Out on a limb

ECONOMIC CONDITIONS IN THE IBERIAN PENINSULA ARE AT THE HEART OF THE CONTINENT'S DEBT AND CURRENCY CRISIS. JONATHAN AMES REPORTS FROM LISBON AND MADRID ON HOW LEADING LAW FIRMS ARE COPING WITH A STORM THAT SOME SUGGEST COULD SPELL THE END OF THE EUROPEAN IDEAL

Wandering the streets of Lisbon, the word 'junk' does not immediately spring to mind.

One of Europe's oldest capital cities may well be a bit frayed round the edges, but locals still pack the pavement bars and cafes of the wide, tree-lined Avenida da Liberdade and the dockside Praça do Comércio. Visitors and residents alike flock to the Lavra, Glória and Bica funiculars, which still trundle up the city's renowned steep hills, albeit with the carriages covered in 1980s New York-style graffiti. And people from around Portugal's former colonies mix in what appears to be a calm and relaxed southern European atmosphere.

But in the harsh world of international credit rating agencies, junk is exactly what Portugal is. In mid-summer, Moody's slashed the country's rating to junk status on fears that Portugal was a cigarette paper away from joining Greece in the humiliated ranks of European states gone bad and that it would need a second bail out from the combined forces of the International Monetary Fund, the EU and the European Central Bank.

Contagion

However, as worrying as the state of the Portuguese economy is, it is nothing compared to concerns for its bigger neighbour. Some 600km to the east, in Madrid, the Spanish government has been battling against the word 'contagion' and the perception that it is next in the breadline following the spectacular collapse of its property market and rocketing unemployment figures. If Spain goes under, runs the argument, then Italy will be next (indeed, there are now even fears over the exposure of France's banks) and Europe can kiss good-bye to the short-lived ideal of a single currency and greater economic and fiscal harmonisation.

Lisbon funicular: Portugal faces steep climb to recovery

Business lawyers in both jurisdictions are understandably restrained and in common with their counterparts at the leading firms in Italy, they are looking overseas to prop up what otherwise would be very wobbly bottom lines. It is estimated that there are about 620 million native speakers of either Spanish or Portuguese around the world, a combined total that falls second only to Mandarin in the global league table. And of those Spanish and Portuguese speakers, more than 563 million live outside the Iberian Peninsula.

Native tongues

So it is businesses and corporations spread across South America, Africa and South-east Asia that are being targeted by Spanish and Portuguese law firms. For however popular and crucial English is as the overwhelming lingua franca of the 21st century, businesspeople still like to speak to their lawyers in their native tongue.

Ironically, therefore, economic trouble at home could trigger a resurgence in the impact and power of Spain and Portugal abroad, as Iberian law firms follow their clients to more prosperous territories around the world. The other issue hovering over the business law firm landscape in the two countries is if and when a true Iberian market will develop. There are some prominent firms that maintain that level of evolution is well on track, while others are adamant that talk of a pan-Iberian business model is little more than marketing hogwash.

Regional focus: Iberia

Portugal

Population: 10.6 million

Capital: Lisbon (population – 550,000)

Currency: euro

World Bank's ease of doing business ranking: 31st in 2011; 33rd in 2010.

It is impossible to disguise that times are tough in Portugal. A relatively small jurisdiction on Europe's western fringe, the country has in the past been dwarfed – and often bullied – by Spain, with the Portuguese historically siding with their long-standing ally, Britain, in European disputes, while the Spanish joined forces with the French.

Relations between Portugal and its bigger sibling have been relatively harmonious since both sides jettisoned fascism in the mid-1970s and joined the then-EEC at the same time a decade later. But it is the country's economic position in the EU that is now the cause of so much debate.

Selling abroad

While the spotlight has been on Portugal recently following speculation that it would become 'the next Greece', its economy has for years been wobbly at best. Comments one leading local commercial lawyer: 'Portugal has been in a depression mood for a few years – even back in 2001, while the rest of Europe was growing at a fast pace, this was not the case in Portugal.'

At the heart of the problem has been an uncompetitive and rigid economy that is over-reliant on the state to create public sector employment. Portugal also suffers from an apparent inability to export at a level expected of a country that historically played such a significant trading and colonial role.

'Portugal doesn't export enough for its size,' the country's

TAP: flag carrier up for sale to boost national coffers

Economy Minister, Alvaro Santos Pereira, told a parliamentary committee at the beginning of August. According to the Dow Jones news agency, Mr Pereira went on to suggest that Portugal should have a target of exporting around half of its gross domestic product in five years' time, an increase on the 35 per cent of GDP it currently exports.

Exporting its way out of a nasty trade deficit is seen as a priority by the government. Indeed, Mr Pereira gave a stark warning to parliament that if the country failed to deal with that gap then 'the government could be forced to impose more austerity measures to meet set targets under the bailout'.

It is that bailout plan that is already imposing hardship, with the country required to slash its budget deficit – which stood at 9.1 per cent of GDP last year – to 5.9 per cent this year and 4.5 per cent next. The IMF and the EU have also forced Portugal to set a raft of core structural reforms, including modernising its judicial processes.

Falling on sword

The crisis and bailout – which was agreed between the Portuguese government, the troika of the IMF, the EU and the European Central Bank – resulted in Socialist Party Prime Minister José Sócrates falling on his sword and triggering elections at the beginning of June. In came a Social Democrat Party government led by new Prime Minister Pedro Passos Coelho, who has been on a mission of implementing the bailout programme ever since combining a special income ta with deep spending cuts.

Those efforts – while causin considerable pain to ordinary Portuguese – are winning plaudits from the business sect 'We are seeing a serious effort on the part of the government – and other relevant parties – t adhere to the principles of the memorandum agreement sign by the troika and the Portugue state,' comments Maria João Ricou, joint managing partner with Diogo Perestrelo at law fi Cuatrecasas Goncalves Pereira. 'We are all focused on trying to avoid becoming the next Greece.' Business lawyers agre that the austerity programme will have a significant impact on the economy and on investment over the next two years. 'Generally, our clients will be badly hit,' acknowledg Ms Ricou. 'They will need to focus on other markets to try t compensate for the business tl can't do domestically. They wi need to focus on exports. But not everyone can do that, and there are other countries tryin to do the same thing and they are better placed to do so than we are because they are more competitive. That is one of th things we need to change and one of the aspects the troika has pointed out. But that is something we cannot change overnight – it will take some time.'

Some practitioners take an

even dimmer view. Manuel Santos Vitor is the managing partner at the country's biggest law firm, PLMJ and he maintains that 'there is significant concern among business lawyers in Portugal that the economic picture could worsen and that we will become the next Greece. If that were to happen it would be a complete nightmare. The economic side of Greece is bad, but even worse is the social unrest. We have been for at least 100 years a quite peaceful nation without social unrest despite some of the difficult times we've had in the past.'

Paulo Costa, a partner at law firm Miranda, is even blunter. 'The current Iberian market is completely flat. Anyone in Portugal with any brains is a bit scared and a bit puzzled and feels very insecure about the short and medium-term future. If Portugal reaches the position of Greece – and it is difficult to say that it won't – then the legal sector here will face very tough times. Indeed, it is already facing tough days.'

For sale

But the main immediate problem is in the real economy, says Mr Vitor. 'Complying with these deadlines will hit many ordinary Portuguese citizens directly in their pockets. There will be additional unemployment and the rate is already quite high. Taxation will also rise – VAT will rise on day-to-day consumer items. This will cause difficulties for most people – but it is unavoidable and we'll have to suck it up. One hopes that by the end of next year things should be better – provided we cut public spending and sell state-owned companies.'

Already, the new government has said it will put Portugal's flag carrier airline, TAP, on the block for sale, as well as the state's interest in the electricity and other utility companies. Indeed, it is the expected privatisation programme that many law firms are banking on as providing some domestic succour.

'Greece is behind Portugal in a privatisation programme, so they have more potential to raise money from selling state-owned companies,' points out Manuel Protasio, a corporate mergers and acquisitions partner at leading law firm Vieira de Almeida & Associados. 'But we still have some companies to be sold and an acceleration of that process is part of the bail-out programme.'

However, Mr Protasio warns that 'most of the major public companies in Portugal have already been brought to the market so there is less money to be raised'. But ultimately he maintains the bailout programme 'should bring more work to law firms', with opportunities in the financing area in addition to traditional privatisation work.

Nonetheless, lawyers acknowledge there is no escaping the fact that there will be a downwards move in terms of straight-forward investment into Portugal, at least while interest rates are so high and the ratings agencies remain twitchy. Mr Protasio forecasts that nervousness will last at least until the end of this year, but he cautiously suggests that the situation could begin to improve at the beginning of 2012.

In addition to the looming privatisation plans, the bailout also calls for the affordability and viability of key elements of Portugal's huge public-private partnership programme to be reappraised, which is likely to lead to a renegotiation of many contracts. For example, the government has already suspended its side of the highly-touted high-speed rail line that was meant to connect Lisbon and Madrid. That decision was taken despite the first section already having been completed, leaving the second phase – involving an expensive bridge to be built over the Tagus River – hanging unfinished.

Plans for a new Lisbon airport have also been put on hold, although lawyers suggest this project is more likely to get another green light as there is private sector interest in backing it.

Slow judges

The bailout deal has also called for Portugal's creaking commercial justice system to go under the spotlight, with measures to be put in place to reduce delays in court decisions. 'They have the same problems in Spain,' admits Cuatrecasas's Diogo Perestrelo. 'The Latin character is not disposed towards taking fast decisions; the judges tend to be very slow. It's getting better – but it is still not as good as we'd like it and as foreign investors would like. And this is a point that is at least partially addressed by the memorandum. It is a cultural problem, but there are some easy measures that can be taken, for example, reducing holidays for judges – currently they get two months or slightly more.'

Domestic issues to one side, it is opportunities overseas that are most enticing for Portuguese law firms. An early proponent of looking abroad has been Miranda, which first turned its attentions to foreign, Portuguese-speaking jurisdictions around two decades ago when it struck an alliance with a practice in Angola.

'We work with local firms and we try to work on more than a referral basis, in a fully-integrated manner with our local partners,' explains Paulo Costa. 'That has always been our model – not just to refer the clients but to be there with them. And this approach applies to all our jurisdictions, whether it be Angola or East Timor.'

According to Mr Costa, Miranda's model was originally heavily criticised by Portuguese and Spanish competitors as being impractical. 'But it has proved to be right. And now our model is being followed by our competition in Portugal and Spain. They are trying to find new markets abroad, with or without their clients. They are all trying to expand there because Portugal is completely stopped – there is not public investment, the state is facing a budget crisis that will continue for at least two to three years – there are no funds whatsoever.'

Bad timing

Are the other firms coming to the overseas game too late? Mr Costa is relatively diplomatic. 'They are perhaps going for the wrong reasons and the timing could not be worse,' he says. Explaining 'the wrong reasons', Mr Costa says Portuguese firms are now looking abroad simply in an attempt to survive. 'It is one thing if your law firm economics are ok and you are looking to expand the business. But if you are going abroad simply to control your losses, perhaps that is not the right reason.'

As far as timing is concerned, Mr Costa again sounds a warning to his firm's competitors. 'These countries where Portuguese firms have a competitive edge require a large amount of resources – not just in terms of money, but in terms of finding the right human resources, finding the right lawyers and training them, teaching our colleagues to work in different environments and to international standards. This takes time – it is not something you can do in six months or a year, or even three years. From our experience, to become acquainted with the local market can take up to four years. The learning curve is long and it goes to your pocket. So doing this when your pockets are not full of money is not a good thing.'

Raposo Bernado is another medium-sized Portuguese firm that has spent the last decade cultivating an overseas mentality. After putting a tentative toe in the water with an office in Madrid in 2002, the firm has subsequently launched either outposts or alliances in Angola, Mozambique, Cape Verde, Poland and Romania. Explains Joana Andrade Correia, the partner co-head of the firm's corporate and M&A department: 'Other Portuguese firms have family heritages that prevent them from taking innovative decisions – whereas we have a vision and ambition.'

But the bigger players are catching up. For example, Cuatrecasas has taken the bold step of opening in Brazil, despite conventional wisdom suggesting that the jurisdiction's legal sector is too advanced and competitive to crack. But as Maria João Ricou points out, 'the Chinese are very interested in both Brazil and Africa'.

Eastern promise

Indeed, that thought is very much at the forefront of thinking at PLMJ. While Manuel Santos Vitor describes Brazil as being a 'too mature' market to require any more commitment from the firm than its existing non-exclusive referral arrangement with local firm TozziniFreire, he sees China as meriting an actual Portuguese lawyer presence. The firm has two senior associates posted to the offices of its associated practice in Beijing. 'We do not expect to see much outbound business from Portugal to China,' he explains, 'but to see significant possibilities from China to Angola and Mozambique. There is significant Chinese interest in Portuguese-speaking Africa.'

And likewise, significant Portuguese law firm interest in Francophone Africa – at least as far as Miranda is concerned. The firm opened in Gabon 18 months ago and in the Republic of Congo earlier this year. 'Africa is what we do best,' explains Paulo Costa. 'This is critical for us because we already have a presence in all Portuguese-speaking African countries and most of our clients are also doing business in the francophone countries. Gabon is already a profitable jurisdiction for us. In the past the UK firms used to look at Africa and say it was too risky, too strange. But Africa in the next few years should explode in terms of growth'

So why aren't the French lawyers servicing those clients? 'That is a problem with the French law firms,' he says. 'French lawyers don't like to travel. The biggest challenge for us now is to find French-speaking lawyers of quality in Africa.'

Whether in Africa or even further afield, overseas endeavours are very much the route to future success, says Mr Costa. 'Most Portuguese corporations that are doing well are making their revenues or transactions outside the country, and therefore they don't need that much domestic legal advice, they need international advice or local advice in those countries in which they are operating. So that is the way to go for Portuguese law firms – pack and fly.'

Spain

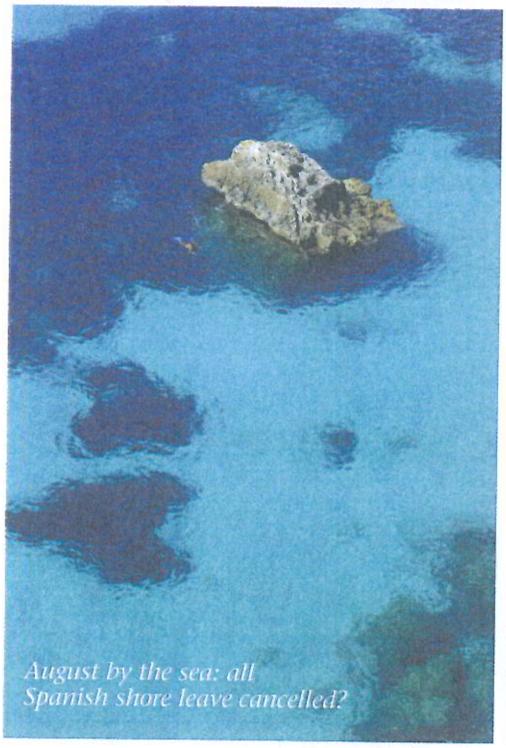
Population: 46 million

Capital: Madrid (population – 3.3 million)

Other important commercial centres: Barcelona (population – 1.6 million); Valencia (population – 810,000)

Currency: euro

World Bank's ease of doing business ranking: 49th in 2011; 48th in 2010.



August by the sea: all Spanish shore leave cancelled?

Often small cultural quirks shed light on macro-economic traumas and recent developments regarding Spanish holiday habits have done just that.

Spaniards – in common with the French – historically aim to down tools for the entire month of August and head for four weeks of cooling breezes at the seaside. But this year, with official unemployment figures running at more than 20 per cent – the highest in the eurozone – and all of Europe on tenterhooks to see whether the country is next in line for an IMF bailout, many of the Spanish are reported to have worked through August.

Small businesses especially – such as bars and specialist shops – are desperate for any revenue they can muster, in

Regional focus: Iberia

addition to being frightened that it if they shut down for a month their clientele might not return in September.

As in Portugal, Spanish business lawyers are quick to recognise the problems in the real economy. 'For the general public, the economic situation in Spain is very bad,' comments Pedro Perez-Llorca, senior partner of Madrid-based law firm Perez-Llorca. 'And that can be summarised in a single figure: 21 per cent unemployment, which is a complete disaster.'

But having pointed out that similarity, leading Spanish practitioners are also adamant that there are crucial differences on the Iberian Peninsula. Comments Rafael Montejo Perez, at partner at Madrid law firm Lener: 'I don't think Spain has to be mixed up in the same group as Greece, Portugal and Ireland. One of the big differences between Spain and Portugal is that in the latter – apart from Lisbon and Porto – most of the country is undeveloped. But in Spain, there are several regional cities and there is economic activity throughout the country.'

Indeed, Spanish lawyers maintain there is a simple answer to their country's economic woes – huge exposure to a real estate bubble that has spectacularly burst. 'There was enormous growth in the 1990s and the early part of the last decade,' says Mr Perez, 'but it was based on speculation.'

No banking crisis

Agustin Bou, a corporate partner at law firm Jausas, supports that view: 'We know very well what our problem is, which is a real estate or construction problem.' He points out that the country is not suffering a banking crisis owing to historically strict regulations in that sector, meaning that the problem with the Spanish banking system has been not with the large commercial providers but with the savings banks, or *cajas*. And those problems are now being addressed through mergers, which in themselves provide a seam of work for the business law sector.

Senior figures at Spain's biggest firms also agree that the business law outlook is by no means entirely grim. 'There are two different levels to this crisis,' remarks Fernando Vives, managing partner of Iberian international firm Garrigues. 'The level of the big corporations and the other level is the real economy of the people in the street. Until now, we've not seen a different approach to business by our clients – nothing has changed if you compare now with six months ago. And the near future offers new opportunities in Portugal. All the privatisations will come on to the market this autumn and some Spanish and foreign companies will be interested.'

Ultimately, some leading Spanish lawyers invoke a well worn cliché to express confidence in their position. 'The advantage of Spain is that it is big,' says Agustin Bou. 'I won't say too big to fail, but a bit big to fail.' While Jose Maria Segovia, the senior partner at Madrid-based international firm Uría Menéndez, goes even further: 'It is true that Spain is too big to fail. And it has one of the lowest sovereign indebtedness levels in Europe.'

That said, Mr Segovia also recognises that these are not normal times and that events can take on a momentum of their own. 'If pressure were put on Spain by the ratings agencies, then that would be a problem. Because I don't see Spain having problems that, say, Italy doesn't have. And if Spain fails and then Italy fails, then everything in the eurozone fails.'

Decreasing revenues

Such a collapse would be unfair on Iberian firms, say their partners, as despite the wider economic problems, their own businesses have performed well. 'Over the last two years, Spanish and Portuguese law firms have done much better than many other European practices,' maintains Mr Segovia. 'Meeting colleagues from Paris and London I hear about decreases in revenue of 12, 17 and 20 per cent. But Spanish firms haven't seen that level of drop.' He maintains that Uría itself increased turnover last year by 3.5 per cent. 'We've had increases – modest increases – but increases nonetheless in revenue throughout the financial crisis. And that is true for nearly all the main Spanish law firms.'

Perhaps the biggest challenge facing the major Spanish business law specialists is one that their counterparts in Paris would recognise – fee cutting by international competitors. Leading partners in Madrid maintain that UK practices are desperate to maintain market share in Iberia and are therefore dramatically reducing fees to keep their instructions up.

'The big international firms in Madrid are reducing rates to keep work,' explains Lener's Rafael Montejo Pérez bluntly. 'And in some cases I've seen amazing price reductions – I don't know how they can make money offering those fee rates.' His counterpart at Garrigues, Fernando Vives, agrees: 'The global firm offices in Madrid are dramatically undercutting fees in an attempt to retain market share. This obviously impacts on domestic firms such as ours, but we have more tools to defend our position. We have a very solid base of clients.

'The question is whether the fees will increase when the crisis subsides and indeed whether the number of lawyers at the Madrid offices of global firms will increase when the situation improves.'

Low-balling

The drop has been so dramatic that some suggest that fee rates in Spain are now lower than they were seven years ago. However, others point out that the fall has not been caused solely by global law firm outsiders, but that domestic Spanish firms are also guilty of low-balling on rates. 'The main problem with prices is with local firms,' maintains Jausas's Agustin Bou. 'The larger firms are making very aggressive offers in the market – cutting prices to really surprising levels. Hourly billing rates have been significantly reduced.'

Indeed, as in Italy, Spain has a history of fixed fee pricing that only in the last decade or so has given way to the more Anglo-Saxon model of hourly rates. Now the Spanish firms say they are keen to revert to tradition and fall back in love with alternative fee structures. 'We are reverting to that, but at very low levels,' says Mr Bou. 'For example, say three years ago a leading firm would have quoted the figure at a factor of 100 for a deal; today it would quote 25-30.'

Others take a more relaxed view of fee rates. 'I believe in economics – I don't believe in conspiracies,' states Pedro Perez-Llorca. 'Fee levels depend purely on supply and demand for our services. Demand for our services increased dramatically between 2005 and 2008 and as a result fees increased. That demand dropped significantly in 2009 to 2010, while the capacity of the firms didn't move much and as a result fees went down. That is the market and you can't blame people for offering lower fees.'

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>
> *Rafael Montejo Pérez*

Nonetheless, plummeting fee rates will have serious impacts on law firm business structures. Not least, say the leading partners, salaries for new recruits have fallen off a cliff, nose diving by at least 20 per cent relative to the peak of the economic boom in 2007.

And partners, too, are feeling the pain as fee undercutting is hitting law firm profitability hard. The Spanish legal market is very opaque, so it is difficult to get a firm grip on profit-per-equity-partner figures, but market rumours suggest that margins at some Madrid partnerships are 40 per cent down relative to three years ago.

Regardless of how well Iberian law firms are keeping up their revenues, such a level of profit pinch is going to hurt.