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NexPoint Residential Trust, Inc.
Form 10-Q
August 01, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2017

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)

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 and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted 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 and post such files). Yes No

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

Large Accelerated Filer

Accelerated Filer

Non-Accelerated Filer

(Do not check if a smaller reporting company)

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

As of August 1, 2017, the registrant had 21,043,669 shares of common stock, \$0.01 par value, outstanding.

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Quarter Ended June 30, 2017

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Cautionary Statement Regarding Forward-Looking Statements

This quarterly 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 quarterly 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;
- intense competition in the real estate market that, combined with low residential mortgage rates that could encourage potential renters to purchase residences rather than lease them, may limit our ability to acquire or lease and re-lease property or increase or maintain rent;
- risks associated with increases in interest rates and our ability to issue additional debt or equity securities in the future;
- failure of acquisitions to yield anticipated results;
- risks associated with our strategy of acquiring value-enhancement multifamily properties, which involves greater risks than more conservative investment strategies;
- the lack of experience of NexPoint Real Estate Advisors, L.P. (our "Adviser") in operating under the constraints imposed by real estate investment trust ("REIT") requirements;
- 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 Highland Capital Management, L.P. (our "Sponsor" or "Highland") or its affiliates;
- loss of key personnel of our Sponsor, our Adviser and our property manager;
- risks associated with our Adviser's ability to terminate the Advisory Agreement;
- our ability to change our major policies, operations and targeted investments without stockholder consent;
- the substantial fees and expenses we will pay to our Adviser and its affiliates;
- risks associated with the potential internalization of our management functions;
- the risk that we may compete with other entities affiliated with our Sponsor or property manager for tenants;
- conflicts of interest and competing demands for time faced by our Adviser, our Sponsor and their officers and employees;
- our dependence on information systems;

lack of or insufficient amounts of insurance;

- contingent or unknown liabilities related to properties or businesses that we have acquired or may acquire;

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

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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 compliance with various accessibility, environmental, building and health and safety laws and regulations, such as the ADA and FHA;

risks associated with our high concentrations of investments in the Southeastern and Southwestern United States;

risks associated with limited warranties we may obtain when purchasing properties;

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

risks associated with operating through joint ventures and funds;

potential reforms to Freddie Mac and Fannie Mae;

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;

risks associated with breaches of our data security;

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 risk that we may be unable to achieve some or all of the benefits that we expect to achieve from the Spin-Off (as defined below);

the risk that we may fail to consummate our pending property acquisitions;

failure to maintain our status as a REIT;

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;

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;

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 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;

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; or

any other risks included under Part I, Item 1A, “Risk Factors” of our annual report on Form 10-K, filed with the Securities and Exchange Commission on March 15, 2017.

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 quarterly 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 – FINANCIAL INFORMATION

Item 1. Financial Statements

NEXPOINT RESIDENTIAL TRUST, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share amounts)

	June 30, 2017 (Unaudited)	December 31, 2016
ASSETS		
Operating Real Estate Investments		
Land (including from VIEs of \$20,233 and \$99,803, respectively)	\$ 169,754	\$ 165,863
Buildings and improvements (including from VIEs of \$112,935 and \$425,945, respectively)	781,683	733,374
Intangible lease assets (including from VIEs of \$3,953 and \$3,926, respectively)	3,953	5,140
Construction in progress (including from VIEs of \$11 and \$1,891, respectively)	2,075	2,828
Furniture, fixtures, and equipment (including from VIEs of \$1,761 and \$21,289, respectively)	38,856	36,616
Total Gross Operating Real Estate Investments	996,321	943,821
Accumulated depreciation and amortization (including from VIEs of \$1,119 and \$32,053, respectively)	(70,729)	(60,214)
Total Net Operating Real Estate Investments	925,592	883,607
Real estate held for sale, net of accumulated depreciation of \$9,903 and \$6,099, respectively (including from VIEs of \$0 and \$60,578, respectively)	100,091	79,430
Total Net Real Estate Investments	1,025,683	963,037
Cash and cash equivalents (including from VIEs of \$314 and \$9,394, respectively)	26,254	22,705
Restricted cash (including from VIEs of \$1,181 and \$22,387, respectively)	29,447	32,556
Accounts receivable (including from VIEs of \$120 and \$2,009, respectively)	2,186	3,008
Prepaid and other assets (including from VIEs of \$193 and \$905, respectively)	3,070	1,678
Fair market value of interest rate swaps	11,941	12,413
TOTAL ASSETS	\$ 1,098,581	\$ 1,035,397
LIABILITIES AND EQUITY		
Mortgages payable, net (including from VIEs of \$81,052 and \$306,235, respectively)	\$ 711,752	\$ 367,453
Mortgages payable held for sale, net (including from VIEs of \$0 and \$47,421, respectively)	77,034	55,685
Credit facilities, net	29,764	310,492
Bridge facility, net	65,612	29,874
	4,956	5,551

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Accounts payable and other accrued liabilities (including from VIEs of \$103 and \$2,232, respectively)		
Accrued real estate taxes payable (including from VIEs of \$718 and \$2,724, respectively)	8,600	6,534
Accrued interest payable (including from VIEs of \$0 and \$855, respectively)	601	1,067
Security deposit liability (including from VIEs of \$154 and \$774, respectively)	1,464	1,364
Prepaid rents (including from VIEs of \$71 and \$728, respectively)	1,566	1,275
Obligation to issue operating partnership units (1)	2,000	—
Total Liabilities	903,349	779,295
NexPoint Residential Trust, Inc. stockholders' equity:		
Preferred stock, \$0.01 par value: 100,000,000 shares authorized; 0 shares issued	—	—
Common stock, \$0.01 par value: 500,000,000 shares authorized; 21,293,825 shares issued	213	213
Additional paid-in capital	211,729	241,450
Accumulated deficit	(20,242)	(14,584)
Accumulated other comprehensive income	8,119	9,052
Common stock held in treasury at cost; 250,156 shares	(4,587)	(4,587)
Noncontrolling interests	—	24,558
Total Equity	195,232	256,102
TOTAL LIABILITIES AND EQUITY	\$1,098,581	\$1,035,397

(1) Common units of the Company's operating partnership were issued on August 1, 2017 (see Notes 2 and 10).
See Notes to Consolidated Financial Statements

NEXPOINT RESIDENTIAL TRUST, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

AND COMPREHENSIVE INCOME

(in thousands, except per share amounts)

(Unaudited)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2017	2016	2017	2016
Revenues				
Rental income	\$ 30,508	\$ 29,404	\$ 62,416	\$ 58,774
Other income	4,726	4,253	9,809	8,394
Total revenues	35,234	33,657	72,225	67,168
Expenses				
Property operating expenses	9,665	9,691	19,536	19,073
Real estate taxes and insurance	5,093	4,090	10,058	8,353
Property management fees (1)	1,057	1,013	2,170	2,018
Advisory and administrative fees (2)	1,849	1,630	3,674	3,246
Corporate general and administrative expenses	1,886	844	3,219	1,626
Property general and administrative expenses	1,576	1,612	3,162	2,946
Depreciation and amortization	12,208	8,084	24,651	17,696
Total expenses	33,334	26,964	66,470	54,958
Operating income	1,900	6,693	5,755	12,210
Interest expense	(7,063)	(5,633)	(14,222)	(10,859)
Loss on extinguishment of debt and modification costs	(4,803)	(834)	(4,803)	(834)
Gain on sales of real estate	19,896	16,370	19,896	16,370
Net income	9,930	16,596	6,626	16,887
Net income attributable to noncontrolling interests	2,524	2,006	2,836	2,312
Net income attributable to common stockholders	\$ 7,406	\$ 14,590	\$ 3,790	\$ 14,575
Other comprehensive loss				
Unrealized losses on interest rate derivatives	(2,095)	(12)	(1,049)	(44)
Total comprehensive income	7,835	16,584	5,577	16,843
Comprehensive income attributable to noncontrolling interests	2,936	2,005	2,720	2,308
Comprehensive income attributable to common stockholders	\$ 4,899	\$ 14,579	\$ 2,857	\$ 14,535
Weighted average common shares outstanding - basic				
	21,044	21,294	21,044	21,294
Weighted average common shares outstanding - diluted				
	21,473	21,294	21,383	21,294
Earnings per share - basic (see Note 2)	\$ 0.35	\$ 0.69	\$ 0.18	\$ 0.68

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Earnings per share - diluted (see Note 2)	\$ 0.34	\$ 0.69	\$ 0.18	\$ 0.68
Dividends declared per common share	\$ 0.220	\$ 0.206	\$ 0.440	\$ 0.412

(1) Fees incurred to an unaffiliated third party that is an affiliate of the former noncontrolling interest members of the Company's joint ventures (see Notes 2 and 8).

(2) Fees incurred to the Company's adviser (see Notes 1 and 8).

See Notes to Consolidated Financial Statements

NEXPOINT RESIDENTIAL TRUST, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF EQUITY

(in thousands)

(Unaudited)

	Preferred Stock		Common Stock		Additional Paid-in Capital	Accumulated Deficit	Common Stock		Noncontrolling Interests	Total
	Number of Shares	Par Value	Number of Shares	Par Value			Other Comprehensive Income (Loss)	Held in Treasury at Cost		
Balances, December 31, 2016	—	\$ —	21,294	\$ 213	\$ 241,450	\$(14,584)	\$ 9,052	\$(4,587)	\$ 24,558	\$ 256,102
Contributions by noncontrolling interests					—	—	—	—	38	38
Purchase of noncontrolling interests					(31,313)	—	—	—	(22,527)	(53,840)
Vesting of stock-based compensation					1,592	—	—	—	—	1,592
Distributions / Dividends					—	(9,448)	—	—	(4,789)	(14,237)
Other comprehensive loss					—	—	(933)	—	(116)	(1,049)
Net income					—	3,790	—	—	2,836	6,626
Balances, June 30, 2017	—	\$ —	21,294	\$ 213	\$ 211,729	\$(20,242)	\$ 8,119	\$(4,587)	\$ —	\$ 195,232

See Notes to Consolidated Financial Statements

NEXPOINT RESIDENTIAL TRUST, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(Unaudited)

	For the Six Months Ended June 30,	
	2017	2016
Cash flows from operating activities		
Net income	\$6,626	\$16,887
Adjustments to reconcile net income to net cash provided by operating activities:		
Gain on sales of real estate	(19,896)	(16,370)
Depreciation and amortization	24,651	17,696
Amortization of deferred financing costs	1,357	983
Change in fair value on derivative instruments included in interest expense	812	6
Net cash paid for derivative settlements	(542)	—
Amortization of fair market value adjustment of assumed debt	(103)	(55)
Vesting of stock-based compensation	1,592	—
Changes in operating assets and liabilities, net of effects of acquisitions:		
Accounts receivable	930	339
Prepaid and other assets	(1,397)	(1,182)
Accounts payable and other accrued liabilities	197	(1,830)
Net cash provided by operating activities	14,227	16,474
Cash flows from investing activities		
Net proceeds from sales of real estate	82,736	63,220
Additions to real estate investments	(12,087)	(12,265)
Acquisitions of real estate investments	(138,106)	—
Net cash provided by (used in) investing activities	(67,457)	50,955
Cash flows from financing activities		
Mortgage proceeds received	583,713	—
Mortgage payments	(211,441)	(224,199)
Credit facilities proceeds received	25,000	200,000
Credit facilities payments	(310,000)	—
Bridge facility proceeds received	65,875	—
Bridge facility payments	(30,000)	(27,000)
Deferred financing costs paid	(3,742)	(2,538)
Purchase of common stock held in treasury	—	(88)
Dividends	(9,259)	—