2025 Client Advisory

We are pleased to present our 2025 Citi Hildebrandt Client Advisory, now in its 17th year.

We hope you find this valuable and welcome your feedback.

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Citi Global Wealth at Work

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Part I. The law firm market in 2024

We wrote in our 2024 Citi Hildebrandt Client Advisory that we expected firms to see a better year than we saw in 2023. So far, we have seen very strong demand and revenue growth in 2024[1].

Industry performance: 9mo'24 vs. 9mo'23

Revenue growth was up 11.9% for the first nine months of 2024. A critical factor in this strong growth was the 3.2% rise in demand. Firms have told us that they have experienced an uptick in demand across a wide range of practices, including litigation, regulatory (particularly anti-trust), funds/investment management, bankruptcy and restructuring – and, for some firms, large cap M&A. Meanwhile, outside of large cap M&A deals, M&A and transactional demand has generally been soft, as has capital markets demand.

As firms reported strong activity levels, we also saw average lawyer billing rate increases of 9%. While we need a full year's worth of data to calculate realization, early indications are that it has also improved, if not held steady.

The collection cycle lengthened by 0.6%. However, some segments shortened or saw only a marginal lengthening of their collection cycles. This is a positive shift from the recent trend of the persistent and notable lengthening of collection cycles across the industry.

Meanwhile, inventory at the end of September was up 12.6%, driven by 14.2% growth in accounts receivable and 11.1% growth in unbilled time. With a better collections experience and strong demand growth this year, many firms may have worked through the aged inventory challenges they faced through 2023. This means that firms have likely seen not just strong growth in inventory, but also an improvement in the quality of their inventory.

Headcount increased by 1.3% – a return to more normal growth levels following three years of unusually strong headcount growth. Headcount growth came from leverage increases, as equity partner headcount was down 0.2%. The normalized rate of headcount growth, coupled with strong demand growth, translated into average lawyer productivity growth of 2.2%. While the industry is not yet back to 2019 productivity levels, it is edging closer.

While equity partner headcount was slightly down in the first nine months of 2024, we have continued to see strong investment in income partners, up 4.4%. As a result, firms saw 1.8% all partner growth, signaling the continued growth mindset of firms across the industry.

[1] Our analyses and projections are based on data collected from a sampling of primarily US-headquartered law firms by Citi Global Wealth at Work, as well as conversations with law firm leaders. Sources include the "Citi Annual Survey Database" of 200 US- and UK-headquartered, including 43 Am Law 1-50 firms, 37 Am Law 51-100 firms, 55 Am Law Second Hundred firms, and 65 additional firms; 188 firms from the "Citi 9mo'24 Flash Survey," including 42 Am Law 1-50 firms, 38 Am Law 51-100 firms, 54 Am Law Second Hundred firms and 54 additional firms; the "Citi Law Firm Leaders Survey" of 57 large firms headquartered in the US, UK, China and India; and the "Law Firm Leaders Confidence Index" which reports the forward-looking opinions of law firm leaders from 136 firms.

Percentages used in the Figures may not add exactly to 100% due to rounding.

Expense pressure has also been present this year. Behind the 7.5% growth in total expenses, firms saw 6.7% growth in compensation expenses. While headcount growth was one factor, the higher cost per unit of leverage was another. Throughout 2024, firms continued to absorb the associate salary increases adopted in late 2023. Meanwhile, growth in income partners and counsel continued to shift the mix of leverage to a more senior, more expensive model.

We saw even stronger growth in operating expenses, up 8.2% for the first nine months of 2024. There were a number of drivers of this expense pressure, particularly office build outs and technology. We also saw increased spending on business development, travel and the continued upskilling of the professional staff leverage model.

Looking ahead to the full year results, the level and quality of inventory at the end of the third quarter place firms in a solid position for year-end collections. We have also heard that firms generally are continuing to see strong activity levels during the fourth quarter. As we continue to see interest rate cuts and with the US election now behind us, we expect to see continued positive momentum in transactional activity. If firms are able to collect on strong inventory levels, and even with expense pressure likely to continue, we anticipate very strong revenue and profit growth.

Performance by revenue segment

Looking at these nine-month results by law firm revenue size, all segments have experienced strong demand growth, most so Am Law 1-50 firms. For this segment, demand for the first nine months of 2024 was up 3.6% on average. While large cap M&A, corporate and transactional work has favored a subset of firms in this segment, this strong demand growth was driven by a range of other practices. There was other good news in the results for this segment. The uptick in demand was reflected in productivity gains, with Am Law 1-50 firms seeing the strongest growth in productivity – up 2.9%. We also saw a steadying of the collection cycle. Revenue growth of 14% outpaced expense growth of 8.2%, while inventory for the first nine months was up 14.1%. If firms are able to collect this inventory during the fourth quarter, we expect to see strong revenue and profit growth for this segment.

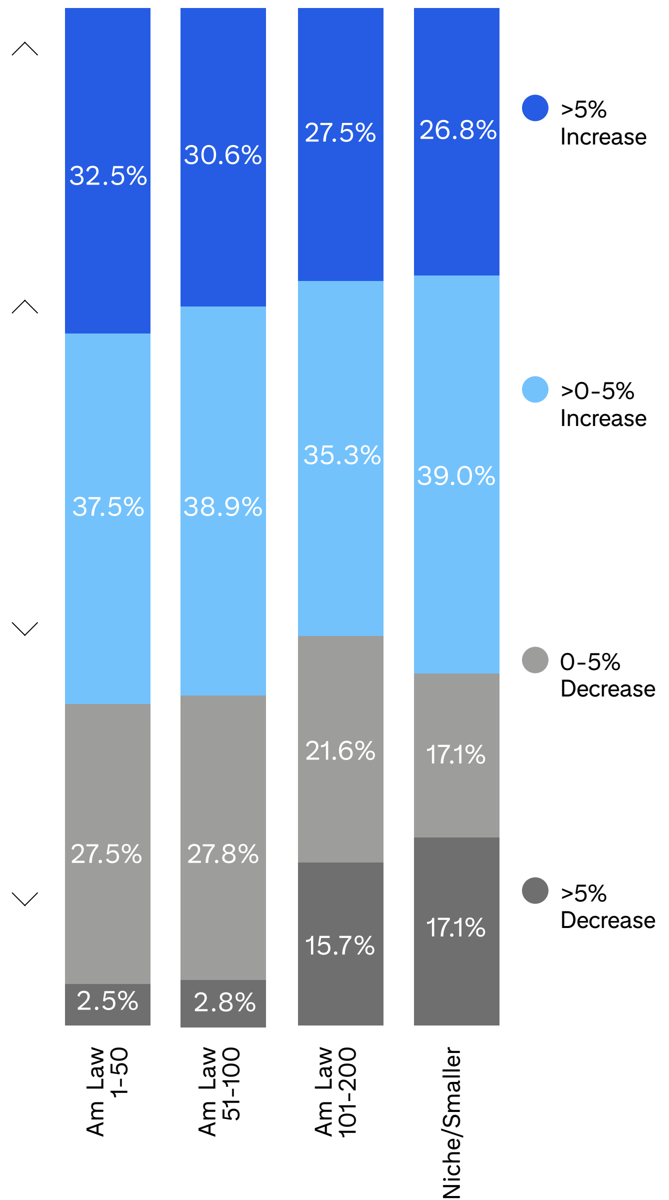
Other Am Law 200 segments have also had a positive demand experience so far in 2024, with demand up 3.2% for Am Law 51-100 firms and up 2.2% for Second Hundred firms. Revenue growth was up in the high-single-digits for both segments during the first nine months of 2024, outpacing expense pressure. With 9.9% and 8.1% growth in inventory for Am Law 51-100 and Second Hundred firms respectively for the first nine months, these firms could also see a strong year end if they are able to collect.

Among firms outside of the Am Law 200, we saw 2.2% demand growth during the first nine months of 2024. This segment also saw a relative stabilizing of the collection cycle. Revenue was up 8.5% for the first nine months, outpacing expense growth. With 8.7% growth in inventory for the first nine months, this segment is also positioned well for a strong year end if they can collect.

Industry demand dispersion: 9mo’24 vs. 9mo’23

Behind the averages, there was dispersion in the performance of individual law firms across all segments of the industry – **Figure 1**. The level of dispersion differed across the segments of the industry by size. In a reversal of last year, and a return to the trend we saw for many years prior, the largest firms outpaced other segments in demand performance – with 70% of Am Law 1-50 firms seeing demand growth through the first nine months of this year. Am Law 51-100 firms were not far behind, with 69.5% of these firms reporting demand growth. A majority of Second Hundred and smaller firms also reported demand growth, though there was comparatively greater dispersion within each of these segments. The presence of wider dispersion among firms outside the Am Law 100 segments suggests that we will likely continue to see consolidation involving Second Hundred and smaller firms.

Figure 1: Demand Dispersion by Revenue Segment: 9mo’24 vs. 9mo’23



Source: Citi Flash Survey © Citibank, N.A. November, 2024

Part II. Looking ahead to 2025 and beyond

A. Growth opportunities and challenges
B. Likely developments in the adoption of Generative AI
C. Growth trends to watch
D. Operational efficiency trends to watch

A. Growth opportunities and challenges

Looking ahead to 2025 – and beyond – there is good reason for law firms to be optimistic. It's clear that 2024 has been a year of improving demand. And, with the interest rate cuts we have seen in the second half of this year projected to continue in 2025, we expect to see positive momentum across a number of areas. These include M&A, corporate and transactional activity, alongside the ongoing success of practices that drove demand in 2024 – such as litigation, regulatory (particularly anti-trust), funds/investment management and bankruptcy and restructuring.

The 2024 Citi Law Firm Leaders Survey reveals that law firms continue to focus on three major opportunities in what's expected to be a strong year ahead. These are increasing their scale; "unlocking their platforms"; and leveraging the power of Generative AI ("Gen AI") to transform their businesses.

We have witnessed the growth mindset of many firms in recent years, as they have sought to outperform their peers through both organic growth and lateral talent acquisition in a historically modest demand-growth environment. Firms will continue to seek growth opportunities with clients where they are not serving all of their needs, across geographies or practices. They will also look to grow in specific high-growth practices and client industries, having seen other firms achieve success with this strategy in the past decade. Firms that invested early in private equity and funds/investment management practices are prime examples of this.

Inherent in growing scale is the effort to leverage the opportunities coming from lateral acquisitions. Having invested heavily in laterals, firms will be focusing on setting up those laterals for success – ensuring that partners across different practices and locations are collaborating to realize the potential of increased scale.

With another year of Gen AI development under the belt of the law firm industry, firms will also continue to look closely at the possibilities that Gen AI brings, not least in terms of the way they deliver legal services and run their businesses.

There are of course challenges ahead. As firms seek growth, they will also face the challenge of retaining talent in an aggressively active lateral market. Talent retention is challenging at the partner level – and it extends to associates and professional staff.

And while the steadying of inflation and recent interest rate cuts are positive signs for next year's activity levels, it's important to note that we remain in a challenging global geopolitical and macroeconomic environment.

As firms seek to grow in high-potential markets, we also expect to see the scaling back or closure of offices in less-profitable markets – as we have already seen with US firms' investments in China and Europe. During the latter half of 2024, we saw a number of large firms announce the closure of offices in less-profitable markets, as they committed to growth in specific, high-profit-potential markets.

Firms will also need to continue addressing the challenge of restoring and retaining their distinctive firm culture. Organizational cultures took a hit during Covid. And, as firms grow rapidly, they face a balancing act of integrating new talent while maintaining and adapting firm culture.

Meanwhile, although Gen AI provides clear opportunities, firms will also need to work out how to keep up with its rapid developments – a dominant topic at client meetings this year. The challenge will be how to sift through the massive number of Gen AI tools being touted as the right solution, only to find these are at varying levels of maturity. Even the best and most suitable solutions will require huge investment – in the technology itself, and the people and processes needed to make it a success.

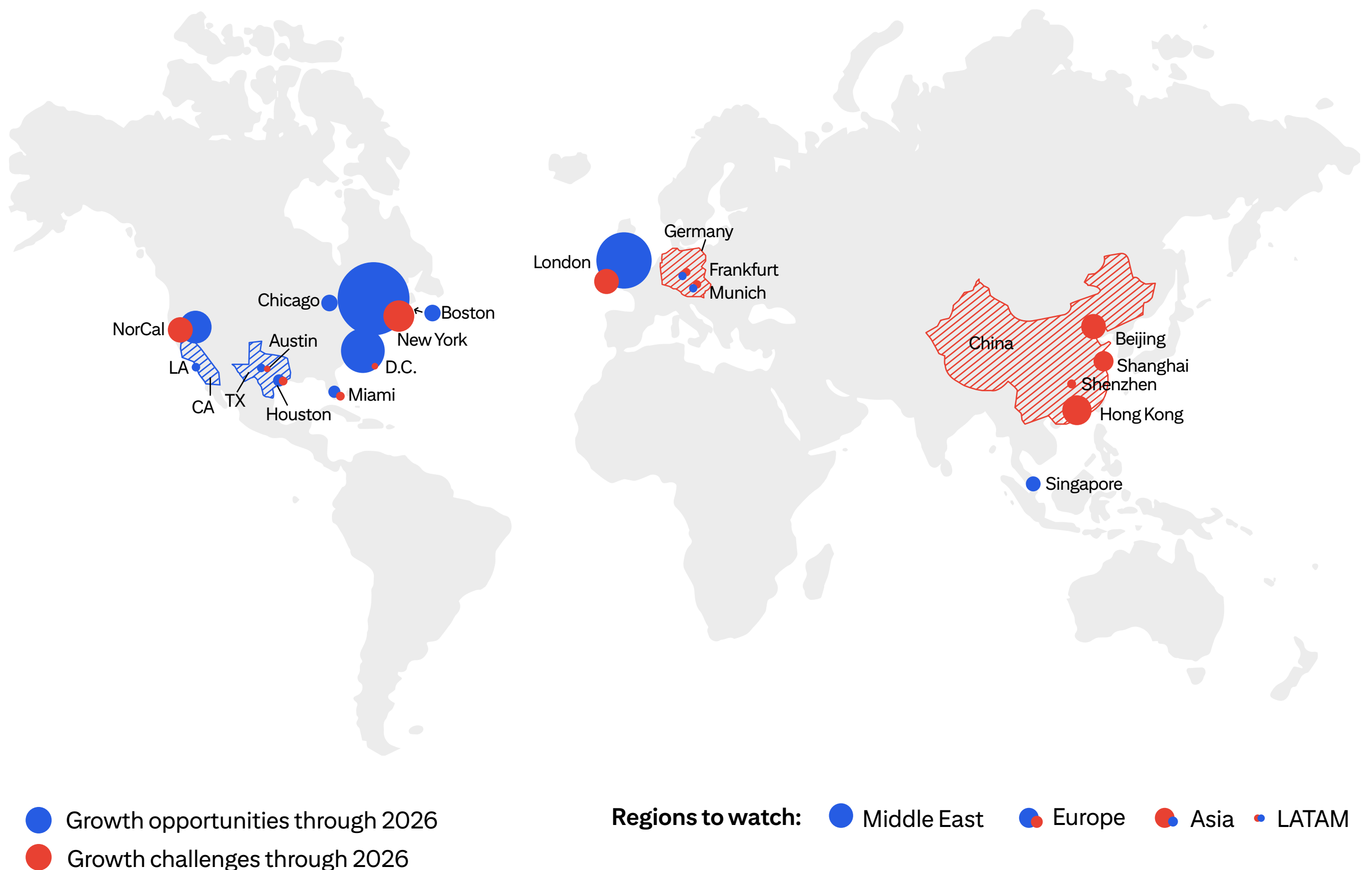
Finally, we expect that firms will continue to focus on how they can overcome the twin challenges of realization and expense pressures in order to improve profitability.

Growth opportunities and challenges by region

Over the past few years, we have seen US law firms retreat from China and reduce their exposure to Europe, with the exception of Germany. Meanwhile, we have seen significant investment in London and the US domestic market.

Looking ahead, based on the 2024 Citi Law Firm Leaders Survey and illustrated in **Figure 2**, we expect to see investment in five major markets – New York, London, Washington DC, Northern California and Texas. In addition, we anticipate increased investment in Chicago, Miami and Boston.

Figure 2: Growth Opportunities and Challenges by Region Through 2026



Growth opportunities through 2026
Growth challenges through 2026

Regions to watch: Middle East, Europe, Asia, LATAM

Source: Citi Law Firm Leaders Survey © Citibank, N.A. July, 2024

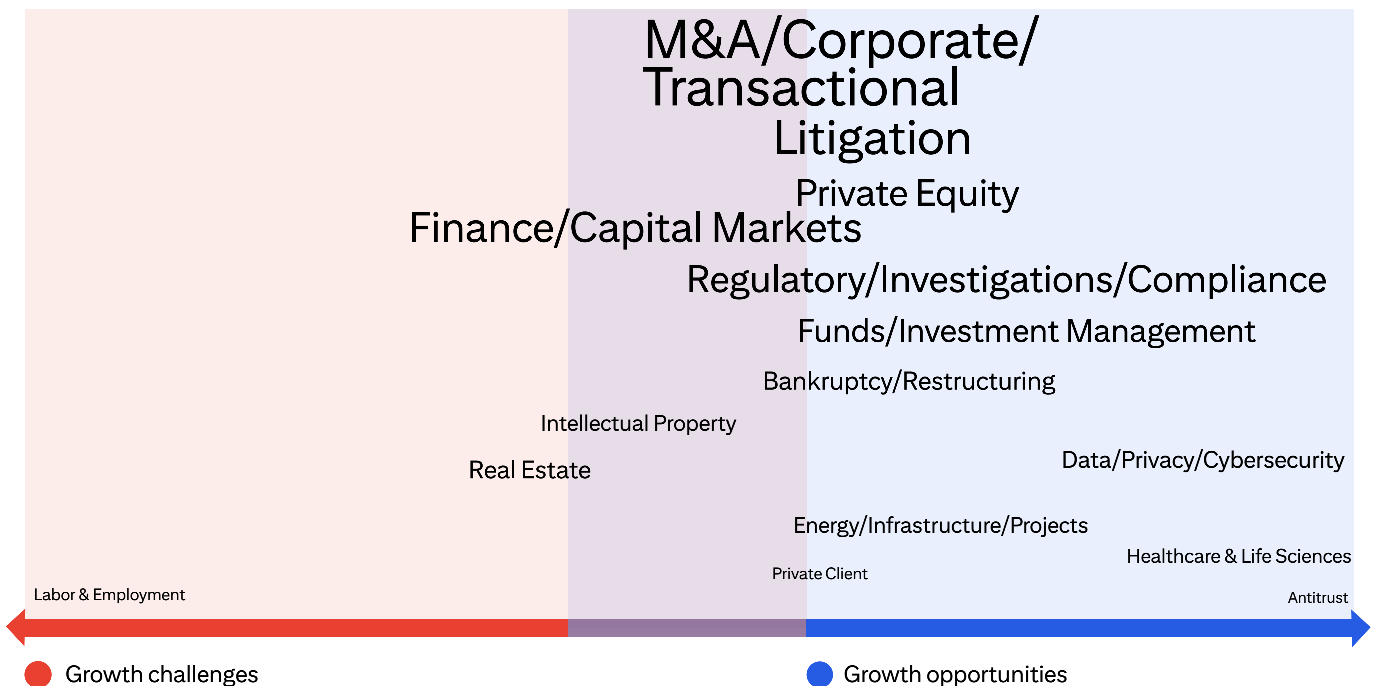
Outside of the US, while London will likely attract the greatest continued investment, we expect to see US firms look for opportunities in Singapore and the United Arab Emirates – although it's important to note that the Singapore offices of foreign firms are not large. These offices mostly serve the regional business needs of firms' foreign clients, and some are questioning their investment. In the United Arab Emirates, firms need local teams to work on local matters and, as they witness the level of infrastructure investment in the region, they are banking on the high volume of legal work expected to flow from it.

While there is some optimism about Europe generally, firms are mixed when it comes to the outlook for Germany – citing the lack of growth, strong competition, political uncertainty and pricing pressure. Meanwhile, China will likely continue to be a challenging market for foreign firms.

Growth opportunities and challenges by practice

Looking at practice growth opportunities, as illustrated in **Figure 3**, firms are more optimistic about a greater number of practices than we have seen in the past couple of years. Firms see continued growth in their litigation practices, as well as their regulatory, investigations and compliance practices. With the level of anti-trust scrutiny around large cap M&A deals seen recently and the anticipated broad rebound in M&A/transactional and corporate practices, firms expect anti-trust work to continue to grow.

Figure 3: Growth Opportunities and Challenges by Practice Through 2026



Source: Citi Law Firm Leaders Survey © Citibank, N.A. July, 2024

While some firms remain concerned about the growth outlook for transactional practices, more firms are optimistic about these practices. We also expect to see growth in private equity and funds/investment management work. And, while the outlook for capital markets remains mixed, we see more optimism ahead than we did a year ago.

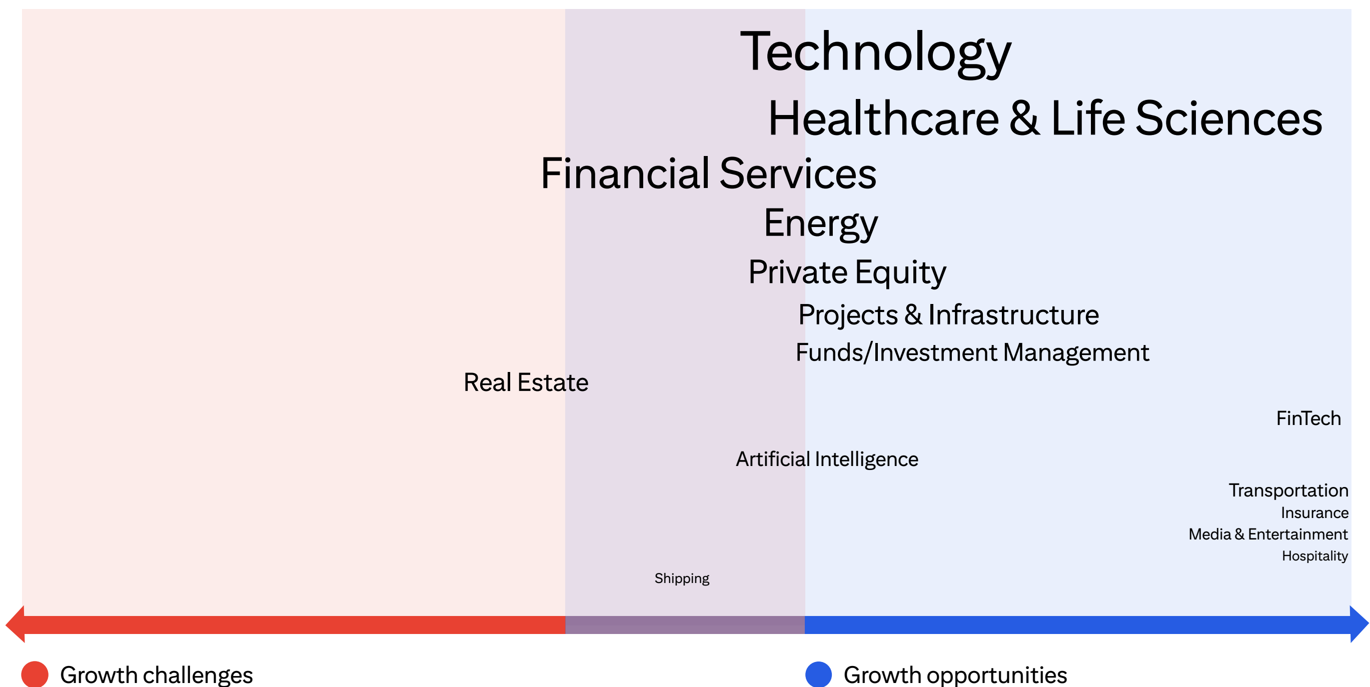
Firms are largely optimistic about their bankruptcy and restructuring practices. We also expect to see growth in data/privacy/cybersecurity practices, as well as energy, infrastructure and projects, and healthcare and life sciences practices.

On the other hand, the outlook for intellectual property ("IP"), real estate, and labor and employment is viewed by large firms as likely to be more challenging. In the case of IP, while activity is expected by a number of firms, some work is clearly under rate pressure. While real estate has been under pressure, we expect activity to pick up there in the coming year, particularly as interest rates continue to fall.

Growth opportunities and challenges by industry

Looking through the lens of client industry, as illustrated in **Figure 4**, the top three growth industries are expected to be technology; healthcare and life sciences; and energy. In the technology client sector, some firms will likely focus specifically on growing their artificial intelligence client base. We also expect to see more growth from private equity and funds/investment management clients. And there is likely to be more attention placed on projects and infrastructure clients over the next two years.

Figure 4: Growth Opportunities and Challenges by Industry Through 2026



Source: Citi Law Firm Leaders Survey © Citibank, N.A. July, 2024

Outside of these major client growth areas, firms will likely invest in fintech; transportation; insurance; media and entertainment; and hospitality clients. Meanwhile, many firms expect the real estate client sector to remain challenging, although we believe there is some reason for optimism, as noted above.

Growth through consolidation

We anticipate further market consolidation in 2025 – and beyond.

For large firms, that growth will likely be fueled by promotions and laterals rather than by mergers with similar-sized firms or acquisitions of smaller firms. For many years, where average annual industry demand growth has been modest at best, the outperformance of Am Law 50 firms has enabled them to take market share from other segments, largely through laterals and promotions.

This growth mindset is particularly evident among some of the world's most profitable law firms. Those firms have leveraged their strong outperformance to attract lateral talent and further solidify their market position. We expect to see both the largest firms and the most profitable firms continue to take a greater share of the market.

Mergers are difficult, especially between large firms – where there is a higher likelihood of client conflicts and a perhaps even greater challenge of successfully integrating two cultures. Yet the higher cost of running a law firm will require scale – and we expect to see more law firm M&A activity.

We saw a wave of mergers either implemented or announced in 2024, with some of the latter due to begin in early 2025. Some of these are between US-headquartered firms, while others are cross-border mergers. Indeed, we also saw the significant merger of a UK firm and a US firm in 2024, in addition to the other successful UK firm investments we have seen in the US market in recent years. We expect to see further investment by large UK firms in the US market in the future.

Aside from creating access to more clients and more markets, we believe that some consolidation activity will also be driven by the higher cost of running a law firm. The adoption of Gen AI and higher salaries are just two factors driving expense pressure at firms and the need for scale.

We would highlight, however, that brand remains more important than scale. Firms can move up in the Am Law revenue rankings through a merger, but it won't necessarily translate into a jump in the profitability ranking. In our experience, the most successful mergers are ones where the practices complement each other, and their cultures and values are aligned. Most importantly, the merger needs to make sense to each firm's clients, as there is no guarantee that clients will stop using other firms.

B. Likely developments in the adoption of Generative AI

Lessons learned so far

Gen AI was top of mind in many of our conversations with law firm leaders throughout 2024, and we expect this to continue through 2025 and beyond. In the 2024 Citi Law Firm Leaders Survey, we asked large firms what key lessons they have learned with another year of this rapidly developing area under their belts. There are six major lessons that firms tell us they have learned:

1. "Don't believe the hype"... although things can change quickly. The market is flooded with Gen AI tools. Assessing the myriad tools available has been time consuming for firms, with many then discovering that some of those tools are not yet ready to be implemented. However, things can change quickly – and firms know that they can't afford to lose focus on new Gen AI tools entering the law firm market.

2. A lot of human input is needed... and a significant shift in behavior. In assessing Gen AI tools, firms have learned that they need to dedicate time and resources. They also recognize that constant human input will be needed to train and refine the tools. This means building a human infrastructure around Gen AI. It also means overcoming the challenge of getting people to use Gen AI once the initial "shiny new toy" novelty wears off.

3. Gen AI will likely augment, not replace, the work of lawyers and law firm professionals. Gen AI tools will likely reduce repetitive low-value-add tasks, and that is going to free up lawyers and law firm professionals to do more interesting, higher-value work.

4. Robust governance around the use of Gen AI is critical. Along with the huge human investment placed on assessing and training these tools, there has also been an extensive effort to identify the risks associated with their use – and a robust set of guidelines around their use. We know that many firms have been reluctant to roll out Gen AI in their client work, restricting its use to internal business processes.

5. "Garbage in, garbage out", hallucinations and the location of data... the need to be careful with the input and the output. Similar to any technology tool, firms talk about the risk of storing and using outdated, low-quality data. However, given how sophisticated Gen AI work product can look, we are seeing a whole new level to the concept of "garbage in/garbage out". Working through hallucinations is a good example of this. Meanwhile, firms are concerned about exactly where their data is stored and how to protect it.

6. Consider the client. There remains a lot of sensitivity among law firm clients on the use of Gen AI. This is unsurprising considering how long it took for clients to become comfortable with cloud technology – and firms are facing a similar challenge in making clients comfortable with Gen AI. It's not all negative, however. Some firms have told us that they see the rapid growth of Gen AI as a business opportunity, enabling them to create a competitive edge.

What should we expect ahead?

Looking ahead to 2025 and beyond, we expect that firms will continue to work through the hype and keep up with the rapid development of legal industry Gen AI technology. They will also continue to dedicate time to understanding and mitigating the risks associated with its use.

Implementing Gen AI is going to be expensive. Firms will need to decide how to fund this investment. We have worked with firms in financing technology projects in the past and anticipate helping finance Gen AI investment going forward. So far, firms have actually spent very little – with the vast majority of large firms telling us they spent less than 1% of their revenue on Gen AI-related technology, consulting and staffing in 2023. We expect that will change over the next two years.

We also expect firms to begin examining how they can recover the high cost of Gen AI – factoring in the expected impact on billable hours and the delivery of a higher value outcome for the client. While we don't anticipate the end of the billable hour any time soon, this seems like the perfect opportunity for firms to introduce changes to their billing models to reflect the superior client outcome and to help recover the cost of Gen AI.

Firms will need to focus on getting lawyers to use Gen AI regularly, not least once the initial novelty wears off. Gen AI tools will need constant maintenance by lawyers, as well as data engineers and the technology team. And it will change the way lawyers work. The challenge will be in how to change lawyers' working habits to incorporate Gen AI in their day-to-day activities. This of course also extends to the willingness of all law firm professionals to embrace it.

Firms will also need to keep working on ensuring their clients are comfortable and accepting of the use of Gen AI.

More broadly, we expect firms to focus on gaining an understanding of how Gen AI will change the ways their firms operate – from the way they staff matters, what the leverage model looks like and how firms price matters; to how they conduct conflict checking and manage billing and collections, and all other areas of these large, complex businesses.

Firms will also face new talent retention challenges as they seek to attract and retain Gen AI specialists. It will likely be challenging for firms to attract and retain data scientists and software engineers when those candidates have so many other industry options.

However, there is a high degree of optimism around what Gen AI will mean for firms in the next couple of years. Firms are optimistic about how Gen AI will impact the delivery of legal services. Gen AI will help reduce risk through greater consistency, higher quality and faster production of legal services. And it will free up lawyers to focus on delivering higher value services and developing new solutions.

Gen AI will also likely make the operation of law firms more efficient, as is discussed later in this Client Advisory.

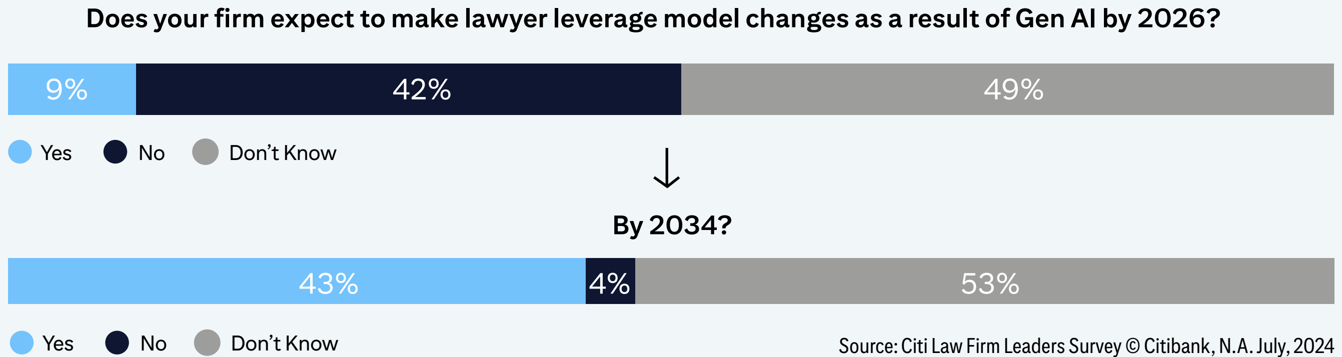
There is also an excellent opportunity for law firms to work with their clients on their adoption of Gen AI, given that many firms will have greater access to more sophisticated technology than their clients.

All of this will result in a better client experience and provide the opportunity for firms to gain a competitive advantage.

Finally, Gen AI will lead to a more fulfilling experience for lawyers, as they are liberated from the grunt work. Indeed, many firms we speak to believe that the widespread adoption of Gen AI will be a transformative opportunity for their businesses.

The impact of Gen AI on lawyer leverage. Few large firms (only 9%) think that Gen AI will cause a change in leverage over the next two years, according to the 2024 Citi Law Firm Leaders Survey. As illustrated in **Figure 5**, 42% believe it won't have any impact through 2026, while 49% simply don't know at this stage.

Figure 5: The Impact of Gen AI on the Lawyer Leverage Model by 2026 and Over the Next Decade



Source: Citi Law Firm Leaders Survey © Citibank, N.A. July, 2024

When we asked firms to predict what the impact of Gen AI might be on their lawyer leverage model over the next decade, the proportion of firms who don't know jumps to 53%. It's perhaps unsurprising that the level of uncertainty increases as the time horizon stretches. And we also note with interest that, among the other 47% of firms, almost all are certain that their leverage will change as a result of Gen AI.

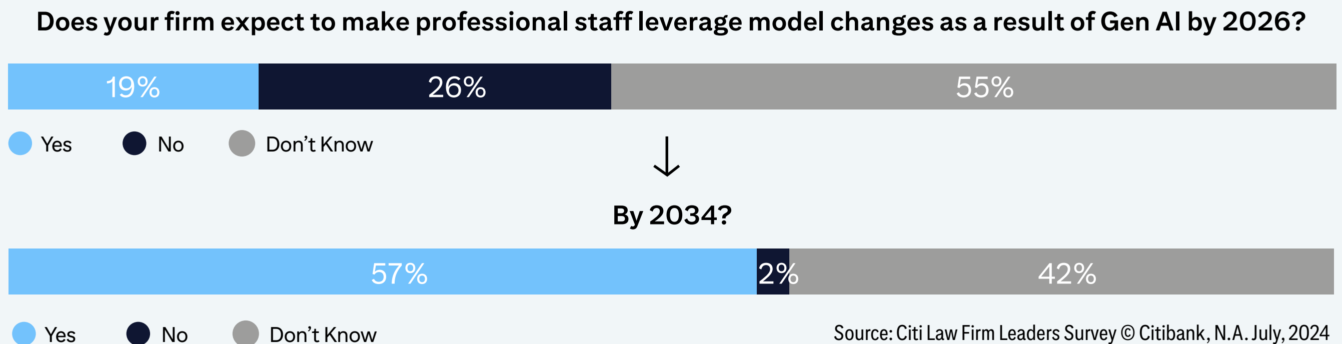
One of the long-term issues firms will need to address is how to train associates to act like mid-level associates if so many of the traditional tasks performed by first- and second-year associates are replaced by Gen AI. Even if Gen AI doesn't lead to a reduction in associate leverage, we expect that the composition of associate leverage will shift to a more senior mix – begging the question: 'how will firms produce competent mid-level and senior associates?'.

We can also expect that Gen AI will have a serious impact on how law schools design their JD programs.

The impact of Gen AI on professional staff leverage. Compared to lawyer leverage, more firms expect Gen AI to cause changes to the professional staff leverage model both in the near and longer term, as illustrated in **Figure 6**. By 2026, 19% of large firms expect to see changes to their professional staff leverage, while 26% don't expect any changes and 55% don't know.

Looking ahead to 2034, 57% of large firms expect changes, while the rest mostly don't know at this stage.

Figure 6: The Impact of Gen AI on the Professional Staff Leverage Model by 2026 and Over the Next Decade



Source: Citi Law Firm Leaders Survey © Citibank, N.A. July, 2024

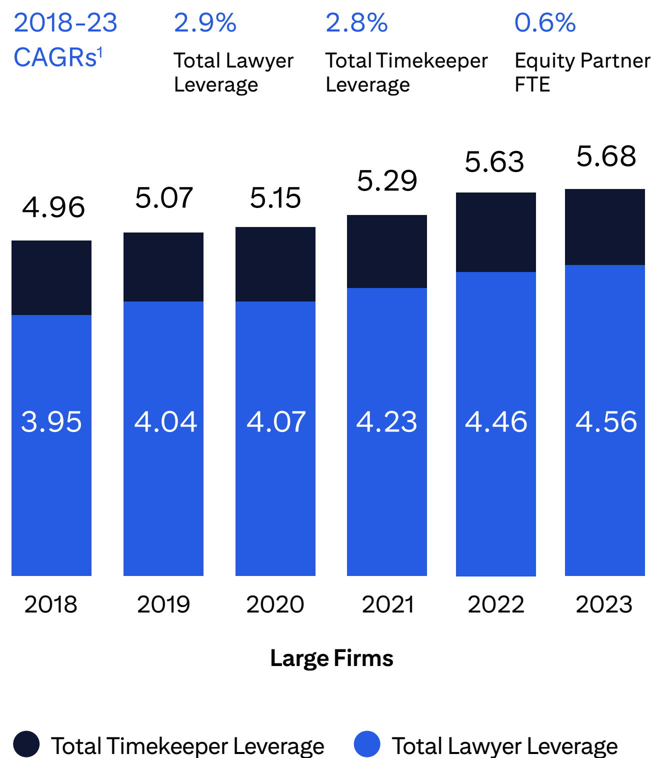
C. Growth trends to watch

1. The continued growth and reshaping of leverage

Leverage growth has been a consistent trend in this industry for many years, and we expect this to continue. As **Figure 7** illustrates, while equity partner headcount at large law firms grew at a modest pace of 0.6% during 2018-23, total lawyer leverage grew at an average annual rate of 2.9% during the same period.

Figure 7: Leverage Growth: 2018-23

Total Lawyer vs. Total Timekeeper Leverage

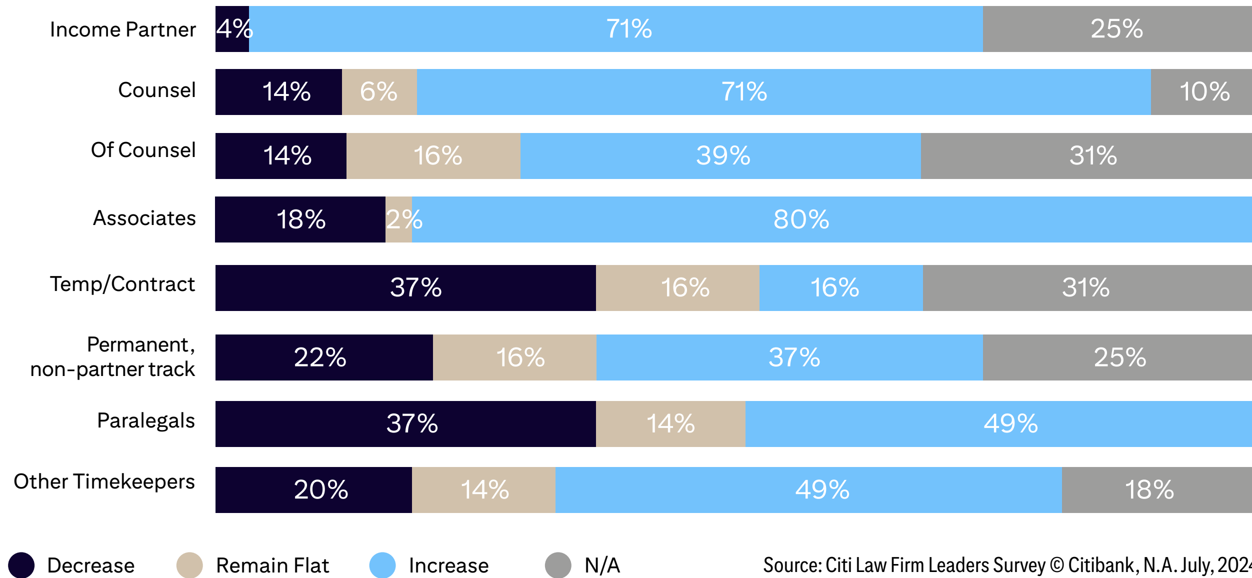


Source: Citi Annual Survey of Law Firm Performance © Citibank, N.A. May, 2024

[1] CAGR: compound annual growth rate

During 2018-23, we also saw the composition of lawyer leverage change. As **Figure 8** illustrates, the 2024 Citi Law Firm Leaders Survey showed that while 80% of large firms reported increasing their associate headcount to some degree during 2018 to 2023, 71% of those firms added income partners and counsel respectively.

Figure 8: Lawyer Leverage Growth by Category: 2023 vs. 2018

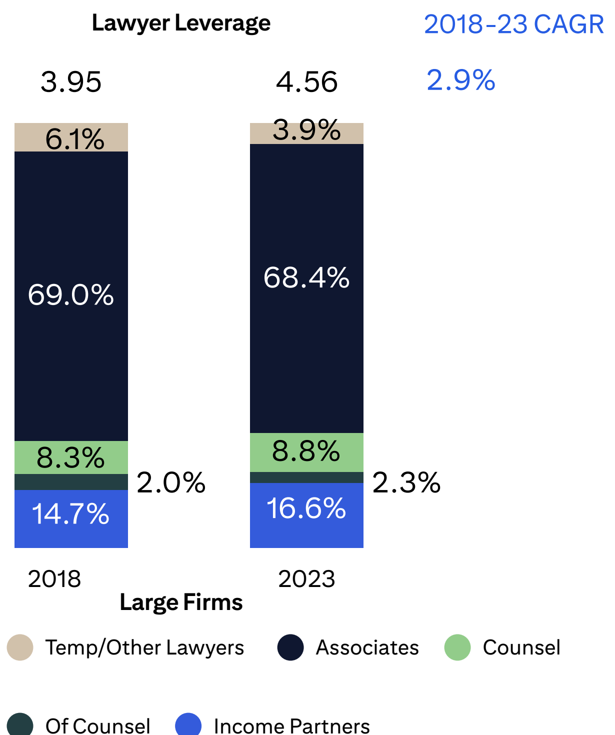


Source: Citi Law Firm Leaders Survey © Citibank, N.A. July, 2024

Meanwhile, the approach to lower-cost and other timekeepers was more mixed across firms. A minority of those firms increased their non-partner track and temp/contract lawyers, paralegals and other timekeepers, while more than one third reduced their temp/contract and paralegal headcount.

The net effect of the changes made to lawyer headcount can be seen in **Figure 9**. In terms of absolute headcount numbers, large firms invested more in growing the number of income partners and counsel compared to temp/other lawyers and associates – resulting in higher, and more senior, leverage over that five-year period.

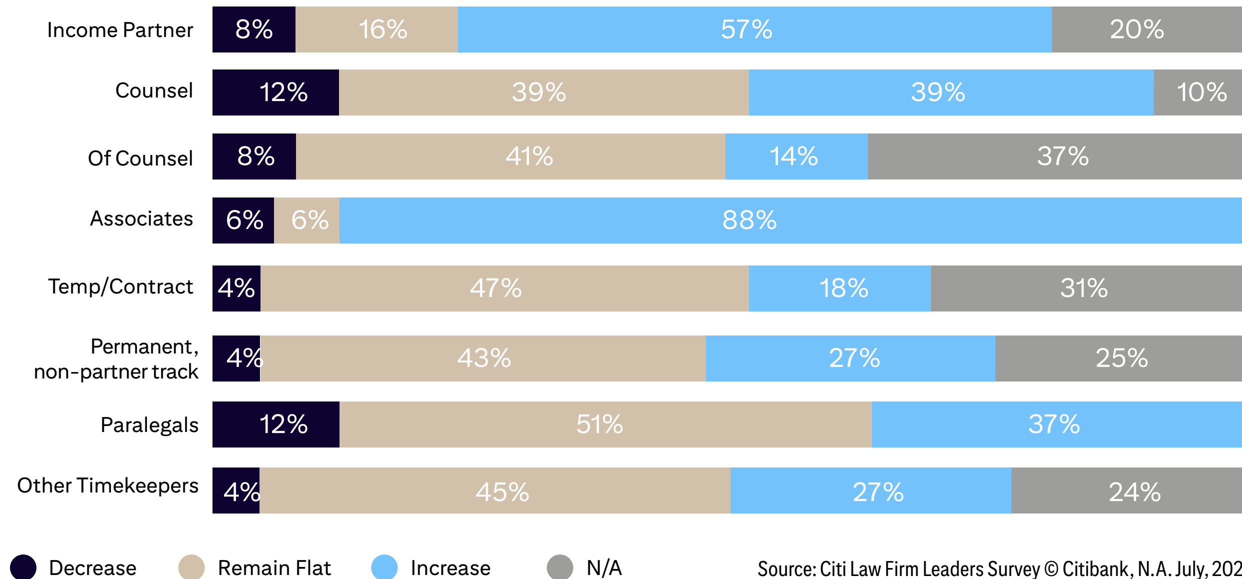
Figure 9: Composition of Lawyer Leverage: 2018-23



Source: Citi Annual Survey of Law Firm Performance © Citibank, N.A. May, 2024

Looking ahead to 2026, there is dispersion across large firms in their leverage projections. 61% of large firms expect continued leverage growth, while more than one third expect to stay at current levels. And while only 7% project a reduction in their leverage, this is up from 4% in last year's survey.

Figure 10: Projected Lawyer Leverage Growth by Category: 2026 vs. 2023



Source: Citi Law Firm Leaders Survey © Citibank, N.A. July, 2024

As for where firms will focus their leverage growth, as illustrated in **Figure 10**, it appears that 88% of firms plan to invest further in associate growth in some measure. The approach to counsel growth is mixed, with firms equally likely to increase counsel headcount or stay at current levels. There may be a few reasons for this. For the firms planning to increase counsel headcount, they may not have income partners, or they may use it as a step before promotion to income partner. Counsel also tend to be more profitable than income partners.

On the other hand, some firms that plan to stay at current counsel levels may be looking to invest more in income partners. It's perhaps worth noting that counsel billing rates tend to match income partners, yet counsel are generally more productive and earn less, making them a stronger contributor to overall firm profitability. However, in a fiercely competitive talent market, some firms might find that the income partner title is a more effective retention tool.

Looking at projected income partner growth, 57% of large firms plan to increase their income partner headcount. While this is a smaller proportion than we saw during 2018-23, we also note that the proportion of firms reporting "N/A" drops from 25% to 20%, indicating the adoption of an income partner category by more firms over the next two years. We discuss income partner growth trends in more detail later in this Client Advisory.

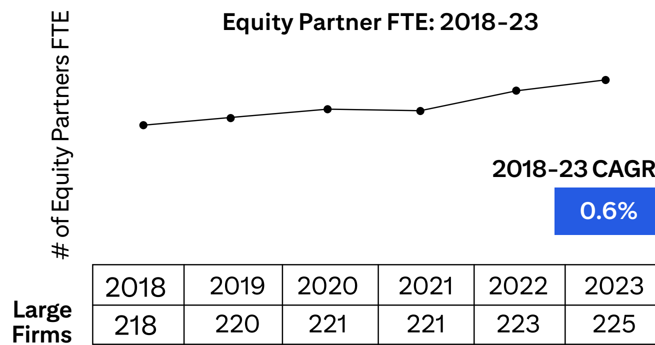
Meanwhile, we see firms most likely expecting to remain at current levels of temp/contact and permanent, non-partner track lawyers, paralegals and other timekeepers. The net effect is likely to be a continuation of the trend of higher and more senior leverage through 2026.

2. Equity partner growth

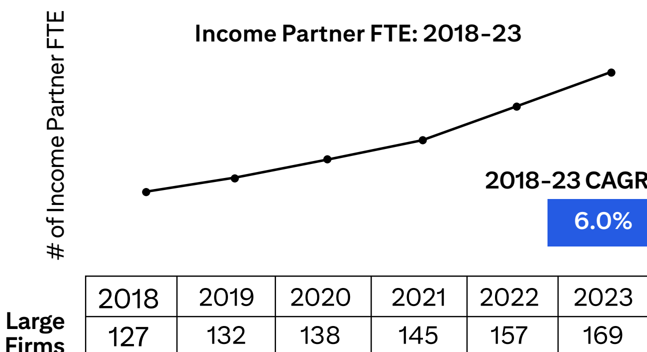
The pace of partner growth during 2018-23. Equity partner ranks have grown at an average annual rate of 0.6% over the past five years, with that pace accelerating in recent years, as illustrated in **Figure 11**. However, this remains a modest growth rate.

That said, during 2018-23, we also saw income partner headcount increase at an average annual rate of 6% as firms looked to retain talent in this highly competitive market.

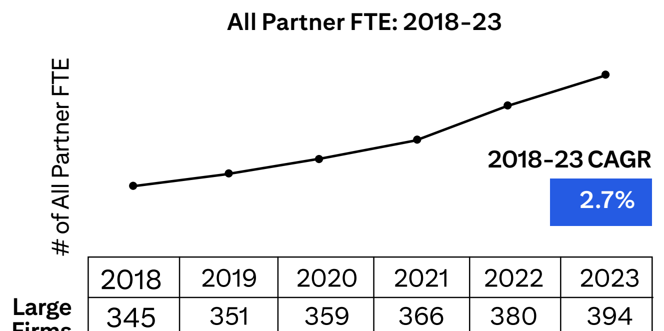
Figure 11: Partner Headcount Growth: 2018-23



	2018	2019	2020	2021	2022	2023
Large Firms	218	220	221	221	223	225



	2018	2019	2020	2021	2022	2023
Large Firms	127	132	138	145	157	169



	2018	2019	2020	2021	2022	2023
Large Firms	345	351	359	366	380	394

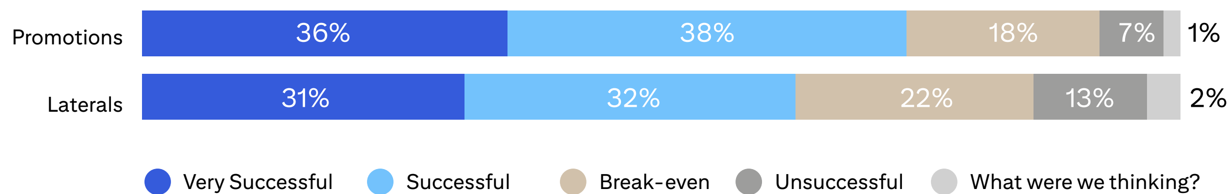
Source: Citi Annual Survey of Law Firm Performance © Citibank, N.A. May, 2024

As a result, all partner headcount has grown at an average annual pace of 2.7%, highlighting how large firms have focused on growing both their current equity partnerships and their pipeline of potentially future equity partners.

And while the rate of equity partner headcount may have been modest, 75% of large firms reported some measure of growth in their equity partner ranks during 2018-23.

The success rate of laterals vs. promoted equity partners. Looking at how firms rate the success of their equity partners promoted or acquired as laterals during the past five years, we continue to see a higher success rate for promoted equity partners vs. laterals, as illustrated in **Figure 12**. In the 2024 Citi Law Firm Leaders Survey, 74% of large firms reported that the equity partners they promoted during 2018-23 were above break even, compared with just a 63% success rate for their laterals brought on during the same period.

Figure 12: Equity Partner Additions: 2019-23: Laterals vs. Promotions



Source: Citi Law Firm Leaders Survey © Citibank, N.A. July, 2024

This lateral success rate is down slightly from last year's survey (at 64%), while the proportion of break even or unsuccessful lateral hires has increased from 33% to 35%.

The greater success of internal promotions may explain why firms are projecting a higher likelihood of investment in internal promotions vs. laterals. It may also explain the investment in income partners as a testing ground, as is further discussed below.

Equity partner growth through 2026. Looking ahead, 73% of large firms expect to grow their equity partner ranks through 2026, while very few believe they will reduce their equity partnerships over the next two years.

As firms pursue a growth mindset, we expect to see more lateral hiring as well as internal promotions. That said, not all these lateral hires will work out.

As partner compensation guarantees have jumped to higher levels, achieving a return on investment has become less likely. Client relationships are not always as portable as lateral candidates might think. We believe there is a high likelihood of an uptick in the number of recently hired lateral equity partner departures from firms in the next couple of years.

Further changes to the equity partner compensation model. In recent years, we have seen more firms make changes to their compensation model to retain and attract talent in an aggressive lateral market. In the 2024 Citi Law Firm Leaders Survey, half of the large firms surveyed told us that they made changes to their model during 2019-23. Those changes involved stretching the spread of compensation and changing the criteria used to assess compensation.

Stretching the spread of compensation took various forms. We have seen increasing use of a bonus pool among firms. Across our annual survey reporting, we have also observed firms allocating a greater proportion of net income to their top 10-20% of equity partners. And, for the few firms with lockstep or modified lockstep models, we have seen various changes made to address how to reward top performers regardless of their level of experience.

At the same time, many firms have changed the criteria used to assess equity partner compensation levels. We note that those changes have centered around (1) bringing more clarity and transparency in how decisions are made; and (2) placing a greater focus on profit growth. That said, not all firms have taken a more transparent approach. Indeed, some firms have moved to a closed compensation system.

It's important to note however that while 50% of large firms reported making changes to their equity partner compensation model over the past five years, almost one quarter did not disclose what they've done – illustrating the sensitivity around equity partner compensation and the war for talent. Meanwhile, another 27% of large firms reported that they had not made any changes.

Looking ahead to 2026, we suspect that will change for some of those firms. As the majority of firms plan to grow their equity partner headcount, more than one third plan to make changes to their equity partner compensation models, either by stretching the spread of compensation or reviewing the criteria used to assess compensation levels. We also expect to see more frequent review of performance in this highly competitive market.

Increased equity partner capital contributions. We have seen growing interest from law firm clients in increasing equity partner capital levels and we expect this to continue. Indeed, over the past five years, we have seen an acceleration in the growth of absolute equity partner paid in capital. These capital contributions have been a critical means of funding firms' growth and investment in their infrastructure.

That said, we have seen net income grow at a comparatively greater pace than the growth in equity partner capital contributions, resulting in equity partner paid in capital/net income ratios actually declining. As firms look to grow, relying on their equity partners to fund that growth makes sense, especially as partner capital increases have not kept pace with net income growth. Relying on partners to provide capital also creates more "skin in the game", especially important in an active lateral market. It's worth noting that some firms also require capital contributions from their income partners, albeit at a typically reduced level from that expected from a full equity partner.

In considering equity partner capital levels, we recommend that firms consider their likely technology spend, real estate needs and other fixed asset investment needs over a three-to-five-year period. Firms can then calibrate the timing and magnitude of any capital raise with those planned investments.

It is also worth considering the demographics of the equity partnership and its impact on the firm's capital base. An increase in retirements could strain a firm's capital base – especially when the largest individual equity partner capital positions may be held by the partners nearing retirement. Meanwhile, newly promoted equity partners tend to have a longer time frame to contribute capital than incoming laterals.

Firms also need to consider their return of capital policies, typically outlined in their partnership agreements. We have seen firms become more intentional around the pace at which capital is raised vs. returned, and we expect this to continue. We also expect to see more of the innovative equity partner capital loan structures designed to bridge the gap between an equity partner's return of capital and the requirement to fund their new firm.

3. Managing income partner growth

As noted earlier, one of the most pronounced trends we have seen in recent years is the focus on growing the income partner population, particularly among some of the most profitable firms in the industry. This trend has largely been driven by the desire to retain top associate talent in an industry where the path to equity partnership has become longer over the years.

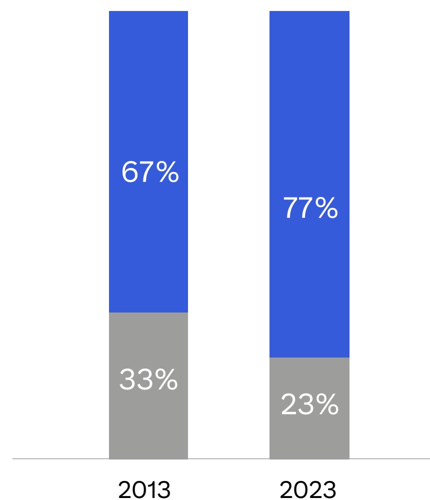
In our experience, a two-tier partnership works well when the income partner population is comprised of junior, highly motivated income partners who want to make their case for becoming an equity partner. Critical to the success of this model is that income partners have a relatively short time to make that business case. The model works best where firms give income partners a two- to three-year time frame to prove they can build and sustain an equity partner practice or move on to another firm.

On the other hand, where firms have historically carried a population of income partners for a long period or as a permanent role, productivity tends to wane as those partners become more senior and realize that they are unlikely to become equity partners. And the worst use of the income partner title is where firms de-equitize an underperforming equity partner. De-equitizing an equity partner rarely corrects the performance issues, but creates a large, fixed cost for the firm. This was a common problem in the early 2010s, when the combination of low productivity and high salaries often resulted in the income partner population being a drain on law firm profitability.

As **Figure 13** illustrates, in 2013, roughly one third of firms across the industry reported negative contribution per income partner. The experience with income partners has improved over the past decade, though still roughly one quarter of firms reported negative contribution per income partner in 2023.

Firms that are investing heavily in income partners will face the risk of negative contribution to firm profitability if they do not carefully manage the size and performance expectations of their income partner classes. Meanwhile, the accelerated growth in income partners and only modest growth in equity partners begs the question of what the career path will look like for many of these income partners.

Figure 13: Contribution per Income Partner: 2013 vs. 2023



% with Negative Contribution % with Positive Contribution

Source: Citi Annual Survey of Law Firm Performance © Citibank, N.A. May, 2024

D. Operational efficiency trends to watch

Moving forward, we expect firms to focus their attention on introducing greater efficiencies in the delivery of legal services and the operation of their businesses. Beyond the continued development of Gen AI (discussed in detail earlier in this Client Advisory), there are several other opportunities for firms to further streamline the delivery of legal services and to introduce more efficiencies across their business processes.

There will also likely be some shift in the operational efficiency priorities of firms in 2025 and beyond. Making adjustments to professional staff leverage models and office space were the dominant priorities in recent years, and these will continue to be important. Expense management will also remain important. However, we expect a clear shift toward technology investment and improving collections and realization as the top priorities of law firms in the coming year, according to the 2024 Citi Law Firm Leaders Survey.

1. Greater investment in technology (and not just Gen AI)

We expect to see firms invest heavily in cloud computing, and for this to actually take priority over investment in Gen AI tools. Given all the media attention placed on Gen AI, this may seem surprising. However, there is a more mature set of cloud computing solutions available to firms, and client acceptance of these solutions has grown, making it easier for firms to implement.

We also expect to see greater investment in Gen AI technology, up from the average spend of below 1% of revenue seen so far. The third major area of technology investment is expected to be cybersecurity-related.

Finally, it is likely that there will be more investment in collaboration tools, while firms also anticipate spending more on training and upskilling their people. This includes upskilling technology teams, and likely training lawyers and other law firm professionals on how to get the most out of Gen AI and other technology solutions.

2. Further improvement in the billing and collections process

Collection cycle pressure will likely continue to be an issue for the industry. Looking ahead, firms will continue to look for ways to shorten the collection cycle – from time entry to billing to collection.

We can expect to see firms enhance their time entry and billing systems. An obvious use of Gen AI will be to produce bills based on the unique rules defined by each client. This will enable firms to reduce the likelihood of client rejection of bills due to errors and outliers. The immediate impact should then be quicker approval and payment of bills, effectively shortening the collection cycle.

We also expect to see firms continue to focus on improving behaviors around collections. Across the industry, with most firms operating on a cash accounting basis, there is a huge push for collections in the fourth quarter. The problem is that firms are competing with others for client attention to pay their bills as the calendar year comes to an end. Some firms have a natural advantage by adopting a different fiscal year-end. Others have established a synthetic version of this by creating an earlier year-end to measure partner contribution and compensation. Many firms have implemented more frequent collections pushes throughout the year.

Improving the production of more compliant bills should be a big step forward in shortening the collection cycle. There is also a big opportunity for firms to change partner behavior around how they approach collections.

3. Optimizing realization and offering different pricing models/new approaches to pricing

Firms are likely to focus on how to improve realization. While many factors can affect realization, such as practice, client and geographic mix, there are some ways that firms can improve realization. Changing a firm's footprint may not be practical, but we have seen firms shift away from clients and practices with low realization. And in our experience, there is an opportunity for many firms to change partner behavior around how they approach pricing and billing discussions with their clients.

We also expect that firms will look to develop different pricing models, particularly in a world where Gen AI will potentially eliminate many hours currently worked to produce the same or higher value outcome, while the cost of implementing these Gen AI tools will be enormous. As we wrote earlier in this Client Advisory, the expected investment in Gen AI must surely be the driver of firms examining how to adopt outcome-based or value-based billing for at least part of their work.

AFAs. We continue to see an increase in the proportion of revenue coming from AFAs. In the 2024 Citi Law Firm Leaders Survey, large firms projected that, on average, 22.3% of their 2024 revenue would come from AFAs, up from 21.9% in 2023. Indeed, 2023 saw more AFA-related revenue than the 20.4% projected by these same firms. This may still seem relatively minor, but we continue to see the proportion increase. Indeed, as recently as 2018, the proportion of revenue coming from AFAs was just 17.5% on average. A growing number of firms are also telling us that more than 20% of their revenue is expected to come from AFAs in 2024. 44% of large firms expect that more than 20% of their revenue in 2024 will have come from AFAs, up from 37% in 2023.

With all of this said, AFAs tend to be fairly straightforward, and are primarily fixed-fee arrangements. Yet for all of the media attention on the desire of law firm clients to use AFAs, law firms regularly tell us that clients are often resistant to AFAs. At the end of the day, they are more comfortable with a deeper discount, as described later in this section.

Nevertheless, by 2026, 73% of large firms expect that the proportion of revenue coming from AFAs will grow. No firm believes that the proportion of revenue coming from AFAs will shrink.

Pre-negotiated discounts. We also expect to see a continued high proportion of revenue subject to some form of a pre-negotiated discount. As an average across large firms, we saw roughly 41% of revenue coming from pre-negotiated discounts, and we expect a similar proportion for 2024. Behind these averages, two thirds of large firms see more than 30% of their revenue subject to a pre-negotiated discount, with 28% reporting that the majority of their revenue is related to a pre-negotiated discount.

By 2026, 56% of large firms expect that the proportion of pre-negotiated discount-related revenue will increase, while one third believe that it will remain at these current high levels.

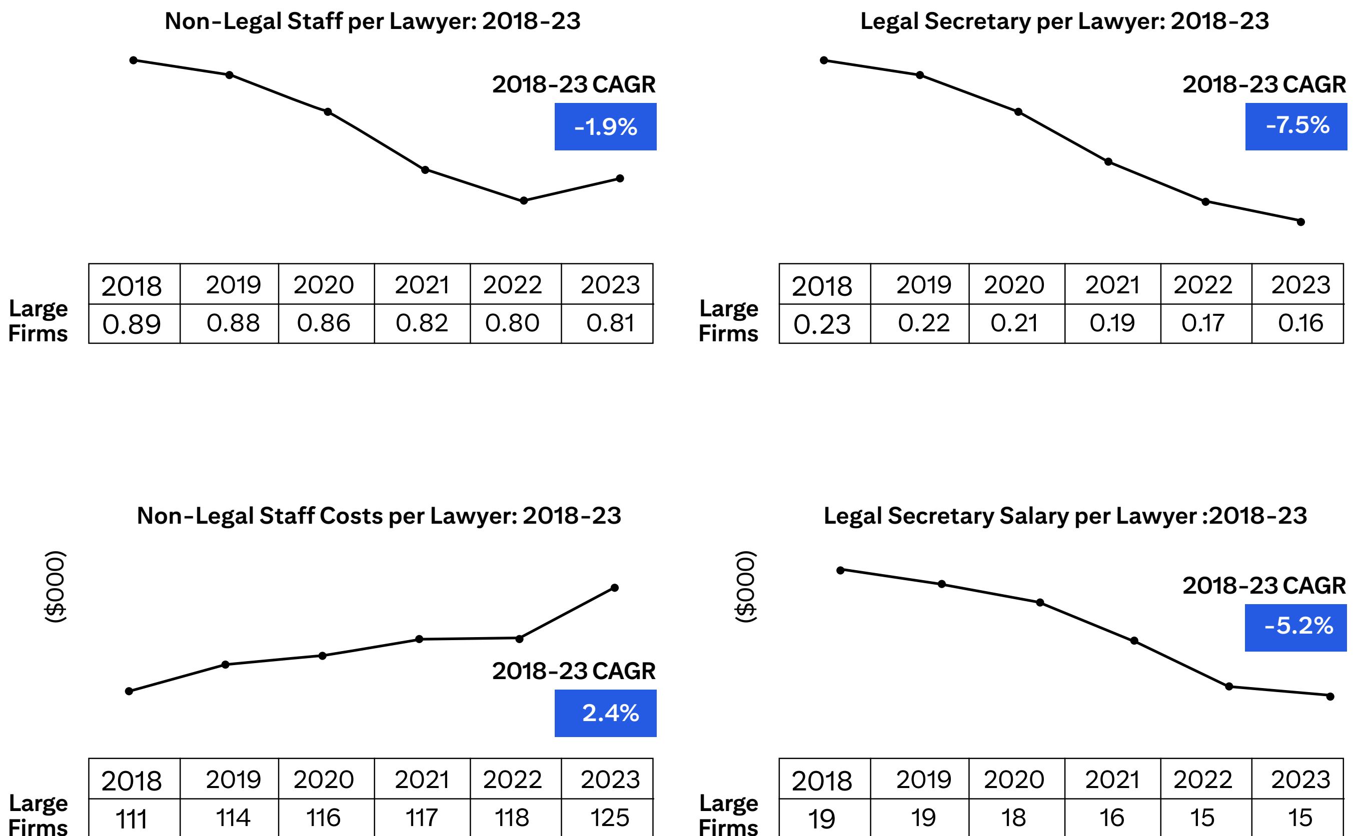
The likelihood of more AFAs and pre-negotiated discounts makes the whole discussion around realization, project management and efficient delivery of legal services even more important.

4. Restructuring the professional staff leverage model

Over the past few years, we have seen a strong focus on reducing professional staff leverage, with the emphasis on reducing personal assistant/secretarial staffing ratios. As **Figure 14** illustrates, while the personal assistant/secretary:lawyer ratio at large firms has come down from 0.23 in 2018 to 0.16 in 2023, firms have also been able to realize a cost saving of $4,000 per lawyer.

During that same period, large firms have also reduced their overall professional staff:lawyer ratio from 0.89 in 2018 to 0.81 in 2023. However, there has been no cost saving. Firms may have reduced the overall staffing leverage numbers, but the composition of that leverage has moved to a higher cost model. In fact, the professional staff:lawyer cost has increased by $14,000 per lawyer over this period.

Figure 14: Professional Staff Trends: 2018-23



Non-Legal Staff per Lawyer: 2018-23

	2018	2019	2020	2021	2022	2023
Large Firms	0.89	0.88	0.86	0.82	0.80	0.81

Legal Secretary per Lawyer: 2018-23

	2018	2019	2020	2021	2022	2023
Large Firms	0.23	0.22	0.21	0.19	0.17	0.16

Non-Legal Staff Costs per Lawyer: 2018-23 ($000)

	2018	2019	2020	2021	2022	2023
Large Firms	111	114	116	117	118	125

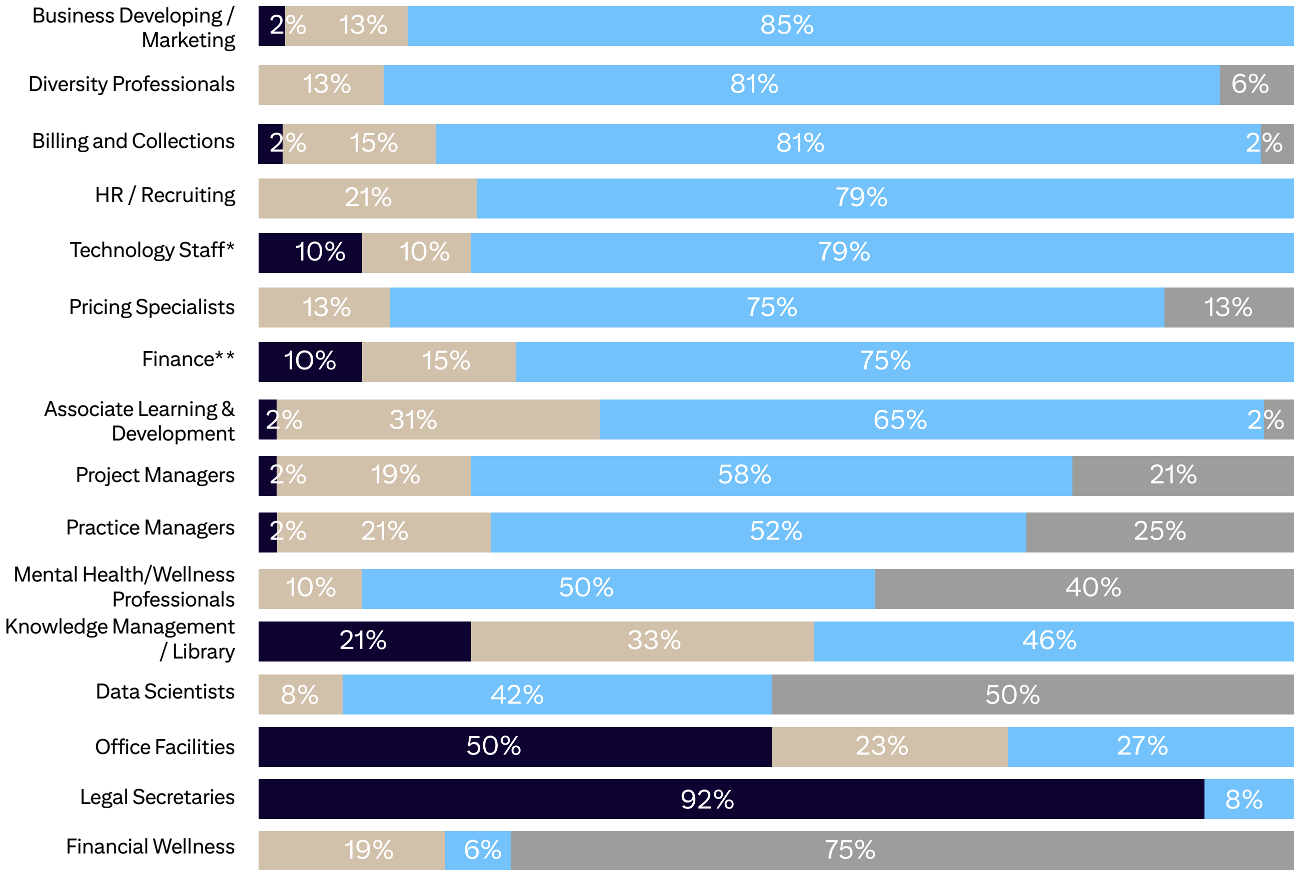
Legal Secretary Salary per Lawyer :2018-23 ($000)

	2018	2019	2020	2021	2022	2023
Large Firms	19	19	18	16	15	15

Source: Citi Annual Survey of Law Firm Performance © Citibank, N.A. May, 2024

As **Figure 15** illustrates, during 2018-23, we saw the biggest growth among business development, billing and collections, recruiting, technology, pricing and finance professionals. All of these are necessary roles in today's law firms, but they cost more.

Figure 15: Professional Staff Leverage Growth by Category: 2023 vs. 2018



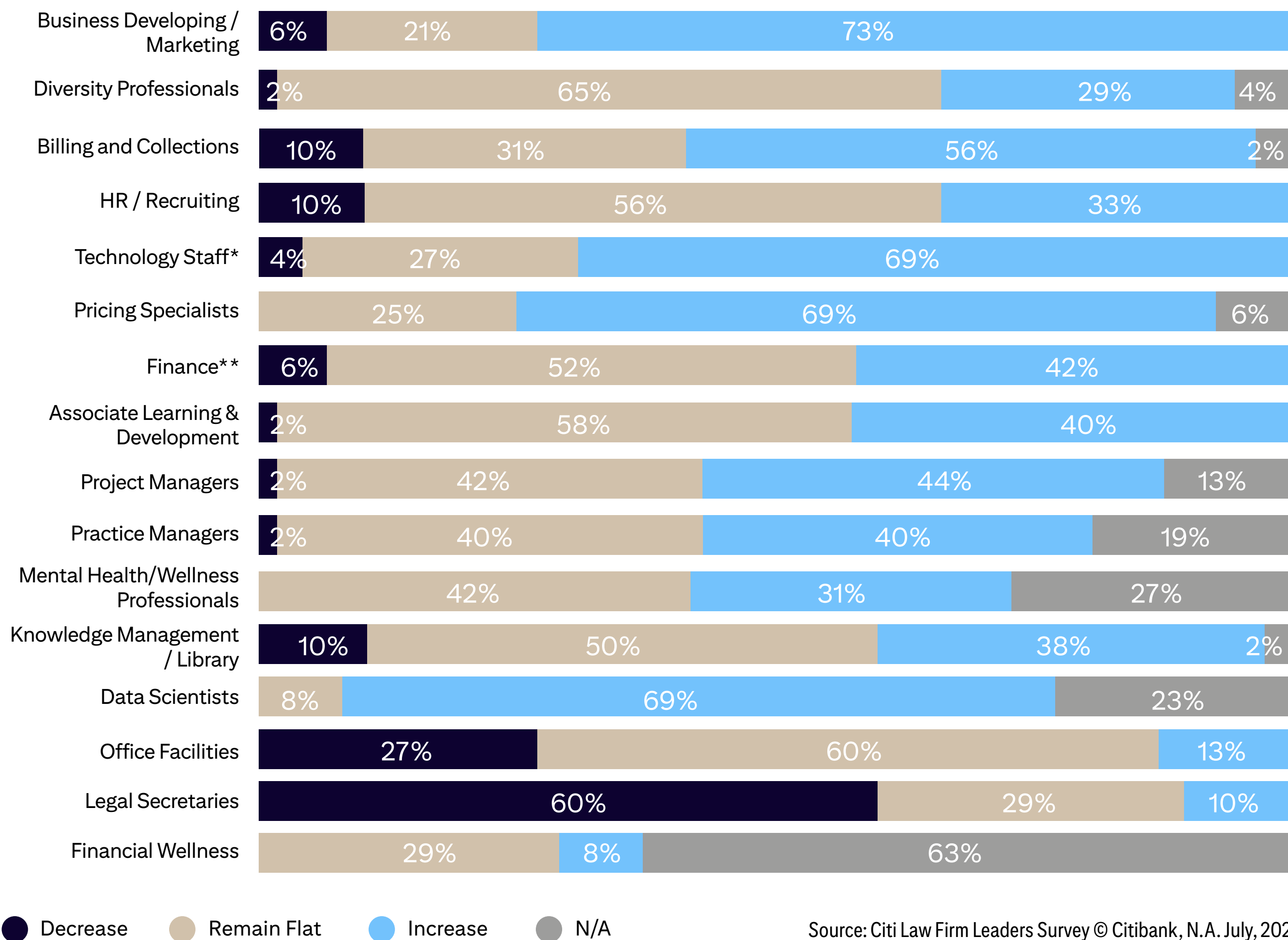
Source: Citi Law Firm Leaders Survey © Citibank, N.A. July, 2024

*Excluding data scientists
**Excluding pricing specialists and billing and collections

Looking out to 2026, most large firms believe they will remain at their current professional staff levels, according to the 2024 Citi Law Firm Leaders Survey. Only 20% believe they will see further growth, while around one quarter expect to reduce the size of their professional staff leverage models.

60% of large firms expect to see further reductions in personal assistant/secretarial staff, as illustrated in **Figure 16**. Meanwhile, we can expect to see further growth for a majority of large firms in business development and marketing teams, pricing specialists, technology professionals and particularly data scientists.

Figure 16: Projected Professional Staff Leverage Growth by Category: 2026 vs. 2023



Source: Citi Law Firm Leaders Survey © Citibank, N.A. July, 202

*Excluding data scientists
**Excluding pricing specialists and billing and collections

We also expect that a majority of large firms will add to their billing and collections teams. These projected professional staff growth patterns reflect the industry's expected focus on technology and process improvement, and on achieving further growth in demand and profitability.

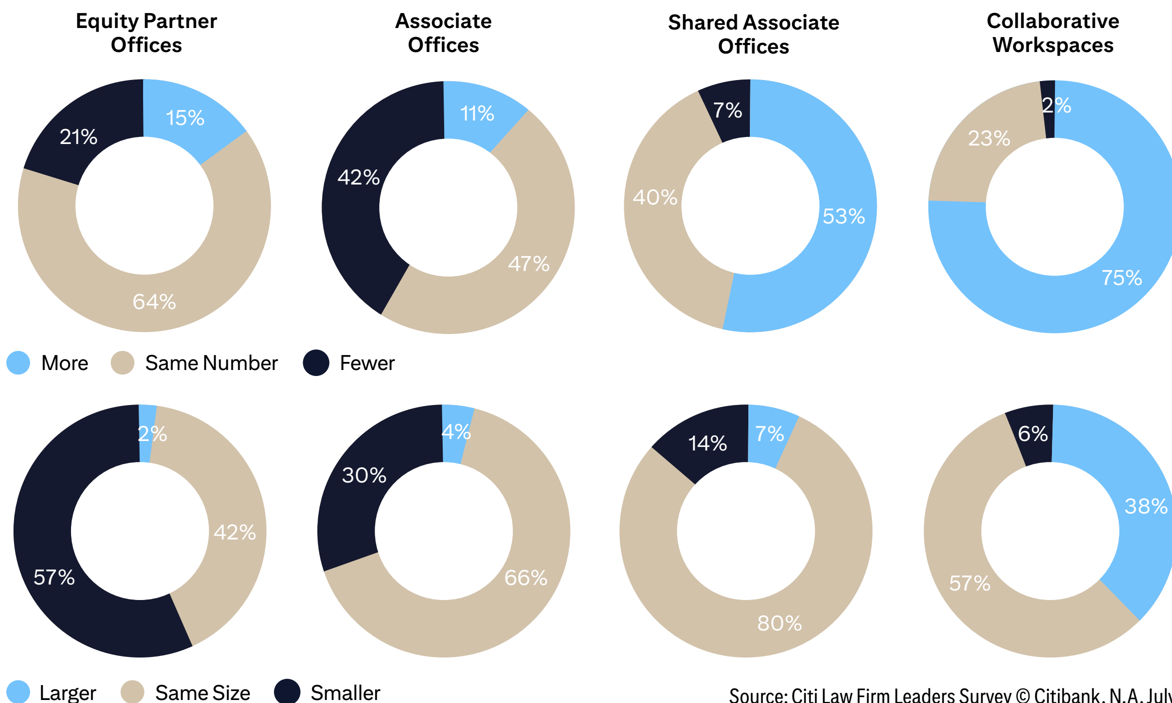
5. Reducing or enhancing space

As we have written in past Client Advisories, discussions around reducing or reconfiguring office space were dominant in the immediate aftermath of Covid and the shift to more remote work. While a majority of large firms still plan to reduce their space as leases come up for renewal, we continue to see growing dispersion in the approaches firms are taking. In fact, we see a smaller majority of firms planning to reduce their square footage compared with the last few years. Meanwhile, we see a growing proportion of firms planning to either increase their space or stay at current levels in the 2024 Citi Law Firm Leaders Survey. This would make sense given many firms' plans to grow headcount and the increasing number of firms that implemented four-day-a-week in-office policies during 2024.

Looking at **Figure 17**, large firms are most likely to retain their current number of equity partner offices, but they will become smaller. We would also note that compared to last year's Citi Law Firm Leaders Survey, we saw growth in the proportion of firms planning to add equity partner offices, which aligns with their future growth plans.

When it comes to associate offices, almost half of the large firms responding to the 2024 Citi Law Firm Leaders Survey expect to keep the same number of associate offices as they currently have, while 42% plan to reduce the number. These results are similar to what we saw in last year's survey. Meanwhile, almost two thirds of these firms appear to have reached the optimal size for an associate office and plan to keep them at that size. While 53% of large firms plan to add more shared associate offices, this is down from 59% in last year's survey. The size of those offices will likely stay the same at 80% of large firms, up from 77% of firms reporting that to be the case last year.

Figure 17: Associate and Equity Partner Offices: What Will Happen?



We have seen no shift over the past year in the likely size and number of collaborative workspaces – with the majority of large firms still planning to further increase the number of these spaces. With the emphasis on collaborative workspaces, we have heard mixed sentiment on how much these spaces are used. While many firms use them effectively, we have heard that, for others, they are not yet being used to their full potential.

6. Focusing more on practice management

There are several interesting aspects to practice management that we expect to see in 2025 and beyond. Productivity may have improved in 2024, as firms made headcount adjustments, but the industry is still not back to pre-pandemic levels. We expect that firms will continue to be more rigorous in managing headcount levels while they focus on improving the productivity of their lawyers.

To help improve lawyer productivity, we expect to see firms focus more on optimal work allocation. This will mean more than just deciding on which lawyer should be doing the work. It could also mean allocating the work to a paralegal or other lower-cost resources to deliver more efficient, cost-effective services to the client.

We also expect to see greater focus on eliminating the inefficiencies that stop lawyers from spending more time on client work. There is an opportunity for firms to review and redesign internal business processes such as pricing, billing and marketing – and to address any inefficiencies. As firms allocate administrative tasks away from lawyers, we can expect to see the use of Gen AI to drive new processes and efficiencies, as discussed in detail earlier in this Client Advisory.

We note that in addition to practice managers, we are seeing a growing number of practice level COOs – a trend that is likely to continue. These practice level COOs will ensure the efficient operation and optimal allocation of resources across a practice. While the growing sophistication of certain practices warrants practice level COOs, it will be critical for firms to create a structure that ensures coordination across the firm.

7. Expanding client relationships

An important aspect of firms' growth strategies will be continuing to find ways to do more with existing clients. We have seen firms implement client and industry teams and expand their business development teams in recent years, and we expect this to trend to continue. This will help firms uncover more opportunities with existing clients and improve the client relationship.

We expect to see more business development training for lawyers, particularly on cross-selling efforts. And we predict more investment in client relationship management systems.

Building deep and extensive institution-wide relationships with clients will be crucial in guarding against the risk of losing those clients in an aggressive lateral market.

Conclusion

Looking ahead, firms will continue to pursue a growth mindset – increasing their scale and finding ways to leverage their bigger platforms to capture market share. Growth will likely come from promotions and strategic lateral hiring. This increased scale will also enable firms to attract and retain talent, while absorbing the necessary costs associated with Gen AI and other technologies.

We also anticipate some merger activity, particularly involving smaller and regional firms. We recognize that there are some firms that may have trouble keeping and retaining talent, as well as making the necessary investments in technology. Those firms may be well advised to examine their long-term strategy and consider merger opportunities.

Another anticipated trend in the coming year is the continued growth in both equity partners and income partners at firms. In what we anticipate will remain a fierce lateral partner market, firms will continue to look for ways to attract and retain top partner talent. This includes firms looking closely at their equity partner compensation models to ensure that they remain competitive. It may also mean creating opportunities for talented senior associates through an income partner program. While some income partner programs are in their infancy, we believe that the next two to three years will be telling in how successful those programs are.

We expect to see continued growth in leverage beyond the projected continued investment in income partners. This will most likely come from continued growth in associate leverage.

Meanwhile, firms will continue to look at how they can leverage the power of Gen AI to transform their businesses. With the possibilities Gen AI brings, this is an exciting time. But it will require significant investment in resources. It may also ultimately change the shape of both lawyer and professional staff leverage, although we believe it will have a minimal impact on leverage in the near term.

In addition to Gen AI investment, firms will continue to face other expense pressures, requiring scale. This need for scale, along with the desire to capture greater market share will likely drive some of the consolidation activity we expect to see beyond promotions and laterals.

Those expense pressures, along with the revenue-related pressures of improving realization and the collection cycle, will also cause firms to continue to focus on both expense- and revenue-related operational efficiencies.

We expect a strong year-end to 2024, outperforming 2023. We believe that the law firm industry is stable and we are optimistic about 2025. In the year ahead, we will likely see continued strength in the practice areas that drove activity in 2024. We also anticipate the return of M&A, corporate and transactional work broadly across all segments, as interest rates continue to fall and market conditions improve. We expect that 2025 will be a very good year for law firms.

Credits

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