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Secrets of success in this year's UK 200

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Focus and a ruthlessly realistic outlook are required in an increasingly segmented and comparatively low-growth market.

This year's The Lawyer UK 200 presents a mixed picture of law firm performance in 2014/15. Some firms have grown well in both revenue and profits while many have flatlined or even declined.

Many factors have caused this variation. Some of the largest international firms suffered due to currency weaknesses, especially the euro. Some grew their revenue as a result of mergers, new offices and team moves. Others posted an impressive recovery after a couple of "challenging" years.

It is clear that firms are generally finding it difficult to achieve profitable growth. Chargeable hours per lawyer did not increase materially in many firms. Furthermore, pressure on fees and the continued rise of fixed price or capped fee billing meant extra hours worked did not necessarily translate into higher revenue. Levels of utilisation and realisation are still significantly below pre-recession levels, keeping the pressure on law firm margins.

Firms have done most of the obvious cost cutting and managed out underperforming associates and partners, so further cost improvements are likely to be incremental rather than transformative. In addition, firms are encountering wage inflation, especially in London, and hot spots are already being reported in the recruitment of the best 3-year to 5-year associates. This is exacerbated by the US firms (who now have around 5,000 lawyers in the UK) who are prepared to pay significant uplifts for associates and still appear to be able to offer attractive guaranteed packages for the right partners. Furthermore, rents for prime office space are rising, putting pressure on firms subject to reviews or looking for new space.

Segmented profitability

What is clear is that in terms of profitability the top 100 market is continuing to segment. Although profit per equity partner (PEP) figures need to be used with caution, especially given the different uses made by firms of non-equity partners, as a rule larger firms are more profitable.

Of the eight firms reporting PEP over £1m five were magic circle [including Slaughter and May] with Macfarlanes and then two very different models: Stewarts Law andDickson Minto. Seven firms saw PEP of between £750,000 and £1m – DLA Piper,Herbert Smith Freehills, Mishcon de Reya, Travers Smith, Stephenson Harwood, Digby Brown and Sackers. A further 18 achieved PEP of between £500,000 and £750,000. This means 67 firms had a PEP of less than £500,000.

Overall, these are still strong figures and mean that most top 100 firm equity partners are in the top 1 per cent of earners in the country. However, the level of segmentation and range of performance is increasingly stark.

Size may not be everything but well over half (18) of the highest PEP firms are in the top 25 by revenue, whereas only four are in the bottom 25 by revenue of The Lawyer 100.

The profitability of the larger firms (which is generally also reflected in revenue per lawyer figures) inevitably encourages lateral movement. The top PEP UK firms, which are consistently raided by some of the more profitable US firms seeking to grow their London practices, can themselves seek recruits from well-regarded but less profitable UK firms. Indeed, for some firms the challenge runs deeper. They may invest in developing a reputation in a market area only to find a bigger firm taking the team rather than growing its own.

Another continuing trend is the extent to which firms are getting bigger. Seven of the top 100 firms have revenue of more than £1bn and 40 have revenues of over £100m. Indeed, the revenues of firms 101 to 200 are, in aggregate, less than that of the highest revenue law firm (DLA Piper).
Size is not everything but it does lower the cost per equity partner of any investment in IT, process centres, offices, laterals or teams and, if used well, can allow firms to develop broader and deeper relationships with their clients. However, there is clearly great reluctance among many firms to address this issue by merger, especially if they are the smaller party. This is often for understandable reasons, but it increases the pressure on the leadership of firms to identify other means of growing revenue and profits or, at least, holding them steady.

Focus and drive
There are no knockout trends evident in this year’s The Lawyer UK 200. There are certainly many firms of different sizes, business models and market and sector focus that are successful. The most successful show a level of clarity, focus and drive that is significantly greater than their peers. But, as the market continues to segment in terms of revenue, PEP, clients, practice and sector, all firms need to be brutally realistic to ensure their strategy and its execution are fit for purpose in this competitive and comparatively low-growth market.

By Tony Williams, principal, Jomati Consultants