

THE LARGE FIRM - MEDIUM FIRM DIVIDE

What is really happening out there?

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In the relatively small environment for commercial work in the main metropolitan centres there are some profound changes going on which will have a significant impact, if the trends experienced across the Common Law world are replicated here – as they usually are.

Consolidation is taking place overseas, particularly among the 'Magic Circle' firms who, in local terms, variously number 4, 6 or 8 firms depending on who you are talking to. Overseas, there has been a polarisation of firms receiving instructions from heavyweight clients partly because it is only very large firms who can assemble several large multi-disciplined teams to meet simultaneous demands for 'big ticket' work. Locally, further pressures may be at work – the market for major work may be shrinking as a reflection of the migration of large NZ listed companies to Australia. This may explain why some large NZ firms are seemingly prepared to undertake work their overseas counterparts would actively chase away. I am referring to residential conveyancing and wealth management work. Big European and US firms simply do not have this expertise and cannot carry out the work. As for providing local print media with comment columns that all too frequently cover mundane issues – elsewhere it simply wouldn't happen – this would be reserved for boutique and medium size firms. There is also the international perspective to consider; NZ doesn't have truly international partnerships preferring, rightly, to maintain correspondent arrangements as required.

There are also real differences in the way large and medium size firms operate. For example, the way matters are handled – large firms' corporate clients are driven to some extent by the capacity of their legal team to add value to their business by the weight of their expertise combined with reputation. By contrast, medium size firms are often more process driven. This process approach is particularly noticeable for some firms who have been successful in capturing market share and developing specific expertise so that they effectively control market access. When reputation is less important and matters do not require large, highly specialised teams some interesting dynamics emerge. The large commercial firms have, in effect, locked-in pricing models and cannot easily compete economically with the more nimble medium size firms. This has occurred as large firms have eschewed building value, preferring to leverage all the profit from the clients now, lest they move to another firm. Add in very low HR leverage/gearing ratios and the results become obvious. If personal income is placed at risk partners will undertake work that should in usual terms be delegated. This perpetuates low gearing and fosters an 'eat what you kill' remuneration system. The fee earning capability of a team comprising a partner and 1-2 assistants on high and fixed charge out rates is limited and often produces little more than \$1M - \$1.3M a year. Hardly great and not a pleasant prospect when well set up medium size firms with lower fixed and variable costs per lawyer can do better from environments that many perceive as more congenial.

What will happen if these opinions are correct? The present crop of magic circle firms becomes vulnerable and is likely to decline in number, through amalgamation and/or downsizing. This presents the next tier down with a golden opportunity and the supply of ready made partners and well trained assistants will be there for the taking. The more nimble of the medium size firms should be able to wrest the presently marginal (low or no profit) work from the big boys and process it profitably. The task is not easy and will require careful strategising but if overseas experience is a guide (and it usually is) it can be done. The key tasks for the medium size practices are to:

- Research, plan and implement, measure and monitor
- Develop systems and applications (including forms and precedents)
- Invest in IT & Training
- Set work assignment/management protocols (including delegation routines)

and, in the words of the marketers, 'go for it'. The timing has never been better; the economy is coming off a high, big firm partner incomes will become vulnerable, clients are aware they can dictate terms/conditions of how/who does their work and at what cost.

Planning for and managing change is not for the faint hearted but thankfully it is what we have been doing for years, well decades actually. Call us, we can offer a range of services designed to optimise law firm performance.