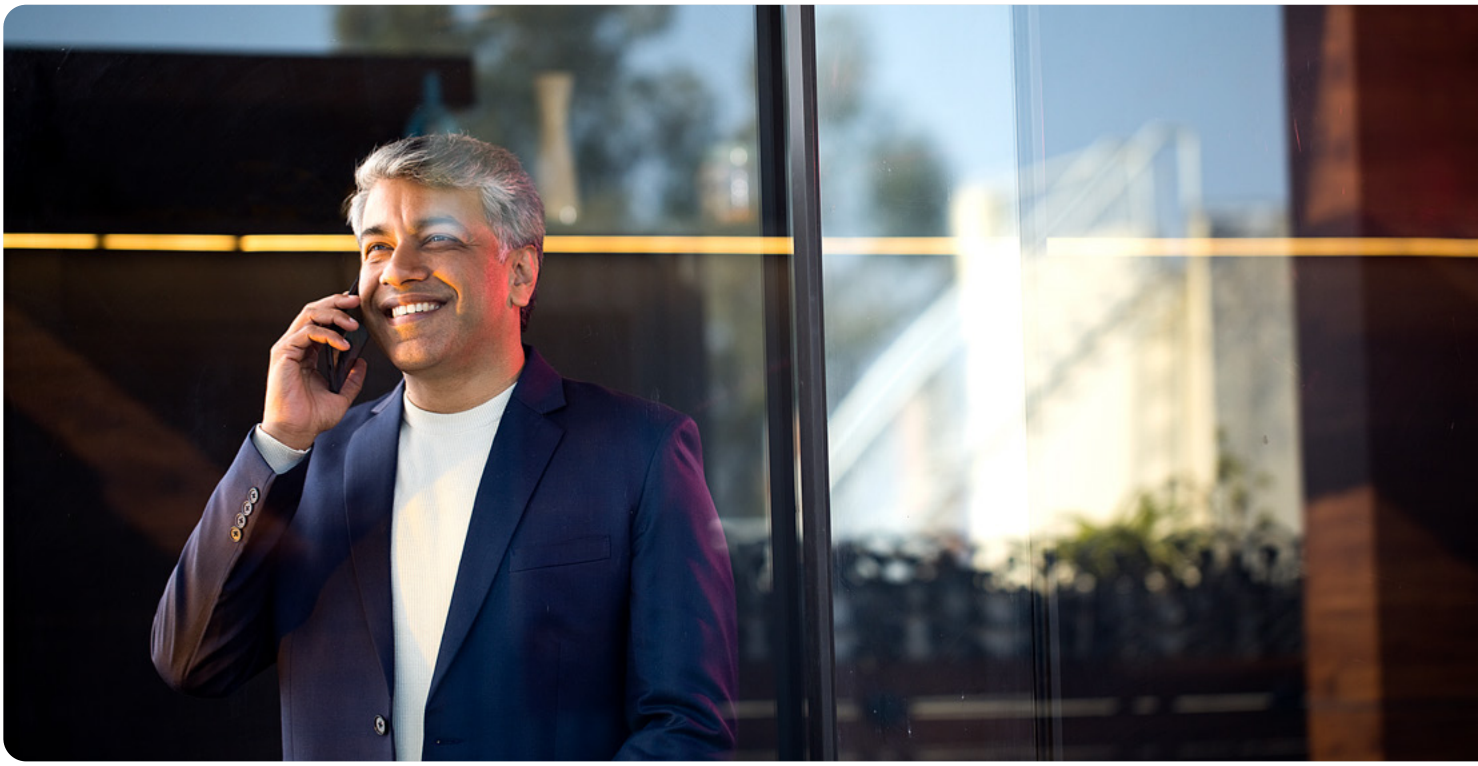
more than money

NAB Professional Services

The Performance Era

How Professional Services are Reimagining Best in Class Business Management

Introduction



In a fluctuating economy, ensuring you are at the top of your game is critical. But that's not easy when the parameters of work are fundamentally shifting. NAB's Professional Services white paper looks at what top firms are doing to stay ahead.

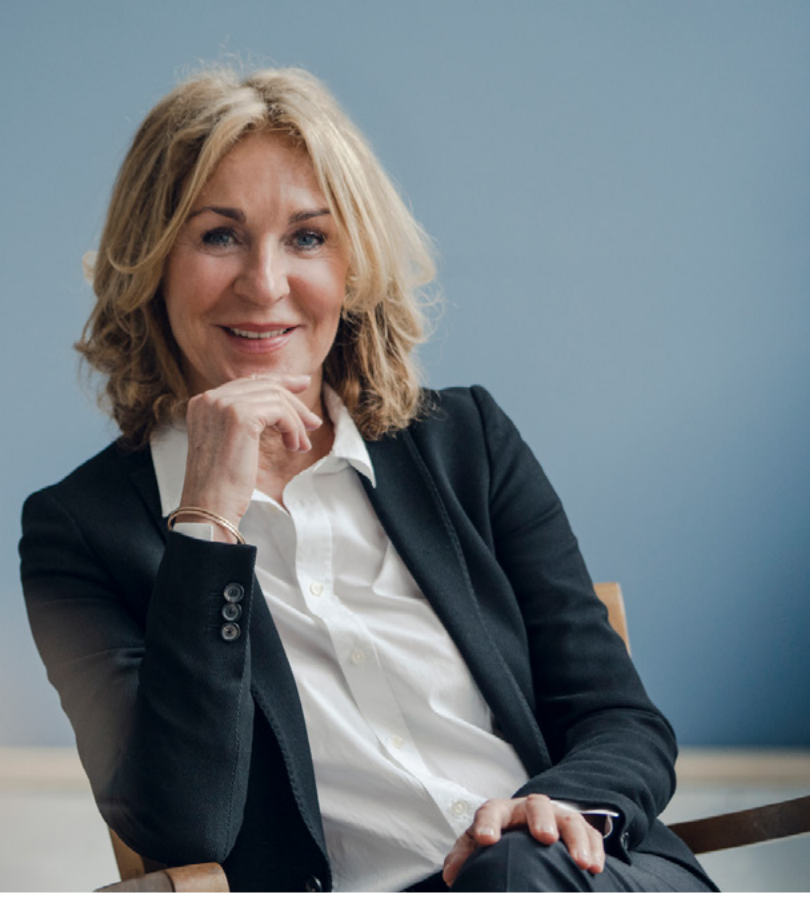
Professional services firms have remained remarkably resilient over the past few years, often enjoying strong growth despite an unpredictable economy, with many expanding their business offering.

And there are signs that this expansion is working. According to The Australian Financial Review's latest Top 100 Accounting Firms list, revenue of mid-tier firms is up 17 per cent. Meanwhile, four in five Australian law firms are reporting profit margins of more than 10 per cent – compared to just over half the industry in 2019, a national survey of Australia's legal industry shows.

There's good news in insurance broking too. The latest figures show industry revenue on track to grow at an annualised 7.7 per cent over the five years to 2023-24, with a 5.4 per cent lift expected this year.

So what are the country's most successful firms doing right? What does 'performing at the top of your game' even mean today?

In our white paper, NAB senior executives and some of their most successful customers discuss what best practice looks like.



01

In pursuit of profitability

Profitability is about being as dynamic as possible.

It's about actively protecting and growing your customer base, but it's also about going the extra mile to get your pricing, costs and debtor management right. Above all, it's about ensuring your cash flow runs as seamlessly as possible, so you have the resources to support new ideas and growth.

Managing your No.1 cost (and asset): staff

It's hard to get away from the high price of doing business these days, and there's no doubt it weighs on firms' profitability. It's not surprising then that staffing costs are a key focus for professional services firms – intensified by the scarcity of ready labour.

> "In Australia, the war for talent is in full swing and we have heard countless stories of firms training up staff – that is, two to five years post-admission – only for them to move for a material uplift in remuneration."
>
> **Courtney Worrall**
> NAB Professional Services Banking Executive

Take law firms. An exodus of lawyers to the UK and US of recent years saw a steep rise in salaries – up to 20 per cent for juniors in 2021 and 2022, according to recruiting firm Mahlab.

It's a problem for insurance brokers too. The tight labour market here has been compounded by the 'ageing' of the industry, with young people few and far between.

And the issue is particularly acute for accounting firms. The ABS has forecast that Australia will require 338,362 accountants by 2026 – almost 10,000 extra a year.

It doesn't help salary levels, but it also doesn't help the quality of people firms are able to attract – something that goes to the very core of your profitability.

"Staff retention and avoiding the costs of attrition have become imperative for businesses," NAB Professional Services Banking Executive Courtney Worrall says. "Not only due to replacement costs, but also due to business continuity in the trusted adviser workplace of our professional services industries."

So, what to do?

It doesn't just have to be about higher salaries. Firms are finding alternative ways to attract desirable staff through work from home policies and additional annual leave. Some are also going to great lengths to make the work environment more attractive to engage employees and encourage them back into the office.

Others, such as accounting firm PKF, are helping staff to envision their career pathway. "In the last few years, we've completely overhauled our entire process, from early education for relatively junior staff all the way through to our final course that's a path into our partnership," PKF Melbourne Managing Partner Timothy Bow says.

The opportunities and challenges of offshoring

Another way to keep staff costs down – and also address the general talent shortage – is to consider where overseas workers could fit into your front- and back-office needs.

"There are some great offshore talent and services available to complement professional services businesses," says NAB Professional Services Banking Executive, Queensland, Donna Kosiek. "Access to them can create differences in terms of one firm's ability to price versus another, particularly when work goes to tender."

But while many professional services firms are gaining a distinct competitive edge by leaning into offshoring, doing so does have its drawbacks.

As accounting firm PKF realised, it can ultimately undermine your own talent pool. "We experienced exactly that outcome a few years ago," PKF's Bow says. "The self-managed superannuation area lent itself very well to offshoring as it's a contained unit and a very specific skill set. But if you invest in an offshoring setup, what you're effectively doing is foregoing the fundamental training for your staff coming through.

"You've almost got to make a conscious decision to say, if I'm going to give that work up, then I can't expect in three or four years' time to have more senior people experienced in that area."

PKF ended up pulling back as a result – but not entirely. "It's a very delicate balance," Bow acknowledges.

At the end of the day, offshoring is particularly problematic for smaller firms, NAB's Kosiek points out. "They are the ones that will potentially miss out as they don't have the scale to engage an offshore partner."

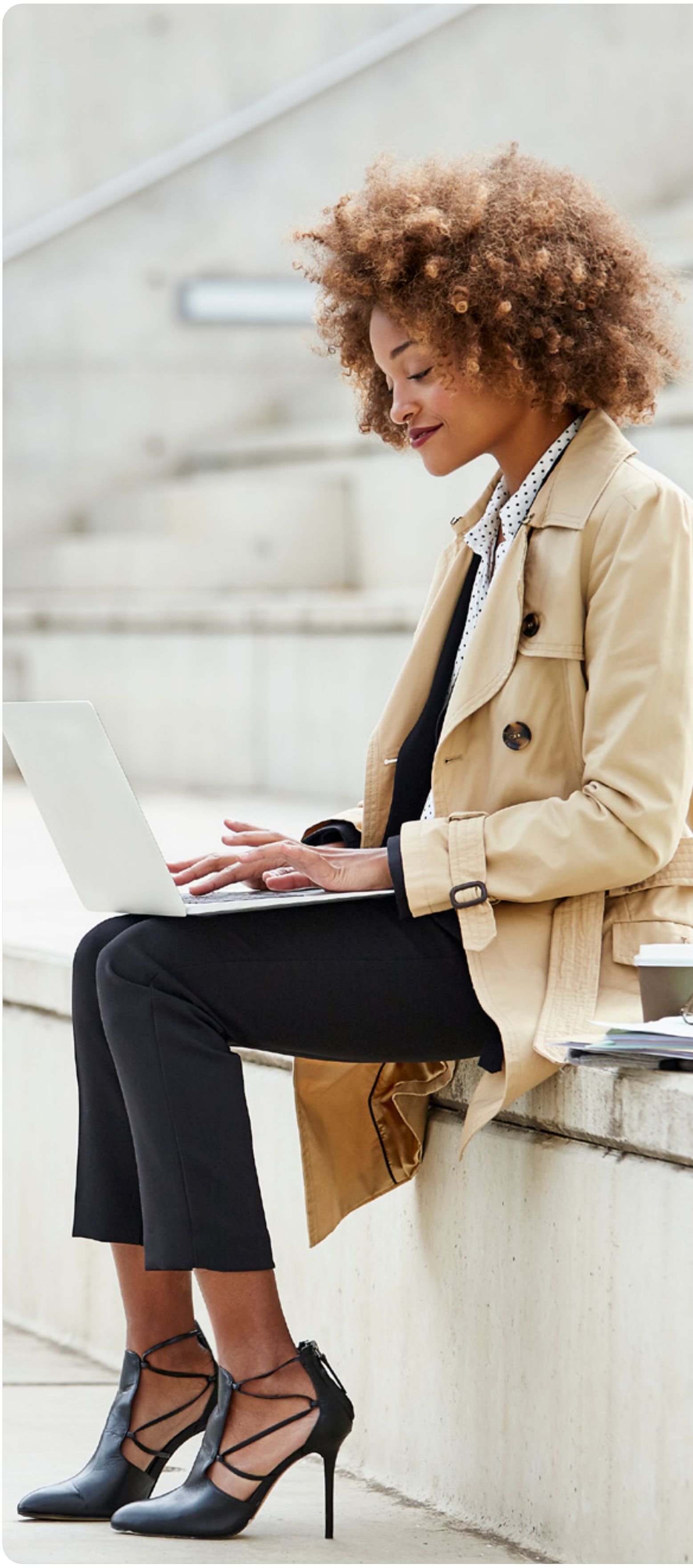
It's all the more reason for them to keep their costs under control elsewhere and to lean into their more personalised service. "If you can't win on costs then differentiation becomes paramount; for example, through niche offerings or customised services," Kosiek says.

Better billing

Profitability also lies in the everyday basics, such as billing.

The issue of billing by the hour or setting a fixed fee has been topical for many years. But in the face of high inflation, it's an issue that's becoming ever more fraught. While clients may understand why your hourly rate may need to rise, value-based billing has the added advantage of giving clients much-needed certainty.

It could well be time to weigh up the relative benefits again. Keep in mind that almost a quarter of law firm respondents told the 2023 New Law CLE Australian Legal Industry Report that they had made more than 90 per cent of their revenue from fixed-fee matters – up from 18 per cent in 2022. Meanwhile, 53 per cent believe fixed pricing increases client retention.



Keeping the cash flowing

Debtor management is another big issue for professional services firms, where there is a culture of accepting long-dated cash lock-up in work in progress and invoice management. Unfortunately, smaller firms are the most vulnerable here.

One solution is upfront payment. While this can be problematic with long-term clients, and something you wish to avoid, it pays to take a different approach with newer customers.

"While stricter debtor management may prove a more confronting conversation with long-term clients, ensuring that all new-to-firm clients are aware of the payment policies is critical," NAB's Worrall says.

Meanwhile, if you're not receiving cash in advance, "it's vital you control your work in progress, debtors and lock-up days – the number of days you aren't being paid for the work you produce," according to NAB's Kosiek.

It's also important to give clients options when it comes to payment. Pay by web, for example, is one solution that can help firms get their money faster, Worrall says.

Ready for growth

Sometimes the answer to profitability goes back to the very basics.

Worrall underlines the power of keeping your financial house in order so you're ready to move at a moment's notice – something that is critical in today's challenging environment.

"Our bankers are having daily discussions with firms looking at acquisition, succession or working capital finance," Worrall explains. "Those firms who have their financial house in order can move more swiftly, and with more certainty, on major decisions – which is particularly relevant in a competitive mergers and acquisitions market."

Yet the practice is not as commonplace as you might think.

"You'd be shocked to know how many professional services firms are out there that don't have their financial information updated, forecasts planned or partnership agreements formalised," Worrall says. "These all become important when you are ready to move on an opportunity to grow – both for your planning and for your bank."

The headlines

- Look for new business in upcoming areas
- Keep the cash flowing by controlling your work in progress, debtors and lock-up days
- Keep costs to a minimum by offshoring – but take care

02 Innovation 101

Beyond everyday concerns, it's important to keep an eye on the bigger picture. Innovation is key here.

Embracing technology

The world has seen an explosion in generative AI and it's an area where many professional services firms are already seeing dividends.

"AI is set to infiltrate so much of our society, home, education and workplaces," NAB's Kosiek says. "The big corporates are investing here and we are seeing more customers on the front foot to ensure their businesses aren't left behind."

National risk adviser McLardy McShane is planning to implement AI over the next 12 months, for the sake of efficiency above all. But the firm will do so cautiously – with good reason.

Its COO, Meg Long, attended a conference earlier in the year where it became clear that many US and European companies had jumped in too early. "I think there's been a lot of businesses that have been quick to implement AI but are now potentially worried about how they control it and the parameters that they probably should have pre-installed before putting it into their business," she says.

This will be the biggest focus for McLardy McShane. "Ultimately, we've just got to treat it like another member of staff," Long says. "It's got to be monitored, compliant and managed to ensure it doesn't cause us any potential exposures."

Business reimagined

Some professional services firms are thinking outside the box when it comes to the services they offer. Accounting firm PKF is one such example.

"Clients want help not just getting a bunch of numbers on a tax return but understanding the metrics in their business and how it helps them grow," PKF Melbourne Managing Partner Timothy Bow says.

For PKF, that means moving into new areas such as cyber risk and ESG. "We're hiring data scientists, climate engineers – areas that are so far removed from an accountant," Bow says. "They bring with them innovation from their fields that we pick up on."

Long-term, it involves seeking out tactical joint ventures or even mergers. "We're looking at, say, an ESG advisory firm that's similar in scale to us, playing in a similar market, that's attracting similar clients," Bow says. The firm can offer PKF its expertise and PKF, in turn, can offer the firm access to its extensive client database.

Expanding your business

Marketing is another area where firms are embracing technology.

One family law firm customer, for instance, has expanded throughout regional Australia off the back of a successful digital marketing strategy. It's now set up offices in numerous locations, and NAB's Kosiek is adamant it couldn't have done so without the help of technology. "It gave them the chance to penetrate markets where they believed they were going to see more opportunity," she says.

The outcome is a win-win for the firm and prospective customers across rural and regional Australia, Kosiek explains. "By setting up an office in Alice Springs, for example, they've given a lot of rural clients access to an even wider range of family law legal professionals."

Doing marketing well

More and more law firms are embracing marketing beyond personal injury work. The New Law report found that, in terms of investment priorities for smaller firms, 50 per cent said that marketing is top of their list.

But it has to be done carefully, NAB's Worrall says. "You need to track whether you're getting a return on your investment."

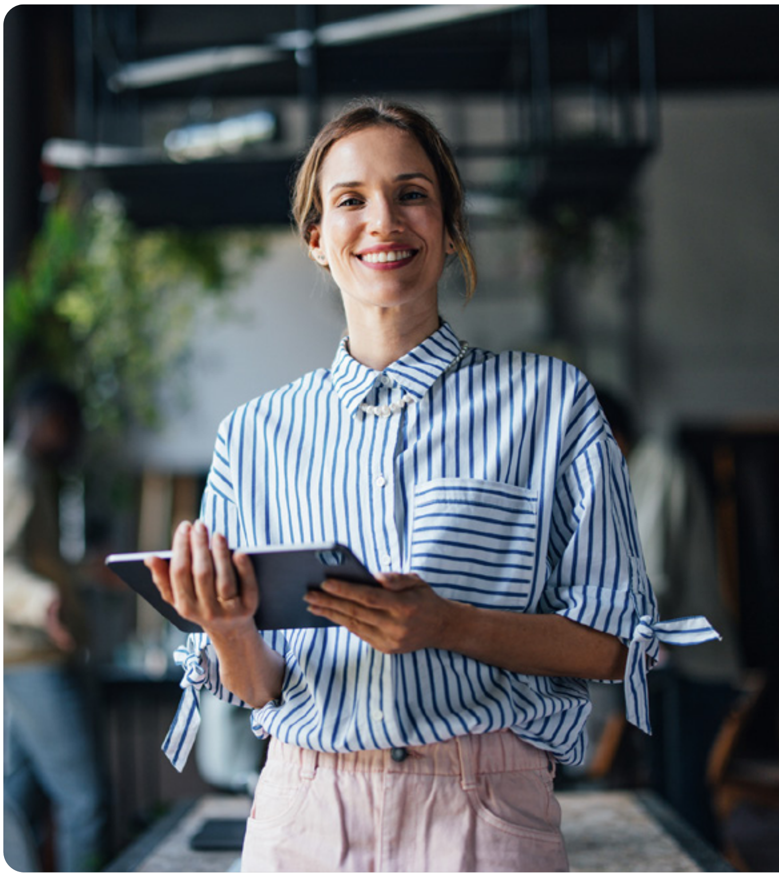
For instance, if your firm has been preparing a newsletter for a number of years, "have you assessed the analytics around click-through rates and how a type of communication either increases client engagement or referral business?" Worrall asks.

It's also important to consider how clients today want to be communicated with – and how often.

"Regular communication with clients remains critical across all professional services sectors, but understanding how your clients want you to communicate with them is best practice," Worrall says.

The headlines

- When it comes to marketing, track whether you're getting a return on your investment
- Ensure your staff are subject matter experts and one step ahead of knowing your clients' needs
- AI needs to be fit for purpose – and compliant!



Staff are still your key strength

While innovation is important, don't forget the basics for growing your business, Worrall says.

"Ensure those staff who are subject-matter experts are out in the market meeting clients. Ensure they can fully articulate the firm's value proposition and why potential clients should choose their firm."

A large part of risk adviser McLardy McShane's success is in ensuring it has the specialised staff to deal with emerging risks.

"Evolving risk is a tricky topic for our industry because we've got to be teaching ourselves at the same time as going out and trying to explain to the client why they might need a certain product," McLardy McShane's Long says.

To do this, staff need to know what clients are thinking at any given time. For example, the 2024 Vero SME Insurance Index found 83 per cent of businesses are considering changes to their insurance. That means your broking team must be able to articulate why insurance is needed more than ever.

"It's about making sure we've got a well of knowledge to meet any of our particular clients' demands throughout the year – a thesaurus of risk advisers as it were," Long says.

03

Managing your risks

Protecting your firm is far more nuanced than simply having the right insurance in place – but it definitely helps.

Australia's professional services firms are more aware than ever of 'black swan' events, whether that's fires, floods, cyber attacks or something else again. And they're certainly more cognisant of managing risk – whatever forms it takes, says NAB's Worrall.

So, what are our high-growth clients doing about it?

First and foremost, they're ensuring they have their financial reporting and binding agreements up to date. As Worrall notes, "The basics that are critical for all businesses are critical for the accounting, legal and insurance broking sectors and it's our market-leading clients who are pursuing best practice here."

It's not simply a matter of having the relevant insurance policy to hand. They're also ensuring they have robust shareholder or partnership agreements in place which capture valuation methodologies to assist with partner or director entry or exit.

And in the meantime, they're pursuing best practice when it comes to preparing their people for risks – whether that's their managers, staff, or even their contractors or suppliers – so they're ready for whatever comes their way.

Not surprisingly, risk is a huge issue for risk adviser McLardy McShane, and one the business manages proactively.

However, as McLardy McShane's Long says, the biggest risk from a personnel perspective is professional indemnity exposure – people providing the wrong advice or policy.

The answer? "Training, training, training," according to Long.

> "The basics that are critical for all businesses are critical for the accounting, legal and insurance broking sectors. That includes having up-to-date, accessible and well-structured accounts."
>
> **Courtney Worrall**
> NAB Professional Services Banking Executive

Putting a succession plan in place

Often a business can be undone by the most foreseeable of events: the founders' eventual departure. And yet it's an issue that's overlooked time and again.

That's particularly problematic just now, NAB's Kosiek says, given Australia currently faces the largest ever intergenerational transfer of wealth. This makes it even more imperative that owners and partners have a robust succession plan in place – before it becomes too late.

"The fact is, a lot of baby boomers and early Gen X are looking to exit, made more urgent by the fact many delayed during COVID," Kosiek says. That means selling up and moving on won't be necessarily as smooth as you would wish.

It makes the creation of fail-proof agreements essential, Kosiek says. But it's also incumbent upon management to prepare the next generation – so they're ready to step up when the time comes.

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>
> **Donna Kosiek**
> NAB Professional Services Banking Executive, QLD

Of course, you need that next generation in the first place – something McLardy McShane has focused on. Of the 11 national heads who now help COO Long run the business, all but two are in their early thirties. That's been a conscious decision, Long says. "We've really concentrated on building a platform of highly skilled people to take us into the future."

When your practice is too expensive to sell…

There are other barriers to exiting your firm. A particular challenge for professional services firms is the high price of their shares post-COVID, which can deter prospective buyers.

"The succession plans for talented staff to become owners are currently inhibited due to the high cost per share," Kosiek says. "They're effectively priced out of the market."

Sources of funding can help, but the cost of buying into a firm these days means a bank loan can only take you so far. This sometimes means partners must adjust their exit timelines and have a more stepped approach to realising their equity sale.

> "We've really concentrated on building a platform of highly skilled people to take us into the future."
>
> **Meg Long**
> McLardy McShane COO

This is not without its issues. If owners are moving to shareholders, they will expect the business to maintain its current value or better – something that may not necessarily eventuate. The upside, though, is the slower 'step out' can be appealing for the incoming generation as they can more readily transition the client relationships and business for continuity.

One potential option that Kosiek has observed is the restructuring of a firm's finances. "Recently, we have seen some firms restructuring their funding arrangements, reducing the value per share and potentially making buy-in more achievable."

This comes with its own challenges and risks, though, and should be pursued with sound independent accounting and tax advice.

In conclusion

There's no doubt the past few years have been challenging for professional services firms, even as they've embraced a vast array of new opportunities. But when we look at the success of many of NAB's most profitable clients, it's clear that a commitment to strategy is everything.

Whether it's finding time and space for continued innovation or keeping the basics bubbling along – their people in regular training or their work in progress under strict control – they are always one step ahead of the pack. And, clearly, it all pays.

The headlines

- Training up your staff is key to risk management
- Maintain up-to-date financial reporting and forecasts for your business
- A comprehensive and transparent exit strategy is critical in succession planning

To find out more, talk to your dedicated NAB Professional Services Banker or visit

nab.com.au/professionalservices