

SECURITIES AND EXCHANGE COMMISSION

FORM 10-K405

Annual report pursuant to section 13 and 15(d), Regulation S-K Item 405

Filing Date: **1999-03-26** | Period of Report: **1998-12-31**  
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FILER

**TRANSCONTINENTAL REALTY INVESTORS INC**

CIK: **733590** | IRS No.: **946565852** | State of Incorpor.: **NV** | Fiscal Year End: **1231**  
Type: **10-K405** | Act: **34** | File No.: **001-09240** | Film No.: **99573788**  
SIC: **6798** Real estate investment trusts

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SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
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FORM 10-K

[X] ANNUAL REPORT PURSUANT TO SECTIONS 13 OR 15(d) OF THE SECURITIES EXCHANGE  
ACT OF 1934

For the Year Ended December 31, 1998

Commission File Number 1-9240  
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Transcontinental Realty Investors, Inc.  
(Exact Name of Registrant as Specified in Its Charter)

Nevada 94-6565852  
(State or Other Jurisdiction of (I.R.S. Employer Identification No.)  
incorporation or Organization)

10670 North Central Expressway, Suite 300, Dallas, Texas 75231  
(Address of Principal Executive Offices) (Zip Code)

(214) 692-4700  
(Registrant's Telephone Number, Including Area Code)

Securities Registered Pursuant to Section 12(b) of the Act:

<TABLE>	<S>	<C>
	Title of each class	Name of each exchange on which registered
</TABLE>	Common Stock, \$.01 par value	New York Stock Exchange

Securities Registered Pursuant to Section 12(g) of the Act:

NONE  
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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 at least the past 90 days. Yes [X] No [ ]

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [X]

As of March 5, 1999, the Registrant had 3,878,463 shares of Common Stock outstanding. Of the total shares outstanding 2,144,193 were held by other than those who may be deemed to be affiliates, for an aggregate value of \$27,472,000 based on the last trade as reported on the New York Stock Exchange on March 5, 1999. The basis of this calculation does not constitute a determination by the Registrant that all of such persons or entities are affiliates of the Registrant as defined in Rule 405 of the Securities Act of 1933, as amended.

Documents Incorporated by Reference:

Consolidated Financial Statements of Income Opportunity Realty Investors, Inc.  
Commission File No. 1-14784  
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PART I

ITEM 1. BUSINESS

Transcontinental Realty Investors, Inc. (the "Company" or the "Registrant"), a Nevada corporation, is the successor to a California business trust, which was organized on September 6, 1983 and commenced operations on January 31, 1984. The Company has elected to be treated as a Real Estate Investment Trust ("REIT") under Sections 856 through 860 of the Internal Revenue Code of 1986, as amended (the "Code"). The Company has, in the opinion of management, qualified for federal taxation as a REIT for each year subsequent to December 31, 1983.

The Company's real estate at December 31, 1998 consisted of 77 properties held for investment, four partnership properties and four properties held for sale which were primarily obtained through foreclosure. 22 of the properties held for investment were purchased during 1998. The Company's mortgage notes receivable portfolio at December 31, 1998 consisted of 16 mortgage loans. In addition, the Company has an interest in a partnership which holds a wraparound mortgage loan. The Company's real estate and mortgage notes receivable portfolios are more fully discussed in ITEM 2. "PROPERTIES."

Proposed Merger with Continental Mortgage and Equity Trust

On September 25, 1998, the Company and Continental Mortgage and Equity Trust ("CMET") jointly announced the agreement of their respective Boards for the Company to acquire CMET. Under the proposal, the Company would acquire all of CMET's outstanding shares of beneficial interest, in a tax free exchange, for shares of its Common Stock. The Company will issue 1.181 shares of its Common Stock for each outstanding share of beneficial interest of CMET. Upon the exchange of shares CMET would merge into the Company. The share exchange and merger are subject to a vote of shareholders of both entities. Approval requires the vote of shareholders holding a majority of CMET's outstanding shares of beneficial interest. As of March 5, 1999, the Company's advisor and its affiliates held shares representing approximately 57.4% of the outstanding

shares of CMET and approximately 44.7% of the outstanding shares of the Company. A date for the special meeting of the shareholders to vote on the merger proposal has not been set. The Company has the same Board and advisor as CMET.

#### Business Plan and Investment Policy

The Company's business is investing in real estate through direct equity ownership and partnerships and financing real estate and real estate related activities through investments in mortgage loans, including first, wraparound and junior mortgage loans. The Company's real estate is located throughout the continental United States. Information regarding the real estate and mortgage notes receivable portfolios of the Company is set forth in ITEM 2. "PROPERTIES", and in Schedules III and IV to the Consolidated Financial Statements included at ITEM 8. "FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA."

The Company's business is not seasonal. The Company has determined to continue to pursue a balanced investment policy, seeking both current income and capital appreciation. With respect to new real estate investments, the Company's plan of operation is to consider all types of real estate, but in an attempt to bring balance to its real estate portfolio, it will focus on apartments, primarily located in the Southeast and Southwest regions of the United States. In making any new real estate investments, emphasis will be on acquiring properties generating current cash flow. The Company expects to continue to invest in and improve these assets to maximize both their immediate and longer term value.

The Company expects to consider property sales opportunities for properties in stabilized real estate markets where its properties have reached their potential. It may also be an opportunistic seller of properties in markets that have become overheated, i.e. an abundance of buyers.

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The Company's operating strategy with regard to its properties is to maximize each property's operating income by aggressive property management through closely monitoring expenses while at the same time making property renovations and/or improvements where appropriate. While such expenditures increase the amount of revenue required to cover operating expenses, management believes that such expenditures are necessary to maintain or enhance the value of the properties.

The Company has determined that in 1999 it may seek to fund or acquire new mortgage loans to take advantage of favorable interest rate spreads or profit participation opportunities. It may also originate mortgage loans in conjunction with providing purchase money financing of a property sale. The Company intends to service and hold for investment the mortgage notes in its portfolio. It may, however, borrow against its mortgage notes using the proceeds from such borrowings to fund additional mortgage loans or for general working capital needs. The Company also intends to pursue its rights vigorously with respect to mortgage notes that are in default. The Articles of Incorporation impose no limitations on the Company's investment policy with respect to mortgage loans and do not prohibit it from investing more than a specified percentage of its assets in any one mortgage loan.

#### Management of the Company

Although the Board of Directors is directly responsible for managing the affairs of the Company and for setting the policies which guide it, the day-to-day operations of the Company are performed by Basic Capital Management, Inc. ("BCM" or the "Advisor"), a contractual advisor under the supervision of the Board of Directors. The duties of the Advisor include, among other things, locating, investigating, evaluating and recommending real estate and mortgage note investment and sales opportunities, as well as financing and refinancing sources. The Advisor also serves as a consultant in connection with the Company's business plan and investment decisions made by the Board of Directors.

BCM is a company owned by a trust for the benefit of the children of Gene E. Phillips. Mr. Phillips served as a Trustee of the Company's predecessor business trust and as a Director of the Company until December 31, 1992. Mr. Phillips also served as a director of BCM until December 22, 1989 and as Chief Executive Officer of BCM until September 1, 1992. Mr. Phillips serves as a representative of his children's trust which owns BCM and, in such capacity, has substantial contact with the management of BCM and input with respect to its performance of advisory services to the Company. BCM is more fully described in ITEM 10. "DIRECTORS, EXECUTIVE OFFICERS AND ADVISOR OF THE REGISTRANT--The Advisor."

BCM has been providing advisory services to the Company since March 28, 1989. Renewal of BCM's advisory agreement was approved by stockholders at their annual meeting held on May 8, 1997. BCM also serves as advisor to CMET and Income Opportunity Realty Investors, Inc. ("IORI"). The Directors of the

Company are also trustees or directors of CMET and IORI and the officers of the Company are also officers of CMET and IORI. BCM also serves as advisor to American Realty Trust, Inc. ("ART"). Randall M. Paulson, President of the Company, also serves as President of BCM, CMET and IORI, and as Executive Vice President of ART. NRLP Management Corp. ("NMC"), a wholly-owned subsidiary of ART, is the general partner of National Realty, L.P. ("NRLP") and National Operating, L.P. ("NOLP"), the operating partnership of NRLP. BCM performs certain administrative functions for NRLP and NOLP on a cost-reimbursement basis. The officers of the Company are also officers of ART and NMC. As of March 5, 1999, the Company owned approximately 22.7% of IORI's outstanding shares of common stock and ART owned approximately 31.1% of the outstanding shares of the Company's Common Stock.

Since February 1, 1990, affiliates of BCM have provided property management services to the Company. Currently, Carmel Realty Services, Ltd. ("Carmel, Ltd.") provides such property management services. Carmel, Ltd. subcontracts with other entities for the provision of property-level management services to the Company. The general partner of Carmel, Ltd. is BCM. The limited partners of Carmel, Ltd. are (1) First Equity Properties, Inc. ("First Equity"), which is 50% owned by a subsidiary of BCM, (2) Gene E. Phillips and (3) a trust for the benefit of the children of Mr. Phillips. Carmel, Ltd. subcontracts the property-level management and leasing of

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29 of the Company's commercial properties, its four hotels and the commercial properties owned by a real estate partnership in which the Company and IORI are partners to Carmel Realty, Inc. ("Carmel Realty"), which is a company owned by First Equity. Carmel Realty is entitled to receive property and construction management fees and leasing commissions in accordance with the terms of its property-level management agreement with Carmel, Ltd. Carmel Realty is also entitled to receive real estate brokerage commissions in accordance with the terms of a non-exclusive brokerage agreement as discussed in ITEM 10. "DIRECTORS, EXECUTIVE OFFICERS AND ADVISOR OF THE REGISTRANT--The Advisor."

The Company has no employees. Employees of the Advisor render services to the Company.

#### Competition

The real estate business is highly competitive and the Company competes with numerous entities engaged in real estate activities (including certain entities described in ITEM 13. "CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS--Related Party Transactions"), some of which have greater financial resources than those of the Company. Management believes that success against such competition is dependent upon the geographic location of the property, the performance of property managers in areas such as marketing, collections and the ability to control operating expenses, the amount of new construction in the area and the maintenance and appearance of the property. Additional competitive factors with respect to commercial properties are the ease of access to the property, the adequacy of related facilities, such as parking, and sensitivity to market conditions in setting rent levels. With respect to apartments, competition is also based upon the design and mix of the units and the ability to provide a community atmosphere for the tenants. Management believes that general economic circumstances and trends and new or renovated properties in the vicinity of each of the Company's properties are also competitive factors.

To the extent that the Company seeks to sell any of its properties, the sales prices for such properties may be affected by competition from other real estate entities and financial institutions also attempting to sell their properties located in areas in which the Company's properties are located, as well as by aggressive buyers attempting to penetrate or dominate a particular market.

As described above and in ITEM 13. "CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS--Related Party Transactions", the officers and Directors of the Company also serve as officers or trustees or directors of certain other entities, each of which is also advised by BCM, and each of which has business objectives similar to those of the Company. The Company's Directors, officers and Advisor owe fiduciary duties to such other entities as well as to the Company under applicable law. In determining to which entity a particular investment opportunity will be allocated, the officers, directors or trustees and the Advisor consider the respective investment objectives of each such entity and the appropriateness of a particular investment in light of each such entity's existing real estate portfolio. To the extent that any particular investment opportunity is appropriate to more than one of such entities, such investment opportunity will be allocated to the entity which has had funds available for investment for the longest period of time or, if appropriate, the investment may be shared among all or some of such entities.

In addition, as also described in ITEM 13. "CERTAIN RELATIONSHIPS AND

RELATED TRANSACTIONS--Certain Business Relationships," the Company also competes with other entities which are affiliates of the Advisor and which may have investment objectives similar to the Company's and that may compete with it in purchasing, selling, leasing and financing of real estate and real estate related investments. In resolving any potential conflicts of interest which may arise, the Advisor has informed management that it intends to continue to exercise its best judgment as to what is fair and reasonable under the circumstances in accordance with applicable law.

#### Certain Factors Associated with Real Estate and Related Investments

The Company is subject to all the risks incident to ownership and financing of real estate and interests therein, many of which relate to the general illiquidity of real estate investments. These risks include, but are not

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limited to, changes in general or local economic conditions, changes in interest rates and the availability of permanent mortgage financing which may render the purchase, sale or refinancing of a property difficult or unattractive and which may make debt service burdensome, changes in real estate and zoning laws, increases in real estate taxes, federal or local economic or rent controls, floods, earthquakes, hurricanes and other acts of God and other factors beyond the control of management or the Advisor. The illiquidity of real estate investments may also impair the ability of management to respond promptly to changing circumstances. Management believes that such risks are partially mitigated by the diversification by geographic region and property type of the Company's real estate and mortgage notes receivable portfolios. However, to the extent new property investments or mortgage lending is concentrated in any particular region or property type, the advantages of diversification may be mitigated.

#### ITEM 2. PROPERTIES

The Company's principal offices are located at 10670 North Central Expressway, Suite 300, Dallas, Texas 75231. In the opinion of management, the offices are suitable and adequate for the Company's present operations.

Details of the Company's real estate and mortgage notes receivable portfolios at December 31, 1998, are set forth in Schedules III and IV, respectively, to the Consolidated Financial Statements included at ITEM 8. "FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA." The discussions set forth below under the headings "Real Estate" and "Mortgage Loans" provide certain summary information concerning the real estate and mortgage notes receivable portfolios.

The Company's real estate portfolio consists of properties held for investment, properties held for sale, primarily obtained through foreclosure of the collateral securing mortgage notes receivable and investments in partnerships. The discussion set forth below under the heading "Real Estate" provides certain summary information concerning the Company's real estate and further summary information with respect to the properties held for investment, properties held for sale and its investment in partnerships.

At December 31, 1998, none of the Company's properties, mortgage notes receivable or investment in a partnership exceeded 10% or more of the Company's total assets. At December 31, 1998, 91% of the Company's assets consisted of properties held for investment, less than 1% consisted of properties held for sale, less than 1% consisted of mortgage notes and interest receivable and 1% consisted of investments in partnerships. The remaining 7% of the Company's assets at December 31, 1998 were invested in cash, cash equivalents and other assets. The percentage of the Company's assets invested in any one category is subject to change and no assurance can be given that the composition of the Company's assets in the future will approximate the percentages listed above.

The Company's real estate is geographically diverse. At December 31, 1998, the Company held investments in apartments and commercial properties in each of the geographic regions of the continental United States, although its apartments and commercial properties are concentrated in the Southeast and Southwest regions, as shown more specifically in the table under "Real Estate" below. At December 31, 1998, the Company held mortgage notes receivable secured by apartments and commercial properties in the Southwest region of the continental United States, as shown more specifically in the table under "Mortgage Loans" below.

To continue to qualify for federal taxation as a REIT under the Code, the Company is required, among other things, to hold at least 75% of the value of its total assets in real estate assets, government securities, cash and cash equivalents at the close of each quarter of each taxable year.

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## Geographic Regions

The Company has divided the continental United States into the following geographic regions.

Northeast region comprised of the states of Connecticut, Delaware, Maryland, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island and Vermont, and the District of Columbia. The Company owns 3 apartments in this region.

Southeast region comprised of the states of Alabama, Florida, Georgia, Mississippi, North Carolina, South Carolina, Tennessee and Virginia. The Company owns 4 apartments and 12 commercial properties in this region.

Southwest region comprised of the states of Arizona, Arkansas, Louisiana, New Mexico, Oklahoma and Texas. The Company owns 26 apartments and 8 commercial properties in this region.

Midwest region comprised of the states of Illinois, Indiana, Iowa, Kansas, Kentucky, Michigan, Minnesota, Missouri, Nebraska, North Dakota, Ohio, South Dakota, West Virginia and Wisconsin. The Company owns 3 commercial properties and 3 hotels in this region.

Mountain region comprised of the states of Colorado, Idaho, Montana, Nevada, Utah and Wyoming. The Company owns 2 commercial properties in this region.

Pacific region comprised of the states of California, Oregon and Washington. The Company owns 5 apartments, 1 hotel and 5 commercial properties in this region.

Excluded from the above are nine parcels of unimproved land, as described below.

## Real Estate

At December 31, 1998, over 90% of the Company's assets were invested in real estate. The Company invests in real estate located throughout the continental United States, either on a leveraged or nonleveraged basis. The Company's real estate portfolio consists of properties held for investment, investments in partnerships and properties held for sale (which were primarily obtained through foreclosure of the collateral securing mortgage notes receivable).

Types of Real Estate Investments. The Company's real estate consists of commercial properties (office buildings, industrial warehouses and shopping centers), hotels and apartments having established income-producing capabilities. In selecting new real estate investments, the location, age and type of property, gross rentals, lease terms, financials and business standing of tenants, operating expenses, fixed charges, land values and physical condition are among the factors considered. The Company may acquire properties subject to or assume existing debt and may mortgage, pledge or otherwise obtain financing for its properties. The Board of Directors may alter the types of and criteria for selecting new real estate investments and for obtaining financing without a vote of stockholders.

The Company has typically invested in developed real estate. The Company may, however also invest in new construction or development either directly or in partnership with nonaffiliated parties or affiliates (subject to approval by the Board of Directors). To the extent that the Company invests in construction and development

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projects, it will be subject to business risks, such as cost overruns and construction delays, associated with such higher risk projects.

At December 31, 1998, the Company had expended \$1.9 million for the construction of the 260 unit Limestone Canyon Apartments in Austin, Texas. The Company expects to expend an additional \$12.8 million to complete construction in the fourth quarter of 1999. The Company has in place a construction loan which will fund up to \$13.0 million of such construction costs.

In the opinion of management, the properties owned by the Company are adequately covered by insurance.

The following table sets forth the percentages, by property type and geographic region, of the Company's real estate (other than four hotels in the Pacific and Midwest regions and nine parcels of unimproved land, as described below) at December 31, 1998.

<TABLE>  
<CAPTION>

COMMERCIAL

REGION	APARTMENTS	PROPERTIES
<S>	<C>	<C>
Pacific.....	6%	9%
Midwest.....	--	14
Northeast.....	10	--
Southwest.....	69	22
Southeast.....	15	50
Mountain.....	--	5
	---	---
	100%	100%

</TABLE>

The foregoing table is based solely on the number of apartment units and amount of commercial square footage owned and does not reflect the value of the Company's investment in each region. The Company also owns nine parcels of unimproved land, 3 parcels of 65.79 acres, 4.66 acres and .67 acre in the Southeast and Southwest region and 6 parcels of .9250 acres, 1.41 acres, 2.14 acres, 4.7 acres, 8.844 acres and 22.99 acres, in the Southwest region, all of which, other than the last five parcels, are held for sale. See Schedule III to the Consolidated Financial Statements included at ITEM 8. "FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA" for a more detailed description of the Company's real estate portfolio.

A summary of activity in the Company's owned real estate portfolio during 1998 is as follows:

<S>	<C>
Owned properties in real estate portfolio at January 1, 1998.....	62
Properties purchased.....	22
Properties sold.....	(4)
Property obtained through foreclosure.....	1
	---
Owned properties in real estate portfolio at December 31, 1998.....	81
	===

</TABLE>

Properties Held for Investment. Set forth below are the Company's properties held for investment and the monthly rental rate for apartments, the average annual rental rate for commercial properties and the average daily room rate and room revenue divided by total available rooms for hotels and occupancy at December 31, 1998, 1997 and 1996 for apartments and commercial properties and average occupancy during 1998, 1997 and 1996 for hotels:

<TABLE>  
<CAPTION>

Property	Location	Units/ Square Footage	Rent Per Square Foot			Occupancy %		
			1998	1997	1996	1998	1997	1996
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Apartments								
4400.....	Midland, TX	92 Units/94,472 Sq. Ft.	\$.49	* \$ *	* 98	* *	* *	
Arbor Point.....	Odessa, TX	195 Units/178,920 Sq. Ft.	.42	.41	.37	78	85	65
Ashton Way.....	Midland, TX	178 Units/138,964 Sq. Ft.	.41	*	*	93	*	*
Bent Tree.....	Addison, TX	204 Units/196,300 Sq. Ft.	.70	*	*	93	*	*
Carseka.....	Los Angeles, CA	54 Units/37,068 Sq. Ft.	1.01	.97	.93	97	98	100
Cliffs of Eldorado.....	McKinney, TX	208 Units/182,288 Sq. Ft.	.92	*	*	80	*	*
Country Bend.....	Fort Worth, TX	166 Units/143,366 Sq. Ft.	.58	.54	*	94	92	*
Coventry.....	Midland, TX	120 Units/105,608 Sq. Ft.	.42	.39	.37	91	96	92
Crescent Place.....	Houston, TX	120 Units/95,520 Sq. Ft.	.60	.57	*	97	93	*
Fairpark.....	Los Angeles, CA	49 Units/43,431 Sq. Ft.	.93	.24	*	99	91	*
Fountain Village.....	Tucson, AZ	410 Units/363,079 Sq. Ft.	.69	.65	.65	91	93	93
Fountains of Waterford..	Midland, TX	172 Units/129,200 Sq. Ft.	.35	*	*	2	*	*
Gladstell Forest.....	Conroe, TX	168 Units/121,536 Sq. Ft.	.70	.67	.65	97	92	92
Harper's Ferry.....	Lafayette, LA	122 Units/112,500 Sq. Ft.	.55	.51	.48	95	97	96
Heritage.....	Tulsa, OK	136 Units/92,464 Sq. Ft.	.69	.64	.62	94	95	95
Hunters Glen.....	Midland, TX	212 Units/174,180 Sq. Ft.	.37	*	*	90	*	*
Limestone Canyon.....	Austin, TX	260 Units/216,000 Sq. Ft.	**	**	**	**	**	**
Mariners Pointe.....	St. Petersburg, FL	368 Units/310,494 Sq. Ft.	.53	.51	.51	93	85	89
Mountain Plaza.....	El Paso, TX	188 Units/220,710 Sq. Ft.	.47	*	*	92	*	*
Sandstone.....	Mesa, AZ	238 Units/363,079 Sq. Ft.	.33	.30	*	94	93	*
Shadow Run.....	Pinellas Park, FL	276 Units/216,400 Sq. Ft.	.76	.74	.71	97	97	96
South Cochran.....	Los Angeles, CA	64 Units/43,100 Sq. Ft.	1.06	.96	.93	99	96	96
Southgate.....	Odessa, TX	180 Units/151,656 Sq. Ft.	.44	.43	.39	88	87	63
Southgreen.....	Bakersfield, CA	80 Units/66,000 Sq. Ft.	.17	*	*	95	*	*
Spa Cove.....	Annapolis, MD	303 Units/305,989 Sq. Ft.	.81	.77	.75	95	94	93
Summerfield.....	Orlando, FL	224 Units/204,116 Sq. Ft.	.66	.63	.59	91	93	92



Summerstone.....	Houston, TX	242 Units/188,734 Sq. Ft.	.63	.61	.59	96	93	94
Sunchase.....	Odessa, TX	300 Units/223,048 Sq. Ft.	.44	.43	*	92	90	*
Terrace Hills.....	El Paso, TX	310 Units/233,192 Sq. Ft.	.63	.58	*	97	95	*
Timbers.....	Tyler, TX	180 Units/101,666 Sq. Ft.	.54	.54	*	87	92	*
Treehouse.....	Irving, TX	160 Units/153,072 Sq. Ft.	.68	.62	*	96	99	*
Villas at Countryside...	Sterling, VA	102 Units/92,840 Sq. Ft.	.97	.94	*	99	96	*
Villa Piedra.....	Los Angeles, CA	132 Units/81,790 Sq. Ft.	1.04	.30	*	98	89	*
Westgate of Laurel.....	Laurel, MD	218 Units/201,704 Sq. Ft.	.85	.82	.81	95	96	96
Westwood.....	Odessa, TX	79 Units/49,001 Sq. Ft.	.45	.45	.40	99	87	65
Woodland Hills.....	San Antonio, TX	96 Units/57,800 Sq. Ft.	.66	.66	.66	84	86	90
Woods Edge.....	Rockville, MD	162 Units/146,460 Sq. Ft.	1.02	.95	.93	96	94	93
Woodview.....	Odessa, TX	232 Units/165,840 Sq. Ft.	.51	*	*	85	*	*

</TABLE>

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<TABLE>  
<CAPTION>

Property	Location	Units/ Square Footage/ Rooms/Acres	Rent Per Square Foot/ Average Room Rate			Occupancy %			Total Room Revenues Divided By Total Available Rooms		
			1998	1997	1996	1998	1997	1996	1998	1997	1996
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Office Buildings											
74 New Montgomery..	San Francisco, CA	109,497 Sq. Ft.	\$ 20.46	\$ 16.18	\$ 14.88	98	97	92			
Atrium.....	Palm Beach, FL	74,603 Sq. Ft.	8.86	*	*	99	*	*			
Bonita Plaza.....	Bonita, CA	47,777 Sq. Ft.	16.59	20.81	*	88	61	*			
Corporate Pointe...	Chantilly, VA	65,918 Sq. Ft.	14.92	13.69	13.41	100	100	100			
Daley Plaza.....	San Diego, CA	62,425 Sq. Ft.	14.69	*	*	92	*	*			
Forum.....	Richmond, VA	79,791 Sq. Ft.	14.82	14.64	14.02	81	96	100			
Hartford.....	Dallas, TX	174,513 Sq. Ft.	9.93	8.86	9.44	57	46	46			
Institute Place....	Chicago, IL	144,915 Sq. Ft.	14.73	12.95	12.31	95	86	75			
Lexington Center...	Colorado Springs, CO	74,603 Sq. Ft.	10.93	9.57	*	80	60	*			
One Steeplechase...	Sterling, VA	103,376 Sq. Ft.	15.74	15.24	14.75	100	100	100			
Parkway North.....	Dallas, TX	71,041 Sq. Ft.	12.62	*	*	78	*	*			
Plaza on Bachman											
Creek.....	Dallas, TX	80,278 Sq. Ft.	10.66	*	*	69	*	*			
Plaza Towers.....	St. Petersburg, FL	186,281 Sq. Ft.	13.33	12.77	12.15	100	96	88			
Savings of											
America.....	Houston, TX	68,634 Sq. Ft.	9.70	11.16	*	89	90	*			
Town and Country...	Houston, TX	64,089 Sq. Ft.	5.06	4.80	4.47	68	76	67			
Valley Rim.....	San Diego, CA	54,194 Sq. Ft.	15.81	*	*	88	*	*			
Venture Center.....	Atlanta, GA	38,272 Sq. Ft.	14.74	13.07	12.67	71	100	94			
Viewridge.....	San Diego, CA	25,062 Sq. Ft.	7.20	*	*	87	*	*			
Waterstreet.....	Boulder, CO	106,257 Sq. Ft.	17.56	16.73	15.60	98	99	96			
Industrial											
Warehouses											
Corporate Center...	Ashburn, VA	177,563 Sq. Ft.	6.32	5.93	5.64	100	98	80			
Encon.....	Fort Worth, TX	256,410 Sq. Ft.	2.00	1.66	*	100	100	*			
Parke Long.....	Chantilly, VA	217,132 Sq. Ft.	6.69	6.15	5.32	87	87	80			
Technology											
Trading.....	Sterling, VA	197,659 Sq. Ft.	5.76	5.10	5.26	87	70	78			
Texstar.....	Arlington, TX	97,846 Sq. Ft.	2.11	2.11	1.86	100	100	100			
Tricon.....	Atlanta, GA	570,877 Sq. Ft.	3.59	3.44	3.29	98	91	93			
Shopping Centers											
Dunes Plaza.....	Michigan City, IN	223,869 Sq. Ft.	4.84	4.58	4.49	43	77	82			
K-Mart.....	Cary, NC	92,033 Sq. Ft.	3.28	***	***	100	***	***			
Parkway Center....	Dallas, TX	28,374 Sq. Ft.	13.86	13.00	12.01	94	100	94			
Sadler Square.....	Amelia Island, FL	70,295 Sq. Ft.	6.90	6.76	6.54	95	96	95			
Sheboygan.....	Sheboygan, WI	74,532 Sq. Ft.	1.99	1.99	1.99	100	100	100			
Hotels											
Belmont.....	Chicago, IL	45 Rooms	101.13	*	*	68	*	*	\$ 67.93	\$ *	\$ *
Brompton.....	Chicago, IL	52 Rooms	98.08	*	*	50	*	*	46.54	*	*
Majestic Inn.....	San Francisco, CA	57 Rooms	148.96	136.08	117.45	71	73	70	112.54	93.26	76.50
Surf.....	Chicago, IL	55 Rooms	98.85	*	*	57	*	*	56.12	*	*
Land											
Eagle Crest.....	Farmers Branch, TX	22.99 Acres									
Las Colinas.....	Las Colinas, TX	4.7 Acres									
Laws.....	Dallas, TX	1.41 Acres									
Lemmon Carlisle....	Dallas, TX	2.14 Acres									
West End.....	Dallas, TX	8.844 Acres									

</TABLE>

\* Property was purchased in either 1997 or 1998.  
 \*\* Property was under construction at December 31, 1998.  
 \*\*\* Obtained through foreclosure in 1998.

Occupancy presented here and throughout this ITEM 2. is without reference to

whether leases in effect are at, below or above market rates.

In January 1998, the Company purchased the 188 unit Mountain Plaza Apartments in El Paso, Texas, for \$4.0 million, paying \$1.0 million in cash and obtaining mortgage financing of \$3.0 million. The mortgage bears interest at 8.2% per annum, requires monthly payments of interest only and matures in January 2000. A real estate brokerage commission of \$139,000 was paid to Carmel Realty and a real estate acquisition fee of \$39,000 was paid to BCM.

Also in January 1998, the Company purchased the 212 unit Hunters Glen Apartments in Midland, Texas, for \$2.5 million, paying \$600,000 in cash and obtaining seller financing of \$1.9 million. The financing bears interest at a variable rate, currently 8.0% per annum, requires monthly payments of interest only for the first twenty-four months and thereafter requires monthly payments of principal and interest of \$14,302 and matures in January 2003. A real estate brokerage commission of \$94,000 was paid to Carmel Realty and a real estate acquisition fee of \$25,000 was paid to BCM.

Further in January 1998, the Company purchased the Laws Street land, a 1.41 acre parcel of land in Dallas, Texas, for \$1.9 million in cash. A real estate brokerage commission of \$39,000 was paid to Carmel Realty and a real estate acquisition fee of \$19,000 was paid to BCM.

In January 1998, the Company purchased the 204 unit Bent Tree Garden Apartments in Addison, Texas, for \$8.1 million, paying \$1.7 million in cash and obtaining mortgage financing of \$6.4 million. The mortgage bears interest at 7.2% per annum, requires monthly payments of principal and interest of \$46,054 and matures in February 2008. A real estate brokerage commission of \$232,000 was paid to Carmel Realty and a real estate acquisition fee of \$81,000 was paid to BCM.

In February 1998, the Company purchased Parkway North, a 71,041 sq. ft. office building in Dallas, Texas, for \$5.4 million, paying \$1.5 million in cash and obtaining mortgage financing of \$3.9 million. The mortgage bears interest at a variable rate, currently 8.69% per annum, requires monthly payments of interest only and matures in March 2000. A real estate brokerage commission of \$179,000 was paid to Carmel Realty and a real estate acquisition fee of \$54,000 was paid to BCM.

Also in February 1998, the Company purchased the Lemmon Carlisle land, a 2.14 acre parcel of land in Dallas, Texas, for \$3.4 million in cash. A real estate brokerage commission of \$54,000 was paid to Carmel Realty and a real estate acquisition fee of \$34,000 was paid to BCM.

In March 1998, the Company purchased the Plaza on Bachman Creek, a 80,278 sq. ft. retail/office complex in Dallas, Texas, for \$3.5 million, paying \$1.1 million in cash and obtaining mortgage financing of \$2.4 million. The mortgage bears interest at a variable rate, currently 9% per annum, requires monthly payments of principal and interest of \$21,593 and matures in March 2018. A real estate brokerage commission of \$124,000 was paid to Carmel Realty and a real estate acquisition fee of \$35,000 was paid to BCM.

Also in March 1998, the Company refinanced the mortgage debt secured by the Tricon Warehouses in Atlanta, Georgia in the amount of \$10.2 million, receiving net cash of \$5.4 million after paying off \$4.8 million in mortgage debt, funding of escrows and the payment of various closing costs. The new mortgage bears interest at a variable rate, currently 7.53% per annum, requires monthly payments of principal and interest of \$75,576 and matures in April 2008. A mortgage brokerage and equity refinancing fee of \$102,000 was paid to BCM.

In April 1998, the Company purchased in a single transaction the 178 unit Ashton Way Apartments in Midland, Texas, and the 92 unit 4400 Apartments also in Midland, Texas, and in May 1998, the 232 unit Woodview Apartments in Odessa, Texas, for a total of \$6.8 million. The Company paid a total of \$1.5 million in cash and obtained mortgage financing secured by all three properties totaling \$5.3 million. The first mortgage of \$4.5 million bears interest at 7.2% per annum and the second mortgage of \$845,000 bears interest at a variable

rate, currently 8.2% per annum. The mortgages require monthly payments of principal and interest totaling \$38,003 and mature in October 1999 and May 2008, respectively. A real estate brokerage commission of \$244,000 was paid to Carmel Realty and a real estate acquisition fee of \$68,000 was paid to BCM.

In May 1998, the Company purchased the Eagle Crest land, a 22.99 acre parcel of land in Farmers Branch, Texas, for \$2.5 million in cash. A real estate brokerage commission of \$95,000 was paid to Carmel Realty and a real estate acquisition fee of \$25,000 was paid to BCM.

Also in May 1998, the Company purchased the 172 unit Fountains of Waterford

Apartments in Midland, Texas, for \$1.5 million, paying \$425,000 in cash, assuming the existing mortgage of \$584,000 and obtaining seller financing of the remaining \$491,000 of the purchase price. The mortgage bears interest at 9.91% per annum, and the seller financing at a variable rate, currently 7.5% per annum, require monthly payments of principal and interest totaling \$10,643 and mature in November 1999 and June 2008. A real estate brokerage commission of \$59,000 was paid to Carmel Realty and a real estate acquisition fee of \$15,000 was paid to BCM.

Further in May 1998, the Company purchased in a single transaction, Daley Plaza, a 62,425 sq. ft. office building and View Ridge, a 25,062 sq. ft. office building, both in San Diego, California, for a total of \$6.5 million. The Company paid \$1.7 million in cash and obtained mortgage financing totaling \$4.8 million. The mortgages bear interest at a variable rate, currently 9.5% per annum, require monthly payments of principal and interest totaling \$42,416 and mature in May 2005. A real estate brokerage commission of \$200,000 was paid to Carmel Realty and a real estate acquisition fee of \$65,000 was paid to BCM.

In May 1998, the Company obtained mortgage financing in the amount of \$2.2 million secured by its unencumbered Lemmon Carlisle land in Dallas, Texas, receiving net cash of \$2.1 million after the payment of various closing costs. The mortgage bears interest at 9.25% per annum, requires monthly payment of interest only and matures in May 2000. A mortgage brokerage and equity refinancing fee of \$22,000 was paid to BCM.

Also in May 1998, the Company refinanced the mortgage debt secured by the Plaza Towers Office Building in St. Petersburg, Florida in the amount of \$7.4 million, receiving net cash of \$2.6 million after paying off \$4.8 million in mortgage debt, funding of required escrows and the payment of various closing costs. The new mortgage bears interest at 7.57% per annum, requires monthly payments of principal and interest of \$55,023 and matures in June 2008. A mortgage brokerage and equity refinancing fee of \$74,000 was paid to BCM.

In June 1998, the Company purchased the Atrium, a 74,603 sq. ft. office building in Palm Beach, Florida, for \$5.4 million, paying \$1.3 million in cash and obtaining mortgage financing of \$4.1 million. The mortgage bears interest at a variable rate, currently 7.93% per annum, requires monthly payments of principal and interest of \$31,455 and matures in July 2001. A real estate brokerage commission of \$179,000 was paid to Carmel Realty and a real estate acquisition fee of \$54,000 was paid to BCM.

In July 1998, the Company purchased Valley Rim, a 54,194 sq. ft. office building in San Diego, California, for \$5.1 million, paying \$1.4 million in cash and obtaining mortgage financing of \$3.7 million. The mortgage bears interest at a variable rate, currently 9.5% per annum, requires monthly payments of principal and interest of \$32,576 and matures in June 2005. A real estate brokerage commission of \$172,000 was paid to Carmel Realty and an acquisition fee of \$51,000 was paid to BCM.

Also in July 1998, the Company purchased the Limestone Canyon land, a 27 acre parcel of unimproved land in Austin, Texas, for \$1.8 million in cash. In conjunction with the purchase, the Company obtained a financing commitment of \$13.0 million for the construction of a 260 unit apartment on the site. The mortgage bears interest at a variable rate, currently 7.63% per annum, requires monthly payments of interest only and matures in July 2000. A real estate brokerage commission of \$70,000 was paid to Carmel Realty and an acquisition fee of \$18,000 was paid to BCM. Construction was commenced in August 1998 and is expected to be completed in the fourth quarter of 1999.

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Further in July 1998, the Company refinanced the matured mortgage debt secured by the Villas at Countryside Apartments in Sterling, Virginia, in the amount of \$5.4 million, receiving net cash of \$400,000 after paying off \$5.0 million in mortgage debt, funding of required escrows and the payment of various closing costs. The new mortgage bears interest at 6.85% per annum, requires monthly payments of principal and interest of \$35,692 and matures in August 2005. A mortgage brokerage and equity refinancing fee of \$54,000 was paid to BCM.

In August 1998, the Company obtained second lien financing of \$1.8 million secured by the Terrace Hills Apartments in El Paso, Texas, receiving net cash of \$1.7 million after the payment of various closing costs. The mortgage bears interest at 7.275% per annum, requires monthly payments of principal and interest of \$11,968 and matures in September 2009. A mortgage brokerage and equity refinancing fee of \$18,000 was paid to BCM.

At December 31, 1997, the Company held a wraparound mortgage note with a principal balance of \$2.5 million secured by a K-Mart in Cary, North Carolina. In February 1998, the Company was informed that the first lien mortgage in the amount of \$2.0 million was in default. To protect its interest, the Company

foreclosed on the property in August 1998 and refinanced the first lien mortgage in the amount of \$2.0 million, paying \$265,000 in cash to complete the refinancing. The new mortgage bears interest at 7.51% per annum, requires monthly payments of principal and interest of \$15,721 and matures in September 2008. A mortgage brokerage and equity refinancing fee of \$19,500 was paid to BCM. No loss was recognized on the foreclosure as the fair value of the property exceeded the carrying value of the note receivable. The property was classified as held for investment as of December 31, 1998.

In 1997, Montgomery Ward ("Ward"), a tenant at the Northtown Mall, a 354,174 sq. ft. shopping center in Dallas, Texas, filed for bankruptcy protection. In an attempt to keep the Ward lease from being sold, Northtown Mall was placed in administrative bankruptcy. Wards Northtown Mall lease, as well as other Ward leases were, however, sold for the benefit of the Ward bankruptcy estate. In September 1998, the Company bought back the lease concurrent with the \$15.6 million sale of Northtown Mall. The Company received net cash of \$12.1 million after paying off \$2.5 million of mortgage debt, \$900,000 for the Ward lease and the payment of various closing costs. In conjunction with the sale, the Northtown Mall bankruptcy proceeding was dismissed. A real estate brokerage commission of \$135,000 was paid to Carmel Realty. A gain of \$3.4 million was recognized on the sale.

In September 1998, the Company sold Chesapeake Ridge, a 100,484 sq. ft. office building in San Diego, California, for \$13.2 million, receiving net cash of \$7.6 million after paying off \$5.3 million of mortgage debt and the payment of various closing costs, including a real estate brokerage commission of \$317,000 paid to Carmel Realty. A gain of \$5.9 million was recognized on the sale.

In October 1998, the Company sold Denton Drive, a 123,800 sq. ft. industrial warehouse in Dallas, Texas, for \$1.2 million, receiving net cash of \$845,000 after paying off \$309,000 in mortgage debt and the payment of various closing costs, including a real estate brokerage commission of \$46,000 paid to Carmel Realty. A gain of \$219,000 was recognized on the sale.

Also in October 1998, the Company purchased the 208 unit Cliffs of Eldorado Apartments in McKinney, Texas, for \$12.8 million, paying \$1.6 million in cash, assuming the existing mortgage of \$10.6 million and issuing 5,829 shares of Series A Cumulative Convertible Preferred Stock with a total liquidation value of \$583,000. The assumed mortgage bears interest at 8.125% per annum, requires monthly payments of principal and interest of \$75,197 and matures in November 2037. A real estate brokerage commission of \$312,000 was paid to Carmel Realty and a real estate acquisition fee of \$128,000 was paid to BCM.

Further in October 1998, the Company refinanced the matured mortgage debt secured by the Bonita Plaza Office Building in Bonita, California in the amount of \$5.2 million, receiving net cash of \$1.2 million after paying off \$4.0 million in mortgage debt, funding of required escrows and the payment of various closing costs. The new mortgage bears interest at a variable rate, currently 7.4% per annum, requires monthly payments of principal and interest of \$37,722 and matures in November 2001. A mortgage brokerage and equity refinancing fee of \$52,000 was paid to BCM.

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In December 1998, the Company purchased the assets of the Neighborhood Inns of Chicago, consisting of three hotels in Chicago, Illinois, the Belmont with 45 rooms, the Brompton with 52 rooms, and the Surf with 55 rooms, for \$11.6 million. The Company paid \$2.3 million in cash and obtained mortgage financing secured by all three hotels of \$9.2 million. The mortgage bears interest at a variable rate, currently 9.376% per annum, requires monthly payments of principal and interest of \$94,108 and matures in December 2001. A real estate brokerage commission of \$293,000 was paid to Carmel Realty and a real estate acquisition fee of \$116,000 was paid to BCM.

Also in December 1998, the Company purchased the 80 unit Southgreen Apartments in Bakersfield, California for \$3.6 million, paying \$1.1 million in cash and obtaining mortgage financing of \$2.5 million. The mortgage bears interest at a variable rate, currently 8.25% per annum, requires monthly payments of principal and interest of \$19,953 and matures in December 2005. A real estate brokerage commission of \$127,000 was paid to Carmel Realty and a real estate acquisition fee of \$36,000 was paid to BCM.

In February 1999, the Company sold the 368 unit Mariner's Pointe Apartments in St. Petersburg, Florida, for \$6.7 million, receiving net cash of \$2.6 million after paying off \$3.9 million in mortgage debt and the payment of various closing costs, including a real estate brokerage commission of \$204,000 paid to Carmel Realty. A gain will be recognized on the sale.

In March 1999, the Company purchased the 264 unit Vista Hills Apartments in El Paso, Texas, for \$5.2 million, paying \$1.6 million in cash and obtaining mortgage financing of \$3.6 million. The mortgage bears interest at a variable rate, currently 7.625% per annum, requires monthly payments of principal and

interest of \$26,897 and matures in April 2004. A real estate brokerage commission of \$173,000 was paid to Carmel Realty and a real estate acquisition fee of \$52,000 was paid to BCM.

Also in March 1999, the Company purchased the Dominion land, a 14.39 acre parcel of land in Dallas, Texas, for \$3.6 million, paying \$1.2 million in cash and obtaining mortgage financing of \$2.4 million. The mortgage bears interest at 15% per annum, requires quarterly payments of interest only and matures in March 2000. A real estate brokerage commission of \$56,000 was paid to Carmel Realty and a real estate acquisition fee of \$36,000 was paid to BCM.

Further in March 1999, the Company refinanced the matured mortgage debt secured by the Lexington Center Office Building in Colorado Springs, Colorado in the amount of \$4.3 million, receiving net cash of \$136,000 after paying off \$4.0 million in mortgage debt and the payment of various closing costs. The new mortgage bears interest at a variable rate, currently 7.75% per annum, requires monthly payments of principal and interest of \$32,479 and matures in April 2004. A mortgage brokerage and equity refinancing fee of \$43,000 was paid to BCM.

Properties Held for Sale. Set forth below are the Company's properties held for sale, primarily obtained through foreclosure.

<TABLE>  
<CAPTION>

Property	Location	Square Footage/ Acres
<S>	<C>	<C>
Land		
Fiesta.....	San Angelo, TX	.6657 Acres
Fruitland.....	Fruitland Park, FL	4.66 Acres
Moss Creek.....	Greensboro, NC	65.79 Acres
Republic land.....	Dallas, TX	.9250 Acres

In March 1998, the Company completed the sale of Shaws Plaza, a 103,482 sq. ft. shopping center in Sharon, Massachusetts, which was under contract for sale at December 31, 1997, for \$3.8 million, receiving net

cash of \$1.1 million after paying off \$2.6 million in existing mortgage debt and the payment of various closing costs, including a real estate brokerage commission of \$134,000 paid to Carmel Realty. No gain or loss was recognized on the sale.

In October 1998, the Company sold approximately 19 acres of land in Greensboro, North Carolina, for \$375,000, receiving net cash of \$356,000 after the payment of various closing costs, including a real estate brokerage commission of \$15,000 paid to Carmel Realty. A gain of \$350,000 was recognized.

Partnership Properties. Set forth below are the properties owned by partnerships which the Company accounts for using the equity method and the monthly rental rate for apartments and the average annual rental rate for commercial properties and occupancy thereof at December 31, 1998, 1997 and 1996:

<TABLE>  
<CAPTION>

PROPERTY	LOCATION	UNITS/ SQUARE FOOTAGE	RENT PER SQUARE FOOT			OCCUPANCY %		
			1998	1997	1996	1998	1997	1996
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
APARTMENT								
Lincoln Court.....	Dallas, TX	55 Units/40,063 Sq. Ft.	\$1.08	\$1.04	\$ .99	95	99	98
OFFICE BUILDING								
MacArthur Mills.....	Carrollton, TX	53,472 Sq. Ft.	9.84	9.35	8.38	100	97	94
SHOPPING CENTERS								
Chelsea Square.....	Houston, TX	70,275 Sq. Ft.	8.61	9.21	9.32	81	49	69
Summit at Bridgewood....	Fort Worth, TX	48,696 Sq. Ft.	9.63	9.48	8.67	79	65	62

The Company owns a noncontrolling combined 55% limited and general partnership interest in Jor-Trans Investors Limited Partnership ("Jor-Trans") which owns the Lincoln Court Apartments.

The Company owns a noncontrolling combined 63.7% limited and general partner interest and IORI owns a 36.3% general partner interest in Tri-City Limited Partnership ("Tri-City") which owns the three other commercial properties in

the table above. In May 1998, Tri-City sold its two apartments for \$3.3 million in cash. Tri-City received net cash of \$1.4 million after paying off \$1.9 million in mortgage debt and the payment of various closing costs. The Company received a distribution of \$701,000 of such net cash. Tri-City recognized a gain of \$496,000 of which the Company's equity share was \$316,000. Tri-City paid a real estate brokerage commission of \$119,000 to Carmel Realty. In 1998, the Company made no advances to the partnership and received \$319,000 in operating distributions. See ITEM 13. "CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS--Related Party Transactions."

MORTGAGE LOANS

In addition to investments in real estate, a portion of the Company's assets are invested in mortgage notes receivable, principally secured by income-producing real estate. The Company expects that the percentage of its assets invested in mortgage loans may increase, as it has determined that in 1999 it may seek to fund or acquire mortgage loans. It may also originate mortgage loans in conjunction with providing purchase money financing of a property sale. The Company intends to service and hold for investment the mortgage notes in its portfolio. The Company's mortgage notes receivable consist of first and junior mortgage loans.

Types of Mortgage Activity. The Company may originate its own mortgage loans, as well as acquire existing mortgage notes either directly from builders, developers or property owners, or through mortgage banking firms, commercial banks or other qualified brokers. BCM, in its capacity as a mortgage servicer, services the Company's mortgage notes. The Company's investment policy is described in ITEM 1. "BUSINESS--Business Plan and Investment Policy."

Types of Properties Securing Mortgage Notes. The properties securing the Company's mortgage notes receivable portfolio at December 31, 1998, consisted of an apartment, a hotel, 5 developed residential lots and a

34,847 sq. ft. parcel of unimproved land. The Board of Directors may alter the types of properties securing or collateralizing mortgage loans in which the Company invests without a vote of stockholders. The Company's Articles of Incorporation impose certain restrictions on transactions with related parties, as discussed in ITEM 13. "CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS."

At December 31, 1998, the Company's mortgage notes receivable portfolio included 4 mortgage loans with an aggregate principal balance of \$1.7 million secured by income-producing real estate located in the Southeast and Southwest regions of the continental United States and 12 loans with an aggregate principal balance of \$654,000 secured by collateral other than income-producing real estate. At December 31, 1998, less than 1% of the Company's assets were invested in notes and interest receivable (less than 1% in junior and other mortgage notes).

The following table sets forth the percentages (based on the mortgage note principal balance) by property type and geographic region, of the properties (other than unimproved land) that serve as collateral for the Company's mortgage notes receivable at December 31, 1998. See Schedule IV to the Consolidated Financial Statements included at ITEM 8. "FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA" for further details of the Company's mortgage notes receivable portfolio.

```
<TABLE>
<CAPTION>
  REGION                                APARTMENTS  HOTEL  TOTAL
  -----                                -
  <S>                                     <C>      <C>  <C>
  Southwest.....                          79%     21% 100%
</TABLE>
```

A summary of the activity in the Company's mortgage notes receivable portfolio during 1998 is as follows:

```
<TABLE>
  <S>                                     <C>
  Loans in mortgage notes receivable portfolio at January 1, 1998..... 20
  Loans purchased..... 1
  Loans paid off..... (4)
  Loan foreclosed..... (1)
  -----
  Loans in mortgage notes receivable portfolio at December 31, 1998..... 16
  ===
</TABLE>
```

During 1998, \$2.9 million was collected in settlement of four mortgage notes

and \$49,000 in principal payments were received.

At December 31, 1998, less than 1% of the Company's assets were invested in mortgage notes secured by non-income-producing real estate, comprised of a first mortgage note secured by 34,847 sq. ft. of unimproved land in Milwaukee, Wisconsin and five first mortgage notes secured by residential lots in Greensboro, North Carolina.

**First Mortgage Loans.** The Company invests in first mortgage notes, with short, medium or long-term maturities. First mortgage loans generally provide for level periodic payments of principal and interest sufficient to substantially repay the loan prior to maturity, but may involve interest-only payments or moderate amortization of principal and a "balloon" principal payment at maturity. With respect to first mortgage loans, the borrower is required to provide a mortgagee's title policy or an acceptable legal title opinion as to the validity and the priority of the mortgage lien over all other obligations, except liens arising from unpaid property taxes and other exceptions normally allowed by first mortgage lenders in the relevant area. The Company may grant to other lenders, participations in first mortgage loans that it originates.

The following discussion briefly describes the events that affected previously funded first mortgage loans during 1998.

In February 1994, the Company provided \$6.7 million of purchase money financing in conjunction with the sale of 1,406 acres of land in 16 residential and commercial subdivisions in Maumelle, Arkansas, secured by a

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first mortgage on the properties sold. The borrower did not make the scheduled February 1995 principal and interest payments. In September 1995, the Company reached a settlement with the borrower that provided for, among other things, the payment by the borrower of \$2.5 million in cash, and the acceptance of a new \$1.4 million note secured by 36.3 acres of commercial land. Such note matured in January 1996. In April 1998, the Company received \$2.1 million in full settlement of its note and accrued but unpaid interest. The original sale had been recorded under the cost recovery method with gain being deferred until the note was collected. Accordingly, the previously deferred gain of \$2.1 million was recognized on collection of the note.

In July 1998, a mortgage note receivable which had been written off in a prior year, was collected. A gain of \$671,000 was recognized.

**Wraparound Mortgage Loans.** A wraparound mortgage loan, sometimes called an all-inclusive loan, is a mortgage loan having an original principal balance equal to the outstanding balance under the prior existing mortgage loan(s) plus the amount actually advanced under the wraparound mortgage loan. Wraparound mortgage loans may provide for full, partial or no amortization of principal. The Company's policy is to make wraparound mortgage loans in amounts and on properties as to which it would otherwise make first mortgage loans.

The following discussion briefly describes the events that affected previously funded wraparound mortgage loans during 1998.

As discussed under "Real Estate" above, at December 31, 1997, the Company held a wraparound mortgage note with a principal balance of \$2.5 million secured by a K-Mart in Cary, North Carolina. In February 1998, the Company was informed that the first lien mortgage in the amount of \$2.0 million was in default. To protect its interest, the Company foreclosed on the property in August 1998 and refinanced the first lien mortgage in the amount of \$2.0 million, paying \$265,000 in cash to complete the refinancing. No loss was recognized on the foreclosure as the fair value of the property exceeded the carrying value of the note receivable.

**Junior Mortgage Loans.** The Company may invest in junior mortgage loans. Such loans are secured by mortgages that are subordinate to one or more prior liens either on the fee or a leasehold interest in real estate. Recourse on such loans ordinarily includes the real estate on which the loan is made, other collateral and personal guarantees by the borrower. The Board of Directors restricts investment in junior mortgage loans, excluding wraparound mortgage loans, to not more than 10% of the Company's assets. At December 31, 1998, less than 1% of the Company's assets were invested in junior mortgage loans.

The following discussion briefly describes the events that affected previously funded junior mortgage loans in 1998.

In August 1998, a mortgage note receivable with a principal balance of \$2.0 million and a carrying value of \$207,000 and secured by a second lien on a hotel in Lake Charles, Louisiana became delinquent. To protect its interest, the Company purchased the first lien mortgage for \$149,000. Foreclosure proceedings have commenced and title to the property is expected to be

received in the second quarter of 1999. No loss is expected to be incurred on foreclosure, as the estimated fair value of the property exceeds the carrying value of the mortgage notes receivable.

Loans Secured by Collateral Other than Real Estate. In June 1992, the Company received ten notes receivable secured by collateral other than real estate in satisfaction of a \$622,000 obligation. At December 31, 1998, five of the notes with a combined principal balance of \$374,000 remained outstanding. The Company's investment policy precludes the origination of loans secured by collateral other than real estate.

Partnership mortgage loans. The Company owns a 60% general partner interest and IORI owns a 40% general partner interest in Nakash Income Associates ("NIA"), which owns a wraparound mortgage note receivable secured by a building occupied by a Wal-Mart in Maulden, Missouri. The Company received \$9,000 in distributions from NIA in 1998 and advanced \$14,000 to the partnership.

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### ITEM 3. LEGAL PROCEEDINGS

#### Olive Litigation

In February 1990, the Company, together with CMET, IORI and National Income Realty Trust, three real estate entities with, at the time, the same officers, directors or trustees and advisor as the Company, entered into a settlement of a class and derivative action entitled Olive et al. v. National Income Realty Trust et al., in the United States District Court for the Northern District of California relating to the operation and management of each of such entities. On April 23, 1990, the Court granted final approval of the terms of the settlement.

On May 4, 1994, the parties entered into a Modification of Stipulation of Settlement dated April 27, 1994 (the "Olive Modification") that settled subsequent claims of breaches of the settlement that were asserted by the plaintiffs and modified certain provisions of the April 1990 settlement. The Olive Modification was preliminarily approved by the Court on July 1, 1994 and final Court approval was entered on December 12, 1994. The effective date of the Olive Modification was January 11, 1995.

The Court retained jurisdiction to enforce the Olive Modification, and during August and September 1996, the Court held evidentiary hearings to assess compliance with the terms of the Olive Modification by the various parties. The Court issued no ruling or order with respect to the matters addressed at the hearings.

Separately, in 1996, legal counsel for the plaintiffs notified the Company's Board of Directors that he intended to assert that certain actions taken by the Board of Directors breached the terms of the Olive Modification. On January 27, 1997, the parties entered into an Amendment to the Olive Modification effective January 9, 1997 (the "Olive Amendment"), which was submitted to the Court for approval on January 29, 1997. The Olive Amendment provides for the settlement of all matters raised at the evidentiary hearings and by plaintiffs' counsel in his notices to the Company's Board of Directors. On May 2, 1997, a hearing was held for the Court to consider approval of the Olive Amendment. As a result of the hearing, the parties entered into a revised Olive Amendment. The Court issued an order approving the Olive Amendment on July 3, 1997.

The Olive Amendment provides for the addition of four new unaffiliated members to the Company's Board of Directors and sets forth new requirements for the approval of any transactions with certain affiliates until April 28, 1999. In addition, the Company, CMET, IORI and their stockholders released the defendants from any claims relating to the plaintiffs' allegations and matters which were the subject of the evidentiary hearings. The plaintiffs' allegations of any breaches of the Olive Modification shall be settled by mutual agreement of the parties or, lacking such agreement, by an arbitration proceeding.

Under the Olive Amendment, all shares of the Company owned by Gene E. Phillips or any of his affiliates shall be voted at all stockholder meetings of the Company held until April 28, 1999 in favor of all new members of the Company's Board of Directors added under the Olive Amendment. The Olive Amendment also requires that, until April 28, 1999, all shares of the Company owned by Mr. Phillips or his affiliates in excess of forty percent (40%) of the Company's outstanding shares shall be voted in proportion to the votes cast by all non-affiliated stockholders of the Company.

In accordance with the Olive Amendment, Richard W. Douglas, Larry E. Harley and R. Douglas Leonhard were added to the Company's Board of Directors in January 1998 and Murray Shaw was added to the Company's Board of Directors in February 1998.



ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

Not applicable.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

The Company's Common Stock is traded on the New York Stock Exchange ("NYSE") using the symbol "TCI". The following table sets forth the high and low sales prices as reported in the consolidated reporting system of the NYSE.

<TABLE>  
<CAPTION>

Quarter Ended	High	Low
<S>	<C>	<C>
March 31, 1999 (through March 5, 1999).....	\$16 3/8	\$12
March 31, 1998.....	18 1/4	14 1/4
June 30, 1998.....	17 15/16	14 3/4
September 30, 1998.....	16 1/4	12 1/2
December 31, 1998.....	14 1/2	11 1/2
March 31, 1997.....	14 7/8	10 3/4
June 30, 1997.....	15 5/8	10 3/4
September 30, 1997.....	21 1/4	14 1/2
December 31, 1997.....	21 3/8	13 3/8

</TABLE>

As of March 5, 1999, the closing price of the Company's Common Stock as reported in the consolidated reporting system of the NYSE was \$12.81 per share.

As of March 5, 1999, the Company's Common Stock was held by 5,025 holders of record.

The Company paid dividends in 1998 and in 1997 as follows:

<TABLE>  
<CAPTION>

Date Declared	Record Date	Payable Date	Amount Per Share
<S>	<C>	<C>	<C>
February 16, 1998	March 13, 1998	March 31, 1998	\$.15
May 27, 1998	June 4, 1998	June 19, 1998	.15
August 31, 1998	September 15, 1998	September 30, 1998	.15
November 24, 1998	December 15, 1998	December 30, 1998	.15
February 26, 1997	March 14, 1997	March 31, 1997	.07
June 5, 1997	June 13, 1997	June 30, 1997	.07
September 3, 1997	September 15, 1997	September 30, 1997	.07
December 1, 1997	December 15, 1997	December 31, 1997	.07

</TABLE>

The Company reported to the Internal Revenue Service that 100% of the dividends paid in 1998 and 1997 represented capital gains.

On December 5, 1989, the Board of Directors approved a share repurchase program. The Board of Directors authorized the repurchase of a total of 687,000 shares of the Company's Common Stock pursuant to such program. Through December 31, 1998, a total of 409,765 shares had been repurchased at a cost of \$3.3 million, 21,950 of such shares having been purchased in 1998, at a cost of \$336,000.

ITEM 6. SELECTED FINANCIAL DATA

<TABLE>  
<CAPTION>

For the Years Ended December 31,					
	1998	1997	1996	1995	1994
<S>	<C>	<C>	<C>	<C>	<C>
	(dollars in thousands, except per share)				

EARNINGS DATA					
Revenues.....	\$ 70,636	\$ 55,961	\$ 46,878	\$ 48,272	\$ 37,983
Expenses.....	76,602	65,578	56,499	58,174	47,154
	-----	-----	-----	-----	-----
(Loss) from operations..	(5,966)	(9,617)	(9,621)	(9,902)	(9,171)
Equity in income (loss) of investees.....	288	812	(20)	(1,083)	(90)
Gain on sale of partnership interests..	--	--	--	--	2,514
Gain on sale of real estate.....	12,584	21,404	1,579	5,822	2,153
Extraordinary gain.....	--	--	--	1,293	1,189
	-----	-----	-----	-----	-----
Net income (loss).....	\$ 6,906	\$ 12,599	\$ (8,062)	\$ (3,870)	\$ (3,405)
	=====	=====	=====	=====	=====

PER SHARE DATA					
Income (loss) before extraordinary gain.....	\$ 1.78	\$ 3.22	\$ (2.02)	\$ (1.29)	\$ (1.15)
Extraordinary gain.....	--	--	--	.32	.30
	-----	-----	-----	-----	-----
Net income (loss).....	\$ 1.78	\$ 3.22	\$ (2.02)	\$ (.97)	\$ (.85)
	=====	=====	=====	=====	=====
Dividends per share.....	\$ .60	\$ .28(/1/)	\$ .28	\$ .07	\$ --
Weighted average Common shares outstanding.....	3,876,797	3,907,221	3,994,687	4,012,275	4,012,275

</TABLE>

-----  
(/1/) Does not include the special dividend of \$1.00 per share

<TABLE>  
<CAPTION>

	December 31,				
	1998	1997	1996	1995	1994
	-----	-----	-----	-----	-----
	(dollars in thousands, except per share)				
<S>	<C>	<C>	<C>	<C>	<C>

BALANCE SHEET DATA

Notes and interest receivable, net.....	\$ 1,493	\$ 3,947	\$ 8,606	\$ 10,017	\$ 11,201
Real estate held for sale, net					
Foreclosed.....	1,356	1,356	910	2,460	8,032
Other.....	--	3,630	2,089	3,415	341
Real estate held for investment, net.....	347,389	269,845	217,010	220,105	213,445
Total assets.....	382,203	319,135	244,971	260,036	247,964
Notes and interest payable.....	282,688	222,029	158,692	159,889	145,514
Stockholders' equity.....	91,132	86,133	78,959	89,084	93,177
Book value per share.....	\$ 23.35	\$ 22.15	\$ 20.11	\$ 22.19	\$ 23.22

</TABLE>

The Company purchased 22 properties in 1998 for a total of \$91.0 million, 15 properties in 1997 for a total of \$60.0 million and six properties in 1996 for a total of \$7.7 million. The Company sold five properties in 1998 for a total of \$31.8 million, five properties in 1997 for a total of \$29.1 million and five properties in 1996 for a total \$8.9 million. See ITEM 2. "PROPERTIES--Real Estate" and ITEM 8. "FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA."

Shares and per share data have been restated for the three for two forward Common Stock split effected February 15, 1996.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Introduction

Transcontinental Realty Investors, Inc. (the "Company") invests in real estate through acquisitions, leases and partnerships and in mortgage loans on real estate, including first, wraparound and junior mortgage loans. The Company is the successor to a California business trust organized on September 6, 1983 which commenced operations on January 31, 1984.

LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents at December 31, 1998 totaled \$10.5 million compared with \$24.7 million at December 31, 1997. The principal reasons for the decrease in cash are discussed in the paragraphs below.

The Company's principal sources of cash have been and will continue to be from property operations, proceeds from property sales, the collection of

mortgage notes receivable, borrowings and to a lesser extent, distributions from partnerships. Management expects that the Company's cash balance at December 31, 1998, and cash that will be generated in 1999 from the collection of mortgage notes receivable, sales of properties and refinancing or extension of certain of its mortgage debt will be sufficient to meet all of its cash requirements, including debt service obligations coming due in 1999, dividend payments and property maintenance and improvements, as more fully discussed in the paragraphs below.

Net cash provided by operating activities decreased to \$3.4 million in 1998 from \$10.0 million in 1997. The primary factors contributing to the Company's cash flow from operations are discussed in the following paragraphs.

The Company's cash flow from property operations (rents collected less payments for property operating expenses) increased to \$29.8 million in 1998 from \$16.2 million in 1997. An increase of \$6.1 million was due to the purchase of 15 income producing properties in 1997 and 18 income producing properties in 1998, an increase of \$6.2 million was due to the sale of Republic Towers Office Building in 1997, and an increase of \$2.2 million was due to increased occupancy and rents at the Company's apartments and commercial properties, and the Company's control of operating expenses. These increases were partially offset by a decrease of \$1.2 million due to the sale of five other income producing properties in 1997 and 1998. Management believes that this trend of increased cash flow from property operations will continue as a result of increased rental rates at both the Company's apartments and commercial properties and increased occupancy at its commercial properties.

Interest collected decreased to \$807,000 in 1998 from \$1.1 million in 1997. This decrease was due to seven mortgage notes receivable being collected in 1997 and 1998 and the foreclosure of the collateral property securing another note in 1998.

Interest paid increased to \$21.2 million in 1998 from \$16.0 million in 1997. An increase of \$5.7 million was due to 33 properties being purchased on a leveraged basis in 1997 and 1998 and refinancings and financings of unencumbered properties during 1997 and 1998. This increase was partially offset by a decrease of \$231,000 due to properties sold in 1998. Interest paid will continue to increase as the Company purchases additional properties on a leveraged basis.

Advisory and net income fee paid to affiliate increased to \$4.1 million in 1998 from \$1.8 million in 1997. This increase was due to the 1997 accrued net income fee not being paid until 1998 and an additional \$574,000 was due to an increase in the advisory fee paid as a result of an increase in the Company's gross assets, the basis for such fee.

General and administrative expenses paid increased to \$2.7 million in 1998 from \$2.5 million in 1997. This increase was due to legal fees related to the Olive and other litigation accrued in 1997 but not paid until 1998 and an increase in advisory cost reimbursements.

In 1997, the Company received an insurance settlement of \$9.6 million relating to 1995 hail storm and flood damage to the Republic Towers Office Building in Dallas, Texas.

The Company received distributions from equity investees operating cash flow of \$482,000 in 1998 and \$687,000 in 1997. See NOTE 5. "INVESTMENT IN EQUITY METHOD REAL ESTATE ENTITIES."

In 1998, the Company received cash of \$2.9 million from the collection of four mortgage notes receivable and an additional \$671,000 from the collection of a mortgage note written off as uncollectible in a previous year. The Company received net cash of a total of \$81.1 million from new mortgage borrowings and refinancings and

an additional \$31.8 million, after debt payoffs, from property sales during 1998. In 1998, the Company expended \$77.4 million in cash on property purchases and made a total of \$34.6 million in principal payments on its mortgage debt.

Scheduled principal payments on notes payable of \$25.6 million are due in 1999. For those mortgages that mature in 1999, it is the Company's intention to either seek to extend the due dates one or more years, or refinance the debt on a long-term basis, or pay them when due. Management believes it will continue to be successful in obtaining loan extensions or refinancings.

As discussed in NOTE 3. "REAL ESTATE AND DEPRECIATION," during 1998, the Company funded \$1.9 million for purchase of the land for the construction cost of the 260 unit Limestone Canyon Apartments in Austin, Texas. Construction commenced in August 1998 and is expected to be completed in the fourth quarter

of 1999. The Company has obtained a financing commitment of \$13.0 million for construction of the apartment.

During 1999, the Company has continued to be an active buyer, purchasing the 264 unit Vista Hills Apartments and a parcel of undeveloped land for a total of \$8.8 million. The Company paid \$2.8 million in cash, with the remainder of the purchase prices financed through mortgage debt. The Company derived the cash portions of these purchases from its cash on hand at December 31, 1998. See NOTE 18. "SUBSEQUENT EVENTS."

In March 1999, the Company sold the 368 unit Mariner's Point Apartments in St. Petersburg, Florida for \$6.7 million, receiving net cash of \$2.6 million. See NOTE 18. "SUBSEQUENT EVENTS."

Pursuant to a repurchase program originally announced on December 5, 1989, Board of Directors has authorized the repurchase of a total of 687,000 shares of the Company's Common Stock. As of March 5, 1999, a total of 409,765 shares had been repurchased at a total cost to the Company of \$3.3 million, 21,950 shares having been repurchased in 1998 at a total cost to the Company of \$336,000.

During 1998, the Company declared and paid dividends of \$2.3 million or \$.60 per share.

Management reviews the carrying values of the Company's properties and mortgage notes receivable at least annually and whenever events or a change in circumstances indicate that impairment may exist. Impairment is considered to exist if, in the case of a property, the future cash flow from the property (undiscounted and without interest) is less than the carrying amount of the property. For notes receivable impairment is considered to exist if it is probable that all amounts due under the terms of the note will not be collected. If impairment is found to exist, a provision for loss is recorded by a charge against earnings. The mortgage note receivable review includes an evaluation of the collateral property securing such note. The property review generally includes: (1) selective property inspections; (2) a review of the property's current rents compared to market rents; (3) a review of the property's expenses; (4) a review of maintenance requirements; (5) a review of the property's cash flow; (6) discussions with the manager of the property; and (7) a review of properties in the surrounding area.

#### Results of Operations

1998 Compared to 1997. The Company's net income for 1998 was \$6.9 million compared to \$12.6 million in 1997. The Company's 1998 net income included gains on the sale of real estate of \$12.6 million. The Company's 1997 net income included gains on sale of real estate of \$21.4 million. Fluctuations in the components of the Company's revenues and expenses between 1998 and 1997 are discussed below.

Rents increased \$15.3 million in 1998 to \$69.8 million compared to \$54.5 million in 1997. An increase of \$16.1 million was due to properties purchased or obtained through foreclosure in 1997 and 1998; and \$2.2 million was due to increased occupancy and rental rates at the Company's apartments and commercial properties primarily: Spa Cove Apartments, Arbor Pointe Apartments, Woods Edge Apartments, Plaza Towers Office

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Building, 74 New Montgomery Office Building, Waterstreet Office Building, Parke Long Warehouse and Hartford Office Building. These increases were partially offset by a decrease of \$3.0 million due to properties sold in 1997 and 1998.

Property operating expenses increased \$5.9 million in 1998 to \$38.3 million as compared to \$32.4 million in 1997. Of the increase, \$10.0 million was due to properties purchased in 1997 and 1998. This increase was partially offset by a decrease of \$4.0 million due to properties sold in 1997 and 1998.

Rents and property operations expenses both are expected to increase in 1999 due to anticipated increases in rents at the Company's apartments, increased occupancy of its commercial properties and as a result of a full year of operations of the properties acquired during 1998 and in the first quarter of 1999.

Interest income decreased to \$807,000 in 1998 from \$1.5 million in 1997. The decrease in interest income was due to seven mortgage notes receivable being collected in 1997 and 1998 and the foreclosure of the collateral property securing another note in 1998. Interest income in 1999 is expected to approximate 1998.

Interest expense increased to \$22.8 million in 1998 from \$16.8 million in 1997. Of this increase, \$5.8 million was attributable to properties purchased in 1998 and 1997 and \$984,000 was attributable to property financings and

refinancings during 1998 and 1997. These increases were partially offset by a decrease of \$759,000 due to properties sold and mortgages paid off in 1998 and 1997. Interest expense is expected to increase in 1999 due to anticipated property refinancings and the properties purchased in the first quarter of 1999 on a leveraged basis.

Depreciation increased to \$10.7 million in 1998 from \$9.6 million in 1997. An increase of \$2.0 million was attributable to property purchases in 1998 and 1997 and an increase of \$522,000 was due to increased depreciation from property additions and tenant improvements. These increases were partially offset by decreases of \$1.4 million due to properties sold in 1998 and 1997 and \$21,000 due to assets becoming fully depreciated. Depreciation expense is expected to increase in 1999 due to a full year of depreciation of properties acquired in 1998 and the income producing property purchased in the first quarter of 1999.

Advisory and net income fees decreased to \$2.5 million in 1998 from \$2.8 million in 1997. The decrease was due to a decrease in the net income fee in 1998 due to a decrease in net income partially offset by an increase in the advisory fee due to an increase in gross assets, the basis for the fee. The advisory fee is expected to increase as the Company's asset base increases. See NOTE 10. "ADVISORY AGREEMENT."

General and administrative expenses decreased to \$2.3 million in 1998 from \$2.6 million in 1997. The decrease was primarily due to a decrease in legal fees related to the Olive and other litigation (see NOTE 15. "COMMITMENTS AND CONTINGENCIES").

In the fourth quarter of 1997, the Company recognized a provision for loss of \$1.3 million to reduce the carrying value of a shopping center to its agreed sales price less estimated costs of sale. Sale of the property occurred in March 1998.

Equity in income of investees decreased to \$288,000 in 1998 from \$812,000 in 1997. Included in equity earnings in 1998 were gains on the sale of real estate of \$316,000, the Company's equity share of the gain recognized by an equity partnership on the sale of its two apartments. Included in equity earnings in 1997 were gains on the sale of real estate of \$890,000, the Company's equity share of the gain recognized by Income Opportunity Realty Investors, Inc. ("IORI") on the sale of three of its apartments. The Company expects its share of equity investees' income or losses to be minimal in 1999. See NOTE 5. "INVESTMENT IN EQUITY METHOD REAL ESTATE ENTITIES."

In 1998, the Company recognized gains totaling \$12.6 million; a \$2.1 million previously deferred gain upon collection of a mortgage note receivable related to a property sale that had been recorded under the cost recovery method, \$671,000 from the collection of a mortgage note receivable which had been written off in a prior year,

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\$3.4 million from the sale of a shopping center in Dallas, Texas, \$219,000 from the sale of an industrial warehouse in Dallas, Texas, \$5.9 million from the sale of an office building in San Diego, California and \$350,000 from the sale of 19 acres of foreclosed land in Greensboro, North Carolina. In 1997, the Company recognized gains totaling \$21.4 million; \$1.4 million from the sale of a .9976 acre parcel of land in Dallas, Texas and \$19.4 million from the sale of an office building in Dallas, Texas, \$55,000 from the sale of a foreclosed single family residence in Scottsdale, Arizona and \$554,000 from the sale of a shopping center in San Antonio, Texas. See NOTE 3. "REAL ESTATE AND DEPRECIATION."

1997 Compared to 1996. The Company's net income for 1997 was \$12.6 million compared to a net loss of \$8.1 million in 1996. The Company's 1997 net income included gains on sale of real estate of \$21.4 million. The Company's 1996 net loss included gains on sale of real estate of \$1.6 million. Fluctuations in the components of the Company's revenues and expenses between the 1997 and 1996 are described below.

Rents increased to \$54.5 million in 1997 from \$45.4 million in 1996. An increase of \$6.9 million in rents was due to property purchases in 1996 and 1997; and \$3.1 million was due to increased occupancy and rental rates at the Company's residential and commercial properties primarily: Plaza Tower Office Building, a 1% increase; Waterstreet Office Building, a 2% increase; Institute Place Office Building, a 10% increase; 74 New Montgomery Office Building, a 2% increase; Corporate Center at Beaumeade Office Building, a 2% increase; and Majestic Inn, a 3% increase. These increases were partially offset by a decrease of \$865,000 due to properties sold in 1997.

Property operating expenses increased to \$32.4 million in 1997 from \$28.5 million in 1996. Of this increase, \$4.3 million was due to properties purchased in 1996 and 1997. This increase was partially offset by a decrease of \$504,000 due to properties sold in 1997.

Interest income of \$1.5 million in 1997 approximated that of 1996.

Interest expense increased to \$16.8 million in 1997 from \$15.0 million in 1996. Of this increase \$1.6 million was attributable to properties purchased in 1997 and \$316,000 was attributable to property financings and refinancings during 1997. These increases were partially offset by decreases of \$73,000 due to properties sold and mortgages paid off and \$71,000 due to a decrease in interest rates on variable interest rate debt.

Depreciation increased to \$9.6 million in 1997 from \$8.5 million in 1996. An increase of \$752,000 was attributable to property purchases and an increase of \$515,000 was due to increased depreciation from property additions and tenant improvements. These increases were partially offset by decreases of \$63,000 due to properties sold and \$88,000 due to assets becoming fully depreciated.

Advisory fee expense of \$1.8 million in 1997 approximated that of 1996.

General and administrative expenses decreased to \$2.6 million in 1997 from \$2.7 million in 1996. The decrease was due to a decrease in legal fees related to the Olive and other litigation (see NOTE 15. "COMMITMENTS AND CONTINGENCIES") partially offset by an increase in advisory cost reimbursements and other professional fees.

As described in "Liquidity and Capital Resources" above, in 1997 the Company received an insurance settlement of \$9.6 million. In 1996, the Company received a litigation settlement of \$1.5 million.

In the fourth quarter of 1997, the Company recognized a provision for loss of \$1.3 million to reduce the carrying value of a shopping center to its agreed sales price less estimated costs of sale. Sale of the property was completed in March 1998. In the second quarter of 1996, the Company recognized a provision for loss of \$1.6 million to reduce the carrying value of an office building to its agreed sales price less estimated costs of sale. Sale of the property was completed in July 1996.

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Equity in income of investees was \$812,000 in 1997 compared to a loss of \$20,000 in 1996. Included in equity earnings in 1997 are gains on the sale of real estate of \$890,000, the Company's equity share of the gain recognized by IORI on the sale of three of its apartments.

In 1997, the Company recognized gains totaling \$21.4 million, \$1.4 million from the sale of a .9976 acre parcel of land and \$19.4 million from the sale of an office building, both in Dallas, Texas, \$55,000 from the sale of a foreclosed single family residence in Scottsdale, Arizona and \$554,000 from the sale of a shopping center in San Antonio, Texas. See NOTE 3. "REAL ESTATE AND DEPRECIATION."

In 1996, the Company recognized gains totaling \$1.6 million; \$218,000 from the sale of Cheyenne Mountain land, \$1.4 million from the sale of Park Forest Apartments and \$56,000 from the sale of Moss Creek land. In September 1996, the Company recognized a loss of \$63,000 from the sale of Byron land. See NOTE 3. "REAL ESTATE AND DEPRECIATION."

#### ENVIRONMENTAL MATTERS

Under various federal, state and local environmental laws, ordinances and regulations, the Company may be potentially liable for removal or remediation costs, as well as certain other potential costs, relating to hazardous or toxic substances (including governmental fines and injuries to persons and property) where property-level managers have arranged for the removal, disposal or treatment of hazardous or toxic substances. In addition, certain environmental laws impose liability for release of asbestos-containing materials into the air, and third parties may seek recovery for personal injury associated with such materials.

Management is not aware of any environmental liability relating to the above matters that would have a material adverse effect on the Company's business, assets or results of operations.

#### INFLATION

The effects of inflation on the Company's operations are not quantifiable. Revenues from property operations tend to fluctuate proportionately with inflationary increases and decreases in housing costs. Fluctuations in the rate of inflation also affect sales values of properties and the ultimate gain to be realized from property sales. To the extent that inflation affects interest rates, the Company's earnings from short-term investments, the cost of new financings as well as the cost of variable interest rate debt will be affected.

TAX MATTERS

For the years 1998, 1997 and 1996, the Company elected and in the opinion of management, qualified to be taxed as a Real Estate Investment Trust ("REIT") as defined under Sections 856 through 860 of the Internal Revenue Code of 1986, as amended (the "Code"). To continue to qualify for federal taxation as a REIT under the Code, the Company is required to hold at least 75% of the value of its total assets in real estate assets, government securities, cash and cash equivalents at the close of each quarter of each taxable year. The Code also requires a REIT to distribute at least 95% of its REIT taxable income, plus 95% of its net income from foreclosure property, all as defined in Section 857 of the Code, on an annual basis to stockholders.

YEAR 2000

Basic Capital Management, Inc. ("BCM"), the Company's advisor, has informed management that its computer hardware operating system and computer software have been certified as year 2000 compliant.

Further, Carmel Realty Services, Ltd. ("Carmel Ltd."), an affiliate of BCM that performs property management services for the Company's properties, has informed management that effective January 1, 1999, it began using year 2000 compliant computer hardware and property management software for the Company's commercial properties. With regard to the Company's apartments, Carmel, Ltd. has informed management that

its subcontractors either have in place or will have in place in the first quarter of 1999, year 2000 compliant computer hardware and property management software.

The Company has not incurred, nor does it expect to incur, any costs related to its computer hardware and accounting and property management software being modified, upgraded or replaced in order to make them year 2000 compliant. Such costs have been or will be borne by either BCM, Carmel, Ltd. or the property management subcontractors of Carmel, Ltd.

Management has completed its evaluation of the Company's computer controlled building systems, such as security, elevators, heating and cooling, etc., to determine what systems are not year 2000 compliant. Management believes that necessary modifications to such systems are insignificant and do not require significant expenditures, as such enhanced operating systems are readily available.

The Company has or will have in place the year 2000 compliant systems that will allow it to operate. The risks the Company faces are that certain of its vendors will not be able to supply goods or services and that financial institutions and taxing authorities will not be able to accurately apply payments made to them. The Company believes that other vendors are readily available and that financial institutions and taxing authorities will, if necessary, apply monies received manually. The likelihood of the above having a significant impact on the Company's operations is negligible.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

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</TABLE>

All other schedules are omitted because they are not required, are not applicable or the information required is included in the Consolidated Financial Statements or the notes thereto.

## REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Directors of  
Transcontinental Realty Investors, Inc.

We have audited the accompanying consolidated balance sheets of Transcontinental Realty Investors, Inc. and Subsidiaries as of December 31, 1998 and 1997 and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 1998. We have also audited the schedules listed in the accompanying index. These financial statements and schedules are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedules based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and schedules are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and schedules. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements and schedules. We believe our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Transcontinental Realty Investors, Inc. and Subsidiaries as of December 31, 1998 and 1997, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 1998, in conformity with generally accepted accounting principles.

Also, in our opinion, the schedules referred to above present fairly, in all material respects, the information set forth therein.

BDO Seidman, LLP

Dallas, Texas  
March 24, 1999

## TRANSCONTINENTAL REALTY INVESTORS, INC.

## CONSOLIDATED BALANCE SHEETS

<TABLE>  
<CAPTION>

	December 31,	
	1998	1997
	(dollars in thousands, except per share)	
<S>	<C>	<C>
Assets		
Notes and interest receivable		
Performing.....	\$ 1,429	\$ 4,388
Nonperforming, nonaccruing.....	950	450
	-----	-----
	2,379	4,838
Less--allowance for estimated losses.....	(886)	(891)
	-----	-----
	1,493	3,947
Foreclosed real estate held for sale.....	1,356	1,356
Real estate held for sale, net of accumulated depreciation (\$1,350 in 1997).....	--	3,630
	-----	-----
	1,356	4,986
Real estate held for investment, net of accumulated depreciation (\$61,241 in 1998 and \$55,487 in 1997)..	347,389	269,845
Investment in real estate entities.....	3,458	4,333
Cash and cash equivalents.....	10,505	24,733
Other assets (including \$1,325 in 1998 and \$497 in 1997 from affiliates).....	18,002	11,291
	-----	-----
	\$ 382,203	\$ 319,135
	=====	=====

Liabilities and Stockholders' Equity  
Liabilities



Notes and interest payable.....	\$ 282,688	\$ 222,029
Other liabilities (including \$62 in 1998 and \$1,157 in 1997 to affiliates).....	8,383	10,973
	-----	-----
	291,071	233,002
Commitments and contingencies		
Stockholders' equity		
Preferred Stock		
Series A; \$.01 par value; authorized, 6,000 shares; issued and outstanding 5,829 shares in 1998 (liquidation preference \$583).....	--	--
Common Stock, \$.01 par value; authorized, 10,000,000 shares; issued and outstanding 3,878,463 shares in 1998 and 3,889,200 shares in 1997.....	39	39
Paid-in capital.....	218,087	217,688
Accumulated distributions in excess of accumulated earnings.....	(126,994)	(131,594)
	-----	-----
	91,132	86,133
	-----	-----
	\$ 382,203	\$ 319,135
	=====	=====

</TABLE>

The accompanying notes are an integral part of these Consolidated Financial Statements.

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TRANSCONTINENTAL REALTY INVESTORS, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

<TABLE>  
<CAPTION>

	For the Years Ended December 31,		
	1998	1997	1996
	-----	-----	-----
	(dollars in thousands, except per share)		
<S>	<C>	<C>	<C>
Revenues			
Rents.....	\$ 69,829	\$ 54,462	\$ 45,405
Interest.....	807	1,499	1,473
	-----	-----	-----
	70,636	55,961	46,878
Expenses			
Property operations (including \$2,753 in 1998, \$2,262 in 1997 and \$1,879 in 1996 to affiliates).....	38,282	32,424	28,491
Interest.....	22,797	16,765	14,999
Depreciation.....	10,691	9,578	8,461
Advisory fee to affiliate.....	1,962	1,807	1,784
Net income fee to affiliate.....	558	1,022	--
General and administrative (including \$1,121 in 1998, \$1,187 in 1997 and \$1,047 in 1996 to affiliates).....	2,312	2,645	2,685
Litigation settlement.....	--	--	(1,500)
Provision for losses.....	--	1,337	1,579
	-----	-----	-----
	76,602	65,578	56,499
(Loss) from operations.....	(5,966)	(9,617)	(9,621)
Equity in income (loss) of investees.....	288	812	(20)
Gain on sale of real estate.....	12,584	21,404	1,579
	-----	-----	-----
Net income (loss).....	6,906	12,599	(8,062)
Preferred dividend required.....	(1)	--	--
Net income (loss) applicable to common shares.....	\$ 6,905	\$ 12,599	\$ (8,062)
	=====	=====	=====
Earnings per share			
Net income (loss) applicable to common shares.....	\$ 1.78	\$ 3.22	\$ (2.02)
	=====	=====	=====
Weighted average common shares used in computing earnings per share.....	3,876,797	3,907,221	3,994,687
	=====	=====	=====

</TABLE>

The accompanying notes are an integral part of these Consolidated Financial Statements.

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TRANSCONTINENTAL REALTY INVESTORS, INC.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

<TABLE>  
<CAPTION>

	Series A Preferred Stock	Common Stock Shares	Common Stock Amount	Paid-in Capital	Accumulated Distributions in Excess of Accumulated Earnings	Stockholders' Equity
	(dollars in thousands, except per share)					
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Balance, January 1, 1996.....	\$ --	4,012,275	\$ 40	\$219,036	\$ (130,036)	\$89,040
Repurchase of Common Stock.....	--	(85,830)	(1)	(903)	--	(904)
Dividends (\$.28 per share).....	--	--	--	--	(1,115)	(1,115)
Net (loss).....	--	--	--	--	(8,062)	(8,062)
Balance, December 31, 1996.....	--	3,926,445	39	218,133	(139,213)	78,959
Fractional shares.....	--	(18)	--	--	--	--
Repurchase of Common Stock.....	--	(37,227)	--	(445)	--	(445)
Dividends (\$.28 per share).....	--	--	--	--	(1,090)	(1,090)
Special dividend (\$1.00 per share) declared....	--	--	--	--	(3,890)	(3,890)
Net income.....	--	--	--	--	12,599	12,599
Balance, December 31, 1997.....	--	3,889,200	39	217,688	(131,594)	86,133
Issuance of Series A Preferred Stock 5,829 shares.....	--	--	--	583	--	583
Repurchase of Common Stock.....	--	(21,950)	--	(336)	--	(336)
Sale of Common Stock under dividend reinvestment plan.....	--	11,213	--	152	--	152
Dividends (\$.60 per share).....	--	--	--	--	(2,306)	(2,306)
Net income.....	--	--	--	--	6,906	6,906
Balance, December 31, 1998.....	\$ --	3,878,463	\$ 39	\$218,087	\$ (126,994)	\$91,132

</TABLE>

The accompanying notes are an integral part of these Consolidated Financial Statements.

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TRANSCONTINENTAL REALTY INVESTORS, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

<TABLE>  
<CAPTION>

	FOR The Years Ended December 31,		
	1998	1997	1996
	(dollars in thousands)		
<S>	<C>	<C>	<C>
Cash Flows from Operating Activities			
Rents collected.....	\$ 69,307	\$ 57,144	\$ 43,401
Interest collected.....	807	1,098	1,232

Interest paid.....	(21,179)	(16,016)	(14,167)
Payments for property operations (including \$2,753 in 1998, \$2,262 in 1997 and \$1,879 in 1996 to affiliates).....	(39,474)	(40,984)	(30,738)
Advisory and net income fee paid to affiliate.....	(4,125)	(1,807)	(1,784)
General and administrative expenses paid (including \$1,121 in 1998, \$1,187 in 1997 and \$1,047 in 1996 to affiliates).....	(2,705)	(2,457)	(2,785)
Distributions from operating cash flow of equity investees.....	482	687	649
Insurance/litigation settlement.....	--	9,633	1,500
Other.....	306	2,684	(612)
	-----	-----	-----
Net cash provided by (used in) operating activities.....	3,419	9,982	(3,304)
Cash Flows from Investing Activities			
Collections on notes receivable.....	2,892	5,048	952
Acquisition of notes receivable.....	(149)	--	--
Real estate improvements.....	(9,595)	(5,767)	(3,406)
Proceeds from sale of real estate.....	31,807	29,081	8,922
Deposits on pending purchase.....	(3,796)	(1,115)	--
Deferred merger costs.....	(519)	--	--
Acquisitions of real estate (including \$3,468 in 1998, \$2,966 in 1997 and \$339 in 1996 to affiliates).....	(77,395)	(46,433)	(7,689)
Distributions from investing cash flow of equity investees.....	701	1,101	--
Contributions to equity investees.....	(21)	(731)	(161)
	-----	-----	-----
Net cash (used in) investing activities..	(56,075)	(18,816)	(1,382)
Cash Flows from Financing Activities			
Payments on notes payable.....	\$ (34,555)	\$ (37,095)	\$ (14,545)
Proceeds from notes payable.....	81,058	73,817	13,550
Reimbursements to advisor.....	(61)	(450)	(142)
Dividends paid.....	(6,196)	(1,090)	(1,115)
Shares of Common Stock repurchased.....	(336)	(445)	(904)
Deferred financing costs.....	(1,634)	(2,130)	(818)
Sale of Common stock under dividend reinvestment plan.....	152	--	--
	-----	-----	-----
Net cash provided by (used in) financing activities.....	38,428	32,607	(3,974)
	-----	-----	-----
Net increase (decrease) in cash and cash equivalents.....	(14,228)	23,773	(8,660)
Cash and cash equivalents, beginning of year.....	24,733	960	9,620
	-----	-----	-----
Cash and cash equivalents, end of year....	\$ 10,505	\$ 24,733	\$ 960
	=====	=====	=====

</TABLE>

The accompanying notes are an integral part of these Consolidated Financial Statements.

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TRANSCONTINENTAL REALTY INVESTORS, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS--(Continued)

<TABLE>

<CAPTION>

	For the Years Ended December 31,		
	1998	1997	1996
	(dollars in thousands)		
<S>	<C>	<C>	<C>
Reconciliation of net income (loss) to net cash provided by (used in) operating activities			
Net income (loss).....	\$ 6,906	\$ 12,599	\$ (8,062)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities			
Depreciation and amortization.....	11,488	10,005	8,857
Provision for losses.....	--	1,337	1,579
Equity in (income) loss of equity			

investees.....	(288)	(812)	20
Gain on sale of real estate.....	(12,584)	(21,404)	(1,579)
Distributions from operating cash flow of equity investees.....	482	687	649
(Increase) in interest receivable.....	--	(244)	(5)
(Increase) decrease in other assets.....	(2,036)	5,305	1,901
Increase in interest payable.....	821	165	200
Increase (decrease) in other liabilities...	(1,370)	2,344	(6,864)
	-----	-----	-----
Net cash provided by (used in) operating activities.....	\$ 3,419	\$ 9,982	\$ (3,304)
	=====	=====	=====

Schedule of noncash investing and financing activities

Carrying value of real estate acquired through foreclosure in satisfaction of notes receivable (with carrying value of \$2,514 in 1998 and \$696 in 1996).....	\$ 2,514	\$ --	\$ 691
Notes payable from purchase of real estate.....	13,607	13,606	--
Series A Preferred Stock issued in conjunction with purchase of real estate..	583	--	--

</TABLE>

The accompanying notes are an integral part of these Consolidated Financial Statements.

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TRANSCONTINENTAL REALTY INVESTORS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The accompanying Consolidated Financial Statements of Transcontinental Realty Investors, Inc. and consolidated entities (the "Company") have been prepared in conformity with generally accepted accounting principles, the most significant of which are described in NOTE 1. "SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES." These, along with the remainder of the Notes to Consolidated Financial Statements, are an integral part of the Consolidated Financial Statements. The data presented in the Notes to Consolidated Financial Statements are as of December 31 of each year and for the year then ended, unless otherwise indicated. Dollar amounts in tables are in thousands, except per share amounts.

Certain balances for 1997 have been reclassified to conform to the 1998 presentation.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization and company business. Transcontinental Realty Investors, Inc. ("TCI"), a Nevada corporation, is successor to a California business trust which was organized on September 6, 1983 and commenced operations on January 31, 1984. The Company invests in real estate through direct equity ownership and investments in real estate entities. It also invests in mortgage loans on real estate, including first, wraparound and junior mortgage loans.

Proposed Merger with Continental Mortgage and Equity Trust

On September 25, 1998, the Company and Continental Mortgage and Equity Trust ("CMET") jointly announced the agreement of their respective Boards for the Company to acquire CMET. Under the proposal, the Company would acquire all of CMET's outstanding shares of beneficial interest, in a tax free exchange, for shares of its Common Stock. The Company will issue 1.181 shares of its Common Stock for each outstanding share of beneficial interest of CMET. Upon the exchange of shares CMET would merge into the Company. The share exchange and merger are subject to a vote of shareholders of both entities. Approval requires the vote of a majority of the shareholders holding a majority of CMET's outstanding shares of beneficial interest. As of March 5, 1999, the Company's advisor and its affiliates held shares representing approximately 57.4% of the outstanding shares of CMET and approximately 44.7% of the outstanding shares of the Company. A date for the special meeting of the shareholders to vote on the merger proposal has not been set. The Company has the same Board and advisor as CMET.

Basis of consolidation. The Consolidated Financial Statements include the accounts of TCI and controlled subsidiaries and partnerships. All significant intercompany transactions and balances have been eliminated.

Accounting estimates. In the preparation of the Consolidated Financial Statements in conformity with generally accepted accounting principles it was necessary for management to make estimates and assumptions that affect the

reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the Consolidated Financial Statements and the reported amounts of revenues and expense for the year then ended. Actual results could differ from these estimates.

Interest recognition on notes receivable. It is the Company's policy to cease recognizing interest income on notes receivable that have been delinquent for 60 days or more. In addition, accrued but unpaid interest income is only recognized to the extent that the net realizable value of the underlying collateral exceeds the carrying value of the receivable.

Allowance for estimated losses. Valuation allowances are provided for estimated losses on notes receivable considered to be impaired. Impairment is considered to exist when it is probable that all amounts due under the terms of the note will not be collected. Valuation allowances are provided for estimated losses on notes

TRANSCONTINENTAL REALTY INVESTORS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

receivable to the extent that the Company's investment in the note exceeds the Company's estimate of fair value of the collateral securing such note.

Real estate held for investment and depreciation. Real estate held for investment is carried at cost. Statement of Financial Accounting Standards No. 121 ("SFAS No. 121") requires that a property be considered impaired, if the sum of the expected future cash flows (undiscounted and without interest charges) is less than the carrying amount of the property. If impairment exists, an impairment loss is recognized, by a charge against earnings, equal to the amount by which the carrying amount of the property exceeds the fair value of the property. If impairment of a property is recognized, the carrying amount of the property is reduced by the amount of the impairment, and a new cost for the property is established. Such new cost is depreciated over the property's remaining useful life. Depreciation is provided by the straight-line method over estimated useful lives, which range from 1 to 40 years.

Real estate held for sale. Foreclosed real estate is initially recorded at new cost, defined as the lower of original cost or fair value minus estimated costs of sale. SFAS No. 121 also requires that properties held for sale be reported at the lower of carrying amount or fair value less costs of sale. If a reduction in a held for sale property's carrying amount to fair value less costs of sale is required, a provision for loss is recognized by a charge against earnings. Subsequent revisions, either upward or downward, to a held for sale property's estimated fair value less costs of sale is recorded as an adjustment to the property's carrying amount, but not in excess of the property's carrying amount when originally classified as held for sale. A corresponding charge against or credit to earnings is recognized. Properties held for sale are not depreciated.

Present value discounts. The Company provides for present value discounts on notes receivable or payable that have interest rates that differ substantially from prevailing market rates and amortizes such discounts by the interest method over the lives of the related notes. The factors considered in determining a market rate for notes receivable include the borrower's credit standing, nature of the collateral and payment terms of the note.

Revenue recognition on the sale of real estate. Sales of real estate are recognized when and to the extent permitted by Statement of Financial Accounting Standards No. 66, "Accounting for Sales of Real Estate" ("SFAS No. 66"). Until the requirements of SFAS No. 66 for full profit recognition have been met, transactions are accounted for using either the deposit, the installment, the cost recovery or the financing method, whichever is appropriate.

Investment in noncontrolled partnerships and equity investees. The Company uses the equity method to account for investments in partnerships which it does not control and for its investment in the shares of common stock of Income Opportunity Realty Investors, Inc., ("IORI"). Under the equity method, the Company's initial investment, recorded at cost, is increased by the Company's proportionate share of the investee's operating income and additional advances and decreased by its proportionate share of the investee's operating losses and distributions received.

Operating segments. Management has determined that the Company's reportable operating segments are those that are based on the Company's method of internal reporting, which disaggregates its operations by type of real estate.

Fair value of financial instruments. The Company used the following assumptions in estimating the fair value of its notes receivable, marketable equity securities and notes payable. For performing notes receivable, the fair

value was estimated by discounting future cash flows using current interest rates for similar loans. For nonperforming notes receivable, the estimated fair value of the Company's interest in the collateral property was

TRANSCONTINENTAL REALTY INVESTORS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

used. For marketable equity securities, fair value was based on the year end closing market price of the security. For notes payable, the fair value was estimated using current rates for mortgages with similar terms and maturities.

Cash equivalents. For purposes of the Consolidated Statements of Cash Flows, the Company considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents.

Earnings per share. Income (loss) per share is presented in accordance with Statement of Financial Accounting Standards No. 128, "Earnings Per Share." Income (loss) per share is computed based upon the weighted average number of shares of Common Stock outstanding during each year.

NOTE 2. NOTES AND INTEREST RECEIVABLE

Notes and interest receivable consisted of the following:

<TABLE>

<CAPTION>

	1998		1997	
	Estimated Fair Value	Book Value	Estimated Fair Value	Book Value
<S>	<C>	<C>	<C>	<C>
Notes receivable				
Performing.....	\$1,407	\$1,429	\$7,264	\$4,389
Nonperforming, nonaccruing.....	719	950	1,400	449
	-----	-----	-----	-----
	\$2,126	2,379	\$8,664	4,838
	=====	=====	=====	=====
Interest receivable.....		3		3
Unamortized (discounts).....		(3)		(3)
		-----		-----
		\$2,379		\$4,838
		=====		=====

</TABLE>

The Company does not recognize interest income on nonperforming notes receivable. For the years 1998, 1997 and 1996, unrecognized interest income on nonperforming notes totaled \$175,000, \$257,000 and \$424,000, respectively.

Performing notes receivable at December 31, 1998, mature from 1999 through 2004 with interest rates ranging from 8.75% to 12.0% per annum, with a weighted average rate of 12.0%. Discounts were based on imputed interest rates at the time of origination. Notes receivable are generally nonrecourse and are generally collateralized by real estate. Scheduled principal maturities of \$930,000 are due in 1999.

In 1998, \$2.9 million was collected in settlement of four mortgage notes and \$49,000 in principal payments were received.

In February 1994, the Company provided \$6.7 million of purchase money financing in conjunction with the sale of 1,406 acres of land in sixteen residential and commercial subdivisions in Maumelle, Arkansas secured by a first mortgage on the properties sold. The borrower did not make the scheduled February 1995 principal and interest payments. In September 1995, the Company reached a settlement with the borrower that provided for, among other things, the payment by the borrower of \$2.5 million in cash and the acceptance of a new \$1.4 million note secured by 36.3 acres of commercial land. Such note matured in January 1996. In April 1998, the Company received \$2.1 million in full settlement of its note and accrued but unpaid interest. The original sale had been recorded under the cost recovery method with the gain being deferred until the note receivable was collected. Accordingly, the previously deferred gain of \$2.1 million was recognized on collection of the note.

TRANSCONTINENTAL REALTY INVESTORS, INC.

At December 31, 1997, the Company held a wraparound mortgage note with a principal balance of \$2.5 million, secured by a K-Mart in Cary, North Carolina. In February 1998, the Company was informed that the first lien mortgage in the amount of \$2.0 million was in default. To protect its interest, the Company foreclosed on the property in August 1998 and refinanced the first lien mortgage in the amount of \$2.0 million, paying \$265,000 in cash to complete the refinancing. No loss was recognized on the foreclosure as the fair value of the property exceeded the carrying value of the note receivable. See NOTE 6. "NOTES AND INTEREST PAYABLE."

In July 1998, a mortgage note receivable which had been written off in a prior year, was collected. A gain of \$671,000 was recognized.

In August 1998, a mortgage note receivable with a principal balance of \$2.0 million and a carrying value of \$207,000, secured by a second lien on a hotel in Lake Charles, Louisiana became delinquent. To protect its interest, the Company purchased the first lien mortgage for \$149,000. Foreclosure proceedings have commenced and title to the property is expected to be received in the second quarter of 1999. No loss is expected to be incurred on foreclosure, as the estimated fair value of the property exceeds the carrying value of the mortgage notes.

In 1997, the Company accepted discounted payoffs totaling \$4.9 million in settlement of two mortgage notes receivable with a combined principal balance of \$5.0 million. The Company recognized no loss on the note settlements in excess of the reserves previously established.

#### NOTE 3. REAL ESTATE AND DEPRECIATION

In January 1998, in separate transactions, the Company purchased (1) the 188 unit Mountain Plaza Apartments in El Paso, Texas, for \$4.0 million, paying \$1.0 million in cash and obtaining mortgage financing of \$3.0 million; (2) the 212 unit Hunters Glen Apartments in Midland, Texas, for \$2.5 million, paying \$600,000 in cash and obtaining seller financing of the remaining \$1.9 million of the purchase price; (3) the Laws Street land, a 1.41 acre parcel of land in Dallas, Texas, for \$1.9 million in cash; and, (4) the 204 unit Bent Tree Garden Apartments in Addison, Texas, for \$8.1 million, paying \$1.7 million in cash and obtaining mortgage financing of \$6.4 million.

In February 1998, in separate transactions, the Company purchased (1) Parkway North, a 71,041 sq. ft. office building in Dallas, Texas, for \$5.4 million, paying \$1.5 million in cash and obtaining mortgage financing of \$3.9 million; and, (2) the Lemmon Carlisle land, a 2.14 acre parcel of land in Dallas, Texas, for \$3.4 million in cash.

In February 1998, the Company obtained through foreclosure a 92,033 sq. ft. K-Mart in Cary, North Carolina. As of December 31, 1998, the property was classified as "real estate held for investment." See NOTE 2. "NOTES AND INTEREST RECEIVABLE."

In March 1998, the Company purchased the Plaza on Bachman Creek, a 80,278 sq. ft. retail/office complex in Dallas, Texas, for \$3.5 million, paying \$1.1 million in cash and obtaining mortgage financing of \$2.4 million.

Also in March 1998, the Company sold Shaws Plaza, a 103,482 sq. ft. shopping center in Sharon, Massachusetts, for \$3.8 million in cash. The Company received net cash of \$1.1 million after paying off \$2.6 million in mortgage debt and the payment of various closing costs. No gain or loss was recognized on the sale.

In April 1998 and May 1998, the Company purchased in a single transaction the 178 unit Ashton Way Apartments in Midland, Texas, and the 92 unit 4400 Apartments, also in Midland, Texas, the 232 unit Woodview Apartments in Odessa, Texas, for a total of \$6.8 million. The Company paid a total of \$1.5 million in cash and obtained mortgage financing secured by all three properties totaling \$5.3 million.

TRANSCONTINENTAL REALTY INVESTORS, INC.

In May 1998, in separate transactions, the Company purchased (1) the Eagle Crest land, a 22.99 acre parcel in Farmers Branch, Texas, for \$2.5 million in cash; and, (2) the 172 unit Fountains of Waterford Apartments in Midland, Texas, for \$1.5 million, paying \$425,000 in cash, assuming an existing mortgage of \$584,000 and obtaining seller financing of \$491,000.

Also in May 1998, the Company purchased in a single transaction, Daley

Plaza, a 62,425 sq. ft. office building and View Ridge, a 25,062 sq. ft. office building, both in San Diego, California, for a total of \$6.5 million. The Company paid \$1.7 million in cash and obtained mortgage financing totaling \$4.8 million.

In June 1998, the Company purchased the Atrium, a 74,603 sq. ft. office building in Palm Beach, Florida, for \$5.4 million, paying \$1.3 million in cash and obtaining mortgage financing of \$4.1 million.

In July 1998, the Company purchased Valley Rim, a 54,194 sq. ft. office building in San Diego, California, for \$5.1 million, paying \$1.4 million in cash and obtaining mortgage financing of \$3.7 million.

Also in July 1998, the Company purchased the Limestone Canyon land, a 27 acre parcel of unimproved land in Austin, Texas, for \$1.8 million in cash. In conjunction with the purchase, the Company obtained a financing commitment of \$13.0 million for the construction of a 260 unit apartment on the site. Construction commenced in August 1998 and is expected to be completed in the fourth quarter of 1999.

In 1997, Montgomery Ward ("Ward"), a tenant at the Northtown Mall, a 354,174 sq. ft. shopping center in Dallas, Texas, filed for bankruptcy protection. In an attempt to keep the Ward's lease from being sold, Northtown Mall was placed in administrative bankruptcy. Ward's Northtown Mall lease, as well as other Ward leases, were, however, sold for the benefit of the Ward bankruptcy estate. In September 1998, the Company bought back the lease concurrent with the \$15.6 million sale of Northtown Mall. The Company received net cash of \$12.1 million after paying off \$2.5 million in mortgage debt, \$900,000 for the Ward lease and the payment of various closing costs. A gain of \$3.4 million was recognized on the sale.

Also in September 1998, the Company sold Chesapeake Ridge, a 100,484 sq. ft. office building in San Diego, California, for \$13.2 million, receiving net cash of \$7.6 million after paying off \$5.3 million of mortgage debt and the payment of various closing costs. A gain of \$5.9 million was recognized on the sale.

In October 1998, the Company sold Denton Drive, a 123,800 sq. ft. industrial warehouse in Dallas, Texas, for \$1.2 million, receiving net cash of \$845,000 after paying off \$309,000 in mortgage debt and the payment of various closing costs. A gain of \$219,000 was recognized on the sale.

Also in October 1998, the Company purchased the 208 unit Cliffs of Eldorado Apartments in McKinney, Texas, for \$12.8 million, paying \$1.6 million in cash, assuming the existing mortgage of \$10.6 million and issuing 5,829 shares of Series A Cumulative Convertible Preferred Stock with a total liquidation value of \$583,000.

Further in October 1998, the Company sold approximately 19 acres of foreclosed land held for sale in Greensboro, North Carolina, for \$375,000 in cash, receiving net cash of \$356,000 after the payment of various closing costs. A gain of \$350,000 was recognized on the sale.

In December 1998, the Company purchased the assets of the Neighborhood Inns of Chicago, consisting of three hotels in Chicago, Illinois, the Belmont with 45 rooms, the Brompton with 52 rooms and the Surf with 55 rooms, for \$11.6 million. The Company paid \$2.3 million in cash and obtained mortgage financing secured by all three properties of \$9.2 million.

TRANSCONTINENTAL REALTY INVESTORS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

Also in December 1998, the Company purchased the 80 unit Southgreen Apartments in Bakersfield, California, for \$3.6 million, paying \$1.1 million in cash and obtaining mortgage financing of \$2.5 million.

In 1997, the Company purchased three commercial properties for a total of \$12.6 million, ten apartments with a total of 1,757 units, for a total of \$42.1 million, an industrial warehouse for \$4.7 million and a parcel of unimproved land for \$11.0 million. In connection with the purchases, the Company either assumed existing mortgage debt or obtained new mortgage debt totaling \$49.5 million with the remainder of the purchase prices paid in cash. Also in 1997, the Company sold three commercial properties for \$27.1 million, a parcel of land for \$2.7 million, and a foreclosed single family residence for \$778,000. The Company received net cash of \$27.8 million from the sales after paying off \$2.0 million in mortgage debt. In conjunction with such sales, gains totaling \$21.4 million were recognized.

NOTE 4. ALLOWANCE FOR ESTIMATED LOSSES



Activity in the allowance for estimated losses on notes and interest receivable was as follows:

	1998	1997	1996
	----	----	-----
<S>	<C>	<C>	<C>
Balance January 1,.....	\$891	\$926	\$1,049
Amounts charged off.....	(5)	(35)	(123)
	----	----	-----
Balance December 31,.....	\$886	\$891	\$ 926
	=====	=====	=====

NOTE 5. INVESTMENT IN EQUITY METHOD REAL ESTATE ENTITIES

Investments in equity method real estate entities consist of the following:

	1998	1997
	----	-----
<S>	<C>	<C>
Income Opportunity Realty Investors, Inc. ("IORI").....	\$ 466	\$ 853
Tri-City Limited Partnership ("Tri-City").....	3,624	4,146
Nakash Income Associates ("NIA").....	(717)	(770)
Other.....	85	104
	----	-----
	\$3,458	\$4,333
	=====	=====

The Company owns an approximate 22.7% interest in IORI, a publicly held Real Estate Investment Trust ("REIT"), having a market value of \$2.3 million at December 31, 1998. At December 31, 1998, IORI had total assets of \$88.7 million and owned four apartments in Texas and ten office buildings (six in California, one in Florida, two in Texas and one in Virginia).

The Company owns a non-controlling combined 63.7% general and limited partner interest in Tri-City which owns three commercial properties in Texas, consisting of two office buildings and a shopping center. In May 1998, Tri-City sold its' two apartments for \$3.3 million in cash, receiving net cash of \$1.4 million after paying off \$1.9 million in mortgage debt and the payment of various closing costs. The Company received a distribution of \$701,000 of such net cash. Tri-City recognized a gain of \$496,000 on the sale of which the Company's equity share was \$316,000. The Tri-City partnership agreement requires the consent of both the Company and IORI (a 36.3% general partner) for any material changes in the operations of Tri-City's properties, including sales, refinancings and changes in property management.

The Company owns a non-controlling 60% general partner interest and IORI owns a 40% general partner interest in NIA, which owns a wraparound mortgage note receivable. The NIA partnership agreement requires the consent of both the Company and IORI for any material changes in the operations of NIA.

TRANSCONTINENTAL REALTY INVESTORS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

Set forth below are summarized financial data for the entities accounted for using the equity method:

	1998	1997
	----	-----
<S>	<C>	<C>
Real estate, net of accumulated depreciation (\$12,117 in 1998 and \$9,967 in 1997).....	\$ 93,165	\$ 94,145
Notes receivable.....	902	2,912
Other assets.....	5,296	7,272
Notes payable.....	(65,115)	(68,155)
Other liabilities.....	(5,113)	(4,455)
	----	-----
Partners' capital.....	\$ 29,135	\$ 31,719
	=====	=====

<TABLE>  
<CAPTION>

	1998	1997	1996
	-----	-----	-----
<S>	<C>	<C>	<C>
Rents and interest income.....	\$18,062	\$19,652	\$12,319
Depreciation.....	(2,703)	(2,139)	(1,685)
Operating expenses.....	(9,202)	(9,485)	(7,927)
Interest expense.....	(6,274)	(4,579)	(3,086)
	-----	-----	-----
Net income (loss).....	\$ (117)	\$ 3,449	\$ (379)
	=====	=====	=====

</TABLE>

The Company's equity share of the above net income (loss) for 1998, 1997 and 1996 was \$343,000, \$835,000 and \$(2,000), respectively, before amortization of property acquisition costs discussed below. The Company's share of the above equity investee capital was \$8.8 million in 1998 and \$9.9 million in 1997.

The excess of the Company's investment over its respective share of the equity in the underlying net assets of equity investees relates primarily to unamortized property acquisition costs of \$77,000 in 1998, \$113,000 in 1997 and \$116,000 in 1996. These amounts are being amortized over the estimated useful lives of the properties.

NOTE 6. NOTES AND INTEREST PAYABLE

Notes and interest payable consist of the following:

<TABLE>  
<CAPTION>

	1998		1997	
	-----	-----	-----	-----
	Estimated		Estimated	
	Fair	Book	Fair	Book
	Value	Value	Value	Value
	-----	-----	-----	-----
<S>	<C>	<C>	<C>	<C>
Notes payable.....	\$275,027	\$280,592	\$219,056	\$220,437
	=====		=====	
Interest payable.....		2,096		1,592
		-----		-----
		\$282,688		\$222,029
		=====		=====

</TABLE>

Scheduled principal payments are due as follows:

<S>	<C>
1999.....	\$ 25,588
2000.....	17,363
2001.....	33,816
2002.....	29,434
2003.....	13,506
Thereafter.....	160,885
	-----
	\$280,592
	=====

</TABLE>

TRANSCONTINENTAL REALTY INVESTORS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

Mortgage notes payable at December 31, 1998 bear interest at rates ranging from 6.5% to 10.56% per annum, and mature between 1999 and 2037. The mortgages are collateralized by deeds of trust on real estate having a net carrying value of \$341.1 million.

In 1998, the Company purchased 10 apartments with a total of 1,566 units, 6 office buildings, 3 hotels and 3 parcels of land for a total of \$91.0 million. In conjunction with the purchases, the Company either assumed existing mortgage debt or obtained mortgage financing totaling \$58.9 million. The mortgages bear interest at rates ranging from 7.2% to 9.5% per annum, require monthly payments of principal and interest, currently totaling \$478,000, and mature from 2000 to 2037.

In March 1998, the Company refinanced the mortgage debt secured by the Tricon Warehouses in Atlanta, Georgia in the amount of \$10.2 million,

receiving net cash of \$5.4 million after paying off \$4.8 million in mortgage debt, funding of escrows and the payment of various closing costs. The new mortgage bears interest at a variable rate, currently 7.53% per annum, requires monthly payments of principal and interest of \$75,576 and matures in April 2008.

In May 1998, the Company obtained mortgage financing in the amount of \$2.2 million secured by its unencumbered Lemmon Carlisle land in Dallas, Texas, receiving net cash of \$2.1 million after the payment of various closing costs. The mortgage bears interest at 9.25% per annum, requires monthly payments of interest only and matures in May 2000.

Also in May 1998, the Company refinanced the mortgage debt secured by the Plaza Tower Office Building in St. Petersburg, Florida in the amount of \$7.4 million, receiving net cash of \$2.6 million after paying off \$4.8 million in mortgage debt, funding of required escrows and the payment of various closing costs. The new mortgage bears interest at 7.57% per annum, requires monthly payments of principal and interest of \$55,023 and matures in June 2008.

In July 1998, the Company refinanced the matured mortgage debt secured by the Villas at Countryside Apartments in Sterling, Virginia, in the amount of \$5.4 million, receiving net cash of \$400,000 after paying off \$5.0 million in mortgage debt, funding of required escrows and the payment of various closing costs. The new mortgage bears interest at 6.85% per annum, requires monthly payments of principal and interest of \$35,692 and matures in August 2005.

In August 1998, the Company obtained second lien financing of \$1.8 million secured by the Terrace Hills Apartments in El Paso, Texas, receiving net cash of \$1.7 million after the payment of various closing costs. The mortgage bears interest at 7.275% per annum, requires monthly payments of principal and interest of \$11,968 and matures in September 2009.

In August 1998, in conjunction with the foreclosure of the collateral securing a wraparound mortgage note receivable, the Company refinanced the first lien mortgage in the amount of \$2.0 million. The new mortgage bears interest at 7.51% per annum, requires monthly payments of principal and interest of \$15,721 and matures in September 2008. See NOTE 2. "NOTES AND INTEREST RECEIVABLE."

In October 1998, the Company refinanced the matured mortgage debt secured by the Bonita Plaza Office Building in Bonita, California in the amount of \$5.2 million, receiving net cash of \$1.2 million after paying off \$4.0 million in mortgage debt, funding of required escrows and the payment of various closing costs. The new mortgage bears interest at a variable rate, currently 7.4% per annum, requires monthly payments of principal and interest of \$37,722 and matures in November 2001.

TRANSCONTINENTAL REALTY INVESTORS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

In December 1998, the mortgage debt in the amount of \$4.0 million secured by the Lexington Center Office Building in Colorado Springs, Colorado matured. In March 1999, the Company refinanced the matured mortgage debt. See NOTE 18. "SUBSEQUENT EVENTS."

Also in December 1998, the mortgage debt in the amount of \$1.2 million secured by the Texstar Warehouse in Arlington, Texas matured. In January 1999, the lender agreed to extend the mortgage's maturity date to March 1999, all other items remain unchanged. The Company expects to have a refinancing of the property completed prior to the March extended maturity date.

In December 1998, the mortgage debt in the amount of \$380,000 secured by the Sadler Square Shopping Center in Amelia Island, Florida matured. In March 1999, the lender agreed to extend the mortgage's maturity date to April 1999, all other terms remain unchanged. The Company expects to have a refinancing of the property completed prior to the April extended maturity date.

In 1997, the Company obtained mortgage financing totaling \$5.6 million secured by two unencumbered apartments and a unencumbered commercial property. The Company received net cash of \$5.0 million after funding escrows and the payment of various closing costs. The mortgages bear interest ranging from 7.6% to 8.49% per annum and mature between July 2007 and October 2007. Also in 1997, the Company refinanced the mortgage debt secured by five commercial properties and three apartments, in the total amount of \$45.3 million. The Company received net cash of \$10.3 million after paying off \$33.2 million in mortgage debt, funding escrows and the payment of various closing costs. The mortgages bear interest at rates ranging from 7.4% to 9.44% per annum and mature between January 2004 and March 2009.

NOTE 7. PREFERRED STOCK

The Company's Series A Cumulative Convertible Preferred Stock consists of a maximum of 6,000 shares with a par value of \$.01 per share and a liquidation preference of \$100.00 per share. Dividends are payable at the rate of \$5.00 per year or \$1.25 per quarter to stockholders of record on the 15th day of each March, June, September and December when and as declared by the Board of Directors. The Series A Preferred Stock may be converted, after November 1, 2003, into Common Stock of the Company at the daily average closing price of the Company's Common Stock for the prior five trading days. At December 31, 1998, 5,829 shares of Series A Preferred Stock were issued and outstanding.

NOTE 8. DIVIDENDS

The Company has paid quarterly dividends since the fourth quarter of 1995. The Company paid dividends of \$2.3 million (\$.60 per share) in 1998, \$1.1 million (\$.28 per share) in 1997 and \$1.1 million (\$.28 per share) in 1996. In addition, the Company declared a special dividend of \$1.00 per share in December 1997 that was paid in January 1998.

The Company reported to the Internal Revenue Service that 100% of the dividends paid in 1997 and 1998 represented capital gains and 100% of the dividends paid in 1996 represented a return of capital.

TRANSCONTINENTAL REALTY INVESTORS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

NOTE 9. RENTS UNDER OPERATING LEASES

The Company's operations include the leasing of commercial properties (office buildings, industrial warehouses and shopping centers). The leases thereon expire at various dates through 2008. The following is a schedule of minimum future rents on non-cancelable operating leases at December 31, 1998:

<u>&lt;TABLE&gt;</u>	<u>&lt;C&gt;</u>
1999.....	\$ 25,865
2000.....	22,183
2001.....	17,885
2002.....	13,016
2003.....	9,067
Thereafter.....	13,039
	-----
	\$101,055
	=====

</TABLE>

NOTE 10. ADVISORY AGREEMENT

Basic Capital Management, Inc. ("BCM" or the "Advisor") has served as advisor to the Company since March 28, 1989. BCM is a company owned by a trust for the benefit of the children of Gene E. Phillips. Mr. Phillips served as a Director of the Company until December 31, 1992, as a director of BCM until December 22, 1989 and as Chief Executive Officer of BCM until September 1, 1992. Mr. Phillips serves as a representative of his children's trust which owns BCM and, in such capacity, has substantial contact with the management of BCM and input with respect to its performance of advisory services to the Company.

At the annual meeting of stockholders held on May 8, 1997, stockholders approved the renewal of the Advisory Agreement with BCM through the next annual meeting of stockholders. Subsequent renewals of the Advisory Agreement with BCM do not require the approval of stockholders but do require the approval of the Board of Directors.

Under the Advisory Agreement, the Advisor is required to formulate and submit annually for approval by the Board of Directors a budget and business plan containing a twelve-month forecast of operations and cash flow, a general plan for asset sales and purchases, lending, foreclosure and borrowing activity and other investments. The Advisor is required to report quarterly to the Board of Directors on the Company's performance against the business plan. In addition, all transactions or investments require prior approval by the Board of Directors unless they are explicitly provided for in the approved business plan or are made pursuant to authority expressly delegated to the Advisor by the Board of Directors. The Advisory Agreement also requires prior approval of the Board of Directors for the retention of all consultants and third party professionals, other than legal counsel.

The Advisory Agreement provides for BCM to be responsible for the day-to-day

operations of the Company and to receive an advisory fee comprised of a gross asset fee of .0625% per month (.75% per annum) of the average of the gross asset value (total assets less allowance for amortization, depreciation or depletion and valuation reserves) and an annual net income fee equal to 7.5% of net income.

The Advisory Agreement also provides for BCM to receive an annual incentive sales fee. BCM or an affiliate of BCM is to receive an acquisition commission for supervising the purchase or long-term lease of real estate. BCM or an affiliate of BCM is to receive a mortgage or loan acquisition fee with respect to the purchase of any existing mortgage loan by the Company. BCM or an affiliate of BCM is also to receive a mortgage brokerage and equity refinancing fee for obtaining loans to or refinancing on the Company's properties. BCM also receives reimbursement of certain expenses incurred by it in the performance of advisory services to the Company.

TRANSCONTINENTAL REALTY INVESTORS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

The Advisory Agreement requires BCM or any affiliate of BCM to pay to the Company one-half of any compensation received from third parties with respect to the origination, placement or brokerage of any loan made by the Company.

Under the Advisory Agreement, all or a portion of the annual advisory fee must be refunded by the Advisor if the Operating Expenses of the Company (as defined in the Advisory Agreement) exceed certain limits specified in the Advisory Agreement. The effect of this limitation was to require that BCM refund \$664,000, \$206,000 and \$87,000 of the annual advisory fee for 1998, 1997 and 1996, respectively.

Additionally, if management were to request that BCM render services to the Company other than those required by the Advisory Agreement, BCM or an affiliate of BCM is separately compensated for such additional services on terms to be agreed upon from time to time. As discussed in NOTE 11. "PROPERTY MANAGEMENT," the Company has hired Carmel Realty Services, Ltd. ("Carmel, Ltd."), an affiliate of BCM, to perform property management for the Company's properties and as discussed in NOTE 12. "REAL ESTATE BROKERAGE," has engaged, on a non-exclusive basis, Carmel Realty, Inc. ("Carmel Realty"), also an affiliate of BCM, to provide brokerage services for the Company.

NOTE 11. PROPERTY MANAGEMENT

Carmel, Ltd. provides property management services for a fee of 5% or less of the monthly gross rents collected on the properties under its management. Carmel, Ltd. subcontracts with other entities for property-level management services at various rates. The general partner of Carmel, Ltd. is BCM. The limited partners of Carmel, Ltd. are (1) First Equity Properties, Inc. ("First Equity"), which is 50% owned by a subsidiary of BCM, (2) Gene E. Phillips and (3) a trust for the benefit of the children of Mr. Phillips. Carmel, Ltd. subcontracts the property-level management and leasing of 29 of the Company's commercial properties, its four hotels and the commercial properties owned by Tri-City, in which the Company and IORI are partners, to Carmel Realty, which is a company owned by First Equity. Carmel Realty is entitled to receive property and construction management fees and leasing commissions in accordance with the terms of its property-level management agreement with Carmel, Ltd.

NOTE 12. REAL ESTATE BROKERAGE

Carmel Realty provides brokerage services on a non-exclusive basis. Carmel Realty is entitled to receive a commission for property purchases and sales, in accordance with a sliding scale of total brokerage fees to be paid by the Company.

NOTE 13. ADVISORY FEES, PROPERTY MANAGEMENT FEES, ETC.

Fees and cost reimbursements to BCM and its affiliates:

<TABLE>  
<CAPTION>

	1998	1997	1996
	-----	-----	-----
<S>	<C>	<C>	<C>
Fees			
Advisory.....	\$1,962	\$1,807	\$1,784
Net income.....	558	1,022	--
Property acquisition.....	3,468	2,966	339
Real estate brokerage.....	767	738	283

Mortgage brokerage and equity refinancing.....	341	517	136
Property and construction management and leasing commissions*.....	2,753	2,262	1,879
	-----	-----	-----
	\$9,849	\$9,312	\$4,421
	=====	=====	=====
Cost reimbursements.....	\$1,121	\$1,187	\$1,047
	=====	=====	=====

</TABLE>

\*Net of property management fees paid to subcontractors, other than Carmel Realty.

TRANSCONTINENTAL REALTY INVESTORS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

NOTE 14. INCOME TAXES

For the years 1998, 1997 and 1996, the Company has elected and qualified to be treated as a REIT, as defined in Sections 856 through 860 of the Internal Revenue Code of 1986, as amended (the "Code"), and as such, will not be taxed for federal income tax purposes on that portion of its taxable income which is distributed to stockholders, provided that at least 95% of its REIT taxable income, plus 95% of its taxable income from foreclosure property as defined in Section 857 of the Code, is distributed. See NOTE 8. "DIVIDENDS."

The Company had a loss for federal income tax purposes (after utilization of operating loss carryforwards) in 1998, 1997 and 1996; therefore, the Company recorded no provision for income taxes. The Company's tax basis in its net assets differs from the amount at which its net assets are reported for financial statement purposes, principally due to the accounting for gains and losses on property sales, the difference in the allowance for estimated losses, depreciation on owned properties and investments in joint venture partnerships. At December 31, 1998, the Company's tax basis in its net assets exceeded their basis for financial statement purposes by \$16.4 million. As a result, aggregate future income for income tax purposes will be less than such amount for financial statement purposes, and the Company would be able to maintain its REIT status without distributing 95% of its financial statement income. Additionally, at December 31, 1998, the Company had tax net operating loss carryforwards of \$60.4 million expiring through the year 2011.

As a result of the Company's election to be treated as a REIT for income tax purposes and of its intention to distribute its taxable income, if any, in future years, no deferred tax asset, liability or valuation allowance was recorded.

NOTE 15. COMMITMENTS AND CONTINGENCIES

Olive Litigation. In February 1990, the Company, together with CMET, IORI and National Income Realty Trust, three real estate entities with, at the time, the same officers, directors or trustees and advisor as the Company, entered into a settlement of a class and derivative action entitled Olive et al. v. National Income Realty Trust et al., relating to the operation and management of each of such entities. On April 23, 1990, the Court granted final approval of the terms of the settlement.

On May 4, 1994, the parties entered into a Modification of Stipulation of Settlement dated April 27, 1994 (the "Olive Modification") that settled subsequent claims of breaches of the settlement that were asserted by the plaintiffs and modified certain provisions of the April 1990 settlement. The Olive Modification was preliminarily approved by the Court on July 1, 1994 and final Court approval was entered on December 12, 1994. The effective date of the Olive Modification was January 11, 1995.

The Court retained jurisdiction to enforce the Olive Modification, and during August and September 1996, the Court held evidentiary hearings to assess compliance with the terms of the Olive Modification by the various parties. The Court issued no ruling or order with respect to the matters addressed at the hearings.

Separately, in 1996, legal counsel for the plaintiffs notified the Company's Board of Directors that he intended to assert that certain actions taken by the Board of Directors breached the terms of the Olive Modification. On January 27, 1997, the parties entered into an Amendment to the Olive Modification effective January 9, 1997 (the "Olive Amendment"), which was submitted to the Court for approval on January 29, 1997. The Olive Amendment provides for the settlement of all matters raised at the evidentiary hearings and by plaintiffs' counsel in his notices to the Company's Board of Directors. On May 2, 1997, a hearing was held by the Court to consider approval of the

Olive Amendment. As a result of the hearing, the parties entered into a revised Olive Amendment. The Court issued an order approving the Olive Amendment on July 3, 1997.

The Olive Amendment provides for the addition of four new unaffiliated members to the Company's Board of Directors and sets forth new requirements for the approval of any transactions with certain affiliates until April 28, 1999. In addition, the Company, CMET, IORI and their stockholders released the defendants from any claims

TRANSCONTINENTAL REALTY INVESTORS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

relating to the plaintiffs' allegations and matters which were the subject of the evidentiary hearings. The plaintiffs' allegations of any breaches of the Olive Modification shall be settled by mutual agreement of the parties or, lacking such agreement, by an arbitration proceeding.

Under the Olive Amendment, all shares of the Company owned by Gene E. Phillips or any of his affiliates shall be voted at all stockholder meetings of the Company held until April 28, 1999 in favor of all new members of the Company's Board of Directors added under the Olive Amendment. The Olive Amendment also requires that, until April 28, 1999, all shares of the Company owned by Mr. Phillips or his affiliates in excess of forty percent (40%) of the Company's outstanding shares shall be voted in proportion to the votes cast by all non-affiliated stockholders of the Company.

In accordance with the Olive Amendment, Richard W. Douglas, Larry E. Harley and R. Douglas Leonhard were added to the Company's Board of Directors in January 1998 and Murray Shaw was added to the Company's Board of Directors in February 1998.

Other Litigation. The Company is also involved in various other lawsuits arising in the ordinary course of business. Management of the Company is of the opinion that the outcome of these lawsuits will have no material impact on the Company's financial condition, results of operations or liquidity.

Litigation settlement. In October 1996, the Company received \$1.5 million from the defendants in a lawsuit brought by the Company against the former owners of an office building in New Jersey and their agents. The Company made a loan secured by the building in 1987 and filed a foreclosure action which was subsequently amended in 1990, to include claims of negligent misrepresentation against the borrowers, their legal counsel, architect and engineers.

NOTE 16. OPERATING SEGMENTS

Significant differences among the accounting policies of the segments as compared to the Company's consolidated financial statements principally involve the calculation and allocation of administrative expenses. Management evaluates the performance of the operating segments and allocates resources to them based on net operating income, and cash flow. The Company based reconciliation of expenses that are not reflected in the segments is \$4.8 million of administrative expenses. There are no intersegment revenues and expenses and the Company conducts all of its business in the United States.

The Company has not disclosed prior years' operating segment data on a comparative basis, because management found it impractical to obtain the necessary data.

The table below presents information about the reported operating income of the Company for 1998. Asset information by operating segment is also presented below.

TRANSCONTINENTAL REALTY INVESTORS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

Property sales:

<TABLE>  
<CAPTION>

Commercial	Properties	Apartments	Hotels	Total
-----	-----	-----	-----	-----

<S>	<C>	<C>	<C>	<C>
Operating revenue.....	\$ 31,282	\$ 35,400	\$ 3,147	\$ 69,829
Operating expenses.....	14,291	21,987	2,004	38,282
	-----	-----	-----	-----
Net operating income.....	16,991	13,413	1,143	31,547
Depreciation and amortization.....	6,268	4,115	308	10,691
Interest on debt.....	11,753	10,415	629	22,797
Capital expenditures.....	5,287	4,130	178	9,595
Segment assets at December 31, 1998.....	173,936	156,933	17,876	348,745

<CAPTION>

	Land	Commercial Properties		
	-----	-----		
<S>	<C>	<C>	<C>	<C>
Sales price.....	\$ 375	\$ 33,665		
Cost of sales.....	25	24,234		
Gain on sales.....	350	9,431		

</TABLE>

NOTE 17. QUARTERLY RESULTS OF OPERATIONS

The following is a tabulation of the Company's quarterly results of operations for the years 1998 and 1997 (unaudited):

<TABLE>  
<CAPTION>

	Three Months Ended			
	-----			
	June			
	March 31,	30,	September 30,	December 31,
	-----	-----	-----	-----
<S>	<C>	<C>	<C>	<C>
1998				
Income.....	\$16,272	\$17,514	\$18,221	\$18,629
Expenses.....	17,460	18,264	20,605	20,273
	-----	-----	-----	-----
(Loss) from operations.....	(1,188)	(750)	(2,384)	(1,644)
Equity in income (loss) of investees.....	(18)	450	(90)	(54)
Gain of sale of real estate..	--	2,132	9,883	569
	-----	-----	-----	-----
Net income (loss) applicable to common shares.....	(1,206)	1,832	7,409	(1,129)
Preferred dividend required..	--	--	--	(1)
	-----	-----	-----	-----
	\$ (1,206)	\$ 1,832	\$ 7,409	\$ (1,130)
	=====	=====	=====	=====
Earnings Per Share				
Net income (loss) applicable to common shares.....	\$ (.31)	\$ .47	\$ 1.91	\$ (.29)
	=====	=====	=====	=====

</TABLE>

In the second quarter of 1998, a gain previously deferred on the sale of real estate under the cost recovery method, of \$2.1 million was recognized on the collection of the mortgage note receivable. In the third quarter of 1998, a gain of \$671,000 was recognized on the collection of a mortgage note receivable written off as uncollectible in a prior year. Also in the third quarter of 1998, a gain on sale of real estate of \$5.9 million was recognized on the sale of Chesapeake Ridge Office Building and a gain of \$3.4 million was recognized on the sale of Northtown Mall Shopping Center. In the fourth quarter of 1998 a gain on sale of real estate of \$219,000 was recognized on the sale of Denton Drive Warehouse and a gain of \$350,000 was recognized on the sale of an 19 acre parcel of land.

TRANSCONTINENTAL REALTY INVESTORS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)

<TABLE>  
<CAPTION>

	Three Months Ended			
	-----			
	June			
	March 31,	30,	September 30,	December 31,
	-----	-----	-----	-----
<S>	<C>	<C>	<C>	<C>
1997				



Income.....	\$12,523	\$13,674	\$14,291	\$15,473
Expenses.....	14,437	15,175	16,279	19,687
	-----	-----	-----	-----
(Loss) from operations.....	(1,914)	(1,501)	(1,988)	(4,214)
Equity in income (loss) of investees.....	348	429	(97)	132
Gain of sale of real estate..	1,400	55	--	19,949
	-----	-----	-----	-----
Net income (loss).....	\$ (166)	\$ (1,017)	\$ (2,085)	\$15,867
	=====	=====	=====	=====
Earnings Per Share				
Net income (loss).....	\$ (.04)	\$ (.26)	\$ (.53)	\$ 4.05
	=====	=====	=====	=====

</TABLE>

In the first quarter of 1997, a gain on sale of real estate of \$1.4 million was recognized on the sale of a .9976 acre parcel of land. In the second quarter of 1997, a gain on sale of real estate of \$55,000 was recognized on the sale of a foreclosed single family residence. In the fourth quarter of 1997, a gain on sale of real estate of \$19.4 million was recognized on the sale of the Republic Towers Office Building and a gain of \$554,000 was recognized on the sale of the President's Square Shopping Center. A provision for loss of \$1.3 million was recorded in the fourth quarter of 1997 to writedown the Shaws Plaza Shopping Center to its agreed sales price less estimated selling costs.

NOTE 18. SUBSEQUENT EVENTS

In February 1999, the Company sold the 368 unit Mariner's Point Apartments in St. Petersburg, Florida, for \$6.7 million, receiving net cash of \$2.6 million after paying off \$3.9 million in mortgage debt and the payment of various closing costs. A gain will be recognized on the sale.

In March 1999, the Company purchased the 264 unit Vista Hills Apartments in El Paso, Texas, for \$5.2 million, paying \$1.6 million in cash and obtaining mortgage financing of \$3.6 million. The mortgage bears interest at a variable rate, currently 7.625% per annum, requires monthly payments of principal and interest of \$26,897 and matures in April 2004.

Also in March 1999, the Company purchased the Dominion land a 14.39 acre parcel of land in Dallas, Texas, for \$3.6 million, paying \$1.2 million in cash and obtaining mortgage financing of \$2.4 million. The mortgage bears interest at 15% per annum, requires quarterly payment of interest only and matures in March 2000.

Further in March 1999, the Company refinanced the matured mortgage debt secured by the Lexington Center in Colorado Springs, Colorado in the amount of \$4.3 million, receiving net cash of \$136,000 after paying off \$4.0 million in mortgage debt and the payment of various closing costs. The new mortgage bears interest at a variable rate, currently 7.75% per annum requires monthly payments of principal and interest of \$32,479 and matures in April 2004.

SCHEDULE III

TRANSCONTINENTAL REALTY INVESTORS, INC.

REAL ESTATE AND ACCUMULATED DEPRECIATION

December 31, 1998

<TABLE>

<CAPTION>

Property/Location	Encumbrances	Cost				Gross Amounts of Which			Accumulated
		Initial Cost	Capitalized Subsequent to Acquisition	Other		Carried at End of Year	(1) Total	Depreciation	
		Land	Buildings & Improvements	Improvements	Other	Land	Buildings & Improvements	Total	
(dollars in thousands)									
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Held for Investment Apartments 4400, Midland, TX .....	\$ 1,340	\$ 349	\$ 1,396	\$ --	\$ --	\$ 349	\$ 1,396	\$ 1,745	\$ 23
Arbor Point, Odessa, TX .....	1,101	321	1,285	526	--	321	1,811	2,132	244
Ashton Way, Midland, TX.....	1,340	384	1,536	25	--	384	1,561	1,945	28
Bent Tree,									

Addison, TX.....	6,321	1,702	6,808	85	--	1,702	6,893	8,595	181
Carseka, Los Angeles, CA.....	1,509	460	1,840	75	--	460	1,915	2,375	123
Cliffs of Eldorado, McKinney, TX....	10,631	2,647	10,589	--	--	2,647	10,589	13,236	66
Country Bend, Fort Worth, TX..	2,527	710	2,842	81	--	710	2,923	3,633	104
Coventry, Midland, TX.....	450	236	369	184	--	236	553	789	81
Crescent Place, Houston, TX.....	1,740	494	1,978	123	--	494	2,101	2,595	126
Fairpark, Los Angeles, CA.....	1,509	425	1,701	--	--	425	1,701	2,126	46
Fountains of Waterford, Midland, TX.....	1,055	311	1,243	495	--	311	1,738	2,049	38
Fountain Village, Tucson, AZ.....	7,844	1,518	8,352	2,035	(2,375) (/2/)	1,162	8,368	9,530	3,734
Gladstell Forest, Conroe, TX.....	2,548	504	2,015	163	--	504	2,178	2,682	223
Harper's Ferry, Lafayette, LA...	1,797	349	1,398	173	--	349	1,571	1,920	353
Heritage, Tulsa, OK.....	1,991	148	839	83	(300) (/3/)	88	682	770	124
Hunters Glen, Midland, TX.....	1,895	519	2,075	272	--	519	2,347	2,866	66
Limestone Canyon, Austin, TX.....	1,604	1,998	--	--	1,895 (/4/)	1,998	1,895	3,893	--
Mariners Pointe, St. Petersburg, FL.....	3,859	716	4,059	880	--	716	4,939	5,655	1,092
Mountain Plaza, El Paso, TX.....	2,931	837	3,347	80	--	837	3,427	4,264	89
Sandstone, Mesa, AZ.....	5,801	1,656	6,625	82	--	1,656	6,707	8,363	217
Shadow Run, Pinellas Park, FL.....	7,029	1,503	8,229	212	--	1,503	8,441	9,944	3,287
South Cochran, Los Angeles, CA.....	1,931	540	2,162	15	--	540	2,177	2,717	412
Southgate, Odessa, TX.....	1,021	335	1,338	318	--	335	1,656	1,991	178
Southgreen, Bakersfield, CA.....	2,500	755	3,021	--	--	755	3,021	3,776	7
Spa Cove, Annapolis, MD...	12,001	2,254	10,297	3,961	682 (/4/)	2,337	14,857	17,194	4,673
Summerfield, Orlando, FL.....	4,678	1,175	4,698	136	--	1,175	4,834	6,009	563

Life on  
Which  
Depreciation  
in Latest  
Statement

Property/Location	Date of Construction	Date Acquired	of Operation is Computed
<S>	<C>	<C>	<C>
Held for Investment Apartments			
4400, Midland, TX .....	1981	04/30/98	40 years
Arbor Point, Odessa, TX .....	1975	08/30/96	5-40 years
Ashton Way, Midland, TX.....	1978	04/30/98	5-40 years
Bent Tree, Addison, TX.....	1979	01/28/98	5-40 years
Carseka, Los Angeles, CA.....	1971	11/19/96	5-40 years
Cliffs of Eldorado, McKinney, TX....	1997	10/20/98	40 years
Country Bend, Fort Worth, TX..	1981	09/25/97	5-40 years
Coventry, Midland, TX.....	1977	08/30/96	5-40 years

Crescent Place, Houston, TX.....	1984	03/28/97	5-40 years
Fairpark, Los Angeles, CA.....	1991	12/22/97	40 years
Fountains of Waterford, Midland, TX.....	1977	05/21/98	5-40 years
Fountain Village, Tucson, AZ.....	1973	01/10/86	5-40 years
Gladstell Forest, Conroe, TX.....	1985	06/30/95	5-40 years
Harper's Ferry, Lafayette, LA...	1972	02/25/92	5-40 years
Heritage, Tulsa, OK.....	1966	05/14/90	5-40 years
Hunters Glen, Midland, TX.....	1982	01/16/98	5-40 years
Limestone Canyon, Austin, TX.....	1997	07/10/98	-
Mariners Pointe, St. Petersburg, FL.....	1972	06/28/91	5-40 years
Mountain Plaza, El Paso, TX.....	1972	01/14/98	5-40 years
Sandstone, Mesa, AZ.....	1986	10/01/97	5-40 years
Shadow Run, Pinellas Park, FL.....	1985	04/10/95	5-40 years
South Cochran, Los Angeles, CA.....	1928	05/29/91	5-40 years
Southgate, Odessa, TX.....	1976	08/30/96	5-40 years
Southgreen, Bakersfield, CA.....	1985	12/23/98	40 years
Spa Cove, Annapolis, MD...	1965	02/27/87	5-40 years
Summerfield, Orlando, FL.....	1971	11/02/94	5-40 years

SCHEDULE III  
(Continued)

TRANSCONTINENTAL REALTY INVESTORS, INC.

REAL ESTATE AND ACCUMULATED DEPRECIATION  
December 31, 1998

<TABLE>  
<CAPTION>

Property/Location	Encumbrances	Cost				Gross Amounts of Which Carried at End of Year			
		Initial Cost		Capitalized Subsequent to Acquisition		Buildings & (1) Land Improvements Total		Accumulated	
		Land	Buildings & Improvements	Improvements	Other	Land	Improvements	Total	Depreciation
(dollars in thousands)									
<S> Held for Investment-- Continued Apartments-- Continued Summerstone, Houston, TX.....	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
	\$4,887	\$1,155	\$4,618	\$ 210	\$ --	\$1,155	\$ 4,828	\$ 5,983	\$ 616

Property/Location	Date of Construction	Date Acquired	Life on Which Depreciation in Latest Statement of Operation is Computed
-------------------	----------------------	---------------	---

<S>	<C>	<C>	<C>						
Held for Investment-- Continued Apartments-- Continued Summerstone, Houston, TX.....	1984	12/17/93	5-40 years						
Sunchase, Odessa, TX.....	2,111	742	2,967	449	--	742	3,416	4,158	149
Terrace Hills, El Paso, TX.....	6,429	1,286	5,145	167	--	1,310	5,288	6,598	249
Timbers, Tyler, TX.....	1,775	497	1,988	--	--	497	1,988	2,485	54
Treehouse, Irving, TX.....	2,732	716	2,865	260	--	716	3,125	3,841	172
Villas at Countryside, Sterling, VA....	5,428	1,323	5,290	30	--	1,323	5,320	6,643	229
Villa Piedra, Los Angeles, CA.....	3,481	979	3,915	--	--	979	3,915	4,894	106
Westgate of Laurel, Laurel, MD.....	7,599	849	9,391	202	--	849	9,593	10,442	3,801
Westwood, Odessa, TX.....	333	85	341	108	--	85	449	534	57
Woodland Hills, San Antonio, TX.....	1,149	228	913	--	--	228	913	1,141	148
Woods Edge, Rockville, MD...	6,104	1,015	7,812	157	--	1,015	7,969	8,984	3,504
Woodview, Odessa, TX.....	2,606	716	2,864	67		716	2,931	3,647	49
Sunchase, Odessa, TX.....	1981	10/08/97	5-40 years						
Terrace Hills, El Paso, TX.....	1985	03/05/97	5-40 years						
Timbers, Tyler, TX.....	1973	12/30/97	40 years						
Treehouse, Irving, TX.....	1974	05/01/97	5-40 years						
Villas at Countryside, Sterling, VA....	1985	05/15/97	5-40 years						
Villa Piedra, Los Angeles, CA.....	1991	12/22/97	40 years						
Westgate of Laurel, Laurel, MD.....	1969	01/01/95	5-40 years						
Westwood, Odessa, TX.....	1977	08/30/96	5-40 years						
Woodland Hills, San Antonio, TX.....	1972	05/01/92	40 years						
Woods Edge, Rockville, MD...	1965	01/01/95	5-40 years						
Woodview, Odessa, TX.....	1974	05/01/98	5-40 years						
Office Buildings									
74 New									
Montgomery, San Francisco, CA.....	6,219	2,277	9,105	4,107	(336) (/2/)	2,210	12,943	15,153	4,849
Atrium, Palm Beach, FL.....	4,078	1,147	4,590	--		1,147	4,590	5,737	67
Bonita Plaza, Bonita, CA.....	5,143	1,168	4,670	448	--	1,168	5,118	6,286	187
Corporate Pointe, Chantilly, VA...	3,973	830	3,321	411	--	830	3,732	4,562	609
Daley Plaza, San Diego, CA.....	3,443	973	3,889	110		973	3,999	4,972	80
Forum, Richmond, VA.....	5,439	1,360	5,439	833	--	1,360	6,272	7,632	1,320
Hartford, Dallas, TX.....	2,214	630	2,520	501	--	630	3,021	3,651	432
Institute Place Lofts, Chicago, IL.....	6,058	665	7,057	393	--	665	7,450	8,115	3,574
Lexington									

Center, Colorado Springs, CO..... One Steeplechase, Sterling, VA.... Plaza Towers, St. Petersburg, FL..... Savings of America, Houston, TX..... Town & Country, Houston, TX..... Office Buildings 74 New Montgomery, San Francisco, CA..... Atrium, Palm Beach, FL..... Bonita Plaza, Bonita, CA..... Corporate Pointe, Chantilly, VA... Daley Plaza, San Diego, CA..... Forum, Richmond, VA..... Hartford, Dallas, TX..... Institute Place Lofts, Chicago, IL..... Lexington Center, Colorado Springs, CO..... One Steeplechase, Sterling, VA.... Plaza Towers, St. Petersburg, FL..... Savings of America, Houston, TX..... Town & Country, Houston, TX.....	4,000	1,103	4,413	367	--	1,103	4,780	5,883	148
	8,146	1,380	5,520	2,807	72 (/4/)	1,380	8,399	9,779	2,299
	7,354	1,760	12,617	6,762	(4,379) (/2/)	1,241	15,519	16,760	8,851
	1,260	338	1,353	341	--	338	1,694	2,032	111
	--	108	432	508	--	108	940	1,048	456
1914	09/21/90	1-40 years							
1985	06/26/98	40 years							
1991	09/16/97	5-40 years							
1992	10/28/94	5-40 years							
1981	05/29/98	5-40 years							
1987	10/30/92	2-40 years							
1980	11/10/94	2-40 years							
1910	01/01/93	2-40 years							
1986	12/30/97	3-40 years							
1987	12/22/92	5-40 years							
1979	11/14/85	1-40 years							
1979	03/31/97	3-40 years							
1982	05/01/92	3-40 years							

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SCHEDULE III  
(Continued)

TRANSCONTINENTAL REALTY INVESTORS, INC.

REAL ESTATE AND ACCUMULATED DEPRECIATION  
December 31, 1998

<TABLE>  
<CAPTION>

Property/Location	Encumbrances	Cost				Gross Amounts of Which Carried at End of Year			Accumulated Depreciation	Date of Construction
		Initial Cost	Buildings & Improvements	Capitalized Subsequent to Acquisition	Other	Land	Buildings & Improvements	(1) Total		
(dollars in thousands)										
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Held for Investment-- Continued Office Buildings-- Continued Valley Rim, San Diego, CA.....	\$ 3,662	\$1,078	\$ 4,311	13	\$ --	\$1,078	\$ 4,324	\$ 5,402	\$ 56	1988
Venture Center, Atlanta, GA..... Viewridge, San	1,117	411	2,746	228	--	411	2,974	3,385	770	1981

Diego, CA.....	1,318	393	1,572	--	--	393	1,572	1,965	26	1979
Waterstreet, Boulder, CO.....	7,932	2,605	10,420	951	--	2,605	11,371	13,976	2,705	1988
Industrial Warehouses Corporate Center, Ashburn, VA.....	6,914	1,259	5,038	1,136	--	1,259	6,174	7,433	1,123	1989
Encon, Fort Worth, TX.....	3,500	984	3,935	--	--	984	3,935	4,919	123	1958
Parke Long, Chantilly, VA... Technology Trading, Sterling, VA....	7,622	1,838	7,361	1,117	--	1,838	8,478	10,316	1,215	1989
Texstar, Arlington, TX... Tricon, Atlanta, GA.....	4,044	1,199	4,796	857	--	1,199	5,653	6,852	725	1987
	1,150	333	1,331	159	--	333	1,490	1,823	202	1967
	10,114	2,761	6,442	1,602	--	2,761	8,044	10,805	1,636	1971- 1975
Shopping Centers Dunes Plaza, Michigan City, IN.....	3,404	1,230	5,430	1,560	(482) (/5/)	1,071	6,667	7,738	1,475	1978
K-Mart, Cary, NC.....	1,940	1,358	1,157	162	--	1,358	1,319	2,677	--	1981
Parkway Center, Dallas, TX.....	1,775	273	1,876	405	--	273	2,281	2,554	788	1979
Parkway North, Dallas, TX.....	3,900	1,173	4,692	182	--	1,173	4,874	6,047	135	1980
Plaza on Bachman Creek, Dallas, TX.....	2,327	734	2,935	255	--	734	3,190	3,924	76	1986
Sadler Square, Amelia Island, FL.....	2,368	679	2,715	77	--	679	2,792	3,471	433	1987
Sheboygan, Sheboygan, WI... Hotels	781	242	1,371	17	--	242	1,388	1,630	224	1977
Belmont, Chicago, IL.....	3,568	950	3,847	--	--	950	3,847	4,797	9	1995
Brompton, Chicago, IL.....	2,139	572	2,365	14	--	572	2,379	2,951	6	1995
Majestic Inn, San Francisco, CA.....	5,627	1,139	4,555	972	--	1,139	5,527	6,666	1,310	1902
Surf, Chicago, IL.....	3,544	945	3,851	--	--	945	3,851	4,796	9	1995
Land Eagle Crest, Farmers Branch, TX.....	--	2,500	--	134	--	2,634	--	2,634	--	--

Property/Location	Date Acquired	Life on Which Depreciation in Latest Statement of Operation is Computed
<S>	<C>	<C>
Held for Investment-- Continued Office Buildings-- Continued Valley Rim, San Diego, CA.....	07/08/98	3-40 years
Venture Center, Atlanta, GA.....	07/04/89	1-40 years
Viewridge, San Diego, CA.....	05/29/98	40 years
Waterstreet, Boulder, CO.....	09/30/91	2-40 years
Industrial Warehouses Corporate Center, Ashburn, VA.....	04/28/94	3-40 years
Encon, Fort Worth, TX.....	10/01/97	40 years
Parke Long,		

Chantilly, VA... Technology Trading, Sterling, VA....	06/16/94	3-40 years
Texstar, Arlington, TX...	12/21/93	3-40 years
Tricon, Atlanta, GA.....	12/16/93	5-40 years
Shopping Centers Dunes Plaza, Michigan City, IN.....	02/11/93	2-40 years
K-Mart, Cary, NC.....	03/17/92	5-40 years
Parkway Center, Dallas, TX.....	08/05/98	--
Parkway North, Dallas, TX.....	11/01/91	1-40 years
Plaza on Bachman Creek, Dallas, TX.....	02/18/98	2-40 years
Sadler Square, Amelia Island, FL.....	03/31/98	5-40 years
Sheboygan, Sheboygan, WI...	11/22/93	3-40 years
Hotels Belmont, Chicago, IL.....	05/21/92	40 years
Brompton, Chicago, IL.....	12/02/98	5-40 years
Majestic Inn, San Francisco, CA.....	12/02/98	5-40 years
Surf, Chicago, IL.....	12/31/90	2-40 years
Land Eagle Crest, Farmers Branch, TX.....	12/02/98	5-40 years
	05/15/98	--

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SCHEDULE III  
(Continued)

TRANSCONTINENTAL REALTY INVESTORS, INC.

REAL ESTATE AND ACCUMULATED DEPRECIATION  
December 31, 1998

<TABLE>  
<CAPTION>

Property/Location	Encumbrances	Cost				Gross Amounts of Which			Accumulated Depreciation
		Initial Cost	Capitalized Subsequent to Acquisition		Carried at End of Year		(1) Total		
		Land	Buildings & Improvements	Improvements	Other	Land	Buildings & Improvements		
(dollars in thousands)									
<S> Held for Investment-- Continued Land--Continued Las Colinas, Las Colinas, TX.....	<C> \$ --	<C> \$ 995	<C> \$ --	<C> \$ 5	<C> \$ --	<C> \$ 995	<C> \$ 5	<C> \$ 1,000	<C> \$ --
Laws, Dallas, TX.....	--	2,047	--	--	--	2,047	--	2,047	--
Lemon Carlisle, Dallas, TX.....	2,141	3,576	--	30	--	3,606	--	3,606	--
West End, Dallas, TX.....	8,716	11,405	--	57	--	11,405	57	11,462	--
Investment Properties.....	280,517	88,855	285,823	39,175	(5,223)	87,965	320,665	408,630	61,241

<CAPTION>

Life on  
Which

Property/Location	Date of Construction	Date Acquired	Depreciation in Latest Statement of Operation is Computed
<S>	<C>	<C>	<C>
Held for Investment--Continued			
Land--Continued			
Las Colinas, Las Colinas, TX.....	--	01/25/96	--
Laws, Dallas, TX.....	--	01/15/98	--
Lemon Carlisle, Dallas, TX.....	--	02/09/98	--
West End, Dallas, TX.....	--	08/05/97	5 year
Investment Properties.....			
Properties Held for Sale			
Land			
Fiesta, San Angelo, TX.....	--	44	--
Fruitland, Fruitland Park, FL.....	--	253	--
Moss Creek, Greensboro, NC..	--	85	--
Republic Parking, Dallas, TX.....	--	1,074	--
Properties held for sale.....	--	1,456	--
	\$280,517	\$90,311	\$285,823
		\$39,175	\$ (5,323)
			\$89,321
			\$320,665
			\$409,986
			\$61,241
Properties Held for Sale			
Land			
Fiesta, San Angelo, TX.....	--	12/31/91	--
Fruitland, Fruitland Park, FL.....	--	05/01/92	--
Moss Creek, Greensboro, NC..	--	12/31/96	--
Republic Parking, Dallas, TX.....	--	11/27/92	--
Properties held for sale.....			

</TABLE>

- 
- (1) The aggregate cost for federal income tax purposes is \$412.6 million.
  - (2) Writedown of property to estimated net realizable value.
  - (3) Escrow deposits deducted from the basis of the property.
  - (4) Construction period interest and taxes.
  - (5) Forgiveness of debt and cash received deducted from the basis of the property, offset by land acquired in 1992.
  - (6) Cash received for easement deducted from the basis of the property.

SCHEDULE III  
(Continued)

TRANSCONTINENTAL REALTY INVESTORS, INC.

REAL ESTATE AND ACCUMULATED DEPRECIATION

<TABLE>  
<CAPTION>

	1998	1997	1996
<S>	<C>	<C>	<C>
	(dollars in thousands)		



Reconciliation of Real Estate			
Balance at January 1,.....	\$331,668	\$270,395	\$269,896
Additions			
Purchases and improvements.....	101,510	79,483	11,097
Foreclosures.....	2,514	--	691
Deductions			
Sale of real estate.....	(25,706)	(15,860)	(7,121)
Sale of foreclosed properties.....	--	(691)	(2,589)
Writedown due to permanent impairment of property.....	--	(1,337)	(1,579)
Other.....	--	(322)	--
	-----	-----	-----
Balance at December 31,.....	\$409,986	\$331,668	\$270,395
	=====	=====	=====

Reconciliation of Accumulated Depreciation			
Balance at January 1,.....	\$ 56,837	\$ 50,386	\$ 44,172
Additions			
Depreciation.....	10,691	9,578	8,461
Deductions			
Sale of real estate.....	(6,287)	(387)	(1,718)
Sale of foreclosed properties.....	--	(2,740)	(529)
	-----	-----	-----
Balance at December 31,.....	\$ 61,241	\$ 56,837	\$ 50,386
	=====	=====	=====

</TABLE>

SCHEDULE IV

TRANSCONTINENTAL REALTY INVESTORS, INC.

MORTGAGE LOANS ON REAL ESTATE  
December 31, 1998

<TABLE>  
<CAPTION>

Description	Interest Rate	Final Maturity Date	Periodic Payment Terms	Prior Liens	Face Amount of Mortgage	Carrying Amounts of Mortgage (1)	Principal Amount of Loans Subject to Delinquent Principal or Interest
(dollars in thousands)							
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
FIRST MORTGAGE LOANS							
MILWAUKEE LAND... Secured by 34,847 sq. ft. of land in Milwaukee, WI.	Varies	01/91	Note receivable bearing interest at prime plus 1%. Monthly interest only payments due until maturity, at which time all principal and unpaid interest was due.	\$ --	\$ 200	\$ 60	\$60 (/2/)
MOSS CREEK LOTS.. Secured by residential lots in Greensboro, NC.	9.0%-12.0%	06/2000	5 notes outstanding at 12/31/98. Monthly payments of principal and interest ranging from \$118 to \$339.	--	140	84	29
Chateau Charles.. Secured by a hotel in Lake Charles, LA	3.85%-10.0%	07/99-02/2016	First and second lien notes bearing interest at 3.85% to 10%. Monthly principal and interest. Payments of \$21,658 due monthly.	--	4,550	356	356
JUNIOR MORTGAGE LOANS							
HAMPTON..... Secured by two office buildings in Milwaukee, WI	Varies	On Demand	Note bearing interest at prime plus 1%. Monthly payments of interest only required. Principal	--	400	92	92 (/2/)

is due upon demand.

LINCOLN COURT APARTMENTS.....	Varies	06/2004	Two notes bearing interest at prime plus 1%. Interest only payments due monthly until maturity, at which time all principal and unpaid interest are due.	1,326	1,369	1,369	--
Secured by apartment building in Dallas, TX.				-----	-----	-----	---
				1,326	6,659	1,961	537
SECURED BY OTHER THAN REAL ESTATE							
CRIVELLO #2.....	Varies	On Demand	Note bearing interest at prime. Monthly payment of interest only.	--	879	193	193 (/2/)
Secured by a mortgage note secured by real property in Milwaukee, WI.							
DOUBLE FEATURE VIDEO.....	Varies	07/98	Three notes outstanding. Quarterly payments due based on gross sales. Unpaid accruals compounded to principal.	--	645	181	181 (/2/)
Secured by a general business security agreement.							

</TABLE>

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SCHEDULE IV  
(Continued)

TRANSCONTINENTAL REALTY INVESTORS, INC.

MORTGAGE LOANS ON REAL ESTATE  
December 31, 1998

<TABLE>  
<CAPTION>

Description	Interest Rate	Final Maturity Date	Periodic Payment Terms	Prior Liens	Face Amount of Mortgage	Carrying Amounts of Mortgage(1)	Principal Amount of Loans Subject to Delinquent Principal or Interest
(dollars in thousands)							
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
SECURED BY OTHER THAN REAL ESTATE--							
Continued							
HOPPER, Secured by a general business security agreements.....	12.5%	11/95	Principal and interest payments of \$480 due monthly.	--	\$ 44	\$ 44	\$ 44 (/2/)
Total.....				-----	-----	-----	-----
				\$1,326	\$8,227	2,379	\$955
				=====	=====		=====
Interest.....						3	
Unamortized discount.....						(3)	
Allowance for estimated losses.....						(886)	
						\$1,493	
						=====	

</TABLE>

- 
- (1) The aggregate cost for federal income tax purposes is \$2.2 million.
  - (2) An allowance for loss has been provided to reduce the carrying value of this loan to the Company's estimate of fair value of the underlying

SCHEDULE IV  
(Continued)

## TRANSCONTINENTAL REALTY INVESTORS, INC.

## MORTGAGE LOANS ON REAL ESTATE

&lt;TABLE&gt;

&lt;CAPTION&gt;

	1998	1997	1996
	-----	-----	-----
	(dollars	in thousands)	
<S>	<C>	<C>	<C>
Balance at January 1,.....	\$ 4,838	\$ 9,485	\$11,166
Additions			
New mortgage loans.....	149	--	--
Deductions			
Collections of principal.....	(94)	(5,025)	(885)
Foreclosed properties and deeds-in-lieu of foreclosure.....	(2,514)	--	(683)
Write off of uncollectible mortgage loan.....	--	--	(63)
Write off of principal due to discount for early payoff.....	--	(135)	(50)
Write off of unamortized discount for early payoff.....	--	513	--
	-----	-----	-----
Balance at December 31,.....	\$ 2,379	\$ 4,838	\$ 9,485
	=====	=====	=====

&lt;/TABLE&gt;

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND  
FINANCIAL DISCLOSURE

Not applicable.

## PART III

## ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND ADVISOR OF THE REGISTRANT

## Directors

The affairs of Transcontinental Realty Investors, Inc. (the "Company" or the "Registrant") are managed by a Board of Directors. The Directors are elected at the annual meeting of stockholders or appointed by the incumbent Board of Directors and serve until the next annual meeting of stockholders or until a successor has been elected or approved.

The Directors of the Company are listed below, together with their ages, terms of service, all positions and offices with the Company or its advisor, Basic Capital Management, Inc. ("BCM" or the "Advisor"), their principal occupations, business experience and directorships with other companies during the last five years or more. The designation "Affiliated", when used below with respect to a Director, means that the Director is an officer, director or employee of the Advisor or an officer of the Company. The designation "Independent", when used below with respect to a Director, means that the Director is neither an officer of the Company nor a director, officer or employee of the Advisor, although the Company may have certain business or professional relationships with such Director as discussed in ITEM 13. "CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS--Certain Business Relationships."

TED P. STOKELY: Age 65, Director (Independent) (since April 1990) and Chairman of the Board (since January 1995).

General Manager (since January 1995) of ECF Senior Housing Corporation, a nonprofit corporation; General Manager (since January 1993) of Housing Assistance Foundation, Inc., a nonprofit corporation; Part-time unpaid Consultant (since January 1993) and paid Consultant (April 1992 to December 1992) of Eldercare Housing Foundation ("Eldercare"), a nonprofit corporation; President (April 1992 to April 1994) of PSA Group; Executive Vice President (1987 to 1991) of Key Companies Inc.; Trustee (since April 1990) and Chairman of the Board (since January 1995) of Continental Mortgage and Equity Trust ("CMET"); Director (since April 1990) and Chairman of the Board (since January 1995) of Income Opportunity Realty

Investors, Inc. ("IORI"); and Trustee (April 1990 to August 1994) of National Income Realty Trust ("NIRT").

RICHARD W. DOUGLAS: Age 51, Director (Independent) (since January 1998).

Executive Vice President of The Staubach Company (since February 1999); President (1991 to 1999) of Dallas Chamber of Commerce; President (1988 to 1991) of North Texas Commission; President (1978 to 1981) of Las Colinas Corporation and Southland Investment Properties, both affiliates of Southland Financial Corporation; Trustee (since January 1998) of CMET; and Director (since January 1998) of IORI.

LARRY E. HARLEY: Age 58, Director (Independent) (since January 1998).

President (1993 to 1997) and Executive Vice President (1992 to 1993) of U.S. Operations, Executive Vice President (1989 to 1992) and Senior Vice President (1986 to 1989) of Distribution Operations, Director of Marketing (1984 to 1986), and Manager of North Central Distribution Center (1974 to 1984) of Mary Kay Cosmetics; Trustee (since January 1998) of CMET; and Director (since January 1998) of IORI.

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R. DOUGLAS LEONHARD: Age 62, Director (Independent) (since January 1998).

Director (since November 1998) of Optel, Inc.; Senior Vice President (1986 to 1997) of LaCantera Development Company, a wholly-owned subsidiary of USAA; Senior Vice President (1980 to 1985) of The Woodlands Development Corporation; Vice President and Houston Projects Manager (1973 to 1979) of Friendswood Development Company; Manager in various capacities (1960 to 1973) of Exxon Corp; Trustee (since January 1998) of CMET; and Director (since January 1998) of IORI.

MURRAY SHAW: Age 67, Director (Independent) (since February 1998).

Chairman of the Board of Regents (since 1997) of Stephen F. Austin University; Vice President (1967 to 1996) of Tracor, Inc.; Trustee (since February 1998) of CMET; and Director (since February 1998) of IORI.

MARTIN L. WHITE: Age 59, Director (Independent) (since January 1995).

Chief Executive Officer (since 1995) of Builders Emporium, Inc.; Chairman and Chief Executive Officer (since 1993) of North American Trading Company Ltd.; President and Chief Operating Officer (since 1992) of Community Based Developers, Inc.; Development Officer and Loan Manager (1986 to 1992) of the City of San Jose, California; Vice President and Director of Programs (1967 to 1986) of Arpact, Inc., a government contractor for small business development and trade; Trustee (since January 1995) of CMET; and Director (since January 1995) of IORI.

EDWARD G. ZAMPA: Age 64, Director (Independent) (since January 1995).

General Partner (since 1976) of Edward G. Zampa and Company; and Trustee (since January 1995) of CMET; and Director (since January 1995) of IORI.

#### Board Committees

The Board of Directors held ten meetings during 1998. For such year, no incumbent Director attended fewer than 75% of the aggregate of (1) the total number of meetings held by the Board of Directors during the period for which he had been a Director and (2) the total number of meetings held by all committees of the Board of Directors on which he served during the period that he served.

The Board of Directors has an Audit Committee, the function of which is to review the Company's operating and accounting procedures. The current members of the Audit Committee, all of whom are Independent Directors, are Messrs. Stokely, Leonhard and White. The Audit Committee met twice during 1998.

The Board of Directors has a Relationship with Advisor Committee and a Board Development Committee. The current members of the Relationship with Advisor Committee are Messrs. Stokely and Zampa. The Relationship with Advisor Committee reviews and reports to the Board of Directors on the services provided to the Company by the Advisor and its affiliates and the terms of any engagement or compensation of the Advisor or its affiliates. The Relationship with Advisor Committee did not meet in 1998. The Board Development Committee reviews and reports to the Board of Directors on the membership, compensation and functions of the Board of Directors. The current member of the Board Development Committee is Mr. White. The Board Development Committee did not meet in 1998.

The Board of Directors does not have Nominating or Compensation Committees.

## Executive Officers

The following persons currently serve as executive officers of the Company: Randall M. Paulson, President; Karl L. Blaha, Executive Vice President--Commercial Asset Management; Bruce A. Endendyk, Executive Vice President; Thomas A. Holland, Executive Vice President and Chief Financial Officer; and Steven K. Johnson, Executive Vice President--Residential Asset Management. Their positions with the Company are not subject to a vote of stockholders. Their ages, terms of service, all positions and offices with the Company or BCM, other principal occupations, business experience and directorships with other companies during the last five years or more are set forth below.

RANDALL M. PAULSON: Age 52, President (since August 1995) and Executive Vice President (January 1995 to August 1995).

President (since August 1995) and Executive Vice President (January 1995 to August 1995) of CMET, IORI and Syntek Asset Management, Inc. ("SAMI"); President (since August 1995) and Executive Vice President (October 1994 to August 1995) of BCM; President (since January 1998) and Director (January 1998 to December 1998) of NRLP Management Corp. ("NMC") the general partner of National Realty, L.P. ("NRLP") and National Operating, L.P. ("NOLP"); Director (August 1995 to November 1998) of SAMI; Executive Vice President (since January 1995) of American Realty Trust, Inc. ("ART"); Vice President (1993 to 1994) of GSSW, LP, a joint venture of Great Southern Life and Southwestern Life; Vice President (1990 to 1993) of Property Company of America Realty, Inc.; and President (1990) of Paulson Realty Group.

KARL L. BLAHA: Age 51, Executive Vice President--Commercial Asset Management (since July 1997).

Executive Vice President--Commercial Asset Management (since July 1997), Executive Vice President and Director of Commercial Management (April 1992 to August 1995) of BCM, CMET, IORI, and SAMI; Director (since June 1996), President (since October 1993) and Executive Vice President and Director of Commercial Management (April 1992 to October 1993) of ART; Executive Vice President (October 1992 to July 1997) of Carmel Realty, Inc. ("Carmel Realty"), a company owned by First Equity Properties, Inc. ("First Equity"), which is 50% owned by a subsidiary of BCM; Director and President (since 1996) of First Equity; Director (since November 1998) of SAMI; Executive Vice President (since January 1998) and Director (since December 1998) of NMC; Executive Vice President and Director of Commercial Management (April 1992 to February 1994) of NIRT and Vinland Property Trust ("VPT"); Partner--Director of National Real Estate Operations (August 1988 to March 1992) of First Winthrop Corporation; and Vice President (April 1984 to August 1988) of Southmark Corporation ("Southmark").

BRUCE A. ENDENDYK: Age 50, Executive Vice President (since January 1995).

President (since January 1995) of Carmel Realty; Executive Vice President (since January 1995) of BCM, SAMI, ART, CMET, IORI and (since January 1998) of NMC; Management Consultant (November 1990 to December 1994); Executive Vice President (January 1989 to November 1990) of Southmark; and President and Chief Executive Officer (March 1988 to January 1989) of Southmark Equities Corporation.

THOMAS A. HOLLAND: Age 56, Executive Vice President and Chief Financial Officer (since August 1995); Secretary (since February 1997); and Senior Vice President and Chief Accounting Officer (June 1990 to August 1995).

Executive Vice President and Chief Financial Officer (since August 1995) and Senior Vice President and Chief Accounting Officer (July 1990 to August 1995) of BCM, SAMI, ART, CMET, IORI; Executive Vice President and Chief Financial Officer (since January 1998) of NMC; Secretary (since February 1997) of CMET and IORI; and Senior Vice President and Chief Accounting Officer (July 1990 to February 1994) of NIRT and VPT.

STEVEN K. JOHNSON: Age 41, Executive Vice President--Residential Asset Management (since August 1998) and Vice President (August 1990 to August 1991).

Executive Vice President--Residential Asset Management (since August 1998) and Vice President (August 1990 to August 1991) of BCM, SAMI, ART, CMET and IORI; Executive Vice President--Residential Management (since August 1998) of NMC; Chief Operating Officer (January 1993 to August 1998) of Garden Capital, Inc.; Executive Vice President (December 1994 to August 1998) of Garden Capital Management, Inc.; Executive Vice President--Residential Asset Management (since January 1999) of NMC; and Vice

President (August 1991 to January 1993) of SHL Properties Realty Advisors, Inc. and SHL Acquisition Corporation II and III.

#### Officers

Although not executive officers of the Company, the following persons currently serve as officers of the Company: Robert A. Waldman, Senior Vice President and General Counsel; and Drew D. Potera, Vice President and Treasurer. Their positions with the Company are not subject to a vote of stockholders. Their ages, terms of service, all positions and offices with the Company or BCM, other principal occupations, business experience and directorships with other companies during the last five years or more are set forth below.

ROBERT A. WALDMAN: Age 46, Senior Vice President and General Counsel (since January 1995), Vice President (December 1990 to January 1995) and Secretary (December 1993 to February 1997).

Senior Vice President and General Counsel (since January 1995), Vice President (December 1990 to January 1995) and Secretary (December 1993 to February 1997) of CMET and IORI; Senior Vice President and General Counsel (since January 1995), Vice President (January 1993 to January 1995) and Secretary (since December 1989) of ART; Senior Vice President and General Counsel (since November 1994), Vice President and Corporate Counsel (November 1989 to November 1994), and Secretary (since November 1989) of BCM; Senior Vice President and General Counsel (since January 1995), Vice President (April 1990 to January 1995) and Secretary (since December 1990) of SAMI; and Senior Vice President, Secretary and General Counsel (since January 1998) of NMC.

DREW D. POTERA: Age 39, Vice President (since December 1996) and Treasurer (since December 1990).

Vice President (since December 1996) and Treasurer (since December 1990) of CMET and IORI; Treasurer (since August 1991) and Assistant Treasurer (December 1990 to August 1991) of ART; Vice President, Treasurer and Securities Manager (since July 1990) of BCM; Vice President and Treasurer (since February 1992) of SAMI; Vice President and Treasurer (since January 1998) of NMC; Treasurer (December 1990 to February 1994) of NIRT and VPT; and Financial Consultant with Merrill Lynch, Pierce, Fenner & Smith Incorporated (June 1985 to June 1990).

In addition to the foregoing officers, the Company has several vice presidents and assistant secretaries who are not listed herein.

#### Compliance with Section 16(a) of the Securities Exchange Act of 1934

Under the securities laws of the United States, the Directors, executive officers, and any persons holding more than ten percent of the Company's shares of Common Stock are required to report their share ownership and any changes in that ownership to the Securities and Exchange Commission (the "Commission"). Specific due dates for these reports have been established and the Company is required to report any failure to file by these dates during 1998. All of these filing requirements were satisfied by the Company's Directors and executive officers and ten percent holders. In making these statements, the Company has relied on the written representations of its incumbent Directors and executive officers and its ten percent holders and copies of the reports that they have filed with the Commission.

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#### The Advisor

Although the Board of Directors is directly responsible for managing the affairs of the Company and for setting the policies which guide it, the day-to-day operations of the Company are performed by a contractual advisor under the supervision of the Board of Directors. The duties of the advisor include, among other things, locating, investigating, evaluating and recommending real estate and mortgage note investment and sales opportunities as well as financing and refinancing sources. The advisor also serves as a consultant to the Board of Directors in connection with the business plan and investment decisions made by the Board of Directors.

BCM has served as the Company's advisor since March 1989. BCM is a corporation of which Messrs. Paulson, Blaha, Endendyk, Holland and Johnson serve as executive officers. BCM is a company owned by a trust for the benefit of the children of Gene E. Phillips. Mr. Phillips served as a director of BCM until December 22, 1989, and as Chief Executive Officer of BCM until September 1, 1992. Mr. Phillips serves as a representative of his children's trust which owns BCM and, in such capacity, has substantial contact with the management of BCM and input with respect to its performance of advisory services to the Company.

At the annual meeting of stockholders held on May 8, 1997, stockholders approved the renewal of the Advisory Agreement with BCM through the next annual meeting of stockholders. Subsequent renewals of the Advisory Agreement with BCM do not require the approval of stockholders but do require the approval of the Board of Directors.

Under the Advisory Agreement, the Advisor is required to formulate and submit annually for approval by the Board of Directors a budget and business plan containing a twelve-month forecast of operations and cash flow, a general plan for asset sales or purchases, lending, foreclosure and borrowing activity, and other investments, and the Advisor is required to report quarterly to the Board of Directors on the Company's performance against the business plan. In addition, all transactions or investments require prior approval by the Board of Directors unless they are explicitly provided for in the approved business plan or are made pursuant to authority expressly delegated to the Advisor by the Board of Directors.

The Advisory Agreement also requires prior approval of the Board of Directors for the retention of all consultants and third party professionals, other than legal counsel. The Advisory Agreement provides that the Advisor shall be deemed to be in a fiduciary relationship to the stockholders; contains a broad standard governing the Advisor's liability for losses by the Company; and contains guidelines for the Advisor's allocation of investment opportunities as among itself, the Company and other entities it advises.

The Advisory Agreement provides for BCM to be responsible for the day-to-day operations of the Company and to receive an advisory fee comprised of a gross asset fee of .0625% per month (.75% per annum) of the average of the gross asset value (total assets less allowance for amortization, depreciation or depletion and valuation reserves) and an annual net income fee equal to 7.5% of the Company's net income.

The Advisory Agreement also provides for BCM to receive an annual incentive sales fee equal to 10% of the amount, if any, by which the aggregate sales consideration for all real estate sold by the Company during such fiscal year exceeds the sum of: (1) the cost of each such property as originally recorded in the Company's books for tax purposes (without deduction for depreciation, amortization or reserve for losses), (2) capital improvements made to such assets during the period owned, and (3) all closing costs, (including real estate commissions) incurred in the sale of such real estate; provided, however, no incentive fee shall be paid unless (a) such real estate sold in such fiscal year, in the aggregate, has produced an 8% simple annual return on the net investment including capital improvements, calculated over the holding period before depreciation and inclusive of operating income and sales consideration and (b) the aggregate net operating income from all real estate owned for each of the prior and current fiscal years shall be at least 5% higher in the current fiscal year than in the prior fiscal year.

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Additionally, pursuant to the Advisory Agreement BCM or an affiliate of BCM is to receive an acquisition commission for supervising the acquisition, purchase or long-term lease of real estate equal to the lesser of (1) up to 1% of the cost of acquisition, inclusive of commissions, if any, paid to nonaffiliated brokers or (2) the compensation customarily charged in arm's-length transactions by others rendering similar property acquisition services as an ongoing public activity in the same geographical location and for comparable property, provided that the aggregate purchase price of each property (including acquisition fees and real estate brokerage commissions) may not exceed such property's appraised value at acquisition.

The Advisory Agreement requires BCM or any affiliate of BCM to pay to the Company, one-half of any compensation received from third parties with respect to the origination, placement or brokerage of any loan made by the Company; provided, however, that the compensation retained by BCM or any affiliate of BCM shall not exceed the lesser of (1) 2% of the amount of the loan commitment or (2) a loan brokerage and commitment fee which is reasonable and fair under the circumstances.

The Advisory Agreement also provides that BCM or an affiliate of BCM is to receive a mortgage or loan acquisition fee with respect to the acquisition or purchase of any existing mortgage loan by the Company equal to the lesser of (1) 1% of the amount of the loan purchased or (2) a brokerage or commitment fee which is reasonable and fair under the circumstances. Such fee will not be paid in connection with the origination or funding of any mortgage loan by the Company.

Under the Advisory Agreement, BCM or an affiliate of BCM is also to receive a mortgage brokerage and equity refinancing fee for obtaining loans or refinancing on properties equal to the lesser of (1) 1% of the amount of the loan or the amount refinanced or (2) a brokerage or refinancing fee which is reasonable and fair under the circumstances; provided, however, that no such fee shall be paid on loans from BCM or an affiliate of BCM without the

approval of the Company's Board of Directors. No fee shall be paid on loan extensions.

Under the Advisory Agreement, BCM receives reimbursement of certain expenses incurred by it in the performance of advisory services.

Under the Advisory Agreement, all or a portion of the annual advisory fee must be refunded by the Advisor if the Operating Expenses of the Company (as defined in the Advisory Agreement) exceed certain limits specified in the Advisory Agreement based on the book value, net asset value and net income of the Company during such fiscal year. The effect of the limitation was to require that BCM refund \$664,000 of the annual advisory fee for 1998.

Additionally, if management were to request that BCM render services to the Company other than those required by the Advisory Agreement, BCM or an affiliate of BCM is separately compensated for such additional services on terms to be agreed upon from time to time. As discussed below, under "Property Management", the Company has hired Carmel Realty Services, Ltd. ("Carmel, Ltd."), an affiliate of BCM, to provide property management services for the Company's properties. Also as discussed below, under "Real Estate Brokerage" the Company has engaged, on a non-exclusive basis, Carmel Realty, also an affiliate of BCM, to perform brokerage services for the Company.

BCM may only assign the Advisory Agreement with the prior consent of the Company.

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The directors and principal officers of BCM are set forth below.

<TABLE>

<C>	<S>
Mickey N. Phillips:	Director
Ryan T. Phillips:	Director
Randall M. Paulson:	President
Karl L. Blaha:	Executive Vice President--Commercial Asset Management
Bruce A. Endendyk:	Executive Vice President
Thomas A. Holland:	Executive Vice President and Chief Financial Officer
A. Cal Rossi, Jr.:	Executive Vice President
Cooper B. Stuart:	Executive Vice President
Clifford C. Towns, Jr.:	Executive Vice President--Finance
Dan S. Allred:	Senior Vice President--Land Division
James D. Canon, III:	Senior Vice President--Portfolio Manager
Robert A. Waldman:	Senior Vice President, Secretary and General Counsel
Drew D. Potera:	Vice President, Treasurer and Securities Manager

</TABLE>

Mickey N. Phillips is Gene E. Phillips' brother and Ryan T. Phillips is Gene E. Phillips' son. Gene E. Phillips serves as a representative of the trust established for the benefit of his children which owns BCM and, in such capacity, has substantial contact with the management of BCM and input with respect to BCM's performance of advisory services to the Company.

#### Property Management

Since February 1, 1990, affiliates of BCM have provided property management services to the Company. Currently, Carmel, Ltd. provides such property management services for a fee of 5% or less of the monthly gross rents collected on the properties under its management. Carmel, Ltd. subcontracts with other entities for the provision of the property-level management services to the Company at various rates. The general partner of Carmel, Ltd. is BCM. The limited partners of Carmel, Ltd. are (1) First Equity, which is 50% owned by a subsidiary of BCM, (2) Gene E. Phillips and (3) a trust for the benefit of the children of Mr. Phillips. Carmel, Ltd. subcontracts the property-level management and leasing of 29 of the Company's commercial properties and its four hotels and the commercial properties owned by a real estate partnership in which the Company and IORI are partners to Carmel Realty, which is a company owned by First Equity. Carmel Realty is entitled to receive property and construction management fees and leasing commissions in accordance with the terms of its property-level management agreement with



## Real Estate Brokerage

Since December 1, 1992, Carmel Realty has been engaged, on a non-exclusive basis, to provide brokerage services for the Company. Carmel Realty is entitled to receive a real estate commission for property purchases and sales in accordance with the following sliding scale of total fees to be paid: (1) maximum fee of 5% on the first \$2.0 million of any purchase or sale transaction of which no more than 4% would be paid to Carmel Realty or affiliates; (2) maximum fee of 4% on transaction amounts between \$2.0 million--\$5.0 million of which no more than 3% would be paid to Carmel Realty or affiliates; (3) maximum fee of 3% on transaction amounts between \$5.0 million--\$10.0 million of which no more than 2% would be paid to Carmel Realty or affiliates; and (4) maximum fee of 2% on transaction amounts in excess of \$10.0 million of which no more than 1.5% would be paid to Carmel Realty or affiliates.

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## ITEM 11. EXECUTIVE COMPENSATION

The Company has no employees, payroll or benefit plans and pays no compensation to its executive officers. The executive officers of the Company, who are also officers or employees of BCM, the Company's Advisor, are compensated by the Advisor. Such executive officers perform a variety of services for the Advisor and the amount of their compensation is determined solely by the Advisor. BCM does not allocate the cash compensation of its officers among the various entities for which it serves as advisor. See ITEM 10. "DIRECTORS, EXECUTIVE OFFICERS AND ADVISOR OF THE REGISTRANT--The Advisor" for a more detailed discussion of the compensation payable to BCM by the Company.

The only remuneration paid by the Company is to the Directors who are not officers or directors of BCM or its affiliated companies. The Independent Directors (1) review the investment policies of the Company to determine that they are in the best interest of stockholders, (2) review the advisory contract, (3) supervise the performance of the advisor and review the reasonableness of the compensation paid to the advisor in terms of the nature and quality of services performed, (4) review the reasonableness of the total fees and expenses of the Company and (5) select, when necessary, a qualified independent real estate appraiser to appraise properties purchased.

Each Independent Director receives compensation in the amount of \$15,000 per year, plus reimbursement for expenses and the Chairman of the Board receives an additional \$1,500 per year for serving in such position. In addition, each Independent Director receives an additional fee of \$1,000 per day for any special services rendered by him to the Company outside of his ordinary duties as Director, plus reimbursement of expenses.

During 1998, \$116,000 was paid to the Independent Directors in total Directors' fees for all services, including the annual fee for service during the period January 1, 1998 through December 31, 1998, and 1998 special service fees as follows: Richard W. Douglas, \$15,000; Larry E. Harley, \$15,000; R. Douglas Leonhard, \$15,000; Murray Shaw, \$13,750; Ted P. Stokely, \$16,500; Edward L. Tixier, \$3,750; Martin L. White, \$15,000; and Edward G. Zampa, \$22,000.

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## PERFORMANCE GRAPH

The following performance graph compares the cumulative total stockholder return on the Company's shares of Common Stock with the Standard & Poor's 500 Stock Index ("S&P 500 Index") and the National Association of Real Estate Investment Trusts, Inc. Hybrid REIT Total Return Index ("REIT Index"). The comparison assumes that \$100 was invested on December 31, 1993 in the Company's shares of Common Stock and in each of the indices and further assumes the reinvestment of all distributions. Past performance is not necessarily an indicator of future performance.

[GRAPH APPEARS HERE]

<TABLE>  
<CAPTION>

	1993	1994	1995	1996	1997	1998
<S>	<C>	<C>	<C>	<C>	<C>	<C>
The Company	100.00	110.19	111.890	126.48	188.82	166.28
S&P 500 Index	100.00	101.31	139.22	171.19	228.29	293.54
REIT Index	100.00	104.00	127.91	165.45	183.24	120.88

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

Security Ownership of Certain Beneficial Owners. The following table sets forth the ownership of the Company's Common Stock, both beneficially and of record, both individually and in the aggregate, for those persons or entities known to be beneficial owners of more than 5% of the outstanding shares of Common Stock as of the close of business on March 5, 1999.

<TABLE>

<CAPTION>

NAME AND ADDRESS OF BENEFICIAL OWNER	AMOUNT AND NATURE OF BENEFICIAL OWNERSHIP	PERCENT OF CLASS (/1/)
<S>	<C>	<C>
American Realty Trust, Inc. 10670 N. Central Expressway Suite 300 Dallas, Texas 75231	1,204,470	31.1%
Basic Capital Management, Inc. 10670 N. Central Expressway Suite 300 Dallas, Texas 75231	422,057	10.9%
Maurice A. Halperin 2500 North Military Trail Suite 225 Boca Raton, Florida 33431	326,450	8.4%

</TABLE>

(1) Percentage is based upon 3,878,463 shares of Common Stock outstanding at March 5, 1999.

Security Ownership of Management. The following table sets forth the ownership of the Company's Common Stock, both beneficially and of record, both individually and in the aggregate, for the Directors and executive officers of the Company as of the close of business on March 5, 1999.

<TABLE>

<CAPTION>

NAME OF BENEFICIAL OWNER	AMOUNT AND NATURE OF BENEFICIAL OWNERSHIP	PERCENT OF CLASS (/1/)
<S>	<C>	<C>
All Directors and Executive Officers as a group (12 individuals)	1,734,270 (/2/) (/3/)	44.7%

</TABLE>

(1) Percentage is based upon 3,878,463 shares of Common Stock outstanding at March 5, 1999.

(2) Includes 80,268 shares owned by CMET of which the Directors may be deemed to be beneficial owners by virtue of their positions as trustees of CMET. The Directors of the Company disclaim beneficial ownership of such shares. Also includes 1,000 shares owned directly by Ted P. Stokely.

(3) Includes 26,475 shares owned by SAMLPL, 422,057 shares owned by BCM and 1,204,470 shares owned by ART, of which the executive officers of the Company may be deemed to be beneficial owners by virtue of their positions as executive officers or directors of SAMI, BCM and ART. The executive officers of the Company disclaim beneficial ownership of such shares. Each of the directors of ART may be deemed to be beneficial owners of the shares owned by ART by virtue of their positions as directors of ART. Each of the directors of BCM may be deemed to be beneficial owners by virtue of their positions as directors of BCM. The directors of ART and BCM disclaim such beneficial ownership.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Certain Business Relationships

In February 1989, the Board of Directors voted to retain BCM as the Company's advisor. See ITEM 10. "DIRECTORS, EXECUTIVE OFFICERS AND ADVISOR TO THE REGISTRANT--The Advisor." BCM is a corporation of which Messrs. Paulson,

Blaha, Endendyk, Holland and Johnson serve as executive officers. Gene E. Phillips served as a director of BCM until December 22, 1989 and as Chief Executive Officer of BCM until September 1, 1992. BCM is owned by a trust for the benefit of the children of Mr. Phillips. Mr. Phillips serves as a representative of his children's trust which owns BCM and, in such capacity, has substantial contact with the management of BCM and input with respect to BCM's performance of advisory services to the Company.

Since February 1, 1991, affiliates of BCM have provided property management services to the Company. Currently, Carmel, Ltd. provides such property management services. The general partner of Carmel, Ltd. is BCM. The limited partners of Carmel, Ltd. are (1) First Equity, which is 50% owned by a subsidiary of BCM, (2) Mr. Phillips and (3) a trust for the benefit of the children of Mr. Phillips. Carmel, Ltd. subcontracts the property-level management and leasing of 29 of the Company's commercial properties and its four hotels and the commercial properties owned by a real estate partnership in which the Company and IORI are partners to Carmel Realty, which is a company owned by First Equity.

Prior to December 1, 1992, affiliates of BCM provided brokerage services for the Company and received brokerage commissions in accordance with the advisory agreement. Since December 1, 1992, the Company has engaged, on a non-exclusive basis, Carmel Realty to perform brokerage services. Carmel Realty is a company owned by First Equity.

The Directors and officers of the Company also serve as trustees or directors and officers of CMET and IORI. The Directors owe fiduciary duties to such entities as well as to the Company under applicable law. CMET and IORI have the same relationship with BCM as the Company. The Company owned approximately 22.7% of the outstanding shares of common stock of IORI at December 31, 1998. BCM also serves as advisor to ART. Messrs. Paulson, Blaha, Endendyk, Holland and Johnson serve as executive officers of ART and NMC. NMC, a wholly-owned subsidiary of ART, is the general partner of NRLP and NOLP. BCM performs certain administrative functions for NRLP and NOLP on a cost-reimbursement basis.

From April 1992 to December 31, 1992, Mr. Stokely was employed as a paid Consultant and since January 1, 1993 as a part-time unpaid Consultant for Eldercare, a nonprofit corporation engaged in the acquisition of low income and elderly housing. Eldercare has a revolving loan commitment from Syntek West, Inc., of which Mr. Phillips is the sole shareholder. Eldercare filed for bankruptcy protection in July 1993, and was dismissed from bankruptcy in October 1994. Eldercare again filed for bankruptcy protection in May 1995, and was reorganized in bankruptcy in February 1996, and has since paid all debts as directed by the Bankruptcy Court.

#### Related Party Transactions

Historically, the Company has engaged in and may continue to engage in business transactions, including real estate partnerships, with related parties. Management believes that all of the related party transactions represented the best investments available at the time and were at least as advantageous to the Company as could have been obtained from unrelated third parties.

As more fully described in ITEM 2. "PROPERTIES--Real Estate," the Company is a partner with IORI in the Tri-City Limited Partnership and Nakash Income Associates. The Company owns 345,728 shares of the common stock of IORI, an approximate 22.7% interest.

In 1998, the Company paid BCM and its affiliates \$4.1 million in advisory and net income fees, \$341,000 in mortgage brokerage and equity refinancing fees, \$3.5 million in property acquisition fees, \$767,000 in real estate brokerage commissions and \$2.8 million in property and construction management fees and leasing

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commissions, net of property management fees paid to subcontractors, other than Carmel Realty. In addition, as provided in the Advisory Agreement, BCM received cost reimbursements of \$1.1 million in 1998.

#### Restrictions on Related Party Transactions

Article FOURTEENTH of the Company's Articles of Incorporation provides that the Company shall not, directly or indirectly, contract or engage in any transaction with (1) any director, officer or employee of the Company, (2) any director, officer or employee of the advisor, (3) the advisor or (4) any affiliate or associate (as such terms are defined in Rule 12b-2 under the Securities Exchange Act of 1934, as amended) of any of the aforementioned persons, unless (a) the material facts as to the relationship among or financial interest of the relevant individuals or persons and as to the contract or transaction are disclosed to or are known by the Board of

Directors or the appropriate committee thereof and (b) the Board of Directors or committee thereof determines that such contract or transaction is fair to the Company and simultaneously authorizes or ratifies such contract or transaction by the affirmative vote of a majority of independent directors of the Company entitled to vote thereon.

Pursuant to the terms of the Modification of Stipulation of Settlement (the "Olive Modification") in the Olive Litigation, as more fully discussed in ITEM 3. "LEGAL PROCEEDINGS--Olive Litigation," which became effective on January 11, 1995, certain related party transactions which the Company may enter into prior to April 28, 1999, require the unanimous approval of the Board of Directors. In addition, such related party transactions are to be discouraged and may only be entered into in exceptional circumstances and after a determination by the Board of Directors that the transaction is in the best interests of the Company and that no other opportunity exists that is as good as the opportunity presented by such transaction.

The Olive Modification requirements for related party transactions do not apply to direct contractual agreements for services between the Company and the Advisor or one of its affiliates (including the Advisory Agreement, the Brokerage Agreement and the property management contracts). These agreements, pursuant to the specific terms of the Olive Modification, require the prior approval by two-thirds of the Directors of the Company, and if required, approval by a majority of stockholders. The Olive Modification requirements for related party transactions also do not apply to joint ventures between or among the Company and CMET, IORI or NIRT or any of their affiliates or subsidiaries and a third party having no prior or intended future business or financial relationship with Gene E. Phillips, William S. Friedman, the Advisor, or any affiliate of such parties. Such joint ventures may be entered into on the affirmative vote of a majority of the Directors of the Company.

An Amendment to the Olive Modification (the "Olive Amendment") was approved by the Court on July 3, 1997. The Olive Amendment requires that additional requirements be met for certain transactions with affiliates ("Affiliated Transaction") prior to April 28, 1999. Independent counsel to the Board must review, advise and report to the Board of Directors on any Affiliated Transaction prior to its consideration and approval by the Board of Directors and the Board of Directors must unanimously approve the transaction after receiving independent counsel's advice and report. In addition, a notice must be given to the plaintiffs' counsel at least 10 days prior to the closing of the transaction and during such 10 day period plaintiffs' counsel is entitled to seek a Court order prohibiting consummation of the transaction. Neither BCM nor any of its affiliates may receive any fees or commissions in connection with an Affiliated Transaction.

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#### ITEM 14. EXHIBITS, FINANCIAL STATEMENTS, SCHEDULES, AND REPORTS ON FORM 8-K

(a) The following documents are filed as part of this Report:

1. Consolidated Financial Statements

Report of Independent Certified Public Accountants

Consolidated Balance Sheets--December 31, 1998 and 1997

Consolidated Statements of Operations--Years Ended December 31, 1998, 1997 and 1996

Consolidated Statements of Stockholders' Equity--Years Ended December 31, 1998, 1997 and 1996

Consolidated Statements of Cash Flows--Years Ended December 31, 1998, 1997 and 1996

Notes to Consolidated Financial Statements

2. Financial Statement Schedules

Schedule III--Real Estate and Accumulated Depreciation

Schedule IV--Mortgage Loans on Real Estate

All other schedules are omitted because they are not applicable or because the required information is shown in the Consolidated Financial Statements or the Notes thereto.

3. Incorporated Financial Statements

Consolidated Financial Statements of Income Opportunity Realty Investors, Inc. (incorporated by reference to Item 8 of Income Opportunity Realty Investors, Inc.'s Annual Report on Form 10-K for the

4. Exhibits

The following documents are filed as Exhibits to this Report:

<TABLE>

<CAPTION>

Exhibit Number -----	Description -----
<C>	<S>
3.0	Articles of Incorporation of Transcontinental Realty Investors, Inc., as filed on December 20, 1991 (incorporated by reference to Exhibit No. 3.1 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1991).
3.1	Certificate of Amendment to the Articles of Incorporation of Transcontinental Realty Investors, Inc., as filed on June 3, 1996 (incorporated by reference to the Registrant's Current Report on Form 8-K, dated June 3, 1996).
3.2	By-Laws of Transcontinental Realty Investors, Inc. (incorporated by reference to Exhibit No. 3.2 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1991).
3.3	Articles of Amendment to the Articles of Incorporation of Transcontinental Realty Investors, Inc., setting forth the Certificate of Designations, Preferences and Rights of Series A Cumulative Convertible Preferred Stock, dated October 20, 1998 (incorporated by reference to Exhibit 3.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 1998).
10.0	Advisory Agreement dated as of March 7, 1995, between Transcontinental Realty Investors, Inc. and Basic Capital Management, Inc. (incorporated by reference to Exhibit 10.2 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1994).
10.1	Advisory Agreement dated as of October 15, 1998, between Transcontinental Realty Investors, Inc. and Basic Capital Management, Inc. (incorporated by reference to Exhibit 10.0 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 1998).
27.0	Financial Data Schedule, filed herewith.

</TABLE>

(b) Reports on Form 8-K:

A Current Report on Form 8-K, dated October 20, 1998, was filed with respect to Item 2. "Acquisition or Disposition of Assets," and Item 7. "Financial Statements and Exhibits," which reports the acquisition of the Cliffs of Eldorado Apartments, filed December 4, 1998.

A Current Report on Form 8-K, dated December 2, 1998, was filed with respect to Item 2. "Acquisition or Disposition of Assets," and Item 7. "Financial Statements and Exhibits," which reports the acquisition of Southgreen Apartments, Belmont Hotel, Brompton Hotel and Surf Hotel, filed February 18, 1999.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Transcontinental Realty Investors,  
Inc.

/s/ Randall M. Paulson

By: \_\_\_\_\_  
Randall M. Paulson  
President

Dated: March 26, 1999

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the date indicated.

<TABLE>

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Signature -----	Title -----	Date ----
<S> /s/ Ted P. Stokely ----- Ted P. Stokely	<C> Chairman of the Board and Director	<C> March 26, 1999
/s/ Richard W. Douglas ----- Richard W. Douglas	Director	March 26, 1999
Larry E. Harley	Director	
/s/ R. Douglas Leonhard ----- R. Douglas Leonhard	Director	March 26, 1999
/s/ Murray Shaw ----- Murray Shaw	Director	March 26, 1999
/s/ Martin L. White ----- Martin L. White	Director	March 26, 1999
/s/ Edward G. Zampa ----- Edward G. Zampa	Director	March 26, 1999
/s/ Thomas A. Holland ----- Thomas A. Holland	Executive Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)	March 26, 1999

</TABLE>

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TRANSCONTINENTAL REALTY INVESTORS, INC.

EXHIBITS TO  
ANNUAL REPORT ON FORM 10-K

For the Year Ended December 31, 1998

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Exhibit Number -----	Description -----	Page ----
<S> 27.0	<C> Financial Data Schedule.	<C>

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