

NATIONAL RETAIL PROPERTIES, INC.
Form 10-Q
August 01, 2017

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

FORM 10-Q

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

For the quarterly period ended 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 001-11290

NATIONAL RETAIL PROPERTIES, INC.

(Exact name of registrant as specified in its charter)

Maryland
(State or other jurisdiction of incorporation or organization) 56-1431377
(I.R.S. Employer Identification No.)

450 South Orange Avenue, Suite 900

Orlando, Florida 32801

(Address of principal executive offices, including zip code)

Registrant's telephone number, including area code: (407) 265-7348

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 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 website, 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 or a smaller reporting company. See definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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 Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practicable date.

149,233,141 shares of common stock, \$0.01 par value, outstanding as of July 28, 2017.

TABLE OF CONTENTS

	PAGE REFERENCE
Part I - Financial Information	
Item 1. <u>Financial Statements:</u>	
<u>Condensed Consolidated Balance Sheets</u>	<u>3</u>
<u>Condensed Consolidated Statements of Income and Comprehensive Income</u>	<u>4</u>
<u>Condensed Consolidated Statements of Cash Flows</u>	<u>6</u>
<u>Notes to Condensed Consolidated Financial Statements</u>	<u>8</u>
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	<u>17</u>
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>27</u>
Item 4. <u>Controls and Procedures</u>	<u>28</u>
Part II - Other Information	
Item 1. <u>Legal Proceedings</u>	<u>29</u>
Item 1A. <u>Risk Factors</u>	<u>29</u>
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>29</u>
Item 3. <u>Defaults Upon Senior Securities</u>	<u>29</u>
Item 4. <u>Mine Safety Disclosures</u>	<u>29</u>
Item 5. <u>Other Information</u>	<u>29</u>
Item 6. <u>Exhibits</u>	<u>29</u>
<u>Signatures</u>	<u>30</u>
<u>Exhibit Index</u>	<u>31</u>

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

NATIONAL RETAIL PROPERTIES, INC.
and SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(dollars in thousands, except per share data)

	June 30, 2017 (unaudited)	December 31, 2016
ASSETS		
Real estate portfolio:		
Accounted for using the operating method, net of accumulated depreciation and amortization	\$6,198,346	\$ 5,881,652
Accounted for using the direct financing method	10,091	11,230
Real estate held for sale	2,341	23,478
Cash and cash equivalents	4,450	294,540
Receivables, net of allowance of \$2,158 and \$1,006, respectively	2,208	3,418
Accrued rental income, net of allowance of \$3,078	25,688	25,101
Debt costs, net of accumulated amortization of \$11,966 and \$11,268, respectively	2,124	2,715
Other assets	91,880	92,017
Total assets	\$6,337,128	\$ 6,334,151
LIABILITIES AND EQUITY		
Liabilities:		
Line of credit payable	\$215,500	\$ —
Mortgages payable, including unamortized premium and net of unamortized debt costs	13,591	13,878
Notes payable, net of unamortized discount and unamortized debt costs	2,299,710	2,297,811
Accrued interest payable	19,921	19,665
Other liabilities	99,720	85,869
Total liabilities	2,648,442	2,417,223
Equity:		
Stockholders' equity:		
Preferred stock, \$0.01 par value. Authorized 15,000,000 shares		
6.625% Series D, 115,000 shares issued and outstanding at December 31, 2016, at stated liquidation value of \$2,500 per share	—	287,500
5.700% Series E, 115,000 shares issued and outstanding, at stated liquidation value of \$2,500 per share	287,500	287,500
5.200% Series F, 138,000 shares issued and outstanding, at stated liquidation value of \$2,500 per share	345,000	345,000
Common stock, \$0.01 par value. Authorized 375,000,000 shares; 149,206,493 and 147,149,945 shares issued and outstanding, respectively	1,493	1,473
Capital in excess of par value	3,415,807	3,322,771
Accumulated deficit	(352,626)	(319,254)
Accumulated other comprehensive income (loss)	(8,989)	(8,191)
Total stockholders' equity of NNN	3,688,185	3,916,799
Noncontrolling interests	501	129
Total equity	3,688,686	3,916,928
Total liabilities and equity	\$6,337,128	\$ 6,334,151
See accompanying notes to condensed consolidated financial statements.		

NATIONAL RETAIL PROPERTIES, INC.

and SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

(dollars in thousands, except per share data)

(Unaudited)

	Quarter Ended June		Six Months Ended	
	30,		June 30,	
	2017	2016	2017	2016
Revenues:				
Rental income from operating leases	\$ 141,298	\$ 126,418	\$ 277,791	\$ 248,063
Earned income from direct financing leases	246	347	502	703
Percentage rent	198	164	746	638
Real estate expense reimbursement from tenants	3,700	3,248	7,560	6,838
Interest and other income from real estate transactions	28	301	217	764
Interest income on commercial mortgage residual interests	80	448	165	901
	145,550	130,926	286,981	257,907
Operating expenses:				
General and administrative	8,820	8,735	17,739	17,984
Real estate	5,424	4,567	11,087	9,355
Depreciation and amortization	41,326	36,489	81,469	71,144
Impairment – commercial mortgage residual interests valuation	—	632	—	852
Impairment losses – real estate and other charges, net of recoveries	(39)	5,459	1,167	6,031
Retirement severance costs	7,428	—	7,428	—
	62,959	55,882	118,890	105,366
Earnings from operations	82,591	75,044	168,091	152,541
Other expenses (revenues):				
Interest and other income	(37)	(72)	(175)	(91)
Interest expense	27,274	24,081	53,888	47,667
Real estate acquisition costs	—	280	—	409
	27,237	24,289	53,713	47,985
Earnings before gain on disposition of real estate	55,354	50,755	114,378	104,556
Gain on disposition of real estate	3,055	1,178	17,679	18,053
Earnings including noncontrolling interests	58,409	51,933	132,057	122,609
Loss (earnings) attributable to noncontrolling interests	(381)	9	(372)	16
Net earnings attributable to NNN	\$ 58,028	\$ 51,942	\$ 131,685	\$ 122,625

See accompanying notes to condensed consolidated financial statements.

NATIONAL RETAIL PROPERTIES, INC.
and SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME -
CONTINUED

(dollars in thousands, except per share data)

(Unaudited)

	Quarter Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Net earnings attributable to NNN	\$58,028	\$ 51,942	\$131,685	\$ 122,625
Series D preferred stock dividends	—	(4,762)	(3,598)	(9,523)
Series E preferred stock dividends	(4,096)	(4,096)	(8,194)	(8,194)
Series F preferred stock dividends	(4,485)	—	(8,970)	—
Excess of redemption value over carrying value of Series D preferred shares redeemed	—	—	(9,855)	—
Net earnings attributable to common stockholders	\$49,447	\$ 43,084	\$101,068	\$ 104,908
Net earnings per share of common stock:				
Basic	\$0.33	\$ 0.30	\$0.68	\$ 0.74
Diluted	\$0.33	\$ 0.30	\$0.68	\$ 0.73
Weighted average number of common shares outstanding:				
Basic	148,372,501	143,443,375	147,655,076	142,141,990
Diluted	148,719,470	143,976,712	148,023,668	142,693,785
Other comprehensive income:				
Net earnings attributable to NNN	\$58,028	\$ 51,942	\$131,685	\$ 122,625
Amortization of interest rate hedges	455	707	903	1,402
Fair value forward starting swaps	(1,140)	312	(1,694)	312
Net gain – commercial mortgage residual interests	—	282	—	107
Net gain (loss) – available-for-sale securities	(81)	379	(7)	553
Comprehensive income attributable to NNN	\$57,262	\$ 53,622	\$130,887	\$ 124,999

See accompanying notes to condensed consolidated financial statements.

NATIONAL RETAIL PROPERTIES, INC.
and SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(dollars in thousands)
(Unaudited)

	Six Months Ended June 30,	
	2017	2016
Cash flows from operating activities:		
Earnings including noncontrolling interests	\$ 132,057	\$ 122,609
Adjustments to reconcile earnings including noncontrolling interests to net cash provided by operating activities:		
Depreciation and amortization	81,469	71,144
Impairment losses – real estate and other charges, net of recoveries	1,167	6,031
Impairment – commercial mortgage residual interests valuation	—	852
Amortization of notes payable discount	878	683
Amortization of debt costs	1,727	1,513
Amortization of mortgages payable premium	(42)	(89)
Amortization of deferred interest rate hedges	903	1,402
Gain on disposition of real estate	(17,679)	(18,053)
Performance incentive plan expense	10,204	5,804
Performance incentive plan payment	(862)	(581)
Change in operating assets and liabilities, net of assets acquired and liabilities assumed in business combinations:		
Decrease in real estate leased to others using the direct financing method	443	692
Decrease in receivables	1,210	1,139
Increase in accrued rental income	(904)	(157)
Decrease in other assets	858	136
Increase (decrease) in accrued interest payable	256	(975)
Increase (decrease) in other liabilities	3,428	(3,971)
Other	(42)	(531)
Net cash provided by operating activities	215,071	187,648
Cash flows from investing activities:		
Proceeds from the disposition of real estate	48,595	73,066
Additions to real estate:		
Accounted for using the operating method	(398,963)	(485,573)
Principal payments on mortgages and notes receivable	—	123
Other	(431)	(1,812)
Net cash used in investing activities	(350,799)	(414,196)

See accompanying notes to condensed consolidated financial statements.

NATIONAL RETAIL PROPERTIES, INC.
and SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS - CONTINUED
(dollars in thousands)
(Unaudited)

	Six Months Ended	
	June 30,	
	2017	2016
Cash flows from financing activities:		
Proceeds from line of credit payable	\$705,200	\$598,500
Repayment of line of credit payable	(489,700)	(451,200)
Repayment of mortgages payable	(253)	(6,990)
Payment of debt costs	(172)	(159)
Proceeds from issuance of common stock	74,503	219,448
Stock issuance costs	(1,238)	(3,379)
Redemption of Series D preferred stock	(287,500)	—
Payment of Series D preferred stock dividends	(3,598)	(9,523)
Payment of Series E preferred stock dividends	(8,194)	(8,194)
Payment of Series F preferred stock dividends	(8,970)	—
Payment of common stock dividends	(134,440)	(123,602)
Net cash provided by (used in) financing activities	(154,362)	214,901
Net decrease in cash, cash equivalents and restricted cash	(290,090)	(11,647)
Cash, cash equivalents and restricted cash at beginning of period ⁽¹⁾	294,540	14,260
Cash, cash equivalents and restricted cash at end of period ⁽¹⁾	\$4,450	\$2,613
Supplemental disclosure of cash flow information:		
Interest paid, net of amount capitalized	\$51,279	\$45,960
Taxes received	\$(3)	\$—
Supplemental disclosure of noncash investing and financing activities:		
Change in other comprehensive income	\$798	\$2,374
Change in lease classification (direct financing lease to operating lease)	\$696	\$—

⁽¹⁾ Cash, cash equivalents and restricted cash at the end of the period is the aggregate of Cash and cash equivalents and Restricted cash and cash held in escrow from the Consolidated Balance Sheets. NNN had no restricted cash and cash held in escrow at June 30, 2017 and \$242 at June 30, 2016.

See accompanying notes to condensed consolidated financial statements.

NATIONAL RETAIL PROPERTIES, INC.
and SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2017
(Unaudited)

Note 1 – Organization and Summary of Significant Accounting Policies:

Organization and Nature of Business – National Retail Properties, Inc., a Maryland corporation, is a fully integrated real estate investment trust (“REIT”) formed in 1984. The terms “NNN” or the “Company” refer to National Retail Properties, Inc. and all of its consolidated subsidiaries.

NNN's assets primarily include real estate assets. NNN acquires, owns, invests in and develops properties that are leased primarily to retail tenants under long-term net leases and primarily held for investment (“Properties”, “Property Portfolio”, or individually a “Property”).

	June 30, 2017
Property Portfolio:	
Total properties	2,675
Gross leasable area (square feet)	28,102,000
States	48
Weighted average remaining lease term (years)	11.5

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and do not include all of the information and note disclosures required by U.S. generally accepted accounting principles (“GAAP”). The unaudited condensed consolidated financial statements reflect all adjustments (including normal recurring accruals) which are, in the opinion of management, necessary for a fair presentation of the results for the interim periods presented. Operating results for the quarter and six months ended June 30, 2017, may not be indicative of the results that may be expected for the year ending December 31, 2017.

Amounts as of December 31, 2016, included in the condensed consolidated financial statements have been derived from the audited consolidated financial statements as of that date. The unaudited condensed consolidated financial statements, included herein, should be read in conjunction with the consolidated financial statements and notes thereto as well as Management's Discussion and Analysis of Financial Condition and Results of Operations in NNN's Form 10-K for the year ended December 31, 2016.

Principles of Consolidation – NNN’s condensed consolidated financial statements include the accounts of each of the respective majority owned and controlled affiliates, including transactions whereby NNN has been determined to be the primary beneficiary in accordance with the Financial Accounting Standards Board (“FASB”) guidance included in Consolidation. All significant intercompany account balances and transactions have been eliminated.

Real Estate Portfolio – NNN records the acquisition of real estate at cost, including acquisition and closing costs. The cost of properties developed by NNN includes direct and indirect costs of construction, property taxes, interest and other miscellaneous costs incurred during the development period until the project is substantially complete and available for occupancy. NNN recorded \$1,113,000 and \$827,000 in capitalized interest during the development period for the six months ended June 30, 2017 and 2016, respectively, of which \$560,000 and \$316,000 was recorded during the quarters ended June 30, 2017 and 2016, respectively.

Purchase Accounting for Acquisition of Real Estate Subject to a Lease – In accordance with the FASB guidance on business combinations, the fair value of the real estate acquired with in-place leases is allocated to the acquired tangible assets, consisting of land, building and tenant improvements, and identified intangible assets and liabilities, consisting of the value of above-market and below-market leases and the value of in-place leases, as applicable, based on their respective fair values. Acquisition costs incurred in connection with a business combination are expensed when incurred.

The fair value of the tangible assets of an acquired leased property is determined by valuing the property as if it were vacant, and the “as-if-vacant” value is then allocated to land, building and tenant improvements based on the

determination of their fair values.

In allocating the fair value of the identified intangible assets and liabilities of an acquired property, above-market and below-market in-place lease values are recorded as other assets or liabilities based on the present value (using an interest rate which reflects the risks associated with the leases acquired) of the difference between (i) the contractual amounts to be paid pursuant to the in-place leases, and (ii) management's estimate of fair market lease rates for the corresponding in-place leases, measured

8

over a period equal to the remaining term of the lease and the applicable option terms if it is probable that the tenant will exercise options. The capitalized above-market lease values are amortized as a reduction of rental income over the remaining terms of the respective leases. The capitalized below-market lease values are amortized as an increase to rental income over the initial term unless the Company believes that it is likely that the tenant will renew the lease for an option term whereby the Company amortizes the value attributable to the renewal over the renewal period.

The aggregate value of other acquired intangible assets, consisting of in-place leases, is measured by the excess of (i) the purchase price paid for a property after adjusting existing in-place leases to market rental rates over (ii) the estimated fair value of the property as-if-vacant, determined as set forth above. The value of in-place leases exclusive of the value of above-market and below-market in-place leases is amortized to expense over the remaining non-cancelable periods of the respective leases. If a lease were to be terminated prior to its stated expiration, all unamortized amounts relating to that lease would be written off in that period. The value of tenant relationships is reviewed on individual transactions to determine if future value was derived from the acquisition.

Intangible assets and liabilities consisted of the following as of (dollars in thousands):

	June 30, December 31,	
	2017	2016
Intangible lease assets (included in Other assets):		
Value of above-market in-place leases, net	\$ 8,091	\$ 9,591
Value of in-place leases, net	54,155	55,290
Intangible lease liabilities (included in Other liabilities):		
Value of below-market in-place leases, net	20,694	22,100

Debt Costs – Line of Credit Payable – Debt costs incurred in connection with NNN’s \$650,000,000 line of credit have been deferred and are being amortized to interest expense over the term of the loan commitment using the straight-line method, which approximates the effective interest method. NNN has recorded debt costs associated with the line of credit as an asset, in Debt costs on the Condensed Consolidated Balance Sheets.

Debt Costs – Mortgages Payable – Debt costs incurred in connection with NNN’s mortgages payable have been deferred and are being amortized over the term of the respective loan commitment using the straight-line method, which approximates the effective interest method. These costs of \$147,000 at June 30, 2017 and December 31, 2016, are included in Mortgages payable on the Condensed Consolidated Balance Sheets net of accumulated amortization of \$46,000 and \$38,000, respectively.

Debt Costs – Notes Payable – Debt costs incurred in connection with the issuance of NNN’s notes payable have been deferred and are being amortized to interest expense over the term of the respective debt obligation using the effective interest method. These costs of \$21,157,000 at June 30, 2017 and December 31, 2016, are included in Notes payable on the Condensed Consolidated Balance Sheets net of accumulated amortization of \$7,397,000 and \$6,376,000, respectively.

Earnings Per Share – Earnings per share have been computed pursuant to the FASB guidance included in Earnings Per Share. The guidance requires classification of the Company’s unvested restricted share units, which carry rights to receive nonforfeitable dividends, as participating securities requiring the two-class method of computing earnings per share. Under the two-class method, earnings per common share are computed by dividing the sum of distributed earnings to common stockholders and undistributed earnings allocated to common stockholders by the weighted average number of common shares outstanding for the period. In applying the two-class method, undistributed earnings are allocated to both common shares and participating securities based on the weighted average shares outstanding during the period.

The following table is a reconciliation of the numerator and denominator used in the computation of basic and diluted earnings per common share using the two-class method (dollars in thousands):

	Quarter Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Basic and Diluted Earnings:				
Net earnings attributable to NNN	\$58,028	\$ 51,942	\$131,685	\$ 122,625
Less: Series D preferred stock dividends	—	(4,762)	(3,598)	(9,523)
Less: Series E preferred stock dividends	(4,096)	(4,096)	(8,194)	(8,194)
Less: Series F preferred stock dividends	(4,485)	—	(8,970)	—
Less: Excess of redemption value over carrying value of Series D preferred shares redeemed	—	—	(9,855)	—
Net earnings available to NNN's common stockholders	49,447	43,084	101,068	104,908
Less: Earnings allocated to unvested restricted shares	(137)	(177)	(267)	(326)
Net earnings used in basic and diluted earnings per share	\$49,310	\$ 42,907	\$100,801	\$ 104,582
Basic and Diluted Weighted Average Shares Outstanding:				
Weighted average number of shares outstanding	149,119,191	144,315,093	148,354,604	142,946,299
Less: Unvested restricted stock	(301,206)	(406,170)	(293,588)	(374,701)
Less: Unvested contingent restricted shares	(445,484)	(465,548)	(405,940)	(429,608)
Weighted average number of shares outstanding used in basic earnings per share	148,372,501	143,443,375	147,655,076	142,141,990
Other dilutive securities	346,969	533,337	368,592	551,795
Weighted average number of shares outstanding used in diluted earnings per share	148,719,470	143,976,712	148,023,668	142,693,785

Fair Value Measurement – NNN's estimates of fair value of financial and non-financial assets and liabilities are based on the framework established in the fair value accounting guidance. The framework specifies a hierarchy of valuation inputs which was established to increase consistency, clarity and comparability in fair value measurements and related disclosures. The guidance describes a fair value hierarchy based upon three levels of inputs that may be used to measure fair value, two of which are considered observable and one that is considered unobservable. The following describes the three levels:

Level 1 – Valuation is based upon quoted prices in active markets for identical assets or liabilities.

Level 2 – Valuation is based upon inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 – Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include option pricing models, discounted cash flow models and similar techniques.

Accumulated Other Comprehensive Income (Loss) – The following table outlines the changes in accumulated other comprehensive income (loss) (dollars in thousands):

	Gains or (Losses) on Cash Flow Hedges (1)	Gains on Available-for-Sale Securities	Total
Beginning balance, December 31, 2016	\$(8,899)	\$ 708	\$(8,191)
Other comprehensive income (loss)	(1,694)	(7)	(1,701)
Reclassifications from accumulated other comprehensive income to net earnings	903	(2) —	903
Net current period other comprehensive income (loss)	(791)	(7)	(798)
Ending balance, June 30, 2017	\$(9,690)	\$ 701	\$(8,989)

(1) Additional disclosure is included in Note 5 – Derivatives.

(2) Reclassifications out of other comprehensive income (loss) are recorded in Interest expense on the Condensed Consolidated Statements of Income and Comprehensive Income.

New Accounting Pronouncements – In May 2014, the FASB issued ASU 2014-09, “Revenue from Contracts with Customers (Topic 606). The core principle of ASU 2014-09, is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Certain contracts are excluded from ASU 2014-09, including lease contracts within the scope of the FASB guidance included in Leases. In March 2016, the FASB issued updated guidance. ASU 2016-08, "Revenue from Contracts with customers (Topic 606) - Principal versus Agent Considerations (Reporting Gross Versus Net)," clarifies the implementation guidance on principal versus agent considerations included within the scope of ASU 2014-09. In February 2017, the FASB issued ASU 2017-05, "Other Income - Gains and Losses from the Derecognition of Nonfinancial Assets (Subtopic 610-20)," which clarifies the scope of subtopic 610-20, which was issued as a part of ASU 2014-09, to add guidance for partial sales of nonfinancial assets. The guidance permits two methods of adoption: full retrospective approach to each prior reporting period presented, or modified retrospective approach with the cumulative effect of initially applying the guidance recognized at the date of initial application (the cumulative catch-up transition method). The guidance was initially effective January 1, 2017, and early adoption was not permitted. The amended guidance provides for a one-year deferral of the effective date to January 1, 2018, with an option of applying the standard on the original effective date. NNN will adopt the guidance on January 1, 2018, and apply the cumulative catch-up transition method. NNN is currently evaluating to determine the potential impact the adoption of ASU 2014-09 and ASU 2016-08 will have on its financial position and results of operations.

In February 2016, the FASB issued ASU 2016-02, "Leases (Topic 842)," effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The FASB issued final guidance that requires lessees to put most leases on their balance sheets but recognize expenses in the income statement in a manner similar to today’s accounting. The guidance also eliminates today’s real estate-specific provisions and changes the guidance on sale-leaseback transactions, initial direct costs and lease executory costs for all entities. For lessors, the standard modifies the classification criteria and the accounting for sales-type and direct financing leases. NNN is currently evaluating to determine the potential impact the adoption of ASU 2016-02 will have on its financial position or results of operations.

In August 2016, the FASB issued ASU 2016-15, "Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments," effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. The amendments in this update provide guidance on certain cash flow classification issues. The objective of the amendment is to reduce existing diversity in practice in how certain cash receipts and cash payments are presented and classified in the statement of cash flows under Topic 230. The adoption of ASU 2016-15

will not impact NNN's financial position or results of operations.

In May 2017, the FASB issued ASU 2017-09, "Compensation - Stock Compensation (Topic 718): Scope of Modification Accounting," effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2017. The amendments in this update provide guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718. NNN has early adopted ASU 2017-09. The adoption of ASU 2017-09 will not impact NNN's financial position or results of operations.

Use of Estimates – Management of NNN has made a number of estimates and assumptions relating to the reporting of assets and liabilities, revenues and expenses and the disclosure of contingent assets and liabilities to prepare these condensed

consolidated financial statements in conformity with GAAP. Significant estimates include provisions for impairment and allowances for certain assets, accruals, useful lives of assets and purchase price allocation. Actual results could differ from those estimates.

Note 2 – Real Estate:

Real Estate – Portfolio

Leases – The following outlines key information for NNN’s leases:

	June 30, 2017
Lease classification:	
Operating	2,713
Direct financing	7
Building portion – direct financing/land portion – operating	
Weighted average remaining lease term (years)	11.5

The leases generally provide for limited increases in rent as a result of fixed increases, increases in the consumer price index, and/or increases in the tenant’s sales volume. Generally, the tenant is also required to pay all property taxes and assessments, substantially maintain the Property and carry property and liability insurance coverage. Certain Properties are subject to leases under which NNN retains responsibility for specific costs and expenses of the Property. Generally, the leases provide the tenant with one or more multi-year renewal options, subject to generally the same terms and conditions of the base term of the lease, including rent increases.

Real Estate Portfolio – Accounted for Using the Operating Method – Real estate subject to operating leases consisted of the following as of (dollars in thousands):

	June 30, 2017	December 31, 2016
Land and improvements	\$2,197,287	\$ 2,103,233
Buildings and improvements	4,785,858	4,489,159
Leasehold interests	5,261	4,565
	6,988,406	6,596,957
Less accumulated depreciation and amortization	(810,460)	(739,362)
	6,177,946	5,857,595
Work in progress	20,400	24,057
	\$6,198,346	\$ 5,881,652

Real Estate – Held For Sale

On a quarterly basis, the Company evaluates its Properties for held for sale classification based on specific criteria as outlined in ASC 360, Property, Plant & Equipment, including management’s intent to commit to a plan to sell the asset. NNN anticipates the disposition of Properties classified as held for sales to occur within 12 months. As of June 30, 2017, NNN had four of its Properties categorized as held for sale. NNN’s real estate held for sale at December 31, 2016, included 18 Properties, 14 of which were sold in 2017. Real estate held for sale consisted of the following as of (dollars in thousands):

	June 30, 2017	December 31, 2016
Land and improvements	\$1,259	\$ 13,796
Building and improvements	1,603	15,535
	2,862	29,331
Less accumulated depreciation and amortization	(521)	(3,105)
Less impairment	—	(2,748)
	\$2,341	\$ 23,478

Real Estate – Dispositions

The following table summarizes the Properties sold and the corresponding gain recognized on the disposition of Properties (dollars in thousands):

	Quarter Ended June 30,				Six Months Ended June 30,			
	2017		2016		2017		2016	
	# of Sold Properties	Gain	# of Sold Properties	Gain	# of Sold Properties	Gain	# of Sold Properties	Gain
Gain on disposition of real estate	8	\$3,055	7	\$1,178	25	\$17,679	17	\$18,053

Real Estate – Commitments

NNN has committed to fund construction commitments on 22 Properties. The improvements are estimated to be completed within 12 months. These construction commitments, as of June 30, 2017, are outlined in the table below (dollars in thousands):

Total commitment ⁽¹⁾	\$126,634
Amount funded	48,304
Remaining commitment	78,330

⁽¹⁾ Includes land, construction costs, tenant improvements and lease costs.

Real Estate – Impairments

Management periodically assesses its real estate for possible impairment whenever certain events or changes in circumstances indicate that the carrying amount of the asset, including accrued rental income, may not be recoverable through operations. Events or circumstances that may occur include significant changes in real estate market conditions and the ability of NNN to re-lease or sell properties that are vacant or become vacant in a reasonable period of time. Impairments are measured as the amount by which the current book value of the asset exceeds the estimated fair value of the asset. As a result of the Company's review of long-lived assets, including identifiable intangible assets, NNN recognized real estate impairments, net of recoveries of \$1,167,000 and \$2,762,000 for the six months ended June 30, 2017 and 2016, respectively, of which (\$39,000) and \$2,190,000 was recorded during the quarters ended June 30, 2017 and 2016, respectively.

The valuation of impaired assets is determined using widely accepted valuation techniques including discounted cash flow analysis, income capitalization, analysis of recent comparable sales transactions, actual sales negotiations and bona fide purchase offers received from third parties, which are Level 3 inputs. NNN may consider a single valuation technique or multiple valuation techniques, as appropriate, when estimating the fair value of its real estate.

Note 3 – Line of Credit Payable:

NNN's \$650,000,000 unsecured revolving credit facility (the "Credit Facility") had a weighted average outstanding balance of \$69,100,000 and a weighted average interest rate of 2.0% during the six months ended June 30, 2017. The Credit Facility matures January 2019, unless the Company exercises its option to extend maturity to January 2020. The Credit Facility bears interest at LIBOR plus 92.5 basis points; however, such interest rate may change pursuant to a tiered interest rate structure based on NNN's debt rating. The Credit Facility also includes an accordion feature to increase the facility size up to \$1,000,000,000, subject to lender approval. As of June 30, 2017, there was \$215,500,000 outstanding balance and \$434,500,000 was available for future borrowings under the Credit Facility, excluding undrawn letters of credit totaling \$230,000.

Note 4 – Stockholders' Equity:

In February 2015, NNN filed a shelf registration statement with the Securities and Exchange Commission (the "Commission") which permits the issuance by NNN of an indeterminate amount of debt and equity securities.

Dividend Reinvestment and Stock Purchase Plan – In February 2015, NNN filed a shelf registration statement with the Commission for its Dividend Reinvestment and Stock Purchase Plan ("DRIP") which permits the issuance by NNN of up to 16,000,000 shares of common stock. The following table outlines the common stock issuances pursuant to NNN's DRIP (dollars in thousands):

	Six Months Ended June 30,	
	2017	2016
Shares of common stock	34,466	149,543
Net proceeds	\$ 1,413	\$ 6,609

At-The-Market Offerings – NNN has established an at-the-market equity program ("ATM") which allows NNN to sell shares of common stock from time to time. The following outlines NNN's ATM programs:

	2016 ATM	2015 ATM
Established date	March 2016	February 2015
Termination date	March 2019	March 2016
Total allowable shares	12,000,000	10,000,000
Total shares issued as of June 30, 2017	5,876,445	9,852,465

The following table outlines the common stock issuances pursuant to NNN's ATM equity programs (dollars in thousands, except per share data):

	Six Months Ended June 30,	
	2017	2016
Shares of common stock	1,653,155	4,613,422
Average price per share (net)	\$43.64	\$45.46
Net proceeds	\$72,139	\$209,722
Stock issuance costs ⁽¹⁾	\$1,183	\$3,379

⁽¹⁾ Stock issuance costs consist primarily of underwriters' fees and commissions, and legal and accounting fees.

Dividends – The following table outlines the dividends declared and paid for each issuance of NNN's stock (dollars in thousands, except per share data):

	Quarter Ended June 30, 2017	Six Months Ended June 30, 2017 2016	
Series D preferred stock ⁽¹⁾ :			
Dividends	\$4,762	\$3,598	\$9,523
Per depositary share	—0.414063	0.312840	0.828125

Series E preferred stock ⁽²⁾ :			
Dividends	4,00696	8,194	8,194
Per depositary share	0.35626050	0.712500	0.712500

Series F preferred stock ⁽³⁾ :			
Dividends	4,485	8,970	—
Per depositary share	0.325000	0.650000	—

Common stock:			
Dividends	67,66051	134,440	123,602
Per share	0.45335	0.910	0.870

⁽¹⁾ The Series D preferred stock was redeemed in February 2017. The dividends paid in 2017 included accumulated and unpaid dividends through the redemption date.

⁽²⁾ The Series E preferred stock has no maturity date and will remain outstanding unless redeemed by NNN. The earliest redemption date for the Series E Preferred Stock is May 2018.

⁽³⁾ The Series F preferred stock was issued in October 2016 and has no maturity date and will remain outstanding unless redeemed by NNN. The earliest redemption date for the Series F preferred stock is October 2021.

In July 2017, NNN declared a dividend of \$0.475 per share, which is payable in August 2017 to its common stockholders of record as of July 31, 2017.

Note 5 – Derivatives:

In accordance with the guidance on derivatives and hedging, NNN records all derivatives on the balance sheet at fair value. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative and the resulting designation. Derivatives used to hedge the exposure to changes in the fair value of an asset, liability, or a firm commitment attributable to a particular risk, such as interest rate risk, are considered fair value hedges. Derivatives used to hedge the exposure to variability in expected future cash flows, or other types of forecasted transactions, are considered cash flow hedges.

NNN's objective in using derivatives is to add stability to interest expense and to manage its exposure to interest rate movements or other identified risks. To accomplish this objective, NNN primarily uses treasury locks, forward swaps and interest rate swaps as part of its cash flow hedging strategy. Treasury locks and forward starting swaps are used to hedge forecasted debt issuances. Treasury locks designated as cash flow hedges lock in the yield/price of a treasury security. Forward swaps also lock the associated swap spread. Interest rate swaps designated as cash flow hedges are used to hedge the variable cash flows associated with floating rate debt and involve the receipt or payment of variable rate amounts in exchange for fixed-rate payments over the life of the agreements without exchange of the underlying principal amount.

For derivatives designated as cash flow hedges, the effective portion of changes in the fair value of the derivative is initially reported in other comprehensive income (outside of earnings) and subsequently reclassified to earnings when the hedged transaction affects earnings, and the ineffective portion of changes in the fair value of the derivative is recognized directly in earnings.

NNN discontinues hedge accounting prospectively when it is determined that the derivative is no longer effective in offsetting changes in the cash flows of the hedged item, the derivative expires or is sold, terminated or exercised, the derivative is re-designated as a hedging instrument or management determines that designation of the derivative as a hedging instrument is no longer appropriate.

When hedge accounting is discontinued, NNN recognizes any changes in its fair value in earnings and continues to carry the derivative on the balance sheet or may choose to settle the derivative at that time with a cash payment or receipt.

The following table outlines NNN's derivatives which were hedging the risk of changes in forecasted interest payments on forecasted issuance of long-term debt (dollars in thousands):

Terminated	Description	Aggregate Notional Amount	Liability	Fair Value
			(Asset) Value When Terminated	Fair Deferred In Other Comprehensive Income ⁽¹⁾
September 2007	Two treasury locks	\$ 100,000	\$ 3,260	\$ 3,228
June 2011	Two treasury locks	150,000	5,300	5,218
April 2013	Four forward starting swaps	240,000	3,156	3,141
May 2014	Three forward starting swaps	225,000	6,312	6,312
October 2015	Four forward starting swaps	300,000	13,369	13,369
December 2016	Two forward starting swaps	180,000	(13,352)	(13,345)

⁽¹⁾ The amount reported in accumulated other comprehensive income will be reclassified to interest expense as interest payments are made on the related notes payable.

As of June 30, 2017, \$7,997,000 remained in other comprehensive income related to the effective portion of NNN's previously terminated interest rate hedges. During the six months ended June 30, 2017 and 2016, NNN reclassified out of other comprehensive income \$903,000 and \$1,402,000, respectively, as an increase in interest expense. Over the next 12 months, NNN estimates that an additional \$1,578,000 will be reclassified as an increase in interest expense. Amounts reported in accumulated other comprehensive income related to derivatives will be reclassified to interest expense as interest payments are made on NNN's long-term debt.

During the six months ended June 30, 2017, NNN entered into two forward starting swaps with a total notional amount of \$250,000,000 to hedge the risk of changes in the interest-related cash outflows associated with the potential issuance of long-term debt. The outstanding forward swaps were designated as cash flow hedges, and at June 30, 2017, have a fair value of \$661,000 included in other assets and \$2,355,000 included in other liabilities, which net (\$1,694,000) in accumulated other comprehensive income (loss) on the condensed consolidated balance sheet. The fair value of the forward starting swaps were based on a Level 2 valuation. No hedge ineffectiveness was recognized during the six months ended June 30, 2017. These derivative financial instruments were still outstanding as of June 30, 2017.

NNN does not use derivatives for trading or speculative purposes or currently have any derivatives that are not designated as hedges.

Note 6 – Fair Value of Financial Instruments:

NNN believes the carrying value of its Credit Facility approximates fair value based upon its nature, terms and variable interest rate. NNN believes that the carrying value of its mortgages and notes receivable and mortgages payable at June 30, 2017 and December 31, 2016, approximate fair value based upon current market prices of comparable instruments (Level 3). At June 30, 2017 and December 31, 2016, the fair value of NNN's notes payable net of unamortized discount and excluding debt costs was \$2,377,525,000 and \$2,367,102,000, respectively, based upon quoted market prices, which is a Level 1 valuation since NNN's notes payable is publicly traded.

Note 7 – Subsequent Events:

NNN reviewed its subsequent events and transactions that have occurred after June 30, 2017, the date of the condensed consolidated balance sheet. There were no reportable subsequent events or transactions.

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

The following discussion and analysis should be read in conjunction with the consolidated financial statements and related notes included in the Annual Report on Form 10-K of National Retail Properties, Inc. for the year ended December 31, 2016. The terms "NNN" and the "Company" refer to National Retail Properties, Inc. and all of its consolidated subsidiaries.

Forward-Looking Statements

The information herein contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities and Exchange Act of 1934 (the "Exchange Act"). These statements generally are characterized by the use of terms such as "believe," "expect," "intend," "may," "estimated" or similar words or expressions. Forward-looking statements are not historical facts or guarantees of future performance and are subject to known and unknown risks. Certain factors that could cause actual results or events to differ materially from those NNN anticipates or projects include, but are not limited to, the following:

- Financial and economic conditions may have an adverse impact on NNN, its tenants, and commercial real estate in general;
- NNN may be unable to obtain debt or equity capital on favorable terms, if at all;
- Loss of rent from tenants would reduce NNN's cash flow;
- A significant portion of the source of the Property Portfolio annual base rent is concentrated in specific industry classifications, tenants and geographic locations;
- Owning real estate and indirect interests in real estate carries inherent risk;
- NNN's real estate investments are illiquid;
- Costs of complying with changes in governmental laws and regulations may adversely affect NNN's results of operations;
- NNN may be subject to known or unknown environmental liabilities and hazardous materials on Properties owned by NNN;
- NNN may not be able to successfully execute its acquisition or development strategies;
- NNN may not be able to dispose of properties consistent with its operating strategy;
- NNN may suffer a loss in the event of a default of or bankruptcy of a borrower or a tenant;
- Certain provisions of NNN's leases or loan agreements may be unenforceable;
- Property ownership through joint ventures and partnerships could limit NNN's control of those investments;
- Competition from numerous other REITs, commercial developers, real estate limited partnerships and other investors may impede NNN's ability to grow;
- NNN's loss of key management personnel could adversely affect performance and the value of its securities;
- Uninsured losses may adversely affect NNN's operating results and asset values;
- Acts of violence, terrorist attacks or war may affect the markets in which NNN operates and NNN's results of operations;
- Vacant properties or bankrupt tenants or borrowers could adversely affect NNN's business or financial condition;
- The amount of debt NNN has and the restrictions imposed by that debt could adversely affect NNN's business and financial condition;
- NNN is obligated to comply with financial and other covenants in its debt instruments that could restrict its operating activities, and the failure to comply with such covenants could result in defaults that accelerate the payment of such debt;
- The market value of NNN's equity and debt securities is subject to various factors that may cause significant fluctuations or volatility;
- NNN's failure to qualify as a REIT for federal income tax purposes could result in significant tax liability;
- Even if NNN remains qualified as a REIT, NNN faces other tax liabilities that reduce operating results and cash flow;

• Adverse legislative or regulatory tax changes could reduce NNN's earnings and cash flow and the market price of NNN's securities;

• Compliance with REIT requirements, including distribution requirements, may limit NNN's flexibility and may negatively affect NNN's operating decisions;

• Changes in accounting pronouncements could adversely impact NNN's or NNN's tenants' reported financial performance;

• NNN's failure to maintain effective internal control over financial reporting could have a material adverse effect on its business, operating results and the market value of NNN's securities;

• NNN's ability to pay dividends in the future is subject to many factors;

- Cybersecurity risks and cyber incidents could adversely affect NNN's business, disrupt operations and expose NNN to liabilities to tenants, employees, capital providers, and other third parties; and

Future investment in international markets could subject NNN to additional risks.

Additional information related to these risks and uncertainties are included in Item 1A. Risk Factors of NNN's Annual Report on Form 10-K for the year ended December 31, 2016, and may cause NNN's actual future results to differ materially from expected results. Given these risks and uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements, which speak only as of the date of this Quarterly Report on Form 10-Q. NNN undertakes no obligation to update or revise such forward-looking statements, whether as a result of new information, future events or otherwise.

Overview

NNN, a Maryland corporation, is a fully integrated real estate investment trust ("REIT") formed in 1984. NNN's assets primarily include real estate assets. NNN acquires, owns, invests in and develops properties that are leased primarily to retail tenants under long-term net leases and primarily held for investment ("Properties" or "Property Portfolio", or individually a "Property").

As of June 30, 2017, NNN owned 2,675 Properties, with an aggregate gross leasable area of approximately 28,102,000 square feet, located in 48 states, with a weighted average remaining lease term of 11.5 years.

Approximately 99 percent of the Properties were leased as of June 30, 2017.

NNN's management team focuses on certain key indicators to evaluate the financial condition and operating performance of NNN. The key indicators for NNN include items such as: the composition of the Property Portfolio (such as tenant, geographic and line of trade diversification), the occupancy rate of the Property Portfolio, certain financial performance ratios and profitability measures, and industry trends and performance compared to that of NNN.

NNN evaluates the creditworthiness of its current and prospective tenants. This evaluation may include reviewing available financial statements, store level financial performance, press releases, public credit ratings from major credit rating agencies, industry news publications, financial market data (debt and equity pricing). NNN may also evaluate the business and operations of its tenants, including periodically meeting with senior management of certain tenants. NNN continues to maintain its diversification by tenant, geography and tenant's line of trade. NNN's largest lines of trade concentrations are the convenience store and restaurant (including full and limited service) sectors. These sectors represent a large part of the freestanding retail property marketplace and NNN's management believes these sectors present attractive investment opportunities. The Property Portfolio is geographically concentrated in the south and southeast United States, which are regions of historically above-average population growth. Given these concentrations, any financial hardship within these sectors or geographic regions could have a material adverse effect on the financial condition and operating performance of NNN.

Results of Operations

Property Analysis

General. The following table summarizes the Property Portfolio:

	June 30, 2017	December 31, 2016	June 30, 2016
Properties Owned:			
Number	2,675	2,535	2,452
Total gross leasable area (square feet)	28,102,000	27,204,000	26,326,000
Properties:			
Leased and unimproved land	2,657	2,508	2,430
Percent of Properties – leased and unimproved land	99	% 99	% 99
Weighted average remaining lease term (years)	11.5	11.6	11.4
Total gross leasable area (square feet) – leased	27,734,000	26,700,000	25,907,000

The following table summarizes the diversification of the Property Portfolio based on the top 10 lines of trade:

Lines of Trade	% of Annual Base Rent ⁽¹⁾			
	June 30, 2017	December 31, 2016	June 30, 2016	
1. Convenience stores	18.1	% 16.9	% 16.7	%
2. Restaurants – full service	11.7	% 11.8	% 12.6	%
3. Restaurants – limited service	7.8	% 7.5	% 7.7	%
4. Automotive service	6.9	% 6.6	% 6.7	%
5. Family entertainment centers	6.1	% 5.8	% 5.7	%
6. Health and fitness	5.6	% 5.7	% 4.2	%
7. Theaters	4.7	% 4.9	% 5.1	%
8. Automotive parts	3.7	% 3.9	% 4.0	%
9. Recreational vehicle dealers, parts and accessories	3.4	% 3.4	% 3.4	%
10. Banks	2.6	% 3.1	% 3.3	%
Other	29.4	% 30.4	% 30.6	%
	100.0	% 100.0	% 100.0	%

⁽¹⁾ Based on annualized base rent for all leases in place for each respective period.

Property Acquisitions. The following table summarizes the Property acquisitions (dollars in thousands):

	Quarter Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Acquisitions:				
Number of Properties	140	165	164	211
Gross leasable area (square feet)	832,000	1,095,000	1,082,000	1,686,000
Initial cash yield	6.9	% 6.9	% 6.9	% 6.9
Total dollars invested ⁽¹⁾	\$299,452	\$343,596	\$407,391	\$468,746

⁽¹⁾ Includes dollars invested in projects under construction or tenant improvements for each respective year.

NNN typically funds Property acquisitions either through borrowings under NNN's unsecured revolving credit facility (the "Credit Facility") (see "Debt – Line of Credit Payable") or by issuing its debt or equity securities in the capital markets.

Property Dispositions. The following table summarizes the Properties sold by NNN (dollars in thousands):

	Quarter Ended		Six Months	
	June 30,		Ended June 30,	
	2017	2016	2017	2016
Number of properties	8	7	25	17
Gross leasable area (square feet)	41,000	171,000	188,000	323,000
Net sales proceeds	\$9,308	\$19,667	\$48,263	\$72,506
Gain	\$3,055	\$1,178	\$17,679	\$18,053

NNN typically uses the proceeds from a Property disposition to either pay down the Credit Facility or reinvest in real estate.

Analysis of Revenue

General. During the quarter and six months ended June 30, 2017, rental income increased, as compared to the same periods in 2016, primarily due to the increase in rental income from Property acquisitions (See “Results of Operations – Property Analysis – Property Acquisitions”). NNN anticipates increases in rental income will continue to come from additional Property acquisitions and increases in rents pursuant to existing lease terms.

The following table summarizes NNN’s revenues (dollars in thousands):

	Quarter Ended June 30,			Six Months Ended June 30,						
	2017	2016	Percent Increase (Decrease)	Percent of Total		Percent of Total		Percent Increase (Decrease)	Percent of Total	
				2017	2016	2017	2016		2017	2016
Rental Income ⁽¹⁾	\$141,742	\$126,929	11.7%	97.4 %	97.0 %	\$279,039	\$249,404	11.9%	97.2 %	96.7 %
Real estate expense reimbursement from tenants	3,700	3,248	13.9%	2.5 %	2.5 %	7,560	6,838	10.6%	2.6 %	2.7 %
Interest and other income from real estate transactions	28	301	(90.7)%	—	0.2 %	217	764	(71.6)%	0.1 %	0.3 %
Interest income on commercial mortgage residual interests	80	448	(82.1)%	0.1 %	0.3 %	165	901	(81.7)%	0.1 %	0.3 %
Total revenues	\$145,550	\$130,926	11.2%	100.0%	100.0%	\$286,981	\$257,907	11.3%	100.0%	100.0%

⁽¹⁾ Includes rental income from operating leases, earned income from direct financing leases and percentage rent (“Rental Income”).

Quarter and Six Months Ended June 30, 2017 versus Quarter and Six Months Ended June 30, 2016

Rental Income. Rental Income increased in amount and as a percent of the total revenues for the quarter and six months ended June 30, 2017, as compared to the same periods in 2016. The increase for the quarter and six months ended June 30, 2017, is primarily due to a partial year of Rental Income received as a result of the acquisition of 164 properties with aggregate gross leasable area of approximately 1,082,000 during 2017 and a full year of Rental Income received as a result of the acquisition of 313 properties with a gross leasable area of approximately 2,734,000 square feet in 2016.

Analysis of Expenses

General. Operating expenses increased for the quarter and six months ended June 30, 2017, as compared to the same periods in 2016, primarily due to an increase in personnel costs and in depreciation expense. The following table summarizes NNN's expenses for the quarter ended June 30, (dollars in thousands):

	2017	2016	Percent Increase (Decrease)	Percentage of Total		Percentage of Revenues	
				2017	2016	2017	2016
General and administrative	\$8,820	\$8,735	1.0%	14.0 %	15.6 %	6.1 %	6.7 %
Real estate	5,424	4,567	18.8%	8.6 %	8.2 %	3.7 %	3.5 %
Depreciation and amortization	41,326	36,489	13.3%	65.7 %	65.3 %	28.4 %	27.8 %
Impairment – commercial mortgage residual interests valuation	—	632	(100.0)%	—	1.1 %	—	0.5 %
Impairment losses – real estate and other charges, net of recoveries	(39)	5,459	(100.7)%	(0.1)%	9.8 %	—	4.2 %
Retirement severance costs	7,428	—	N/C ⁽¹⁾	11.8 %	—	5.1 %	— %
Total operating expenses	\$62,959	\$55,882	12.7%	100.0 %	100.0 %	43.3 %	42.7 %
Interest and other income	\$(37)	\$(72)	(48.6)%	(0.1)%	(0.3)%	—	(0.1)%
Interest expense	27,274	24,081	13.3%	100.1 %	99.1 %	18.7 %	18.4 %
Real estate acquisition costs	—	280	(100.0)%	—	1.2 %	—	0.2 %
Total other expenses	\$27,237	\$24,289	12.1%	100.0 %	100.0 %	18.7 %	18.5 %

⁽¹⁾ Not calculable ("N/C")

The following table summarizes NNN's expenses for the six months ended June 30, (dollars in thousands):

	2017	2016	Percent Increase (Decrease)	Percentage of Total		Percentage of Revenues	
				2017	2016	2017	2016
General and administrative	\$17,739	\$17,984	(1.4)%	14.9 %	17.1 %	6.2 %	7.0 %
Real estate	11,087	9,355	18.5%	9.4 %	8.9 %	3.8 %	3.6 %
Depreciation and amortization	81,469	71,144	14.5%	68.5 %	67.5 %	28.4 %	27.6 %
Impairment – commercial mortgage residual interests valuation	—	852	(100.0)%	—	0.8 %	—	0.3 %
Impairment losses – real estate and other charges, net of recoveries	1,167	6,031	(80.6)%	1.0 %	5.7 %	0.4 %	2.4 %
Retirement severance costs	7,428	—	N/C ⁽¹⁾	6.2 %	—	2.6 %	— %
Total operating expenses	\$118,890	\$105,366	12.8%	100.0 %	100.0 %	41.4 %	40.9 %
Interest and other income	\$(175)	\$(91)	92.3%	(0.3)%	(0.2)%	(0.1)%	—
Interest expense	53,888	47,667	13.1%	100.3 %	99.3 %	18.8 %	18.5 %
Real estate acquisition costs	—	409	(100.0)%	—	0.9 %	—	0.1 %
Total other expenses	\$53,713	\$47,985	11.9%	100.0 %	100.0 %	18.7 %	18.6 %

⁽¹⁾ Not calculable ("N/C")

Quarter and Six Months Ended June 30, 2017 versus Quarter and Six Months Ended June 30, 2016

Depreciation and Amortization. Depreciation and amortization expenses increased in amount and as a percentage of total operating expenses and revenues for the quarter and six months ended June 30, 2017, as compared to the same periods in 2016. The increase in expenses is primarily due to the acquisition of 164 properties with an aggregate gross leasable area of approximately 1,082,000 square feet in 2017 and 313 properties with an aggregate gross leasable area

of approximately 2,734,000 square feet during 2016.

Impairment losses – real estate and other charges, net of recoveries. NNN reviews long-lived assets for impairment whenever certain events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. Events or circumstances that may occur include changes in real estate market conditions, the ability to re-lease properties that are currently vacant or become vacant, and the ability to sell properties at an attractive price. Management evaluates whether an impairment in value has occurred by comparing the estimated future cash flows (undiscounted and without interest charges), including the residual value of the real estate, with the carrying cost of the individual asset. If an impairment is indicated, a loss will be recorded for the amount by which the carrying value of the asset exceeds its fair value. NNN recognized real estate impairments, net of recoveries of \$1,167,000 and \$2,762,000 for the six months ended June 30, 2017 and 2016, respectively of which (\$39,000) and \$2,190,000 was recorded during the quarters ended June 30, 2017 and 2016, respectively. In addition, during the quarter ended June 30, 2016, NNN recorded a loss on mortgage receivable of \$3,269,000.

Retirement Severance Costs. For the quarter ended June 30, 2017, retirement severance costs relate primarily to Craig Macnab's retirement as CEO on April 28, 2017.

Interest Expense. Interest expense increased in amount, as a percentage of total other expenses and as a percentage of revenues for the quarter and six months ended June 30, 2017, as compared to the same periods in 2016.

The following represents the primary changes in debt that have impacted interest expense:

- (i) the repayment in January 2016 of \$5,876,000 principal amount of mortgages payable with an interest rate of 5.750%,
- (ii) the repayment in March 2016 of \$722,000 principal amount of mortgages payable with an interest rate of 6.900%,
- (iii) the repayment in October 2016 of \$2,709,000 principal amount of mortgages payable with an interest rate of 6.400%,
- (iv) the issuance in December 2016 of \$350,000,000 principal amount of notes payable with a maturity of December 2026, and stated interest rate of 3.600%, and
- (v) the Credit Facility had a \$23,898,000 increase in the weighted average outstanding balance and a slightly higher weighted average interest rate for the six months ended June 30, 2017, as compared to the six months ended June 30, 2016.

Liquidity

General. NNN's demand for funds has been, and will continue to be, primarily for (i) payment of operating expenses and cash dividends; (ii) Property acquisitions and development; (iii) capital expenditures; (iv) payment of principal and interest on its outstanding indebtedness; and (v) other investments.

Cash and Cash Equivalents. NNN's cash and cash equivalents includes the aggregate of Cash and cash equivalents and Restricted cash and cash held in escrow from the Condensed Consolidated Balance Sheets. The table below summarizes NNN's cash flows (dollars in thousands):

	Six Months Ended	
	June 30,	
	2017	2016
Cash and cash equivalents:		
Provided by operating activities	\$215,071	\$187,648
Used in investing activities	(350,799)	(414,196)
Provided by (used in) financing activities	(154,362)	214,901
Decrease	(290,090)	(11,647)
Net cash at beginning of period	294,540	14,260
Net cash at end of period	\$4,450	\$2,613

Cash provided by operating activities represents cash received primarily from Rental Income and interest income less cash used for general and administrative expenses. NNN's cash flow from operating activities has been sufficient to pay the distributions for each period presented. The change in cash provided by operations for the six months ended June 30, 2017, and 2016, is primarily the result of changes in revenues and expenses as discussed in "Results of

Operations.” Cash generated from operations is expected to fluctuate in the future.

Changes in cash for investing activities are primarily attributable to the acquisitions and dispositions of Properties. NNN typically uses proceeds from its Credit Facility to fund the acquisition of its Properties.

NNN's financing activities for the six months ended June 30, 2017, included the following significant transactions: \$287,500,000 paid to fully redeem NNN's 6.625% Series D Cumulative Redeemable Preferred Stock (the "Series D Preferred Stock"),

\$1,413,000 in net proceeds from the issuance of 34,466 shares of common stock in connection with the Dividend Reinvestment and Stock Purchase Plan ("DRIP"),

\$72,139,000 in net proceeds from the issuance of 1,653,155 shares of common stock in connection with the at-the-market ("ATM") equity program,

\$3,598,000 in dividends paid to holders of the depositary shares of NNN's Series D Preferred Stock,

\$8,194,000 in dividends paid to holders of the depositary shares of NNN's 5.700% Series E Cumulative Redeemable Preferred Stock (the "Series E Preferred Stock"),

\$8,970,000 in dividends paid to holders of the depositary shares of NNN's 5.200% Series F Cumulative Redeemable Preferred Stock (the "Series F Preferred Stock"), and

\$134,440,000 in dividends paid to common stockholders.

Contractual Obligations and Commercial Commitments. NNN has committed to fund construction commitments on 22 Properties. The improvements are estimated to be completed within 12 months. These construction commitments, at June 30, 2017, are outlined in the table below (dollars in thousands):

Total commitment ⁽¹⁾	\$ 126,634
Amount funded	48,304
Remaining commitment	78,330

⁽¹⁾ Includes land, construction costs, tenant improvements and lease costs.

As of June 30, 2017, NNN did not have any other material contractual cash obligations, such as purchase obligations, financing lease obligations or other long-term liabilities other than those reflected in the tables above and previously disclosed under Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations included in NNN's Annual Report on Form 10-K for the year ended December 31, 2016. In addition to items reflected in the tables, NNN has issued preferred stock with cumulative preferential cash distributions, as described below under "Dividends."

Management anticipates satisfying these obligations with a combination of NNN's cash provided from operations, current capital resources on hand, its credit facility, debt or equity financings and asset dispositions.

Generally, the Properties are leased under long-term net leases, which require the tenant to pay all property taxes and assessments to maintain the interior and exterior of the property and to carry property and liability insurance coverage. Therefore, management anticipates that capital demands to meet obligations with respect to these Properties will be modest for the foreseeable future and can be met with funds from operations and working capital. Certain Properties are subject to leases under which NNN retains responsibility for specific costs and expenses associated with the Property. Management anticipates that the costs associated with the vacant Properties or those Properties that become vacant will also be met with funds from operations and working capital. NNN may be required to borrow under its credit facility or use other sources of capital in the event of significant capital expenditures.

The lost revenues and increased property expenses resulting from vacant Properties or uncollectibility of lease revenues could have a material adverse effect on the liquidity and results of operations if NNN is unable to re-lease the Properties at comparable rental rates and in a timely manner. As of June 30, 2017, NNN owned 18 vacant, un-leased Properties which accounted for less than one percent of total Properties held in the Property Portfolio. Additionally, as of June 30, 2017, approximately three percent of the Property Portfolio is leased to four tenants, including Gander Mountain, that each filed a petition for bankruptcy under Chapter 11 of the U.S. Bankruptcy Code. As a result, these tenants have the right to reject or affirm their leases with NNN.

NNN generally monitors the financial performance of its significant tenants on an ongoing basis.

Dividends. NNN has made an election to be taxed as a REIT under Sections 856 through 860 of the Code, as amended, and related regulations and intends to continue to operate so as to remain qualified as a REIT for federal income tax purposes. NNN generally will not be subject to federal income tax on income that it distributes to its

stockholders, provided that it distributes 100 percent of its REIT taxable income and meets certain other requirements for qualifying as a REIT. If NNN fails to qualify

as a REIT in any taxable year, it will be subject to federal income tax on its taxable income at regular corporate rates and will not be permitted to qualify for treatment as a REIT for federal income tax purposes for the four years following the year during which qualification is lost. Such an event could materially adversely affect NNN's income and ability to pay dividends. NNN believes it has been structured as, and its past and present operations qualify NNN as, a REIT.

One of NNN's primary objectives, consistent with its policy of retaining sufficient cash for reserves and working capital purposes and maintaining its status as a REIT, is to distribute a substantial portion of its funds available from operations to its stockholders in the form of dividends.

The following table outlines the dividends declared and paid for each issuance of NNN's stock (dollars in thousands, except per share data):

	Quarter Ended June 30, 2017	Six Months Ended June 30, 2017 2016	
Series D Preferred Stock ⁽¹⁾ :			
Dividends	\$-4,762	\$3,598	\$9,523
Per depositary share	—0.414063	0.312840	0.828125
Series E Preferred Stock ⁽²⁾ :			
Dividends	4,000	8,194	8,194
Per depositary share	0.35636050	0.712500	0.712500
Series F Preferred Stock ⁽³⁾ :			
Dividends	4,485	8,970	—
Per depositary share	0.325000	0.650000	—
Common stock:			
Dividends	67,660	134,440	123,602
Per share	0.45435	0.910	0.870

⁽¹⁾ The Series D Preferred Stock was redeemed in February 2017. The dividends paid in 2017 included accumulated and unpaid dividends through the redemption date.

⁽²⁾ The Series E Preferred Stock has no maturity date and will remain outstanding unless redeemed by NNN. The earliest redemption date for the Series E Preferred Stock is May 2018.

⁽³⁾ The Series F Preferred Stock was issued in October 2016 and has no maturity date and will remain outstanding unless redeemed by NNN. The earliest redemption date for the Series F Preferred Stock is October 2021.

In July 2017, NNN declared a dividend of \$0.475 per share which is payable in August 2017 to its common stockholders of record as of July 31, 2017.

Capital Resources

Generally, cash needs for Property acquisitions, debt payments, capital expenditures, development and other investments have been funded by equity and debt offerings, bank borrowings, the sale of Properties and, to a lesser extent, by internally generated funds. Cash needs for operating and interest expenses and dividends have generally been funded by internally generated funds. If available, future sources of capital include proceeds from the public or private offering of NNN's debt or equity securities, secured or unsecured borrowings from banks or other lenders,

proceeds from the sale of Properties, as well as undistributed funds from operations.

Debt

The following is a summary of NNN's total outstanding debt as of (dollars in thousands):

	June 30, 2017	Percentage of Total	December 31, 2016	Percentage of Total
Line of credit payable	\$215,500	8.5 %	\$—	—
Mortgages payable	13,591	0.5 %	13,878	0.6 %
Notes payable	2,299,710	91.0 %	2,297,811	99.4 %
Total outstanding debt	\$2,528,801	100.0 %	\$2,311,689	100.0 %

Indebtedness. NNN expects to use indebtedness primarily for property acquisitions and development of single-tenant retail properties, either directly or through investment interests. Additionally indebtedness may be used to refinance existing indebtedness.

Line of Credit Payable. NNN's \$650,000,000 unsecured revolving Credit Facility had a weighted average outstanding balance of \$69,100,000 and a weighted average interest rate of 2.0% during the six months ended June 30, 2017. The Credit Facility matures January 2019, unless the Company exercises its option to extend maturity to January 2020. The Credit Facility currently bears interest at LIBOR plus 92.5 basis points; however, such interest rate may change pursuant to a tiered interest rate structure based on NNN's debt rating. The Credit Facility also includes an accordion feature to increase the facility size up to \$1,000,000,000, subject to lender approval. As of June 30, 2017, there was \$215,500,000 outstanding balance and \$434,500,000 was available for future borrowings, under the Credit Facility, excluding undrawn letters of credit totaling \$230,000.

Debt and Equity Securities

NNN has used, and expects to use in the future, issuances of debt and equity securities primarily to pay down its outstanding indebtedness and to finance investment acquisitions.

Securities Offerings. In February 2015, NNN filed a shelf registration statement with the Securities and Exchange Commission (the "Commission") which was automatically effective and permits the issuance by NNN of an indeterminate amount of debt and equity securities.

Information related to NNN's publicly held debt and equity securities is included in NNN's Annual Report on Form 10-K for the year ended December 31, 2016.

Dividend Reinvestment and Stock Purchase Plan. In February 2015, NNN filed a shelf registration statement which was automatically effective with the Commission for its DRIP, which permits the issuance by NNN of up to 16,000,000 shares of common stock. NNN's DRIP provides an economical and convenient way for current stockholders and other interested new investors to invest in NNN's common stock. The following outlines the common stock issuances pursuant to NNN's DRIP (dollars in thousands):

	Six Months Ended June 30, 2017		2016
Shares of common stock	34,466	149,543	
Net proceeds	\$1,413	\$6,609	

At-The-Market Offerings. NNN established an at-the-market equity program ("ATM") which allows NNN to sell shares of common stock from time to time. The following outlines NNN's ATM programs:

	2016 ATM	2015 ATM
Established date	March 2016	February 2015
Termination date	March 2019	March 2016
Total allowable shares	12,000,000	10,000,000
Total shares issued at June 30, 2017	5,876,445	9,852,465

The following table outlines the common stock issuances pursuant to NNN's ATM equity programs (dollars in thousands, except per share data):

	Six Months Ended	
	June 30,	
	2017	2016
Shares of common stock	1,653,155	4,613,422
Average price per share (net)	\$43.64	\$45.46
Net proceeds	\$72,139	\$209,722
Stock issuance costs ⁽¹⁾	\$1,183	\$3,379

⁽¹⁾ Stock issuance costs consist primarily of underwriters' fees and commissions, and legal and accounting fees.

Recent Accounting Pronouncements

Refer to Note 1 to the June 30, 2017, Condensed Consolidated Financial Statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

NNN is exposed to interest rate risk primarily as a result of its variable rate Credit Facility and its fixed rate debt which is used to finance NNN's development and acquisition activities, as well as for general corporate purposes. NNN's interest rate risk management objective is to limit the impact of interest rate changes on earnings and cash flows and to reduce overall borrowing costs. To achieve its objectives, NNN borrows at both fixed and variable rates on its long-term debt. As of June 30, 2017, NNN has two forward starting swaps with a total notional amount of \$250,000,000 to hedge the risk of changes in the interest-related cash outflows associated with the potential issuance of long-term debt.

The information in the table below summarizes NNN's market risks associated with its debt obligations outstanding as of June 30, 2017 and December 31, 2016. The table presents principal payments and related interest rates by year for debt obligations outstanding as of June 30, 2017. The table incorporates only those debt obligations that existed as of June 30, 2017, and it does not consider those debt obligations or positions which could arise after this date and therefore has limited predictive value. As a result, NNN's ultimate realized gain or loss with respect to interest rate fluctuations will depend on the exposures that arise during the quarter, NNN's hedging strategies at that time and interest rates. If interest rates on NNN's variable rate debt increased by one percent, NNN's interest expense would have increased by less than one percent for the six months ended June 30, 2017.

Debt Obligations (dollars in thousands)

	Variable Rate Debt Credit Facility		Fixed Rate Debt Mortgages ⁽¹⁾		Unsecured Debt ⁽²⁾	
	Debt Obligation	Weighted Average Interest Rate	Debt Obligation	Weighted Average Effective Interest Rate	Debt Obligation	Effective Interest Rate
2017	\$—	—	\$300	5.23%	\$249,965	6.92%
2018	—	—	623	5.23%	—	—
2019	215,500	2.02%	653	5.23%	—	—
2020	—	—	682	5.23%	—	—
2021	—	—	716	5.23%	297,983	5.69%
Thereafter	—	—	10,718	5.23%	1,765,522	3.73% ⁽³⁾
Total	\$215,500	2.02%	\$13,692		\$2,313,470	4.39%
Fair Value:						
June 30, 2017	\$215,500		\$13,692		\$2,377,525	
December 31, 2016	\$—		\$13,987		\$2,367,102	

⁽¹⁾ NNN's mortgages payable represent principal payments by year and include unamortized premiums and exclude debt costs.

⁽²⁾ Includes NNN's notes payable, each exclude debt costs and are net of unamortized discount. NNN uses market prices quoted from Bloomberg, a third party, which is a Level 1 input, to determine the fair value.

⁽³⁾ Weighted average effective interest rate for periods after 2021.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures. An evaluation was performed under the supervision and with the participation of NNN's management, including NNN's Chief Executive Officer, Chief Financial Officer, and Chief Accounting Officer, of the effectiveness as of June 30, 2017, of the design and operation of NNN's disclosure controls and procedures as defined in Rule 13a-15(e) under the Exchange Act. Based on that evaluation, the Chief Executive Officer, Chief Financial Officer, and Chief Accounting Officer concluded that the design and operation of these disclosure controls and procedures were effective as of the end of the period covered by this report.

Changes in Internal Control over Financial Reporting. There has been no change in NNN's internal control over financial reporting that occurred during the most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, NNN's internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings. Not applicable.

Item Risk Factors. There were no material changes in NNN's risk factors disclosed in Item 1A. Risk Factors of 1A. NNN's Annual Report on Form 10-K for the year ended December 31, 2016.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds. Not applicable.

Item 3. Defaults Upon Senior Securities. Not applicable.

Item 4. Mine Safety Disclosures. Not applicable.

Item 5. Other Information. Not applicable.

Item 6. Exhibits

The following exhibits are filed as a part of this report.

10. Material Contracts

Amended and Restated Employment Agreement, dated as of September 29, 2016, between the registrant and 10.1 Julian Whitehurst (filed as Exhibit 10.2 to the Registrant's Current Report on Form 8-K filed with the Securities and Exchange Commission on September 30, 2016, and incorporated herein by reference).

2017 Performance Incentive Plan (filed as Annex A to the Registrant's 2017 Annual Proxy Statement on 10.2 Schedule 14A filed with the Securities and Exchange Commission on March 29, 2017, and incorporated herein by reference).