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Have we forgotten about clients in merger discussions?

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Law firm mergers are fascinating things. They mix high drama and Greek tragedy as courting parties – initially with uncharacteristic coyness and latterly with a disregard to sensible decision making – waltz towards ultimate consummation. However, much of the discussion is tangential to the real issues at play.

Understandably, negotiating teams are keen to present a failsafe proposal focused on the consolidatory aspects of the deal – squeezing the cost base, removing duplication, reshaping the partnership, finding economies of scale and consolidating property.

They are proposals founded on a ‘sweat the assets’ approach which, combined with a reduction in partner numbers, seek to elevate PEP to the levels enjoyed pre-recession. They are founded in a belief that being better at what we already do will be sufficient.

I believe that this is a fundamentally erroneous starting point for such discussions. Firms need to be better at doing things differently rather than just more efficient at doing things the same way.

That is not to say that ‘sweating the assets’ or being more efficient are not important (for they surely are), but rather that a merger founded on such a premise simply puts off the inevitable day. With continuous downwards pressure on prices, the impact of new competitors which are unencumbered by a historic operating model and the inevitable cost-increasing effects of inflation, profit erosion will continue unabated in the new firm as it had in the old.

Perhaps one of the most striking (and worrying) manifestations of this myopic view of the opportunities afforded by a merger can be seen in the cursory way in which client opportunity is assessed, sensible revenue growth projections arrived at and the delivery of client services shaped.

It is almost as though the combined client base of the new firm is incidental when set alongside the cost saving opportunities. And yet it is the client base, combined with the new firm’s ability to exploit it in way that neither antecedent firm could, which presents the real opportunity of any sensible deal.

While initial consolidation benefits are both important and necessary, it is through revenue growth and operational improvements that sustainable profit increases will come. This can come from a limited number of sources:

- charge more for the current volume of work (which is fanciful in today's market);
- do current work volumes more efficiently than downwards price pressure erodes margin (which is necessary but difficult); or
- find ways of increasing volumes while simultaneously improving operational efficiency.

In any merger, the easiest way to increase volumes is through the combined client base. Yet the quantification of this opportunity, the assessment of the business development activities that will be needed to realise it and the confidence of the negotiating teams to present this to their partnerships as a series of scenarios (tested, sensible and stretching) is often missing.

A proposal based purely on cost reduction, combined with the presentation of an unchallenging operating model of 'business as usual' post-merger, trumps the more radical and ambitious scenario of operational efficiency and client opportunity maximisation all too often.

This is the real challenge in many merger negotiations. For the negotiating teams, the challenge should not be about how we rearrange the deckchairs on what is still, in the final reckoning, the Titanic, but rather how we create a new client-centric model, for a new world, which provides a sustainable future rather than simply a staging post before the next crisis.

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