

Modulaire: Building through Modules

Last week, Modulaire, a UK provider of modular space leasing and remote accommodation services, released its latest financial results.

Modulaire is a credit with exposure to cyclical end-markets, including construction and industrial sectors. Among credit portfolio managers in the European high-yield market, Modulaire is a well-known name; many investors have engaged with this sector and this credit in particular since TDR, the former sponsor, acquired Algeco in 2004. Brookfield Business Partners subsequently purchased the company from TDR in 2021.

The sector has always faced challenges and financial difficulties, as many investors recall the contentious restructuring of Algeco Scotsman in 2017 (I have been investing in the credit since the aggressive and famous deals brought to the market by RBS in 2005-2008). Arguably, it is one of the most challenging industries to analyse because it requires an examination of various end markets, such as housing, infrastructure, and public buildings to name just a few examples.

In discussions with colleagues and other investors, I have often struggled to reconcile Modulaire's reported total net leverage, which the company calculated to be just above 5x in 2022, with my own estimates that exceed 6.2x when excluding critical EBITDA adjustments and incorporating the impact of lease financing.

By 2022, the economic downturn began to affect Modulaire's end markets, prompting the company's management to consider whether to consolidate the borrower's balance sheet or pursue growth through acquisitions. Ultimately, they opted for the latter approach, which, compounded by an already weak construction market, has strained the company's credit metrics, pushing leverage above 6.5x, approaching 7x, and ultimately exceeding that threshold.

The credit picture has been mixed for quite some time.

Rating agencies began to raise alert signals toward the end of 2024 and the beginning of 2025, indicating that concerns have been surfacing for some time. Many investors remained unfazed (especially CLOs).

While I will not delve into the numbers complexities, management's initiatives, and results of the last three years, I can affirm creditors have continued to show

strong and significant confidence in the company's liabilities despite a backdrop of deteriorating operating performance and elevated leverage. Throughout this period, I have closely monitored key financial indicators, including capital expenditures, fluctuations in working capital, free cash flow (negative), and the weak interest coverage ratio. The persistent contraction in demand for its modular space and storage units has emerged as the primary driver of the negative outlook.

I have consistently been intrigued by the volatility of the SUNs, notes that I have never particularly liked or fully understood in their price fluctuations, especially during the recent rally that occurred a few months ago before the drop in secondary since mid of February 2026.

The critical issue for Modulaire, which has always intensely focused on managing its liabilities (totaling around €4 billion), see the refinancing of July 2025, arises in the context of many other companies acquired in 2021 and 2022 at elevated multiples, financed through a blend of senior term loans, senior secured notes (SSNs), and unsecured notes (SUNs). Currently, Modulaire's liabilities—rated B3/B—are set to mature in 2028, totaling approximately £1 billion, with additional maturities for another €2 billion in 2031. The presence of €435 million in CCC-rated SUNs maturing in Q4 2029 (issued in 2021 but difficult to address or refinance until today for obvious reasons), positioned in the credit curve between secured debt instruments, complicates the analysis and raises concerns regarding the borrower's ability to manage its capital structure effectively over the next 24 months.

When asked for my perspective, I believe that by 2027, Modulaire will need to confront its balance sheet and excessive debt. Potential strategies for addressing this situation may include asset disposals, sponsor support, or organic deleveraging initiatives. In my view, the prospects for an upswing in end markets, put under pressure from interest rates and other factors, appear limited (a point clearly shown in Q1 2026 results), and I do not anticipate that divesting its APAC operations will sufficiently resolve its financial challenges.

While Brookfield's support may serve as a critical lifeline, a strategic assessment and execution of any LME will require innovative solutions and possible restructurings of existing debt, which may necessitate adjustments likely already reflected in current market prices. The yield to worst (YTW) of the notes and term loan appears, at this moment, to compensate for the associated risk.

A potential and big issue could arise from a rating downgrade to CCC—currently avoided due to strong liquidity and the absence of short-term debt maturities—which could create new scenarios and affect recovery outcomes even on the long senior bonds and term loan.

One final point: credit investors have financed and tolerated high-leverage metrics in the sector, likely due to its resilience and elevated EV/EBITDA multiples observed in recent years. The general business model possesses both attractiveness and rationale, particularly for larger players. However, in my opinion, the concerns lie with the maturity of the liabilities, which in the high-yield credit market often do not align with fluctuations and downturns in economic cycles, placing the involved companies at risk. I leave interest rates considerations on the side.

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