

Positive Financial Progress Detected in Report on Law Firm Performance



In a recent analysis of first-quarter economic indicators, the Thomson Reuters Institute's Law Firm Financial Index has shown a positive shift in the financial picture for law firms. After more than a year of gloom, the index has risen by 14 points, marking the first increase since the second quarter of 2021.

One of the key indicators of this improved performance is the healthy growth in billing rates, which have increased by nearly 6% over the past year. This upward trend is a positive sign for law firms, indicating improved profitability. Additionally, law firm direct expenses grew at a slower rate in the first quarter compared to the previous year, as associate salaries have not been raised in the last 12 months.

The index also reveals an increase in demand for practices such as litigation and labor and employment, which typically thrive during a slow economy. Comparing the first quarter of 2023 with the last quarter of 2022, these practice areas experienced a noticeable uptick in demand. This positive shift can be attributed to current economic metrics being compared to leaner times in 2022 rather than the record-setting profits and high demand seen in 2021.

While the overall outlook is improving, challenges still persist in the legal industry. Profits-per-lawyer have declined by 0.6% over the past 12 months, although this marks the smallest decline in more than a year. Lawyer productivity has also fallen by more than 3% during the same period, suggesting a need for firms to address efficiency and performance.

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The index also highlights a divergence between large law firms and their midsize counterparts, each facing unique strengths and challenges. Midsize firms have experienced a nearly 2% increase in demand over the past year and have responded by expanding their headcount by almost 5%. However, this hiring boost has led to a direct expense increase of more than 8% for these firms.

On the other hand, Am Law 100 firms, known as the most profitable law firms in the United States, have managed to keep their direct expense growth to less than 5%. However, demand for their services has declined by nearly 2% over the past year, particularly affecting transactional practices. The 50 most-profitable law firms have faced a particularly steep slowdown in demand, as noted by William Josten, manager for enterprise legal content at the Thomson Reuters Institute.

Overall, the improved first-quarter performance in the legal industry signals a positive turn after a challenging period. With billing rate growth, increased demand in certain practice areas, and controlled direct expenses, law firms are regaining some stability. However, firms must address declining profits per lawyer and productivity to sustain this positive trajectory. The divergence between large and midsize firms also calls for careful management strategies to navigate their respective challenges and capitalize on their unique strengths.