

**International Academy of Business and
Public Administration Disciplines
Dallas, Texas, April 7-11, 2011**

**WHAT LESSONS CAN WE LEARN FROM THE
PRESENT ECONOMIC CRISIS FOR THE
POSSIBLE FUTURE STRATEGIES OF ENTERPRISES
- LESSONS FROM HUNGARY AND SLOVAKIA¹**

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ABSTRACT

The paper explores the characteristics of the present economic crisis at enterprise level and its consequences for possible growth after the crisis. The study builds on international experiences concerning recovery from crisis during the previous economic downturns between 1980 and 2002.

Survey results in Hungary and Slovakia are presented with special attention to how companies tried to react to the present economic recession. The study analyses the possible consequences of the strategies followed by the Slovakian and Hungarian firms during the crisis period from the point of view of capabilities for utilizing the options for growth when demand will start to increase.

INTRODUCTION

The present worldwide economic crisis has drastical consequences for most of the economies in the world. Cross-border business and international trade declined in 2009 by about 9%, and foreign direct investment dropped by more than 40% in the same year (Ghemawat, 2010, p. 56). While the leading nations of the world economy were phased with recession, countries like China and India have progressed further on their growth path. China realized 66% of global growth in GDP, and India 11% in 2009 (Ghemawat, 2010, p. 56). The projected high growth rate of the BRIC² countries will lead to radical restructuring in the world economy where North America and Europe will lose its previous political and economic influence. According to the Goldaman Sachs forecast, „by 2020 the BRICs will account for a third of the global economy and contribute about 49,0% of global GDP growth” (BRICS Monthly, May 20, 2010).

The crisis has influenced enormously the transforming Central and Eastern European economies as well. Some of these countries like Hungary, Romania and Bulgaria had serious difficulties due to macroeconomic imbalance and increasing inflation (Muraközy, 2010). These countries were not prepared for the consequences of the rapidly spreading crisis, and –

¹ The participation in the conference is supported by TÁMOP-4.2.1/B-09/01/KMR-2010-0005

² Brazil, Russia, India and China

contributing to the difficulties – seriously underestimated the possible extent of the crisis. In Hungary for example the official opinion of the Hungarian National Bank in early October 2008 was that the crisis will not have relevant consequences for the economy. Two months later the National Bank and the Hungarian Government started intensive work on preparing a plan to prevent the Hungarian economy from collapse. The financial aid of the IMF was necessary for the survival of Hungary in 2009 and 2010.

As we arrive closer and closer to the end of the crisis period, the really interesting strategic question is what will be happening after the crisis. Whether will the development path repeat the tendencies followed before the crisis, or totally new directions of development will emerge. We have rather limited research evidence to answer properly this question. Scholars try to get answers by studying the consequences of the previous crisis periods (Gulati, Nohria and Wohlgezogen, 2010). But the present crisis is unique in its nature, expansion and rather accelerated spread all over the world.

The present paper tries to analyse the above issue from a company angle. We are interested in learning what has happened during the crisis, what were the reactions of companies to the emerging new economic, technological and social conditions, and what tendencies of development may be identified at the present stage of the crisis. The author has been involved in studies at the above areas for some years and has conducted empirical studies in Hungary and the Slovak Republic. The empirical background of the paper includes analysis of publications of researchers engaged in doing surveys in the field (e.g. Ringland, Sparrow and Lusteig, 2000; Waldman, 2010), as well as primary data collections through questionnaire surveys and interviews conducted in Hungary and the Slovak Republic.

MACROECONOMIC BACKGROUND

Hungary and Slovakia has a lot of similarities concerning the social, economic and political heritage dating back to the period before the political changes around 1990 (Kiezun, 1991). But behind these similarities there are interesting alterations in the patterns of development, especially after 1990 (Balaton, 2007).

Hungary was rather successful in hosting relatively large volume of foreign direct investments (FDI) during the first half of the 1990s. The Hungarian Government decided to adapt the sales type of privatisation. It meant that state owned firms were offered for sales for those who could offer acceptable prices for the companies. As capital inside the country was rather limited, that type of privatisation resulted in the overwhelming role of foreign investors in the ownership structure of enterprises located in Hungary by the end of the century. The accumulated high debt at the time of the political turnaround urged for the sales type of privatisation and it was the only possibility to pay back the loans from the income of privatisation.

Slovakia (and until January 1993 Czechoslovakia) followed different economic policy concerning privatisation. Vouchers were distributed among the population and these vouchers could be changed into shares of state owned enterprises. The shares than were purchased by investment funds owned by state owned banks. So the privatisation had resulted in restored state ownership of enterprises by the mid 1990s. No relevant structural changes were implemented during the first half of the 1990s (Clark and Soulsby, 1999). This policy had temporary macroeconomic advantages compared to Hungary. While in Hungary the restructuring was relatively accelerated it resulted in high level of inflation (about 39% in 1993), great depression (38% GDP decline between 1989 and 1993 measured by comparable prices, and about 17% unemployment rate) (Kornai, 1993), in the Czech Republic and Slovakia there were no such radical consequences. Economic restructuring had taken a major step in Slovakia after the involvement of foreign direct investors during the second half of the

1990s. The necessary restructuring resulted in economic slow-down, inflation and increasing unemployment as well, but these consequences were moderate in their extent compared to that of Hungary.

Slovakia was rather successful since the second half of the 1990s in inviting foreign direct investors especially in the motorcar industry. This fact has contributed to the relatively fast growth rate of the Slovak Republic around the turn of the century and helped the integration of Slovakia into the European Union. The growth rate of the country has even accelerated after the integration and it has resulted in the capability to change to the Euro as the national currency in 2009.

In the same period Hungary became less attractive for foreign investors, partially due to high tax rates and increasing level of macroeconomic instability and forecastability, parallel with rapidly spreading corruption. During the period between 2002 and 2010 the economic stability of Hungary has eroded and the country became incapable of introducing the Euro. State expenditures had exceeded the level of incomes and the country was near to bankruptcy during the summer of 2010. The newly elected Government has introduced radical measures to restore the balance and the first results of it may be observed at the beginning of 2011.

PREVIOUS RESEARCH EVIDENCE ON STRATEGIC CONSEQUENCES OF THE CRISIS AT ENTERPRISE LEVEL

The start of the present economic crisis has been marked by filing for Chapter 11 bankruptcy protection by Lehman Brothers on September 15, 2008. Within six months the crisis has spread throughout the world and endangered many previously successful economies like Ireland. Even economically stable economies like the US, Germany and France were hit seriously and the consequences will influence the coming years in nearly all countries of the world.

As the crisis today is becoming closer to its end, more and more scholars are interested in discovering what will happen after the crisis. Harvard Business Review has published a series of three papers in the March 2010 issue, dealing with „Strategy in a Weak Recovery”. The articles signed by influential authors like Pankaj Ghemawat, Ranjay Gulati, Nitin Nohria and others agree that rather limited research evidence is available in the field and they tried to get ideas by studying the experiences of the previous crises since 1980. Although the authors admit that the previous crises were much more limited in their expansion and were also different in their origin and nature, they have arrived some conclusions worth of having in mind when thinking on possible future enterprise strategies after the present economic crisis. One of the important conclusions drawn by Gulati, Nohria and Wohlgezogen (2010) is that concentration only on cost-cutting during the crisis will hardly lead to successful expansion after the crisis (Gulati et al., 2010. p. 65). The authors have found that emphasis on operational efficiency parallel with concentration on market development and asset investment have resulted in the best results measured by increase in sales income and EBITDA (Gulati et al., 2010. p. 67). Mere concentration on reduction of employment level and cost cutting have not resulted in successful recovery after the crisis.

It is also noteworthy from their studies that concentration only on innovation and asset investment during the crisis was not connected to successful enterprise performance after the crisis. So neither restriction nor mere innovation in itself seemed not to be the proper cure during the economic crises. Parallel efforts of economic stabilization and renewal seems to be the advisable solution based on the examples of the three crisis periods between 1980 and 2002.

In developing such solutions organizations may probably learn useful lessons from the idea of combining exploration with exploitation (March, 1991). It is also a lesson to be learned

in mind that rapid, short term solutions often have disadvantages evaluated by taking into account consequences on the long run (March, 2003). Another framework to discuss the necessary changes during crisis is to get engaged in first-order or second-order changes. Bakacsi argues that „It is the leader’s responsibility to decide whether the system needs first-order or second-order change, and therefore initiate rather double-loop learning, instead of single-loop.” (Bakacsi, 2010, p. 7).

Ghemawat (2010, p. 57) has forecasted the possibly more important role to adapt to local norms and the growing organizational power of the local country. Parallel with increased pressures on pricing, multinationals have to be sensitive to regional varieties of their offering, as local differences will become more important (Ghemawat, 2010, p. 589). These organizational changes will increase diversity within multinational firms, but at the same time create the need for cohesive corporate cultures and tightening talent management practices (Ghemawat, 2010, p. 60).

Rapid development in IT systems have continued even during the crisis. Companies planning their new strategies for the period after the crisis have to bear in mind that their rivals have invested a lot during the last years in technologies and applications, and in order to be able to maintain advantageous competitive position it is necessary to use the opportunities of real-time data and reports, and have ambitious, flexible managers in key positions throughout the organization (Sull, 2010, p.73).

As a consequence of the accelerated changes and turbulence during the last few years some authors speak about the next wave of creative disruption. Waldman in his recent book postulates: „In fact, the growth of the mobile internet, the return of economic growth after 2012, and the constant potential for entrepreneurs to come up with products and services that satisfy fundamental consumer needs are, I believe, going to drive another great wave of creative disruption in the near future. ...I predict that the era of creative disruption has only really just begun.” (Waldman, 2010, p. 46-48).

The radical strategic changes possibly emerging during the coming years will probably have an influence of the organizational structures and processes companies will be adopting. Ringland et al. (2010, pp. 90-92) speak about double-cone organizations where traditional hierarchy dealing with specified and routinized activities will be existing parallel with activities characterized by lack of clarity, ad hoc solutions, private inspiration, and luck. The well-known structures and mechanisms of control systems, governance and asset allocation have to live together with spreading ad hoc mechanisms and organizational structures described as adhocracies (Mintzberg, 1983).

Summarizing the above discussed predictions for the after-crisis situation it may be stated that there seems to be limited possibility for using previously prescribed solutions. Learning, adaptation to emerging new situations and flexibility may be regarded as crucial capabilities organization of the future will need in order to be competitive. Bahrami and Evans have formulated that requirement as follows: „The object of becoming super-flexible is to be able to either intentionally precipitate a transformation, or to make modifications in response to changing situations. Adaptation occurs either during the course of, or after, an unfolding change episode, and may simply be random in that one may be just at the right place at the right time.” (Bahrami and Evans, 2005, p. 22).

RESEARCH METHODS AND SAMPLES

Research methods utilized in both countries included questionnaire surveys. Interviews with top managers, analysis of company documents and case study development were conducted in Slovakia. In Hungary interviews and case study research will be done later this year. In Slovakia both the questionnaire survey, the case studies and the interviews were

conducted by grauating studenst at master level under the supervision of the present author. Findings have been summarized in Master theses defended at Selye János University in years 2009 and 2010. The questionnaire survey included 200 companies in Slovakia. Distribution according to number of employees were as follows: below 10 employees: 34%, between 10 and 49: 39%, between 50 and 99: 14%, between 100 and 249: 13%. 49% of the firms belonged to the service sector, 34% to industry, 4% to agriculture, and 12% to public administration (Muraközy, 2009, pp.: 40-41).

The Hungarian survey was part of a larger research endeavour aiming at studying the competitiveness of Hungarian enterprises. The author was responsible for coordinating the research work related to enterprise strategies. The survey was conducted in Hungary between April and November 2009. The survey collected answeres from 1246 top managers working in 313 enterprises, belonging mainly to the SME sector. Distribution of firms according to number of employees were as follows: 47% of the firms had employees between 50 and 99, 21% below 50, 20% between 100 and 29, and only 2% had more than one thousand employees. Manufacturing industry companies represented 42,4% of the sample. Service firms had a ratio of 23,0%, and trading companies 19,1%. The empirical findigs used in the present paper have been published in the Preliminary Report of the survey (Chikán, Czakó and Zoltayná Paprika, [eds.], 2010).

REACTIONS OF ENTERPRISES TO THE CRISIS IN HUNGARY AND SLOVAKIA

Hungarian experiences

Our empirical evidences from the questionnaire survey in Hungary show that the first – and most frequently observable – reaction of enterprises were to reduce cost levels, to downsize operations and reshape organizational structures towards more simple and less expensive management systems. This is the traditionally observable reacton of companies and this strategy is most frequently adviced for executives by standard textbooks of economics and management. This strategy has resulted in many cases in capabilities to survive the crisis situation and preserve condition for continuing business activities when the crisis would have had its end.

Our sample shows that 34,6% of the companies suffered more than 10% decrease in domestic sales turnover in 2009 compared to the previous year, while 20,3% experince less than 10% decrease. 24,5% of the firms reported stagnation in their comestic sales. 35,9% realized less than 10% growth, and 15,0% managed to increase domestic sales turnover by more than 10%.

In export sales 40,4% of the companies reported more than 10% annual decrease, and 20,2% less than 10% decrease. 18% of the firms in our sample experienced stagnation in exports, and 13,5% managed to realize modest growth bellow 10%, and only 7,9% was cabable to increase export sales by more than 10%.

The crisis resulted in relevant changes in company strategies. While during the previous surveys in 2004, 1999, and 1996 realization of profit was the most important target, in the 2009 survey 170 company (60,3%) gave the answer that surviving the crises was the most important aim, and 123 mentioned profit realization as the no. 1 strategic goal. The most frequently followed strategy was defensive (26% of firms), and shrinking strategy proved to be no. 2 (20% of companies). In 2008 growth oriented strategies were the most frequently observable ones (43%), and defensive strategies were followed by less than 10 % of the firms. In 2009 companies mainly used their resources to defend their existing market positions. The

defensive strategy in many cases was not the consequence of a purposeful strategy, but more as a result of lack of strategy and a situation which might be described as muddling-through.

It was a clear sign of defensive enterprise strategies that R&D was evaluated as the less important functional area within the company. 43% of the firms have not had branded products. The companies in our sample more frequently used the company name as brand name, and only one fifth of the sample firms had independent product brand names. The ratio of companies introducing new products and technologies has decreased compared to the previous survey in 2004. Companies generally complained that they got limited state support for innovation and lack of adequate financial resources was mentioned as a major reason behind the limited innovation. The importance of organization development was also under-evaluated by the responding managers. Modernization of organizational and management structures got rather limited importance among the priorities of top managers.

The overall picture observable in the survey of 2009 shows a rather defensive management approach where companies concentrate only on survival. They generally did not have strategies concerning how to start development, had rather restricted information on their future possibilities, and in many cases have not had clear strategic direction. We could hardly observe conscious steps to improve existing products and even more to develop new ones, and upgrade existing technologies. The marketing efforts only concentrated on maintaining existing market shares and there were hardly any signs of trying to enter into new markets and develop products to be sold on new markets.

The characteristics of strategies of the Hungarian enterprises in 2009 do not offer real hopes for getting out of the crisis within a short period of time as the necessary preparatory actions were missing in the practices of the companies. We could not find any signs of managerial awareness related to need for innovation even during the crisis period in order to improve the prospects of the firm to realize growth when market demand will start to grow.

Connections to other enterprises and participation in networks can be regarded as a relevant factor of enterprise development from the point of view of the present paper. The questionnaire survey provides some information on network relationships of enterprises. The survey of 2009 shows that Hungarian enterprises preferred short term contract relations instead of longer term ones. It was explained by top managers as an intention to increase flexibility (Chikán et al., 2010, p.46). It is a positive feature of inter-company relationships that cooperations in research and development have started to grow. The ratio of R&D cooperations was the highest compared to the previous surveys within the competitiveness research. This is somehow a contradictory feature as other characteristics of enterprise activity do not show clear signs of recognition of the need for innovation.

Slovakian experiences³

The questionnaire survey in Slovakia was conducted between September 2008 and February 2009, a few months before the Hungarian survey. The overall picture of the survey reveals that companies stagnated or decreased the volume of their output. A majority of the responding managers (59%) shared the view that the crises will last for about 2 to 3 years (end of the crisis was connected to starting increase of the GDP in the country).

Labor costs were unchanged in 51% of the companies, while 26% reported decrease, and another 15% forecasted changes during the coming months. Possible increase in wage level was mentioned by 5% of the respondents. Expenditure related to education and training was unchanged in 33% of the firms, it decreased in 31%, and 21% of the managers expected decrease during 2009. 12% forecasted increase in educational expenditures.

³ This section is based on Muraközy (2009).

Costs related to advertisement and communication remained unchanged in 34% of the firms, it decreased in 29%, and expected decrease was reported by 17% of the respondents. Expected growth of costs were mentioned by 13% of the companies in the sample. Overall marketing expenditures were unchanged in the practice of 60% of the firms, decrease was reported by 14%, and expected decrease by another 14%. Possible increase of marketing cost was mentioned by 9% of the answers.

Investments were reduced in 32% of the companies, 27% reported no changes, and 28% mentioned possible decrease during the coming months. Increase in investments were forecasted by 12% of the firms.

Introduction of new technologies were reported as being unchanged in its intensity after the crisis by 56%, and decrease was mentioned by 13%. Possible decrease was the experience of 12%, and possible increase was reported by 15% of the managers. Increase in the intensity of introducing new technologies was characteristic for 4% of the firms.

It can be seen from the above data that innovation and growth was less characteristic for Slovakian firms during the crisis period. There were however some examples showing company strategies different from the generally observable ones. Let us take the example of an internet service providing company is Southern Slovakia (Csiba, 2010). The firm has been set up in 1997 by Slovakian privat persons. Today it is owned by one slovakian entrepreneur. The firm started its activity in wireless access provision and became the member of the European Coordination Centre in 2000. The company continued its expansion strategy during the early 2000s by expanding its products portfolio and geographical coverage. The strategy followed may be described as a typical diversification strategy and it proved to be rather successful. Meeting customer expectations and flexible adaptation to changes in the market is a strong element in the strategy of the firm.

The company continuously invested in upgrading and extending its service providing network during the crisis period. The firm did not change the previously followed differentiation strategy and introduced new services called FiberHome and PanelNet Max. The optical network of the firm had been extended in years 2009 and 2010. At the beginning of 2010 the company defined its strategy as aiming continuous growth by providing high quality services taking into account the environment protection criterias and extending the services towards new regions in Southern Slovakia. The emerging major profile of the firm in the future is defined as extending access to the Internet (Csiba, 2010).

Comparison of the Hungarian and Slovakian experiences during the crisis

Empirical evidence summarized above concerning the strategies of Hungarian and Slovakian companies during the crisis period shows that in both countries defensive strategies aiming at reducing costs of operation by laying off employees and reducing production and service provision capacities had dominant roles. Innovation and preparation for growth after the crisis was hardly observable in the practice of companies we analyzed. Comparing the Hungarian and Slovakian data we may observe however that the Hungarian companies were even less innovation oriented than the Slovakian firms. Data on growth, innovation and expansion showed somewhat higher values in the Slovakian survey. The example of the innovative Slovakian internet service providing company clearly shows the possibility to go ahead even in a period of economic downturn. Using Internet may be regarded as a relevant element of future development either at private individual and enterprise levels. The owner of the Slovakian firm had understood this challenge and gave adequate answers to the opportunity. The latter example shows that perception and attitude of owners and executives can make a difference. As Leavitt has described it, path-finding managers can open the road towards innovation and growth (Leavitt, 1986).

DISCUSSION

The surveys during the period of economic crisis show that survival and short term orientation was characteristic for most of the enterprises. Goals related to innovation and growth were hardly present in the strategies of enterprises. While the general picture is rather negative from the point of view of preparation for the period after the recession, there are some examples showing that there are possibilities for other ways of thinking. The case of the innovative Slovakian internet service providing firm shows that when ownership and top management aspirations are motivated by longer term considerations, innovation may have a stake in shorter term enterprise strategies as well.

The above consideration shows that executive orientation and way of strategic thinking has a decisive role in company strategies during the crisis period. Another important influencing factor behind was the available financial resources which provided possibility for executives to think ahead and start preparations for the possible growth period after the crisis. Our empirical studies show that this way of thinking was observable at the minority of enterprises especially in case of SMEs.

The entreprenurially minded managers of the latter group of firms shared the view that the crisis period is not only an area with difficult problems to be solved in a short period of time, but at the same time it is a period of unprecedented opportunities to move forward and develop competitive advantages when increase in demands will have been arriving (Waldman, 2010). These companies started to develop new R&D projects, invested in broader areas of innovation and now they are more or less prepared to launch their new products and services which represent a higher level of technological development and meet customer needs at a higher level compared to the period before the crisis.

Based on his previous experiences and insights concerning the future possible directions of strategic development the present author is convinced the the success stories after the crises will be connected to enterprises following the innovation trajectory during the years of crisis.

Another field of development observable in our empirical studies is related to the increasing role of inter-organizational relationships through different forms of strategic alliances and emergence of clusters. The permanently prevailing need for cost efficiency and improvement of innovation capabilities drives companies towards new forms of strategic alliances enhancing the capabilities of business firms to accelerate innovation, develop new capabilities through co-operation, share risks and make costly innovation projects financially realizable. The above development tendencies were observable especially in industries characterized by severe competition, high technological development rates and needs for meeting new customer expectations (see: Hokansson and Lind, 2004).

CONCLUSIONS AND FURTHER RESEARCH OPTIONS

We have to admit that the available empirical evidences are rather limited from the point of view of making general forecasts for the future development tendencies. Additional research work is needed covering broader areas of enterprises and a more concentrated focus on the connections between innovation and future growth options of enterprises. Special attention should be devoted to the SME sector as it has an important role in future economic growth. But the observable intentions of the enterprises in our surveys probably provide possibilities for drawing attention to the emerging new tendencies and new strategic logics developed by enterprise managers.

It can be seen that managerial behaviour concentrating on short term survival is not favourable for realizing the possibilities of growth which will be provided when the crisis will have been finished. Increasing demand for products and services parallel with starting economic growth will offer outstanding growth option for those companies which have made the necessary preparatory steps during the crisis years. It seems to be clear that enterprises capable of offering new products and services representing higher level of technological capabilities and better adjustment to customer requirements will have the winning position after the crisis. This forecast is supported by the observable fact that during the crisis period in Hungary companies concentrating on R&D had the possibility for increasing their sales turnover.

Further and more extended studies will be necessary to check whether the above sketched directions of development are broadly observable new tendencies of enterprise level strategic management, or they are only examples observable locally. The present author and his colleagues have been working on this research question.

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