

in-depth:

Market Threats 2019

an Altman Weil special report
Law Firms in Transition

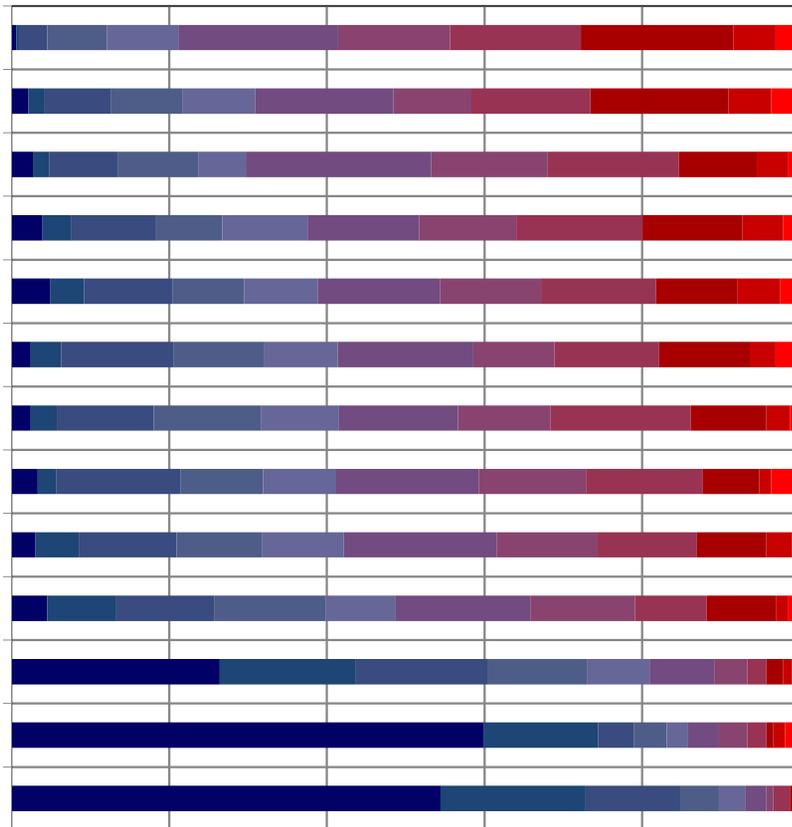
in-depth: **Market Threats 2019**

In the *2019 Law Firms in Transition Survey*, we asked law firm leaders to rate their concern about the threats posed by a range of market forces. In this report we've added a new breakout of the top responses from each of five law firm size categories to illustrate where each cohort differs and where they align. To add a new level of context, Altman Weil experts have rated the threats based on their own market perspectives and expanded on their thinking about top threats in brief essays.

Conducted in March and April 2019, the *Law Firms in Transition Survey* polled Managing Partners and Chairs at 810 US law firms with 50 or more lawyers. Completed surveys were received from 362 firms, including 49% of the 500 largest US law firms and 46% of the AmLaw 200. A copy of the full survey can be downloaded at: www.altmanweil.com/LFiT2019.

How concerned are you that each of the following market forces will negatively affect your law firm in the next five to ten years?

Rate on a scale of 0 to 10: 0 = Not at all concerned to 10 = An existential threat



Broad economic recession	6.0
Competition from larger firms	5.6
Competition from more differentiated firms	5.3
Inability to retain high-potential associates	5.2
Loss of key clients when partners retire	5.0
Too many underproductive lawyers	5.0
Artificial intelligence tools	5.0
Alternative Legal Service Providers	4.9
Competition from lower-priced firms	4.8
Loss of key partners to other opportunities	4.4
Onerous lease obligations	2.4
Unfunded retirement obligations	1.4
Excessive bank debt	1.2

AVERAGE RATINGS
ALL LAW FIRMS



0 = Not at all concerned

10 = An existential threat

How worried are law firm leaders in 2019?

Not very, according to the 2019 *Law Firms in Transition Survey*. On a scale of 0 (not at all concerned) to 10 (existential threat), no potential market threat rated higher than 6 on average and few law firm leaders see any existential threats at all.

How concerned are you that each of the following market forces will negatively affect your law firm in the next five to ten years?

Rate on a scale of 0 to 10: 0 = Not at all concerned to 10 = An existential threat

50-99 LAWYER FIRMS	
RANKING	AVG.
1. Broad economic recession	5.8
2. Loss of high-potential associates	5.5
3. Loss of clients as partners retire	5.4
4. Larger firms	5.3
5. More differentiated firms	5.0

100-249 LAWYER FIRMS	
RANKING	AVG.
1. Broad economic recession	6.0
2. Larger firms	5.7
3. More differentiated firms	5.4
4. Loss of high-potential associates	5.3
5. Underproductive lawyers	5.1

250-499 LAWYER FIRMS	
RANKING	AVG.
1. Larger firms	6.4
2. Broad economic recession	6.3
3. More differentiated firms	5.5
4. Artificial intelligence tools	5.1
5. Underproductive lawyers	5.0

500-999 LAWYER FIRMS	
RANKING	AVG.
1. Broad economic recession	6.4
2. Larger firms	6.1
3. Lower-priced firms	5.8
4. More differentiated firms	5.7
5. Underproductive lawyers	5.5

1,000+ LAWYER FIRMS	
RANKING	AVG.
1. Broad economic recession	6.9
2. Alternative Legal Service Providers	5.8
3. Artificial intelligence tools	5.6
4. More differentiated firms	5.4
5. Underproductive lawyers	5.4

TOP FIVE CONCERNS

- BY FIRM SIZE -

- ⇒ Firms of all sizes are concerned about an upcoming recession, as well as the competitive threat posed by more differentiated law firms.
- ⇒ All firms under 1,000 lawyers worry about competition from larger law firms.
- ⇒ Firms with 100 or more lawyers share a concern that they have too many underproductive lawyers in their firms.

#1 THREAT

Artificial Intelligence Tools Doing Work Once Done by Lawyers

By Thomas S. Clay

Undeniably, the single greatest threat to lawyers and law firms is the continued and accelerating erosion of work that has historically been their sole purview. Lawyers, like other professionals, have relied on specialized knowledge for generations as their highest value to clients. They have been historically, what Peter Drucker called "knowledge workers," with very little competition from people who were not lawyers. That has all begun to change and the pace is accelerated by the application of artificial intelligence and machine learning.

Work that lawyers have done exclusively in the past such as document drafting, due diligence, document review in litigation matters and the like is already being done by machines. As lawyers and nonlawyers increasingly train machines to do these kinds of work at a much lower price point, available lawyer billable hours will continue to erode.

Moore's Law states that technological capabilities will double every 24 months. Apply that to what is going on already in the use of artificial intelligence and it's clear how fast the erosion will occur. All firms should be seeking to understand how AI is already being applied in the legal marketplace and, more importantly, considering how it is or will affect their various practices. It really isn't a question of if firms should participate but if they will do so before they fall too far behind and the market moves beyond them.

Finally, dozens of law firms both large and small are experimenting with and adopting more sophisticated, next-level artificial intelligence in their practices. These firms are capturing first-mover status that will likely translate to a long-term competitive advantage.

TOM CLAY RATES THE MARKET FORCES

RANKING	RATING
1. Artificial intelligence tools	10
2. Alternative Legal Service Providers	9
3. Underproductive lawyers	9
4. Loss of key partners	7
5. Loss of key clients as partners retire	6
6. Larger firms	6
7. More differentiated firms	5
8. Loss of high-potential associates	5
9. Broad economic recession	3
10. Onerous lease obligations	3
11. Unfunded retirement obligations	3
12. Lower-priced firms	2
13. Excessive bank debt	1

Tom Clay heads consulting assignments in strategic planning, law firm management and organization and law firm mergers and acquisitions. He is the co-author of Altman Weil's *Law Firms in Transition Survey*. Contact Tom at: tsclay@altmanweil.com.

#1 THREAT

Broad Economic Recession

By Eric A. Seeger

“Existential threat” is a high bar, but a broad and deep economic recession would accelerate many of the market trends that law firms have been wrestling with over the last ten years and cause a major shakeup over the next ten. Firms will suffer and some will fail.

Our survey work has shown widespread agreement that heavy competition, price sensitivity, technological encroachment, alternative providers, commoditization and the like are permanent fixtures in the legal marketplace. Clients have been staffing up to handle work more economically in-house and are gaining confidence in non-law firm providers of lawyerly services. Artificial intelligence and less sexy technology developments will continue to eat away at the need for pricey lawyers. A broad economic recession will exacerbate all the usual problems as clients deal with another round of budget cuts, vendor reviews and reassessment of organizational priorities.

A recession is coming. I know not when, how deep, or how long, but I know that it will create new pressures and intensify familiar pressures in such a way that complacency, inertia and fear will yield to the need to redefine, restructure and repackage what law firms do and how they do it. Firms should be thinking about this now to avoid crisis management later.

I’ve given low weight to the problem of “too many underproductive lawyers” because that very real problem is easily solved in an environment where other firms are firing them too – but then those lawyers become yet another form of competition as they disperse among the non-law firm options and join or create virtual networks of high quality, low-cost, on-demand legal talent.

ERIC SEEGER RATES THE MARKET FORCES

RANKING	RATING
1. Broad economic recession	10
2. More differentiated firms	8
3. Lower-priced firms	8
4. Alternative Legal Service Providers	7
5. Artificial intelligence tools	7
6. Loss of key clients as partners retire	7
7. Larger firms	6
8. Loss of key partners	6
9. Onerous lease obligations	6
10. Unfunded retirement obligations	3
11. Excessive bank debt	2
12. Loss of high-potential associates	2
13. Underproductive lawyers	1

Eric Seeger works with law firms on strategy formulation and execution, practice group planning and training, merger search, and organizational issues including administrative audits and succession planning. He is the co-author of Altman Weil's *Law Firms in Transition Survey*. Contact Eric at: eseeger@altmanweil.com.

#1 THREAT

Broad Economic Recession | Too Many Underproductive Lawyers

By James D. Cotterman

Recession – I believe the fundamental signals are aligning in a way that suggests a heightened likelihood of recession. My guess is it will be milder and longer than the last recession. Milder because we are less exposed to extreme overheating. Longer because of the structural deficits, high national debt and already historically low interest rates, as well as the hyper-political divisions that limit policy makers' response options and challenge reaching consensus on corrective measures. This profile also holds mostly true in the EU. High corporate and personal debt will decrease investment and consumption opportunities to grow out of recession. Those with strong balance sheets will be able to ride it out, but not alter its course.

Underproductive Lawyers – Despite solid evidence of the effectiveness of removing underproductive lawyers, far too few firms have undertaken the effort. Profession-wide there remains a 13% or so overhang of warehoused lawyer talent. This will be exacerbated for three reasons: 1) the recession will bring about a drop in demand causing a spike in overcapacity; 2) technology proficiency, which some states have made an ethics requirement, will further reduce the labor component of legal services; 3) there is not a one-to-one transfer of work from underproductive lawyers, as underutilized lawyers' work is often completed by busier lawyers in less time. This means deeper cuts are required to obtain desired productivity levels.

Longer-Term Threats – Looking at the full ten-year horizon, I believe Artificial Intelligence will lead the threat list, as we see a permanent shift in the lawyer-centric business model away from labor and toward automation. This will be exacerbated as Alternative Legal Service Providers and in-house counsel continue to chip away at work directed to law firms making demand more volatile.

JIM COTTERMAN RATES THE MARKET FORCES

RANKING	RATING
1. Broad economic recession	8
1. Underproductive lawyers	8
3. Artificial intelligence tools	6
4. Loss of key clients as partners retire	6
5. Alternative Legal Service Providers	4
6. Loss of key partners	4
7. Unfunded retirement obligations	4
8. Larger firms	3
9. Excessive bank debt	3
10. Onerous lease obligations	3
11. More differentiated firms	2
12. Lower-priced firms	2
13. Loss of high-potential associates	2

Jim Cotterman is a thought leader on law firm compensation, capital structure, profitability and other economic issues. He also advises firms on governance, management and law firm merger assessments. Contact Jim at: jdcotterman@altmanweil.com.

#1 THREAT

Loss of Key Partners to Other Firms / Opportunities

By James S. Wilber

In today's ultra-competitive marketplace, law firms frantically try to increase market share, as the competition between firms for work is the chief challenge they face. We see this resulting in the number of law firm mergers and combinations that have broken new records year-over-year for the past several years. We also see it in the only other way to obtain market share — hiring partners with solid books of business away from other firms.

At the same time, law departments continue to internalize more and more legal work. In order to hire experienced practitioners for the new volume of work, general counsel and their companies also are competing with law firms for partner-level practitioners.

Perhaps the newest indicia of the competition for talent is the rapidly increasing focus on lateral partner recruiting by law firms, and particularly the creation of new, high-level positions for professionals to lead those lateral recruiting efforts. The most astute firms make key partner engagement a part of the job description, asking their lateral recruiting professionals to determine what might make their most important partners less likely to consider approaches from competitor firms.

Losing partners with solid client followings can be devastating to a firm and it can take years to rebuild. It has often been said that the only assets a professional firm has are its people, and, for law firms, protecting those assets is of existential importance today.

JIM WILBER RATES THE MARKET FORCES

RANKING	RATING
1. Loss of key partners	9
2. Artificial intelligence tools	8
3. Broad economic recession	8
4. Underproductive lawyers	8
5. Larger firms	7
6. Loss of key clients as partners retire	7
7. More differentiated firms	6
8. Lower-priced firms	6
9. Alternative Legal Service Providers	5
10. Excessive bank debt	4
11. Onerous lease obligations	4
12. Unfunded retirement obligations	4
13. Loss of high-potential associates	2

Jim Wilber co-heads Altman Weil's services to corporate and government law departments, leads consulting projects in organization, practice management, and lawyer professional development and conducts high-level law firm executive searches.

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