PEER MONITOR INDEX

THOMSON REUTERS INSTITUTE

Q4 2021 EXECUTIVE REPORT
ISSUED 2.14.2022

2021 ENDS ON HIGH NOTES — SOME GOOD, SOME NOT

You really couldn't blame the fourth quarter of 2021 if it faltered. Unlike its previous three brethren, Q4 2021 did not benefit by comparison to the absurdly low 2020 baselines that the others enjoyed. By Q4 2020, conditions had improved to the point that performance was relatively "normal". Despite that, 2021 closed out with incredibly strong performance on key metrics such as demand, rates, and productivity. At the same time, however, increasing competition for talent set new high-water marks, leading to some calls for caution as we move into 2022.

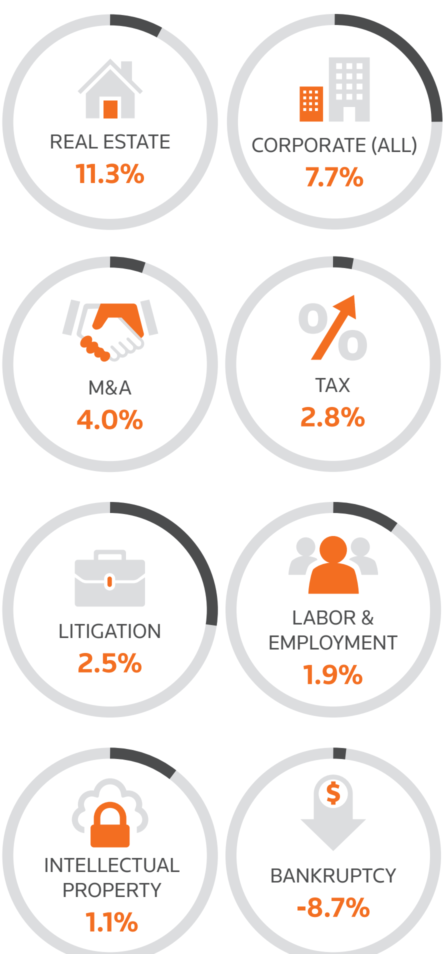
Large jumps in both direct and overhead expenses, coupled with a general cooling of worked rate growth, combined to offset a three-year high in Q4 demand growth and strong productivity growth to once again push the Thomson Reuters Peer Monitor Index (PMI) down, arriving at a score of 58 for the quarter.

Overall demand for the average law firm grew 4.2% compared to the same time in 2020. Given that improvement in demand growth had already begun by Q4 2020, this figure actually represents an appreciable degree of organic growth, even compared to pre-pandemic times. Relative to Q4 2019, average firm demand grew 3.8%. If we consider 2019 and 2021 to be "normal", this would represent roughly three-times the demand growth we would have seen in a typical year-over-year comparison.

This growth has been driven almost exclusively by transactional practices. Real estate, corporate (all), M&A, and tax practices — which increasingly represent a large share of lawyers' work — all posted strong performances not only in Q4, but for the year. These practices also have become an increasingly large share of the work being done by large law firms. By 2021's close, these practices accounted for 37% of the total hours tracked, a proportional increase of 2.6 percentage points in just one year's time and 5 points since 2015.

PRACTICE DEMAND GROWTH

Y/Y Change | **Q4 '21 vs. Q4 '20**

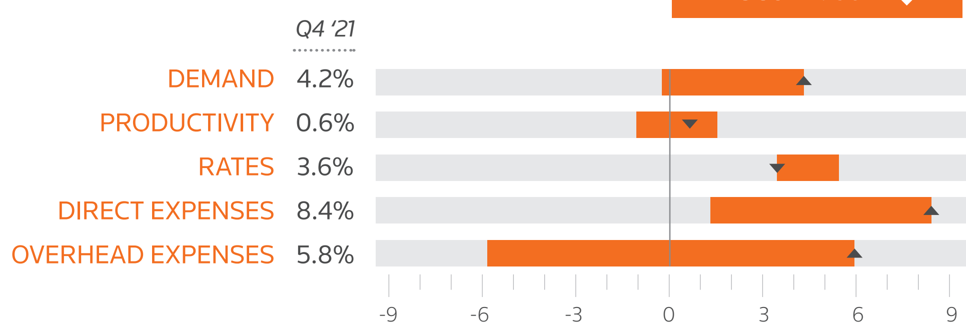


**Circular band surrounding practice is equal to Proportion of Hours Worked in 2021.*

KEY FACTORS ANALYSIS

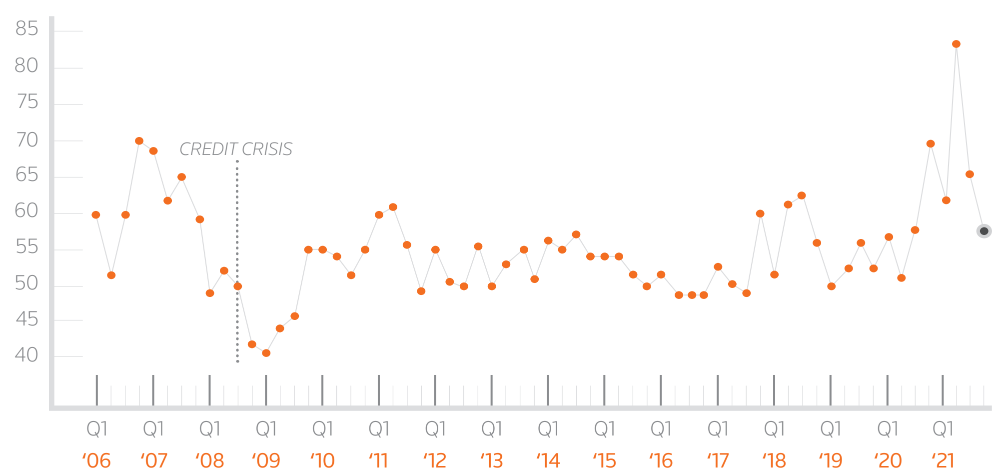
Year-Over-Year | **Q4 '21 vs. Q4 '20**

PMI SCORE: 58 ⬇ 9



Change from Q4 2020: ▲ = Up ● = Flat ▼ = Down **Current Reading (Q4 2021):** 3-Year Q4 Range

PEER MONITOR ECONOMIC INDEX (PMI)



[1]Direct expenses for the purposes of this analysis consist of compensation and benefits for all attorneys who are not equity partners.
[2]The PMI is a composite score, representing the quarter-over-quarter change in drivers of law firm profitability, including rates, demand, productivity, and expenses. Positive factors driving firm profitability will produce a higher score.

2022 will be the year of talent

Expenses were another vital component of Q4 2021, a trend which is likely to continue. Looking first at overhead expenses, Q4 2021 was almost a polar opposite of Q1 2021, posting a rolling 12-month growth in overhead expenses of 5.8%. This growth was driven by large jumps in technology, office, and marketing expenses. Increases in office expenditures are particularly noteworthy because many firms have yet to implement full return-to-office plans, indicating that this category is likely not done growing. The same can be said for marketing & business development expenses because sources of these expenses, such as conferences and client visits, have only just begun to ramp back up. Despite strong growth in Q4, total overhead expenses on a per-lawyer-FTE basis are still 2.4% below where they were in Q4 2019.

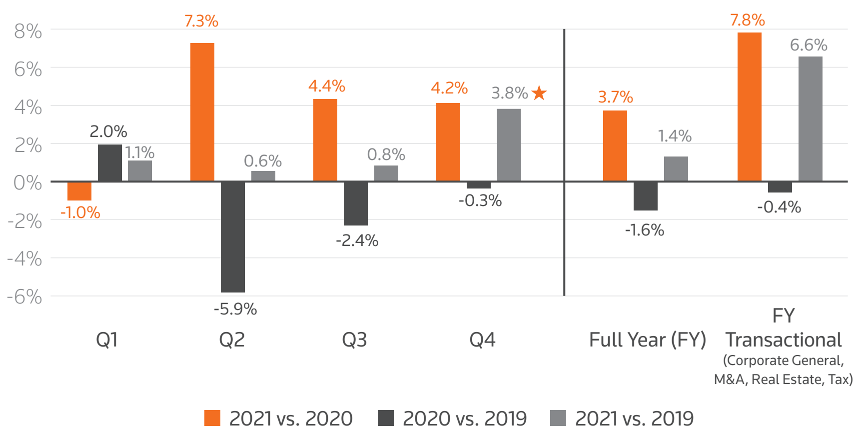
Direct expenses, on the other hand, were up 8.4%, posting a second consecutive year of Q4 growth. This increase is driven by a combination of continued aggressive hiring, with the average firm increasing headcount by 3.8%, plus growth in average associate compensation of 11.4%, reflecting increasing compensation costs.

Rising associate compensation has not, as of yet, seemed to make much of a difference in decreasing attorney turnover rates. Continued increases in the cost of associates, coupled with fast-paced turnover, is likely not a sustainable formula for many firms. Going forward, law firms may struggle to justify these costly associates, especially if they have only a short tenure. In the short-term, this may be a necessary arrangement, but eventually something must give.

This report utilizes information from the Peer Monitor / Financial Insights competitive intelligence platform. For addition detail on the data which underpins these reports, please contact Brent Turner at **763-326-6625**. To uncover the latest granular and narrowly tailed information on the large law firm industry visit the website **here** or by emailing **brent.turner@thomsonreuters.com**.

DEMAND — YEAR IN REVIEW

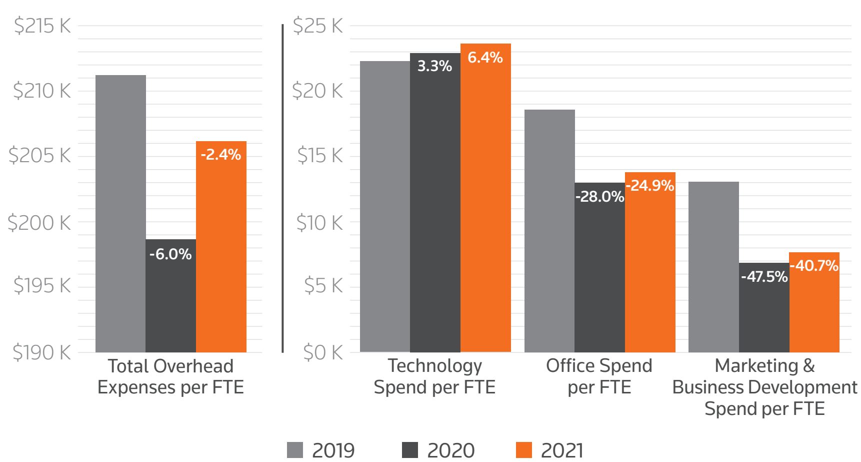
All Segments



All timekeepers; Billable time type; non-contingent matters

OVERHEAD EXPENSES PER FTE

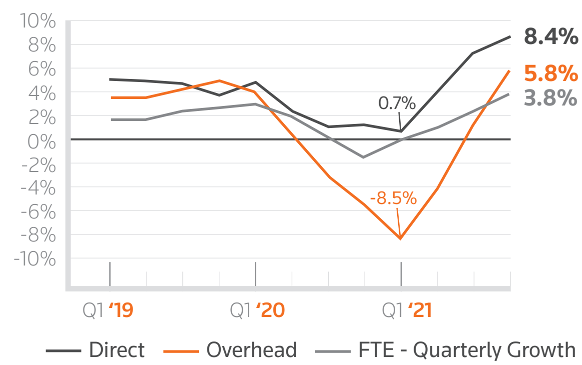
All Segments | Rolling 12-Month Values



Percentages measures change from 2019 values

EXPENSE GROWTH

Rolling 12-Month Y/Y Change



OVERHEAD HIGHLIGHTS

Rolling 12-Month Y/Y Change | Q4 '21

TECHNOLOGY
5.8%

OFFICE
7.9%

MARKETING & BUSINESS DEVELOPMENT
15.2%

PRACTICE DEMAND GROWTH

All Segments | Q4 '21 vs. Q4 '19

REAL ESTATE
10.4%

CORPORATE (ALL)
10.2%

M&A
6.0%

TAX
5.2%

LITIGATION
-1.0%

All timekeepers; Billable time type; non-contingent matters

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