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Strategy In A Down Economy

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The business press relentlessly reports recessionary news these days — layoffs, stock market volatility, speculation regarding further interest rate cuts by the Fed, reduced corporate earnings, the dot.com crash. We may not be in a recession (yet); economists require two consecutive quarters of negative growth in GDP for a down-term to be defined as such. But we clearly are in a slowdown. Many law firms today are finding a slowdown in their intake of new matters, reduced utilization, slower payment by clients, increasing receivables and slower revenue growth.

Law firm management is acutely aware of this situation and attempting to deal with it in a timely manner. In some firms this action takes the predictable form of hunkering down, cutting back on new hires and cutting costs in non-personnel areas — marketing, technology, travel and entertainment, communications. Other firms view this as an opportunity to increase market share, upgrade staff and client base, add and grow some practice areas, at the same time de-emphasizing or eliminating others, and through it all growing both revenues and profits. The difference between these two approaches is the difference between a short-term, tactical orientation and a long-term, strategic approach. Historically, firms taking the latter approach have survived recessions more effectively and been more successful in the long run. The strategies historically employed effectively in a down economy include the following.

Cost Reduction

Clearly costs need to be managed, and not just in a recession. Productive areas for focus include staffing, communications, travel and entertainment — but not to an extreme in marketing and client development, lateral acquisition, new lawyer hires, mergers and technology.

Lessons learned in the last recession of 1990-91 include problems created by moratoria on new hires, deep cuts in advertising and promotion and abandonment of technology improvements. Hiring moratoria resulted in a dearth of experienced, trained associates when the economy recovered; deep cuts in marketing sacrificed the positive momentum of prior efforts and exacerbated the slowdown in new business development. Abandonment of technology upgrades permanently ceded ground to those firms that stayed the course and achieved competitive advantage.

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Trading Up in Staffing

Economic difficulties of firms not sufficiently capitalized to hunker down effectively or that are otherwise in duress create opportunities for better capitalized firms to attract strong laterals, in many cases with portable client bases. At the same time, current legal staff can be vetted to eliminate those whose economic contribution over the intermediate term does not justify their continued presence. A convenient test to determine where such consideration should be directed is to consider the effect of a competitive withdrawal of each lawyer. If that effect would be an increase in the incomes of remaining partners, that lawyer should be considered a potential downsizing candidate. Were the competitive withdrawal to produce a decrease in the incomes of remaining partners, that lawyer should not be considered a downsizing candidate. Most lawyers can quickly and easily be categorized by this standard. Obviously, elimination of partners meeting this criterion will have a greater positive impact than elimination of lower-compensated associates.

Trading Up Clients

Scrutiny should be applied to clients in terms of rates, collections, discounting, write-offs and overall maintenance, to eliminate those less profitable to allow concentration on existing and new high-quality clients through an organized marketing effort.

Trading Up Practices

Investment in growth of discrete practice areas must be concentrated in those with greatest long-term potential. That requires an objective analysis of each area in terms of two primary factors — growth potential and future profitability, much of it driven by upward elasticity in rates. Practice areas with less growth and profit potential must be either eliminated or de-emphasized so profits are not diluted by their underperformance. This process requires a discipline that many firms find difficult to implement. A slowdown provides an opportunity to focus on this strategy.

Additionally, investment in "counter-cyclical" practice areas (bankruptcy, litigation, employment law) ideally should be made before a recession occurs. Plans also might include cross-training "up cycle" specialists in "down cycle" practices (e.g., corporate or real estate lawyers in creditors' rights or bankruptcy) to reduce externally induced impediments to utilization.

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Expanding Geographically

Recessions are not uniform, nationally. In 1990-91, the recession hit first on the East Coast, later on the West Coast, and the Midwest was hardly affected at all. Geographic expansion makes multi-city firms less vulnerable to localized economies, and is part of the strategic rationale behind new offices, especially those created by way of "remote" mergers. This is true in the international arena, as well. For example, the economic slowdown in the US has yet to affect UK and European economies.

Merger

Some experts identify two successful generic strategies in a down marketplace — occupying a niche or "aggressive amalgamation" — and identify the latter as the preferred long-term approach.[1] As a result almost every firm should be considering mergers which might create economic value for its owners and better secure its long-term future. In some cases this consideration might suggest a mega-merger or being acquired by a larger firm; in others, serial acquisition of smaller firms might be preferable; in still others, a merger of equals might be pursued.

Revenue Growth

Throughout most of the strategies to be considered in a downturn, one overriding objective is the increase is revenue growth, either in the aggregate or on a per-lawyer basis. Nothing will have a greater impact on profits in most firms than an increase in revenue per lawyer, almost all of which falls directly to the bottom line. RPL is directly affected by individual player productivity and by the number of lawyers. For example, elimination of an underproductive lawyer whose work can be re-distributed to others will immediately increase RPL and profitability.

Conclusion

Strategies for law firms in a down economy are often counter-intuitive. Hunkering down is less likely to succeed than a longer-term approach that draws on capital to invest in new lawyers, new offices, marketing and technology. Effective long-term strategic planning will consider recessionary contingencies and create the capital structure to enable continuing investment, even when economic times are hard. ◆

1 Day, George S., "Strategies for Surviving a Shakeout," *Harvard Business Review*, March-April 1997, page 92.

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