Managing Strategically, Managing Operationally

One of the most significant challenges for law firms in the current economic and competitive climate is managing effectively both their strategic development and operational performance. The strategic development is concerned with achieving agreed mid-long term strategic objectives and a future market position which provides a platform for building some form of sustainable competitiveness. Operational management, in contrast, is essentially concerned with the current, more immediate, financial and economic performance achieved including the servicing and winning of clients and achievement of other key related performance targets (covering, for example, HR, service standards, etc.).

At any time balancing these two critical facets of management raises challenges but perhaps now, more than any time in the recent past, in both the US and Europe, this requires a complex balance of analysis, judgement, sensitivity, resolve and courage of commitment.

More immediate, financial, economic and related considerations require firms to focus strongly on achieving particular levels of profitability to meet partners' expectations and to maintain performance broadly in line with peer group firms. A failure to achieve either or both will put at risk, at least to some extent, many firms' competitiveness both in terms of retaining the most ambitious and able partners and other lawyers and in terms of the financial attractiveness of such firms in the **lateral market**.

On the other hand, focusing very strongly on operational performance at the expense of investing in strategic development is potentially equally damaging. Of course, reducing investment in strategic development can assist firms achieve particular levels of financial performance in the short term. Remaining in cheaper, but inefficient premises, delaying upgrades in IT, cutting back on marketing and business development, reducing commitment to training and recruitment, holding salaries below the market norm and so on can all impact positively on profit margins, overall, profitability and profit per partner in the short term.

Taking 10,000, 100,000 or 1,000,000 Euros, Dollars or Pounds out of costs in this way can deliver a similar, or close to similar, increase in the bottom line.

The danger of any such decisions is that the impact on medium term competitiveness will be adverse and potentially, catastrophically so (assuming that the initial decision to make such investments was sound). Of course, all investment and expenditure decisions should be periodically reviewed and there is perhaps a validity in doing this more frequently in certain economic conditions. However, to overturn previous 'sound' expenditure and investment decisions simply on the basis of current economic conditions is both short-sighted and potentially highly damaging. Of course, there is a need to be realistic and pragmatic and the adage of 'cutting-one's cloth' is valid. There may also in some circumstances be some validity in the argument that 'if we don't achieve particular results in the short term there will be no long term'. (Our experience, however, suggests that this argument is put forward in many circumstances where there seems to be limited justification).

The reality, however, as can be witnessed within both the legal sector and all other sectors of the economy is that those who fail to invest adequately in their development ultimately fail. The world of both fast moving consumer goods and industrial products is littered with examples of sound businesses that in pursuit of short term operational targets were compromised in their ability to invest adequately in their strategic development and consequently ultimately failed. Examples of such failures can also readily be found in the world of banking and financial services and other professional services businesses. (This is not to imply that all such failures in such sectors are due to a lack of investment in strategic development but undoubtedly it is a factor in many such failures).

The 'balancing' challenge for many law firms between the short term financial demands and the need for investment in medium-longer term strategic development is, in fact, even more challenging than for businesses in other sectors. And the reason for this is as follows.

Some firms are currently 'underperforming' their peer group and are doing so for reasons that are unrelated to their 'fundamental competitiveness' (and by this term we mean their innate capability to perform at a level equivalent to their peer group). Instead they are underperforming for other reasons: perhaps they are significantly over staffed or over partnered and/or under leveraged. Alternatively, it maybe a consequence of how hard people do or are prepared to work; achieving 4/5 chargeable hours a day is simply not competitive in any part of the legal market nowadays, yet there remains a belief (or perhaps more accurately a forlorn hope) that because such levels of performance were historically adequate they remain so today. A third such reason for underperformance may relate to poor financial management: too high levels of work-in-progress, inadequate billing and collection procedures and so on - all contributing to unnecessarily low realisation rates. (Any firm that has a significant percentage of its billings and/or collections occurring in the last month(s) of the year (the year-end billing-blitz) is likely, at least in part, to be reducing its performance, and potentially substantially so, as a result).

The reality, however, is that most law firms that are underperforming their peer group are doing so for reasons directly related to their fundamental competitiveness and for such firms not to invest in their strategic development is a deeply flawed decision.

For firms that are generating below peer group average levels of profitability and margin due to a lack of fundamental competitiveness there has to be a significant and priority focus on building profitability back to levels comparable with competitor firms (or accept a market repositioning of the firm in a different, lower position in the marketplace); and to achieve this without investment and hence cost and impact on short term profit is highly likely to be an unrealistic expectation. Such investment is required, quite simply, to rebuild competitiveness to a point where competitive levels of profit can be generated.

Such investment may be in terms of restructuring, development of know-how and precedents, recruitment of new, higher calibre partners and other lawyers, targeted business development, upgrading of IT to improve service and/or reduce 'unit' costs, development and implementations of new services and/or more effective and efficient means of delivering existing services, and so on. Clearly, such investment has to be directed at those areas that are most important in terms of building or re-establishing competitiveness and client research can here fulfil a critical role in helping identify such areas. Irrespective, however, of where the investment is required, it clearly will be required somewhere and to expect to regain competitiveness (and this we define as performance at least the equal of any competitor in the perceptions of target core clients) is blatantly nave.

However, achieving such investment is no straightforward task when profitability is already below that of peer group firms and/or below partner expectations. It is, however, possible.

It requires above all else a partnership willing to accept reduced profit in the short term (in much the same way that some corporate businesses have to do so at times) in order to be able to invest adequately in building medium and longer term competitiveness and hence profit. Such investment maybe in terms of greater expenditure or in terms of reduced income - a consequence of some partners focusing increasingly on non-fee earning activities to build strengths and/or develop **new opportunities** that will contribute to the building of greater competitiveness, or it maybe a combination of the two.

In our experience those firms that have or currently are making such investments, even though current performance is below partners' expectations and/or that of peer group firms share a number of common characteristics. In particular such firms:

i) have a high degree throughout the partnership of commitment to a well thought out strategy;

ii) have a high level of loyalty throughout the partnership with shared values and ambitions;

iii) have an appropriate compensation scheme that encourages and recognises high levels of contribution and performance supporting the achievement of the firms strategic objectives;

iv) have a highly respected and trusted management that is closely in 'touch' with the sentiment in the partnership but is nevertheless prepared where necessary to make and implement unpopular decisions.

In the absence of such characteristics it is far less likely that any firm will be able to make and sustain the level of investment required to build competitiveness and without such investment the future is likely to be one of failure.

Hence, a critical challenge for any firm is to ensure that it pays substantial attention to maintaining its internal fabric and cohesion, making it more likely to be able to make and implement difficult decisions should the firm find itself in the position where it needs to do so.