

BALTIC BUSINESS LAW CONFERENCE 2010

Practical interactive insights:
recent market shifts

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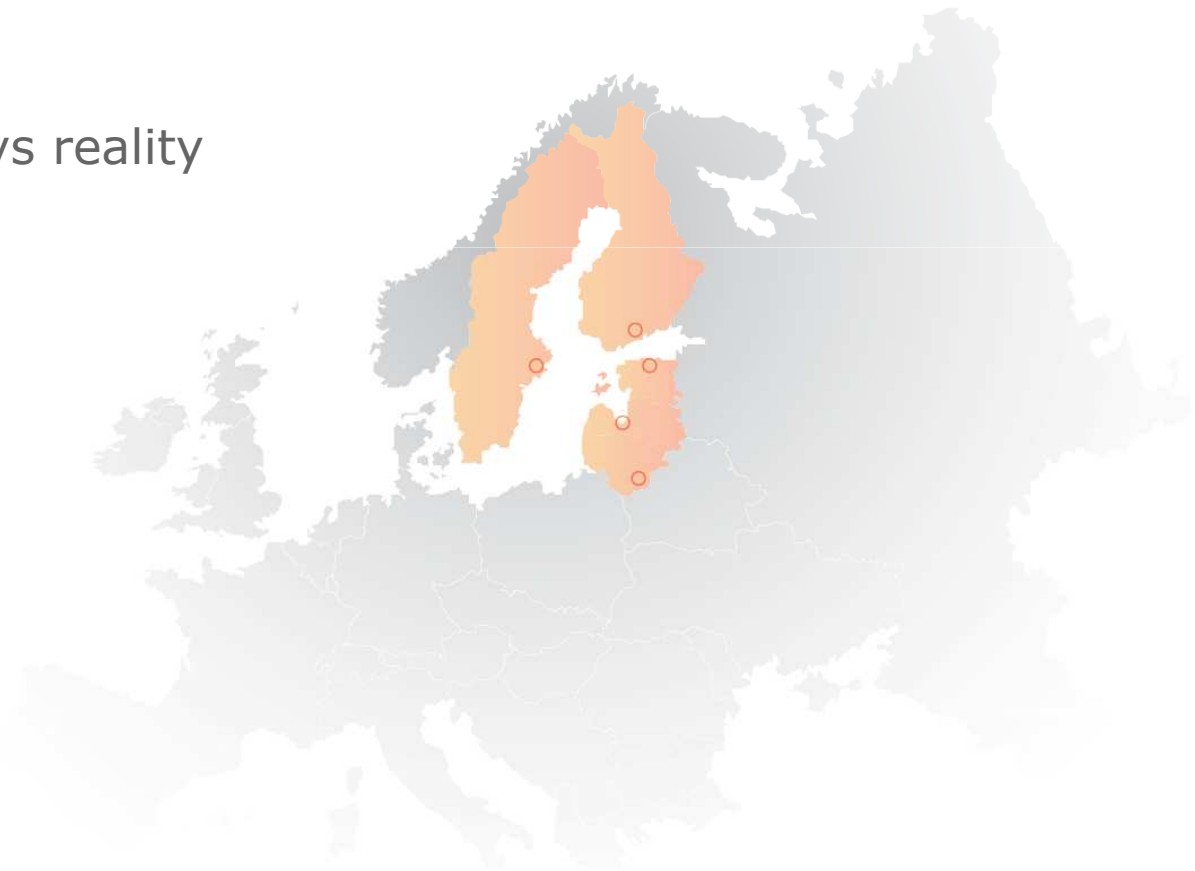
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1. Prior expectations vs reality
2. Impact of the crisis on the legal profession
3. Response of the legal profession to the crisis



Prior expectations vs reality



Expectations

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ESTONIA

Estonian prime minister assured in his Christmas address 2008 -
Estonia will not be hit by the global financial crisis

Expectations

LATVIA – DENIAL AND RECKONING

- **Prime minister Godmanis in:**

- February 2008

**“I am sure the situation will improve after this summer. Don’t panic!
Don’t panic!”**

- June 2008

“Well, how do you define ‘crisis’?”

- February 2009

“We are in hell.”

Expectations

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LITHUANIA

- Geographical midpoint of Europe, but small and remote financial market, therefore expected to avoid any significant damages;
- At the end of 2008 forecasts for 2009: - 4.8 % GDP;
- Former Prime Minister Gediminas Kirkilas (April 2008):

“There definitely will not be an economic downturn in Lithuania”

“There is currently no risk of crisis in Lithuania”.

Reality

LATVIA

- ≡ general government deficit in 2009: 9.0%
- ≡ IMF-led bail-out worth 7.5 bn EUR between 2008 and 2011
- ≡ long-term currency-denominated bonds downgraded to junk; current ratings and outlook – Fitch: BB+, negative; Moody's: Baa3, stable; S&P's: BB, stable; R&I: BB+, negative
- ≡ real wage fall in 2009: 10.8%
- ≡ euro-peg maintained
- ≡ largest domestic lender nationalised
- ≡ "Swedish banks" remained committed to the Latvian market
- ≡ output in catering, construction and retail fell by almost a third in 2009

	2008	2009
GDP fall	10.3%	16.9%
Inflation	15.4%	3.5%
Unemployment	9.9%	19.7%
Current account (% of GDP)	8.3% deficit	8.8% surplus

Reality

ESTONIA

business sector prepared for the worst (bankruptcies, unemployment, etc.),

ACTUALLY:

- financial crisis was avoided largely because Scandinavian parent banks supported their Baltic subsidiaries, but lending became to standstill
- real crisis in real estate market and construction
- number of bankruptcies increased, but no major bankruptcies
- GDP: - 14 %
- consumer spending: - 25%
- unemployment: 14%
- export: - 20%
- import: - 30%
- average salary: - 5.2% (still decreasing in 2010 by another 5.3%)
- decisive cuts in public spending kept Estonian budget deficit at 1.7%, virtually no debt, Maastricht criteria fulfilled – Euro in sight

LITHUANIA

- ≡ collapse of stock markets: Vilnius OMX market capitalisation declined by 62.16 % compared to the end of 2007
- ≡ downfall of real estate market: 1) construction companies restructured and bankrupted; 2) chain of defaults in all related sectors; 3) sharp decline in prices of realty
- ≡ decline in foreign investments: FDI level fell from LTL 35,5 billion in 2008 down to LTL 31,59 billion (11 % decline during a year)
- ≡ employment crisis: 1) number of registered bankruptcies rose by 15 times (from 117 in 2007 up to 1736 in 2009); 2) unemployment levels rose to 5,8 % in 2008 and doubled in 2009, reaching a 13,7 % high
- ≡ decline of GDP: during HY1 2009 GDP fell by 18,1 % compared to HY1 2008;
- ≡ political reaction: “one-night reform”

LITHUANIA (2) - RECOVERY

- ≡ safer than neighbours (?): recession was shorter in Lithuania compared to Latvia and Estonia.
- ≡ monetary stability: no devaluation of Lithuanian Litas.
- ≡ trust of investors restored: in January 2010 the Lithuanian Government raised USD 2 billion in international markets.
- ≡ returning foreign investments: a) FDI on 1 January 2010 amounted LTL 33,28 billion (increase by 5,3% compared to 1 January 2009); b) real case - Barclays Bank, which established its IT support centre in Vilnius.
- ≡ unemployment stabilized: 20 % less unemployed persons were registered in March 2010 compared to March 2009.

LITHUANIA (3) – FUTURE PROSPECTS

- ≡ unibet: bookmakers predict Lithuanian BVP rather rising than falling.
- ≡ World Bank: 1) Lithuania this year to be the third according to the economic growth among the new EU members; 2) predicted GDP growth of 1,6% (2010) and 3,2% (2011).
- ≡ Ministry of Finance of Lithuania: GDP growth in 2010 + 1,6%, 2011 + 3,2%, in 2012 + 1,2%, unemployment rate in 2010 – 13,6 %, 2011 – 15,5 %, in 2012 – 14,7 %.
- ≡ commercial banks forecasts: GDP from - 3 % to + 8 %.

Impact of the crisis on the legal profession



LITHUANIA

- ≡ industry has contracted, although in 2009 RLN Vilnius revenue grew by 6,84 % (compared to “two-digit” growth in earlier years)
- ≡ no lay-offs, streamlining /replacement of personnel, no salary cuts
- ≡ price competition; new pan-Baltic players, no market is reserved for “Big Five” firms in the Baltics
- ≡ in 2009 more work in dispute resolution, bankruptcy and corporate restructuring, less work in transactions and financing, real estate
- ≡ in 2010 transactions returning: Linas Agro IPO (LTL 100 million), Neste’s acquisition, Lifosa buy-out by Eurochem, shipyard sale, wind energy sector consolidation, retail markets consolidation etc.
- ≡ less foreign clients, more local clients. In 2010 foreign/local client ratio is improving
- ≡ state is emerging as a client: new energy, infrastructure projects; liberalization of different markets under EU law
- ≡ innovative pricing. Success fees, discretionary fees

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- ≡ very little M&A, real estate and other transactional activity
- ≡ sharp increase in litigation, insolvency and restructuring work
- ≡ pressure on fees (reduction by 15–20%); strong client insistence on caps, success fees and other alternative arrangements
- ≡ tender bids of some suggestive of desperation
- ≡ more legal work done in-house
- ≡ increased use of results-based remuneration at law firms
- ≡ substantial increase in tax burden
- ≡ calls for reduced number of admissions to the bar

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- ≡ deals by volume/value: – 10%

(investor confidence: public takeover: TeliaSonera on Estonian Telecom and Autoliv on Norma, M&A: Ericsson acquired Elcoteq, local consortium acquired Loksa Shipyard, currently pending IPO: Premia, Eesti Energia)

- ≡ less deals – less work, but number of litigation increased by some 25%
- ≡ more specialist (senior/partner) advice requested
- ≡ no structural changes – no major lay-offs, but severe cost cutting
- ≡ pressure on fees (in combination with "less transactions – less work") – decreased turnover by 10-15% (but severe cost cutting has "saved" the profits of law firms?)
- ≡ increased competition – everything is subject to tender

Response of the legal profession to the crisis



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- ≡ increased focus on added value; more 'black or white' advice, less 'shades of gray' discourse
- ≡ emphasis on senior specialists with experience and ability to handle projects
- ≡ some junior staff has become redundant
- ≡ increased value of specialization: limits of price competition exhausted, focused knowledge and experience is what will give competitive advantage
- ≡ less pickiness about the types of assignments one accepts
- ≡ cost-cutting
- ≡ more active and better-targeted marketing
- ≡ expectation that 'leaner operations' will give competitive advantage in a resuming market

LITHUANIA

- ≡ structural changes (e.g. mergers) may be expected in Lithuania and throughout the Baltics;
- ≡ large firms will try to ring fence certain markets (large transactions, restructurings, IPO, energy etc.);
- ≡ billing based on value not on time spent;
- ≡ fee levels will not recover until 2011.

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- ≡ increased efficiency – less resources, standard services, packages
- ≡ increased marketing efforts
- ≡ new pricing models – packages, contingent fees, risk sharing arrangements, etc.
- ≡ EXPECTATION - to reach 2007 levels in 2011

THANK YOU!

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