Global Trends in the Legal Market and Asia's Influence: Critical Factors for Success
The International Legal Market Consists of Two Broad Groups of Firms

Each group following a somewhat different strategy

- **The ‘Global Elite’ (GEs)** made up of the UK’s Magic Circle and the very top Wall St firms – a group of 12 to 14 firms
  - Target the largest transactions and financial deals plus Litigation

- **The International Business Law firms (IBLs)** consisting of 25 to 30 mainly US and UK firms with more that 25% of lawyers abroad
  - This group includes Latham, White & Case, Mayer Brown, Herbert Smith Freehills, Ashurst, Baker & McKenzie, DLA Piper, Jones day, K&L Gates for example
  - Some are focused more upmarket and some more focused down

- **There is also some blurring between the groups**

- **The GEs** are transaction focused, with the major capital markets as their primary locations; the Global 500 corporates (and similar) as their core client base
  - Target the largest transactions and financial deals plus Litigation

- **The IBLs** offer a wider practice focus and seek to locate in major legal markets in the world – the client focus being the Global 500 to 1000
  - Need strong domestic practices in order to win market share in local markets and then generate international work out of their clients
  - Hence many more offices and they develop competitive domestic practices in all locations – present a serious threat to independent local firms
There has been a major expansion among the leading international firms – both by office and by jurisdiction

And particularly by the International Business Law firms

<table>
<thead>
<tr>
<th></th>
<th>Offices</th>
<th>Jurisdictions</th>
<th></th>
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</thead>
<tbody>
<tr>
<td></td>
<td>2010</td>
<td>2013</td>
<td>Change</td>
</tr>
<tr>
<td><strong>UK</strong></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Global Elite</td>
<td>125</td>
<td>141</td>
<td><strong>13%</strong></td>
</tr>
<tr>
<td>IBL</td>
<td>284</td>
<td>344</td>
<td><strong>21%</strong></td>
</tr>
<tr>
<td>Total</td>
<td>409</td>
<td>485</td>
<td><strong>19%</strong></td>
</tr>
<tr>
<td><strong>US</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Global Elite</td>
<td>86</td>
<td>92</td>
<td><strong>7%</strong></td>
</tr>
<tr>
<td>IBL</td>
<td>410</td>
<td>463</td>
<td><strong>13%</strong></td>
</tr>
<tr>
<td>Total</td>
<td>496</td>
<td>555</td>
<td><strong>12%</strong></td>
</tr>
</tbody>
</table>
Clients continue to push for a more competitive approach from their legal service providers

Maintaining pressure on firms if they wish to be selected – a buyer’s market

• The demand side of the market is driving change within the supply side
  – Clients choose firms based on their perception of a firm’s strengths
  – Seeking greater certainty in the price of work – and greater efficiencies in the work processes
  – Reducing the number of firms who are their main suppliers: fewer firms are sharing the work
  – Building an in-house capability where they can be more competitive than external suppliers
  – Increasing their use of Legal Process Outsourcing, contract lawyers etc
  – Demanding better industry knowledge, company knowledge and client service from suppliers
  – Seeking deeper and wider relationships with their main suppliers – requiring firms to invest more time in these activities

• Internal resistance and systems inhibit response to these pressures
  – Requires a significant change in how many firms have operated until now
    • Partner resistance to change is strong in too many cases
    • Performance metrics need to change to reflect the required changes in partner behaviour

• Many firms will not adapt easily to what clients are demanding – leading to a reduction in the number of highly competitive firms
MAJOR COMPETITIVE TRENDS IN THE GLOBAL LEGAL MARKET CONTINUE UNABATED (1/2)

With competitive pressures requiring a change in business models

• A few firms are responding by improving their service delivery and client relationship management processes
  – Seeking increased consistency in service levels – especially between offices
  – Managing through practice groups across offices in an effort to ‘enforce’ standard processes
  – Investing heavily in training, technology, knowledge management and standardising work
  – But partner resistance to change is strong

• A number of US firms are following their UK peer firms by broadening partner performance metrics – recognising that performance is more than generating hours
  – Revenue/profit managed by a partner is replacing Personal Billable Hours as a major metric
  – Including metrics on client relationship management and business development activity (not just origination)

• A growing realisation that the underlying issue is achieving behaviour change within a partnership
  – Many of the required changes require a fundamental shift away from the traditional practice of law

• But the majority of firms are still working along the traditional model
MAJOR COMPETITIVE TRENDS IN THE GLOBAL LEGAL MARKET CONTINUE UNABATED (2/2)

With competitive pressures requiring a change in business models

- Four major trends are reshaping global markets
  - Market segmentation
  - Pricing and work process efficiency
  - Demand vs Supply focus in the business model
  - Globalization
    - With consolidation and scale advantages being across all of these

- These trends will impact firms at all levels and in all legal markets
  - The difference between firms and markets is one of timing
  - These trends are more obvious in mature markets and at the upper end – but are spreading outwards and down

- While the impact of some of these will be felt more in the long term, firms need to be planning for them now
  - It will be too late once they are ‘on your doorstep’
MARKET SEGMENTATION IS CHANGING THE LAW FIRM BUSINESS MODEL

Requiring greater strategic clarity – and a more competitive approach

• Market segmentation breaks a large, mainly undifferentiated market down into segments that differ in their competitive requirements
  – Closely related segments allow a firm to pursue them within the same strategy
  – Others will have widely different bases of competition, making it difficult for a firm to compete across a wide range of segments
    • Means a firm fails to compete effectively in any segment
    • Or if it succeeds in one, it will be difficult to do so in the other
    • E.g. competing in both high-value and low-value market segments is no longer possible

• Need to identify the client types and work types that represent the core business in the market position on which the firm is focusing
  – Where they compete effectively – other work types play a support role or are being abandoned
  – Equally, firms are moving away from clients who do not fit the core

• The move away from a ‘full service’ to a more focused strategic approach is well under way in the upper end UK firms
  – And US firms are beginning to follow this as well
Pricing is on the agenda of most firms – although few are dealing with the issue effectively

Tackling this requires a fundamental change in behaviour/working practices

- Clients are open to a variety of pricing methods but the trend towards more certainty in the end price is clear
  - Unquestioned hourly rate pricing has all but disappeared – except at the very high value level
  - Most hourly rate pricing is subject to significant discounting – partly requested by clients but also offered by competitive firms
  - Fixed or estimated pricing is slowly creeping in

- Partners in many firms are struggling to move away from hourly rate pricing – easier to just discount rates rather than make the behavioural change required
  - Discounting with no change in work processes simply erodes profitability

- Fundamental changes are required to work processes if firms are to meet the price constraints and maintain/improve profit margins
  - Need to understand the actual/likely end price before commencing the work
  - Manage the work to meet the price set by the client and the profit margin required by the firm
  - A complete re-orientation as to how law firms have worked

- Partner resistance to this is very high across the legal profession
THE DEMAND VS SUPPLY APPROACH TO THE BUSINESS MODEL IS A KEY ISSUE TO ADDRESS STRATEGICALLY

Then matching the supply elements to the demand issues

- 95% of law firms operate with a supply side model, while the market changes require a shift to a demand focused model
  - Marketing materials and selling approaches are supply focused
  - Lawyers focus on their technical expertise rather than their client expertise
- With a demand-side focus, client needs are understood and work types and processes are developed to suit these
  - A supply-side focus means that the work types are developed from the law firm perspective and then an attempt is made to accommodate client requirements
- The result is that law firms present themselves as a ‘department store’ for legal services
  - Everything laid out waiting for clients to match their needs to the law firm offering
  - Whereas a demand focus does the matching for the client
- Finding a balance between the supply side and demand side is crucial
  - Increasingly firms are realising the need to approach their business with a strong client approach
  - Focusing on the issues as the client sees them then adapting their ‘product’ to these
- A demand focus will change the role of the partner – including reducing the billable hours per partner
A different structure is taking shape over the next decade

- More than 50 law firms are competing either as Global Elite or International Business Law firms – or aspiring to do so
  - The market cannot support such a number given the size they will need to be to compete effectively across the globe
- By 2020 there will be a leading group of 10 or so firms with the capabilities to compete effectively in all major regions in higher value work
  - It will be a mixture of present Global Elite and IBLs
  - There will be a second tier of firms who compete in a lower value position than the first group
- There will be more transatlantic mergers, and mergers between these firms and local firms in many jurisdictions
- There will undoubtedly be more large law firm failures
  - The competitive demands plus the financing problems faced by partnerships are creating a very fragile environment
  - Some others will decline in market position and survive only by a significant restructuring – with many being forced into different ownership structures
THE LONG-TERM MARKET STRUCTURE WILL BE FUNDAMENTALLY DIFFERENT FROM THAT TODAY (2/3)

A different structure is taking shape over the next decade (cont’d)

• The middle ground in the mature markets will disappear
  – The high value end dominated by the successful international firms and smaller (often local) specialists

• Purely domestic firms seeking to compete at the higher value end will need a different focus to the international firms – a narrower focused strategy
  – A re-orientation of how a law firm works will be essential – moving to a demand focus rather than supply – and a new business model
  – A strong focus on client service, relationships, industry knowledge and local business/regulatory contacts
  – A strong international capability of some type for those at the upper end of a market
  – Focus on work in which the firm has a real edge
  – And work where their depth satisfies clients against the international firms
  – Focus on a small number of related industries
  – Adopt new pricing policies and cost efficient processes
  – Strong organization capabilities - implement efficient and effective management structures
A different structure is taking shape over the next decade (cont’d)

- There will be significant change at the lower value end as well
- Firms who seek to compete successfully here will face a range of new competitors
  - LPO suppliers; Contract Lawyers; low cost law firms with high leverage; artificial intelligence systems
  - Will need a new business model to succeed
    - Fixed price
    - No frills
    - Standardised processes backed by technology
      - Standardised cost structures
    - Partners who sell and supervise
    - Tightly managed – not a partnership governance model
    - Demand not supply focused

- Will require a different way of thinking – abandoning the traditional business model of law firms
THE CORPORATE MARKET SHOWS A SIGNIFICANT SHIFT TO EMERGING MARKETS – PARTICULARLY ASIA PACIFIC

Globalising of business leads to the globalising of law

Fortune Global 500 Companies (by Revenue)

<table>
<thead>
<tr>
<th></th>
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</thead>
<tbody>
<tr>
<td>North America</td>
<td>189</td>
<td>167</td>
<td>143</td>
<td>-46</td>
</tr>
<tr>
<td>Europe</td>
<td>178</td>
<td>190</td>
<td>161</td>
<td>-17</td>
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<tr>
<td>Asia Pacific</td>
<td>127</td>
<td>132</td>
<td>181</td>
<td>+54</td>
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<tr>
<td>Latin America</td>
<td>5</td>
<td>10</td>
<td>13</td>
<td>+8</td>
</tr>
<tr>
<td>Middle East</td>
<td>1</td>
<td>1</td>
<td>2</td>
<td>+1</td>
</tr>
<tr>
<td>Total</td>
<td>500</td>
<td>500</td>
<td>500</td>
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</tr>
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</table>

Note: There were 16 Chinese companies in the Global 500 in 2005 and 89 in 2012.
GROWTH RATES FOR THE LEGAL MARKET DEMONSTRATE THE GEOGRAPHIC SHIFT

Geographic diversity in growth rates will lead to a restructuring of the global legal market

<table>
<thead>
<tr>
<th>Forecast revenue growth (US$Bn)</th>
<th>2013</th>
<th>% of market</th>
<th>2017</th>
<th>% of market</th>
<th>CAGR</th>
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<tbody>
<tr>
<td>North America</td>
<td>390</td>
<td>48</td>
<td>504</td>
<td>44</td>
<td>5</td>
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<tr>
<td>West Europe (ex UK)</td>
<td>134</td>
<td>16</td>
<td>151</td>
<td>13</td>
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</tr>
<tr>
<td>UK</td>
<td>40</td>
<td>5</td>
<td>46</td>
<td>4</td>
<td>3</td>
</tr>
<tr>
<td>Russia/CIS/CEE</td>
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<td>1</td>
<td>17</td>
<td>1</td>
<td>8</td>
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<tr>
<td>Asia Pacific</td>
<td>109</td>
<td>13</td>
<td>215</td>
<td>19</td>
<td>14</td>
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<tr>
<td>Latin America</td>
<td>105</td>
<td>13</td>
<td>167</td>
<td>15</td>
<td>10</td>
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<tr>
<td>Africa</td>
<td>24</td>
<td>3</td>
<td>34</td>
<td>3</td>
<td>7</td>
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<tr>
<td>Middle East</td>
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<td>1</td>
<td>9</td>
<td>1</td>
<td>5</td>
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<tr>
<td>TOTAL</td>
<td>820</td>
<td>100</td>
<td>1143</td>
<td>100</td>
<td>7</td>
</tr>
</tbody>
</table>

Based on world economic growth forecasts and demand for legal services we forecast an average growth rate in the global legal market of 7% for next 4 years – with some slowdown to around 5% after that
THE ASIAN LEGAL MARKET WILL PLAY AN IMPORTANT ROLE IN SHAPING THE GLOBAL LEGAL MARKET

• The size and growth of the corporate and institutional business in the region will lead to a rapid growth in the market for legal services

• A leading position in the Asian market will be an essential component of global leadership
  – Some of the present leaders are likely to lose out due to a lack of competitiveness in Asia

• A key decision will be to decide on the core markets in Asia – leaders will not need to be everywhere
  – PRC, Hong Kong, Japan, Singapore, India, Indonesia are likely to be core
  – South Korea, Malaysia, Thailand, Vietnam, Cambodia, Taiwan and the Philippines likely to be secondary
  – But will need to monitor economic and industry developments

• A presence in Asia will be critical in winning work going out of the region
  – It is less about servicing work into Asia – although important
  – The nature of the market is that you need to be here to capture the work going out
FDI FLOWS HELP TO IDENTIFY THE MORE ‘OPEN’ ECONOMIES

Where international legal work is more likely

- The major countries in terms of FDI over 2007 to 2012 are:

<table>
<thead>
<tr>
<th>Country</th>
<th>FDI In (US$ Bn)</th>
<th>FDI Out (US$ Bn)</th>
<th>2012 GDP (US$ Bn)</th>
<th>2012 GDP/capita (US$ K)</th>
</tr>
</thead>
<tbody>
<tr>
<td>China</td>
<td>1236</td>
<td>486</td>
<td>8227</td>
<td>6</td>
</tr>
<tr>
<td>Hong Kong</td>
<td>437</td>
<td>460</td>
<td>263</td>
<td>37</td>
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<tr>
<td>Japan</td>
<td>72</td>
<td>582</td>
<td>5961</td>
<td>47</td>
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<tr>
<td>Singapore</td>
<td>250</td>
<td>143</td>
<td>277</td>
<td>52</td>
</tr>
<tr>
<td>South Korea</td>
<td>18</td>
<td>125</td>
<td>1130</td>
<td>23</td>
</tr>
<tr>
<td>Indonesia</td>
<td>74</td>
<td>29</td>
<td>878</td>
<td>4</td>
</tr>
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ASIA HAS BEEN A RECENT EXPANSION MARKET FOR IBLs – NEW PLAYERS AND EXISTING FIRMS EXPANDING

Newer players and Asian Offices and Lawyers (2006 – 2014)

<table>
<thead>
<tr>
<th>Firm</th>
<th>Offices</th>
<th>Lawyers</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2006</td>
<td>2014</td>
</tr>
<tr>
<td>Kirkland &amp; Ellis</td>
<td>0</td>
<td>3</td>
</tr>
<tr>
<td>Weil, Gotshal &amp; Manges</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>Latham &amp; Watkins</td>
<td>4</td>
<td>5</td>
</tr>
<tr>
<td>Orrick, Herrington &amp; Sutcliffe</td>
<td>1</td>
<td>5</td>
</tr>
<tr>
<td>DLA Piper</td>
<td>6</td>
<td>7</td>
</tr>
<tr>
<td>Baker &amp; McKenzie</td>
<td>14</td>
<td>14</td>
</tr>
<tr>
<td>Mayer Brown</td>
<td>0</td>
<td>7</td>
</tr>
<tr>
<td>Reed Smith</td>
<td>0</td>
<td>2</td>
</tr>
<tr>
<td>Total</td>
<td>27</td>
<td>46</td>
</tr>
</tbody>
</table>

Source: ALB Top 50, firm's websites, NLJ.
INTERNATIONAL FIRMS ARE BUILDING POSITIONS IN ASIA WITHIN A VERY FRAGMENTED LOCAL MARKET

- The top 50 firms in Asia have over 27,000 lawyers including 3,000 in firms based from outside the region, the US and UK
- The largest international firms are Baker & McKenzie (1032 lawyers); Clifford Chance (345); DLA Piper (303); Linklaters (299); Mayer Brown (254); Hogan Lovells (247); Herbert Smith Freehills (242); and Freshfields (235)
  - And 7 others with between 100 and 200 lawyers
  - There are over 150 foreign firms operating in the region (70 in Hong Kong alone)
- There are 25 UK and US firms each with over 20 lawyers in the region
  - This group has 3,500 lawyers and 120 offices in total
- There are some very large ‘local’ firms – 12 over 500 lawyers (includes KWM)
  - Although many are not organized into a coherent structure and operate more as a ‘loose group of individuals’ with little consistency
- The local market is very fragmented
  - e.g. of the 800 Hong Kong firms, 90% have 5 partners or less
  - This could change once LLP legislation is implemented – mergers will be likely
# The Top 50 Asian Law Firms Is Dominated by Chinese Firms

<table>
<thead>
<tr>
<th></th>
<th>Firms (no.)</th>
<th>Lawyers (no.)</th>
<th>Lawyers per Firm (avg.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>China</td>
<td>20</td>
<td>16212</td>
<td>811</td>
</tr>
<tr>
<td>South Korea</td>
<td>6</td>
<td>2866</td>
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</tr>
<tr>
<td>India</td>
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<td>1690</td>
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<tr>
<td>Japan</td>
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<td>1936</td>
<td>387</td>
</tr>
<tr>
<td>Singapore</td>
<td>4</td>
<td>1233</td>
<td>308</td>
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<tr>
<td>Hong Kong</td>
<td>1</td>
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<td>279</td>
</tr>
<tr>
<td>Taiwan</td>
<td>1</td>
<td>413</td>
<td>413</td>
</tr>
<tr>
<td><strong>Asian Firms</strong></td>
<td><strong>42</strong></td>
<td><strong>24630</strong></td>
<td><strong>586</strong></td>
</tr>
<tr>
<td><strong>UK/ US Firms</strong></td>
<td><strong>8</strong></td>
<td><strong>2968</strong></td>
<td><strong>371</strong></td>
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<td><strong>Total</strong></td>
<td><strong>50</strong></td>
<td><strong>27598</strong></td>
<td><strong>552</strong></td>
</tr>
</tbody>
</table>
BESIDE A FEW MAJOR PLAYERS, MOST IBLS HAVE YET TO DEVELOP ROBUST PRESENCES IN ASIA

IBL Lawyers by Firm and Region (2014)

Source: Firm Websites
THE ASIAN LEGAL MARKET IS LOWER IN CONCENTRATION THAN MANY MATURE MARKETS – ALTHOUGH HONG KONG IS GETTING CLOSE

Number of lawyers per 10k citizens

[Graph showing number of lawyers per 10k citizens for various countries, with Israel having the highest number, followed by the US, Brazil, and others in descending order.]
THE ASIAN MARKET CONTAINS A SIGNIFICANT NUMBER OF CHALLENGES – FOR FOREIGN FIRMS (1/2)

- There are some important issues that international firms will need to address if they are to succeed in Asia
  - Different cultural influences – between Asia and elsewhere and within Asia
    - A major influence on buying patterns
  - Pricing – local buyers are generally not prepared to pay the prices international firms charge
  - Relationships – requires a considerable amount of non billable time over a long period - usually with little revenue and profit
  - Need to bring on local lawyers at all levels
  - Training and lawyer development requires a different approach
  - Regulatory issues
  - Recruitment and secondments
  - Expatriate remuneration packages
The Asian market contains a significant number of challenges – and for local firms as well (2/2)

- There are some important issues that Asian firms will need to address if they are to succeed as independent of international firms
  - A clear strategic focus that positions the firm ‘to the side’ of the major international firms
    - A core practice and core client focus – not a full service approach
  - Recognise the strength of the international firms is much greater than their numbers in Asia
  - Developing clear role for partners – where they spend their time
  - Building client relationships with key decision makers - ensuring they know what you are best at
  - Developing an effective organisation that supports the lawyers achieve their goals
    - Business development
    - Technology
    - Human resources
    - Finance
  - Clear decision making processes that are effective in a competitive environment
MANAGING REFERRALS IS A KEY ISSUE FOR INDEPENDENT ASIAN FIRMS

• A fast growing emerging market will always create a strong flow of referral work from foreign to local firms
  – This work can be an attractive revenue source and profitable – helps maintain utilisation and can be good quality work
• Essential to monitor referrals in and not become too reliant on them
  – Firms referring in a volume of work are likely to set up here eventually
  – Partners can use this to avoid their own business development
  – Some referral work will be outside the strategic focus and create ‘busy fools’
  – A tendency for lower profit referral work to increase
• Firms find their strategic options are limited by the amount and source of referrals
  – Difficult to explore options if it affects referral flow
  – A minority of partners benefit more than others and block strategic moves
  – Referral work flows can be short to medium term and should not create barriers to longer term strategic thinking
• Referral work needs to be treated as a flow of work from specific clients and assessed for strategic importance, profitability and risk of ending suddenly
ENTRY INTO ASIA REQUIRES EXTREME CLARITY OF STRATEGIC VISION

It is not for the faint hearted

- It requires a significant investment planned over the long term
  - Establish long term goals for the business (5-year) and annual milestones in terms of development
  - Ensure the Asian strategy is a subset of the firm’s overall business strategy
  - Enter with one or two core practices, for which the firm has a strong reputation in its home market
    - ...and are core at home
    - Focus on ‘home market core clients’ where the firm’s name is known
    - Build a competitive depth in these practices
      - Outsource other work – beware of ‘strategic creep’
    - Develop the client base beyond ‘home’ clients
    - Only add another core practice once the initial practices are profitable
      - Repeat the process
    - Invest significant partner time in relationship building and business development
    - Structure the economics to suit the local market and the different role of the partner
There are seven areas on which all law firms need to focus for success in any market position

Many have given these some attention, but within a traditional view of the market

1. Ensure there is clarity of strategic positioning and the related strategy – and its acceptance within the firm – along with a supporting business model
2. Achieve competitive levels of performance – financial but also across a range of activities
3. Implement processes to ensure work is done cost effectively – while meeting profit targets
4. Develop very effective, structured and disciplined business development and client relationship programs – appropriate to the strategy
5. Develop an economic structure for each practice group – given its role in the firm’s strategy
6. Articulate and manage a set of acceptable behavioural standards
7. Implement lean and effective management structures, along with strong organizational processes that support the strategy