THOMSON REUTERS INSTITUTE & FINANCIAL INSIGHTS

# Law Firm Financial Index

Q1 2025 Executive Report | Issued 5.5.2025

## Trade-war whiplash hits law firms

Law firms found a successful yet quiet first quarter transformed in its final weeks as a global trade war boosted their short-term prospects but could threaten their long-term prosperity. The Law Firm Financial Index[1] (LFFI) score fell 13 points in Q1 2025 to a score of 51 points, signaling that the next few quarters may be rocky indeed.

The first quarter is typically dominated by rate-setting news as law firms implement new rate schedules and test their client's willingness to accept them. On that front, firms came out of the gate with their most aggressive increases since at least 2005, with the average law firm growing their worked rates by 7.3% over their Q1 2024 levels. All segments, from Midsize all the way up to the Am Law 100, pushed the envelope with aggressive across-the-board rate setting.

At first, it looked like this aggressive rate setting would be necessary to counteract a forecasted slowing in demand growth, as the early months of the quarter looked to prove this true. However, as the trade war heated up, law firms found themselves flooded with client demand in March, with both counter-cyclical[2] practices such as litigation and transactional work like tax seeing significant spikes late in Q1. With one less working day in Q1 2025 compared to Q1 2024, this late surge did not come soon enough to elevate the overall demand for the quarter above Q4 2024 growth levels, and thus, productivity contracted as a result.

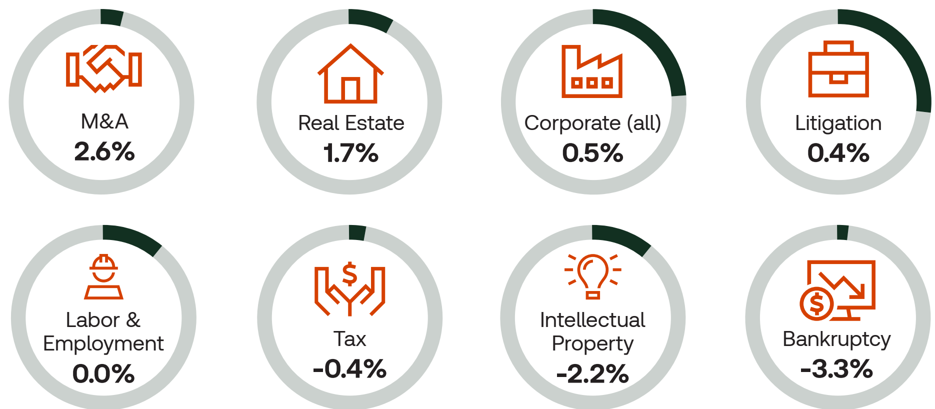
One practice that was anticipated to have a very strong 2025 but now appears to be underperforming is mergers & acquisitions. For a year that was supposed to be the

*continued*

## Practice demand growth

Y/Y Change | Q1 2025 vs. Q1 2024

Circular band surrounding practice is equal to proportion of hours worked in 2024.



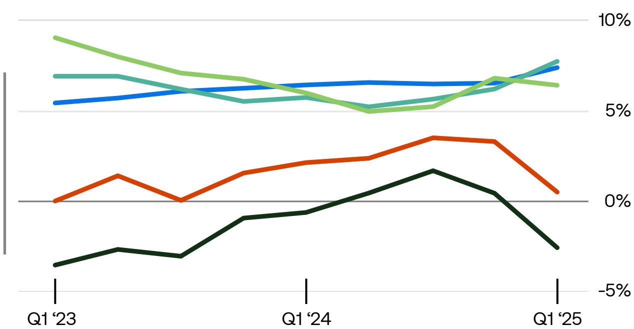

*Source: Thomson Reuters 2025*

## LFFI key factors

LFFI SCORE: 51

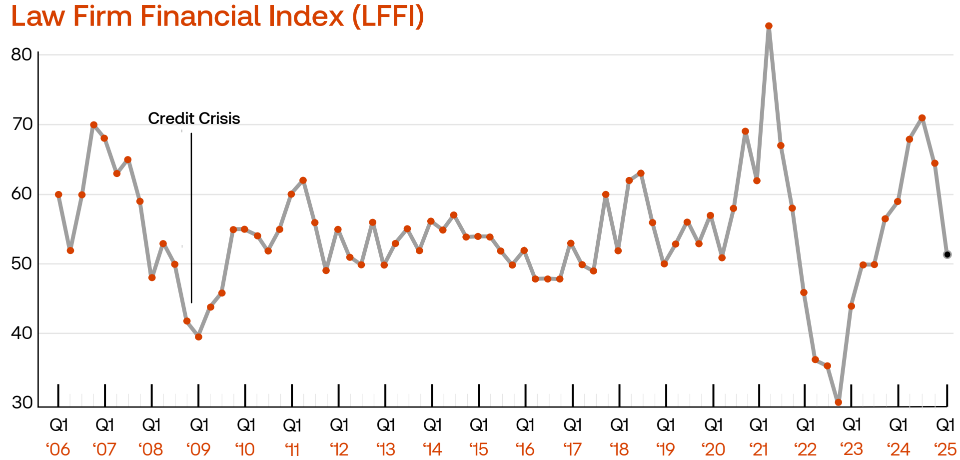
Y/Y Change | Q1 '25 vs. Q1 '24

| | Q1 '25 |
|---|---|
| Demand | 0.5% |
| Productivity | -2.4% |
| Worked rates | 7.3% |
| Direct expenses | 7.6% |
| Overhead expenses | 6.3% |




*Source: Thomson Reuters 2025*

## Law Firm Financial Index (LFFI)




*Source: Thomson Reuters 2025*

Thomson Reuters Institute

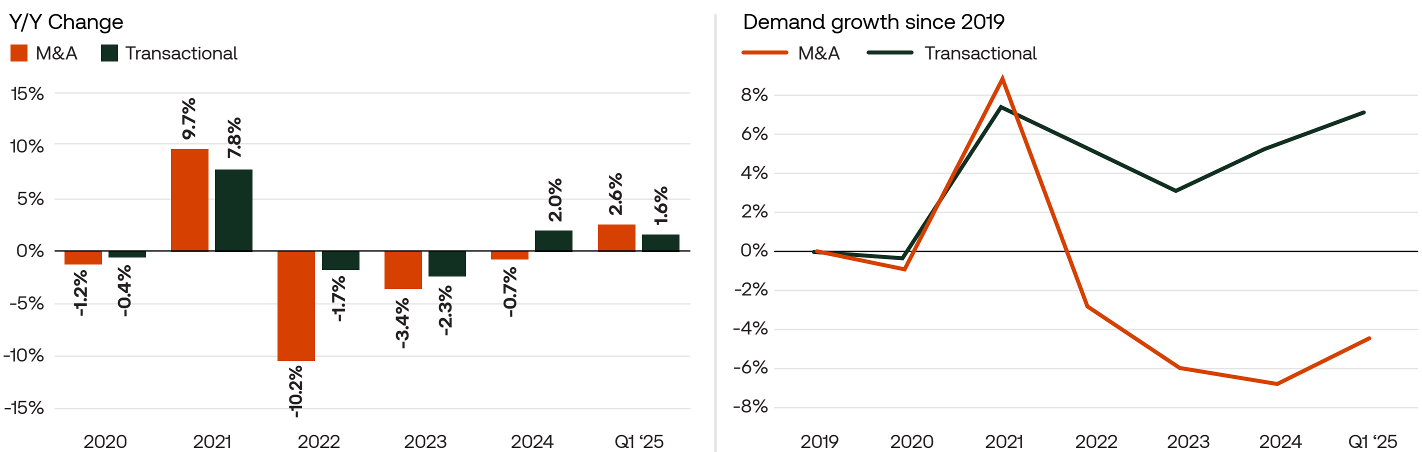
unbottling of long-delayed super-mergers and debuts, 2.6% growth in Q1 2025, compared to Q1 2024, may be below the grand expectations of the marketplace. Overall, if 2025 ended at 2.6% growth for M&A, the average firm would still be down 11.7% in billable hour volume from their 2021 highs and 4.2% below 2019 levels. It appears that the conflicting forces between the current administration's pro-business and deregulation aims, and the lingering uncertainty stymieing decision-making is limiting the upside of the usually lucrative practice.

That said, the aforementioned surge in demand within the quarter is quite real, and nowhere can the rush of client needs be seen clearer than in the realization figures for Q1. Collection compared to worked-rate realization, or the difference between the rate clients agreed to pay for a matter compared to what firms ended up collecting after the matter's completion, was off to a concerning start in Q1 in the face of a historically aggressive rate setting. Yet as the fires of the global trade war spread, it seems clients had greater concerns than trying to bargain with the firefighters. Worked versus collected realization ended Q1 2025 higher than it did in Q1 2024, a first in two years, signaling that clients were actually pushing back *less* against 2025's rates than they did against 2024's.

However, while the short-term rates and demand picture may appear solid for law firms, some challenges are emerging. For example, direct expenses[3] shot up in the first quarter as law firms aggressively competed for talent and continued to pay out performance bonuses from 2024.

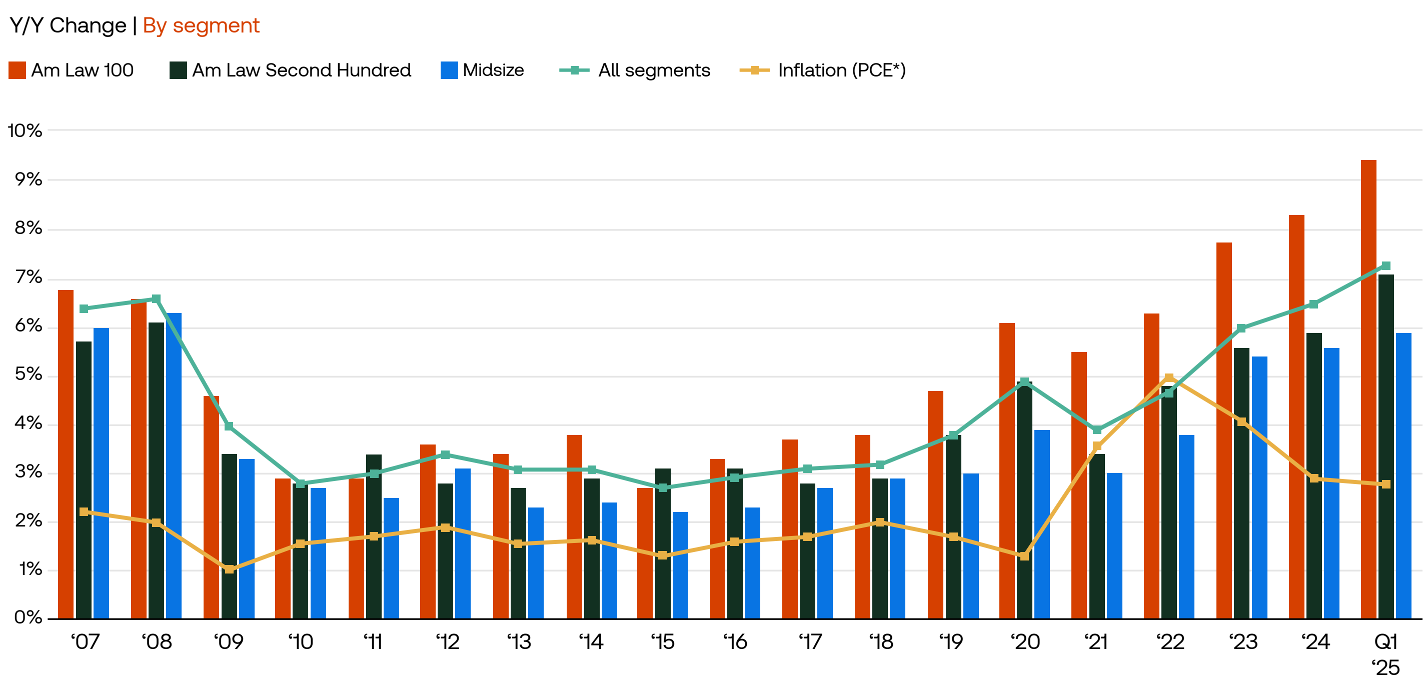
*continued*

## Mergers and Acquisitions (M&A) and transactional demand growth




*Source: Thomson Reuters 2025*

## Worked rate growth vs. inflation




*PCE Inflation measure = Personal Consumption Expenditures Excluding Food and Energy.

*Source: Thomson Reuters 2025*

Worryingly, direct expenses grew 7.6% on a rolling 12-month average, actually surpassing the record rate growth of law firms themselves.

This may mean that the long-term outlook for law firms is far more concerning. While the trade war is boosting demand and pricing power, it poses a direct threat to law firms' prospects in the latter half of the year and beyond. Interestingly, the Global Financial Crisis (GFC) resulted in an eerily similar surge in legal demand as the financial markets began collapsing in 2007, leading to that year being one of the more prosperous years for law firms. Indeed, our LFFI scores remained in fairly strong territory until Q4 2007.

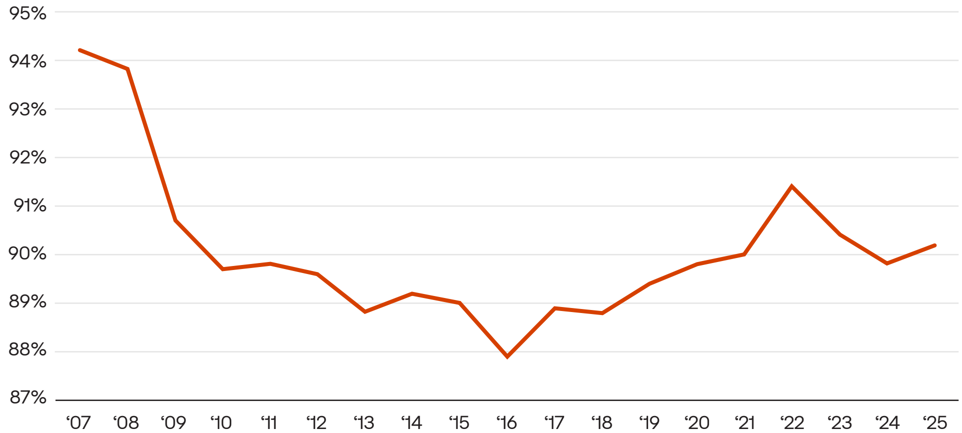
It was also their last such strong year, as in 2008 the economies of the United States and countries around the world experienced a significant downturn, resulting in broad decreases in demand and pricing power. It took law firms the better part of a decade to rebuild their transactional and counter-cyclical demand to their pre-GFC levels. Thus, economic recessions tend to benefit law firms only in the short term. While the Conference Board does not yet forecast a recession, its relatively optimistic outlook has been consistently downgraded in recent months. Other global institutions such as the World Trade Organization and major banks like J.P. Morgan have increased their recession probability to 60%, meaning law firms may face a long-lasting decline in transactional demand, which is typically a fundamental portion of their operations.

At the same time, many law firms have been put between a rock and a hard place in terms of their potential expense growth. Law firms may soon find themselves in a position in which they have to choose between spending increases to continue competing for talent and improving operations, or cutting back on expenses and investments, which slowly may make them less competitive.

Going into 2025, forecasts predicted law firms on the path to a stable, if not thrilling year, building into a much more promising 2026. In light of recent events, 2025 may now hold greater profit capacity for law firms than expected in the short term, given the sheer depth of need for their services and market-wide highs in rate growth. Yet, this also puts their future prospects in much more dire jeopardy.

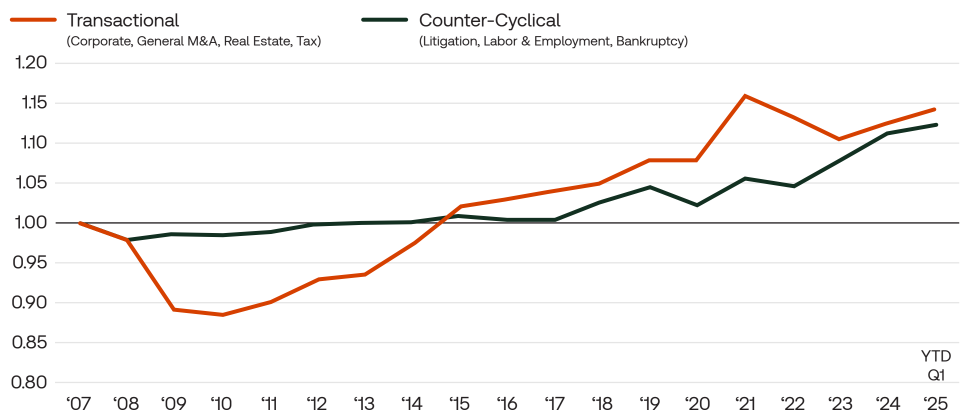
## Collection realization against worked – Q1s

All segments




*Source: Thomson Reuters 2025*

## Indexed practice demand since 2007




*Source: Thomson Reuters 2025*

1 The LFFI is a composite score, representing the quarter-over-quarter change in the key drivers of law firm profitability, including rates, demand, productivity, and expenses. Positive factors driving firm profitability will produce a higher score.

2 Counter-cyclical practices are those that typically rise as other portions of the economy slow and include litigation, bankruptcy, and labor & employment.

3 Direct expenses are those which are directly attributable to the salaries and/or bonuses of lawyers. For example: associate salaries or benefits.

*This report utilizes information from the Thomson Reuters Financial Insights competitive intelligence platform. For additional details on the data underpinning these reports, please contact Isaac Brooks at **612-270-5728**. To uncover the latest granular and tailored information on the large law firm industry, visit the customer support **website** or email isaac.brooks@thomsonreuters.com.*

Thomson Reuters Institute