering, we issued 2,702,500 shares of our common stock, par value \$0.01 per share, at a public offering price of \$33.00 per share, for net proceeds of approximately \$84.8 million (after underwriters' discounts and offering costs). We contributed the net proceeds from the 2018 Offering to the OP in exchange for 2,702,500 OP Units, and the OP in turn used a majority of the net proceeds to repay the \$50.0 million outstanding under the \$60 Million Credit Facility and the \$30.0 million outstanding under the \$30 Million Bridge

Facility (see Notes 6 and 8 to our consolidated financial statements).

We have elected to be taxed as a REIT under Sections 856 through 860 of the Code, and expect to continue to qualify as a REIT. To qualify as a REIT, we must meet a number of organizational and operational requirements, including a requirement that we distribute at least 90% of our REIT taxable income to our stockholders. As a REIT, we will be subject to federal income tax on our undistributed REIT taxable income and net capital gain and to a 4% nondeductible excise tax on any amount by which distributions we pay with respect to any calendar year are less than the sum of (1) 85% of our ordinary income, (2) 95% of our capital gain net income and (3) 100% of our undistributed income from prior years. We believe we qualify for taxation as a REIT under the Code, and we intend to continue to operate in such a manner, but no assurance can be given that we will operate in a manner so as to qualify as a REIT. Taxable income from certain non-REIT activities is managed through a TRS and is subject to applicable federal, state, and local income and margin taxes. We had no significant taxes associated with our TRS for the years ended December 31, 2018, 2017 and 2016.

Components of Our Revenues and Expenses

Revenues

Rental income. Our earnings are primarily attributable to the rental revenue from our multifamily properties. We anticipate that the leases we enter into for our multifamily properties will typically be for one year or less on average.

Other income. Other income includes ancillary income earned from tenants such as application fees, late fees, laundry fees, utility reimbursements, and other rental related fees charged to tenants.

Expenses

Property operating expenses. Property operating expenses include property maintenance costs, salary and employee benefit costs, utilities, casualty-related expenses and recoveries and other property operating costs.

Acquisition costs. Acquisition costs include the costs to acquire additional properties. On October 1, 2016, we early adopted Accounting Standards Update (“ASU”) 2017-01, which requires an entity to capitalize acquisition costs associated with an acquisition that is determined to be an acquisition of an asset as opposed to an acquisition of a business. Prior to our adoption of ASU 2017-01, acquisition costs were expensed as incurred. We believe most future acquisition costs will be capitalized in accordance with ASU 2017-01.

Real estate taxes and insurance. Real estate taxes include the property taxes assessed by local and state authorities depending on the location of each property. Insurance includes the cost of commercial, general liability, and other needed insurance for each property.

Property management fees. Property management fees include fees paid to BH, our property manager, or other third party management companies for managing each property (see Note 10 to our consolidated financial statements).

Advisory and administrative fees. Advisory and administrative fees include the fees paid to our Adviser pursuant to the Advisory Agreement (see Note 11 to our consolidated financial statements).

Corporate general and administrative expenses. Corporate general and administrative expenses include, but are not limited to, audit fees, legal fees, listing fees, board of director fees, equity-based compensation expense, investor relations costs and payments of reimbursements to our Adviser for operating expenses. Corporate general and administrative expenses and the advisory and administrative fees paid to our Adviser (including advisory and administrative fees on properties defined in the Advisory Agreement as New Assets) will not exceed 1.5% of Average Real Estate Assets per calendar year (or part thereof that the Advisory Agreement is in effect), calculated in accordance with the Advisory Agreement, or the Expense Cap. The Expense Cap does not limit the reimbursement by us of expenses related to securities offerings paid by our Adviser. The Expense Cap also does not apply to legal, accounting, financial, due diligence, and other service fees incurred in connection with mergers and acquisitions, extraordinary litigation, or other events outside our ordinary course of business or any out-of-pocket acquisition or due diligence expenses incurred in connection with the acquisition or disposition of real estate assets.

Property general and administrative expenses. Property general and administrative expenses include the costs of marketing, professional fees, general office supplies, and other administrative related costs of each property.

Depreciation and amortization. Depreciation and amortization costs primarily include depreciation of our multifamily properties and amortization of acquired in-place leases.

Other Income and Expense

Interest expense. Interest expense primarily includes the cost of interest expense on debt, the amortization of deferred financing costs and the related impact of interest rate derivatives used to manage our interest rate risk.

Loss on extinguishment of debt and modification costs. Loss on extinguishment of debt and modification costs includes prepayment penalties and defeasance costs, the write-off of unamortized deferred financing costs and fair market value adjustments of assumed debt related to the early repayment of debt, costs incurred in a debt modification that are not capitalized as deferred financing costs and other costs incurred in a debt extinguishment.

Gain on sales of real estate. Gain on sales of real estate includes the gain recognized upon sales of properties. Gain on sales of real estate is calculated by deducting the carrying value of the real estate and costs incurred to sell the properties from the sales prices of the properties.

Results of Operations for the Years Ended December 31, 2018, 2017 and 2016

The year ended December 31, 2018 as compared to the year ended December 31, 2017

The following table sets forth a summary of our operating results for the years ended December 31, 2018 and 2017 (in thousands):

	For the Year Ended December 31,		\$ Change
	2018	2017	
Total revenues	\$ 146,597	\$ 144,235	\$ 2,362
Total expenses	(129,805)	(130,946)	1,141
Operating income	16,792	13,289	3,503
Interest expense	(28,572)	(29,576)	1,004
Loss on extinguishment of debt and modification costs	(3,576)	(5,719)	2,143
Gain on sales of real estate	13,742	78,365	(64,623)
Net income (loss)	(1,614)	56,359	(57,973)
Net income attributable to noncontrolling interests	—	2,836	(2,836)
Net income (loss) attributable to redeemable noncontrolling interests in the Operating Partnership	(5)	149	(154)
Net income (loss) attributable to common stockholders	\$(1,609)	\$53,374	\$(54,983)

The change in our net income (loss) for the year ended December 31, 2018 as compared to the year ended December 31, 2017 primarily relates to a decrease in gain on sales of real estate, and was partially offset by an increase in total revenues and decreases in total property operating expenses, depreciation and amortization expense and loss on extinguishment of debt and modification costs. The change in our net income (loss) between the periods was also due to our acquisition and disposition activity in 2017 and 2018 and the timing of the transactions (we acquired one property in the first quarter of 2017, one property in the second quarter of 2017, one property in the fourth quarter of 2017 and three properties in the third quarter of 2018; we sold four properties in the second quarter of 2017, five properties in the third quarter of 2017 and one property in the first quarter of 2018).

Revenues

Rental income. Rental income was \$128.0 million for the year ended December 31, 2018 compared to \$125.0 million for the year ended December 31, 2017, which was an increase of approximately \$3.0 million. The increase between the periods was primarily due to our acquisition and disposition activity in 2017 and 2018 and the timing of the transactions, as described above, and a 3.9% increase in the weighted average monthly effective rent per occupied apartment unit in our Portfolio to \$985 as of December 31, 2018 from \$948 as of December 31, 2017, primarily driven by the value-add program that we have implemented and organic growth in rents in the markets where our properties are located. The increase between the periods was also due to an increase in the occupancy rate of our Portfolio of 0.8% to 94.6% as of December 31, 2018 from 93.8% as of December 31, 2017.

Other income. Other income was \$18.6 million for the year ended December 31, 2018 compared to \$19.2 million for the year ended December 31, 2017, which was a decrease of approximately \$0.6 million. The decrease between the periods was primarily due to our acquisition and disposition activity in 2017 and 2018 and the timing of the transactions, as described above. The decrease between the periods was also due to a \$0.7 million, or 6.0%, decrease in utility reimbursements.

Expenses

Property operating expenses. Property operating expenses were \$35.8 million for the year ended December 31, 2018 compared to \$38.9 million for the year ended December 31, 2017, which was a decrease of approximately \$3.1 million. The decrease between the periods was primarily due to our acquisition and disposition activity in 2017 and 2018 and the timing of the transactions, as described above. The decrease between the periods was also due to a \$1.5 million, or 13.5%, decrease in utility costs and a \$0.8 million, or 4.8%, decrease in labor costs.

Real estate taxes and insurance. Real estate taxes and insurance costs were \$20.7 million for the year ended December 31, 2018 compared to \$19.2 million for the year ended December 31, 2017, which was an increase of approximately \$1.5 million. The increase between the periods was primarily due to a \$1.5 million, or 9.4%, increase in property taxes. Property taxes incurred in the first year of ownership may be significantly less than subsequent years since the purchase price of the property may trigger a significant increase in assessed value by the taxing authority in subsequent years, increasing the cost of real estate taxes.

Property management fees. Property management fees were \$4.4 million for the year ended December 31, 2018 compared to \$4.3 million for the year ended December 31, 2017, which was an increase of approximately \$0.1 million. The increase between the periods was primarily due to an increase in total revenues, which the fee is primarily based on.

Advisory and administrative fees. Advisory and administrative fees were \$7.5 million for the year ended December 31, 2018 compared to \$7.4 million for the year ended December 31, 2017, which was an increase of approximately \$0.1 million. The amount incurred during the years ended December 31, 2018 and 2017 represents the maximum fee allowed on properties defined as Contributed Assets under the Advisory Agreement plus approximately \$2.1 million and \$2.0 million, respectively, of advisory and administrative fees incurred on certain properties defined as New Assets. For the year ended December 31, 2018, our Adviser elected to voluntarily waive the advisory and administrative fees incurred on the eight properties we acquired subsequent to October 2016, which totaled approximately \$4.1 million. For the year ended December 31, 2017, our Adviser elected to voluntarily waive the advisory and administrative fees incurred on the five properties we acquired subsequent to October 2016, which totaled approximately \$2.4 million. The advisory and administrative fees waived by our Adviser for the years ended December 31, 2018 and 2017 are considered to be permanently waived for the periods. Our Adviser is not contractually obligated to waive fees on New Assets in the future and may cease waiving fees on New Assets at its discretion. Advisory and administrative fees may increase in future periods as we acquire additional properties, which will be classified as New Assets.

Corporate general and administrative expenses. Corporate general and administrative expenses were \$7.8 million for the year ended December 31, 2018 compared to \$6.3 million for the year ended December 31, 2017, which was an increase of approximately \$1.5 million. The increase between the periods was primarily due to approximately \$4.2 million of equity-based compensation expense recognized during the year ended December 31, 2018 related to the grants of restricted stock units to our directors, officers, employees and certain key employees of our Adviser pursuant to our long-term incentive plan (the “2016 LTIP”), compared to \$3.1 million of equity-based compensation expense recognized during the year ended December 31, 2017 (see Note 8 to our consolidated financial statements). Subject to the Expense Cap, corporate general and administrative expenses may increase in future periods as we acquire additional properties.

Property general and administrative expenses. Property general and administrative expenses were \$6.1 million for the year ended December 31, 2018 compared to \$6.2 million for the year ended December 31, 2017, which was a decrease of approximately \$0.1 million. The decrease between the periods was primarily due to our acquisition and disposition activity in 2017 and 2018 and the timing of the transactions, as described above.

Depreciation and amortization. Depreciation and amortization costs were \$47.5 million for the year ended December 31, 2018 compared to \$48.8 million for the year ended December 31, 2017, which was a decrease of approximately \$1.3 million. The decrease between the periods was primarily due to the amortization of intangible lease assets of \$2.5 million related to four properties for the year ended December 31, 2018 compared to \$8.9 million related to seven properties for the year ended December 31, 2017, which was a decrease of approximately \$6.4 million. The decrease between the periods was partially offset by a \$5.1 million increase in depreciation expense, primarily due to our acquisition activity in 2017 and 2018 and the timing of the transactions, as described above. The amortization of intangible lease assets over a six-month period from the date of acquisition is expected to increase the amortization expense during the initial year of operations for each property.

Other Income and Expense

Interest expense. Interest expense was \$28.6 million for the year ended December 31, 2018 compared to \$29.6 million for the year ended December 31, 2017, which was a decrease of approximately \$1.0 million. The decrease between the periods was primarily due to an increase in gain recognized related to the effective portion of changes in fair value of our interest rate swap derivatives designated as cash flow hedges of approximately \$5.3 million (see “Debt, Derivatives and Hedging Activity – Interest Rate Swap Agreements” below). The decrease between the periods was partially offset by an increase in interest on debt of approximately \$4.6 million. The following table details the various costs included in interest expense for the years ended December 31, 2018 and 2017 (in thousands):

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	For the Year Ended December 31,		
	2018	2017	\$ Change
Interest on debt	\$30,870	\$26,268	\$4,602
Amortization of deferred financing costs	1,650	1,995	(345)
Interest rate swaps - effective portion	(4,224)	1,113	(5,337)
Interest rate swaps - ineffective portion (1)	—	(309)	309
Interest rate caps expense	276	509	(233)
Total	\$28,572	\$29,576	\$(1,004)

(1) Prior to our adoption of ASU 2017-12, Derivatives and Hedging (Topic 815) (“ASU 2017-12”) on January 1, 2018, the ineffective portion of changes in the fair value of our derivatives designated as cash flow hedges was recognized directly in net income (loss) as interest expense. The adoption of ASU 2017-12 eliminates the separate measurement of effectiveness and ineffectiveness, and all changes in the fair value of derivatives that are designated as cash flow hedges are recorded directly in other comprehensive income (“OCI”). See Notes 2 and 7 to our consolidated financial statements for additional information.

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Loss on extinguishment of debt and modification costs. Loss on extinguishment of debt and modification costs was \$3.6 million for the year ended December 31, 2018 compared to \$5.7 million for the year ended December 31, 2017, which was a decrease of approximately \$2.1 million. The decrease between the periods was primarily due to decreases in debt modification and other extinguishment costs of approximately \$1.5 million and prepayment penalties and defeasance costs of approximately \$1.0 million. The following table details the various costs included in loss on extinguishment of debt and modification costs for the years ended December 31, 2018 and 2017 (in thousands):

	For the Year Ended December 31,		
	2018	2017	\$ Change
Prepayment penalties and defeasance costs	\$1,706	\$2,701	\$(995)
Write-off of deferred financing costs	1,412	1,003	409
Write-off of fair market value adjustment of assumed debt	(27)	—	(27)
Debt modification and other extinguishment costs	485	2,015	(1,530)
Total	\$3,576	\$5,719	\$(2,143)

Gain on sales of real estate. Gain on sales of real estate was \$13.7 million for the year ended December 31, 2018 compared to \$78.4 million for the year ended December 31, 2017, which was a decrease of approximately \$64.7 million. During the year ended December 31, 2018, we sold one property; during the year ended December 31, 2017, we sold nine properties.

The year ended December 31, 2017 as compared to the year ended December 31, 2016

The following table sets forth a summary of our operating results for the years ended December 31, 2017 and 2016 (in thousands):

	For the Year Ended December 31,		
	2017	2016	\$ Change
Total revenues	\$144,235	\$132,848	\$11,387
Total expenses	(130,946)	(111,003)	(19,943)
Operating income	13,289	21,845	(8,556)
Interest expense	(29,576)	(20,167)	(9,409)
Loss on extinguishment of debt and modification costs	(5,719)	(1,722)	(3,997)
Gain on sales of real estate	78,365	25,932	52,433
Net income	56,359	25,888	30,471
Net income attributable to noncontrolling interests	2,836	4,006	(1,170)
Net income attributable to redeemable noncontrolling interests in the Operating Partnership	149	—	149
Net income attributable to common stockholders	\$53,374	\$21,882	\$31,492

The change in our net income for the year ended December 31, 2017 as compared to the year ended December 31, 2016 primarily relates to increases in total revenues and gain on sales of real estate, and was partially offset by increases in total property operating expenses, depreciation and amortization expense, interest expense and loss on extinguishment of debt and modification costs. The change in our net income between the periods was also due to our acquisition and disposition activity in 2016 and 2017 and the timing of the transactions (we acquired one property in the third quarter of 2016, three properties in the fourth quarter of 2016, one property in the first quarter of 2017, one property in the second quarter of 2017 and one property in the fourth quarter of 2017; we sold three properties in the

second quarter of 2016, four properties in the third quarter of 2016, four properties in the second quarter of 2017 and five properties in the third quarter of 2017).

Revenues

Rental income. Rental income was \$125.0 million for the year ended December 31, 2017 compared to \$115.4 million for the year ended December 31, 2016, which was an increase of approximately \$9.6 million. The increase between the periods was primarily due to our acquisition and disposition activity in 2016 and 2017 and the timing of the transactions, as described above. The increase between the periods was also due to a 7.7% increase in the weighted average monthly effective rent per occupied apartment unit in our Portfolio to \$948 as of December 31, 2017 from \$880 as of December 31, 2016, primarily driven by the value-add program that we have implemented and organic growth in rents in the markets where our properties are located, and an increase in the occupancy rate of our Portfolio of 0.4% to 93.8% as of December 31, 2017 from 93.4% as of December 31, 2016.

Other income. Other income was \$19.2 million for the year ended December 31, 2017 compared to \$17.4 million for the year ended December 31, 2016, which was an increase of approximately \$1.8 million. The increase between the periods was primarily due to our acquisition and disposition activity in 2016 and 2017 and the timing of the transactions, as described above. The increase between the periods was also due to a \$1.1 million, or 11.3%, increase in utility reimbursements and a \$0.5 million, or 56.1%, increase in other resident charges.

Expenses

Property operating expenses. Property operating expenses were \$38.9 million for the year ended December 31, 2017 compared to \$38.2 million for the year ended December 31, 2016, which was an increase of approximately \$0.7 million. The increase between the periods was primarily due to our acquisition and disposition activity in 2016 and 2017 and the timing of the transactions, as described above. The increase between the periods was also due to a \$1.0 million, or 8.8%, increase in repairs and maintenance costs, partially offset by a \$0.4 million increase in casualty recoveries.

Acquisition costs. No acquisition costs were expensed for the year ended December 31, 2017 compared to \$0.4 million for the year ended December 31, 2016. During the year ended December 31, 2017, we acquired three properties and capitalized all acquisition costs incurred. During the year ended December 31, 2016, we acquired four properties; we expensed the acquisition costs related to one acquisition and capitalized acquisition costs of approximately \$0.7 million related to three acquisitions. Acquisition costs depend on the specific circumstances of each closing and are one-time costs associated with each acquisition. We believe most future acquisition costs will be capitalized.

Real estate taxes and insurance. Real estate taxes and insurance costs were \$19.2 million for the year ended December 31, 2017 compared to \$16.1 million for the year ended December 31, 2016, which was an increase of approximately \$3.1 million. The increase between the periods was primarily due to our acquisition and disposition activity in 2016 and 2017 and the timing of the transactions, as described above. The increase between the periods was also due to a \$2.8 million, or 20.3%, increase in property taxes and a \$0.3 million, or 13.6%, increase in property liability insurance. Property taxes incurred in the first year of ownership may be significantly less than subsequent years since the purchase price of the property may trigger a significant increase in assessed value by the taxing authority in subsequent years, increasing the cost of real estate taxes.

Property management fees. Property management fees were \$4.3 million for the year ended December 31, 2017 compared to \$4.0 million for the year ended December 31, 2016, which was an increase of approximately \$0.3 million. The increase between the periods was primarily due to increases in rental income and other income, which the fee is primarily based on.

Advisory and administrative fees. Advisory and administrative fees were \$7.4 million for the year ended December 31, 2017 compared to \$6.8 million for the year ended December 31, 2016, which was an increase of approximately \$0.6 million. The amount incurred during the years ended December 31, 2017 and 2016 represents the maximum fee allowed on properties defined as Contributed Assets under the Advisory Agreement plus approximately \$2.0 million and \$1.4 million, respectively, of advisory and administrative fees incurred on certain properties defined as New Assets. For the year ended December 31, 2017, our Adviser elected to voluntarily waive the advisory and administrative fees incurred on the five properties we acquired subsequent to October 2016, which totaled approximately \$2.4 million. For the year ended December 31, 2016, our Adviser elected to voluntarily waive the advisory and administrative fees incurred on the two properties we acquired subsequent to October 2016, which totaled less than \$0.1 million. The advisory and administrative fees waived by our Adviser for the years ended December 31, 2017 and 2016 are considered to be permanently waived for the periods. Our Adviser is not contractually obligated to waive fees on New Assets in the future and may cease waiving fees on New Assets at its

discretion. Advisory and administrative fees may increase in future periods as we acquire additional properties, which will be classified as New Assets.

Corporate general and administrative expenses. Corporate general and administrative expenses were \$6.3 million for the year ended December 31, 2017 compared to \$4.0 million for the year ended December 31, 2016, which was an increase of approximately \$2.3 million. The increase between periods primarily relates to \$3.1 million of equity-based compensation expense recognized during the year ended December 31, 2017 related to the grants of restricted stock units to our directors and officers pursuant to our 2016 LTIP, compared to \$0.8 million of equity-based compensation expense recognized during the year ended December 31, 2016 (see Note 8 to our consolidated financial statements). Subject to the Expense Cap, corporate general and administrative expenses may increase in future periods as we acquire additional properties.

Property general and administrative expenses. Property general and administrative expenses were \$6.2 million for the year ended December 31, 2017 compared to \$5.9 million for the year ended December 31, 2016, which was an increase of approximately \$0.3 million. The increase between the periods was primarily due to our acquisition and disposition activity in 2016 and 2017 and the timing of the transactions, as described above. The increase between the periods was also due to a \$0.3 million, or 24.4%, increase in advertising and promotional costs.

Depreciation and amortization. Depreciation and amortization costs were \$48.8 million for the year ended December 31, 2017 compared to \$35.6 million for the year ended December 31, 2016, which was an increase of approximately \$13.2 million. The increase between the periods was primarily due to the amortization of intangible lease assets of \$8.9 million related to seven properties for the year ended December 31, 2017 compared to \$1.4 million related to five properties for the year ended December 31, 2016, which was an increase of approximately \$7.5 million, as well as the acquisition of three properties subsequent to December 31, 2016. The amortization of intangible lease assets over a six-month period from the date of acquisition is expected to increase the amortization expense during the initial year of operations for each property. The increase between the periods was partially offset by a reduction in depreciation expense related to the disposition of nine properties subsequent to December 31, 2016.

Other Income and Expense

Interest expense. Interest expense was \$29.6 million for the year ended December 31, 2017 compared to \$20.2 million for the year ended December 31, 2016, which was an increase of approximately \$9.4 million. The increase between the periods was primarily due to an increase in interest on debt and a reduction in gain recognized related to the ineffective portion of changes in fair value of our interest rate swap derivatives designated as cash flow hedges (see “Debt, Derivatives and Hedging Activity – Interest Rate Swap Agreements” below), as shown in the table below. The following table details the various costs included in interest expense for the years ended December 31, 2017 and 2016 (in thousands):

	For the Year Ended December 31,		
	2017	2016	\$ Change
Interest on debt	\$26,268	\$19,390	\$6,878
Amortization of deferred financing costs	1,995	1,423	572
Interest rate swaps - effective portion	1,113	995	118
Interest rate swaps - ineffective portion	(309)	(1,683)	1,374
Interest rate caps expense	509	42	467
Total	\$29,576	\$20,167	\$9,409

Loss on extinguishment of debt and modification costs. Loss on extinguishment of debt and modification costs was \$5.7 million for the year ended December 31, 2017 compared to \$1.7 million for the year ended December 31, 2016, which was an increase of approximately \$4.0 million. The increase between the periods was primarily due to increases in prepayment penalties and defeasance costs of approximately \$1.9 million and debt modification and other extinguishment costs of approximately \$1.8 million. During the years ended December 31, 2017 and 2016, we sold nine properties and seven properties, respectively. The following table details the various costs included in loss on extinguishment of debt and modification costs for the years ended December 31, 2017 and 2016 (in thousands):

	For the Year Ended December 31,		
	2017	2016	\$ Change
Prepayment penalties and defeasance costs	\$2,701	\$827	\$1,874
Write-off of deferred financing costs	1,003	698	305
Debt modification and other extinguishment costs	2,015	197	1,818
Total	\$5,719	\$1,722	\$3,997

Gain on sales of real estate. Gain on sales of real estate was \$78.4 million for the year ended December 31, 2017 compared to \$25.9 million for the year ended December 31, 2016, which was an increase of approximately \$52.5 million. During the year ended December 31, 2017, we sold nine properties; during the year ended December 31, 2016, we sold seven properties.

Non-GAAP Measurements

Net Operating Income and Same Store Net Operating Income

NOI is a non-GAAP financial measure of performance. NOI is used by investors and our management to evaluate and compare the performance of our properties to other comparable properties, to determine trends in earnings and to compute the fair value of our properties as NOI is not affected by (1) the cost of funds, (2) acquisition costs, (3) advisory and administrative fees, (4) the impact of depreciation and amortization expenses as well as gains or losses from the sale of operating real estate assets that are included in net income computed in accordance with GAAP, (5) corporate general and administrative expenses, (6) other gains and losses that are specific to us, (7) casualty-related expenses/(recoveries) and (8) property general and administrative expenses that are not reflective of the continuing operations of the properties or are incurred on our behalf at the property for expenses such as legal, professional and franchise tax fees.

The cost of funds is eliminated from net income (loss) because it is specific to our particular financing capabilities and constraints. The cost of funds is also eliminated because it is dependent on historical interest rates and other costs of capital as well as past decisions made by us regarding the appropriate mix of capital, which may have changed or may change in the future. Acquisition costs and non-operating fees to affiliates are eliminated because they do not reflect continuing operating costs of the property owner. Depreciation and amortization expenses as well as gains or losses from the sale of operating real estate assets are eliminated because they may not accurately represent the actual change in value in our multifamily properties that result from use of the properties or changes in market conditions. While certain aspects of real property do decline in value over time in a manner that is reasonably captured by depreciation and amortization, the value of the properties as a whole have historically increased or decreased as a result of changes in overall economic conditions instead of from actual use of the property or the passage of time. Gains and losses from the sale of real property vary from property to property and are affected by market conditions at the time of sale, which will usually change from period to period. Casualty-related expenses and recoveries are excluded because they do not reflect continuing operating costs of the property owner. Entity level general and administrative expenses incurred at the properties are eliminated as they are specific to the way in which we have chosen to hold our properties and are the result of our ownership structuring. Also, expenses that are incurred upon acquisition of a property do not reflect continuing operating costs of the property owner. These gains and losses can create distortions when comparing one period to another or when comparing our operating results to the operating results of other real estate companies that have not made similarly timed purchases or sales. We believe that eliminating these items from net income is useful because the resulting measure captures the actual ongoing revenue generated and actual expenses incurred in operating our properties as well as trends in occupancy rates, rental rates and operating costs.

However, the usefulness of NOI is limited because it excludes corporate general and administrative expenses, interest expense, loss on extinguishment of debt and modification costs, acquisition costs, certain fees to affiliates such as advisory and administrative fees, depreciation and amortization expense and gains or losses from the sale of properties, and other gains and losses as determined under GAAP, the level of capital expenditures and leasing costs necessary to maintain the operating performance of our properties, all of which are significant economic costs. NOI may fail to capture significant trends in these components of net income, which further limits its usefulness.

NOI is a measure of the operating performance of our properties but does not measure our performance as a whole. NOI is therefore not a substitute for net income (loss) as computed in accordance with GAAP. This measure should be analyzed in conjunction with net income (loss) computed in accordance with GAAP and discussions elsewhere in “—Results of Operations” regarding the components of net income (loss) that are eliminated in the calculation of NOI. Other companies may use different methods for calculating NOI or similarly entitled measures and, accordingly, our NOI may not be comparable to similarly entitled measures reported by other companies that do not define the measure exactly as we do.

We define “Same Store NOI” as NOI for our properties that are comparable between periods. We view Same Store NOI as an important measure of the operating performance of our properties because it allows us to compare operating results of properties owned for the entirety of the current and comparable periods and therefore eliminates variations caused by acquisitions or dispositions during the periods.

Net Operating Income for Our 2017-2018 Same Store and Non-Same Store Properties for the Years Ended December 31, 2018 and 2017

There are 29 properties encompassing 10,123 units of apartment space in our same store pool for the years ended December 31, 2018 and 2017 (our “2017-2018 Same Store” properties). Our 2017-2018 Same Store properties exclude the following six properties in our Portfolio as of December 31, 2018: Hollister Place, Rockledge Apartments, Atera Apartments, Cedar Pointe, Crestmont Reserve and Brandywine I & II.

The following table reflects the revenues, property operating expenses and NOI for the years ended December 31, 2018 and 2017 for our 2017-2018 Same Store and Non-Same Store properties (dollars in thousands):

	For the Year Ended December 31,		\$ Change	% Change	
	2018	2017			
Revenues					
Same Store					
Rental income	\$107,312	\$102,643	\$4,669	4.5	%
Other income	16,273	15,827	446	2.8	%
Same Store revenues	123,585	118,470	5,115	4.3	%
Non-Same Store					
Rental income	20,652	22,380	(1,728)	-7.7	%
Other income	2,360	3,385	(1,025)	-30.3	%
Non-Same Store revenues	23,012	25,765	(2,753)	-10.7	%
Total revenues	146,597	144,235	2,362	1.6	%
Operating expenses					
Same Store					
Property operating expenses (1)	31,479	31,792	(313)	-1.0	%
Real estate taxes and insurance	16,318	15,735	583	3.7	%
Property management fees (2)	3,715	3,562	153	4.3	%
Property general and administrative expenses (3)	4,166	4,135	31	0.7	%
Same Store operating expenses	55,678	55,224	454	0.8	%
Non-Same Store					
Property operating expenses (4)	5,008	7,345	(2,337)	-31.8	%
Real estate taxes and insurance	4,395	3,426	969	28.3	%
Property management fees (2)	667	768	(101)	-13.2	%
Property general and administrative expenses (5)	674	894	(220)	-24.6	%
Non-Same Store operating expenses	10,744	12,433	(1,689)	-13.6	%
Total operating expenses	66,422	67,657	(1,235)	-1.8	%
NOI					
Same Store	67,907	63,246	4,661	7.4	%
Non-Same Store	12,268	13,332	(1,064)	-8.0	%
Total NOI	\$80,175	\$76,578	\$3,597	4.7	%

(1) For the years ended December 31, 2018 and 2017, excludes approximately \$656,000 and \$305,000, respectively, of casualty-related recoveries.

- (2) Fees incurred to an unaffiliated third party that is an affiliate of the noncontrolling limited partner of the OP.
 - (3) For the years ended December 31, 2018 and 2017, excludes approximately \$1,013,000 and \$939,000, respectively, of expenses that are not reflective of the continuing operations of the properties or are incurred on our behalf at the property for expenses such as legal, professional and franchise tax fees.
 - (4) For the years ended December 31, 2018 and 2017, excludes approximately \$(7,000) and \$18,000, respectively, of casualty-related expenses/(recoveries).
 - (5) For the years ended December 31, 2018 and 2017, excludes approximately \$281,000 and \$191,000, respectively, of expenses that are not reflective of the continuing operations of the properties or are incurred on our behalf at the property for expenses such as legal, professional and franchise tax fees.
- See reconciliation of net income (loss) to NOI below under “NOI and 2017-2018 Same Store NOI for the Years Ended December 31, 2018 and 2017.”

2017-2018 Same Store Results of Operations for the Years Ended December 31, 2018 and 2017

As of December 31, 2018, our 2017-2018 Same Store properties were approximately 94.5% leased with a weighted average monthly effective rent per occupied apartment unit of \$963. As of December 31, 2017, our 2017-2018 Same Store properties were approximately 93.9% leased with a weighted average monthly effective rent per occupied apartment unit of \$925. For our 2017-2018 Same Store properties, we recorded the following operating results for the year ended December 31, 2018 as compared to the year ended December 31, 2017:

Revenues

Rental income. Rental income was \$107.3 million for the year ended December 31, 2018 compared to \$102.6 million for the year ended December 31, 2017, which was an increase of approximately \$4.7 million, or 4.5%. The majority of the increase is related to a 4.1% increase in the weighted average monthly effective rent per occupied apartment unit to \$963 as of December 31, 2018 from \$925 as of December 31, 2017, as well as a 0.6% increase in occupancy.

Other income. Other income was \$16.3 million for the year ended December 31, 2018 compared to \$15.8 million for the year ended December 31, 2017, which was an increase of approximately \$0.5 million, or 2.8%. The majority of the increase is related to a \$0.4 million, or 9.6%, increase in administrative and application fees.

Expenses

Property operating expenses. Property operating expenses were \$31.5 million for the year ended December 31, 2018 compared to \$31.8 million for the year ended December 31, 2017, which was a decrease of approximately \$0.3 million, or 1.0%. The majority of the decrease is related to a \$0.8 million, or 8.8%, decrease in utility costs, partially offset by a \$0.3 million, or 2.5%, increase in labor costs.

Real estate taxes and insurance. Real estate taxes and insurance costs were \$16.3 million for the year ended December 31, 2018 compared to \$15.7 million for the year ended December 31, 2017, which was an increase of approximately \$0.6 million, or 3.7%. The majority of the increase is related to a \$0.4 million, or 3.2%, increase in property taxes.

Property management fees. Property management fees were \$3.7 million for the year ended December 31, 2018 compared to \$3.6 million for the year ended December 31, 2017, which was an increase of approximately \$0.1 million, or 4.3%. The majority of the increase is related to a \$4.7 million, or 4.5%, increase in rental income, and a \$0.5 million, or 2.8%, increase in other income, which the fee is primarily based on.

Property general and administrative expenses. Property general and administrative expenses were \$4.2 million for the year ended December 31, 2018 compared to \$4.1 million for the year ended December 31, 2017, which was an increase of approximately \$0.1 million, or 0.7%.

Net Operating Income for Our 2016-2018 Same Store and Non-Same Store Properties for the Years Ended December 31, 2018, 2017 and 2016

There are 25 properties encompassing 8,567 units of apartment space in our same store pool for the years ended December 31, 2018, 2017 and 2016 (our “2016-2018 Same Store” properties). Our 2016-2018 Same Store properties exclude the following 10 properties in our Portfolio as of December 31, 2018: Parc500, The Colonnade, Old Farm, Stone Creek at Old Farm, Hollister Place, Rockledge Apartments, Atera Apartments, Cedar Pointe, Crestmont Reserve and Brandywine I & II.

The following table reflects the revenues, property operating expenses and NOI for the years ended December 31, 2018, 2017 and 2016 for our 2016-2018 Same Store and Non-Same Store properties (dollars in thousands):

	For the Year Ended December 31,			2018 compared to 2017		2017 compared to 2016			
	2018	2017	2016	\$ Change	% Change	\$ Change	% Change		
Revenues									
Same Store									
Rental income	\$89,216	\$84,871	\$79,900	\$4,345	5.1 %	\$4,971	6.2 %		
Other income	13,403	13,270	11,947	133	1.0 %	1,323	11.1 %		
Same Store revenues	102,619	98,141	91,847	4,478	4.6 %	6,294	6.9 %		
Non-Same Store									
Rental income	38,748	40,152	35,519	(1,404)	-3.5 %	4,633	13.0 %		
Other income	5,230	5,942	5,482	(712)	-12.0 %	460	8.4 %		
Non-Same Store revenues	43,978	46,094	41,001	(2,116)	-4.6 %	5,093	12.4 %		
Total revenues	146,597	144,235	132,848	2,362	1.6 %	11,387	8.6 %		
Operating expenses									
Same Store									
Property operating expenses (1)	26,312	26,668	25,578	(356)	-1.3 %	1,090	4.3 %		
Real estate taxes and insurance	12,635	11,828	11,058	807	6.8 %	770	7.0 %		
Property management fees (2)	3,089	2,949	2,759	140	4.7 %	190	6.9 %		
Property general and administrative expenses (3)	3,447	3,451	3,359	(4)	-0.1 %	92	2.7 %		
Same Store operating expenses	45,483	44,896	42,754	587	1.3 %	2,142	5.0 %		
Non-Same Store									
Property operating expenses (4)	10,175	12,469	12,507	(2,294)	-18.4 %	(38)	-0.3 %		
Real estate taxes and insurance	8,078	7,333	5,004	745	10.2 %	2,329	46.5 %		
Property management fees (2)	1,293	1,381	1,224	(88)	-6.4 %	157	12.8 %		
Property general and administrative expenses (5)	1,393	1,578	1,639	(185)	-11.7 %	(61)	-3.7 %		
Non-Same Store operating expenses	20,939	22,761	20,374	(1,822)	-8.0 %	2,387	11.7 %		
Total operating expenses	66,422	67,657	63,128	(1,235)	-1.8 %	4,529	7.2 %		
NOI									
Same Store	57,136	53,245	49,093	3,891	7.3 %	4,152	8.5 %		
Non-Same Store	23,039	23,333	20,627	(294)	-1.3 %	2,706	13.1 %		
Total NOI	\$80,175	\$76,578	\$69,720	\$3,597	4.7 %	\$6,858	9.8 %		

(1)

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For the years ended December 31, 2018, 2017 and 2016, excludes approximately \$(664,000), \$(318,000) and \$56,000, respectively, of casualty-related expenses/(recoveries).

- (2) Fees incurred to an unaffiliated third party that is an affiliate of the noncontrolling limited partner of the OP.
- (3) For the years ended December 31, 2018, 2017 and 2016, excludes approximately \$853,000, \$760,000 and \$596,000, respectively, of expenses that are not reflective of the continuing operations of the properties or are incurred on our behalf at the property for expenses such as legal, professional and franchise tax fees.
- (4) For the years ended December 31, 2018, 2017 and 2016, excludes approximately \$1,000, \$31,000 and \$95,000, respectively, of casualty-related expenses.
- (5) For the years ended December 31, 2018, 2017 and 2016, excludes approximately \$441,000, \$370,000 and \$283,000, respectively, of expenses that are not reflective of the continuing operations of the properties or are incurred on our behalf at the property for expenses such as legal, professional and franchise tax fees.

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See reconciliation of net income (loss) to NOI below under “NOI and 2016-2018 Same Store NOI for the Years Ended December 31, 2018, 2017 and 2016.”

2016-2018 Same Store Results of Operations for the Years Ended December 31, 2018 and 2017

As of December 31, 2018, our 2016-2018 Same Store properties were approximately 94.7% leased with a weighted average monthly effective rent per occupied apartment unit of \$945. As of December 31, 2017, our 2016-2018 Same Store properties were approximately 94.0% leased with a weighted average monthly effective rent per occupied apartment unit of \$904. For our 2016-2018 Same Store properties, we recorded the following operating results for the year ended December 31, 2018 as compared to the year ended December 31, 2017:

Revenues

Rental income. Rental income was \$89.2 million for the year ended December 31, 2018 compared to \$84.9 million for the year ended December 31, 2017, which was an increase of approximately \$4.3 million, or 5.1%. The majority of the increase is related to a 4.5% increase in the weighted average monthly effective rent per occupied apartment unit to \$945 as of December 31, 2018 from \$904 as of December 31, 2017, as well as a 0.7% increase in occupancy.

Other income. Other income was \$13.4 million for the year ended December 31, 2018 compared to \$13.3 million for the year ended December 31, 2017, which was an increase of approximately \$0.1 million, or 1.0%. The majority of the increase is related to a \$0.3 million, or 8.1%, increase in administrative and application fees, partially offset by a \$0.1 million, or 2.0%, decrease in utility reimbursements.

Expenses

Property operating expenses. Property operating expenses were \$26.3 million for the year ended December 31, 2018 compared to \$26.7 million for the year ended December 31, 2017, which was a decrease of approximately \$0.4 million, or 1.3%. The majority of the decrease is related to a \$0.8 million, or 10.3%, decrease in utility costs, partially offset by a \$0.3 million, or 2.4%, increase in labor costs.

Real estate taxes and insurance. Real estate taxes and insurance costs were \$12.6 million for the year ended December 31, 2018 compared to \$11.8 million for the year ended December 31, 2017, which was an increase of approximately \$0.8 million, or 6.8%. The majority of the increase is related to a \$0.7 million, or 6.8%, increase in property taxes.

Property management fees. Property management fees were \$3.1 million for the year ended December 31, 2018 compared to \$2.9 million for the year ended December 31, 2017, which was an increase of approximately \$0.2 million, or 4.7%. The majority of the increase is related to a \$4.3 million, or 5.1%, increase in rental income, and a \$0.1 million, or 1.0%, increase in other income, which the fee is primarily based on.

Property general and administrative expenses. Property general and administrative expenses were \$3.4 million for the year ended December 31, 2018 compared to \$3.5 million for the year ended December 31, 2017, which was a decrease of approximately \$0.1 million, or 0.1%.

2016-2018 Same Store Results of Operations for the Years Ended December 31, 2017 and 2016

As of December 31, 2017, our 2016-2018 Same Store properties were approximately 94.0% leased with a weighted average monthly effective rent per occupied apartment unit of \$904. As of December 31, 2016, our 2016-2018 Same Store properties were approximately 93.7% leased with a weighted average monthly effective rent per occupied apartment unit of \$865. For our 2016-2018 Same Store properties, we recorded the following operating results for the

year ended December 31, 2017 as compared to the year ended December 31, 2016:

Revenues

Rental income. Rental income was \$84.9 million for the year ended December 31, 2017 compared to \$79.9 million for the year ended December 31, 2016, which was an increase of approximately \$5.0 million, or 6.2%. The majority of the increase is related to a 4.5% increase in the weighted average monthly effective rent per occupied apartment unit to \$904 as of December 31, 2017 from \$865 as of December 31, 2016, as well as a 0.3% increase in occupancy.

Other income. Other income was \$13.3 million for the year ended December 31, 2017 compared to \$11.9 million for the year ended December 31, 2016, which was an increase of approximately \$1.4 million, or 11.1%. The majority of the increase is related to a \$0.8 million, or 11.8%, increase in utility reimbursements and a \$0.4 million, or 77.1%, increase in other resident charges.

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Expenses

Property operating expenses. Property operating expenses were \$26.7 million for the year ended December 31, 2017 compared to \$25.6 million for the year ended December 31, 2016, which was an increase of approximately \$1.1 million, or 4.3%. The majority of the increase is related to a \$0.9 million, or 11.6%, increase in repairs and maintenance costs.

Real estate taxes and insurance. Real estate taxes and insurance costs were \$11.8 million for the year ended December 31, 2017 compared to \$11.1 million for the year ended December 31, 2016, which was an increase of approximately \$0.7 million, or 7.0%. The majority of the increase is related to a \$0.7 million, or 7.4%, increase in property taxes.

Property management fees. Property management fees were \$2.9 million for the year ended December 31, 2017 compared to \$2.8 million for the year ended December 31, 2016, which was an increase of approximately \$0.1 million, or 6.9%. The majority of the increase is related to a \$5.0 million, or 6.2%, increase in rental income, and a \$1.3 million, or 11.1%, increase in other income, which the fee is primarily based on.

Property general and administrative expenses. Property general and administrative expenses were \$3.5 million for the year ended December 31, 2017 compared to \$3.4 million for the year ended December 31, 2016, which was an increase of approximately \$0.1 million, or 2.7%.

NOI and 2017-2018 Same Store NOI for the Years Ended December 31, 2018 and 2017

The following table, which has not been adjusted for the effects of noncontrolling interests, reconciles our NOI and our 2017-2018 Same Store NOI for the years ended December 31, 2018 and 2017 to net income (loss), the most directly comparable GAAP financial measure (in thousands):

	For the Year Ended December 31,	
	2018	2017
Net income (loss)	\$(1,614)	\$56,359
Adjustments to reconcile net income (loss) to NOI:		
Advisory and administrative fees	7,474	7,419
Corporate general and administrative expenses	7,808	6,275
Casualty-related recoveries	(1) (663)	(287)
Property general and administrative expenses	(2) 1,294	1,130
Depreciation and amortization	47,470	48,752
Interest expense	28,572	29,576
Loss on extinguishment of debt and modification costs	3,576	5,719
Gain on sales of real estate	(13,742)	(78,365)
NOI	\$80,175	\$76,578
Less Non-Same Store		
Revenues	(23,012)	(25,765)
Operating expenses	10,744	12,433
Same Store NOI	\$67,907	\$63,246

(1) Adjustment to net income (loss) to exclude certain property operating expenses that are casualty-related recoveries.

(2) Adjustment to net income (loss) to exclude certain property general and administrative expenses that are not reflective of the continuing operations of the properties or are incurred on our behalf at the property for expenses such as legal, professional and franchise tax fees.

NOI and 2016-2018 Same Store NOI for the Years Ended December 31, 2018, 2017 and 2016

The following table, which has not been adjusted for the effects of noncontrolling interests, reconciles our NOI and our 2016-2018 Same Store NOI for the years ended December 31, 2018, 2017 and 2016 to net income (loss), the most directly comparable GAAP financial measure (in thousands):

	For the Year Ended December 31,		
	2018	2017	2016
Net income (loss)	\$(1,614)	\$56,359	\$25,888
Adjustments to reconcile net income (loss) to NOI:			
Advisory and administrative fees	7,474	7,419	6,802
Corporate general and administrative expenses	7,808	6,275	4,014
Casualty-related expenses/(recoveries)	(1) (663)	(287)	151
Property general and administrative expenses	(2) 1,294	1,130	879
Depreciation and amortization	47,470	48,752	35,643
Interest expense	28,572	29,576	20,167
Loss on extinguishment of debt and modification costs	3,576	5,719	1,722
Gain on sales of real estate	(13,742)	(78,365)	(25,932)
Acquisition costs	—	—	386
NOI	\$80,175	\$76,578	\$69,720
Less Non-Same Store			
Revenues	(43,978)	(46,094)	(41,001)
Operating expenses	20,939	22,761	20,374
Same Store NOI	\$57,136	\$53,245	\$49,093

(1) Adjustment to net income (loss) to exclude certain property operating expenses that are casualty-related expenses/(recoveries).

(2) Adjustment to net income (loss) to exclude certain property general and administrative expenses that are not reflective of the continuing operations of the properties or are incurred on our behalf at the property for expenses such as legal, professional and franchise tax fees.

FFO, Core FFO and AFFO

We believe that net income, as defined by GAAP, is the most appropriate earnings measure. We also believe that funds from operations (“FFO”), as defined by the National Association of Real Estate Investment Trusts (“NAREIT”), core funds from operations (“Core FFO”) and adjusted funds from operations (“AFFO”) are important non-GAAP supplemental measures of operating performance for a REIT.

Since the historical cost accounting convention used for real estate assets requires depreciation except on land, such accounting presentation implies that the value of real estate assets diminishes predictably over time. However, since real estate values have historically risen or fallen with market and other conditions, presentations of operating results for a REIT that use historical cost accounting for depreciation could be less informative. Thus, NAREIT created FFO as a supplemental measure of operating performance for REITs that excludes historical cost depreciation and amortization, among other items, from net income, as defined by GAAP. FFO is defined by NAREIT as net income computed in accordance with GAAP, excluding gains or losses from real estate dispositions, plus real estate depreciation and amortization and impairment charges. We compute FFO attributable to common stockholders in accordance with NAREIT’s definition. Our presentation differs slightly in that we begin with net income (loss) before adjusting for amounts attributable to (1) noncontrolling interests in consolidated joint ventures and (2) redeemable noncontrolling interests in the OP and we show the combined amounts attributable to such noncontrolling interests as an adjustment to arrive at FFO attributable to common stockholders.

Core FFO makes certain adjustments to FFO, which are either not likely to occur on a regular basis or are otherwise not representative of the ongoing operating performance of our portfolio. Core FFO adjusts FFO to remove items such as acquisition expenses, losses on extinguishment of debt and modification costs (including prepayment penalties and defeasance costs incurred on the early repayment of debt, the write-off of unamortized deferred financing costs and fair market value adjustments of assumed debt related to the early repayment of debt, costs incurred in a debt modification that are not capitalized as deferred financing costs and other costs incurred in a debt extinguishment), casualty-related expenses and recoveries, the amortization of deferred financing costs incurred in connection with obtaining short-term debt financing, the ineffective portion of fair value adjustments on interest rate derivatives designated as cash flow hedges (see Notes 2 and 7 to our consolidated financial statements), and the noncontrolling interests (as described above) related to these items. We believe Core FFO is useful to investors as a supplemental gauge of our operating performance and is useful in comparing our operating performance with other REITs that are not as involved in the aforementioned activities.

AFFO makes certain adjustments to Core FFO in order to arrive at a more refined measure of the operating performance of our portfolio. There is no industry standard definition of AFFO and practice is divergent across the industry. AFFO adjusts Core FFO to remove items such as equity-based compensation expense and the amortization of deferred financing costs incurred in connection with obtaining long-term debt financing, and the noncontrolling interests (as described above) related to these items. We believe AFFO is useful to investors as a supplemental gauge of our operating performance and is useful in comparing our operating performance with other REITs that are not as involved in the aforementioned activities.

The effect of the conversion of OP Units held by noncontrolling limited partners is not reflected in the computation of basic and diluted FFO, Core FFO and AFFO per share, as they are exchangeable for common stock on a one-for-one basis. The FFO, Core FFO and AFFO allocable to such units is allocated on this same basis and reflected in the adjustments for noncontrolling interests in the table below. As such, the assumed conversion of these units would have no net impact on the determination of diluted FFO, Core FFO and AFFO per share. See Note 9 to our consolidated financial statements for additional information.

We believe that the use of FFO, Core FFO and AFFO, combined with the required GAAP presentations, improves the understanding of operating results of REITs among investors and makes comparisons of operating results among such companies more meaningful. While FFO, Core FFO and AFFO are relevant and widely used measures of operating performance of REITs, they do not represent cash flows from operations or net income (loss) as defined by GAAP and should not be considered as an alternative or substitute to those measures in evaluating our liquidity or operating performance. FFO, Core FFO and AFFO do not purport to be indicative of cash available to fund our future cash requirements. Further, our computation of FFO, Core FFO and AFFO may not be comparable to FFO, Core FFO and AFFO reported by other REITs that do not define FFO in accordance with the current NAREIT definition or that interpret the current NAREIT definition or define Core FFO or AFFO differently than we do.

The following table reconciles our calculations of FFO, Core FFO and AFFO to net income (loss), the most directly comparable GAAP financial measure, for the years ended December 31, 2018, 2017 and 2016 (in thousands, except per share amounts):

	For the Year Ended December 31,		
	2018	2017	2016
Net income (loss)	\$(1,614)	\$56,359	\$25,888
Depreciation and amortization	47,470	48,752	35,643
Gain on sales of real estate	(13,742)	(78,365)	(25,932)
Adjustment for noncontrolling interests	(96)	(1,695)	(4,583)
FFO attributable to common stockholders	32,018	25,051	31,016
FFO per share - basic	\$1.51	\$1.19	\$1.46
FFO per share - diluted	\$1.48	\$1.17	\$1.46
Acquisition costs	—	—	386
Loss on extinguishment of debt and modification costs	3,576	5,719	1,722
Casualty-related expenses/(recoveries)	(663)	(287)	151
Change in fair value on derivative instruments - ineffective portion (1)	—	(309)	(1,683)
Amortization of deferred financing costs - acquisition term notes	159	403	—
Adjustment for noncontrolling interests	(9)	(430)	(107)
Core FFO attributable to common stockholders	35,081	30,147	31,485
Core FFO per share - basic	\$1.66	\$1.43	\$1.48
Core FFO per share - diluted	\$1.62	\$1.41	\$1.48
Amortization of deferred financing costs - long term debt	1,491	1,592	1,423
Equity-based compensation expense	4,198	3,109	825
Adjustment for noncontrolling interests	(17)	(76)	(140)
AFFO attributable to common stockholders	40,753	34,772	33,593
AFFO per share - basic	\$1.92	\$1.65	\$1.58
AFFO per share - diluted	\$1.88	\$1.62	\$1.58
Weighted average common shares outstanding - basic	21,189	21,057	21,232
Weighted average common shares outstanding - diluted	21,667	21,399	21,314
Dividends declared per common share	\$1.025	\$0.910	\$0.838
FFO Coverage - diluted	(2) 1.44x	1.29x	1.74x
Core FFO Coverage - diluted	(2) 1.58x	1.55x	1.76x
AFFO Coverage - diluted	(2) 1.84x	1.79x	1.88x

(1) Prior to our adoption of ASU 2017-12 on January 1, 2018, the ineffective portion of changes in the fair value of our derivatives designated as cash flow hedges was recognized directly in net income (loss) as interest expense. The adoption of ASU 2017-12 eliminates the separate measurement of effectiveness and ineffectiveness, and all changes in the fair value of derivatives that are designated as cash flow hedges are recorded directly in OCI. See Notes 2 and 7 to our consolidated financial statements for additional information.

(2)

Indicates coverage ratio of FFO/Core FFO/AFFO per common share (diluted) over dividends declared per common share during the period.

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The year ended December 31, 2018 as compared to the year ended December 31, 2017

FFO was \$32.0 million for the year ended December 31, 2018 compared to \$25.1 million for the year ended December 31, 2017, which was an increase of approximately \$6.9 million. The change in our FFO between the periods primarily relates to an increase in total revenues of \$2.4 million and decreases in total property operating expenses of \$1.4 million, interest expense of \$1.0 million and loss on extinguishment of debt and modification costs of \$2.1 million, partially offset by an increase in corporate general and administrative expenses of \$1.5 million and adjustments for amounts attributable to noncontrolling interests.

Core FFO was \$35.1 million for the year ended December 31, 2018 compared to \$30.1 million for the year ended December 31, 2017, which was an increase of approximately \$5.0 million. The change in our Core FFO between the periods primarily relates to an increase in FFO, partially offset by a decrease in loss on extinguishment of debt and modification costs of \$2.1 million and adjustments for amounts attributable to noncontrolling interests.

AFFO was \$40.8 million for the year ended December 31, 2018 compared to \$34.8 million for the year ended December 31, 2017, which was an increase of approximately \$6.0 million. The change in our AFFO between the periods primarily relates to increases in Core FFO and equity-based compensation expense of \$1.1 million.

The year ended December 31, 2017 as compared to the year ended December 31, 2016

FFO was \$25.1 million for the year ended December 31, 2017 compared to \$31.0 million for the year ended December 31, 2016, which was a decrease of approximately \$5.9 million. The change in our FFO between the periods primarily relates to increases in total property operating expenses of \$4.0 million, interest expense of \$9.4 million, loss on extinguishment of debt and modification costs of \$4.0 million and corporate general and administrative expenses of \$2.3 million, partially offset by an increase in total revenues of \$11.4 million and adjustments for amounts attributable to noncontrolling interests.

Core FFO was \$30.1 million for the year ended December 31, 2017 compared to \$31.5 million for the year ended December 31, 2016, which was a decrease of approximately \$1.4 million. The change in our Core FFO between the periods primarily relates to a decrease in FFO and a decrease in gain recognized related to the ineffective portion of changes in fair value of our interest rate swap derivatives designated as cash flow hedges of \$1.4 million, partially offset by an increase in loss on extinguishment of debt and modification costs of \$4.0 million and adjustments for amounts attributable to noncontrolling interests.

AFFO was \$34.8 million for the year ended December 31, 2017 compared to \$33.6 million for the year ended December 31, 2016, which was an increase of approximately \$1.2 million. The change in our AFFO between the periods primarily relates to an increase in equity-based compensation expense of \$2.3 million, partially offset by a decrease in Core FFO.

Liquidity and Capital Resources

Our short-term liquidity requirements consist primarily of funds necessary to pay for debt maturities, operating expenses and other expenditures directly associated with our multifamily properties, including:

- capital expenditures to continue our value-add program and to improve the quality and performance of our multifamily properties;
- interest expense and scheduled principal payments on outstanding indebtedness (see “—Obligations and Commitments” below);
- recurring maintenance necessary to maintain our multifamily properties;

- distributions necessary to qualify for taxation as a REIT;
- advisory and administrative fees payable to our Adviser;
- general and administrative expenses;
- reimbursements to our Adviser; and
- property management fees payable to BH.

We expect to meet our short-term liquidity requirements generally through net cash provided by operations and existing cash balances. As of December 31, 2018, we had approximately \$2.0 million of renovation value-add reserves for our planned capital expenditures to implement our value-add program. Renovation value-add reserves are not required to be held in escrow by a third party. We may reallocate these funds, at our discretion, to pursue other investment opportunities or meet our short-term liquidity requirements.

Our long-term liquidity requirements consist primarily of funds necessary to pay for the costs of acquiring additional multifamily properties, renovations and other capital expenditures to improve our multifamily properties and scheduled debt payments and distributions. We expect to meet our long-term liquidity requirements through various sources of capital, which may include a revolving credit facility and future debt or equity issuances, existing working capital, net cash provided by operations, long-term mortgage indebtedness and other secured and unsecured borrowings, and property dispositions. However, there are a number of factors that may have a material adverse effect on our ability to access these capital sources, including the state of overall equity and credit markets, our degree of leverage, our unencumbered asset base and borrowing restrictions imposed by lenders (including as a result of any failure to comply with financial covenants in our existing and future indebtedness), general market conditions for REITs, our operating performance and liquidity, market perceptions about us and restrictions on sales of properties under the Code. The success of our business strategy will depend, in part, on our ability to access these various capital sources.

In addition to our value-add program, our multifamily properties will require periodic capital expenditures and renovation to remain competitive. Also, acquisitions, redevelopments, or expansions of our multifamily properties will require significant capital outlays. Long-term, we may not be able to fund such capital improvements solely from net cash provided by operations because we must distribute annually at least 90% of our REIT taxable income, determined without regard to the deductions for dividends paid and excluding net capital gains, to qualify and maintain our qualification as a REIT, and we are subject to tax on any retained income and gains. As a result, our ability to fund capital expenditures, acquisitions, or redevelopment through retained earnings long-term is limited. Consequently, we expect to rely heavily upon the availability of debt or equity capital for these purposes. If we are unable to obtain the necessary capital on favorable terms, or at all, our financial condition, liquidity, results of operations, and prospects could be materially and adversely affected.

We believe that our available cash, expected operating cash flows, and potential debt or equity financings will provide sufficient funds for our operations, anticipated scheduled debt service payments and dividend requirements for the twelve-month period following December 31, 2018.

Cash Flows

The following table presents selected data from our consolidated statements of cash flows for the years ended December 31, 2018, 2017 and 2016 (in thousands):

	For the Year Ended December 31,		
	2018	2017	2016
Net cash provided by operating activities	\$41,743	\$37,506	\$33,776
Net cash provided by (used in) investing activities	(136,954)	2,324	(51,904)
Net cash provided by (used in) financing activities	95,092	(51,843)	10,294
Net decrease in cash, cash equivalents and restricted cash	(119)	(12,013)	(7,834)
Cash, cash equivalents and restricted cash, beginning of period	43,248	55,261	63,095
Cash, cash equivalents and restricted cash, end of period	\$43,129	\$43,248	\$55,261

The year ended December 31, 2018 as compared to the year ended December 31, 2017

Cash flows from operating activities. During the year ended December 31, 2018, net cash provided by operating activities was \$41.7 million compared to net cash provided by operating activities of \$37.5 million for the year ended December 31, 2017. The change in cash flows from operating activities was mainly due to an increase in total revenues, decreases in total property operating expenses, prepayment penalties and defeasance costs and debt modification and other extinguishment costs paid and changes in operating assets and liabilities.

Cash flows from investing activities. During the year ended December 31, 2018, net cash used in investing activities was \$137.0 million compared to net cash provided by investing activities of \$2.3 million for the year ended December 31, 2017. The change in cash flows from investing activities was mainly due to a decrease in net proceeds from sales of real estate. We sold one property for net proceeds of approximately \$29.6 million during the period in 2018; we sold nine properties for net proceeds of approximately \$224.4 million during the period in 2017. The change in cash flows from investing activities was partially offset by the acquisition of three properties for a combined purchase price of approximately \$131.0 million during the period in 2018 compared to the acquisition of three properties for a combined purchase price of approximately \$197.2 million during the period in 2017.

Cash flows from financing activities. During the year ended December 31, 2018, net cash provided by financing activities was \$95.1 million compared to net cash used in financing activities of \$51.8 million for the year ended December 31, 2017. The change in cash flows from financing activities was mainly due to receiving net proceeds of approximately \$84.8 million in the 2018 Offering and a net increase in debt of approximately \$14.1 million between the periods, partially offset by increases in common stock repurchases of approximately \$7.2 million and common stock dividends paid of approximately \$3.0 million between the periods and the \$51.7 million purchase amount of the purchase of 100% of the joint venture interests in our Portfolio owned by BH Equities, LLC

and its affiliates (collectively, “BH Equity”) (the “BH Buyout”) during the period in 2017 (see Note 10 to our consolidated financial statements).

The year ended December 31, 2017 as compared to the year ended December 31, 2016

Cash flows from operating activities. During the year ended December 31, 2017, net cash provided by operating activities was \$37.5 million compared to net cash provided by operating activities of \$33.8 million for the year ended December 31, 2016. The change in cash flows from operating activities was mainly due to an increase in total revenues, partially offset by increases in total property operating expenses, interest on debt, prepayment penalties and defeasance costs and debt modification and other extinguishment costs paid and changes in operating assets and liabilities.

Cash flows from investing activities. During the year ended December 31, 2017, net cash provided by investing activities was \$2.3 million compared to net cash used in investing activities of \$51.9 million for the year ended December 31, 2016. The change in cash flows from investing activities was mainly due to the acquisition of three properties for a combined purchase price of approximately \$197.2 million during the period in 2017, compared to the acquisition of four properties for a combined purchase price of approximately \$175.1 million during the period in 2016. The change in cash flows from investing activities was partially offset by an increase in net proceeds from sales of real estate; we sold nine properties for net proceeds of approximately \$224.4 million during the period in 2017, compared to selling seven properties for net proceeds of approximately \$131.8 million during the period in 2016.

Cash flows from financing activities. During the year ended December 31, 2017, net cash used in financing activities was \$51.8 million compared to net cash provided by financing activities of \$10.3 million for the year ended December 31, 2016. The change in cash flows from financing activities was mainly due to a net decrease in debt of approximately \$13.9 million between the periods and the \$51.7 million purchase amount of the BH Buyout during the period in 2017.

Debt, Derivatives and Hedging Activity

Mortgage Debt

As of December 31, 2018, our subsidiaries had aggregate mortgage debt outstanding to third parties of approximately \$845.7 million at a weighted average interest rate of 4.07% and an adjusted weighted average interest rate of 3.17%. For purposes of calculating the adjusted weighted average interest rate of our mortgage debt outstanding, we have included the weighted average fixed rate of 1.3388% for one-month LIBOR on our combined \$650.0 million notional amount of interest rate swap agreements, which effectively fix the interest rate on \$650.0 million of our floating rate mortgage debt. See Notes 6 and 7 to our consolidated financial statements for additional information.

We have entered into and expect to continue to enter into interest rate swap and cap agreements with various third parties to fix or cap the floating interest rates on a majority of our floating rate mortgage debt outstanding. The interest rate swap agreements generally have a term of four to five years and effectively establish a fixed interest rate on debt on the underlying notional amounts. The interest rate swap agreements involve the receipt of variable-rate amounts from a counterparty in exchange for us making fixed-rate payments over the life of the agreements without exchange of the underlying notional amount. As of December 31, 2018, interest rate swap agreements effectively covered \$650.0 million, or 80%, of our \$808.0 million of floating rate mortgage debt outstanding.

The interest rate cap agreements generally have a term of three to four years, cover the outstanding principal amount of the underlying debt and are generally required by our lenders. Under the interest rate cap agreements, we pay a fixed fee in exchange for the counterparty to pay any interest above a maximum rate. As of December 31, 2018,

interest rate cap agreements covered \$255.2 million of our \$808.0 million of floating rate mortgage debt outstanding. These interest rate cap agreements effectively cap one-month LIBOR on \$255.2 million of our floating rate mortgage debt at a weighted average rate of 5.82%.

Refinancings. During the year ended December 31, 2018, we refinanced mortgages on seven properties, as detailed in the table below (dollars in thousands). See Note 6 to our consolidated financial statements for additional information.

Property Name	Date of Refinance	Accounting Treatment	Write-off of Deferred Financing Costs (1)	Capitalized Deferred Financing Costs	Prepayment Penalties and Defeasance Costs (1)	Debt Modification and Other Extinguishments Costs (1)	Reduction in Spread (in basis points) (2)
Belmont at Duck Creek	6/1/2018	Extinguishment	\$ —	(3)\$ 293	\$ —	\$ —	79 (4)
Sabal Palm at Lake Buena Vista	8/20/2018	Extinguishment	228	442	371	—	51
Abbingtion Heights	8/21/2018	Extinguishment	—	105	446	202	4 (4)
Beechwood Terrace	8/31/2018	Extinguishment	405	100	202	196	24
Timber Creek	9/28/2018	Extinguishment	151	296	191	—	56
Radbourne Lake	9/28/2018	Extinguishment	144	266	189	—	52
Hollister Place	9/28/2018	Modification	—	141	135	87	