June 2021 Update With Justin Ford

Bob Irish
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As one of our privileged members, you get access to real estate expert Justin Ford's monthly DealBook updates.

DealBook covers special situations with our network of experts in the kinds of private deals most people never even hear about.

Each month, I check in with Justin to see how his previous real estate deals are performing. Justin also discusses the latest trends in the market, what to look for when purchasing property as an investment, and much more.

You can listen to my monthly interview with Justin or read the transcript below.

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Transcript

Bob Irish: Welcome to our monthly call with Justin Ford of PAX Properties, our resident real estate expert. Bob Irish, here, your Infinity liaison. If you've been with us for a while, you know that Justin has been an extraordinarily successful real estate investor.

Throughout real estate booms and busts, PAX Properties has never failed to produce a positive result for investors or missed a mortgage payment. With that said, Justin, great to have you back. How're you doing?

Justin Ford: I'm doing well, Bob, thank you. How are you?

Bob: I'm doing great. Things are good here in Delray Beach. How are things at PAX Properties? How has the last month gone? Did you have some updates for us?

Justin: Yeah, absolutely.

Well Melbourne – the former most visited place by police in Melbourne – became the immediate TripAdvisor top award winner, et cetera. When we finished it. It has won county awards and very successful financially. That hotel just won the TripAdvisor top award for the fifth year in a row.

Bob: Oh, wow.

Justin: Yep, every year it has been open it has won that award, and now business is really growing as we're coming out of COVID. The last two quarters we paid an eight and a half percent cash on cash yield and a 10% cash yield. And we expect to pay the same coming up this July for the second quarter. So we're doing very, very well.

We've got a new restaurant lease to a sushi restaurant, who is an established restaurateur, so that guy is doing very good business. He now opened up in another one of our locations as well.

We're working on our next thing which is that we're looking to do a refi return on a significant chunk of investor capital as the financing market for hospitality slowly begins to recover. At which case, our already high cash on cash yields could climb significantly higher. So we like our developments available.

Bob: Oh, I like the sound of that, too. And I must say I'm an investor in the Melbourne property and it was nice to see that check come in not too long ago, for sure.

Let's move from Melbourne, but I'm delighted things are going so well. Let's go to Tallahassee and let's talk a little bit about The Baymont. Earlier we were talking about how people who are making travel plans now are finding hotel prices have come up quite a bit from the depth of the COVID depression. Hopefully that's helped The Baymont a little bit. What's going on there?

Justin: We're going to new markets all the time in other states, and I used to be paying so cheap. And now those rates have doubled in the hotels I'm staying at. But I can't complain because they're climbing, too, at our own hotel, and that includes Baymont.

At Baymont, the rates are going up and our occupancy is starting to climb. Baymont has been our one lagger. It's the one that suffered the most during COVID. And now we have new group bookings coming on from construction in other places.

In Baymont, we just got an SBA loan for relief for COVID, but it's going to be paid back. We already did all those PPP loans when COVID first hit. And that was great, and we qualified for the full forgiveness if we hired people back according to our business.

And now we just got a $500,000 loan at 3% for 30 years, which really helped strengthen our balance sheet there, and helped us make it through the end of COVID. And again, we have new sales coming on.

Our manager there, one of his best qualities is that he's really kept a tight rein on expenses. Where we were falling short there, was the top line during COVID. We weren't driving it as much; he didn't get in COVID as much as we should.

But now revenue is really growing with these group bookings. We have new people coming out to help us with group bookings, and we're amply supplied with cash there – some cushion. Baymont is making good progress and we think it might qualify for best improved by next quarter. It's certainly making good progress.

Bob: Well, fingers crossed there. Let's talk a little bit about Governor Square.

Justin: Governor Square might take the place of Melbourne as the jewel in our crown. At Governor Square, I just finished a P&L [profits and losses] call, our monthly P&L with the property manager. And our new property manager from the new property we have in another state was attending as well, because she's learning our new processes and all that stuff.

Everywhere we go we train people on how we operate. We have a very specific way that we like to operate, which is efficiently and effectively and with great consideration for those involved.

We just had that call, and you have Baymont grossing $171,000 month, possibly one of its best ever, and certainly its best coming out of COVID. it posted about 91K in NOI (Net Operating Income), which is quite strong. That puts you on track to almost 1.1 million in EBITDA (Earnings Before Interest, Taxes, Depreciation, and Amortization).

We're forecasting 1.3 million in EBITDA, a little over that option, over the next 12 months. And we're on the verge of that refi I talked about. We expect to close the bridge loan portion of that refi probably within a month. We have our property inspection report a week from today. And they're going to the property and doing their Phase One Environmental Property Condition Assessment and other reports.

About a month to maybe five or six weeks from today we'll pay off all private investment loans, we'll refi that other loan, and bring down the rate significantly of the mortgage loan. And then we're set up for the HUD (Housing and Urban Development) loan.

The HUD loan will kick in around November or December at the latest, I think. And there we return a huge chunk of investor capital. Probably well over half.

Our cash on cash there, again, goes into the double digits at that point. And that HUD loan rate will be 2.8 to 2.9% fixed for 35 years. Check cash flow will be just stupendous. So we're executing according to plan and even starting to do a bit better than that, I would say.

Bob: Well that's good news about Governor Square. Let's talk a little bit about Seven Hills.

Justin: Seven Hills won the Trip Advisor top award when we first finished, and then COVID hit... we leased out three-quarters of the property to a charity organization and they left a couple of months ago.

We're finishing about a $300,000 renovation there, and a good portion of that is paid by the former charitable organization that was with us. So we're getting it back to completely like new. And it's a well worthwhile environment because throughout COVID that property paid for all its expenses. It paid its debt service without a problem.

Now we've taken a step back because we let those folks go. We're finishing renovations and we're marketing. We're still number two in the market out of 62 hotels. We were number one, and I think we'll get back to No. 1 fairly soon once we finish our renovations.

We also brought in a new fractional chief marketing officer. He helps us with all of our hotels, and he's really got good experience. Combined with my experience in hotels and in marketing, I think we're coming in with some really solid plans.

Seven Hills, toward the fourth quarter this year, will start to get back to its original budget. The original budget is close to well over a million dollars in EBITDA on about 10 million invested. And we're making strides in that right now. I'm really hoping for that second Trip Advisor top award in the next few weeks. We'll see if that happens.

And I like our prospects going forward as we continue to grow our revenue and have a fully renovated, beautiful hotel.

Bob: Perfect. So let's talk about Equus in Ocala.

Justin: At Equus, we finished renovations. The only thing we're waiting on is the pool. The pool should be done in about a week, but everything is done. All the rooms, the lobby, all the amenities, the front, the special video board. Even before it finished renovations, I don't think I've told you this, this is fairly new ... It's only two or three weeks ago, Equus has become our third independent hotel to win TripAdvisor's top award as well.

Bob: Wow.

Justin: Frankly, our last three independent hotels have won TripAdvisor's top award every year they've been in existence. So it's really a tribute to our management team we've built up over the years and how hard these folks work. And revenue is growing too.

We just posted our highest revenue month since we owned the hotel. We had been under renovation previously, so not all our rooms were available. And we're making record bookings with groups. We have a tremendous reputation in the community. We recently appeared in one of the local newspapers. We have a grand opening on June 17th in Ocala. And I'll be coming back from Nicaragua, from Rancho Santana down there, where I think you and I are going to be hanging out a little bit.

And then I'll be coming back a little early to go to our grand opening in Ocala. And I think Ocala is going to be another financially successful hotel and also well regarded by the public. Like I said, it's booked over $170,000 just last month as we were still coming out of COVID.

Bob: Well be sure to take some pictures at the grand opening. Maybe we can post them on next month's update.

That covers all the investments that *Infinity* DealBook subscribers are invested in. Justin, but I know you're actively investing in some other markets. I went to the PAX Properties website and got a taste of what you're doing. Can you talk a little bit about that?

Justin: We like to go to the tertiary and quaternary markets when the market is super-hot, and it gets a bit inflated. So our margin of safety is one, we buy cash flow, we fix our interest rates. We expect rain, we budget for rain to make it through the tough times. We focus on execution. We like to keep cash available to make it through any sudden surprises. And this has worked for us a great deal.

But another thing that we're doing is we always buy stuff in the value-add category, working class, and middle class. And we end up far below replacement costs. For instance, we're in the Midwest and we closed on a 91-unit property. And this thing is in what I call a stealth growth market.

I call it the next Austin. And I invested in Austin when no one else knew about it, and I made money on it. When all the markets crashed, I told people to move from the coastal markets in 2006 and 2007. I said, "Move your money to places like Austin." Austin was my number one pick.

I find this new market in the Midwest, which is not Austin, to be the next Austin. People don't know about it, it's charming, it's got great culture. And we're buying stuff at $50 to $70 a square foot.

When we do extensive renovations, we're adding big value. But even after extensive renovations, you have a beautiful, finished product with hardwood cabinets, three-centimeter quartz countertops, stainless steel and under mount sinks, recessed LED lighting, revamped bathrooms, and the amenities completely done. Even after all this, we're in it for maybe $85 a foot. And these are true, there's a $91 million property and one is a 26-pointer we should close on in a month or so.

But the point is that if you look at a market like this there are tremendous opportunities out there if you're not blindly following the leader into places like Miami or Houston. Although we're actively scouting in Texas as well.

But the point is, if you really know how to look, there are deals out there. If you know how to create value, you can create some significant long-term investment returns. And I'm talking about cash-on-cash yields after you're stabilized that are 8% to a bit better than that.

The part of your mortgage payment that reduces your mortgage balance, that's principal reduction, which also is known as amortization. That's also equity you build up without property prices rising a single dollar. So we don't talk about inflation. We've benefited a lot from inflation. We've made probably tens of millions from inflation as a group, for investors and ourselves.

But we know that market inflation is up to the gods. What's up to us is what we can control, and that's cash flow, amortization, positive leverage and focusing on execution.

And so just when you take the cash flow in these types of deals, I'm talking about where you can buy at those rates, and you add another 4% that you're making cash on cash from principal reduction, you're looking at stabilizing terms after year two or maybe three at the most, of 12-14%, not counting any appreciation. If you get appreciation, then that's whipped cream and now your IRRs (Internal Rate of Return) might be well into the high teens or in your low 20% range.

But it's focusing on what you can control. And buying under replacement cost in this category is very important. Because when we own this property all, in a really good area, growing popularity, across the street from a Barnes and Noble, down the block from Chick-fil-A, these are major demographic identifiers. These are corporations that do their homework on the top 10 people moving to that area.

And when you have that in $85 a foot, all renovated and everything else, a competitor can't come in the market and undersell you. Because if they gave them the land for free, you can't build for close to $85 a foot anywhere in the country.

If you're doing just stick frame with basic finishes, you're going to be close to $135 a foot today. That kind of deep discount to replacement costs, combined with a cash flow, combined with our conservative financing model and strenuous execution, discipline creates interesting long-term returns and that's what we're all about.

Bob: Wow, well those are spectacular returns, in the environment we're in right now. That's exciting stuff and again, when I looked at your website, I was like, "Whoa."

Pretty cool stuff, Justin. Anything you'd like to add before we sign off?

Justin: Now when you went to our website you spelled PAX correctly, right? It's P-A-X.

Bob: Yeah, cool stuff.

I'll look forward to our call next month, unless you have anything else you'd like to say before we sign off.

Justin: Nope, it's been a slice of heaven, Bob, as always.

Bob: Yeah. I love that expression. Justin, great talking to you. We'll see you next month.

Justin: Thanks.