

HIGHLAND CAPITAL
M A N A G E M E N T

Highland Funds I

Highland Long/Short Equity Fund
Highland Long/Short Healthcare Fund
Highland Merger Arbitrage Fund
Highland Opportunistic Credit Fund

Semi-Annual Report
December 31, 2018

Highland Funds I

**Highland Long/Short Equity Fund
Highland Long/Short Healthcare Fund
Highland Merger Arbitrage Fund
Highland Opportunistic Credit Fund**

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Economic and market conditions change frequently.
There is no assurance that the trends described in this report will continue or commence.

A prospectus must precede or accompany this report. Please read the prospectus carefully before you invest.

FUND PROFILE (unaudited)

Highland Long/Short Equity Fund

Objective

Highland Long/Short Equity Fund seeks consistent, above average total returns primarily through capital appreciation, while also attempting to preserve capital and mitigate risk through hedging activities.

Net Assets as of December 31, 2018

\$236.4 million

Portfolio Data as of December 31, 2018

The information below provides a snapshot of Highland Long/Short Equity Fund at the end of the reporting period. Highland Long/Short Equity Fund is actively managed and the composition of its portfolio will change over time. Current and future holdings are subject to risk.

| Sectors as of 12/31/2018 (%) ⁽¹⁾ | Long Exposure | Short Exposure | Net Exposure |
|---|---------------|----------------|--------------|
| Communication Services | 7.0 | (1.6) | 5.4 |
| Consumer Discretionary | 8.5 | (1.0) | 7.5 |
| Energy | 2.5 | — | 2.5 |
| Financial | 10.5 | (1.6) | 8.9 |
| Healthcare | 12.9 | (0.5) | 12.4 |
| Industrials | 9.3 | (6.5) | 2.8 |
| Information Technology | 38.9 | (18.1) | 20.8 |
| Materials | 1.8 | — | 1.8 |
| Real Estate | 4.4 | — | 4.4 |
| Other Investments and Assets & Liabilities ⁽²⁾ | 42.6 | (9.1) | 33.5 |

Top 5 Holdings as of 12/31/2018 (%)⁽¹⁾ Long Securities

| | |
|--------------------|-----|
| Visa, Inc. | 4.2 |
| Alphabet, Inc. | 3.5 |
| SBA Communications | 3.4 |
| CDK Global, Inc. | 3.4 |
| Broadcom, Inc. | 3.3 |

Short Securities

| | |
|----------------------------|-------|
| iShares S&P 500 Growth ETF | (4.8) |
| CSX Corp. | (2.4) |
| Fastenal | (2.2) |
| Texas Instruments, Inc. | (2.2) |
| Paychex, Inc. | (2.2) |

⁽¹⁾ Sectors and holdings are calculated as a percentage of total net assets.

⁽²⁾ Includes the Fund's investment in an investment company purchased with cash collateral from securities lending.

FUND PROFILE (unaudited)

Highland Long/Short Healthcare Fund

Objective

Highland Long/Short Healthcare Fund seeks long-term capital appreciation.

Net Assets as of December 31, 2018

\$48.1 million

Portfolio Data as of December 31, 2018

The information below provides a snapshot of Highland Long/Short Healthcare Fund at the end of the reporting period. Highland Long/Short Healthcare Fund is actively managed and the composition of its portfolio will change over time. Current and future holdings are subject to risk.

| Sectors as of 12/31/2018 (%) ⁽¹⁾ | Long Exposure | Short Exposure | Net Exposure |
|---|---------------|----------------|--------------|
| Healthcare: | | | |
| Biotechnology | 27.9 | (2.7) | 25.2 |
| Healthcare Equipment | 1.8 | — | 1.8 |
| Healthcare Facilities | 1.1 | — | 1.1 |
| Healthcare Services | 7.0 | (0.4) | 6.6 |
| Healthcare Technology | 1.4 | — | 1.4 |
| Life Sciences Tools & Services | 6.5 | (0.8) | 5.7 |
| Managed Healthcare | 1.8 | — | 1.8 |
| Pharmaceuticals | 19.1 | (3.6) | 15.5 |
| Other Investments and Assets & Liabilities ⁽²⁾ | 40.9 | — | 40.9 |

Top 5 Holdings as of 12/31/2018 (%)⁽¹⁾⁽³⁾ Long Securities

| | |
|-----------------------------|-----|
| Minerva Neurosciences, Inc. | 7.9 |
| HLS Therapeutics, Inc. | 7.4 |
| Bio-Rad Laboratories, Inc. | 5.3 |
| Shire PLC | 5.2 |
| AMINO, Inc. | 5.1 |

Short Securities

| | |
|------------------------|-------|
| Roche Holding AG, Inc. | (1.6) |
| Incyte | (1.3) |
| WaVe Life Sciences | (0.8) |
| Cambrex | (0.8) |
| Eli Lilly | (0.6) |

⁽¹⁾Sectors and holdings are calculated as a percentage of total net assets.

⁽²⁾Includes the Fund's investment in an investment company purchased with cash collateral from securities lending and cash equivalent investments.

⁽³⁾Excludes the Fund's investment in cash equivalent investments.

FUND PROFILE (unaudited)

Highland Merger Arbitrage Fund

Objective

Highland Merger Arbitrage Fund seeks to generate positive absolute returns.

Net Assets as of December 31, 2018

\$26.8 million

Portfolio Data as of December 31, 2018

The information below provides a snapshot of Highland Merger Arbitrage Fund at the end of the reporting period. Highland Merger Arbitrage Fund is actively managed and the composition of its portfolio will change over time. Current and future holdings are subject to risk.

| Sectors as of 12/31/2018 (%) ⁽¹⁾ | Long Exposure | Short Exposure | Net Exposure |
|---|---------------|----------------|--------------|
| Consumer Discretionary | 10.5 | — | 10.5 |
| Energy | 0.2 | (0.2) | — |
| Financial | 5.0 | (6.0) | (1.0) |
| Healthcare | 11.3 | (0.7) | 10.6 |
| Industrials | 4.4 | — | 4.4 |
| Information Technology | 15.4 | (11.2) | 4.2 |
| Real Estate | 0.6 | (0.6) | — |
| Utilities | 7.2 | (9.7) | (2.5) |
| Other Investments and Assets & Liabilities ⁽²⁾ | 76.3 | (2.5) | 73.8 |

Top 5 Holdings as of 12/31/2018 (%)⁽¹⁾⁽³⁾ Long Securities

| | |
|---------------------------|------|
| Valero Energy Partners LP | 12.7 |
| SendGrid, Inc. | 9.6 |
| Nutrisystem, Inc. | 5.8 |
| athenahealth, Inc. | 5.5 |
| SCANA Corp. | 5.2 |

Short Securities

| | |
|--------------------------------|-------|
| Dominion Energy, Inc. | (9.7) |
| Twilio, Inc. | (9.6) |
| Western Gas Equity Partners LP | (2.5) |
| First Merchants Corp. | (2.2) |
| Berkshire Hills Bancorp, Inc. | (1.4) |

⁽¹⁾ Sectors and holdings are calculated as a percentage of total net assets.

⁽²⁾ Includes the Fund's investment in cash equivalent investments.

⁽³⁾ Excludes the Fund's investment in cash equivalent investments.

FUND PROFILE (unaudited)

Highland Opportunistic Credit Fund

Objective

Highland Opportunistic Credit Fund seeks to achieve high total returns while attempting to minimize losses.

Net Assets as of December 31, 2018

\$48.2 million

Portfolio Data as of December 31, 2018

The information below provides a snapshot of Highland Opportunistic Credit Fund at the end of the reporting period. Highland Opportunistic Credit Fund is actively managed and the composition of its portfolio will change over time. Current and future holdings are subject to risk.

| Quality Breakdown as of 12/31/2018 (%) ⁽¹⁾ | |
|---|------|
| BB | 8.7 |
| B | 35.3 |
| CCC | 32.2 |
| C | 0.7 |
| NR | 23.1 |

| Top 5 Sectors as of 12/31/2018 (%) ⁽²⁾⁽³⁾ | |
|--|---------------------|
| Utilities | 10.7 |
| Financial | 10.6 ⁽⁴⁾ |
| Materials | 9.6 |
| Retail | 8.2 |
| Energy | 7.4 |

| Top 10 Holdings as of 12/31/2018 (%) ⁽²⁾⁽³⁾ | |
|---|-----|
| MPM Holdings, Inc. (Common Stocks) | 6.9 |
| Fieldwood Energy LLC, Closing Date Loan, 2nd Lien, LIBOR USD 1 Month+7.250%, 4/11/2023 (U.S. Senior Loans) | 6.8 |
| Vistra Energy Corp. (Common Stocks) | 6.8 |
| Ditech Holding Corporation (fka Walter Investment Management Corp.), Tranche B Term Loan, LIBOR USD 3 Month+6.000%, 6/30/2022 (U.S. Senior Loans) | 4.0 |
| Toys 'R' Us-Delaware, Inc., Term Loan B-4 (U.S. Senior Loans) | 3.8 |
| iHeartCommunications, Inc. Tranche D Term Loan (U.S. Senior Loans) | 3.5 |
| Academy, Ltd., Initial Term Loan, LIBOR USD 3 Month+4.000%, 7/1/2022 (U.S. Senior Loans) | 3.4 |
| Granite Acquisition, Inc., Term Loan B, 2nd Lien, LIBOR USD 3 Month+7.250%, 12/19/2022 (U.S. Senior Loans) | 3.3 |
| Advantage Sales & Marketing Inc., Term Loan, 2nd Lien, LIBOR USD 1 Month+6.500%, 7/25/2022 (U.S. Senior Loans) | 3.3 |
| TerreStar Corporation (Common Stocks) | 2.9 |

⁽¹⁾Quality is calculated as a percentage of total bonds & notes. Sectors and holdings are calculated as a percentage of total net assets. The quality ratings reflected were issued by Standard & Poors, a nationally recognized statistical rating organization. Ratings are measured on a scale that generally ranges from AAA (highest) to D (lowest). Quality ratings reflect the credit quality of the underlying bonds in the Fund's portfolio and not that of the Fund itself. Quality Ratings are subject to change.

⁽²⁾Sectors and holdings are calculated as a percentage of total net assets.

⁽³⁾Excludes the Fund's investment in an investment company purchased with cash collateral from securities lending and cash equivalent investments.

⁽⁴⁾Includes Collateralized Loan Obligations

FINANCIAL STATEMENTS

December 31, 2018

A guide to understanding each Fund's financial statements

| | |
|--|--|
| Investment Portfolio | The Investment Portfolio details each of the Fund's holdings and their market value as of the last day of the reporting period. Portfolio holdings are organized by type of asset and industry to demonstrate areas of concentration and diversification. |
| Statement of Assets and Liabilities | This statement details each Fund's assets, liabilities, net assets and share price for each share class as of the last day of the reporting period. Net assets are calculated by subtracting all of a Fund's liabilities (including any unpaid expenses) from the total of the Fund's investment and noninvestment assets. The net asset value per share for each class is calculated by dividing net assets allocated to that share class by the number of shares outstanding in that class as of the last day of the reporting period. |
| Statement of Operations | This statement reports income earned by each Fund and the expenses incurred by each Fund during the reporting period. The Statement of Operations also shows any net gain or loss a Fund realized on the sales of its holdings during the period as well as any unrealized gains or losses recognized over the period. The total of these results represents a Fund's net increase or decrease in net assets from operations. |
| Statement of Changes in Net Assets | This statement details how each Fund's net assets were affected by its operating results, distributions to shareholders and shareholder transactions (e.g., subscriptions, redemptions and distribution reinvestments) during the reporting period. The Statement of Changes in Net Assets also details changes in the number of shares outstanding. |
| Statement of Cash Flows | This statement reports net cash and foreign currency provided or used by operating, investing and financing activities and the net effect of those flows on cash and foreign currency during the period. |
| Financial Highlights | The Financial Highlights demonstrate how each Fund's net asset value per share was affected by the Fund's operating results. The Financial Highlights also disclose the classes' performance and certain key ratios (e.g., net expenses and net investment income as a percentage of average net assets). |
| Notes to Financial Statements | These notes disclose the organizational background of the Funds, certain of their significant accounting policies (including those surrounding security valuation, income recognition and distributions to shareholders), federal tax information, fees and compensation paid to affiliates and significant risks and contingencies. |

INVESTMENT PORTFOLIO (unaudited)

As of December 31, 2018

Highland Long/Short Equity Fund

| Shares | Value (\$) | |
|---------------------------------------|--|-------------------|
| Common Stocks - 95.8% | | |
| COMMUNICATION SERVICES - 7.0% | | |
| 8,000 | Alphabet, Inc., Class A (a)(b) | 8,359,680 |
| 42,000 | Facebook, Inc., Class A (a)(b) | 5,505,780 |
| 54,000 | Live Nation Entertainment (a)(b) | 2,659,500 |
| | | <u>16,524,960</u> |
| CONSUMER DISCRETIONARY - 8.5% | | |
| 20,000 | Alibaba Group Holding ADR (b) | 2,741,400 |
| 4,000 | Amazon.com, Inc. (a)(b) | 6,007,880 |
| 6,000 | AutoZone (b) | 5,030,040 |
| 27,000 | Expedia Group | 3,041,550 |
| 82,000 | Penske Automotive Group | 3,306,240 |
| | | <u>20,127,110</u> |
| ENERGY - 2.5% | | |
| 70,000 | Continental Resources, Inc. (a)(b) | 2,813,300 |
| 23,000 | Pioneer Natural Resources | 3,024,960 |
| | | <u>5,838,260</u> |
| FINANCIAL - 10.5% | | |
| 20,000 | Ameriprise Financial, Inc. | 2,087,400 |
| 129,000 | CIT Group, Inc. (a) | 4,936,830 |
| 30,000 | CME Group, Inc., Class A (a) | 5,643,600 |
| 14,000 | Diamond Hill Investment Group | 2,092,300 |
| 113,000 | E*TRADE Financial Corp. (a) | 4,958,440 |
| 55,000 | US Bancorp | 2,513,500 |
| 63,000 | Western Alliance Bancorp (b) | 2,487,870 |
| | | <u>24,719,940</u> |
| HEALTHCARE - 12.9% | | |
| 35,000 | Abbott Laboratories (a) | 2,531,550 |
| 80,000 | Aerie Pharmaceuticals, Inc. (b)(c) | 2,888,000 |
| 10,000 | Anthem, Inc. (a) | 2,626,300 |
| 20,000 | Bio-Rad Laboratories, Inc., Class A (a)(b) | 4,644,400 |
| 65,000 | CryoLife, Inc. (b) | 1,844,700 |
| 120,000 | Heron Therapeutics, Inc. (b)(c) | 3,112,800 |
| 6,500 | Intuitive Surgical, Inc. (b) | 3,112,980 |
| 127,000 | La Jolla Pharmaceutical (b)(c) | 1,197,610 |
| 30,000 | LHC Group, Inc. (a)(b) | 2,816,400 |
| 160,000 | Portola Pharmaceuticals, Inc. (b)(c) | 3,123,200 |
| 260,000 | Surgery Partners, Inc. (b)(c) | 2,545,400 |
| | | <u>30,443,340</u> |
| INDUSTRIALS - 9.3% | | |
| 125,000 | JetBlue Airways Corp. (b) | 2,007,500 |
| 40,000 | Middleby (a)(b) | 4,109,200 |
| 1 | Pendrell Corp. (b) | 150,000 |
| 25,000 | Roper Technologies, Inc. (a) | 6,663,000 |
| 30,000 | United Rentals (b) | 3,075,900 |
| 67,500 | Waste Management, Inc. (a) | 6,006,825 |
| | | <u>22,012,425</u> |
| INFORMATION TECHNOLOGY - 38.9% | | |
| 38,000 | Automatic Data Processing (a) | 4,982,560 |
| 250,000 | Avaya Holdings Corp. (b)(c) | 3,640,000 |
| 31,000 | Broadcom, Inc. (a) | 7,882,680 |
| 169,000 | CDK Global, Inc. (a) | 8,091,720 |
| 150,000 | Ciena Corp. (b) | 5,086,500 |

| Shares | Value (\$) | |
|---|---|---------------------|
| INFORMATION TECHNOLOGY (continued) | | |
| 50,000 | Cornerstone OnDemand, Inc. (b) | 2,521,500 |
| 37,000 | EPAM Systems (a)(b) | 4,292,370 |
| 35,000 | Fortinet, Inc. (b) | 2,465,050 |
| 65,000 | Intel Corp. | 3,050,450 |
| 47,000 | Lumentum Holdings, Inc. (b) | 1,974,470 |
| 250,000 | Marvell Technology Group | 4,047,500 |
| 67,000 | Mellanox Technologies (b) | 6,189,460 |
| 48,000 | Microsoft Corp. (a) | 4,875,360 |
| 60,000 | Nutanix, Class A (b)(c) | 2,495,400 |
| 25,000 | Palo Alto Networks, Inc. (a)(b) | 4,708,750 |
| 240,000 | Sage Group | 1,839,213 |
| 30,000 | salesforce.com, Inc. (a)(b) | 4,109,100 |
| 25,000 | ServiceNow (a)(b) | 4,451,250 |
| 20,000 | Shopify, Class A (b)(c) | 2,769,000 |
| 75,000 | Visa, Inc., Class A (a) | 9,895,500 |
| 30,000 | Xilinx | 2,555,100 |
| | | <u>91,922,933</u> |
| MATERIALS - 1.8% | | |
| 11,000 | Sherwin-Williams Co/The (a) | 4,328,060 |
| REAL ESTATE - 4.4% | | |
| 297,279 | Newmark Group, Inc., Class A (a) | 2,384,178 |
| 50,000 | SBA Communications, REIT, Class A (b) | 8,094,500 |
| | | <u>10,478,678</u> |
| | Total Common Stocks (Cost \$239,677,687) | <u>226,395,706</u> |
| Registered Investment Companies - 4.7% | | |
| 374,333 | Highland Merger Arbitrage Fund, Class Z (d) | 6,797,881 |
| 4,387,313 | State Street Navigator Securities Lending Government Money Market Portfolio, 2.350% (e) | 4,387,313 |
| | Total Registered Investment Companies (Cost \$11,895,136) | <u>11,185,194</u> |
| Contracts | | |
| | Purchased Put Options (b) - 0.3% | |
| | Total Purchased Put Options (Cost \$1,360,211) | <u>721,500</u> |
| | Total Investments - 100.8% | <u>238,302,400</u> |
| | (Cost \$252,933,034) | |
| Shares | | |
| Securities Sold Short - (38.4%) | | |
| EXCHANGE-TRADED FUNDS - (9.1%) | | |
| (58,000) | Health Care Select Sector SPDR Fund ETF .. | (5,017,580) |
| (75,000) | iShares S&P 500 Growth ETF | (11,300,250) |
| (71,000) | SPDR S&P Biotech ETF | (5,094,250) |
| | Total Exchange-Traded Funds (Proceeds \$22,147,385) | <u>(21,412,080)</u> |

INVESTMENT PORTFOLIO (unaudited) (continued)

As of December 31, 2018

Highland Long/Short Equity Fund

| Shares | Value (\$) |
|--|---------------------|
| Securities Sold Short (continued) | |
| COMMON STOCKS - (29.3)% | |
| Communication Services - (1.6)% | |
| (7,000) IAC Corp. (f) | (1,281,280) |
| (22,000) TripAdvisor (f) | (1,186,680) |
| (43,000) Twitter (f) | (1,235,820) |
| | <u>(3,703,780)</u> |
| Consumer Discretionary - (1.0)% | |
| (87,000) eBay, Inc. (f) | (2,442,090) |
| Financial - (1.6)% | |
| (77,000) Ares Management Corp. | (1,369,060) |
| (24,000) Interactive Brokers Group, Class A | (1,311,600) |
| (77,000) Regions Financial | (1,030,260) |
| | <u>(3,710,920)</u> |
| Healthcare - (0.5)% | |
| (75,000) Tenet Healthcare, Inc. (f) | (1,285,500) |
| Industrials - (6.5)% | |
| (92,000) CSX Corp. | (5,715,960) |
| (100,000) Fastenal | (5,229,000) |
| (44,500) Republic Services, Class A | (3,208,005) |
| (28,000) Sensata Technologies Holding (f) | (1,255,520) |
| | <u>(15,408,485)</u> |
| Information Technology - (18.1)% | |
| (11,000) Adobe, Inc. (f) | (2,488,640) |
| (40,000) Akamai Technologies, Inc. (f) | (2,443,200) |
| (23,000) Analog Devices | (1,974,090) |
| (24,000) Citrix Systems, Inc. | (2,459,040) |
| (77,000) Dropbox, Class A (f) | (1,573,110) |
| (21,000) Euronet Worldwide (f) | (2,149,980) |
| (16,000) F5 Networks (f) | (2,592,480) |
| (19,000) Fidelity National Information Services | (1,948,450) |
| (40,000) Maxim Integrated Products | (2,034,000) |
| (30,000) NetApp | (1,790,100) |
| (75,000) Oracle | (3,386,250) |
| (79,000) Paychex, Inc. | (5,146,850) |
| (15,000) PayPal Holdings, Inc. (f) | (1,261,350) |
| (25,000) Splunk (f) | (2,621,250) |
| (16,000) TE Connectivity | (1,210,080) |
| (55,000) Texas Instruments, Inc. | (5,197,500) |
| (17,000) Worldpay, Class A (f) | (1,299,310) |
| (30,000) Zscaler (f) | (1,176,300) |
| | <u>(42,751,980)</u> |
| Total Common Stocks (Proceeds \$71,613,372) | <u>(69,302,755)</u> |
| Total Securities Sold Short - (38.4)% (Proceeds \$93,760,757) | <u>(90,714,835)</u> |
| Other Assets & Liabilities, Net - 37.6% | 88,827,089 |
| Net Assets - 100.0% | 236,414,654 |

- (c) Securities (or a portion of securities) on loan. As of December 31, 2018, the market value of securities loaned was \$14,582,940. The loaned securities were secured with cash and securities collateral of \$14,928,531. Collateral is calculated based on prior day's prices.
- (d) Affiliated issuer. Assets with a total aggregate market value of \$6,797,881, or 2.9% of net assets, were affiliated with the Fund as of December 31, 2018.
- (e) Represents investments of cash collateral received in connection with securities lending.
- (f) No dividend payable on security sold short.

- (a) All or part of this security is pledged as collateral for short sales and or written option contracts. The market value of the securities pledged as collateral was \$120,915,840.
- (b) Non-income producing security.

INVESTMENT PORTFOLIO (unaudited) (continued)

As of December 31, 2018

Highland Long/Short Equity Fund

Purchased options contracts outstanding as of December 31, 2018 were as follows:

| Description | Exercise price | Counterparty | Expiration Date | Number of Contracts | Notional Value | Premium | Value |
|-------------------------------|----------------|--------------|-----------------|---------------------|----------------|-------------|-----------|
| PURCHASED PUT OPTIONS: | | | | | | | |
| Invesco QQQ Trust Series 1 | \$156.00 | Jefferies | January 2019 | 1,500 | 23,139,000 | \$1,360,211 | \$721,500 |

Written options contracts outstanding as of December 31, 2018 were as follows:

| Description | Exercise price | Counterparty | Expiration Date | Number of Contracts | Notional Value | Premium | Value |
|------------------------------|----------------|--------------|-----------------|---------------------|----------------|---------------|-------------|
| WRITTEN CALL OPTIONS: | | | | | | | |
| Invesco QQQ Trust Series 1 | \$156.00 | Jefferies | January 2019 | (1,500) | 23,139,000 | \$(1,360,211) | \$(721,500) |

Remaining Contractual Maturity of the Agreements:

| | Overnight and Continuous | Total |
|---|--------------------------|--------------------|
| Securities Lending Transactions¹ | | |
| Common Stocks | \$4,387,313 | \$4,387,313 |
| Total Borrowings | \$4,387,313 | \$4,387,313 |
| Gross amount of recognized liabilities for securities lending transactions | | \$4,387,313 |

¹ Amounts represent the payable for cash collateral received on securities on loan. This will generally be in "Overnight and Continuous" column as the securities are typically callable on demand.

INVESTMENT PORTFOLIO (unaudited)

As of December 31, 2018

Highland Long/Short Healthcare Fund

| Shares | Value (\$) |
|--|--|
| Common Stocks - 66.6% | |
| HEALTHCARE - 66.6% | |
| Biotechnology - 27.9% | |
| 24,300 | Aimmune Therapeutics, Inc. (a)(b)(c) 581,256 |
| 135,000 | Amarin, Inc. ADR (a)(c) 1,837,350 |
| 3,000 | Amgen, Inc. 584,010 |
| 58,800 | Amicus Therapeutics, Inc. (b)(c) 563,304 |
| 4,500 | BioMarin Pharmaceutical (c) 383,175 |
| 60,000 | Coherus Biosciences, Inc. (b)(c) 543,000 |
| 15,000 | Deciphera Pharmaceuticals, Inc. (c) 314,850 |
| 10,000 | G1 Therapeutics, Inc. (b)(c) 191,500 |
| 22,500 | Global Blood Therapeutics, Inc. (b)(c) 923,625 |
| 12,000 | Heron Therapeutics, Inc. (b)(c) 311,280 |
| 561,424 | Minerva Neurosciences, Inc. (a)(c) 3,783,998 |
| 13,000 | Portola Pharmaceuticals, Inc. (b)(c) 253,760 |
| 7,000 | Sage Therapeutics, Inc. (a)(b)(c) 670,530 |
| 14,500 | Shire PLC ADR (a) 2,523,580 |
| | <hr/> 13,465,218 |
| Healthcare Equipment - 1.8% | |
| 10,000 | Axonics Modulation Technologies (b)(c) 151,100 |
| 5,000 | Baxter International 329,100 |
| 2,250 | Inogen (c) 279,383 |
| 2,500 | Nevro (c) 97,225 |
| | <hr/> 856,808 |
| Healthcare Facilities - 1.1% | |
| 20,000 | Acadia Healthcare, Inc. (b)(c) 514,200 |
| Healthcare Services - 7.0% | |
| 2,000 | Anthem, Inc. 525,260 |
| 3,000 | Centene (c) 345,900 |
| 5,000 | Cigna Corp. 949,600 |
| 10,000 | DaVita, Inc. (c) 514,600 |
| 4,000 | LHC Group, Inc. (c) 375,520 |
| 6,000 | McKesson, Inc. 662,820 |
| | <hr/> 3,373,700 |
| Healthcare Technology - 1.4% | |
| 12,000 | Evolent Health, Class A (c) 239,400 |
| 8,500 | Teladoc Health, Inc. (b)(c) 421,345 |
| | <hr/> 660,745 |
| Life Sciences Tools & Services - 6.5% | |
| 11,000 | Bio-Rad Laboratories, Inc., Class A (a)(c) 2,554,420 |
| | Charles River Laboratories International |
| 5,000 | Inc. (c) 565,900 |
| | <hr/> 3,120,320 |
| Managed Healthcare - 1.8% | |
| 3,000 | Humana, Inc. (a) 859,440 |
| Pharmaceuticals - 19.1% | |
| 3,000 | Aerie Pharmaceuticals, Inc. (b)(c) 108,300 |
| 5,000 | AstraZeneca, Inc. ADR (b) 189,900 |
| 10,000 | Collegium Pharmaceutical, Inc. (a)(c) 171,700 |
| 34,740 | Dermira, Inc. (b)(c) 249,781 |
| 50,000 | EyePoint Pharmaceuticals (b)(c) 94,500 |
| 5,000 | GlaxoSmithKline ADR 191,050 |

| Shares | Value (\$) |
|---|---|
| Pharmaceuticals (continued) | |
| 333,500 | HLS Therapeutics, Inc. 3,577,226 |
| 8,000 | Merck & Co., Inc. (a) 611,280 |
| 10,000 | Novartis ADR 858,100 |
| 58,478 | Paratek Pharmaceuticals, Inc. (a)(c) 299,992 |
| 54,749 | SteadyMed, Ltd. (c)(d)(e) 14,508 |
| 30,000 | Takeda Pharmaceutical Co., Ltd. 1,015,815 |
| 30,000 | Urovant Sciences, Inc. (c) 197,700 |
| 45,000 | Zogenix, Inc. (a)(b)(c) 1,640,700 |
| | <hr/> 9,220,552 |
| Total Common Stocks | |
| | (Cost \$35,096,718) 32,070,983 |
| Preferred Stock - 5.1% | |
| INFORMATION TECHNOLOGY - 5.1% | |
| 608,695 | AMINO, Inc., Series C (c)(d)(e)(f)(g) 2,440,867 |
| Total Preferred Stock | |
| | (Cost \$3,499,996) 2,440,867 |
| Contracts | |
| Purchased Call Options (c) - 3.2% | |
| Total Purchased Call Options | |
| | (Cost \$270,148) 1,549,375 |
| Registered Investment Company - 0.2% | |
| State Street Navigator Securities Lending | |
| Government Money Market Portfolio, | |
| 100,000 | 2.350% (h) 100,000 |
| Total Registered Investment | |
| Companies (Cost \$100,000) 100,000 | |
| Units | |
| Warrants - 0.1% | |
| HEALTHCARE - 0.1% | |
| Biotechnology - 0.0% | |
| Galena Biopharma, Inc., Expires | |
| 1,717,910 | 03/18/2020 (c) - |
| Gemphire Therapeutics, Inc., Expires | |
| 118,797 | 03/15/2022 (c) 17,159 |
| | <hr/> 17,159 |
| Pharmaceuticals - 0.1% | |
| 255,000 | Scynexis, Inc., Expires 06/21/2021 (c) 43,086 |
| Total Warrants | |
| | (Cost \$—) 60,245 |
| Rights - 0.0% | |
| HEALTHCARE - 0.0% | |
| Healthcare Equipment - 0.0% | |
| 79,326 | Wright Medical Group NV, Inc. (c) 992 |
| Total Rights | |
| | (Cost \$197,727) 992 |

INVESTMENT PORTFOLIO (unaudited) (continued)

As of December 31, 2018

Highland Long/Short Healthcare Fund

| Shares | Value (\$) |
|---|--|
| Cash Equivalents - 28.1% | |
| MONEY MARKET FUND (i) - 28.1% | |
| | State Street Institutional U.S. Government Money Market Fund, Premier Class 2.170% |
| 13,521,969 | 13,521,969 |
| | Total Cash Equivalents (Cost \$13,521,969) |
| | 13,521,969 |
| Total Investments - 103.3% | 49,744,431 |
| (Cost \$52,686,558) | |
| Securities Sold Short - (7.5)% | |
| COMMON STOCKS - (7.5)% | |
| Healthcare - (7.5)% | |
| Biotechnology - (2.7)% | |
| (3,000) | AnaptysBio, Inc. (j) |
| (10,000) | Incyte (j) |
| (4,000) | Ionis Pharmaceuticals, Inc. (j) |
| (5,000) | Seattle Genetics, Inc. (j) |
| | (1,326,810) |
| Healthcare Services - (0.4)% | |
| (10,000) | Tenet Healthcare, Inc. (j) |
| | (171,400) |
| Life Sciences Tools & Services - (0.8)% | |
| (10,000) | Cambrex (j) |
| | (377,600) |
| Pharmaceuticals - (3.6)% | |
| (4,000) | Catalent (j) |
| (2,500) | Eli Lilly |
| (3,500) | Pacira Pharmaceuticals, Inc. (j) |
| (25,000) | Roche Holding AG, Inc. ADR |
| (9,700) | WaVe Life Sciences (j) |
| | (1,749,378) |
| Total Common Stocks (Proceeds \$3,956,322) | |
| | (3,625,188) |
| Total Securities Sold Short - (7.5)% (Proceeds \$3,956,322) | |
| | (3,625,188) |
| Other Assets & Liabilities, Net - 4.2% | 2,027,751 |
| Net Assets - 100.0% | 48,146,994 |

- (e) Securities with a total aggregate value of \$2,455,375, or 5.1% of net assets, were classified as Level 3 within the three-tier fair value hierarchy. Please see Notes for an explanation of this hierarchy, as well as a list of unobservable inputs used in the valuation of these instruments.
- (f) There is currently no rate available.
- (g) Restricted Securities. These securities are not registered and may not be sold to the public. There are legal and/or contractual restrictions on resale. The Fund does not have the right to demand that such securities be registered. The values of these securities are determined by valuations provided by pricing services, brokers, dealers, market makers, or in good faith under the procedures established by the Fund's Board of Trustees. Additional Information regarding such securities follows:

| Restricted Security | Security Type | Acquisition Date | Cost of Security | Market Value at Period End | Percent of Net Assets |
|---------------------|------------------|------------------|------------------|----------------------------|-----------------------|
| AMINO, Inc. | Preferred Stocks | 11/18/2016 | \$3,499,996 | \$2,440,867 | 5.1% |

- (h) Represents investments of cash collateral received in connection with securities lending.
- (i) Rate shown is 7 day effective yield.
- (j) No dividend payable on security sold short.

- (a) All or part of this security is pledged as collateral for short sales and or written option contracts. The market value of the securities pledged as collateral was \$4,757,795.
- (b) Securities (or a portion of securities) on loan. As of December 31, 2018, the market value of securities loaned was \$5,148,783. The loaned securities were secured with cash and securities collateral of \$5,281,757. Collateral is calculated based on prior day's prices.
- (c) Non-income producing security.
- (d) Represents fair value as determined by the Fund's Board of Trustees (the "Board"), or its designee in good faith, pursuant to the policies and procedures approved by the Board. Securities with a total aggregate value of \$2,455,375, or 5.1% of net assets, were fair valued under the Fund's valuation procedures as of December 31, 2018.

INVESTMENT PORTFOLIO (unaudited) (continued)

As of December 31, 2018

Highland Long/Short Healthcare Fund

Purchased options contracts outstanding as of December 31, 2018 were as follows:

| Description | Exercise price | Counterparty | Expiration Date | Number of Contracts | Notional Value | Premium | Value |
|--------------------------------|----------------|-----------------|-----------------|---------------------|----------------|------------------|--------------------|
| PURCHASED CALL OPTIONS: | | | | | | | |
| Amarin | \$17.00 | Jefferies | March 2019 | 250 | 425,000 | \$ 80,517 | \$ 28,750 |
| Amarin | 25.00 | Jefferies | June 2019 | 250 | 625,000 | 96,931 | 20,000 |
| Amarin | 5.00 | Bank of America | January 2019 | 1,750 | 875,000 | 92,700 | 1,500,625 |
| | | | | | | <u>\$270,148</u> | <u>\$1,549,375</u> |

Remaining Contractual Maturity of the Agreements:

| | Overnight and Continuous | Total |
|---|--------------------------|------------------|
| Securities Lending Transactions¹ | | |
| Common Stocks | \$100,000 | \$100,000 |
| Total Borrowings | \$100,000 | \$100,000 |
| Gross amount of recognized liabilities for securities lending transactions | | \$100,000 |

¹ Amounts represent the payable for cash collateral received on securities on loan. This will generally be in "Overnight and Continuous" column as the securities are typically callable on demand.

INVESTMENT PORTFOLIO (unaudited)

As of December 31, 2018

| Shares | Value (\$) | |
|--|---|-------------------|
| Common Stocks - 54.6% | | |
| CONSUMER DISCRETIONARY - 10.5% | | |
| 68,000 | Bojangles', Inc. (a) | 1,093,440 |
| 29,239 | Nevada Gold & Casinos, Inc. (a) | 69,589 |
| 35,639 | Nutrisystem, Inc. (b) | 1,563,839 |
| 73,067 | OurPet's Co (a) | 70,510 |
| | | <u>2,797,378</u> |
| ENERGY - 0.2% | | |
| 4,700 | WildHorse Resource Development Corp. (a)... | 66,317 |
| FINANCIAL - 5.0% | | |
| 100 | Beneficial Bancorp, Inc. | 1,429 |
| 4,604 | Blue Hills Bancorp, Inc. | 98,249 |
| 1,985 | Guaranty Bancorp | 41,189 |
| 7,000 | MB Financial, Inc. | 277,410 |
| 7,700 | Navigators Group, Inc. | 535,073 |
| 29,264 | SI Financial Group, Inc. | 372,531 |
| | | <u>1,325,881</u> |
| HEALTHCARE - 11.3% | | |
| 11,200 | athenahealth, Inc. (a)(b) | 1,477,616 |
| 38,000 | Civitas Solutions, Inc. (a) | 665,380 |
| 11,800 | TESARO, Inc. (a)(b) | 876,150 |
| | | <u>3,019,146</u> |
| INDUSTRIALS - 4.4% | | |
| 1,877 | Dun & Bradstreet Corp. | 267,923 |
| 8,522 | Engility Holdings, Inc. (a) | 242,536 |
| 70,195 | Intersections, Inc. (a)(b) | 259,020 |
| 22,200 | Spartan Corp. (a) | 403,818 |
| | | <u>1,173,297</u> |
| INFORMATION TECHNOLOGY - 15.4% | | |
| 19,460 | Apptio, Inc., Class A (a) | 738,701 |
| 16,354 | Electro Scientific Industries, Inc. (a) | 489,966 |
| 9,822 | Hortonworks, Inc. (a) | 141,633 |
| 59,383 | SendGrid, Inc. (a)(b) | 2,563,564 |
| 12,298 | Travelport Worldwide, Ltd. | 192,095 |
| | | <u>4,125,959</u> |
| REAL ESTATE - 0.6% | | |
| 23,800 | Select Income, REIT | 175,168 |
| UTILITIES - 7.2% | | |
| 29,000 | SCANA Corp. | 1,385,620 |
| 7,500 | Vectren Corp. | 539,850 |
| | | <u>1,925,470</u> |
| | Total Common Stocks (Cost \$14,855,245) | <u>14,608,616</u> |
| Master Limited Partnerships - 23.8% | | |
| ENERGY - 23.8% | | |
| 67,102 | Dominion Energy Midstream Partners LP (b) .. | 1,210,520 |
| 26,976 | TransMontaigne Partners LP (b) | 1,094,686 |
| 80,292 | Valero Energy Partners LP (b) | 3,385,914 |
| 16,000 | Western Gas Partners LP | 675,680 |
| | Total Master Limited Partnerships (Cost \$6,423,535) | <u>6,366,800</u> |

Highland Merger Arbitrage Fund

| Shares | Value (\$) | |
|--|--|--------------------|
| Cash Equivalents - 9.5% | | |
| MONEY MARKET FUND (d) - 9.5% | | |
| | State Street Institutional U.S. Government Money Market Fund, Premier Class 2.170% | 2,530,035 |
| | Total Cash Equivalents (Cost \$2,530,035) | <u>2,530,035</u> |
| Total Investments - 87.9% | | 23,505,451 |
| (Cost \$23,808,815) | | |
| Securities Sold Short - (30.9)% | | |
| COMMON STOCKS - (28.4)% | | |
| Energy - (0.2)% | | |
| (24,700) | Chesapeake Energy Corp. (c) | <u>(51,870)</u> |
| Financial - (6.0)% | | |
| (13,961) | Berkshire Hills Bancorp, Inc. | (376,528) |
| (10,150) | Fifth Third Bancorp | (238,830) |
| (17,060) | First Merchants Corp. | (584,646) |
| (5,344) | Independent Bank Corp. | (375,737) |
| (920) | Independent Bank Group, Inc. | (42,108) |
| | | <u>(1,617,849)</u> |
| Healthcare - (0.7)% | | |
| (7,662) | Tivity Health, Inc. | <u>(190,094)</u> |
| Information Technology - (11.2)% | | |
| (12,896) | Cloudera, Inc. | (142,630) |
| (4,395) | Science Applications International Corp. | (279,962) |
| (28,731) | Twilio, Inc., Class A | <u>(2,565,678)</u> |
| | | <u>(2,988,270)</u> |
| Real Estate - (0.6)% | | |
| (24,820) | Government Properties Income Trust | <u>(170,513)</u> |
| Utilities - (9.7)% | | |
| (36,123) | Dominion Energy, Inc. | <u>(2,581,350)</u> |
| | Total Common Stocks (Proceeds \$7,827,211) | <u>(7,599,946)</u> |
| MASTER LIMITED PARTNERSHIP - (2.5)% | | |
| Energy - (2.5)% | | |
| (24,400) | Western Gas Equity Partners LP .. | <u>(676,612)</u> |
| | Total Master Limited Partnerships (Proceeds \$674,219) | <u>(676,612)</u> |
| | Total Securities Sold Short - (30.9)% (Proceeds \$8,501,430) | <u>(8,276,558)</u> |
| Other Assets & Liabilities, Net - 43.0% | | 11,524,419 |
| Net Assets - 100.0% | | 26,753,312 |
| (a) | Non-income producing security. | |
| (b) | All or part of this security is pledged as collateral for short sales. The market value of the securities pledged as collateral was \$7,739,806. | |
| (c) | No dividend payable on security sold short. | |
| (d) | Rate shown is 7 day effective yield. | |

INVESTMENT PORTFOLIO (unaudited) (continued)

As of December 31, 2018

Highland Merger Arbitrage Fund

The Fund had the following swaps contracts, for which \$650,000 was pledged as collateral, open at December 31, 2018:

Swap contracts outstanding as of December 31, 2018 were as follows:

| Underlying Instrument | Financing Rate | Payment Frequency | Counter-party | Expiration Date | Currency | Notional Amount (\$) | Upfront Premiums Paid (Received) (\$) | Unrealized Appreciation/ (Depreciation) (\$) | Market Value (\$) |
|-----------------------------|--------------------------|-------------------|-----------------------------|-------------------|----------|----------------------|---------------------------------------|--|-------------------|
| LONG EQUITY TRS | | | | | | | | | |
| ATHN | 1 Month LIBOR plus 0.50% | Upon Maturity | Goldman Sachs International | December 26, 2019 | USD | 435,369 | (13) | 4,783 | 4,770 |
| BHBK | 1 Month LIBOR plus 0.50% | Upon Maturity | Goldman Sachs International | January 3, 2020 | USD | 398,717 | (71) | 1,093 | 1,022 |
| EGL | 1 Month LIBOR plus 0.50% | Upon Maturity | Goldman Sachs International | December 26, 2019 | USD | 40,015 | (5) | 1,723 | 1,718 |
| MBTF | 1 Month LIBOR plus 0.50% | Upon Maturity | Goldman Sachs International | December 23, 2019 | USD | 575,949 | (235) | 9,211 | 8,976 |
| Total Long Equity Index TRS | | | | | | | | <u>16,810</u> | <u>16,486</u> |

INVESTMENT PORTFOLIO (unaudited)

As of December 31, 2018

| Principal Amount (\$) | Value (\$) |
|--|--|
| U.S. Senior Loans (a) - 39.9% | |
| COMMUNICATION SERVICES - 1.9% | |
| 893,654 | TerreStar Corporation Term Loan A, 11.000% PIK 02/27/20 (b)(c) 892,760 |
| 20,956 | TerreStar Corporation Term Loan C, 11.000% PIK 02/27/20 (b)(c) 20,935 |
| | <u>913,695</u> |
| ENERGY - 6.9% | |
| 3,738,682 | Fieldwood Energy LLC, Closing Date Loan, 2nd Lien, LIBOR USD 1 Month+7.250%, 04/11/23 3,301,256 |
| FINANCIAL - 4.0% | |
| 2,209,338 | Ditech Holding Corporation (fka Walter Investment Management Corp.), Tranche B Term Loan, LIBOR USD 3 Month+6.000%, 06/30/22 1,918,434 |
| HEALTHCARE - 1.4% | |
| 686,544 | Quorum Health Corporation, Term Loan, LIBOR USD 1 Month+6.750%, 04/29/22 .. 682,768 |
| HOUSING - 1.9% | |
| 936,709 | 84 Lumber Company, Term Loan B-1, LIBOR USD 1 Month+5.250%, 10/25/23 .. 927,342 |
| INFORMATION TECHNOLOGY - 1.1% | |
| 560,083 | Procera Networks, Inc., Initial Term Loan, LIBOR USD 1 Month+4.500%, 10/31/25 .. 548,881 |
| MANUFACTURING - 1.3% | |
| 646,667 | VC GB Holdings, Inc., Term Loan, 2nd Lien, LIBOR USD 1 Month+8.000%, 02/28/25 .. 636,967 |
| MEDIA/TELECOMMUNICATIONS - 3.5% | |
| 2,500,000 | iHeartCommunications, Inc. Tranche D Term Loan (d) 1,690,975 |
| OIL & GAS - 1.7% | |
| 844,278 | Traverse Midstream Partners LLC, Term Loan, LIBOR USD 3 Month+4.000%, 09/27/24 812,617 |
| RETAIL - 8.2% | |
| 2,456,300 | Academy, Ltd., Initial Term Loan, LIBOR USD 1 Month+4.000%, 07/01/22 1,650,843 |
| 553,779 | Neiman Marcus Group LTD LLC, Other Term Loan, 1st Lien, LIBOR USD 1 Month+3.250%, 10/25/20 469,848 |
| 3,736,582 | Toys 'R' Us-Delaware, Inc., Term Loan B-4 (d) 1,849,608 |
| | <u>3,970,299</u> |
| SERVICE - 3.3% | |
| 2,000,000 | Advantage Sales & Marketing Inc., Term Loan, 2nd Lien, LIBOR USD 1 Month+6.500%, 07/25/22 1,584,170 |
| TRANSPORTATION - 1.3% | |
| 617,395 | Gruden Acquisition, Inc., Incremental Term Loan, 1st Lien, LIBOR USD 3 Month+5.500%, 08/18/22 606,075 |

Highland Opportunistic Credit Fund

| Principal Amount (\$)/Shares | Value (\$) |
|---|---|
| UTILITIES - 3.4% | |
| 1,623,513 | Granite Acquisition, Inc., Term Loan B, 2nd Lien, LIBOR USD 3 Month+7.250%, 12/19/22 1,590,231 |
| 15,190,310 | Texas Competitive Electric Holdings Co., LLC, Extended Escrow Loan, (e) 37,976 |
| | <u>1,628,207</u> |
| | Total U.S. Senior Loans (Cost \$22,891,725) 19,221,686 |
| Common Stocks - 23.0% | |
| COMMUNICATION SERVICES - 2.9% | |
| 5,082 | TerreStar Corporation (b)(c)(f) 1,417,167 |
| ENERGY - 0.0% | |
| 1 | Arch Coal, Inc. (g) 83 |
| FINANCIALS - 0.0% | |
| 11,732 | Ditech Holding Corp. (g)(h) 1,173 |
| INFORMATION TECHNOLOGY - 1.9% | |
| 62,227 | Avaya Holdings Corp. (g)(h) 906,025 |
| MATERIALS - 9.6% | |
| 105,492 | MPM Holdings, Inc. (h) 3,322,998 |
| 6,632 | Omnimax International, Inc. (b)(c) 1,290,310 |
| | <u>4,613,308</u> |
| MEDIA - 1.8% | |
| 2,895,971 | Gambier Bay LLC (b)(c)(i) 333,037 |
| 6,369 | Metro-Goldwyn-Mayer, Inc (f) 520,137 |
| | <u>853,174</u> |
| UTILITIES - 6.8% | |
| 3,322 | Entegra TC LLC (b)(c) — |
| 143,772 | Vistra Energy Corp. (h) 3,290,941 |
| | <u>3,290,941</u> |
| | Total Common Stocks (Cost \$13,698,886) 11,081,871 |
| Collateralized Loan Obligations - 4.5% | |
| 1,000,000 | Acis CLO, Ltd., Series 2014-5A, Class E1 LIBOR USD 3 Month+6.520%, 9.06%, 11/1/2026 (j)(k) 950,000 |
| 1,000,000 | Eaton Vance CLO, Ltd., Series 2016-1A, Class DR LIBOR USD 3 Month+7.600%, 10.04%, 1/15/2028 (j)(k) 996,248 |
| 219,365 | Highland Park CDO I, Ltd., Series 2006-1A, Class A2 LIBOR USD 3 Month+0.400%, 3.09%, 11/25/2051 (j)(k)(l) 205,106 |
| | Total Collateralized Loan Obligations (Cost \$2,081,814) 2,151,354 |
| Corporate Bonds & Notes - 2.2% | |
| ENERGY - 0.4% | |
| 2,437,000 | Ocean Rig UDW, Inc. 7.25%, 04/01/19 (b)(c)(d)(k) 168,153 |
| 4,000,000 | Rex Energy Corp (d) 58,800 |

INVESTMENT PORTFOLIO (unaudited) (continued)

As of December 31, 2018

| Principal Amount (\$)/Shares | Value (\$) |
|---|------------------|
| Corporate Bonds & Notes (continued) | |
| ENERGY (continued) | |
| 464 Sable Permian Resources LLC/AEPB Finance Corp. 7.38%, 11/01/21 (k) | 105 |
| | <u>227,058</u> |
| HEALTHCARE - 1.6% | |
| 900,000 Surgery Center Holdings 6.75%, 07/01/25 (g)(k) | 769,500 |
| INFORMATION TECHNOLOGY - 0.0% | |
| 2,500,000 Avaya, Inc. 10.50%, 03/01/21 (c)(d) | — |
| UTILITIES - 0.2% | |
| 467,000 Texas Competitive Electric Holdings Co., LLC (e) | 1,868 |
| 3,506,000 Texas Competitive Electric Holdings Co., LLC (e) | 14,024 |
| 15,307,000 Texas Competitive Electric Holdings Co., LLC (e) | 61,228 |
| 3,000,000 Texas Competitive Electric Holdings Co., LLC (e) | 9,000 |
| | <u>86,120</u> |
| Total Corporate Bonds & Notes (Cost \$2,461,482) | <u>1,082,678</u> |
| Preferred Stocks - 2.1% | |
| FINANCIAL - 2.1% | |
| 1,500 Grayson CLO, Ltd. (j)(k)(l) | 600,000 |
| 1,000 Westchester CLO, Ltd. (j)(k)(l) | 410,000 |
| Total Preferred Stocks (Cost \$1,443,578) | <u>1,010,000</u> |
| Registered Investment Companies - 1.6% | |
| 753,227 State Street Navigator Securities Lending Government Money Market Portfolio, 2.350% (m) | 753,227 |
| Total Registered Investment Companies (Cost \$753,227) | <u>753,227</u> |
| Rights - 0.4% | |
| UTILITIES - 0.4% | |
| 253,272 Texas Competitive Electric Holdings Co., LLC (h) | 187,421 |
| Total Rights (Cost \$838,632) | <u>187,421</u> |
| Warrants - 0.0% | |
| FINANCIAL - 0.0% | |
| 15,861 Ditech Holding Corp., Expires 02/14/2028 (h) | 2 |
| 19,989 Ditech Holding Corp.*, Expires 02/14/2028 (h) | 4 |
| | <u>6</u> |

Highland Opportunistic Credit Fund

| Shares/Principal Amount (\$) | Value (\$) |
|---|--------------------------|
| INFORMATION TECHNOLOGY - 0.0% | |
| 10,195 Avaya, Inc., Expires 12/19/2022 (d)(h) | 28,291 |
| Total Warrants (Cost \$14,311) | <u>28,297</u> |
| Foreign Corporate Bonds & Notes - 0.0% | |
| NETHERLANDS - 0.0% | |
| 317,982 Celtic Pharma Pinco BV (b)(d) | — |
| Total Foreign Corporate Bonds & Notes (Cost \$212,561) | <u>—</u> |
| Cash Equivalents - 25.8% | |
| MONEY MARKET FUND (n) - 25.8% | |
| 12,455,304 State Street Institutional U.S. Government Money Market Fund, Premier Class 2.170% | 12,455,304 |
| Total Cash Equivalents (Cost \$12,455,304) | <u>12,455,304</u> |
| Total Investments - 99.5% | <u>47,971,838</u> |
| (Cost \$56,851,520) | |
| Other Assets & Liabilities, Net - 0.5% | <u>251,517</u> |
| Net Assets - 100.0% | <u>48,223,355</u> |

- (a) Senior loans (also called bank loans, leveraged loans, or floating rate loans) in which the Fund invests generally pay interest at rates which are periodically determined by reference to a base lending rate plus a spread (unless otherwise identified, all senior loans carry a variable rate of interest). These base lending rates are generally (i) the Prime Rate offered by one or more major United States banks, (ii) the lending rate offered by one or more European banks such as the London Interbank Offered Rate ("LIBOR") or (iii) the Certificate of Deposit rate. As of December 31, 2018, the LIBOR USD 1 Month and LIBOR USD 3 Month rates were 2.50% and 2.81%, respectively. Senior loans, while exempt from registration under the Securities Act of 1933, as amended (the "1933 Act"), contain certain restrictions on resale and cannot be sold publicly. Senior secured floating rate loans often require prepayments from excess cash flow or permit the borrower to repay at its election. The degree to which borrowers repay, whether as a contractual requirement or at their election, cannot be predicted with accuracy. As a result, the actual remaining maturity maybe substantially less than the stated maturity shown.
- (b) Securities with a total aggregate value of \$4,122,362, or 8.5% of net assets, were classified as Level 3 within the three-tier fair value hierarchy. Please see Notes for an explanation of this hierarchy, as well as a list of unobservable inputs used in the valuation of these instruments.
- (c) Represents fair value as determined by the Fund's Board of Trustees (the "Board"), or its designee in good faith, pursuant to the policies and procedures approved by the Board. The Board considers fair valued securities to be securities for which market quotations are not readily available and these securities may be valued using a combination of observable and unobservable inputs. Securities with a total aggregate value of \$4,122,362, or 8.5% of net assets, were fair valued under the Fund's valuation procedures as of December 31, 2018. Please see Notes to Investment Portfolio.
- (d) The issuer is, or is in danger of being, in default of its payment obligation.
- (e) Represents value held in escrow pending future events. No interest is being accrued.

INVESTMENT PORTFOLIO (unaudited) (concluded)

As of December 31, 2018

Highland Opportunistic Credit Fund

- (f) Restricted Securities. These securities are not registered and may not be sold to the public. There are legal and/or contractual restrictions on resale. The Fund does not have the right to demand that such securities be registered. The values of these securities are determined by valuations provided by pricing services, brokers, dealers, market makers, or in good faith under the procedures established by the Fund's Board of Trustees. Additional Information regarding such securities follows:

| Restricted Security | Security Type | Acquisition Date | Cost of Security | Market Value at Period End | Percent of Net Assets |
|---------------------------|---------------|------------------|------------------|----------------------------|-----------------------|
| Metro-Goldwyn-Mayer, Inc. | Common Stocks | 12/20/2010 | \$ 238,560 | \$ 520,137 | 1.1% |
| TerreStar Corporation | Common Stocks | 12/12/2014 | \$1,456,829 | \$1,417,167 | 2.9% |

- (g) Securities (or a portion of securities) on loan. As of December 31, 2018, the market value of securities loaned was \$1,639,466. The loaned securities were secured with cash and securities collateral of \$1,682,567. Collateral is calculated based on prior day's prices.
- (h) Non-income producing security.
- (i) Affiliated issuer. Assets with a total aggregate market value of \$333,037, or 0.7% of net assets, were affiliated with the Fund as of December 31, 2018.
- (j) Variable or floating rate security. The base lending rates are generally the lending rate offered by one or more European banks such as the LIBOR. The interest rate shown reflects the rate in effect December 31, 2018. LIBOR, otherwise known as London Interbank Offered Rate, is the benchmark interest rate that banks charge each other for short-term loans. Current LIBOR rates include 1 month which is equal to 2.50% and 3 months equal to 2.81%.
- (k) Securities exempt from registration under Rule 144A of the 1933 Act. These securities may only be resold in transaction exempt from registration to qualified institutional buyers. At December 31, 2018, these securities amounted to \$4,099,112 or 8.5% of net assets.
- (l) Securities of collateralized loan obligations where an affiliate of the Investment Adviser serves as collateral manager.
- (m) Represents investments of cash collateral received in connection with securities lending.
- (n) Rate shown is 7 day effective yield.

Remaining Contractual Maturity of the Agreements:

| | Overnight and Continuous | Total |
|---|--------------------------|------------------|
| Securities Lending Transactions¹ | | |
| Common Stocks | \$753,227 | \$753,227 |
| Total Borrowings | \$753,227 | \$753,227 |
| Gross amount of recognized liabilities for securities lending transactions | | \$753,227 |

¹ Amounts represent the payable for cash collateral received on securities on loan. This will generally be in "Overnight and Continuous" column as the securities are typically callable on demand

GLOSSARY: (abbreviations that may be used in the preceding statements) (unaudited)

Currency Abbreviations:

USD United States Dollar

Other Abbreviations:

ADR American Depositary Receipt
CDO Collateralized Debt Obligation
CLO Collateralized Loan Obligation
ETF Exchange-Traded Fund
LIBOR London Interbank Offered Rate
LLC Limited Liability Company
LTD Limited
PIK Payment-in-Kind
PLC Public Limited Company
SPDR Standard & Poor's Depository Receipt

Underlying Instrument Abbreviations:

ATHN athenahealth, Inc.
BHBK Blue Hills Bancorp, Inc.
EGL Engility Holdings, Inc.
MBTF MBT Financial Corp.
REIT Real Estate Investment Trust

STATEMENTS OF ASSETS AND LIABILITIES

As of December 31, 2018 (unaudited)

Highland Funds I

| | Highland Long/Short Equity Fund (\$) | Highland Long/Short Healthcare Fund (\$) | Highland Merger Arbitrage (\$) | Highland Opportunistic Credit Fund (\$) |
|---|---|--|---|--|
| Assets | | | | |
| Investments, at value ^(a) | 231,504,519 | 36,222,462 | 20,975,416 | 35,183,497 |
| Affiliated investments, at value (Note 9) | 6,797,881 | — | — | 333,037 |
| Total Investments, at value | 238,302,400 | 36,222,462 | 20,975,416 | 35,516,534 |
| Cash equivalents (Note 2) | — | 13,521,969 | 2,530,035 | 12,455,304 |
| Cash | — | — | — | 97,631 |
| Restricted Cash — Securities Sold Short and Written | | | | |
| Options (Notes 2 and 3) | 76,402,517 | 2,635,712 | 11,146,037 | — |
| Restricted Cash (Note 2) | — | — | 650,000 | — |
| Foreign currency | 1,357 | — | — | — |
| Swaps, at value | — | — | 16,810 | — |
| Foreign tax reclaim receivable | 37,212 | 4,463 | 45,998 | — |
| Receivable for: | | | | |
| Investment sold | 56,273,917 | 1,940,535 | 3,846,959 | 45,025 |
| Dividends and interest | 177,453 | 35,161 | 11,636 | 124,945 |
| Investment advisory and administration fees (Note 6) | — | — | — | 37,664 |
| Fund shares sold | 2,087,723 | 149,674 | 161,832 | 722,144 |
| Due from broker | — | 851,688 | 263,872 | 208,624 |
| Prepaid expenses and other assets | 71,375 | 15,633 | 27,791 | 47,884 |
| Total assets | <u>373,353,954</u> | <u>55,377,297</u> | <u>39,676,386</u> | <u>49,255,755</u> |
| Liabilities: | | | | |
| Securities sold short, at value (Notes 2 and 8) | 90,714,835 | 3,625,188 | 8,276,558 | — |
| Due to broker | 9,661,931 | 67,090 | — | — |
| Due to custodian | 1,221,367 | — | 645 | — |
| Written options contracts, at value (Note 3) | 721,500 | — | — | — |
| Payable for: | | | | |
| Investments purchased | 20,197,970 | 3,056,427 | 4,223,582 | — |
| Fund shares redeemed | 8,881,627 | 183,794 | 222,932 | 77,967 |
| Upon receipt of securities loaned (Note 4) | 4,387,313 | 100,000 | — | 753,227 |
| Investment advisory and administration fees (Note 6) | 275,582 | 51,090 | 20,429 | — |
| Swap payments | 265,245 | — | — | — |
| Accounting services fees | 238,299 | 15,719 | 115,769 | 34,316 |
| Transfer agent fees | 144,782 | 22,754 | 1,200 | — |
| Audit fees | 49,085 | 9,315 | 6,079 | 148,246 |
| Accrued dividends on securities sold short | 40,538 | — | 6,030 | — |
| Trustees fees | 6,937 | 3,988 | — | 1,339 |
| Distribution and shareholder servicing fees (Note 6) .. | 26 | — | 76 | — |
| Income distribution payable | — | — | — | 8,333 |
| Foreign currency | — | — | 32,414 | — |
| Accrued expenses and other liabilities | 132,263 | 94,938 | 17,360 | 8,972 |
| Total liabilities | <u>136,939,300</u> | <u>7,230,303</u> | <u>12,923,074</u> | <u>1,032,400</u> |
| Commitments and Contingencies (Note 7) | | | | |
| Net Assets | <u><u>236,414,654</u></u> | <u><u>48,146,994</u></u> | <u><u>26,753,312</u></u> | <u><u>48,223,355</u></u> |

STATEMENTS OF ASSETS AND LIABILITIES (continued)

As of December 31, 2018 (unaudited)

Highland Funds I

| | Highland Long/Short Equity Fund \$ | Highland Long/Short Healthcare Fund \$ | Highland Merger Arbitrage \$ | Highland Opportunistic Credit Fund \$ |
|--|---|--|---------------------------------------|--|
| Net Assets Consist of: | | | | |
| Paid-in capital | 263,072,545 | 237,501,464 | 29,172,120 | 73,347,018 |
| Total distributable loss | (26,657,891) | (189,354,470) | (2,418,808) | (25,123,663) |
| Net Assets | <u>236,414,654</u> | <u>48,146,994</u> | <u>26,753,312</u> | <u>48,223,355</u> |
| Investments, at cost | 245,425,211 | 39,164,589 | 21,278,780 | 42,054,641 |
| Affiliated investments, at cost (Note 9) | 7,507,823 | — | — | 2,341,575 |
| Cash equivalents, at cost (Note 2) | — | 13,521,969 | 2,530,035 | 12,455,304 |
| Foreign currency, at cost | 1,345 | — | (32,358) | — |
| Proceeds from securities sold short | 93,760,757 | 3,956,322 | 8,501,430 | — |
| Written option premiums received | 1,360,211 | — | — | — |
| (a) Includes market value of securities on loan | 14,582,940 | 5,148,783 | — | 1,639,466 |
| Class A: | | | | |
| Net assets | 19,097,119 | 12,710,304 | 730,358 | 3,688,652 |
| Shares outstanding (\$0.001 par value; unlimited shares authorized) | 1,907,186 | 935,418 | 40,490 | 893,610 |
| Net asset value per share ^(a) | 10.01 | 13.59 | 18.04 | 4.13 |
| Maximum offering price per share ^{(b)(c)} | 10.59 | 14.38 | 19.09 | 4.28 |
| Class C: | | | | |
| Net assets | 14,720,813 | 11,397,008 | 1,049,332 | 3,438,843 |
| Shares outstanding (\$0.001 par value; unlimited shares authorized) | 1,613,124 | 894,457 | 58,382 | 828,795 |
| Net asset value and offering price per share ^(a) | 9.13 | 12.74 | 17.97 | 4.15 |
| Class Z: | | | | |
| Net assets | 202,596,722 | 24,039,682 | 24,973,622 | 41,095,860 |
| Shares outstanding (\$0.001 par value; unlimited shares authorized) | 19,243,164 | 1,706,794 | 1,375,201 | 10,015,577 |
| Net asset value, offering and redemption price per share | 10.53 | 14.08 | 18.16 | 4.10 |

^(a) Redemption price per share is equal to net asset value per share less any applicable contingent deferred sales charge ("CDSC").

^(b) Purchases of \$500,000 or more are subject to a 1.00% CDSC if redeemed within eighteen months of purchase.

^(c) The sales charge is 5.50% for Long/Short Equity Fund, the Long/Short Healthcare Fund and Merger Arbitrage Fund. The sales charge is 3.50% for the Opportunistic Credit Fund. On sales of \$1,000,000 or more, there is no sales charge and therefore the offering will be lower.

STATEMENTS OF OPERATIONS

For the six months ended December 31, 2018 (unaudited)

Highland Funds I

| | Highland Long/Short Equity Fund (\$) | Highland Long/Short Healthcare Fund (\$) | Highland Merger Arbitrage (\$) | Highland Opportunistic Credit Fund (\$) |
|---|---|--|---|--|
| Investment Income: | | | | |
| Income: | | | | |
| Dividends from unaffiliated issuers | 1,526,275 | 175,797 | 2,867,214 | — |
| Dividends from affiliated issuers (Note 9) ⁽¹⁾ | 1,071,250 | — | — | — |
| Less: Foreign taxes withheld | — | (4,507) | (166,844) | — |
| Securities lending income (Note 4) ⁽¹⁾⁽²⁾ | 1,748 | 16,845 | — | 9,256 |
| Interest from unaffiliated issuers | 1,006,385 | 93,572 | 120,854 | 1,226,842 |
| Total income | <u>3,605,658</u> | <u>281,707</u> | <u>2,821,224</u> | <u>1,236,098</u> |
| Expenses: | | | | |
| Investment advisory (Note 6) | 3,754,993 | 274,034 | 222,862 | 278,995 |
| Administration fees (Note 6) | 327,736 | 54,804 | 34,229 | — |
| Distribution and shareholder service fees: (Note 6) | | | | |
| Class A | 42,607 | 26,496 | 1,716 | 7,677 |
| Class C | 97,543 | 65,671 | 6,157 | 15,420 |
| Accounting services fees | 134,055 | 26,967 | 17,229 | 26,349 |
| Transfer agent fees | 201,684 | 34,469 | 2,834 | 8,050 |
| Legal fees | 12,786 | 2,693 | 2,160 | 13,158 |
| Registration fees | 32,706 | 23,320 | 26,839 | 23,683 |
| Audit fees | 51,591 | 10,673 | 7,725 | 151,741 |
| Interest expense and commitment fees (Note 7) | 502,516 | 1,121 | — | — |
| Insurance | 2,624 | — | 1,572 | 1,472 |
| Trustees fees (Note 6) | 38,479 | 7,413 | 3,556 | 6,599 |
| Reports to shareholders | 29,022 | 16,467 | 1,100 | 4,749 |
| Custodian/wire agent fees | 11,510 | 5,383 | 1,677 | 1,502 |
| Pricing fees | 1,516 | 1,516 | 3,033 | 3,033 |
| Dividends and fees on securities sold short (Note 2) | 1,407,844 | 17,276 | 610,754 | — |
| Other | 179 | 17,806 | 319 | 15,415 |
| Total operating expenses before waiver and reimbursement (Note 6) | 6,649,391 | 586,109 | 943,762 | 557,843 |
| Less: Expenses waived or borne by the adviser and administrator | (2,124,572) | — | (45,701) | (283,711) |
| Net operating expenses | <u>4,524,819</u> | <u>586,109</u> | <u>898,061</u> | <u>274,132</u> |
| Net investment income (loss) | <u>(919,161)</u> | <u>(304,402)</u> | <u>1,923,163</u> | <u>961,966</u> |
| Net Realized and Unrealized Gain (loss) on Investments | | | | |
| Realized gain (loss) on: | | | | |
| Investments from unaffiliated issuers | (1,484,055) | 8,487,306 | 1,302,093 | 691,519 |
| Securities sold short (Note 2) | (1,037,814) | 1,124,453 | (444,851) | — |
| Swap contracts (Note 3) | 1,482,135 | — | (368,972) | — |
| Written options contracts (Note 3) | (383,445) | 483,254 | 1,091 | — |
| Futures contracts (Note 3) | 5,724 | — | 7,576 | — |
| Foreign currency related transactions | (175,138) | (3,180) | (43,190) | — |
| Net Change in Unrealized Appreciation (Depreciation) on: | | | | |
| Investments in unaffiliated issuers | (34,489,151) | (7,089,726) | (936,721) | (3,577,028) |
| Investments in affiliated issuers (Note 9) | (871,734) | — | — | (39,819) |
| Securities sold short (Note 2) | 3,343,925 | 298,375 | 518,207 | — |
| Swap contracts (Note 3) | (2,487,701) | — | (734,059) | — |
| Written options contracts (Note 3) | 640,397 | — | 328 | — |
| Foreign currency related translations | 50,094 | 374 | (1,514) | — |
| Net realized and unrealized gain (loss) on investments | <u>(35,406,763)</u> | <u>3,300,856</u> | <u>(700,012)</u> | <u>(2,925,328)</u> |
| Total increase (decrease) in net assets resulting from operations | <u>(36,325,924)</u> | <u>2,996,454</u> | <u>1,223,151</u> | <u>(1,963,362)</u> |

STATEMENTS OF CHANGES IN NET ASSETS

Highland Funds I

| | Highland Long/Short Equity Fund | |
|---|--|-------------------------------------|
| | Six Months Ended December 31, 2018 (unaudited) (\$) | Year Ended June 30, 2018 (\$) |
| Increase (Decrease) in Net Assets | | |
| Operations: | | |
| Net investment loss | (919,161) | (4,657,665) |
| Net realized gain (loss) on investments, securities sold short, written options, futures contracts and foreign currency transactions | (1,592,593) | 36,863,657 |
| Net decrease in unrealized depreciation on investments, securities sold short, written options, futures contracts and foreign currency transactions | <u>(33,814,170)</u> | <u>(1,031,975)</u> |
| Net increase (decrease) from operations | <u>(36,325,924)</u> | <u>31,174,017</u> |
| Distributions⁽¹⁾ | | |
| Class A | (1,980,312) | (897,492) |
| Class C | (1,644,015) | (667,393) |
| Class Z | <u>(21,375,685)</u> | <u>(8,383,528)</u> |
| Total distributions | <u>(25,000,012)</u> | <u>(9,948,413)</u> |
| Increase (decrease) in net assets from operations and distributions | <u>(61,325,936)</u> | <u>21,225,604</u> |
| Share transactions: | | |
| Proceeds from sale of shares | | |
| Class A | 3,475,467 | 7,926,311 |
| Class C | 643,802 | 2,251,241 |
| Class Z | 47,156,292 | 86,574,355 |
| Value of distributions reinvested | | |
| Class A | 1,829,535 | 835,687 |
| Class C | 1,363,455 | 530,096 |
| Class Z | 13,251,145 | 5,636,542 |
| Cost of shares redeemed | | |
| Class A | (6,134,009) | (17,774,126) |
| Class C | (4,340,497) | (9,245,975) |
| Class Z | <u>(117,460,182)</u> | <u>(133,922,556)</u> |
| Net decrease from shares transactions | <u>(60,214,992)</u> | <u>(57,188,425)</u> |
| Total decrease in net assets | <u>(121,540,928)</u> | <u>(35,962,821)</u> |
| Net Assets | | |
| Beginning of period | 357,955,582 | 393,918,403 |
| End of period ⁽²⁾ | <u>236,414,654</u> | <u>357,955,582</u> |

⁽¹⁾ Current year presentation of distributions conforms with S-X Disclosure Simplification. Prior year distributions have been consolidated to conform with S-X Disclosure Simplification.

⁽²⁾ Includes accumulated net investment loss of \$(3,136,168) as of the year ended June 30, 2018. In August 2018, the SEC eliminated the requirement to disclose undistributed net investment income in 2018 (See Note 10).

STATEMENTS OF CHANGES IN NET ASSETS (continued)

Highland Funds I

| | Highland Long/Short Equity Fund | |
|--|--|-----------------------------|
| | Six Months Ended December 31, 2018 (unaudited) | Year Ended June 30, 2018 |
| Class A: | | |
| Shares Sold | 282,887 | 649,162 |
| Issued for distribution reinvested | 186,307 | 69,409 |
| Shares Redeemed | <u>(541,899)</u> | <u>(1,464,260)</u> |
| Net Decrease in fund shares | <u>(72,705)</u> | <u>(745,689)</u> |
| Class C: | | |
| Shares Sold | 62,772 | 196,589 |
| Issued for distribution reinvested | 152,341 | 47,542 |
| Shares Redeemed | <u>(422,036)</u> | <u>(815,532)</u> |
| Net Decrease in fund shares | <u>(206,923)</u> | <u>(571,401)</u> |
| Class Z: | | |
| Shares Sold | 3,755,110 | 6,762,221 |
| Issued for distribution reinvested | 1,284,026 | 449,127 |
| Shares Redeemed | <u>(9,965,945)</u> | <u>(10,388,753)</u> |
| Net Decrease in fund shares | <u>(4,926,809)</u> | <u>(3,177,405)</u> |

STATEMENTS OF CHANGES IN NET ASSETS

Highland Funds I

| | Highland Long/Short Healthcare Fund | |
|---|--|-------------------------------------|
| | Six Months Ended December 31, 2018 (unaudited) (\$) | Year Ended June 30, 2018 (\$) |
| Increase (Decrease) in Net Assets | | |
| Operations: | | |
| Net investment loss | (304,402) | (1,458,407) |
| Net realized gain on investments, securities sold short and written options | 10,091,833 | 8,395,373 |
| Net increase (decrease) in unrealized appreciation (depreciation) on investments, securities sold short, written options, futures contracts and foreign currency transactions | <u>(6,790,977)</u> | <u>565,953</u> |
| Net increase from operations | <u>2,996,454</u> | <u>7,502,919</u> |
| Distributions⁽¹⁾ | | |
| Class A | — | (113,620) |
| Class Z | — | (455,274) |
| Total distributions | <u>—</u> | <u>(568,894)</u> |
| Increase in net assets from operations and distributions | <u>2,996,454</u> | <u>6,934,025</u> |
| Share transactions: | | |
| Proceeds from sale of shares | | |
| Class A | 1,872,714 | 700,095 |
| Class C | 491,100 | 661,941 |
| Class Z | 6,414,422 | 15,545,740 |
| Value of distributions reinvested | | |
| Class A | — | 104,710 |
| Class Z | — | 449,520 |
| Cost of shares redeemed | | |
| Class A | (6,682,743) | (17,207,744) |
| Class C | (3,059,526) | (11,706,522) |
| Class Z | <u>(10,436,303)</u> | <u>(46,541,902)</u> |
| Net decrease from shares transactions | <u>(11,400,336)</u> | <u>(57,994,162)</u> |
| Total decrease in net assets | <u>(8,403,882)</u> | <u>(51,060,137)</u> |
| Net Assets | | |
| Beginning of period | <u>56,550,876</u> | <u>107,611,013</u> |
| End of period ⁽²⁾ | <u>48,146,994</u> | <u>56,550,876</u> |

⁽¹⁾ Current year presentation of distributions conforms with S-X Disclosure Simplification. Prior year distributions have been consolidated to conform with S-X Disclosure Simplification.

⁽²⁾ Includes accumulated net investment loss of \$(803,187) as of the year ended June 30, 2018. In August 2018, the SEC eliminated the requirement to disclose undistributed net investment income in 2018 (See Note 10).

STATEMENTS OF CHANGES IN NET ASSETS (continued)

Highland Funds I

| | Highland Long/Short Healthcare Fund | |
|--|--|-----------------------------|
| | Six Months Ended December 31, 2018 (unaudited) | Year Ended June 30, 2018 |
| Class A: | | |
| Shares Sold | 126,468 | 59,924 |
| Issued for distribution reinvested | — | 8,762 |
| Shares Redeemed | (469,682) | (1,456,677) |
| Net Decrease in fund shares | <u>(343,214)</u> | <u>(1,387,991)</u> |
| Class C: | | |
| Shares Sold | 36,697 | 59,026 |
| Shares Redeemed | (233,015) | (1,053,077) |
| Net Decrease in fund shares | <u>(196,318)</u> | <u>(994,051)</u> |
| Class Z: | | |
| Shares Sold | 440,486 | 1,260,353 |
| Issued for distribution reinvested | — | 36,428 |
| Shares Redeemed | (722,911) | (3,779,363) |
| Net Decrease in fund shares | <u>(282,425)</u> | <u>(2,482,582)</u> |

STATEMENTS OF CHANGES IN NET ASSETS

Highland Funds I

| | Highland Merger Arbitrage | |
|---|--|-------------------------------------|
| | Six Months Ended December 31, 2018 (unaudited) (\$) | Year Ended June 30, 2018 (\$) |
| Increase (Decrease) in Net Assets | | |
| Operations: | | |
| Net investment income (loss)..... | 1,923,163 | (329,883) |
| Net realized gain on investments, securities sold short, written options, futures contracts and foreign currency transactions | 453,747 | 1,027,850 |
| Net increase (decrease) in unrealized appreciation (depreciation) on investments, securities sold short, written options, futures contracts and foreign currency transactions | <u>(1,153,759)</u> | <u>335,088</u> |
| Net increase from operations | <u>1,223,151</u> | <u>1,033,055</u> |
| Distributions⁽¹⁾ | | |
| Class A | (121,464) | (121,175) |
| Class C | (182,213) | (81,503) |
| Class Z | <u>(4,035,849)</u> | <u>(2,147,401)</u> |
| Total distributions | <u>(4,339,526)</u> | <u>(2,350,079)</u> |
| Decrease in net assets from operations and distributions | <u>(3,116,375)</u> | <u>(1,317,024)</u> |
| Share transactions: | | |
| Proceeds from sale of shares | | |
| Class A | 293,841 | 325,206 |
| Class C | 112,335 | 866,516 |
| Class Z | 1,610,196 | 10,827,811 |
| Value of distributions reinvested | | |
| Class A | 77,643 | 121,174 |
| Class C | 169,659 | 67,622 |
| Class Z | 3,997,105 | 2,143,897 |
| Cost of shares redeemed | | |
| Class A | (568,758) | (979,433) |
| Class C | (401,787) | (641,792) |
| Class Z | <u>(13,890,556)</u> | <u>(2,990,058)</u> |
| Net increase (decrease) from shares transactions | <u>(8,600,322)</u> | <u>9,740,943</u> |
| Total increase (decrease) in net assets | <u>(11,716,697)</u> | <u>8,423,919</u> |
| Net Assets | | |
| Beginning of period | <u>38,470,009</u> | <u>30,046,090</u> |
| End of period ⁽²⁾ | <u>26,753,312</u> | <u>38,470,009</u> |

⁽¹⁾ Current year presentation of distributions conforms with S-X Disclosure Simplification. Prior year distributions have been consolidated to conform with S-X Disclosure Simplification.

⁽²⁾ Includes accumulated net investment loss of \$(513,494) as of the year ended June 30, 2018. In August 2018, the SEC eliminated the requirement to disclose undistributed net investment income in 2018 (See Note 10).

STATEMENTS OF CHANGES IN NET ASSETS (continued)

Highland Funds I

| | Highland Merger Arbitrage | |
|--|--|-----------------------------|
| | Six Months Ended December 31, 2018 (unaudited) | Year Ended June 30, 2018 |
| Class A: | | |
| Shares Sold | 13,826 | 15,115 |
| Issued for distribution reinvested | 4,323 | 5,905 |
| Shares Redeemed | <u>(26,755)</u> | <u>(48,636)</u> |
| Net Decrease in fund shares | <u>(8,606)</u> | <u>(27,616)</u> |
| Class C: | | |
| Shares Sold | 5,373 | 41,998 |
| Issued for distribution reinvested | 9,478 | 3,312 |
| Shares Redeemed | <u>(20,431)</u> | <u>(32,179)</u> |
| Net Increase (Decrease) in fund shares | <u>(5,580)</u> | <u>13,131</u> |
| Class Z: | | |
| Shares Sold | 77,201 | 512,098 |
| Issued for distribution reinvested | 221,071 | 104,054 |
| Shares Redeemed | <u>(648,014)</u> | <u>(145,457)</u> |
| Net Increase (Decrease) in fund shares | <u>(349,742)</u> | <u>470,695</u> |

STATEMENTS OF CHANGES IN NET ASSETS

Highland Funds I

| | Highland Opportunistic Credit Fund | |
|---|--|-------------------------------------|
| | Six Months Ended December 31, 2018 (unaudited) (\$) | Year Ended June 30, 2018 (\$) |
| Increase (Decrease) in Net Assets | | |
| Operations: | | |
| Net investment income | 961,966 | 4,731,919 |
| Net realized gain (loss) on investments and foreign currency transactions | 691,519 | (1,018,149) |
| Net increase (decrease) in unrealized appreciation (depreciation) on investments, securities sold short, written options, futures contracts and foreign currency transactions | <u>(3,616,847)</u> | <u>2,767,265</u> |
| Net increase (decrease) from operations | <u>(1,963,362)</u> | <u>6,481,035</u> |
| Distributions⁽¹⁾ | | |
| Class A | (65,915) | (373,116) |
| Class C | (45,089) | (239,387) |
| Class Z | (799,812) | (3,837,432) |
| Return of capital: | | |
| Class A | — | (6,671) |
| Class C | — | (4,280) |
| Class Z | — | (68,612) |
| Total distributions | <u>(910,816)</u> | <u>(4,529,498)</u> |
| Increase (decrease) in net assets from operations and distributions | <u>(2,874,178)</u> | <u>1,951,537</u> |
| Share transactions: | | |
| Proceeds from sale of shares | | |
| Class A | 500,354 | 2,055,977 |
| Class C | 357,708 | 1,083,561 |
| Class Z | 3,420,410 | 12,821,291 |
| Value of distributions reinvested | | |
| Class A | 64,465 | 346,654 |
| Class C | 18,577 | 90,311 |
| Class Z | 779,825 | 3,640,501 |
| Cost of shares redeemed | | |
| Class A | (1,419,297) | (6,293,216) |
| Class C | (299,942) | (1,432,301) |
| Class Z | <u>(11,490,423)</u> | <u>(39,026,551)</u> |
| Net decrease from shares transactions | <u>(8,068,323)</u> | <u>(26,713,773)</u> |
| Total decrease in net assets | <u>(10,942,501)</u> | <u>(24,762,236)</u> |
| Net Assets | | |
| Beginning of period | <u>59,165,856</u> | <u>83,928,092</u> |
| End of period ⁽²⁾ | <u>48,223,355</u> | <u>59,165,856</u> |

⁽¹⁾ Current year presentation of distributions conforms with S-X Disclosure Simplification. Prior year distributions have been consolidated to conform with S-X Disclosure Simplification.

⁽²⁾ Includes distributions in excess of net investment income of \$(4,864) as of the year ended June 30, 2018. The SEC eliminated the requirement to disclose undistributed net investment income in 2018.

STATEMENTS OF CHANGES IN NET ASSETS (continued)

Highland Funds I

| | Highland Opportunistic Credit Fund | |
|--|--|-----------------------------|
| | Six Months Ended December 31, 2018 (unaudited) | Year Ended June 30, 2018 |
| Class A: | | |
| Shares Sold | 112,892 | 485,249 |
| Issued for distribution reinvested | 14,887 | 82,044 |
| Shares Redeemed | <u>(323,988)</u> | <u>(1,497,135)</u> |
| Net Decrease in fund shares | <u>(196,209)</u> | <u>(929,842)</u> |
| Class C: | | |
| Shares Sold | 80,834 | 256,621 |
| Issued for distribution reinvested | 4,282 | 21,270 |
| Shares Redeemed | <u>(68,582)</u> | <u>(336,427)</u> |
| Net Increase (Decrease) in fund shares | <u>16,534</u> | <u>(58,536)</u> |
| Class Z: | | |
| Shares Sold | 776,810 | 3,061,821 |
| Issued for distribution reinvested | 181,274 | 866,440 |
| Shares Redeemed | <u>(2,666,956)</u> | <u>(9,290,157)</u> |
| Net Decrease in fund shares | <u>(1,708,872)</u> | <u>(5,361,896)</u> |

STATEMENT OF CASH FLOWS

For the Six Months Ended December 31, 2018 (unaudited)

Highland Long/Short Equity Fund

(\$)

Cash Flows Provided by Operating Activities:

Net decrease in net assets resulting from operations (36,325,924)

Adjustments to Reconcile Net Investment Loss to Net Cash Used Provided by Operating Activities:

Purchases of investment securities from unaffiliated issuers (526,767,980)
Purchases of investment securities from affiliated issuers (1,087,660)
Proceeds from disposition of investment securities from unaffiliated issues 564,819,088
Proceeds from the sale of short-term portfolio investments, net 11,107,119
Purchases of securities sold short (510,144,504)
Proceeds of securities sold short 466,741,849
Net proceeds received from on written options contracts 876,324
Net realized loss on Investments from unaffiliated issuers 1,484,055
Net realized loss on securities sold short, written options contracts and foreign currency transactions 1,596,397
Net change in unrealized appreciation (depreciation) on investments, affiliated investments, securities sold short, written options contracts, swap contracts and translation on assets and liabilities denominated in foreign currency 33,814,170
Decrease in restricted cash 78,561,918
Increase in receivable for investments sold (22,225,558)
Increase in dividends and interest receivable (43,341)
Increase in foreign tax reclaim receivable (37,212)
Increase in prepaid expenses and other assets (24,983)
Change in swap premium 37,216
Increase due to broker 8,971,931
Decrease in payable upon receipt of securities on loan (649,593)
Increase in payable for investments purchased 5,486,497
Decrease in payable for swap payments (44,258)
Increase in payables to related parties 171,102
Decrease in payable for distribution and shareholder service fees (4,822)
Increase in payable to transfer agent fees 93,372
Decrease in accrued dividends on short sales (128,973)
Decrease in payable for commitment fees (266)
Decrease in accrued expenses and other liabilities (179,646)
Net cash flow provided by operating activities 76,096,316

Cash Flows Used In Financing Activities:

Distributions paid in cash (8,555,877)
Payments of shares redeemed (119,238,955)
Proceeds from shares sold 49,487,162
Net cash flow used in financing activities (78,307,670)
Effect of exchange rate changes on cash (125,044)
Net Decrease in Cash (2,336,398)

Cash and Foreign Currency/Due to Custodian:

Beginning of period 1,116,388
End of period (1,220,010)

Supplemental disclosure of cash flow information:

Reinvestment of distributions 16,444,135
Cash paid during the period for interest expense and commitment fees 502,516

STATEMENT OF CASH FLOWS

For the Six Months Ended December 31, 2018 (unaudited)

Highland Merger Arbitrage Fund

(\$)

| | |
|---|---------------------|
| Cash Flows Provided by Operating Activities: | |
| Net increase in net assets resulting from operations | 1,223,151 |
| Adjustments to Reconcile Net Investment Loss to Net Cash Used Provided by Operating Activities: | |
| Purchases of investment securities from unaffiliated issuers | (164,260,053) |
| Proceeds from disposition of investment securities from unaffiliated issues | 213,303,295 |
| Purchases of short-term portfolio investments, net | (2,530,035) |
| Purchases of securities sold short | (107,126,641) |
| Proceeds of securities sold short | 77,994,499 |
| Net proceeds received from on written options contracts | (19,203) |
| Net realized gain on Investments from unaffiliated issuers | (1,302,093) |
| Net realized loss on securities sold short, written options contracts and foreign currency transactions | 488,950 |
| Net change in unrealized appreciation (depreciation) on investments, affiliated investments, securities sold short, written options contracts, swap contracts and translation on assets and liabilities denominated in foreign currency | 1,153,759 |
| Increase in restricted cash | (4,578,811) |
| Increase in receivable for investments sold | (2,232,231) |
| Decrease in dividends and interest receivable | 214,711 |
| Increase due from broker | (157,356) |
| Increase in foreign tax reclaim receivable | (45,998) |
| Decrease in prepaid expenses and other assets | 12,329 |
| Change in swap premium | 24,772 |
| Increase in payable for investments purchased | 1,599,028 |
| Decrease in payable for swap payments | (275,372) |
| Increase in payables to related parties | 103,837 |
| Decrease in payable for distribution and shareholder service fees | (192) |
| Decrease in payable to transfer agent fees | (1,256) |
| Decrease in accrued dividends on short sales | (107,172) |
| Decrease in accrued expenses and other liabilities | (150,728) |
| Net cash flow provided by operating activities | <u>13,329,190</u> |
| Cash Flows Used In Financing Activities: | |
| Distributions paid in cash | (95,119) |
| Payments of shares redeemed | (14,653,363) |
| Proceeds from shares sold | <u>1,854,540</u> |
| Net cash flow used in financing activities | <u>(12,893,942)</u> |
| Effect of exchange rate changes on cash | <u>(44,704)</u> |
| Net Increase in Cash | <u>390,544</u> |
| Cash and Foreign Currency/Due to Custodian: | |
| Beginning of period | <u>(423,603)</u> |
| End of period | <u>(33,059)</u> |
| Supplemental disclosure of cash flow information: | |
| Reinvestment of distributions | <u>4,244,407</u> |
| Cash paid during the period for interest expense and commitment fees | <u>—</u> |

FINANCIAL HIGHLIGHTS

Highland Long/Short Equity Fund, Class A

Selected data for a share outstanding throughout each period is as follows:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Years Ended June 30, | | | | |
|---|---|------------------------------|-------------|---------------|---------------|------------------|
| | | 2018 | 2017 | 2016 | 2015 | 2014 |
| Net Asset Value, Beginning of Period | \$ 12.38 | \$ 11.80 | \$ 10.95 | \$ 11.98 | \$ 12.18 | \$ 11.37 |
| Income from Investment Operations: | | | | | | |
| Net investment loss ^(a) | (0.05) | (0.18) | (0.18) | (0.18) | (0.20) | (0.21) |
| Redemption fees added to paid-in capital | — | — | — | — | — | — ^(b) |
| Net realized and unrealized gain (loss) | <u>(1.29)</u> | <u>1.09</u> | <u>1.03</u> | <u>(0.40)</u> | <u>0.48</u> | <u>1.97</u> |
| Total from Investment Operations | (1.34) | 0.91 | 0.85 | (0.58) | 0.28 | 1.76 |
| Less Distributions Declared to shareholders: | | | | | | |
| From net realized gains | <u>(1.03)</u> | <u>(0.33)</u> | <u>—</u> | <u>(0.45)</u> | <u>(0.48)</u> | <u>(0.95)</u> |
| Total distributions declared to shareholders | (1.03) | (0.33) | — | (0.45) | (0.48) | (0.95) |
| Net Asset Value, End of period^(c) | \$ 10.01 | \$ 12.38 | \$ 11.80 | \$ 10.95 | \$ 11.98 | \$ 12.18 |
| Total Return ^{(c)(d)} | (10.64)% ^(g) | 7.77% | 7.76% | (4.99)% | 2.45% | 15.60% |
| Ratios to Average Net Assets/Supplemental Data:^{(e)(f)} | | | | | | |
| Net Assets, End of Period (000's) | \$19,097 | \$24,514 | \$32,163 | \$40,219 | \$76,813 | \$195,612 |
| Gross operating expenses ^(h) | 4.24% | 4.06% | 3.89% | 3.62% | 3.58% | 3.75% |
| Net investment loss | (0.78)% | (1.43)% | (1.64)% | (1.56)% | (1.63)% | (1.69)% |
| Portfolio turnover rate | 167% ^(g) | 247% | 404% | 457% | 414% | 349% |

(a) Per share data was calculated using average shares outstanding during the period.

(b) Represents less than \$0.005 per share.

(c) The Net Asset Value per share and total return have been calculated based on net assets which include adjustments made in accordance with U.S. Generally Accepted Accounting Principles required at period end for financial reporting purposes. These figures do not necessarily reflect the Net Asset Value per share or total return experienced by the shareholder at period end.

(d) Total return is at net asset value assuming all distributions are reinvested and no initial sales charge or CDSC. For periods with waivers/reimbursements, had the Fund's investment adviser not waived or reimbursed a portion of expenses, total return would have been lower.

(e) All ratios for the period have been annualized, unless otherwise indicated.

(f) Includes dividends and fees on securities sold short.

(g) Not annualized.

(h) Supplemental expense ratios are shown below:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Years Ended June 30, | | | | |
|--|---|------------------------------|-------|-------|-------|-------|
| | | 2018 | 2017 | 2016 | 2015 | 2014 |
| Net operating expenses (net of waiver/reimbursement, if applicable, but gross of all other operating expenses) | 2.99% | 2.81% | 2.64% | 2.37% | 2.33% | 2.50% |
| Interest expense and commitment fees | 0.30% | 0.30% | 0.01% | 0.02% | 0.07% | —% |
| Dividends and fees on securities sold short | 0.85% | 0.71% | 0.80% | 0.57% | 0.49% | 0.56% |

FINANCIAL HIGHLIGHTS

Highland Long/Short Equity Fund, Class C

Selected data for a share outstanding throughout each period is as follows:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Years Ended June 30, | | | | |
|---|---|------------------------------|-------------|---------------|---------------|------------------|
| | | 2018 | 2017 | 2016 | 2015 | 2014 |
| Net Asset Value, Beginning of Period | \$ 11.43 | \$ 10.98 | \$ 10.25 | \$ 11.32 | \$ 11.62 | \$ 10.95 |
| Income from Investment Operations: | | | | | | |
| Net investment loss ^(a) | (0.09) | (0.24) | (0.24) | (0.23) | (0.26) | (0.27) |
| Redemption fees added to paid-in capital | — | — | — | — | — | — ^(b) |
| Net realized and unrealized gain (loss) | <u>(1.18)</u> | <u>1.02</u> | <u>0.97</u> | <u>(0.39)</u> | <u>0.44</u> | <u>1.89</u> |
| Total from Investment Operations | (1.27) | 0.78 | 0.73 | (0.62) | 0.18 | 1.62 |
| Less Distributions Declared to shareholders: | | | | | | |
| From net realized gains | <u>(1.03)</u> | <u>(0.33)</u> | <u>—</u> | <u>(0.45)</u> | <u>(0.48)</u> | <u>(0.95)</u> |
| Total distributions declared to shareholders | (1.03) | (0.33) | — | (0.45) | (0.48) | (0.95) |
| Net Asset Value, End of period^(c) | \$ 9.13 | \$ 11.43 | \$ 10.98 | \$ 10.25 | \$ 11.32 | \$ 11.62 |
| Total Return ^{(c)(d)} | (10.83)% ^(e) | 7.16% | 7.12% | (5.65)% | 1.69% | 14.89% |
| Ratios to Average Net Assets/Supplemental Data:^{(e)(f)} | | | | | | |
| Net Assets, End of Period (000's) | \$14,721 | \$20,796 | \$26,263 | \$50,006 | \$55,639 | \$55,795 |
| Gross operating expenses ^(h) | 4.89% | 4.71% | 4.51% | 4.27% | 4.28% | 4.39% |
| Net investment loss | (1.47)% | (2.10)% | (2.31)% | (2.20)% | (2.27)% | (2.35)% |
| Portfolio turnover rate | 167% ^(g) | 247% | 404% | 457% | 414% | 349% |

(a) Per share data was calculated using average shares outstanding during the period.

(b) Represents less than \$0.005 per share.

(c) The Net Asset Value per share and total return have been calculated based on net assets which include adjustments made in accordance with U.S. Generally Accepted Accounting Principles required at period end for financial reporting purposes. These figures do not necessarily reflect the Net Asset Value per share or total return experienced by the shareholder at period end.

(d) Total return is at net asset value assuming all distributions are reinvested and no initial sales charge or CDSC. For periods with waivers/reimbursements, had the Fund's investment adviser not waived or reimbursed a portion of expenses, total return would have been lower.

(e) All ratios for the period have been annualized, unless otherwise indicated.

(f) Includes dividends and fees on securities sold short.

(g) Not annualized.

(h) Supplemental expense ratios are shown below:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Years Ended June 30, | | | | |
|--|---|------------------------------|-------|-------|-------|-------|
| | | 2018 | 2017 | 2016 | 2015 | 2014 |
| Net operating expenses (net of waiver/reimbursement, if applicable, but gross of all other operating expenses) | 3.64% | 3.46% | 3.26% | 3.02% | 3.03% | 3.14% |
| Interest expense and commitment fees | 0.30% | 0.30% | 0.01% | 0.01% | 0.07% | —% |
| Dividends and fees on securities sold short | 0.85% | 0.72% | 0.77% | 0.57% | 0.54% | 0.56% |

FINANCIAL HIGHLIGHTS

Highland Long/Short Equity Fund, Class Z

Selected data for a share outstanding throughout each period is as follows:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Years Ended June 30, | | | | |
|---|---|------------------------------|-------------|---------------|---------------|------------------|
| | | 2018 | 2017 | 2016 | 2015 | 2014 |
| Net Asset Value, Beginning of Period | \$ 12.94 | \$ 12.27 | \$ 11.34 | \$ 12.35 | \$ 12.51 | \$ 11.61 |
| Income from Investment Operations: | | | | | | |
| Net investment loss ^(a) | (0.03) | (0.14) | (0.15) | (0.14) | (0.16) | (0.17) |
| Redemption fees added to paid-in capital | — | — | — | — | — | — ^(b) |
| Net realized and unrealized gain (loss) | <u>(1.35)</u> | <u>1.14</u> | <u>1.08</u> | <u>(0.42)</u> | <u>0.48</u> | <u>2.02</u> |
| Total from Investment Operations | (1.38) | 1.00 | 0.93 | (0.56) | 0.32 | 1.85 |
| Less Distributions Declared to shareholders: | | | | | | |
| From net realized gains | <u>(1.03)</u> | <u>(0.33)</u> | <u>—</u> | <u>(0.45)</u> | <u>(0.48)</u> | <u>(0.95)</u> |
| Total distributions declared to shareholders | (1.03) | (0.33) | — | (0.45) | (0.48) | (0.95) |
| Net Asset Value, End of period^(c) | \$ 10.53 | \$ 12.94 | \$ 12.27 | \$ 11.34 | \$ 12.35 | \$ 12.51 |
| Total Return ^{(c)(d)} | (10.41)% ^(g) | 8.22% | 8.20% | (4.67)% | 2.71% | 16.07% |
| Ratios to Average Net Assets/Supplemental Data:^{(e)(f)} | | | | | | |
| Net Assets, End of Period (000's) | \$202,597 | \$312,646 | \$335,493 | \$570,998 | \$724,250 | \$766,646 |
| Gross operating expenses ^(h) | 3.91% | 3.71% | 3.51% | 3.27% | 3.28% | 3.39% |
| Net investment loss | (0.47)% | (1.12)% | (1.31)% | (1.20)% | (1.27)% | (1.34)% |
| Portfolio turnover rate | 167% ^(g) | 247% | 404% | 457% | 414% | 349% |

(a) Per share data was calculated using average shares outstanding during the period.

(b) Represents less than \$0.005 per share.

(c) The Net Asset Value per share and total return have been calculated based on net assets which include adjustments made in accordance with U.S. Generally Accepted Accounting Principles required at period end for financial reporting purposes. These figures do not necessarily reflect the Net Asset Value per share or total return experienced by the shareholder at period end.

(d) Total return is at net asset value assuming all distributions are reinvested and no initial sales charge or CDSC. For periods with waivers/reimbursements, had the Fund's investment adviser not waived or reimbursed a portion of expenses, total return would have been lower.

(e) All ratios for the period have been annualized, unless otherwise indicated.

(f) Includes dividends and fees on securities sold short.

(g) Not annualized.

(h) Supplemental expense ratios are shown below:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Years Ended June 30, | | | | |
|--|---|------------------------------|-------|-------|-------|-------|
| | | 2018 | 2017 | 2016 | 2015 | 2014 |
| Net operating expenses (net of waiver/reimbursement, if applicable, but gross of all other operating expenses) | 2.66% | 2.46% | 2.26% | 2.02% | 2.03% | 2.14% |
| Interest expense and commitment fees | 0.30% | 0.30% | 0.01% | 0.01% | 0.07% | —% |
| Dividends and fees on securities sold short | 0.85% | 0.72% | 0.77% | 0.57% | 0.54% | 0.56% |

FINANCIAL HIGHLIGHTS

Highland Long/Short Healthcare Fund, Class A

Selected data for a share outstanding throughout each period is as follows:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Years Ended June 30, | | | | |
|---|---|------------------------------|-------------|---------------|---------------|---------------------|
| | | 2018 | 2017 | 2016 | 2015 | 2014 |
| Net Asset Value, Beginning of Period | \$ 12.96 | \$ 11.61 | \$ 11.50 | \$ 16.22 | \$ 15.07 | \$ 11.03 |
| Income from Investment Operations: | | | | | | |
| Net investment loss ^(a) | (0.08) | (0.21) | (0.21) | (0.28) | (0.32) | (0.27) |
| Redemption fees added to paid-in capital | — | — | — | — | — | — ^{(a)(b)} |
| Net realized and unrealized gain (loss) ^(a) | <u>0.71</u> | <u>1.62</u> | <u>0.32</u> | <u>(3.86)</u> | <u>2.15</u> | <u>4.31</u> |
| Total from Investment Operations | 0.63 | 1.41 | 0.11 | (4.14) | 1.83 | 4.04 |
| Less Distributions Declared to shareholders: | | | | | | |
| From net investment income | — | (0.06) | — | — | — | — |
| From net realized gains | <u>—</u> | <u>—</u> | <u>—</u> | <u>(0.58)</u> | <u>(0.68)</u> | <u>—</u> |
| Total distributions declared to shareholders | — | (0.06) | — | (0.58) | (0.68) | — |
| Net Asset Value, End of period^(c) | \$ 13.59 | \$ 12.96 | \$ 11.61 | \$ 11.50 | \$ 16.22 | \$ 15.07 |
| Total Return ^{(c)(d)} | 4.78% ^(e) | 12.23% | 0.96% | (26.03)% | 12.71% | 36.63% |
| Ratios to Average Net Assets/Supplemental Data:^{(e)(f)} | | | | | | |
| Net Assets, End of Period (000's) | \$12,710 | \$16,573 | \$30,967 | \$83,952 | \$179,486 | \$153,358 |
| Gross operating expenses ^(h) | 2.16% | 2.62% | 2.72% | 2.70% | 2.55% | 2.55% |
| Net investment loss | (1.17)% | (1.79)% | (1.82)% | (2.01)% | (2.09)% | (1.82)% |
| Portfolio turnover rate | 94% ^(g) | 489% | 964% | 901% | 409% | 538% |

(a) Per share data was calculated using average shares outstanding during the period.

(b) Represents less than \$0.005 per share.

(c) The Net Asset Value per share and total return have been calculated based on net assets which include adjustments made in accordance with U.S. Generally Accepted Accounting Principles required at period end for financial reporting purposes. These figures do not necessarily reflect the Net Asset Value per share or total return experienced by the shareholder at period end.

(d) Total return is at net asset value assuming all distributions are reinvested and no initial sales charge or CDSC. For periods with waivers/reimbursements, had the Fund's investment adviser not waived or reimbursed a portion of expenses, total return would have been lower.

(e) All ratios for the period have been annualized, unless otherwise indicated.

(f) Includes dividends and fees on securities sold short.

(g) Not annualized.

(h) Supplemental expense ratios are shown below:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Years Ended June 30, | | | | |
|--|---|------------------------------|-------|-------|-------|-------|
| | | 2018 | 2017 | 2016 | 2015 | 2014 |
| Net operating expenses (net of waiver/reimbursement, if applicable, but gross of all other operating expenses) | 2.16% | 2.62% | 2.72% | 2.70% | 2.55% | 2.55% |
| Interest expense and commitment fees | —% ⁽ⁱ⁾ | 0.32% | 0.01% | —% | —% | —% |
| Dividends and fees on securities sold short | 0.06% | 0.19% | 0.70% | 0.85% | 0.77% | 0.77% |

(i) Represents less than 0.005%.

FINANCIAL HIGHLIGHTS

Highland Long/Short Healthcare Fund, Class C

Selected data for a share outstanding throughout each period is as follows:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Years Ended June 30, | | | | |
|---|---|------------------------------|-------------|---------------|---------------|---------------------|
| | | 2018 | 2017 | 2016 | 2015 | 2014 |
| Net Asset Value, Beginning of Period | \$ 12.19 | \$ 10.94 | \$ 10.90 | \$ 15.48 | \$ 14.50 | \$ 10.68 |
| Income from Investment Operations: | | | | | | |
| Net investment loss ^(a) | (0.12) | (0.27) | (0.27) | (0.34) | (0.42) | (0.35) |
| Redemption fees added to paid-in capital | — | — | — | — | — | — ^{(a)(b)} |
| Net realized and unrealized gain (loss) ^(a) | <u>0.67</u> | <u>1.52</u> | <u>0.31</u> | <u>(3.66)</u> | <u>2.08</u> | <u>4.17</u> |
| Total from Investment Operations | 0.55 | 1.25 | 0.04 | (4.00) | 1.66 | 3.82 |
| Less Distributions Declared to shareholders: | | | | | | |
| From net realized gains | <u>—</u> | <u>—</u> | <u>—</u> | <u>(0.58)</u> | <u>(0.68)</u> | <u>—</u> |
| Total distributions declared to shareholders | — | — | — | (0.58) | (0.68) | — |
| Net Asset Value, End of period^(c) | \$ 12.74 | \$ 12.19 | \$ 10.94 | \$ 10.90 | \$ 15.48 | \$ 14.50 |
| Total Return ^{(c)(d)} | 4.43% ^(g) | 11.43% | 0.37% | (26.37)% | 12.02% | 35.77% |
| Ratios to Average Net Assets/Supplemental Data:^{(e)(f)} | | | | | | |
| Net Assets, End of Period (000's) | \$11,397 | \$13,300 | \$22,805 | \$55,381 | \$83,971 | \$47,964 |
| Gross operating expenses ^(h) | 2.81% | 3.28% | 3.37% | 3.38% | 3.29% | 3.25% |
| Net investment loss | (1.77)% | (2.45)% | (2.47)% | (2.66)% | (2.81)% | (2.51)% |
| Portfolio turnover rate | 94% ^(g) | 489% | 964% | 901% | 409% | 538% |

(a) Per share data was calculated using average shares outstanding during the period.

(b) Represents less than \$0.005 per share.

(c) The Net Asset Value per share and total return have been calculated based on net assets which include adjustments made in accordance with U.S. Generally Accepted Accounting Principles required at period end for financial reporting purposes. These figures do not necessarily reflect the Net Asset Value per share or total return experienced by the shareholder at period end.

(d) Total return is at net asset value assuming all distributions are reinvested and no initial sales charge or CDSC. For periods with waivers/reimbursements, had the Fund's investment adviser not waived or reimbursed a portion of expenses, total return would have been lower.

(e) All ratios for the period have been annualized, unless otherwise indicated.

(f) Includes dividends and fees on securities sold short.

(g) Not annualized.

(h) Supplemental expense ratios are shown below:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Years Ended June 30, | | | | |
|--|---|------------------------------|-------|-------|-------|-------|
| | | 2018 | 2017 | 2016 | 2015 | 2014 |
| Net operating expenses (net of waiver/reimbursement, if applicable, but gross of all other operating expenses) | 2.81% | 3.28% | 3.37% | 3.38% | 3.29% | 3.25% |
| Interest expense and commitment fees | —% ⁽ⁱ⁾ | 0.32% | 0.01% | —% | 0.01% | —% |
| Dividends and fees on securities sold short | 0.06% | 0.20% | 0.70% | 0.87% | 0.84% | 0.79% |

(i) Represents less than 0.005%.

FINANCIAL HIGHLIGHTS

Highland Long/Short Healthcare Fund, Class Z

Selected data for a share outstanding throughout each period is as follows:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Years Ended June 30, | | | | |
|---|---|------------------------------|-------------|---------------|---------------|---------------------|
| | | 2018 | 2017 | 2016 | 2015 | 2014 |
| Net Asset Value, Beginning of Period | \$ 13.41 | \$ 12.04 | \$ 11.87 | \$ 16.66 | \$ 15.40 | \$ 11.23 |
| Income from Investment Operations: | | | | | | |
| Net investment loss ^(a) | (0.06) | (0.19) | (0.18) | (0.23) | (0.30) | (0.22) |
| Redemption fees added to paid-in capital | — | — | — | — | — | — ^{(a)(b)} |
| Net realized and unrealized gain (loss) ^(a) | <u>0.73</u> | <u>1.69</u> | <u>0.35</u> | <u>(3.98)</u> | <u>2.24</u> | <u>4.39</u> |
| Total from Investment Operations | 0.67 | 1.50 | 0.17 | (4.21) | 1.94 | 4.17 |
| Less Distributions Declared to shareholders: | | | | | | |
| From net investment income | — | (0.13) | — | — | — | — |
| From net realized gains | <u>—</u> | <u>—</u> | <u>—</u> | <u>(0.58)</u> | <u>(0.68)</u> | <u>—</u> |
| Total distributions declared to shareholders | — | (0.13) | — | (0.58) | (0.68) | — |
| Net Asset Value, End of period^(c) | \$ 14.08 | \$ 13.41 | \$ 12.04 | \$ 11.87 | \$ 16.66 | \$ 15.40 |
| Total Return ^{(c)(d)} | 4.92% ^(g) | 12.58% | 1.43% | (25.75)% | 13.16% | 37.13% |
| Ratios to Average Net Assets/Supplemental Data:^{(e)(f)} | | | | | | |
| Net Assets, End of Period (000's) | \$24,040 | \$26,677 | \$53,839 | \$158,854 | \$454,021 | \$112,879 |
| Gross operating expenses ^(h) | 1.81% | 2.34% | 2.38% | 2.32% | 2.41% | 2.26% |
| Net investment loss | (0.76)% | (1.52)% | (1.49)% | (1.62)% | (1.90)% | (1.51)% |
| Portfolio turnover rate | 94% ^(g) | 489% | 964% | 901% | 409% | 538% |

(a) Per share data was calculated using average shares outstanding during the period.

(b) Represents less than \$0.005 per share.

(c) The Net Asset Value per share and total return have been calculated based on net assets which include adjustments made in accordance with U.S. Generally Accepted Accounting Principles required at period end for financial reporting purposes. These figures do not necessarily reflect the Net Asset Value per share or total return experienced by the shareholder at period end.

(d) Total return is at net asset value assuming all distributions are reinvested and no initial sales charge or CDSC. For periods with waivers/reimbursements, had the Fund's investment adviser not waived or reimbursed a portion of expenses, total return would have been lower.

(e) All ratios for the period have been annualized, unless otherwise indicated.

(f) Includes dividends and fees on securities sold short.

(g) Not annualized.

(h) Supplemental expense ratios are shown below:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Years Ended June 30, | | | | |
|--|---|------------------------------|-------|-------|-------|-------|
| | | 2018 | 2017 | 2016 | 2015 | 2014 |
| Net operating expenses (net of waiver/reimbursement, if applicable, but gross of all other operating expenses) | 1.81% | 2.34% | 2.38% | 2.32% | 2.41% | 2.26% |
| Interest expense and commitment fees | —% ⁽ⁱ⁾ | 0.32% | 0.01% | —% | 0.01% | —% |
| Dividends and fees on securities sold short | 0.06% | 0.26% | 0.70% | 0.82% | 0.96% | 0.80% |

(i) Represents less than 0.005%.

FINANCIAL HIGHLIGHTS

Highland Merger Arbitrage Fund, Class A

Selected data for a share outstanding throughout each period is as follows:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Year Ended June 30, 2018 ^(a) | For the Six Months Ended June 30, 2017 | For the Period Ended December 31 2016 ^(b) |
|---|---|---|--|--|
| Net Asset Value, Beginning of Period | \$20.75 | \$21.65 | \$20.53 | \$20.00 |
| Income from Investment Operations: | | | | |
| Net investment income (loss) ^(c) | 1.05 | (0.20) | 0.24 | (0.22) |
| Net realized and unrealized gain (loss) | <u>(0.41)</u> | <u>0.70</u> | <u>0.88</u> | <u>0.75</u> |
| Total from Investment Operations | 0.64 | 0.50 | 1.12 | 0.53 |
| Less Distributions Declared to shareholders: | | | | |
| From net investment income | (2.64) | (1.07) | — | — |
| From net realized gains | <u>(0.71)</u> | <u>(0.33)</u> | <u>—</u> | <u>—^(d)</u> |
| Total distributions declared to shareholders | (3.35) | (1.40) | — | — ^(d) |
| Net Asset Value, End of period^(e) | \$18.04 | \$20.75 | \$21.65 | \$20.53 |
| Total Return ^{(e)(f)} | 3.15% ⁽ⁱ⁾ | 2.53% | 5.46% | 2.66% |
| Ratios to Average Net Assets/Supplemental Data:^{(g)(h)} | | | | |
| Net Assets, End of Period (000's) | \$ 730 | \$1,019 | \$1,661 | \$ 121 |
| Gross operating expenses ⁽ⁱ⁾ | 5.33% | 4.77% | 6.40% | 7.16% |
| Net investment income (loss) | 9.96% | (0.98)% | 2.30% | (3.00)% |
| Portfolio turnover rate | 323% ⁽ⁱ⁾ | 401% | 233% ⁽ⁱ⁾ | 718% |

(a) For the year ended December 31, 2017, the Highland Merger Arbitrage Fund had a fiscal year end change from December 31 to June 30.

(b) Class commenced operations on August 19, 2016.

(c) Per share data was calculated using average shares outstanding during the period.

(d) Represents less than \$0.005 per share.

(e) The Net Asset Value per share and total return have been calculated based on net assets which include adjustments made in accordance with U.S. Generally Accepted Accounting Principles required at period end for financial reporting purposes. These figures do not necessarily reflect the Net Asset Value per share or total return experienced by the shareholder at period end.

(f) Total return is at net asset value assuming all distributions are reinvested and no initial sales charge or CDSC. For periods with waivers/reimbursements, had the Fund's investment adviser not waived or reimbursed a portion of expenses, total return would have been lower.

(g) All ratios for the period have been annualized, unless otherwise indicated.

(h) Includes dividends and fees on securities sold short.

(i) Not annualized.

(j) Supplemental expense ratios are shown below:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Year Ended June 30, 2018 ^(a) | For the Six Months Ended June 30, 2017 | For the Period Ended December 31 2016 ^(b) |
|--|---|---|--|--|
| Net operating expenses (net of waiver/reimbursement, if applicable, but gross of all other operating expenses) | 5.09% | 3.97% | 5.05% | 4.62% |
| Interest expense and commitment fees | —% | 0.65% | —% | 1.60% |
| Dividends and fees on securities sold short | 3.29% | 1.38% | 3.19% | 1.14% |

FINANCIAL HIGHLIGHTS

Highland Merger Arbitrage Fund, Class C

Selected data for a share outstanding throughout each period is as follows:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Year Ended June 30, 2018 ^(a) | For the Six Months Ended June 30, 2017 | For the Period Ended December 31 2016 ^(b) |
|---|---|---|--|--|
| Net Asset Value, Beginning of Period | \$20.65 | \$21.52 | \$20.48 | \$20.00 |
| Income from Investment Operations: | | | | |
| Net investment income (loss) ^(c) | 0.96 | (0.39) | 0.05 | (0.28) |
| Net realized and unrealized gain (loss) | <u>(0.40)</u> | <u>0.77</u> | <u>0.99</u> | <u>0.76</u> |
| Total from Investment Operations | 0.56 | 0.38 | 1.04 | 0.48 |
| Less Distributions Declared to shareholders: | | | | |
| From net investment income | (2.53) | (0.92) | — | — |
| From net realized gains | <u>(0.71)</u> | <u>(0.33)</u> | <u>—</u> | <u>—^(d)</u> |
| Total distributions declared to shareholders | (3.24) | (1.25) | — | — ^(d) |
| Net Asset Value, End of period^(e) | \$17.97 | \$20.65 | \$21.52 | \$20.48 |
| Total Return ^{(e)(f)} | 2.77% ⁽ⁱ⁾ | 1.95% | 5.08% | 2.41% |
| Ratios to Average Net Assets/Supplemental Data:^{(g)(h)} | | | | |
| Net Assets, End of Period (000's) | \$1,049 | \$1,321 | \$1,094 | \$ 96 |
| Gross operating expenses ^(j) | 5.88% | 5.51% | 7.28% | 8.15% |
| Net investment income (loss) | 9.15% | (1.88)% | 0.47% | (3.93)% |
| Portfolio turnover rate | 323% ⁽ⁱ⁾ | 401% | 233% ⁽ⁱ⁾ | 718% |

(a) For the year ended December 31, 2017, the Highland Merger Arbitrage Fund had a fiscal year end change from December 31 to June 30.

(b) Class commenced operations on August 19, 2016.

(c) Per share data was calculated using average shares outstanding during the period.

(d) Represents less than \$0.005 per share.

(e) The Net Asset Value per share and total return have been calculated based on net assets which include adjustments made in accordance with U.S. Generally Accepted Accounting Principles required at period end for financial reporting purposes. These figures do not necessarily reflect the Net Asset Value per share or total return experienced by the shareholder at period end.

(f) Total return is at net asset value assuming all distributions are reinvested and no initial sales charge or CDSC. For periods with waivers/reimbursements, had the Fund's investment adviser not waived or reimbursed a portion of expenses, total return would have been lower.

(g) All ratios for the period have been annualized, unless otherwise indicated.

(h) Includes dividends and fees on securities sold short.

(i) Not annualized.

(j) Supplemental expense ratios are shown below:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Year Ended June 30, 2018 ^(a) | For the Six Months Ended June 30, 2017 | For the Period Ended December 31 2016 ^(b) |
|--|---|---|--|--|
| Net operating expenses (net of waiver/reimbursement, if applicable, but gross of all other operating expenses) | 5.65% | 4.72% | 5.95% | 5.62% |
| Interest expense and commitment fees | —% | 0.65% | —% | 1.39% |
| Dividends and fees on securities sold short | 3.29% | 1.53% | 3.47% | 1.69% |

FINANCIAL HIGHLIGHTS

Highland Merger Arbitrage Fund, Class Z

Selected data for a share outstanding throughout each period is as follows:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Year Ended June 30, 2018 ^(a) | For the Six Months Ended June 30, 2017 | For the Period Ended December 31 2016 ^(b) |
|---|---|---|--|--|
| Net Asset Value, Beginning of Period | \$ 20.95 | \$ 21.76 | \$ 20.60 | \$ 20.05 |
| Income from Investment Operations: | | | | |
| Net investment income (loss) ^(c) | 1.11 | (0.18) | 0.19 | (0.12) |
| Net realized and unrealized gain (loss) | <u>(0.44)</u> | <u>0.77</u> | <u>0.97</u> | <u>0.67</u> |
| Total from Investment Operations | 0.67 | 0.59 | 1.16 | 0.55 |
| Less Distributions Declared to shareholders: | | | | |
| From net investment income | (2.75) | (1.07) | — | — |
| From net realized gains | <u>(0.71)</u> | <u>(0.33)</u> | <u>—</u> | <u>—^(d)</u> |
| Total distributions declared to shareholders | (3.46) | (1.40) | — | — ^(d) |
| Net Asset Value, End of period^(e) | \$ 18.16 | \$ 20.95 | \$ 21.76 | \$ 20.60 |
| Total Return ^{(e)(f)} | 3.28% ⁽ⁱ⁾ | 2.93% | 5.63% | 2.76% |
| Ratios to Average Net Assets/Supplemental Data:^{(g)(h)} | | | | |
| Net Assets, End of Period (000's) | \$24,974 | \$36,130 | \$27,291 | \$22,393 |
| Gross operating expenses ⁽ⁱ⁾ | 5.04% | 4.59% | 6.11% | 6.04% |
| Net investment income (loss) | 10.40% | (0.88)% | 1.84% | (1.68)% |
| Portfolio turnover rate | 323% ⁽ⁱ⁾ | 401% | 233% ⁽ⁱ⁾ | 718% |

(a) For the year ended December 31, 2017, the Highland Merger Arbitrage Fund had a fiscal year end change from December 31 to June 30.

(b) Class commenced operations on August 19, 2016.

(c) Per share data was calculated using average shares outstanding during the period.

(d) Represents less than \$0.005 per share.

(e) The Net Asset Value per share and total return have been calculated based on net assets which include adjustments made in accordance with U.S. Generally Accepted Accounting Principles required at period end for financial reporting purposes. These figures do not necessarily reflect the Net Asset Value per share or total return experienced by the shareholder at period end.

(f) Total return is at net asset value assuming all distributions are reinvested and no initial sales charge or CDSC. For periods with waivers/reimbursements, had the Fund's investment adviser not waived or reimbursed a portion of expenses, total return would have been lower.

(g) All ratios for the period have been annualized, unless otherwise indicated.

(h) Includes dividends and fees on securities sold short.

(i) Not annualized.

(j) Supplemental expense ratios are shown below:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Year Ended June 30, 2018 ^(a) | For the Six Months Ended June 30, 2017 | For the Period Ended December 31 2016 ^(b) |
|--|---|---|--|--|
| Net operating expenses (net of waiver/reimbursement, if applicable, but gross of all other operating expenses) | 4.80% | 3.80% | 4.75% | 3.50% |
| Interest expense and commitment fees | —% | 0.65% | —% | 0.84% |
| Dividends and fees on securities sold short | 3.29% | 1.63% | 3.22% | 1.14% |

FINANCIAL HIGHLIGHTS

Highland Opportunistic Credit Fund, Class A

Selected data for a share outstanding throughout each period is as follows:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Years Ended June 30, | | | |
|--|---|------------------------------|-------------|---------------|-------------------------|
| | | 2018 | 2017 | 2016 | 2015* |
| Net Asset Value, Beginning of Period | \$ 4.36 | \$ 4.22 | \$ 3.73 | \$ 5.30 | \$ 6.22 |
| Income from Investment Operations: | | | | | |
| Net investment income ^(a) | 0.07 | 0.30 | 0.38 | 0.53 | 0.24 |
| Net realized and unrealized gain (loss) | <u>(0.23)</u> | <u>0.11</u> | <u>0.48</u> | <u>(1.59)</u> | <u>(0.93)</u> |
| Total from Investment Operations | (0.16) | 0.41 | 0.86 | (1.06) | (0.69) |
| Less Distributions Declared to shareholders: | | | | | |
| From net investment income | (0.07) | (0.27) | (0.37) | (0.51) | (0.23) |
| From return of capital | <u>—</u> | <u>0.00^(g)</u> | <u>—</u> | <u>—</u> | <u>—</u> |
| Total distributions declared to shareholders | (0.07) | (0.27) | (0.37) | (0.51) | (0.23) |
| Net Asset Value, End of period^(b) | \$ 4.13 | \$ 4.36 | \$ 4.22 | \$ 3.73 | \$ 5.30 |
| Total Return ^{(b)(c)} | (3.65)% ^(d) | 10.21% | 23.79% | (19.68)% | (11.14)% ^(d) |
| Ratios to Average Net Assets/Supplemental Data:^(e) | | | | | |
| Net Assets, End of Period (000's) | \$3,689 | \$4,754 | \$8,527 | \$ 5,149 | \$ 7,730 |
| Gross operating expenses ^(f) | 2.26% | 1.74% | 1.94% | 2.14% | 2.30% |
| Net investment income | 3.17% | 7.01% | 9.15% | 13.06% | 4.43% |
| Portfolio turnover rate | 2% ^(d) | 42% | 113% | 83% | 41% ^(d) |

* Effective July 1, 2014, the Highland Opportunistic Credit Fund changed its fiscal year end from December 31 to June 30. Class A shares commenced operations on July 1, 2014.

(a) Per share data was calculated using average shares outstanding during the period.

(b) The Net Asset Value per share and total return have been calculated based on net assets which include adjustments made in accordance with U.S. Generally Accepted Accounting Principles required at period end for financial reporting purposes. These figures do not necessarily reflect the Net Asset Value per share or total return experienced by the shareholder at period end.

(c) Total return is at net asset value assuming all distributions are reinvested and no initial sales charge or CDSC. For periods with waivers/reimbursements, had the Fund's investment adviser not waived or reimbursed a portion of expenses, total return would have been lower.

(d) Not annualized.

(e) All ratios for the period have been annualized, unless otherwise indicated.

(f) Supplemental expense ratios are shown below:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Years Ended June 30, | | | |
|--|---|------------------------------|-------------------|-------|-------|
| | | 2018 | 2017 | 2016 | 2015* |
| Net operating expenses (net of waiver/reimbursement, if applicable, but gross of all other operating expenses) | 1.25% | 1.25% | 1.44% | 1.53% | 1.27% |
| Interest expense and commitment fees | —% | —% | —% ^(h) | 0.23% | —% |
| Dividends and fees on securities sold short | —% | —% | 0.06% | —% | —% |

(g) Represents less than \$0.005 per share.

(h) Represents less than 0.005%.

FINANCIAL HIGHLIGHTS

Highland Opportunistic Credit Fund, Class C

Selected data for a share outstanding throughout each period is as follows:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Years Ended June 30, | | | |
|--|---|------------------------------|-------------|---------------|-------------------------|
| | | 2018 | 2017 | 2016 | 2015* |
| Net Asset Value, Beginning of Period | \$ 4.38 | \$ 4.24 | \$ 3.75 | \$ 5.30 | \$ 6.22 |
| Income from Investment Operations: | | | | | |
| Net investment income ^(a) | 0.06 | 0.27 | 0.30 | 0.50 | 0.21 |
| Net realized and unrealized gain (loss) | <u>(0.24)</u> | <u>0.12</u> | <u>0.54</u> | <u>(1.58)</u> | <u>(0.93)</u> |
| Total from Investment Operations | (0.18) | 0.39 | 0.84 | (1.08) | (0.72) |
| Less Distributions Declared to shareholders: | | | | | |
| From net investment income | (0.05) | (0.25) | (0.35) | (0.47) | (0.20) |
| From return of capital | <u>—</u> | <u>0.00^(g)</u> | <u>—</u> | <u>—</u> | <u>—</u> |
| Total distributions declared to shareholders | (0.05) | (0.25) | (0.35) | (0.47) | (0.20) |
| Net Asset Value, End of period^(b) | \$ 4.15 | \$ 4.38 | \$ 4.24 | \$ 3.75 | \$ 5.30 |
| Total Return ^{(b)(c)} | (3.92)% ^(d) | 9.65% | 23.14% | (20.16)% | (11.61)% ^(d) |
| Ratios to Average Net Assets/Supplemental Data:^(e) | | | | | |
| Net Assets, End of Period (000's) | \$3,439 | \$3,562 | \$3,695 | \$ 344 | \$ 160 |
| Gross operating expenses ^(f) | 2.81% | 2.24% | 2.41% | 2.64% | 2.80% |
| Net investment income | 2.72% | 6.35% | 6.99% | 12.85% | 3.88% |
| Portfolio turnover rate | 2% ^(d) | 42% | 113% | 83% | 41% ^(d) |

* Effective July 1, 2014, the Highland Opportunistic Credit Fund changed its fiscal year end from December 31 to June 30. Class C shares commenced operations on July 1, 2014.

(a) Per share data was calculated using average shares outstanding during the period.

(b) The Net Asset Value per share and total return have been calculated based on net assets which include adjustments made in accordance with U.S. Generally Accepted Accounting Principles required at period end for financial reporting purposes. These figures do not necessarily reflect the Net Asset Value per share or total return experienced by the shareholder at period end.

(c) Total return is at net asset value assuming all distributions are reinvested and no initial sales charge or CDSC. For periods with waivers/reimbursements, had the Fund's investment adviser not waived or reimbursed a portion of expenses, total return would have been lower.

(d) Not annualized.

(e) All ratios for the period have been annualized, unless otherwise indicated.

(f) Supplemental expense ratios are shown below:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Years Ended June 30, | | | |
|--|---|------------------------------|-------------------|-------|-------|
| | | 2018 | 2017 | 2016 | 2015* |
| Net operating expenses (net of waiver/reimbursement, if applicable, but gross of all other operating expenses) | 1.75% | 1.76% | 1.91% | 2.03% | 1.77% |
| Interest expense and commitment fees | —% | —% | —% ^(h) | 0.23% | —% |
| Dividends and fees on securities sold short | —% | —% | 0.06% | —% | —% |

(g) Represents less than \$0.005 per share.

(h) Represents less than 0.005%.

FINANCIAL HIGHLIGHTS

Highland Opportunistic Credit Fund, Class Z

Selected data for a share outstanding throughout each period is as follows:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Years Ended June 30, | | | | For the Six Months Ended June 30, 2014** | For the Year Ended December 31, 2013** |
|--|---|------------------------------|---------------------|---------------------|---------------------|--|--|
| | | 2018 | 2017 | 2016 | 2015* | | |
| Net Asset Value, Beginning of Period | \$ 4.34 | \$ 4.20 | \$ 3.71 | \$ 5.30 | \$ 6.21 | \$ 6.04 | \$ 4.49 |
| Income from Investment Operations: | | | | | | | |
| Net investment income | 0.08 ^(a) | 0.30 ^(a) | 0.38 ^(a) | 0.54 ^(a) | 0.26 ^(a) | (0.05) | 0.05 |
| Net realized and unrealized gain (loss) | <u>(0.25)</u> | <u>0.13</u> | <u>0.49</u> | <u>(1.59)</u> | <u>(0.92)</u> | <u>0.22</u> | <u>1.50</u> |
| Total from Investment Operations | (0.17) | 0.43 | 0.87 | (1.05) | (0.66) | 0.17 | 1.55 |
| Less Distributions Declared to shareholders: | | | | | | | |
| From net investment income | (0.07) | (0.28) | (0.38) | (0.54) | (0.25) | — | — |
| From return of capital | <u>—</u> | <u>(0.01)</u> | <u>—</u> | <u>—</u> | <u>—</u> | <u>—</u> | <u>—</u> |
| Total distributions declared to shareholders | (0.07) | (0.29) | (0.38) | (0.54) | (0.25) | — | — |
| Net Asset Value, End of period^(b) | \$ 4.10 | \$ 4.34 | \$ 4.20 | \$ 3.71 | \$ 5.30 | \$ 6.21 | \$ 6.04 |
| Total Return ^{(b)(c)} | (3.49)% | 10.62% | 24.31% | (19.43)% | (10.63)% | 2.81% ^(d) | 34.52% |
| Ratios to Average Net Assets/Supplemental Data:^(e) | | | | | | | |
| Net Assets, End of Period (000's) | \$41,096 | \$50,850 | \$71,706 | \$53,977 | \$78,893 | \$2,721 | \$ 816 |
| Gross operating expenses ^(f) | 1.91% | 1.39% | 1.63% | 1.79% | 1.95% | 4.23% ^(f) | 8.52% ^(f) |
| Net investment income | 3.53% | 7.22% | 9.28% | 13.35% | 4.80% | (1.53)% | 0.93% |
| Portfolio turnover rate | 2% ^(d) | 42% | 113% | 83% | 41% | —% | —% |

* Effective July 1, 2014, the Highland Opportunistic Credit Fund changed its fiscal year end from December 31 to June 30.

** Historical data shown is that of the Highland Special Situations Fund, which reorganized into the Highland Opportunistic Credit Fund on July 1, 2014.

(a) Per share data was calculated using average shares outstanding during the period.

(b) The Net Asset Value per share and total return have been calculated based on net assets which include adjustments made in accordance with U.S. Generally Accepted Accounting Principles required at period end for financial reporting purposes. These figures do not necessarily reflect the Net Asset Value per share or total return experienced by the shareholder at period end.

(c) Total return is at net asset value assuming all distributions are reinvested and no initial sales charge or CDSC. For periods with waivers/reimbursements, had the Fund's investment adviser not waived or reimbursed a portion of expenses, total return would have been lower.

(d) Not annualized.

(e) All ratios for the period have been annualized, unless otherwise indicated.

(f) Supplemental expense ratios are shown below:

| | For the Six Months Ended December 31, 2018 (unaudited) | For the Years Ended June 30, | | | | For the Six Months Ended June 30, 2014** | For the Year Ended December 31, 2013** |
|---|---|------------------------------|-------------------|-------|-------|--|--|
| | | 2018 | 2017 | 2016 | 2015* | | |
| Net operating expenses (net of waiver/ reimbursement, if applicable, but gross of all other operating expenses) | 0.90% | 0.91% | 1.13% | 1.18% | 0.91% | 4.23% | 8.52% |
| Interest expense and commitment fees | —% | —% | —% ^(g) | 0.23% | —% | —% | —% |
| Dividends and fees on securities sold short | —% | —% | 0.06% | —% | —% | —% | —% |

(g) Represents less than 0.005%.

Note 1. Organization

Highland Funds I (the “Trust”) was organized as a Delaware statutory trust on February 28, 2006. The Trust is registered under the Investment Company Act of 1940, as amended (the “1940 Act”), as an open-end management investment company with five portfolios that were offered as of December 31, 2018, each of which is non-diversified. This report includes information for the six months ended December 31, 2018 for Highland Long/Short Equity Fund (the “Long/Short Equity Fund”), Highland Long/Short Healthcare Fund (the “Long/Short Healthcare Fund”), Highland Merger Arbitrage Fund (the “Merger Arbitrage Fund”), and Highland Opportunistic Credit Fund (the “Opportunistic Credit Fund”) (each a “Fund” and, collectively, the “Funds”). Highland/iBoxx Senior Loan ETF is reported separately.

On September 6, 2017, the Board of Trustees approved an agreement and plan of reorganization pursuant to which Highland Floating Rate Opportunities Fund, a previous series in the Trust, would re-domicile into the sole series of a newly-formed Massachusetts business trust, Highland Floating Rate Opportunities Fund II. The re-domiciling was effective on September 25, 2017.

Fund Shares

Each Fund is authorized to issue an unlimited number of transferable shares of beneficial interest with a par value of \$0.001 per share (each a “Share” and collectively, the “Shares”). Each Fund currently offers the following three share classes to investors, Class A, Class C, and Class Z Shares. Class A Shares are sold with a front-end sales charge. Class A and Class C Shares may be subject to a contingent deferred sales charge. Class Z Shares are sold only to certain eligible investors. Certain share classes have their own sales charge and bear class specific expenses, which include distribution fees and service fees.

Class A Shares are sold with a front-end sales charge. Maximum sales load imposed on purchases of Class A Shares (as a percentage of offering price) is as follows:

| Fund | % |
|----------------------------|------|
| Long/Short Equity Fund | 5.50 |
| Long/Short Healthcare Fund | 5.50 |
| Merger Arbitrage Fund | 5.50 |
| Opportunistic Credit Fund | 3.50 |

There is no front-end sales charge imposed on individual purchases of Class A Shares of \$500,000 or more. The front-end sales charge is also waived in other instances as described in the Funds’ prospectus. Purchases of \$500,000 or more of Class A Shares at net asset value (“NAV”) pursuant to a sales charge waiver are subject to a 1.00% contingent deferred sales charge (“CDSC”) if redeemed within one year

of purchase. Class C shares may be subject to a CDSC. The maximum CDSC imposed on redemptions of Class C Shares for all Funds is 1.00% within the first year of purchase and 0.00% thereafter.

No front-end or CDSCs are assessed by the Trust with respect to Class Z Shares of all Funds.

Note 2. Significant Accounting Policies

The following summarizes the significant accounting policies consistently followed by the Funds in the preparation of their financial statements.

Use of Estimates

The Funds are investment companies that apply the accounting and reporting guidance of Accounting Standards Codification Topic 946 applicable to investment companies. The Funds’ financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (“GAAP”), which require Highland Capital Management Fund Advisors, L.P. (the “Investment Adviser”) to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Changes in the economic environment, financial markets and any other parameters used in determining these estimates could cause actual results to differ materially.

Determination of Class Net Asset Values

Each Fund’s income, expenses (other than distribution fees and shareholder service fees) and realized and unrealized gains and losses are allocated proportionally each day among each Fund’s respective share classes based upon the relative net assets of each share class. Expenses of the Trust, other than those incurred by a specific Fund are allocated pro rata among the Funds and their share classes. Certain class specific expenses (such as distribution and shareholder service fees) are allocated to the class that incurs such expense.

Valuation of Investments

In computing the Funds’ net assets attributable to shares, securities with readily available market quotations on the New York Stock Exchange (NYSE), National Association of Securities Dealers Automated Quotation (NASDAQ) or other nationally recognized exchange, use the closing quotations on the respective exchange for valuation of those securities. Securities for which there are no readily available market quotations will be valued pursuant to policies adopted by the Funds’ Board of Trustees (the “Board”). Typically, such securities will be valued at the mean between the most recently

quoted bid and ask prices provided by the principal market makers. If there is more than one such principal market maker, the value shall be the average of such means. Securities without a sale price or quotations from principal market makers on the valuation day may be priced by an independent pricing service. Generally, the Funds' loan and bond positions are not traded on exchanges and consequently are valued based on a mean of the bid and ask price from the third-party pricing services or broker-dealer sources that the Investment Adviser has determined to have the capability to provide appropriate pricing services which have been approved by the Board.

Securities for which market quotations are not readily available, or for which the Funds have determined that the price received from a pricing service or broker-dealer is "stale" or otherwise does not represent fair value (such as when events materially affecting the value of securities occur between the time when market price is determined and calculation of the Funds' net asset value ("NAV"), will be valued by the Funds at fair value, as determined by the Board or its designee in good faith in accordance with procedures approved by the Board, taking into account factors reasonably determined to be relevant, including, but not limited to: (i) the fundamental analytical data relating to the investment; (ii) the nature and duration of restrictions on disposition of the securities; and (iii) an evaluation of the forces that influence the market in which these securities are purchased and sold. In these cases, the Funds' NAV will reflect the affected portfolio securities' fair value as determined in the judgment of the Board or its designee instead of being determined by the market. Using a fair value pricing methodology to value securities may result in a value that is different from a security's most recent sale price and from the prices used by other investment companies to calculate their NAVs. Determination of fair value is uncertain because it involves subjective judgments and estimates.

There can be no assurance that the Funds' valuation of a security will not differ from the amount that it realizes upon the sale of such security. Those differences could have a material impact to the Funds. The NAV shown in the Funds' financial statements may vary from the NAV published by each Fund as of its period end because portfolio securities transactions are accounted for on the trade date (rather than the day following the trade date) for financial statement purposes.

Fair Value Measurements

The Funds have performed an analysis of all existing investments and derivative instruments to determine the significance and character of inputs to their fair value determination. The levels of fair value inputs used to measure the Funds' investments are characterized into a fair

value hierarchy. Where inputs for an asset or liability fall into more than one level in the fair value hierarchy, the investment is classified in its entirety based on the lowest level input that is significant to that investment's valuation. The three levels of the fair value hierarchy are described below:

- Level 1* — Quoted unadjusted prices for identical instruments in active markets to which the Fund has access at the date of measurement;
- Level 2* — Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active, but are valued based on executed trades; broker quotations that constitute an executable price; and alternative pricing sources supported by observable inputs are classified within Level 2. Level 2 inputs are either directly or indirectly observable for the asset in connection with market data at the measurement date; and
- Level 3* — Model derived valuations in which one or more significant inputs or significant value drivers are unobservable. In certain cases, investments classified within Level 3 may include securities for which the Fund has obtained indicative quotes from broker-dealers that do not necessarily represent prices the broker may be willing to trade on, as such quotes can be subject to material management judgment. Unobservable inputs are those inputs that reflect the Fund's own assumptions that market participants would use to price the asset or liability based on the best available information.

The Investment Adviser has established policies and procedures, as described above and approved by the Board, to ensure that valuation methodologies for investments and financial instruments that are categorized within all levels of the fair value hierarchy are fair and consistent. A Pricing Committee has been established to provide oversight of the valuation policies, processes and procedures, and is comprised of personnel from the Investment Adviser and its affiliates. The Pricing Committee meets monthly to review the proposed valuations for investments and financial instruments and is responsible for evaluating the overall fairness and consistent application of established policies.

As of December 31, 2018, the Funds' investments consisted of senior loans, asset-backed securities, corporate bonds and notes, foreign bonds, sovereign bonds, claims, common stocks, preferred stocks, exchange-traded funds, other registered investment companies, cash equivalents, master limited partnerships, rights, warrants, securities sold short, futures, equity swaps, collateralized loan obligations and

NOTES TO FINANCIAL STATEMENTS (unaudited) (continued)

December 31, 2018

Highland Funds I

options. The fair value of the Funds' loans, bonds and asset-backed securities are generally based on quotes received from brokers or independent pricing services. Loans, bonds and asset-backed securities with quotes that are based on actual trades with a sufficient level of activity on or near the measurement date are classified as Level 2 assets. Loans, bonds and asset-backed securities that are priced using quotes derived from implied values, indicative bids, or a limited number of actual trades are classified as Level 3 assets because the inputs used by the brokers and pricing services to derive the values are not readily observable.

The fair value of the Funds' common stocks, preferred stocks, exchange-traded funds, other registered investment companies, master limited partnerships, rights, warrants and options that are not actively traded on national exchanges are generally priced using quotes derived from implied values, indicative bids, or a limited amount of actual trades and are classified as Level 3 assets because the inputs used by the brokers and pricing services to derive the values are not readily observable. Exchange-traded options are valued based on the last trade price on the primary exchange on which they trade. If an option does not trade, the mid-price,

The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities. Transfers in and out of the levels are recognized at the value at the end of the period. A summary of the inputs used to value each Fund's assets as of December 31, 2018 is as follows:

which is the mean of the bid and ask price, is utilized to value the option.

At the end of each calendar quarter, the Investment Adviser evaluates the Level 2 and 3 assets and liabilities for changes in liquidity, including but not limited to: whether a broker is willing to execute at the quoted price, the depth and consistency of prices from third party services, and the existence of contemporaneous, observable trades in the market. Additionally, the Investment Adviser evaluates the Level 1 and 2 assets and liabilities on a quarterly basis for changes in listings or delistings on national exchanges.

Due to the inherent uncertainty of determining the fair value of investments that do not have a readily available market value, the fair value of the Funds' investments may fluctuate from period to period. Additionally, the fair value of investments may differ significantly from the values that would have been used had a ready market existed for such investments and may differ materially from the values the Funds may ultimately realize. Further, such investments may be subject to legal and other restrictions on resale or otherwise less liquid than publicly traded securities.

| | Total value at December 31, 2018 | Level 1 Quoted Price | Level 2 Significant Observable Inputs | Level 3 Significant Unobservable Inputs |
|---------------------------------|-------------------------------------|----------------------------|--|--|
| Long/Short Equity Fund | | | | |
| Assets | | | | |
| Common Stocks ⁽¹⁾ | \$226,395,706 | \$226,395,706 | \$ — | \$ — |
| Registered Investment Companies | 11,185,194 | 11,185,194 | — | — |
| Purchased Put Options | 721,500 | 721,500 | — | — |
| Total Assets | 238,302,400 | 238,302,400 | — | — |
| Liabilities | | | | |
| Securities Sold Short | | | | |
| Exchange-Traded Funds | (21,412,080) | (21,412,080) | — | — |
| Common Stocks ⁽¹⁾ | (69,302,755) | (69,302,755) | — | — |
| Other Financial Instruments | | | | |
| Written Call Options | (721,500) | (721,500) | — | — |
| Total Liabilities | (91,436,335) | (91,436,335) | — | — |
| Total | \$146,866,065 | \$146,866,065 | \$ — | \$ — |

⁽¹⁾ See Investment Portfolio detail for industry breakout.

NOTES TO FINANCIAL STATEMENTS (unaudited) (continued)

December 31, 2018

Highland Funds I

| | Total value at December 31, 2018 | Level 1 Quoted Price | Level 2 Significant Observable Inputs | Level 3 Significant Unobservable Inputs |
|-----------------------------------|-------------------------------------|----------------------------|--|--|
| Long/Short Healthcare Fund | | | | |
| Assets | | | | |
| Common Stocks | | | | |
| Healthcare | | | | |
| Biotechnology | \$13,465,218 | \$13,465,218 | \$ — | \$ — |
| Healthcare Equipment | 856,808 | 856,808 | — | — |
| Healthcare Facilities | 514,200 | 514,200 | — | — |
| Healthcare Services | 3,373,700 | 3,373,700 | — | — |
| Healthcare Technology | 660,745 | 660,745 | — | — |
| Life Sciences Tools & Services | 3,120,320 | 3,120,320 | — | — |
| Managed Healthcare | 859,440 | 859,440 | — | — |
| Pharmaceuticals | 9,220,552 | 9,206,044 | — | 14,508 |
| Preferred Stock ⁽¹⁾ | 2,440,867 | — | — | 2,440,867 |
| Purchased Call Options | 1,549,375 | 1,549,375 | — | — |
| Registered Investment Companies | 100,000 | 100,000 | — | — |
| Warrants ⁽¹⁾ | 60,245 | — | 60,245 ⁽²⁾ | — |
| Rights ⁽¹⁾ | 992 | 992 | — | — |
| Cash Equivalents | 13,521,969 | 13,521,969 | — | — |
| Total Assets | 49,744,431 | 47,228,811 | 60,245 | 2,455,375 |
| Liabilities | | | | |
| Securities Sold Short | | | | |
| Common Stocks ⁽¹⁾ | (3,625,188) | (3,625,188) | — | — |
| Total Liabilities | (3,625,188) | (3,625,188) | — | — |
| Total | \$46,119,243 | \$43,603,623 | \$60,245 | \$2,455,375 |

⁽¹⁾ See Investment Portfolio detail for industry breakout.

⁽²⁾ This category includes securities with a value of zero.

| | Total value at December 31, 2018 | Level 1 Quoted Price | Level 2 Significant Observable Inputs | Level 3 Significant Unobservable Inputs |
|--|-------------------------------------|----------------------------|--|--|
| Merger Arbitrage Fund | | | | |
| Assets | | | | |
| Common Stocks ⁽¹⁾ | | | | |
| Common Stocks ⁽¹⁾ | \$14,608,616 | \$14,608,616 | \$ — | \$ — |
| Master Limited Partnerships ⁽¹⁾ | 6,366,800 | 6,366,800 | — | — |
| Other Financial Instruments | | | | |
| Swap Contracts Outstanding | 16,810 | — | 16,810 | — |
| Total Assets | 20,992,226 | 20,975,416 | 16,810 | — |
| Liabilities | | | | |
| Securities Sold Short | | | | |
| Common Stocks ⁽¹⁾ | (7,599,946) | (7,599,946) | — | — |
| Master Limited Partnership ⁽¹⁾ | (676,612) | (676,612) | — | — |
| Other Financial Instruments | | | | |
| Total Liabilities | (8,276,558) | (8,276,558) | — | — |
| Total | \$12,715,668 | \$12,698,858 | \$16,810 | \$ — |

⁽¹⁾ See Investment Portfolio detail for industry breakout.

NOTES TO FINANCIAL STATEMENTS (unaudited) (continued)

December 31, 2018

Highland Funds I

| | Total value at December 31, 2018 | Level 1 Quoted Price | Level 2 Significant Observable Inputs | Level 3 Significant Unobservable Inputs |
|--|-------------------------------------|----------------------------|--|--|
| Opportunistic Credit Fund | | | | |
| Assets | | | | |
| U.S. Senior Loans | | | | |
| Communication Services | \$ 913,695 | \$ — | \$ — | \$ 913,695 |
| Energy | 3,301,256 | — | 3,301,256 | — |
| Financial | 1,918,434 | — | 1,918,434 | — |
| Healthcare | 682,768 | — | 682,768 | — |
| Housing | 927,342 | — | 927,342 | — |
| Information Technology | 548,881 | — | 548,881 | — |
| Manufacturing | 636,967 | — | 636,967 | — |
| Media/Telecommunications | 1,690,975 | — | 1,690,975 | — |
| Oil & Gas | 812,617 | — | 812,617 | — |
| Retail | 3,970,299 | — | 3,970,299 | — |
| Service | 1,584,170 | — | 1,584,170 | — |
| Transportation | 606,075 | — | 606,075 | — |
| Utilities | 1,628,207 | — | 1,628,207 | — |
| Common Stocks | | | | |
| Communication Services | 1,417,167 | — | — | 1,417,167 |
| Energy | 83 | 83 | — | — |
| Financials | 1,173 | 1,173 | — | — |
| Information Technology | 906,025 | 906,025 | — | — |
| Materials | 4,613,308 | 3,322,998 | — | 1,290,310 |
| Media | 853,174 | 520,137 | — | 333,037 |
| Utilities | 3,290,941 | 3,290,941 | — | — ⁽²⁾ |
| Collateralized Loan Obligations | 2,151,354 | — | 2,151,354 | — |
| Corporate Bonds & Notes | | | | |
| Energy | 227,058 | — | 58,905 | 168,153 |
| Healthcare | 769,500 | — | 769,500 | — |
| Information Technology | — | — | — | — ⁽²⁾ |
| Utilities | 86,120 | — | 86,120 | — |
| Preferred Stocks ⁽¹⁾ | 1,010,000 | — | 1,010,000 | — |
| Registered Investment Companies | 753,227 | 753,227 | — | — |
| Rights | 187,421 | — | 187,421 | — |
| Warrants | | | | |
| Financial | 6 | — | 6 | — |
| Information Technology | 28,291 | — | 28,291 | — |
| Foreign Corporate Bonds & Notes ⁽¹⁾ | — | — | — | — ⁽²⁾ |
| Cash Equivalents | 12,455,304 | — | 12,455,304 | — |
| Total | \$47,971,838 | \$8,794,584 | \$35,054,892 | \$4,122,362 |

⁽¹⁾ See Investment Portfolio detail for industry breakout.

⁽²⁾ This category includes securities with a value of zero.

NOTES TO FINANCIAL STATEMENTS (unaudited) (continued)

December 31, 2018

Highland Funds I

The tables below set forth a summary of changes in the Long/Short Healthcare Fund, and the Opportunistic Credit Fund's assets measured at fair value using significant unobservable inputs (Level 3) for the six months ended December 31, 2018. The Long/Short Equity Fund and Merger Arbitrage Fund had no Level 3 assets as of December 31, 2018.

| | Balance as of June 30, 2018 | Transfers into Level 3 | Transfers out of Level 3 | Net Amortization (Accretion) of Premium/ (Discount) | Net Realized Gains/ (Losses) | Net Unrealized Gain/ (Losses) | Net Purchases | Net (Sales) | Balance as of December 31, 2018 | Change in Unrealized Appreciation (Depreciation) from Investments Held at December 31, 2018 |
|--|--------------------------------------|------------------------------|--------------------------------|---|---------------------------------------|--|------------------|----------------|--|---|
| Highland Long/Short Healthcare Fund | | | | | | | | | | |
| Common Stocks | | | | | | | | | | |
| Pharmaceuticals | \$ — | \$14,508 | \$ — | \$ — | \$ — | \$ — | \$ — | \$ — | \$ 14,508 | \$ — |
| Preferred Stock | | | | | | | | | | |
| Information Technology | 3,195,649 | — | — | — | — | (754,782) | — | — | 2,440,867 | (745,782) |
| Warrants | | | | | | | | | | |
| Biotechnology | 736,088 | — | (736,088) | — | — | — | — | — | — | — |
| Pharmaceuticals | 248,786 | — | (43,086) | — | (205,700) | — | — | — | — | — |
| Total | \$4,180,523 | \$14,508 | \$(779,174) | \$ — | \$(205,700) | \$(754,782) | \$ — | \$ — | \$2,455,375 | \$(745,782) |

| | Balance as of June 30, 2018 | Net Transfers into Level 3 | Net Transfers out of Level 3 | Accrued Discounts (Premiums) | Realized Gain (Loss) | Change in Unrealized Appreciation (Depreciation) | Net Purchases | Net (Sales) | Balance as of December 31, 2018 | Change in Unrealized Appreciation (Depreciation) from Investments Held at December 31, 2018 |
|--|--------------------------------------|-------------------------------------|---------------------------------------|------------------------------------|----------------------------|---|------------------|-------------------|--|---|
| Highland Opportunistic Credit Fund | | | | | | | | | | |
| U.S. Senior Loans | | | | | | | | | | |
| Communication Services | \$ 862,883 | \$ — | \$ — | \$(27) | \$— | \$ 807 | \$50,032 | \$ — | \$ 913,695 | \$ 807 |
| Common Stocks | | | | | | | | | | |
| Communication Services | 1,330,620 | — | — | — | — | 86,547 | — | — | 1,417,167 | 86,547 |
| Materials | 2,237,436 | — | — | — | — | (947,126) | — | — | 1,290,310 | (947,126) |
| Media | 372,856 | — | — | — | — | (39,819) | — | — | 333,037 | (39,819) |
| Utilities | 26,975 | — | — | — | — | 7,807 | — | (34,782) | — | 7,807 |
| Corporate Bonds & Notes | | | | | | | | | | |
| Energy | 168,153 | — | — | — | — | — | — | — | 168,153 | — |
| Foreign Corporate Bonds & Notes | | | | | | | | | | |
| Netherlands | — | — | — | — | — | — | — | — | — | — |
| Warrants | | | | | | | | | | |
| Information Technology | 36,498 | — | (28,291) | — | — | (8,207) | — | — | — | — |
| Total | \$5,035,421 | \$ — | \$(28,291) | \$(27) | \$— | \$(899,991) | \$50,032 | \$(34,782) | \$4,122,362 | \$(891,784) |

Investments designated as Level 3 may include assets valued using quotes or indications furnished by brokers which are based on models or estimates without observable inputs and may not be executable prices. In light of the developing market conditions, the Investment Adviser continues to search for observable data points and evaluate broker

quotes and indications received for portfolio investments. As a result, for the six months ended December 31, 2018, a net amount of \$28,291 of the Opportunistic Credit Fund's portfolio investments were transferred from Level 3 to Level 2. For the six months ended December 31, 2018, a net amount of \$779,174 of the Long/Short Healthcare's portfolio

NOTES TO FINANCIAL STATEMENTS (unaudited) (continued)

December 31, 2018

Highland Funds I

investments were transferred from Level 3 to Level 1. Determination of fair values is uncertain because it involves subjective judgments and estimates that are unobservable. Transfers from Level 2 to 3 were due to a decline in market activity (e.g. frequency of trades), which resulted in a reduction of available market inputs to determine price, and transfers from Level 3 to Level 2 were due to an increase in

market activity which resulted in an increase of available market inputs to determine price.

For the six months ended December 31, 2018, a net amount of \$14,508 was transferred from Level 2 to Level 3. Transfers from Level 2 to Level 3 were due to a decrease in observable pricing inputs as compared to the previous period.

The following is a summary of significant unobservable inputs used in the fair valuations of assets and liabilities categorized within Level 3 of the fair value hierarchy:

| Category | Market Value at 12/31/2018 | Valuation Technique | Unobservable Inputs | Input Value(s) |
|--|----------------------------|-------------------------|---------------------------------|-------------------|
| Highland Long/Short Healthcare Fund | | | | |
| Preferred Stock | 2,440,867 | Multiples Analysis | Multiple of NFY+2 Total Revenue | 1.25x - 1.75x |
| Common Stocks | 14,508 | Intrinsic | N/A | N/A |
| Total | \$2,455,375 | | | |
| Highland Opportunistic Credit Fund | | | | |
| U.S. Senior Loans | \$ 913,695 | Discounted Cash Flow | Discount Rate | 11.1% |
| | | | Spread Adjustment | 0.10% |
| Corporate Bonds | 168,153 | Liquidation Analysis | Claim Amount: Percent of Par | 6.9% |
| Common Stocks | 3,040,514 | Multiples Analysis | Unadjusted Price/MHz-PoP | \$0.12 - \$0.80 |
| | | | Risk Discount | 33.0% - 35.8% |
| | | | Multiple of EBITDA | 6.0x - 7.0x |
| | | Discounted Cash Flow | Discount Rate | 11.0% - 15.0% |
| | | | Terminal Multiple | 6.5x |
| | | Transaction Analysis | Multiple of EBITDA | 7.25x - 7.75x |
| | | Bid Indication of Value | Enterprise Value (\$mm) | \$720.0 - \$765.0 |
| | | Net Asset Value | N/A | N/A |
| Total | \$4,122,362 | | | |

The significant unobservable inputs used in the fair value measurement of the Long/Short Healthcare Fund's preferred stock securities are: multiple of revenue, discount rate, terminal multiple, weightings and volatility adjustment. Significant increases (decreases) in any of those inputs in isolation could result in a significantly lower (higher) fair value measurement.

The significant unobservable inputs used in the fair value measurement of the Opportunistic Credit Fund's bank loans securities are: spread adjustment and discount rate. Significant increases (decreases) in any of those inputs in isolation could result in a significantly lower (higher) fair value measurement.

The significant unobservable inputs used in the fair value measurement of the Opportunistic Credit Fund's common equity securities are: multiple of EBITDA, price/MHz-PoP multiple, risk discount, scenario probabilities, illiquidity discount, discount rate and terminal multiple. Significant increases (decreases) in any of those inputs in isolation could result in a significantly lower (higher) fair value measurement.

Generally, a change in the assumption used for the risk discount is accompanied by a directionally opposite change in the assumption for the price/MHz-PoP multiple.

Certain Illiquid Positions Classified as Level 3

As of December 31, 2018, the Long/Short Healthcare Fund held an investment in the preferred stock of Amino, Inc. ("Amino") valued at \$2,440,867, or 5.1% of net assets. Amino owns and operates a website that allows users to find doctors, compare experiences, and book an appointment in the United States. The preferred stock of Amino is valued using an independent third-party pricing service, and this value is determined using unobservable inputs. Please see the tables above for a description of these inputs.

As of December 31, 2018, the Opportunistic Credit Fund held an investment in the common shares of TerreStar Corporation ("TerreStar") valued at \$1,417,167, or 2.9% of net assets. TerreStar is a nonoperating company that does not currently generate revenue and which primarily derives its value from two spectrum frequencies, the license with respect to one of which was terminated by the FCC and is

being contested by TerreStar on technical and public policy grounds. TerreStar currently anticipates such contest may take between 12 to 30 months and expects deployment of its other spectrum asset to require a similar period of time. If TerreStar is ultimately unsuccessful in its efforts, the terminated license would not be reinstated and the value of the TerreStar equity would likely be materially negatively impacted. The fair valuation of TerreStar involves uncertainty as it is materially dependent on these estimates. With regard to the likelihood of TerreStar regaining the terminated license, the Investment Adviser assigned a high probability of success, based in part in consultation with outside experts. The shares of TerreStar are valued using an independent third-party pricing service, and this value is determined using unobservable inputs. Please see the tables above for a description of these inputs.

The Funds may hold other illiquid positions that are classified as Level 3 that are not described here. Please see Note 7 for additional disclosure of risks from investments in illiquid securities.

Security Transactions

Security transactions are accounted for on the trade date. Realized gains/(losses) on investments sold are recorded on the basis of the specific identification method for both financial statement and U.S. federal income tax purposes taking into account any foreign taxes withheld.

Income Recognition

Corporate actions (including cash dividends) are recorded on the ex-dividend date, net of applicable withholding taxes, except for certain foreign corporate actions, which are recorded as soon after ex-dividend date as such information becomes available and is verified. Interest income is recorded on the accrual basis.

Accretion of discount on taxable bonds and loans is computed to the call date, while amortization of premium on taxable bonds and loans is computed to the call or maturity date, whichever is shorter, both using the effective yield method. Withholding taxes on foreign dividends have been provided for in accordance with the Funds' understanding of the applicable country's tax rules and rates.

U.S. Federal Income Tax Status

Each Fund is treated as a separate taxpayer for U.S. federal income tax purposes. The Funds intend to qualify each year as a "regulated investment company" under Subchapter M of the Internal Revenue Code of 1986, as amended, and will distribute substantially all of their taxable income and gains, if any, for the tax year, and as such will not be subject to U.S. federal income taxes. In addition, the Funds intend to distribute, in each calendar year, all of their net investment

income, capital gains and certain other amounts, if any, such that the Funds should not be subject to U.S. federal excise tax. Therefore, no U.S. federal income or excise tax provisions are recorded.

The Investment Adviser has analyzed the Funds' tax positions taken on U.S. federal income tax returns for all open tax years (current and prior three tax years), and has concluded that no provision for U.S. federal income tax is required in the Funds' financial statements. The Funds' U.S. federal and state income and U.S. federal excise tax returns for tax years for which the applicable statutes of limitations have not expired are subject to examination by the Internal Revenue Service and state departments of revenue. Furthermore, the Investment Adviser of the Funds is also not aware of any tax positions for which it is reasonably possible that the total amounts of unrecognized tax benefits will significantly change in the next 12 months.

Distributions to Shareholders

The Long/Short Equity Fund, Long/Short Healthcare Fund and Merger Arbitrage Fund intend to pay distributions from net investment income, if any, on an annual basis. The Opportunistic Credit Fund intend to pay distributions from net investment income, if any, on a monthly basis.

Statement of Cash Flows

Information on financial transactions which have been settled through the receipt or disbursement of cash is presented in the Statement of Cash Flows. The cash amount shown in the Statement of Cash Flows is the amount included within each Fund's Statement of Assets and Liabilities and includes cash on hand at its custodian bank and/or sub-custodian bank(s) and investments in money market funds deemed to be cash equivalents, and does not include cash posted as collateral in a segregated account or with broker-dealers.

Cash & Cash Equivalents

The Funds consider liquid assets deposited with a bank and certain short-term debt instruments of sufficient credit quality with original maturities of three months or less to be cash equivalents. The Fund also considers money market instruments that invest in cash equivalents to be cash equivalents. These investments represent amounts held with financial institutions that are readily accessible to pay Fund expenses or purchase investments. Cash and cash equivalents are valued at cost plus accrued interest, which approximates market value. The value of cash equivalents denominated in foreign currencies is determined by converting to U.S. dollars on the date of this financial report.

Foreign Currency

Accounting records of the Funds are maintained in U.S. dollars. Foreign currencies, investments and other assets and liabilities denominated in foreign currencies are translated into U.S. dollars at exchange rates using the current 4:00 PM London Time Spot Rate. Fluctuations in the value of the foreign currencies and other assets and liabilities resulting from changes in exchange rates, between trade and settlement dates on securities transactions and between the accrual and payment dates on dividends, interest income and foreign withholding taxes, are recorded as unrealized foreign currency gains/(losses). Realized gains/(losses) and unrealized appreciation/ (depreciation) on investment securities and income and expenses are translated on the respective dates of such transactions. The effects of changes in foreign currency exchange rates on investments in securities are not segregated in the Statement of Operations from the effects of changes in market prices of those securities, but are included with the net realized and unrealized gain or loss on investment securities.

Securities Sold Short

The Funds may sell securities short. A security sold short is a transaction in which the Fund sells a security it does not own in anticipation that the market price of that security will decline. When the Fund sells a security short, it must borrow the security sold short from a broker-dealer and deliver it to the buyer upon conclusion of the transaction. A Fund may have to pay a fee to borrow particular securities and is often obligated to pay over any dividends or other payments received on such borrowed securities. In some circumstances, a Fund may be allowed by its prime broker to utilize proceeds from securities sold short to purchase additional investments, resulting in leverage. Securities and cash held as collateral for securities sold short are shown on the Investments Portfolios for each of the Funds. Cash held as collateral for securities sold short is classified as restricted cash on each Fund's Statement of Assets and Liabilities, as applicable. Restricted cash in the amounts of \$76,402,517, \$2,635,712 and \$11,146,037 were held with the broker for the Long/Short Equity Fund, Long/Short Healthcare Fund and Merger Arbitrage Fund, respectively. Additionally, securities valued at \$120,915,840, \$4,757,795 and \$7,739,806 were posted in the Long/Short Equity Fund, Long/Short Healthcare Fund and Merger Arbitrage Fund segregated accounts as collateral, respectively.

Other Fee Income

Fee income may consist of origination/closing fees, amendment fees, administrative agent fees, transaction break-up fees and other miscellaneous fees. Origination fees, amendment fees, and other similar fees are nonrecurring fee sources. Such fees are received on a transaction by transaction

basis and do not constitute a regular stream of income and are recognized when incurred.

Note 3. Derivative Transactions

The Funds are subject to equity securities risk, interest rate risk and currency risk in the normal course of pursuing their investment objectives. The Funds enter into derivative transactions for the purpose of hedging against the effects of changes in the value of portfolio securities due to anticipated changes in market conditions, to gain market exposure for residual and accumulating cash positions and for managing the duration of fixed income investments.

Futures Contracts

A futures contract represents a commitment for the future purchase or sale of an asset at a specified price on a specified date. The Funds may invest in interest rate, financial and stock or bond index futures contracts subject to certain limitations. The Funds invest in futures contracts to manage their exposure to the stock and bond markets and fluctuations in currency values. Buying futures tends to increase a Fund's exposure to the underlying instrument while selling futures tends to decrease a Fund's exposure to the underlying instrument, or economically hedge other Fund investments. With futures contracts, there is minimal counterparty credit risk to the Funds since futures contracts are exchange-traded and the exchange's clearinghouse, as counterparty to all traded futures, guarantees the futures against default. A Fund's risks in using these contracts include changes in the value of the underlying instruments, non-performance of the counterparties under the contracts' terms and changes in the liquidity of the secondary market for the contracts. Futures contracts are valued at the settlement price established each day by the board of trade or exchange on which they principally trade.

Upon entering into a financial futures contract, the Funds are required to pledge to the broker an amount of cash and/or other assets equal to a certain percentage of the contract amount, known as initial margin deposit. Subsequent payments, known as variation margins, are made or can be received by the Funds each day, depending on the daily fluctuation in the fair value of the underlying security. The Funds record an unrealized gain/(loss) equal to the daily variation margin. Should market conditions move unexpectedly, the Funds may not achieve the anticipated benefits of the futures contracts and may incur a loss. The Funds recognize a realized gain/(loss) on the expiration or closing of a futures contract.

During the six months ended December 31, 2018, the Long/Short Equity Fund and Merger Arbitrage Fund entered into futures transactions for the purpose of hedging against the effects of changes in the value of portfolio securities due to anticipated changes in market conditions, and to gain market

NOTES TO FINANCIAL STATEMENTS (unaudited) (continued)

December 31, 2018

Highland Funds I

exposure for residual and accumulating cash positions. Cash held as collateral for futures contracts classified as restricted cash.

For the six months ended December 31, 2018, the Long/Short Healthcare Fund and Opportunistic Credit Fund did not invest in futures contracts.

Options

The Funds may utilize options on securities or indices to varying degrees as part of their principal investment strategy. An option on a security is a contract that gives the holder of the option, in return for a premium, the right to buy from (in the case of a call) or sell to (in the case of a put) the writer of the option the security underlying the option at a specified exercise or “strike” price. The writer of an option on a security has the obligation upon exercise of the option to deliver the underlying security upon payment of the exercise price or to pay the exercise price upon delivery of the underlying security. The Funds may hold options, write option contracts, or both.

If an option written by a Fund expires unexercised, a Fund realizes on the expiration date a capital gain equal to the premium received by a Fund at the time the option was written. If an option purchased by a Fund expires unexercised, a Fund realizes a capital loss equal to the premium paid. Prior to the earlier of exercise or expiration, an exchange-traded option may be closed out by an offsetting purchase or sale of an option of the same series (type, underlying security, exercise price and expiration). There can be no assurance, however, that a closing purchase or sale transaction can be effected when a Fund desires. A Fund will realize a capital gain from a closing purchase transaction if the cost of the closing option is less than the premium received from writing the option, or, if the cost of the closing option is more than the premium received from writing the option, a capital loss. A Fund will realize a capital gain from a closing sale transaction if the premium received from the sale is more than the original premium paid when the option position was opened, or a capital loss, if the premium received from a sale is less than the original premium paid.

During the six months ended December 31, 2018, the Long/Short Equity Fund, the Long/Short Healthcare Fund and the Merger Arbitrage Fund had written options to provide leveraged short exposure, and purchased options to provide leveraged long exposure, to the underlying equity, which is consistent with the investment strategies of these Funds.

For the six months ended December 31, 2018, the Opportunistic Credit Fund did not invest or write in options.

Swap Contracts

The Funds may use swaps as part of its investment strategy or to manage its exposure to interest, commodity, and currency rates as well as adverse movements in the debt and equity markets. Swap agreements are privately negotiated in

the over-the-counter (“OTC”) market or may be executed in a multilateral or other trade facility platform, such as a registered exchange (“centrally cleared swaps”).

Total return swaps are agreements to exchange the return generated by one instrument for the return generated by another instrument; for example, the agreement to pay interest in exchange for a market or commodity-linked return based on a notional amount. To the extent the total return of the market or commodity-linked index exceeds the offsetting interest obligation, the Fund will receive a payment from the counterparty. To the extent it is less, the Fund will make a payment to the counterparty. Periodic payments received or made by the Fund are recorded in “Net realized gain (loss) on swap contracts” on the accompanying Statement of Operations and Changes in Net Assets as realized gains or losses, respectively. As of December 31, 2018, the Merger Arbitrage Fund was a party to open swap contracts having a net fair value of \$16,592.

For the six months ended December 31, 2018, the Long/Short Equity Fund, Long/Short Healthcare Fund and Opportunistic Credit Fund did not invest in swap contracts.

Additional Derivative Information

The Funds follow adopted amendments to authoritative guidance on disclosures about derivative instruments and hedging activities which require that the Funds disclose; a) how and why an entity uses derivative instruments; b) how derivative instruments and related hedged items are accounted for; c) how derivative instruments and related hedged items affect an entity’s financial position, financial performance and cash flows; and d) how the netting of derivatives subject to master netting arrangements (if applicable) affects the net exposure of the Funds related to the derivatives.

The fair value of derivative instruments on the Statement of Assets and Liabilities have the following risk exposure at December 31, 2018:

| Fund | Fair Value | |
|---------------------------------------|---------------------------|----------------------------|
| | Asset Derivative | Liability Derivative |
| Long/Short Equity Fund | | |
| Equity Price Risk | \$ 721,500 ⁽¹⁾ | \$(721,500) ⁽²⁾ |
| Long/Short Healthcare Fund | | |
| Equity Price Risk | 1,763,750 ⁽¹⁾ | (214,375) ⁽²⁾ |
| Highland Merger Arbitrage Fund | | |
| Equity Price Risk | 16,810 ⁽³⁾ | — ⁽³⁾ |

(1) Statement of Assets and Liabilities location: Investments, at value.

(2) Statement of Assets and Liabilities location: Written options contracts, at value.

(3) Statement of Assets and Liabilities location: Swaps, at value

NOTES TO FINANCIAL STATEMENTS (unaudited) (continued)

December 31, 2018

Highland Funds I

To reduce counterparty credit risk with respect to over-the-counter (“OTC”) transactions, the Funds have entered into master netting arrangements, established within the Funds’ International Swap and Derivatives Association, Inc. (“ISDA”) master agreements, which allows the Funds to make (or to have an entitlement to receive) a single net payment in the event of default (close-out netting) for outstanding payables and receivables with respect to certain OTC derivative positions in forward currency exchange contracts for each individual counterparty. In addition, the Funds may require that certain counterparties post cash and/or securities in collateral accounts to cover their net payment obligations for those derivative contracts subject to ISDA master agreements. If the counterparty fails to perform under these contracts and agreements, the cash and/or securities will be made available to the Funds.

Certain ISDA master agreements include credit related contingent features which allow counterparties to OTC derivatives to terminate derivative contracts prior to maturity in the event the Funds’ net assets decline by a stated percentage or the Funds fail to meet the terms of its ISDA master agreements, which would cause the Funds to accelerate payment of any net liability owed to the counterparty.

For financial reporting purposes, the Funds do not offset derivative assets and derivative liabilities that are subject to netting arrangements in the Statement of Assets and Liabilities. Bankruptcy or insolvency laws of a particular jurisdiction may impose restrictions on or prohibitions against the right of offset in bankruptcy, insolvency or other events.

Collateral terms are contract specific for OTC derivatives. For derivatives traded under an ISDA master agreement, the collateral requirements are typically calculated by netting the mark to market amount for each transaction under such agreement and comparing that to the value of any collateral currently pledged by the Fund or the Counterparty.

For financial reporting purposes, cash collateral that has been pledged to cover obligations of the Funds, if any, is reported in restricted cash on the Statement of Assets and Liabilities. Generally, the amount of collateral due from or to a party must exceed a minimum transfer amount threshold before a transfer has to be made. To the extent amounts due to the Funds from their counterparties are not fully collateralized, contractually or otherwise, the Funds bear the risk of loss from counterparty non-performance.

The following tables present derivative instruments that are subject to enforceable netting arrangements as of December 31, 2018:

| Fund | Gross Amounts Not Offset in the Statement of Assets and Liabilities | | | | |
|------------------------------|---|--|----------------------|--------------------------|------------|
| | Gross Amounts of Recognized Assets | Gross Amounts of Offset in the Statement of Assets & Liabilities | Financial Instrument | Cash Collateral Received | Net Amount |
| Merger Arbitrage Fund | | | | | |
| Swaps | \$16,810 | \$ — | \$16,810 | \$ — | \$16,810 |

The effect of derivative instruments on the Statement of Operations for the six months ended December 31, 2018, is as follows:

| Fund | Net Realized Gain/(Loss) on Derivatives | Net Change in Unrealized Appreciation/(Depreciation) on Derivatives |
|-----------------------------------|---|---|
| Long/Short Equity Fund | | |
| Equity Price Risk | \$2,790,709 ⁽¹⁾⁽²⁾⁽³⁾⁽⁴⁾ | \$(2,406,506) ⁽⁵⁾⁽⁶⁾⁽⁷⁾ |
| Long/Short Healthcare Fund | | |
| Equity Price Risk | 460,547 ⁽¹⁾⁽²⁾⁽³⁾ | 1,404,358 ⁽⁵⁾⁽⁶⁾ |
| Merger Arbitrage Fund | | |
| Equity Price Risk | (392,711) ⁽¹⁾⁽²⁾⁽³⁾⁽⁴⁾ | (717,398) ⁽⁵⁾⁽⁶⁾⁽⁷⁾ |

- (1) Statement of Operations location: Realized gain (loss) on investments from unaffiliated issuers. Purchased options only.
 (2) Statement of Operations location: Realized gain (loss) on written options contracts.

- (3) Statement of Operations location: Realized gain (loss) on swap contracts.
 (4) Statement of Operations location: Realized gain (loss) on futures contracts.
 (5) Statement of Operations location: Net increase (decrease) in unrealized appreciation (depreciation) on investments. Purchased options only.
 (6) Statement of Operations location: Net increase (decrease) in unrealized appreciation (depreciation) on written options contracts.
 (7) Statement of Operations location: Net increase (decrease) in unrealized appreciation (depreciation) on swap contracts.

NOTES TO FINANCIAL STATEMENTS (unaudited) (continued)

December 31, 2018

Highland Funds I

The average monthly volume of derivative activity for the six months ended December 31, 2018 is as follows:

| Fund | Units/ Contracts | Appreciation/ (Depreciation) |
|-----------------------------------|---------------------|---------------------------------|
| Long/Short Equity Fund | | |
| Purchased Options Contracts | 1,042 | \$ — |
| Futures Contracts ⁽¹⁾ | — | (2,538) |
| Swap Contracts | — | 1,913,121 |
| Written Options Contracts | 667 | — |
| Long/Short Healthcare Fund | | |
| Purchased Options Contracts | 2,250 | — |
| Written Options Contracts | 168 | — |
| Merger Arbitrage Fund | | |
| Purchased Options Contracts | 2,333 | — |
| Futures Contracts ⁽¹⁾ | — | 7,805 |
| Swap Contracts | — | (183,839) |
| Written Options Contracts | 2,333 | — |

⁽¹⁾ Futures Contracts average monthly volume is calculated using Appreciation/(Depreciation).

Note 4. Securities Lending

Each Fund may seek additional income by making secured loans of its portfolio securities through its custodian, State Street Bank and Trust Company (“State Street”). Such loans will be in an amount not greater than one-third of the value of the Fund’s total assets. State Street will charge a Fund fees based on a percentage of the securities lending income.

The Funds will receive collateral consisting of cash (U.S. and foreign currency), securities issued or guaranteed by the U.S. government or its agencies or instrumentalities, sovereign debt, convertible bonds, irrevocable bank letters of credit or such other collateral as may be agreed on by the parties to a securities lending arrangement, initially with a value of 102% or 105% of the market value of the loaned securities and thereafter maintained at a value of 100% of the market value of the loaned securities. If the collateral consists of non-cash collateral, the borrower will pay the Fund a loan premium fee. If the collateral consists of cash, State Street will reinvest the cash. Although voting rights, or rights to consent, with respect to the loaned securities pass to the borrower, the Fund will recall the loaned securities upon reasonable notice in order that the securities may be voted by the Fund if the holders of such securities are asked to vote upon or consent to matters materially affecting the investment. The Fund also may call such loans in order to sell the securities involved.

Securities lending transactions are entered into pursuant to Securities Loan Agreements (“SLA”), which provide the right, in the event of default (including bankruptcy or insolvency) for the non-defaulting party to liquidate the collateral and calculate a net exposure to the defaulting party or request additional collateral. In the event that a borrower defaults,

the Funds, as lenders, would offset the market value of the collateral received against the market value of the securities loaned. The value of the collateral is typically greater than that of the market value of the securities loaned, leaving the lender with a net amount payable to the defaulting party. However, bankruptcy or insolvency laws of a particular jurisdiction may impose restrictions on or prohibitions against such a right of offset in the event of a SLA counterparty’s bankruptcy or insolvency. Under the SLA, the Funds can reinvest cash collateral, or, upon an event of default, resell or repledge the collateral, and the borrower can resell or repledge the loaned securities. The risks of securities lending also include the risk that the borrower may not provide additional collateral when required or may not return the securities when due. To mitigate this risk, each Fund benefits from a borrower default indemnity provided by State Street Bank and Trust Company (“State Street”). State Street’s indemnity generally provides for replacement of securities lent or the approximate value thereof.

The following table presents financial instruments that are subject to enforceable netting arrangements as of December 31, 2018:

| Fund | Gross Amounts of Liabilities Presented in Statement of Assets & Liabilities ⁽¹⁾ | Financial Instrument ⁽²⁾ | Collateral Received | Net Amount (not less than 0) |
|----------------------------|--|-------------------------------------|---------------------|------------------------------|
| Long/Short Equity Fund | \$4,387,313 | \$14,582,940 | \$ — | \$ — |
| Long/Short Healthcare Fund | 100,000 | 5,148,783 | — | — |
| Opportunistic Credit Fund | 753,227 | 1,639,466 | — | — |

⁽¹⁾ In some instances, the actual collateral received and/or pledged may be more than the amount shown here due to overcollateralization.

⁽²⁾ Represents market value of securities on loan at period end.

For the six months ended December 31, 2018, the market value of securities loaned and the amounts secured with cash and securities collateral, which are included on each Fund’s Investment Portfolio were as follows:

| Fund | Security Lending Market Value | Security Lending Collateral Cash Collateral ⁽¹⁾ | Security Lending Collateral Non-Cash Collateral ⁽²⁾ |
|----------------------------|-------------------------------|--|--|
| Long/Short Equity Fund | \$14,582,940 | \$4,387,313 | \$10,195,627 |
| Long/Short Healthcare Fund | 5,148,783 | 100,000 | 5,048,783 |
| Opportunistic Credit Fund | 1,639,466 | 753,227 | 917,933 |

⁽¹⁾ The loaned securities were secured with cash collateral which was invested in the State Street Navigator Securities Lending Government Money Market Portfolio.

⁽²⁾ Security lending non-cash collateral consists of U.S. Treasuries and Common Stock.

NOTES TO FINANCIAL STATEMENTS (unaudited) (continued)

December 31, 2018

Highland Funds I

Note 5. U.S. Federal Income Tax Information

The character of income and gains to be distributed is determined in accordance with income tax regulations which may differ from U.S. GAAP. These differences include (but are not limited to) investments organized as partnerships for tax purposes, foreign taxes, investments in futures, losses deferred to off-setting positions, tax treatment of organizational start-up costs, losses deferred due to wash sale transactions, tax treatment of net investment loss and distributions in excess of net investment income, dividends deemed paid upon shareholder redemption of Fund shares and tax attributes from Fund reorganizations. Reclassifications are made to the Funds' capital accounts to reflect income and gains available for distribution (or available capital loss carryovers) under income tax regulations. These reclassifications have no impact on net investment income, realized gains or losses, or NAV of the Funds. The

calculation of net investment income per share in the Financial Highlights table excludes these adjustments.

As of June 30, 2018, permanent differences chiefly resulting from net investment losses, non-deductible excise taxes paid, partnership-basis adjustments, return of capital distributions, dividends on short sales, foreign currency gains and losses, equalization, short sale holding period reclass, capital loss carryover write-offs and REITs were identified and reclassified among the components of the Funds' net assets as follows:

| | Distributable Earnings (Loss) | Paid-in-Capital |
|----------------------------|-------------------------------|-----------------|
| Long/Short Equity Fund | \$(5,489,068) | \$ 5,489,068 |
| Long/Short Healthcare Fund | 2,215,143 | (2,215,143) |
| Merger Arbitrage Fund | 668 | (668) |
| Opportunistic Credit Fund | 780,908 | (780,908) |

At June 30, 2018, the Funds' most recent tax year end, components of distributable earnings on a tax basis is as follows:

| | Undistributed Income | Other Temporary Differences ⁽¹⁾ | Accumulated Capital and Other Losses | Net Tax Appreciation/Depreciation ⁽²⁾ |
|----------------------------|----------------------|--|--------------------------------------|--|
| Long/Short Equity Fund | \$19,231,660 | \$ — | \$ 3,269,582 | \$12,166,803 |
| Long/Short Healthcare Fund | — | (37,213) | (194,604,078) | 2,290,367 |
| Merger Arbitrage Fund | 825,858 | — | 65,712 | (194,003) |
| Opportunistic Credit Fund | — | 508 | (13,736,005) | (8,512,972) |

⁽¹⁾ Other temporary differences are comprised of dividends payable, organizational expenses, partnership adjustments and default loan market discounts.

⁽²⁾ Any differences between book-basis and tax-basis net unrealized appreciation/(depreciation) are primarily due to deferral of losses from wash sales and other adjustments.

At June 30, 2018, the Long/Short Healthcare Fund and the Opportunistic Credit Fund had capital loss carryovers as indicated below. The capital loss carryovers are available to offset future realized capital gains to the extent provided in the Code and regulations promulgated thereunder. To the extent that these carryover losses are used to offset future capital gains, it is probable that the gains so offset will not be distributed to shareholders because they would be taxable as ordinary income.

| Fund | 2019 | No Expiration Short-Term ⁽¹⁾ | No Expiration Long-Term ⁽¹⁾ | Total |
|----------------------------|------|---|--|---------------|
| Long/Short Healthcare Fund | \$ — | \$173,379,291 | \$19,280,615 | \$192,659,906 |
| Opportunistic Credit Fund | — | 3,551,182 ⁽²⁾ | 9,715,602 ⁽²⁾ | 13,266,784 |

⁽¹⁾ On December 22, 2010, the Regulated Investment Company Modernization Act of 2010 (the "Modernization Act") was signed into law. The Modernization Act modifies several of the Federal income and excise tax provisions related to RICs. Under the Modernization Act, new capital losses may now be carried forward indefinitely, and retain the character of the original loss as compared with pre-enactment law where capital losses could be carried forward for eight years, and carried forward as short-term capital losses, irrespective of the character of the original loss.

⁽²⁾ These capital loss carry forward amounts were limited due to an ownership change and are available to offset future capital gains of the Opportunistic Credit Fund. The Fund's ability to utilize the capital loss carry forwards is limited under Internal Revenue Service Regulations.

For the year ended June 30, 2018, there were no capital loss carryforwards for the Long/Short Equity Fund and the Merger Arbitrage Fund.

During the year ended June 30, 2018, \$780,886 in capital loss carryforwards expired for Opportunistic Credit Fund.

NOTES TO FINANCIAL STATEMENTS (unaudited) (continued)

December 31, 2018

Highland Funds I

The tax character of distributions paid during the years ended June 30, 2018 and June 30, 2017 (unless otherwise indicated) is as follows:

| | Distributions | Return of Capital |
|----------------------------|---------------|-------------------|
| Long/Short Equity Fund | | |
| 2018 | \$9,948,413 | \$ — |
| 2017 | — | — |
| Long/Short Healthcare Fund | | |
| 2018 | 568,894 | — |
| 2017 | — | — |
| Merger Arbitrage Fund | | |
| 2018 | 2,350,079 | — |
| 2017 | — | — |
| Opportunistic Credit Fund | | |
| 2018 | 4,449,935 | 79,563 |
| 2017 | 6,968,664 | — |

Unrealized appreciation and depreciation at December 31, 2018, based on cost of investments for U.S. federal income tax purposes was:

| | Gross Appreciation | Gross Depreciation | Net Appreciation/ (Depreciation) | Federal Tax Cost (\$ Thousands) |
|----------------------------|--------------------|--------------------|----------------------------------|---------------------------------|
| Long/Short Equity Fund | \$4,241,063 | \$(18,871,697) | \$(14,630,634) | \$252,933,034 |
| Long/Short Healthcare Fund | 2,969,629 | (5,911,756) | (2,942,127) | 52,686,558 |
| Merger Arbitrage Fund | 52,663 | (356,027) | (303,364) | 23,808,815 |
| Opportunistic Credit Fund | 1,118,781 | (9,998,463) | (8,879,682) | 56,851,520 |

Qualified Late Year Ordinary and Post October Losses

Under current laws, certain capital losses realized after October 31 may be deferred (and certain ordinary losses after January 1st may be deferred) and treated as occurring on the first day of the following fiscal year. For the fiscal year ended June 30, 2018, the Funds elected to defer the following losses incurred from November 1, 2017 through June 30, 2018:

| Fund | Realized Capital Losses | Ordinary Losses |
|----------------------------|-------------------------|-----------------|
| Long/Short Healthcare Fund | \$(1,178,198) | \$(765,974) |
| Opportunistic Credit Fund | (468,567) | (654) |

Note 6. Advisory, Administration, Service and Distribution, Trustee, and Other Fees

Investment Advisory Fees and Sub-Advisory Fees

For its investment advisory and sub-advisory services, each Fund pays the Investment Adviser a monthly fee, computed and accrued daily, based on an annual rate of the Funds' Average Daily Managed Assets. Average Daily Managed Assets of a Fund means the average daily value of the total assets of a Fund less all accrued liabilities of a Fund (other

than the aggregate amount of any outstanding borrowings constituting financial leverage).

The table below shows each Fund's contractual advisory fee with the Investment Adviser for the six months ended December 31, 2018:

| Fund | Annual Fee Rate to the Investment Adviser |
|----------------------------|---|
| Long/Short Equity Fund | 2.25% |
| Long/Short Healthcare Fund | 1.00% |
| Merger Arbitrage Fund | 1.20% |
| Opportunistic Credit Fund | 1.00% |

Administration Fees

HCMFA provides administration services to the Long/Short Equity Fund and Long/Short Healthcare Fund for a monthly administration fee. For its services, the Investment Adviser receives a monthly administration fee, computed and accrued daily, at the annual rate of 0.20% of each Fund's Average Daily Managed Assets from each Fund. Under a separate sub-administration agreement, HCMFA delegates certain administrative functions and pays the sub-administrator a portion of the fees it receives from each

NOTES TO FINANCIAL STATEMENTS (unaudited) (continued)

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Highland Funds I

Fund. Effective October 1, 2018, HCMFA entered into an administrative services agreement with SEI Investments Global Funds Services (“SEI”), a wholly owned subsidiary of SEI Investments Company. Prior to October 1, 2018, State Street served as sub-administrator to each Fund. Effective October 1, 2018, SEI also provides administration services to the Opportunistic Credit Fund and Merger Arbitrage Fund for a monthly administration fee. Prior to October 1, 2018, State Street provided administration services to the Opportunistic Credit Fund and Merger Arbitrage Fund for a monthly administration fee.

Service and Distribution Fees

Highland Capital Funds Distributor, Inc. (formerly, Foreside Funds Distributors LLC (the “Underwriter”), serves as the principal underwriter and distributor of each Fund’s shares. The Underwriter receives the front-end sales charge imposed on the sale of Class A Shares and the contingent deferred sales charge (“CDSC”) imposed on certain redemptions of Class A and Class C Shares. For the six months ended December 31, 2018, the Underwriter received \$2,506, \$2,673, \$29 and \$699 of front end sales charges for Class A Shares of the Long/Short Equity Fund, the Long/Short Healthcare Fund, the Merger Arbitrage Fund, and the Opportunistic Credit Fund, respectively. The Underwriter also received _____ for Class C Shares of the Long/Short Equity Fund, the Long/Short Healthcare Fund, the Merger Arbitrage Fund and the Opportunistic Credit Fund, respectively.

The Funds have adopted a plan pursuant to Rule 12b-1 under the 1940 Act (the “Plan”) for Class A Shares and Class C Shares of the Funds, which requires the payment of a monthly fee to the Underwriter at an annual rate of the average daily net assets of each class as follows:

| Fund | Class A Shares | Class C Shares |
|----------------------------|----------------|----------------|
| Long/Short Equity Fund | 0.35% | 1.00% |
| Long/Short Healthcare Fund | 0.35% | 1.00% |
| Merger Arbitrage Fund | 0.35% | 1.00% |
| Opportunistic Credit Fund | 0.35% | 0.85% |

For the six months ended December 31, 2018, the Distribution and Service fees, which are included on the Statement of Operations for each class, were as follows:

| Fund | Class A Fees | Class C Fees |
|----------------------------|--------------|--------------|
| Long/Short Equity Fund | \$42,607 | \$97,543 |
| Long/Short Healthcare Fund | 26,496 | 65,671 |
| Merger Arbitrage Fund | 1,716 | 6,157 |
| Opportunistic Credit Fund | 7,677 | 15,420 |

Expense Limits and Fee Reimbursements

For the Long/Short Equity Fund, the Investment Adviser contractually agreed to waive a portion of its advisory fee in

an amount equal to 1.25% of the Fund’s Average Daily Managed Assets. This waiver will continue through at least October 31, 2019 and may not be terminated prior to this date without the action or consent of the Board of Trustees.

For Merger Arbitrage Fund, the Investment Adviser contractually agreed to limit the total annual operating expenses (exclusive of fees paid by the Fund pursuant to its distribution plan under Rule 12b-1 under the Investment Company Act of 1940, taxes, dividend expenses on short sales, interest payments, brokerage commissions and other transaction costs, acquired fund fees and expenses, and extraordinary expenses (collectively, the “Excluded Expenses”)) to 1.50% of average daily net assets of the Fund (the “Expense Cap”). The Expense Cap will continue through at least October 31, 2019, and may not be terminated prior to this date without the action or consent of the Board of Trustees. Under the expense limitation agreement, the Investment Adviser may recoup waived and/or reimbursed amounts with respect to the Fund within thirty-six months of the date such amounts were waived or reimbursed, provided the Fund’s total annual operating expenses, including such recoupment, do not exceed the Expense Cap in effect at the time of such waiver/ reimbursement.

For Opportunistic Credit Fund, the Investment Adviser has contractually agreed to limit the total annual operating expenses (exclusive of fees paid by the Fund pursuant to its Plan, taxes, dividend expenses on short sales, interest payments, brokerage commissions and other transaction costs, acquired fund fees and expenses, and extraordinary expenses to 0.90% of average daily net assets of the Fund (the “HOFC Expense Cap”). The HOFC Expense Cap will continue through at least October 31, 2019, and may not be terminated prior to this date without the action or consent of the Board of Trustees. Under the expense limitation agreement, the Investment Adviser may recoup waived and/or reimbursed amounts with respect to the Fund within thirty-six months of the date such amounts were waived or reimbursed, provided the Fund’s total annual operating expenses, including such recoupment, do not exceed the HOFC Expense Cap in effect at the time of such waiver/ reimbursement.

There can be no assurance that these fee reductions will be sufficient to avoid any loss. On December 31, 2018, the amounts subject to possible future recoupment under the Funds’ expense limitations were as follows:

| | Fiscal Years Ended June 30, | | | |
|---------------------------|-----------------------------|-----------|-----------|-----------|
| | 2019 | 2020 | 2021 | 2022 |
| Merger Arbitrage Fund | \$ — | \$385,547 | \$282,878 | \$ 45,701 |
| Opportunistic Credit Fund | 175,142 | 377,527 | 320,810 | 283,711 |

During the six months ended December 31, 2018, the Investment Adviser did not recoup any amounts previously waived or reimbursed and \$213,080 of fees of the Opportunistic Credit Fund previously waived and or reimbursed by the Investment Adviser that were eligible for recoupment expired.

Fees Paid to Officers and Trustees

Each Trustee who is not an “interested person” of the Funds as defined in the 1940 Act (the “Independent Trustees”) receives an annual retainer of \$150,000 payable in quarterly installments and allocated among each portfolio in the Highland Fund Complex overseen by such Trustee based on relative net assets. The “Highland Fund Complex” consists of all of the registered investment companies advised by the Investment Adviser or its affiliated advisers and NexPoint Capital, Inc., a closed-end management investment company that has elected to be treated as a business development company under the 1940 Act as of the date of this report.

The Funds pay no compensation to their officers, all of whom are employees of the Investment Adviser or one of its affiliates.

Indemnification

Under the Fund’s organizational documents, the officers and Trustees have been granted certain indemnification rights against certain liabilities that may arise out of performance of their duties to the Fund. Additionally, in the normal course of business, the Fund may enter into contracts with service providers that contain a variety of indemnification clauses. The Fund’s maximum exposure under these arrangements is dependent on future claims that may be made against the Fund and, therefore, cannot be estimated.

Note 7. Disclosure of Significant Risks and Contingencies

The primary risks of investing in the Funds are described below in alphabetical order:

Counterparty Risk

Counterparty risk is the potential loss the Funds may incur as a result of the failure of a counterparty or an issuer to make payments according to the terms of a contract. Counterparty risk is measured as the loss the Funds would record if its counterparties failed to perform pursuant to the terms of their obligations to the Funds. Because the Funds may enter into over-the-counter forwards, options, swaps and other derivative financial instruments, the Funds may be exposed to the credit risk of their counterparties. To limit the counterparty risk associated with such transactions, the Funds conduct business only with financial institutions judged by the Investment Adviser to present acceptable credit risk.

Credit Risk

Investments rated below investment grade are commonly referred to as high-yield, high risk or “junk debt.” They are regarded as predominantly speculative with respect to the issuing company’s continuing ability to meet principal and/or interest payments. Investments in high yield debt and high yield Senior Loans may result in greater NAV fluctuation than if a Fund did not make such investments.

Corporate debt obligations, including Senior Loans, are subject to the risk of non-payment of scheduled interest and/or principal. Non-payment would result in a reduction of income to a Fund, a reduction in the value of the corporate debt obligation experiencing non-payment and a potential decrease in the NAV of the Fund.

Currency Risk

A portion of the Funds’ assets may be quoted or denominated in non-U.S. currencies. These securities may be adversely affected by fluctuations in relative currency exchange rates and by exchange control regulations. The Funds’ investment performance may be negatively affected by a devaluation of a currency in which the Funds’ investments are quoted or denominated. Further, the Funds’ investment performance may be significantly affected, either positively or negatively, by currency exchange rates because the U.S. dollar value of securities quoted or denominated in another currency will increase or decrease in response to changes in the value of such currency in relation to the U.S. dollar.

Derivatives Risk

Derivatives risk is a combination of several risks, including the risks that: (1) an investment in a derivative instrument may not correlate well with the performance of the securities or asset class to which the Fund seeks exposure, (2) derivative contracts, including options, may expire worthless and the use of derivatives may result in losses to the Fund, (3) a derivative instrument entailing leverage may result in a loss greater than the principal amount invested, (4) derivatives not traded on an exchange may be subject to credit risk, for example, if the counterparty does not meet its obligations (see also “Counterparty Risk”), and (5) derivatives not traded on an exchange may be subject to liquidity risk and the related risk that the instrument is difficult or impossible to value accurately. As a general matter, when the Fund establishes certain derivative instrument positions, such as certain futures, options and forward contract positions, it will segregate liquid assets (such as cash, U.S. Treasury bonds or commercial paper) equivalent to the Fund’s outstanding obligations under the contract or in connection with the position. In addition, changes in laws or regulations may make the use of derivatives more costly, may limit the

availability of derivatives, or may otherwise adversely affect the use, value or performance of derivatives. A Fund's ability to pursue its investment strategy, including its strategy of investing in certain derivative instruments, may be limited to or adversely affected by the Fund's intention to qualify as a regulated investment company, and its strategy may bear adversely on its ability to so qualify.

Distressed and Defaulted Securities Risk

The Funds may invest in companies that are troubled, in distress or bankrupt. As such, they are subject to a multitude of legal, industry, market, environmental and governmental forces that make analysis of these companies inherently difficult. Further, the Investment Adviser relies on company management, outside experts, market participants and personal experience to analyze potential investments for the Funds. There can be no assurance that any of these sources will prove credible, or that the resulting analysis will produce accurate conclusions.

Hedging Risk

Each Fund may engage in "hedging," the practice of attempting to offset a potential loss in one position by establishing an opposite position in another investment. Hedging strategies in general are usually intended to limit or reduce investment risk, but can also be expected to limit or reduce the potential for profit. For example, if the Fund has taken a defensive posture by hedging its portfolio, and stock prices advance, the return to investors will be lower than if the portfolio had not been hedged. No assurance can be given that any particular hedging strategy will be successful, or that the Investment Adviser will elect to use a hedging strategy at a time when it is advisable.

Illiquid and Restricted Securities Risk

The investments made by the Funds may be illiquid, and consequently the Funds may not be able to sell such investments at prices that reflect the Investment Adviser's assessment of their value or the amount originally paid for such investments by the Funds. Illiquidity may result from the absence of an established market for the investments as well as legal, contractual or other restrictions on their resale and other factors. Furthermore, the nature of the Funds' investments, especially those in financially distressed companies, may require a long holding period prior to profitability.

Restricted securities (i.e., securities acquired in private placement transactions) and illiquid securities may offer higher yields than comparable publicly traded securities. The Funds, however, may not be able to sell these securities when the Investment Adviser considers it desirable to do so or, to the extent they are sold privately, may have to sell

them at less than the price of otherwise comparable securities. Restricted securities are subject to limitations on resale which can have an adverse effect on the price obtainable for such securities. Also, if in order to permit resale the securities are registered under the Securities Act at a Fund's expense, the Fund's expenses would be increased.

Leverage Risk

Each Fund may use leverage in its investment program, including the use of borrowed funds and investments in certain types of options, such as puts, calls and warrants, which may be purchased for a fraction of the price of the underlying securities. While such strategies and techniques increase the opportunity to achieve higher returns on the amounts invested, they also increase the risk of loss. To the extent the Funds purchase securities with borrowed funds, their net assets will tend to increase or decrease at a greater rate than if borrowed funds are not used. If the interest expense on borrowings were to exceed the net return on the portfolio securities purchased with borrowed funds, the Funds' use of leverage would result in a lower rate of return than if the Funds were not leveraged.

Merger Arbitrage Risk

Merger arbitrage risk is the risk that the Adviser's evaluation of the outcome of a proposed event, whether it be a merger, reorganization, regulatory issue or other event, will prove incorrect and that the Fund's return on the investment will be negative. Even if the Adviser's judgment regarding the likelihood of a specific outcome proves correct, the expected event may be delayed or completed on terms other than those originally proposed, which may cause the Fund to lose money. The Fund's expected gain on an individual arbitrage investment is normally considerably smaller than the possible loss should the transaction be unexpectedly terminated. The Fund's principal investment strategies are not specifically designed to benefit from general appreciation in the equity markets or general improvement in the economic conditions in the global economy. Accordingly, the Fund may underperform the broad equity markets under certain market conditions, such as during periods when there has been rapid appreciation in the equity markets.

Non-U.S. Securities Risk

Non-U.S. securities risk is the risk associated with investing in non-U.S. issuers. Investments in securities of non-U.S. issuers involve certain risks not involved in domestic investments (for example, fluctuations in foreign exchange rates (for non-U.S. securities not denominated in U.S. dollars); future foreign economic, financial, political and social developments; nationalization; exploration or confiscatory taxation; smaller markets; different trading and settlement practices; less governmental supervision; and different accounting,

auditing and financial recordkeeping standards and requirements) that may result in each Fund experiencing more rapid and extreme changes in value than a fund that invests exclusively in securities of U.S. companies. These risks are magnified for investments in issuers tied economically to emerging markets, the economies of which tend to be more volatile than the economies of developed markets. In addition, certain investments in non-U.S. securities may be subject to foreign withholding and other taxes on interest, dividends, capital gains or other income or proceeds. Those taxes will reduce each Fund's yield on any such securities.

Options Risk

There are several risks associated with transactions in options on securities. For example, there are significant differences between the securities and options markets that could result in an imperfect correlation between these markets, causing a given transaction not to achieve its objectives. A transaction in options or securities may be unsuccessful to some degree because of market behavior or unexpected events.

When a Fund writes a covered call option, the Fund forgoes, during the option's life, the opportunity to profit from increases in the market value of the security covering the call option above the sum of the premium and the strike price of the call, but retains the risk of loss should the price of the underlying security decline. The writer of an option has no control over the time when it may be required to fulfill its obligation and once an option writer has received an exercise notice, it must deliver the underlying security in exchange for the strike price.

When a Fund writes a covered put option, the Fund bears the risk of loss if the value of the underlying stock declines below the exercise price minus the put premium. If the option is exercised, the Fund could incur a loss if it is required to purchase the stock underlying the put option at a price greater than the market price of the stock at the time of exercise plus the put premium the Fund received when it wrote the option. While the Fund's potential gain in writing a covered put option is limited to distributions earned on the liquid assets securing the put option plus the premium received from the purchaser of the put option, the Fund risks a loss equal to the entire exercise price of the option minus the put premium.

Senior Loans Risk

The risk that the issuer of a senior loan may fail to pay interest or principal when due, and changes in market interest rates may reduce the value of the senior loan or reduce the Fund's returns. The risks associated with senior loans are similar to the risks of high yield debt securities. Senior loans and other debt securities are also subject to the risk of price

declines and to increases in interest rates, particularly long-term rates. Senior loans are also subject to the risk that, as interest rates rise, the cost of borrowing increases, which may increase the risk of default. In addition, the interest rates of floating rate loans typically only adjust to changes in short-term interest rates; long-term interest rates can vary dramatically from short-term interest rates. Therefore, senior loans may not mitigate price declines in a long-term interest rate environment. The Fund's investments in senior loans are typically below investment grade and are considered speculative because of the credit risk of their issuers.

Short Sales Risk

Short sales by the Funds that are not made where there is an offsetting long position in the asset that it is being sold short theoretically involve unlimited loss potential since the market price of securities sold short may continuously increase. Short selling allows the Funds to profit from declines in market prices to the extent such decline exceeds the transaction costs and costs of borrowing the securities. However, since the borrowed securities must be replaced by purchases at market prices in order to close out the short position, any appreciation in the price of the borrowed securities would result in a loss. Purchasing securities to close out the short position can itself cause the price of securities to rise further, thereby exacerbating the loss. The Funds may mitigate such losses by replacing the securities sold short before the market price has increased significantly. Under adverse market conditions, a Fund might have difficulty purchasing securities to meet margin calls on its short sale delivery obligations, and might have to sell portfolio securities to raise the capital necessary to meet its short sale obligations at a time when fundamental investment considerations would not favor such sales.

Swaps Risk

The use of swaps is a highly specialized activity which involves investment techniques, risk analyses and tax planning different from those associated with ordinary portfolio securities transactions. These transactions can result in sizeable realized and unrealized capital gains and losses relative to the gains and losses from a Fund's direct investments in securities.

Transactions in swaps can involve greater risks than if a Fund had invested in the reference assets directly since, in addition to general market risks, swaps may be leveraged and are also subject to illiquidity risk, counterparty risk, credit risk and pricing risk. However, certain risks may be reduced (but not eliminated) if a Fund invests in cleared swaps. Regulators also may impose limits on an entity's or group of entities' positions in certain swaps. Because bilateral swap agreements are two party contracts and because they may have

NOTES TO FINANCIAL STATEMENTS (unaudited) (continued)

December 31, 2018

Highland Funds I

terms of greater than seven days, these swaps may be considered to be illiquid. Moreover, a Fund bears the risk of loss of the amount expected to be received under a swap in the event of the default or bankruptcy of a swap counterparty. Many swaps are complex and valued subjectively. Swaps and other derivatives may also be subject to pricing or “basis” risk, which exists when the price of a particular derivative diverges from the price of corresponding cash market instruments. Under certain market conditions it may not be economically feasible to initiate a transaction or liquidate a position in time to avoid a loss or take advantage of an opportunity. If a swap transaction is particularly large or if the relevant market is illiquid, it may not be possible to initiate a transaction or liquidate a position at an advantageous time or price, which may result in significant losses.

The value of swaps can be very volatile, and a variance in the degree of volatility or in the direction of securities prices from the Adviser’s expectations may produce significant losses in a Fund’s investments in swaps. In addition, a perfect correlation between a swap and a reference asset may be impossible to achieve. As a result, the Adviser’s use of swaps may not be effective in fulfilling the Adviser’s investment

strategies and may contribute to losses that would not have been incurred otherwise.

Note 8. Investment Transactions

Purchases & Sales of Securities

The cost of purchases and the proceeds from sales of investments, other than short-term securities and short-term options, for the six months ended December 31, 2018, were as follows:

| Fund | U.S Government Securities ⁽¹⁾ | | Other Securities | |
|----------------------------|--|-------|------------------|---------------|
| | Purchases | Sales | Purchases | Sales |
| Long/Short Equity Fund | \$— | \$— | \$519,249,398 | \$551,478,247 |
| Long/Short Healthcare Fund | — | — | 45,718,628 | 63,683,390 |
| Merger Arbitrage Fund | — | — | 214,490,933 | 196,105,154 |
| Opportunistic Credit Fund | — | — | 1,037,283 | 1,175,862 |

⁽¹⁾ The Funds did not have any purchases or sales of U.S. Government Securities for the six months ended December 31, 2018.

Note 9. Affiliated Issuers

Under Section 2 (a) (3) of the Investment Company Act of 1940, as amended, a portfolio company is defined as “affiliated” if a fund owns five percent or more of its outstanding voting securities or if the portfolio company is under common control. The tables below show affiliated issuers of each Fund as of the year ended December 31, 2018:

| Long/Short Equity Fund | | | | | | | | | | |
|--|-------------------------|-------------------------------------|-------------------|---------------------|---|--|--------------------------------------|-----------------------------|-------------------|--|
| Issuer | Shares at June 30, 2018 | Beginning Value as of June 30, 2018 | Purchases at Cost | Proceeds from Sales | Net Realized Gain/(Loss) on Sales of Affiliated Issuers | Change in Unrealized Appreciation/Depreciation | Ending Value as of December 30, 2018 | Shares at December 30, 2018 | Affiliated Income | |
| | | | | | | | | | | |
| Other Affiliates | | | | | | | | | | |
| Highland Merger Arbitrage Fund (Registered Investment Companies) | 314,174 | \$6,581,955 | \$1,087,660 | \$— | \$— | \$(871,734) | \$6,797,881 | 374,333 | \$1,071,250 | |
| Highland Opportunistic Credit Fund | | | | | | | | | | |
| Issuer | Shares at June 30, 2018 | Beginning Value as of June 30, 2018 | Purchases at Cost | Proceeds from Sales | Net Realized Gain/(Loss) on Sales of Affiliated Issuers | Change in Unrealized Appreciation/Depreciation | Ending Value as of December 30, 2018 | Shares at December 30, 2018 | Affiliated Income | |
| | | | | | | | | | | |
| Other Affiliates | | | | | | | | | | |
| Gambier Bay LLC (Common Stocks) | 2,895,971 | \$372,856 | \$— | \$— | \$— | \$(39,819) | \$333,037 | 2,895,971 | \$— | |

Note 10. Regulatory Matters

On August 17, 2018, the SEC adopted amendments to Regulation S-X. These changes are effective for periods after November 5, 2018. The updates to Registered Investment Companies were mainly focused on simplifying the presentation of distributable earnings by eliminating the need to present the components of distributable earnings on a

book basis in the Statements of Assets and Liabilities. The update also impacted the presentation of undistributed net investment income and distribution to shareholders on the Statements of Changes in Net Assets. The amounts presented in the current Statements of Changes in Net Assets represent the aggregated total distributions of net investment income and realized capital gains, except for distributions classified as

NOTES TO FINANCIAL STATEMENTS (unaudited) (concluded)

December 31, 2018

Highland Funds I

return of capital which are still presented separately. The disaggregated amounts from the prior fiscal year are broken out below if there were both distributions from net investment income and realized capital gains. Otherwise, the amount on the current Statement of Changes for the prior fiscal year end represents distributions of net investment income.

| Fund | Net Investment Income | Net Realized Gains |
|-------------------------------|-----------------------|--------------------|
| Long/Short Equity Fund | | |
| Class A | \$ — | \$ (897,492) |
| Class C | — | (667,393) |
| Class Z | — | (8,383,528) |
| Merger Arbitrage Fund | | |
| Class A | (93,186) | (27,989) |
| Class C | (60,287) | (21,216) |
| Class Z | (1,611,468) | (535,933) |

Note 11. New Accounting Pronouncements

In March 2017, the FASB issued Accounting Standards Update 2017-08, Receivables — Nonrefundable Fees and Other Costs (Subtopic 310-20). The amendments in this update shorten the amortization period for certain callable debt securities held at premium. Specifically, the amendments require the premium to be amortized to the earliest call date. The amendments do not require an accounting change for securities held at a discount; the discount continues to be amortized to maturity. For public entities this update will be effective for fiscal years beginning after December 15, 2018, and for interim periods within those fiscal years. The Investment Adviser is currently evaluating the impact of this new guidance on the Funds' financial statements.

In February 2018, the FASB issued Accounting Standards Update 2018-03, Technical Corrections and Improvements to Financial Instruments — Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. The amendments in this update provide a variety of technical corrections and improvements to how entities should account for financial instruments. For public entities this update will be effective for fiscal years beginning after December 15, 2017, and for interim periods within those fiscal years beginning after June 15, 2018. The Investment Adviser is currently evaluating the impact of this new guidance on its financial statement presentation and disclosures.

In August 2018, the FASB issued Accounting Standards Update 2018-13, Fair Value Measurement (Topic 820). The new guidance includes additions and modifications to disclosures requirements for fair value measurements. For public entities, the amendments are effective for financial statements issued for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. At this time, management is currently evaluating the impact of this new guidance on the financial statements and disclosures.

Note 12. Subsequent Events

Management has evaluated the impact of all subsequent events on the Funds through the date the financial statements were issued, and has determined that there were no subsequent events to report which have not already been recorded or disclosed in these financial statements and accompanying notes.

ADDITIONAL INFORMATION (unaudited)

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Highland Funds I

Additional Portfolio Information

The Investment Adviser and its affiliates manage other accounts, including registered and private funds and individual accounts. Although investment decisions for the Funds are made independently from those of such other accounts, the Investment Adviser may, consistent with applicable law, make investment recommendations to other clients or accounts that may be the same or different from those made to the Funds, including investments in different levels of the capital structure of a company, such as equity versus senior loans, or that involve taking contradictory positions in multiple levels of the capital structure. The Investment Adviser has adopted policies and procedures that address the allocation of investment opportunities, execution of portfolio transactions, personal trading by employees and other potential conflicts of interest that are designed to ensure that all client accounts are treated equitably over time. Nevertheless, this may create situations where a client could be disadvantaged because of the investment activities conducted by the Investment Adviser for other client accounts. When the Funds and one or more of such other accounts are prepared to invest in, or desire to dispose of, the same security, available investments or opportunities for each will be allocated in a manner believed by the Investment Adviser to be equitable to the Funds and such other accounts. The Investment Adviser also may aggregate orders to purchase and sell securities for the Funds and such other accounts. Although the Investment Adviser believes that, over time, the potential benefits of participating in volume transactions and negotiating lower transaction costs should benefit all accounts including the Funds, in some cases these activities may adversely affect the price paid or received by the Funds or the size of the position obtained or disposed of by the Funds.

Disclosure of Fund Expenses

As a shareholder of a Fund, you incur two types of costs: (1) transaction costs, including sales charges (loads) on purchases and redemption fees; and (2) ongoing costs, including management fees; distribution (12b-1) and service fees; and other Fund expenses. This example is intended to help you understand the ongoing costs (in dollars) of investing in your Fund and to compare these costs with the ongoing costs of investing in other mutual funds. The example is based on an investment of \$1,000 invested at the beginning of the period and held for the six-month period July 1, 2018 through December 31, 2018, unless otherwise indicated. This table illustrates your Fund's costs in two ways:

Actual Expenses: The first part of the table provides information about actual account values and actual expenses. You may use the information in this line, together with the amount you invested, to estimate the expenses that

you paid over the period. Simply divide your account value by \$1,000 (for example, an \$8,600 account value divided by \$1,000 = 8.6), then multiply the result by the number in the first line under the heading entitled "Expenses Paid During Period" to estimate the expenses you paid on your account during this period.

Hypothetical Example for Comparison Purposes: The second part of the table provides information about hypothetical account values and hypothetical expenses based on your Fund's actual expense ratio and an assumed rate of return of 5% per year before expenses, which is not your Fund's actual return. The actual expense ratio includes voluntary fee waivers or expense reimbursements by the Fund's investment adviser. The expense ratio would be higher had the fee waivers or expense reimbursements not been in effect. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period. You may use this information to compare the ongoing costs of investing in your Fund and other funds. To do so, compare this 5% hypothetical example with the 5% hypothetical examples that appear in the shareholder reports of the other funds. Please note that the expenses shown in the table are meant to highlight your ongoing costs only and do not reflect any transactional costs, such as sales charges (loads) or redemption fees. Therefore, the second part of the table is useful in comparing ongoing costs only, and will not help you determine the relative total costs of owning different funds. In addition, if these transactional costs were included, your costs would have been higher.

| | Beginning Account Value 7/1/18 | Ending Account Value 12/31/18 | Annualized Expense Ratios ⁽¹⁾ | Expenses Paid During Period ⁽²⁾ |
|--|---|--|--|---|
| Highland Long/Short Equity Fund | | | | |
| <i>Actual Fund Return</i> | | | | |
| Class A | \$1,000.00 | \$ 893.60 | 2.99% | \$14.27 |
| Class C | 1,000.00 | 891.70 | 3.64% | 17.36 |
| Class Z | 1,000.00 | 895.90 | 2.66% | 12.71 |
| <i>Hypothetical</i> | | | | |
| Class A | \$1,000.00 | \$1,010.13 | 2.99% | \$15.15 |
| Class C | 1,000.00 | 1,006.86 | 3.64% | 18.41 |
| Class Z | 1,000.00 | 1,011.80 | 2.66% | 13.49 |
| Highland Long/Short Healthcare Fund | | | | |
| <i>Actual Fund Return</i> | | | | |
| Class A | \$1,000.00 | \$1,048.60 | 2.16% | \$11.15 |
| Class C | 1,000.00 | 1,045.10 | 2.81% | 14.48 |
| Class Z | 1,000.00 | 1,049.90 | 1.81% | 9.35 |
| <i>Hypothetical</i> | | | | |
| Class A | \$1,000.00 | \$1,014.32 | 2.16% | \$10.97 |
| Class C | 1,000.00 | 1,011.04 | 2.81% | 14.24 |
| Class Z | 1,000.00 | 1,016.08 | 1.81% | 9.20 |

ADDITIONAL INFORMATION (unaudited) (continued)

December 31, 2018

Highland Funds I

| | Beginning Account Value 7/1/18 | Ending Account Value 12/31/18 | Annualized Expense Ratios ⁽¹⁾ | Expenses Paid During Period ⁽²⁾ |
|---|---|--|--|---|
| Highland Merger Arbitrage | | | | |
| <i>Actual Fund Return</i> | | | | |
| Class A | \$1,000.00 | \$1,031.50 | 5.33% | \$27.29 |
| Class C | 1,000.00 | 1,027.70 | 5.88% | 30.05 |
| Class Z | 1,000.00 | 1,032.80 | 5.04% | 25.82 |
| <i>Hypothetical</i> | | | | |
| Class A | \$1,000.00 | \$ 998.34 | 5.33% | \$26.85 |
| Class C | 1,000.00 | 995.56 | 5.88% | 29.58 |
| Class Z | 1,000.00 | 999.80 | 5.04% | 25.40 |
| Highland Opportunistic Credit Fund | | | | |
| <i>Actual Fund Return</i> | | | | |
| Class A | \$1,000.00 | \$ 963.50 | 1.25% | \$ 6.19 |
| Class C | 1,000.00 | 960.80 | 1.75% | 8.65 |
| Class Z | 1,000.00 | 965.10 | 0.90% | 4.46 |
| <i>Hypothetical</i> | | | | |
| Class A | \$1,000.00 | \$1,018.90 | 1.25% | \$ 6.36 |
| Class C | 1,000.00 | 1,016.38 | 1.75% | 8.89 |
| Class Z | 1,000.00 | 1,020.67 | 0.90% | 4.58 |

- (1) Annualized, based on the Fund's most recent fiscal half-year expenses, including dividends on short positions and interest expenses, if any.
- (2) Expenses are equal to the Fund's annualized expense ratio including interest expense and dividends on short positions, if any, multiplied by the average account value over the period, multiplied by the number of days in the most recent fiscal half-year, divided by the number of days in the full fiscal year (184/365).

Changes of Independent Registered Public Accounting Firms

On September 28, 2018, Highland Long/Short Equity Fund, Highland Long/Short Healthcare Fund, Highland Merger Arbitrage Fund, Highland Opportunistic Credit Fund and Highland/iBoxx Senior Loan ETF, each a series of Highland Funds I (the "Trust"), dismissed KPMG LLP ("KPMG") as the Trust's independent registered public accounting firm, effective on such date. The decision to dismiss KPMG was approved by the audit committee and by the full board of trustees of the Trust (the "Board"). On September 27, 2018, the Trust approved the appointment of PricewaterhouseCoopers LLP ("PwC") as the Trust's independent registered public accounting firm.

KPMG's audit reports on the Trust's financial statements as of and for the years ended June 30, 2018 and 2017 did not contain any adverse opinion or disclaimer of opinion, nor were they qualified or modified as to uncertainty, audit scope, or accounting principles.

During its audits of the Trust as of June 30, 2018, KPMG concluded management's review control over a certain hard-to-value security held by Opportunistic Credit Fund was not designed at an appropriate level of precision to assess the orderly nature of transactions involving the security and

reasonableness and reliability of certain inputs to the fair value model for the security. In connection with this audit, KPMG advised the Trust of the need to expand significantly the scope of its audits. Although Management of the Trust initially disagreed with KPMG's position, subsequent to KPMG's dismissal Management ultimately took the position that the transactions were orderly and revised certain non-observable inputs to the fair value model for the security.

KPMG and Management individually identified a material weakness in the control environment of Highland Opportunistic Credit Fund related to the assessment of orderly transactions and non-observable inputs used in fair valuation of a fair valued asset held.

Other than the disagreements and reportable events disclosed above, during the Trust's years ended June 30, 2018 and 2017 and the subsequent interim period through September 28, 2018, there were no: (1) disagreements (as defined in Item 304(a)(1)(iv) of Regulation S-K and the related instructions) with KPMG on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedures, which disagreements if not resolved to their satisfaction would have caused them to make reference in connection with their opinion to the subject matter of the disagreement, or (2) reportable events (as described in Item 304(a)(1)(v) of Regulation S-K). The audit committee of the Trust discussed the subject matter of these disagreements and reportable events with KPMG. The Trust has authorized KPMG to respond fully to the inquiries of PwC concerning the subject matter of these disagreements and reportable events.

During the years ended June 30, 2018 and 2017 and the subsequent interim period through September 28, 2018, neither Management, the Trust, nor anyone on its behalf, consulted PwC regarding either (i) the application of accounting principles to a specified transaction, either completed or proposed, or the type of audit opinion that might be rendered on the financial statements of the Trust, and no written report or oral advice was provided to the Trust by PwC that PwC concluded was an important factor considered by the Trust in reaching a decision as to any accounting, auditing or financial reporting issue; or (ii) any matter that was either the subject of a disagreement (as defined in Item 304(a)(1)(iv) of Regulation S-K and the related instructions) or a reportable event (as described in Item 304(a)(1)(v) of Regulation S-K).

Approval of Highland Funds I Investment Advisory Agreement

The Trust has retained the Investment Adviser to manage the assets of each Fund pursuant to investment advisory agreements between the Investment Adviser and each such Fund (the "Advisory Agreements"). The Advisory Agreements

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were approved by the Funds' Board of Trustees, including a majority of the Independent Trustees.

Following an initial two-year term, each of the Advisory Agreements continues in effect from year-to-year, provided that such continuance is specifically approved at least annually by the vote of holders of at least a majority of the outstanding shares of the Fund or by the Board of Trustees and, in either event, by a majority of the Independent Trustees of the Fund casting votes in person at a meeting called for such purpose.

During telephonic meetings held on August 16, 2018 and August 28, 2018, the Board of Trustees gave preliminary consideration to information bearing on the continuation of the Agreements for a one-year period commencing November 1, 2018 with respect to the Funds. The primary objective of the meetings was to ensure that the Trustees had the opportunity to consider matters they deemed relevant in evaluating the continuation of the Agreement, and to request any additional information they considered reasonably necessary for their deliberations.

At an in-person meeting held on September 16-17, 2018, the Board of Trustees, including the Independent Trustees, approved the continuance of the Agreement for a one-year period commencing on November 1, 2018. As part of its review process, the Board of Trustees requested, through Fund counsel and its independent legal counsel, and received from the Investment Adviser, various information and written materials including: (1) information regarding the financial soundness of the Investment Adviser and the profitability of the Advisory Agreements to the Investment Adviser; (2) information on the advisory and compliance personnel of the Investment Adviser, including compensation arrangements; (3) information on the internal compliance procedures of the Investment Adviser; (4) comparative information showing how the Funds' fees and operating expenses compare to those of other accounts of the Investment Adviser and comparable funds managed by unaffiliated advisers, both of which follow investment strategies similar to those of the Funds; (5) information on the investment performance of the Funds, including comparisons of the Funds' performance against that of other registered investment companies and comparable funds that follow investment strategies similar to those of the Funds; (6) information regarding brokerage and portfolio transactions; and (7) information on any legal proceedings or regulatory audits or investigations affecting the Investment Adviser. In addition, the Trustees received an independent report from Morningstar Inc. ("Morningstar"), an independent source of investment company data, relating to each Fund's performance, volatility and expenses compared to the performance, volatility and expenses of a peer group determined by Morningstar to be comparable. The Trustees

also relied on information provided at periodic meetings of the Board of Trustees over the course of the year. The Trustees reviewed various factors discussed in independent counsel's legal memoranda regarding their responsibilities in considering the Advisory Agreements, the detailed information provided by the Investment Adviser and other relevant information and factors. The Trustees' conclusions as to the approval of the Advisory Agreements were based on a comprehensive consideration of all information provided to the Trustees without any single factor being dispositive in and of itself. Some of the factors that figured particularly in the Trustees' deliberations are described below, although individual Trustees may have evaluated the information presented differently from one another, giving different weights to various factors.

The nature, extent, and quality of the services to be provided by the Investment Adviser.

The Board of Trustees considered the portfolio management services to be provided by the Investment Adviser under the Advisory Agreements and the activities related to portfolio management, including use of technology, research capabilities, and investment management staff. The Trustees discussed the relevant experience and qualifications of the personnel providing advisory services, including the background and experience of the members of each Fund's portfolio management team. The Trustees reviewed the management structure, assets under management and investment philosophies and processes of the Investment Adviser. The Trustees also reviewed and discussed information regarding the Investment Adviser's compliance policies, procedures and personnel, including portfolio manager compensation arrangements. The Trustees concluded that the Investment Adviser had the quality and depth of personnel and investment methods essential to performing its duties under the Advisory Agreements, and that the nature and the quality of such advisory services were satisfactory.

The Investment Adviser's historical performance in managing the Funds.

The Board of Trustees reviewed the historical performance of each Fund over various time periods and reflected on previous discussions regarding matters bearing on the Investment Adviser's performance at its meetings throughout the year. With respect to each Fund, the Trustees discussed the historical performance of the Fund and contrasted the relative performance of the Fund and its portfolio management team to that of the Fund's peers, as represented by certain other registered investment companies and comparable funds that follow investment strategies similar to the Fund, as well as comparable indices and the Fund's applicable Morningstar category. With respect to

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each Fund, the Trustees concluded that the Fund's performance or other relevant factors supported the continuation of the Advisory Agreement(s) relating to that Fund for an additional one-year period.

In the case of each Fund that had performance that lagged, as applicable, the performance of its Morningstar peer group median, category median and/or benchmark for certain periods, the Trustees considered information provided by the Investment Adviser relating to the attribution of performance results for each such Fund, including information that demonstrated that such Fund's underperformance was attributable, to a significant extent, to investment decisions (such as security selection or sector allocation) by the Investment Adviser that were reasonable under the circumstances prevailing at the time and consistent with the applicable Fund's investment objective and policies.

With respect to each Fund, the Trustees concluded that the Fund's performance and other relevant factors supported the continuation of the Advisory Agreements.

The costs of the services to be provided by the Investment Adviser and the profits to be realized by the Investment Adviser and its affiliates from the relationship with the Funds.

The Board of Trustees also gave consideration to the fees payable under the Advisory Agreements, the expenses that the Investment Adviser incurs in providing advisory services and the profitability to the Investment Adviser of managing the Funds, including: (1) information regarding the financial condition of the Investment Adviser; (2) information regarding the total fees and payments received by the Investment Adviser for its services and whether such fees are appropriate given economies of scale and other considerations; (3) comparative information showing (a) the fees payable under the Advisory Agreements versus the investment advisory fees of certain registered investment companies and comparable funds that follow investment strategies similar to those of the Funds and (b) the expense ratios of the Funds versus the expense ratios of certain registered investment companies and comparable funds that follow investment strategies similar to those of the Funds; and (4) information regarding the total fees and payments received and the related amounts waived and/or reimbursed by the Investment Adviser for providing administrative services with respect to certain of the Funds under separate agreements and whether such fees are appropriate. The Trustees also considered the so-called "fall-out benefits" to the Investment Adviser with respect to the Funds, such as the reputational value of serving as Investment Adviser to the Funds, potential fees paid to the Investment Adviser's affiliates by a Fund or portfolio companies for services provided, including administrative services provided to certain Funds by the

Investment Adviser pursuant to separate agreements, the benefits of scale from investment by the Funds in affiliated funds and the benefits of research made available to the Investment Adviser by reason of brokerage commissions (if any) generated by the Funds' securities transactions, and, with respect to certain Funds that invest in one or more other funds in the Highland fund complex, the fees paid to the Adviser of the underlying Fund and its affiliates with respect to such investments. After such review, the Trustees determined that the anticipated profitability rates to the Investment Adviser with respect to the Advisory Agreements were fair and reasonable. The Trustees also took into consideration the amounts waived and/or reimbursed, if any, where expense caps or advisory fee waivers had been implemented.

The extent to which economies of scale would be realized as each Fund grows and whether fee levels reflect these economies of scale for the benefit of shareholders.

The Board of Trustees considered the respective asset levels of the Funds over time and historical net expenses relative to such asset levels, the information provided by the Investment Adviser relating to its costs and information comparing the fee rates charged by the Investment Adviser with fee rates charged by other unaffiliated investment advisers to their clients. The Trustees concluded that the fee structures are reasonable, and with respect to the Investment Adviser, should result in a sharing of economies of scale in view of the information provided. The Board determined to continue to review ways, and the extent to which, economies of scale might be shared between the Investment Adviser on the one hand and shareholders of the Funds on the other. The Board also requested that the Investment Adviser consider ways in which economies of scale can be shared with Fund shareholders.

Conclusion.

Throughout the process, the Board of Trustees was advised by Fund counsel and independent legal counsel, and was empowered to engage such other third parties or request additional information as it deemed appropriate. Following a further discussion of the factors above and the merits of the Advisory Agreements and their various provisions, it was noted that in considering the approval of the Advisory Agreements, no single factor was determinative to the decision of the Board of Trustees. Rather, after weighing all of the factors and reasons discussed above, the Trustees, including the Independent Trustees, unanimously agreed that the Advisory Agreements, including the advisory fees to be paid to the Investment Adviser, are fair and reasonable to the Funds in light of the services that the Investment Adviser provides, the expenses that it incurs and the reasonably foreseeable asset levels of the Funds.

IMPORTANT INFORMATION ABOUT THIS REPORT

Investment Adviser

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200 Crescent Court, Suite 700
Dallas, TX 75201

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430 W. 7th Street, Suite 219424
Kansas City, Missouri 64105-1407

Underwriter

Highland Capital Funds Distributor, Inc.
200 Crescent Court, Suite 700
Dallas, TX 75201

Custodian

State Street Bank and Trust Company
One Lincoln Street
Boston, Massachusetts 02111

Independent Registered Public Accounting Firm

PricewaterhouseCoopers LLP
2121 N. Pearl Street, Suite 2000,
Dallas, TX 75201

Fund Counsel

K&L Gates LLP
1 Lincoln Street
Boston, MA 02111

This report has been prepared for shareholders of Highland Long/Short Equity Fund, Highland Long/Short Healthcare Fund, Highland Merger Arbitrage Fund, and Highland Opportunistic Credit Fund, (collectively, the "Funds"). The Funds mail one shareholder report to each shareholder address. If you would like more than one report, please call shareholder services at 1-877-665-1287 to request that additional reports be sent to you.

A description of the policies and procedures that the Funds use to determine how to vote proxies relating to their portfolio securities, and the Funds' proxy voting records for the most recent 12-month period ended June 30, are available (i) without charge, upon request, by calling 1-877-665-1287 and (ii) on the Securities and Exchange Commission's website at <http://www.sec.gov>.

The Funds file their complete schedules of portfolio holdings with the Securities and Exchange Commission for the first and third quarters of each fiscal year on Form N-Q. The Funds' Forms N-Q are available on the Commission's website at <http://www.sec.gov> and also may be reviewed and copied at the Commission's Public Reference Room in Washington, DC. Information on the Public Reference Room may be obtained by calling 1-800-SEC-0330. Shareholders may also obtain the Form N-Q by visiting the Funds' website at www.highlandfunds.com.

The Statements of Additional Information include additional information about the Funds' Trustees and are available upon request without charge by calling 1-877-665-1287.

Beginning on January 1, 2021, as permitted by regulations adopted by the U.S. Securities and Exchange Commission, paper copies of the Funds' annual and semi-annual shareholder reports will no longer be sent by mail, unless you specifically request paper copies of the reports. Instead, the reports will be made available on the Funds' website (highlandfunds.com), and you will be notified by mail each time a report is posted and provided with a website link to access the report.

If you already elected to receive shareholder reports electronically, you will not be affected by this change and you need not take any action. You may elect to receive shareholder reports and other communications from a Fund electronically by contacting your financial intermediary (such as a broker-dealer or bank) or, if you are a direct investor, by contacting the Funds' transfer agent at [1-877-665-1287].

Beginning on January 1, 2019, you may elect to receive all future reports in paper free of charge. If you invest through a financial intermediary, you can contact your financial intermediary to request that you continue to receive paper copies of your shareholder reports. If you invest directly with a Fund, you can call [1-877-665-1287] to let the Fund know you wish to continue receiving paper copies of your shareholder reports. Your election to receive reports in paper will apply to all funds held in your account if you invest through your financial intermediary or all funds held with the fund complex if you invest directly with a Fund.

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