

# MADRID REPORT 2011: UNLOCKING THE PRACTICE PUZZLE

*Posted on 30/06/2011*



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**The Madrid legal market is a barometer of the Spanish economy. If the country does well so do the capital's law firms. Spain may be in many senses federal but the Capital remains the focus of much of the country's corporate, finance and commercial activity. The city's law firms are therefore acutely aware of the prevailing economic challenges and looking to adjust their operations accordingly.**

El mercado legal de Madrid es un barómetro de la economía española. España tiene muchos elementos de un Estado federal, pero su capital concentra gran parte de la actividad comercial y financiera del país. Los despachos en Madrid son plenamente conscientes de los desafíos económicos actuales y ya se están adaptando a los cambios.

"Spain has clear economic challenges but we are nowhere near the situations faced by Greece, Ireland or Portugal. The country does not need rescuing. Our firm, like others, has been affected by

the downturn and we continue to face short-term challenges. But we are still moving forward," says Fernando Vives, co-Managing Partner of Spain and Continental Europe's largest law firm, Garrigues.

Lawyers agree that the nature of day-to-day legal work has changed with the downturn. There is more housekeeping work alongside a boom in litigation, refinancing and restructuring, and labour mandates, with significantly less transactional and M&A work. The result has been firms having to adjust both their practice focus and revenue expectations.

According to MergerMarket, during 2010 there were 356 announced Iberian M&A deals with a total value of €33billion, a long way off the 482 deals seen in 2007 worth a total €121bn.

Spain may not be suffering direct contagion from the troubles affecting other members of the eurozone but uncertainties remain, says Carlos Pazos, Managing Partner of SJ Berwin in Madrid. "The downturn is evident in the streets, with protests and falling consumer demand, and the Government still faces a significant deficit. So in relation to countries such as France or Germany our position is not good."

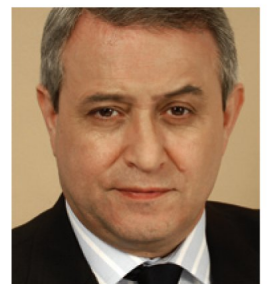
The Government has embarked on reforms and more are needed, say lawyers. A major challenge remains in bringing more flexibility to the labour market although with official unemployment figures at 21 percent there is less political will to do so.

But there have been relative successes. The Government has dramatically cut public spending, albeit by cancelling a large number of planned construction projects, and the consolidation of the country's regional savings banks (cajas) is under way. A process encouraged by The Bank of Spain which has imposed increased capital ratio thresholds, and facilitated mergers among cajas with heavy exposure to the collapsed real estate market.

This summer will likely see the first IPOs of the year, of Telefónica's call centre division Atento, and most significantly of three new merger driven banks: Bankia, Banca Cívica and Banca Mare Nostrum, and the restructuring of La Caixa as CaixaBank. Lawyers continue to highlight the potential negative impact of events in neighbouring Portugal, and elsewhere in Europe, but many in the market remain stubbornly optimistic over the prospects for the economy and Madrid's legal market through 2011.

“ If the challenge consists of offering high quality services but at a lower price the solution lies in reducing the cost of providing this service or in reducing margins. ”

Manuel Martín, Managing Partner,  
Gómez-Acebo & Pombo



"The risk issues impacting on Spain affect all of Europe and we are clearly better off in the EU than out of it," says Ignacio Ojanguren, Managing Partner of Clifford Chance in Spain. "France and Germany are on different trajectories, but we do see Spanish companies doing increasingly well and this will ultimately be reflected in a rise in their legal needs and spending." His firm is among those to feature prominently among the proposed IPOs, alongside Uría Menéndez and Linklaters.

Others also sense a tentative return of international investors. "Recent months have seen an increase in the national and international interest for specific sectors and targets, with clear movement in the financial sector. In this context, Madrid is gaining a position as the business and legal capital of Spain and it is a trend that is unlikely to reverse," says Luis Briones, Managing Partner of Baker & McKenzie in the capital.

### Management focus

The economic and productivity challenges facing Spanish businesses are though also applicable to its law firms, which are learning to better manage themselves.

"The effective utilisation of lawyers and the realisation of work is crucial. This is not a new issue and nothing that does not also apply to companies in other sectors that need to increase competitive,"

says Manuel Martín, Managing Partner of Gómez-Acebo & Pombo.

A recurring issue nonetheless is pricing. As clients have sought to reduce their cost base they have placed enormous pressure on their suppliers, including law firms. But for some in the market, it is unsustainable for firms to keep reducing fees.

"As regards fees, I think there is a structural component, which goes beyond the current economic circumstances and which is linked to the idea that the knowledge cycle gets shorter over time. To successfully adjust to this, we need to offer truly innovative law services, which add real value to the client," says Vives at Garrigues.

Some suggest however that clients are less concerned about fee levels and more about the value created by any advice given. Clients see through artificially low proposals. One of the 14 bids for the recent privatisation mandate of Spain's airports operator AENA – won by Cuatrecasas Gonçalves Pereira – was disqualified as being below the accepted "professional standard".

"In the current environment I understand that we cannot be paid as we were a few years ago, but if we reduce our fees below a certain threshold we will not return, at least for a long time, to the levels we had prior to the onset of the crisis," says Julio Veloso, Partner with Broseta in Madrid.

Some may highlight the "ridiculous offers" in the market but others emphasise that the downturn has merely heightened pre-existing tensions. Nonetheless, firms need to be efficient but it is profitability that draws top professionals to leading firms. "If the challenge consists of offering high quality services but at a lower price the solution lies in reducing the cost of providing this service or in reducing margins," says Martín at Gómez-Acebo & Pombo.

But the client demand is not always to pay "less for more" but rather to pay the appropriate amount in each case, says Andrés Monereo Velasco, Partner with at mid-sized firm Monereo Meyer Marinello Abogados. While an inevitable additional issue is ensuring payment. "Law firms have been compelled to devote more administrative staff for collection and recovery and to reduce as much as possible their fix costs – excluding salaries and social commitments," says Francisco Pala Laguna at Madrid-based Ramon & Cajal.

Spain may not be in the best of shape economically, but there is a more consistent optimism among law firms with a more evident practice or business sector niche, not least because the "traditional" law firm model relies on growth. "Our clients in IT and IP related businesses continue to do reasonably well, as they remain sectors which have been less affected by the economic crisis," says Pedro Alemán Laín, Founding Partner at Madrid's Pedro Alemán Abogados.

For most firms however the economic situation continues to present very real challenges. There is a degree of cost and lawyer manoeuvrability but there is less room for new growth in terms of lawyer and partner numbers. This means recurring issues on how to incentivise the best young lawyers and present credible career paths.

"I am at least relatively positive in this respect," says Rafael Sebastián, Director of the Madrid office of Uría Menéndez. "We have proved to be flexible in the way our staff work and in keeping our lawyers busy. We have a natural practice balance and the rise in disputes has, for example, shown that litigation can be as profitable as many M&A or corporate deals."

The downturn will nonetheless continue to present varying levels of demand, which will impact on how firms plan ahead, say others. "The main challenge will continue to be how to deal with such an adverse environment. Business generation and entrepreneurial spirit are an increasingly valuable asset among young lawyers," says José Luis Huerta, Managing Partner of Hogan Lovells in Madrid.



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Firms have to be able to adapt, but the lack of a consistent recovery across all sectors of the economy means that firms will continue to experience variable practice demand. Flexibility and focus is the key. With some beginning to question the viability of established law firm models.

“It is a challenge to balance the different practice demands and we do not yet know what the new growth model will be. What specific areas of expertise will be sustainable in the new economy and what will not, and ultimately what our law firm structures must look like,” says Fernando Torrente, co-Head of Corporate at Cuatrecasas Gonçalves Pereira in Madrid.

### Outside investment

The impetus for renewed economic growth is ultimately down to market confidence, say the Capital's lawyers. The summer IPOs will present a dramatic test of both the outside perception of the country and specifically the success of the restructuring of Spain's financial institutions.

“Since 2009 we have seen the country face two specific challenges as regards new inward investment. The first being the general uncertainty over the direction of the economy, and for those that were prepared to still do deals, the significant challenges they faced in raising the necessary finance,” says Pedro Pérez-Llorca, Senior Partner of Pérez-Llorca.

There are now two economic realities, say some: that affecting peoples' everyday lives, and the other where companies are beginning to return to profit – having restructured their operations and debt obligations – but which are less connected, or at least less reliant, on the domestic Spanish market. Many businesses are looking for new growth opportunities across Latin America, as well as now the Middle East and Asia.

Such a development inevitably presents Madrid's firms with a challenge: how to continue to demonstrate that they can add value to clients' international operations.

“Spanish law is not utilised globally in the same way as English or US law so we have to accept certain limitations, but for us it is important to be in the major legal centres and to develop strong connections in markets such as London and New York,” says Martin at Gómez-Acebo & Pombo.

Latin America is naturally attractive for Spanish firms, but even the UK firms in the market are increasingly looking towards it. “A firm such as ours is seeing more demand to open in new markets, albeit currently the Middle East and Asia, to help clients as they grow internationally. But we also accept that we have jurisdiction-specific expertise. We have therefore to sell the expertise of the 'network' we have already invested in,” says Inaki Gabilondo, Managing Partner of Freshfields in Madrid.

Others suggest nonetheless that Spanish firms can compete around the world. “For many international transactions our clients are not necessarily looking to capitalise only on our legal skills. They want to understand the local commercial perspective and to increasingly rely on our project management expertise,” says Torrente at Cuatrecasas.

### Legal capital

Domestically at least, the Madrid offices of Spanish law firms are already at an advantage believe many managing partners. It is increasingly viewed as the corporate capital of the country, as well as already being the seat of the major policymakers and regulatory agencies, and the centre of the banking, finance and insurance sectors.

Some national firms admit that well over three-quarters of their revenues are now derived from the

Madrid offices albeit the legal market is more competitive than ever. "Practically all major transactions with an international component are negotiated and closed in Madrid," says Diego Lozano, Partner with Ramón & Cajal.

But in a country with a large degree of regional autonomy a geographic reach outside the Capital remains important for many firms. However with a foot in both Barcelona and Madrid, many feel sufficiently content. "We opened in Barcelona in 1994 and we have never felt the need to open offices other than here and Madrid," says Pedro Pérez-Llorca.

For some, Madrid is also gaining more importance as a legal centre reflecting the desire of many multinationals to adopt a single regional headquarters and commercial strategy for the Peninsula. "It is possible that the ongoing crisis will change the business map, and that as a consequence of this, Madrid will become the business and 'legal' capital of Iberia. However, Barcelona and Lisbon will always be of importance in the legal and business sectors," agrees fellow Partner Iván Delgado.

Although in the prevailing difficult environment the willingness of some companies to maintain the unity of their Spanish and Portuguese operations may be challenged.

"The concept of 'Iberia' functions well in good economic times but we see a rapid disaggregation of business structures in these more difficult times. Businesses can be structured to benefit from logistic and administrative synergies but the Spanish and Portuguese markets are still very different, and legal issues remain jurisdiction specific," says Serena Argente Escartin, who leads the Madrid office of Lisbon-based Raposo Bernardo & Asociados.

### **An attractive destination**

Even in the face of the economic downturn there is however no doubt the attraction of Spain continues, and Madrid remains the focus of many foreign firms' wishing to cover the market. The legal market has continued to experience change over the past year, including the arrival of new firms, among them London-based Olswang which launched with the hire of a team from Bird & Bird led by corporate Partner Javier Vasserot, shortly after the launch of Watson Farley & Williams, while Squire Sanders has now returned to the market through a merger.

More recently, there have also been significant team moves as firms look to capitalise on those areas where there is the continuing potential for growth. Typical was the relocation of almost the entire Madrid restructuring and insolvency team of Roca Junyent, led by Partners Javier Díaz-Gálvez and Luis Martín, to DLA Piper's Madrid office.

"One of the key implications of the current fee pressure we see is that teams tend to be smaller and more senior. Clients demand more partner time, which as a matter of fact, even if more expensive per hour may prove cheaper in terms of efficiency," says Juan Picón, Managing Partner of DLA Piper in Spain.

Competition boutique Martínez Lage has regained its independence, rebranded as Martínez Lage Allendesalazar Brokelmann, following the collapse of Howrey, while Eversheds is another firm experiencing change, with an imminent new local affiliate. Madrid-based Nicea Abogados is to replace Lupicinio, which has decided to leave the network citing strategic differences.

Other firms have also however seen management changes, among the most notable being the elevation of Mercedes Fernández as Managing Partner of Jones Day, following the relocation of Luis Riesgo to lead the firm's Brazilian venture.

For some firms, the downturn has clearly proved an opportunity to attract talent, among them Herbert Smith. "We are now focusing our efforts on consolidating our market exposure but at the same time believe we have a quite balanced practice. In general terms we perceive law firms in Madrid focusing on maintaining work levels and managing fixed costs," says Partner Ignacio Díez-

Picazo.

Some may question whether there will be more new international arrivals in the short term, but for those managing partners already with them the benefits of an established cross-border network is obvious. "The approach of clients is changing. Major Spanish companies look to Madrid for international firms able to deal with their legal business. The one stop shop concept really sells well," says Rafael Alonso, Managing Partner of what is now Squire Sanders Hammonds.

Some suggest that the downturn and evident practice pressures may also prompt a continuance of the merger trend among mid-tier firms, the most notable in recent years of Dutilh with Barcelona's Vialegis, and the emergence of new smaller and niche practices – such as Gold, Hernández-Echevarría and Laffer. Large firms continue to quietly downsize, either not replacing those who leave or "assisting" others to leave. Some are also seeing the departure of partners and senior assistants in the face of fewer promotion prospects or practice rationalisation.

"Deeper changes, although hidden in most cases, are taking place. But we may all have to review the way we structure our law firms," says Veloso at Broseta. "In a growth environment, the model works. In a decreasing environment, we have to see what we must do to attract and retain talent if we cannot offer partnership or we have to extend the period to become a partner."

### Natural selection

A number of firms have already begun, in private, to question their trajectories and with limited prospects for new growth begun looking for a new direction or niche. "Arguably some players may in the short term either have to shut down operations or keep costs to a minimum to make it through the downturn," believes Picón at DLA Piper.

For others such developments are merely the inevitable reaction of firms confronting the continuing economic uncertainty. Large law firms let people go as activity has reduced just as they increased numbers in the boom years. This time round there is merely more transparency, but clearly firms need not only to have a strategy but be willing to implement it. "It is difficult to speculate when the long-awaited economic recovery will appear. But we do see companies across various sectors reacting boldly, participating in transactions and entering new markets. There is also no doubt that Madrid is Spain's nerve centre for business decision-making, its investment centre, and the leading legal sector," says Julián García Rubí, Madrid Partner of Cuatrecasas Gonçalves Pereira. "But a presence in the capital is not enough to guarantee future success. Firms need to think ahead."

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Madrid, DLA Piper



For some smaller firms their ability to offer very niche services will remain a market differentiator. But others see a continuing need to innovate. "Even if we consider the sector in which we operate, the entertainment and media industries, the two words that best describe our present legal market are 'change and innovation'. There is no 'business as usual'," says José Antonio Suárez Lozano, Managing Partner of boutique Suárez de la Dehesa.

For other firms their differentiation is their international structure, geographic or practice spread. There is no "one-size-fits-all approach" and many firms are wrestling with how to adapt to the new "normal" with structures built in economically better times.

All agree however that there is no easy solution to the practice challenges they face, at home or abroad. Economic recovery is a slow process, and for many, Spain is only now beginning to show the first tentative results of the ongoing restructuring the country requires. This summer will present a clear test of investor confidence, which may yet however lead to more rapid change.

Statistics show that the Madrid economy is doing better than elsewhere in Spain but the Capital's law firms have to live with the national market as they find it. The focus for many therefore is on retaining cohesion, developing new service lines, and managing the expectations of their own lawyers.

"We are still growing but do not want to become fixated by profits," says Vives at Garrigues. His firm has seen five percent revenue growth and a continuing rise in demand for specific areas of expertise.

Firms have however to continue to reduce costs, to react to market and economic changes, and pressures, and ultimately to decide how their lawyers can develop their careers, be that in Madrid, Spain or elsewhere.