

Private equity in the legal sector: the approaching wave

These developments have taken a lot of law firms by surprise as many observers never thought private equity would branch out into consumer facing legal services

22 Dec 2023 – Solicitors Journal



Jeff Zindani discusses the rise of private equity in the legal sector and his predictions for 2024

Talk of private equity or other external investors invariably elicits a negative response with many law firms viewing them as ‘ruthless asset strippers’ or questioning their ability to run law firms compared to the traditional partnership model.

Perhaps this isn’t surprising when even the likes of Warren Buffet see private equity firms as ‘evil’ actors with exaggerated promises and poor returns.

There remains an opaqueness around private equity but the reality is they follow a predictable playbook and more importantly are becoming a real force in the legal sector with the potential to challenge conventional firms. December saw yet

another private equity backed expansion with Stowe Family Law acquiring fellow family specialist Crisp & Co, a firm with 17 offices across the country.

Movement in the legal sector

The legal sector is seen as a new frontier for private equity, where solid margins of around 30 per cent are the norm for most well-run law firms, with profits well above those typically enjoyed by non-legal businesses. Established firms are regarded by many as 'eternally profitable businesses', particularly if they are full-service firms that can ride economic storms due to mixed practice areas.

Private equity investors generally have a strategy around buy-and-build, which involves forming a platform company and then aggregating and integrating smaller add-on acquisitions to achieve rapid growth and scale.

On exit, the investment benefits from the arbitrage between the higher EBITDA (earnings before interest, taxes, depreciation and amortisation) multiples that larger enterprises command and the lower multiples paid across for the various smaller acquisitions.

We can see already this strategy being used by Lawfront who have, in the past two years acquired north west firm Farleys, Essex practice FJG and Nelsons in the East Midlands, giving the company annual revenues of over £45m. Another active private equity backed business in a similar space is MAPD Group (standing for Making a Positive Difference), which most recently acquired Cumbrian firm Thomson Hayton Winkley and Ashton-under-Lyne practice Bromleys.

Consolidation

It appears that consolidation in the legal sector is becoming a coherent and properly funded strategy. As private equity steps up its investment, this is bound to gather more pace, particularly around mid-sized law firms.

Consider the entry by Sun European Partners into the legal sector two years ago when it acquired leading claimant serious personal injury firm Fletchers for over £40m, clearly demonstrating not only intent but real firepower.

These developments have taken a lot of law firms by surprise as many observers never thought private equity would branch out into consumer facing legal services. This is perhaps because the history of private equity in the personal injury sector is controversial, with another large personal injury practice Roberts

Jackson becoming one of the biggest failures, leaving its private equity investors North Edge Capital with a £22.5m loss back in 2019.

Private equity firms are some of the most sophisticated buyers and investors out there. The likes of Sun European Partners would not be investing unless they could see a return. It is also worth pointing out that, although it might be counterintuitive to many in the legal sector, private equity likes to take underperforming businesses and turn them into something special. The rationale behind private equity is to take a business and to make it more valuable. This will clearly chime with law firm partners who know that while they may be excellent managers, they never came into the law to run a business.

The future

My prediction is that in 2024 we will see the major players in private equity continuing to follow this playbook of making a law firm more valuable by buying a firm they then use as a platform for further acquisitions, with a clear ‘buy-to-build’ strategy.

We know from discussions with law firms over the past five years that there is little appetite for private equity, particularly among traditional law firms, but this may well change as the success of these outfits becomes more apparent.

If not enamoured by private equity, perhaps law firms can learn something from their buy-to-build approach – imitation can be better than innovation. What is clear however, is that we are looking at a coming wave of private equity that is set to increase competition and heat up this fluid sector.

Jeff Zindani is a merger consultant and matchmaker for law firms and legal tech companies at Acqira Professional Services <https://www.acquiraps.co.uk/>