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MANAGEMENT CONSULTING TRENDS IN THE CEE REGION

Abstract: Countries of the CEE region are on their way to economic development, which is supported by foreign investments and thus technology transfer. All of them have entered the so-called investment driven growth stage by Porter during the last 3 decades. The recent challenge they have to face is the achievement of the stage of innovation-driven economic growth. The ability to create innovations presupposes knowledge-oriented domestic enterprises, as well as significant investment on R&D. The paper examines the general economic performance and innovation indicators in the 2 CEE country groups. As management consultants are directly involved in both the technology adoption process and the creation of new innovations, data of management consulting industry provide key information on the country's innovation potential. Observing the growth paths of eight CEE countries, we can note different combinations of FDI attraction and focus on domestic corporate sector. While inflow of FDI generates immediate growth, improvement of domestic enterprises resulting stability and sovereign growth is perceptible only in the longer term.

Keywords: FDI, management consulting, economic growth

1. INTRODUCTION

In the history of the CEE region, the regime change was the watershed that allowed individuals to set up a self-employed business or buy previously state-owned companies. The first wave of privatization came to close by the end of the 1990s in all countries of the Central and Eastern European region. An essential condition necessary to the establishment of a competitive market economy was fulfilled. Moreover, the legal and institutional system was transformed to ensure that market mechanism's allocation and information role was unbiased. However, the market liberalization, private property and free competition are not the sufficient conditions of the growth of economic efficiency and productivity. At present, the income-generating capacity of all the countries, the well-being of their societies and their economic development depend on how prepared and how successfully they can join the global industrialization that has lasted for almost 250 years. The countries of the CEE region have sought to alleviate the shocks caused by the regime change by opening their markets and accepting foreign capital investments. The structural transformation of the region's economies experienced over the past 30 years has been determined by the direction and intensity of FDI inflows. The stability and sustainable growth of the catching-up CEE region can be achieved however by moving forward from investment-driven growth, to the growth accelerated by own innovations (Porter, 1990). The importance of "technology competence" as the source of competitiveness is clearly demonstrated both at the corporate level and at the level of the national economy (Porter 1990, Pavitt 1990). Under term „technology competence" we mean a package of technology resources, skills and experience that give companies a distinct competitive advantage (Prahalad-Hamel 1990, Bessant-Rush 1993). This competence can be developed internally, through research and development (R&D), or through various organizational learning processes

that improve and maintain the knowledge base (Dodgson 1993, Nonaka 1991). Each country or group of countries may choose its own specific growth path (Solow 1956, 1957; Swan 1956), according to the neoclassical growth theory, in the case of equal capital stock level and equal technology level, convergence will take place in the long run. Empirical research has confirmed the fulfillment of the convergence hypothesis exclusively among individual states of the United States (Barro-Salaimartin 1991), some conditional convergence can be seen in Europe, it has been proven solely in developed countries within the homogeneous groups of countries (Quah, 1996; Ben-David, 1997). This paper seeks to examine the growth strategies of two chosen groups of countries that can be considered more or less homogeneous and are situated in the broader CEE region. National governments may choose different growth strategies that follow different economic policy directions and goals. Countries with larger internal market are characterized by its focus on the domestic market-, the smaller ones are rather export-oriented. Their governments protect and support domestic industries at varying degrees, and the nature of strategic measures to build innovation potential can be also diverse. Modern (endogenous) growth theory considers technological progress as the internal market's own product and as a variable that depends on R&D expenditures (Romer 1986, 1989, Lucas 1988, King-Rebelo 1990,1993).

The existence of the focused support of domestic enterprises has been proven by analysis of the size and availability of management consulting sector, and then in much longer term in the number of technical patents and in the export data of high-tech sector. Many authors believe that the organization of R&D can take place through two types of mechanisms, one of which is the involvement of external consultants in R&D activities and the other is the creation of independent R&D units (Bessant-Rush, 1995; Tether-Tajar, 2008). The successful organization of R&D activities influences the company's ability to turn external technological knowledge into product innovation. Consultants include external actors, such as management consultants, technology brokers, innovation agencies, or technical and scientific service providers, who support companies on an ad hoc, temporary basis in their research and development activities without being formally represented in their organizational structure.

2. METODOLOGY

The paper seeks to examine the growth trajectories of eight countries in the CEE region, based on their achievements at a given point in time. The study divides the countries of the broader CEE region into 2 homogeneous groups of countries. One such group is the V4 countries Poland, Hungary, Czechia and Slovakia, which focus on industry, including the automotive and electronics industries, and the other group contains the southern countries Croatia, Slovenia, Romania and Bulgaria with a developed service sector. What they have in common is that all eight countries began to build a competition based economic system in the early 1990s, and so the regime change was accompanied by significant shocks and economic crises in all cases. During that time, these countries have undergone significant institutional and structural transformation and economic development, in which foreign capital has played a role in varying degrees. By comparing the latest available data provided by international institutions, we can get insight into the development path of these countries and their present situation on the way of economic development and social well-being compared to each other. Various combinations of foreign capital investment (that generates rapid growth and the influx of technology), and domestically produced innovations can emerge as countries strive to take advantage of their own capabilities and adapt to the demands of global economic competition. The paper lists some general economic indicators, such as nominal GDP, exports, GDP per capita, and the average economic growth during the last 10 years. Innovation indicators that predicts the ability to produce new technologies and processes, as well as the indicator tracking the prevalence of management consulting, are used to forecast the direction and intensity of future growth. The article undertakes a single analysis of secondary data to assess the achievements of the countries so far as well as the currently measurable efforts. It does not examine long-run relationships between individual variables and economic outcomes.

Hypothesis 1: By absorbing foreign capital investments, developing countries can produce faster economic results than by strengthening the domestic corporate sector, however, in order to establish long-term stable and sovereign growth, it is necessary to develop strong global leaders from domestic entrepreneurs.

The hypothesis is based on the neoclassical notion that countries can choose specific growth paths, while at a low level of capital stock there is higher growth until the capital reaches the equilibrium level.

Hypothesis 2: The competitiveness and innovation potential of the domestic business sector in the developing countries can be achieved through conscious governmental efforts.

The hypothesis is based on Keynes's assumption that market mechanisms do not fully ensure fair distribution, targeted state intervention is needed in certain areas.

3. RESULTS AND DISCUSSION

The economies of the CEE region have been characterized in recent decades by catching up, strong FDI inflows, knowledge- and technology transfer. During this time, they have been able to take advantage of their position, and it is time to move on from investment-led growth to create economies built on their own improvements. The studied country groups of the CEE region are the V4 countries (Poland, Hungary, Czechia, Slovakia) and the coastal countries in the south: Romania, Bulgaria, Slovenia and Croatia.

The largest economy among Visegrad countries, with its population of 38 million, is Poland. Although Poland is one of the most dynamically developing economies in the region, GDP per capita is still the weakest compared to the other three

countries (World Bank, 2019). It is characterized by stable economic growth, with an average rate of 4.2% over the past 20 years (Fredriksson, 2019). Poland may enjoy the benefits of its large market, with serious internal consumption, on which the domestic production and service sector can confidently rely. Accordingly, exports account for only half of GDP. Within the region, Poland plays the largest role in funding transnationally coordinated R&D at national level. It contributes exactly twice as much as the other three countries together. Despite of that, high-tech exports account for only 8% of total exports, which is the lowest proportion within the region. The consulting industry is extensive, 40% of the region's consulting revenue comes from Poland (consultancy.com, 2020). On the other hand, the per capita annual turnover of the consulting market, is the lowest in Poland. Due to its huge domestic market and developed labor market, it is extremely attractive to foreign investors, its economic development relies heavily on foreign capital. Poland is a global player at video game development market.

Slovakia and the Czech Republic are the two smallest countries in the region, the structure of their economies is very similar. The largest share of foreign capital has been invested in industry, especially in automotive industry in both countries. In Slovakia, the automotive industry accounts for 35% of total industrial production and 13% of GDP (Szeiner-Szobi-Sklenár, 2018). The Czech Republic has a long tradition of car production, with its own brand Škoda dating back more than 120 years. 20,000 technical engineers graduate at the nine Czechish technical universities every year, its world-leading automotive research and development laboratories (eg EATON, Škoda Auto, ZF, Robert Bosch, Varroc Lighting) employ about 5,000 knowledge workers (czechinvest.org, 2020). In terms of the number of high-tech patents per million inhabitants, the Czech Republic ranks second in the region after Hungary. Hungary has developed a specific growth path. Over the past 10 years has managed to get out of the indebtedness inflated by previous governments, and then launched its unique programs supporting families and domestic businesses. The per capita turnover of the consulting industry is not by chance the highest in Hungary. Its economy has been characterized by export oriented intense growth over the last 10 years.

Table 1: Economic growth and innovation in the Visegrad countries

| | GDP/capita 2019 | GDP growth, 2010-2018 (average) | Export of G&S 2017 | MC turnover \$/1000 inhabitant 2017 | High—tech trade (mill.€) 2017 | Business Expenditure on R&D €/inhabitant 2017 | NPF to transnationally coordinated R&D (mill.€) 2017 | Technology patents/ million inhabitant 2005-2015 |
|-----------------|-----------------|---------------------------------|--------------------|-------------------------------------|-------------------------------|---|--|--|
| Czechia | 23.079 | 2,3 | 79,7% | 20,500 | 15.887 | 204 | 42.795 | 31,2 |
| Hungary | 16.162 | 2,51 | 87,1% | 39,600 | 9.746 | 124,8 | 21.152 | 45,8 |
| Poland | 15.421 | 3,53 | 54,3% | 14,200 | 16.345 | 82,1 | 129.998 | 13,7 |
| Slovakia | 19.443 | 3,10 | 95% | 17,300 | 8.915 | 74,6 | 8.844 | 11,6 |

Source: Eurostat 2020, Consultancy.eu 2020, OECD 2020, World Bank 2020

The largest country in the southern region is Romania. With a population of 19,5 million, it is characterized by a relatively large internal market and expanding consumption. GDP per capita is relatively low, but economic growth is fast-paced and balanced. Romania is very consciously concentrating on its domestic innovative industry with great forces. It supports the creation and development of innovative businesses. Over the past 20 years, Romania has grown into a major center for mobile technology, information security and related hardware research in Eastern Europe. The country is characterized by High Humane Development Index and a well-developed labor market. It is one of the main targets of FDI in the CEE region (Fan-Urs-Hamlin, 2019). Thanks to foreign direct investment, Romania has become the largest electronics manufacturer in the CEE. The country is also a regional leader in areas such as IT and automotive manufacturing. Bucharest, the capital, is one of the leading financial and industrial centers in Eastern Europe (Gruia et al, 2019).

Slovenia, with a population of 2 million, is the smallest country with highest income per capita in the region. Due to its pleasant beach and professional ski resorts built on its mountains, it is a popular tourist destination in both winter and summer seasons. Its economy is developed, steadily growing, service-oriented, nearly two-thirds of the workforce is employed in the service sector. The value of foreign capital investments is the lowest in the region, while the export of goods and services account for 83% of GDP. The consulting industry is extensive, with the highest per capita income compared to all countries surveyed, and the highest number of patents per million inhabitants during the last 10 years, compared to all countries surveyed.

Croatia is also a popular tourist destination especially in the summer months. 60% of GDP comes from the service sector and 10% from shipbuilding, which has a long tradition in Croatia. It is characterized by a highly developed service sector, and performs very well in the high-tech industry, which accounts for 16% of its exports (Eurostat, 2017).

The role of business consulting is not provided only by private service providers, but also by “Enterprise Support Institutions (regional development agencies, entrepreneurial centers, business incubators, business and technology parks, and business zones primarily aimed at providing information and consulting services related to business plan development and writing project applications for the public tenders issued by different governmental agencies)” established specifically to support domestic businesses (Barišić, 2017). Services provided by PSIs are available below the market price, which worsens the competitive conditions in the consulting market and, of course, the sales revenue of consulting also reveals less information about the real size of the consulting sector. Nevertheless, it can be stated that the use of consultants in

business development and innovation is widespread in Croatia, which is largely due to the government's conscious business development efforts.

Bulgaria, with a population of 7 million, is one of the lowest-income countries in the region and within the EU. Foreign direct investment increased much later than in other countries, following Bulgaria's accession to the EU. During the 2000s the economic growth was relatively low until 2015, when the inflow of FDI increased significantly. Industry accounts for 27% of income production, of which 67% goes to export. Tourism accounts for only 3.7% of GDP and employs 12% of workers. The management consulting industry started to develop immediately after the regime change, however the annual per capita turnover of consulting is still not too significant.

Table 2: Economic growth and innovation in the southern CEE countries

| | GDP/capita 2019 | GDP growth, 2010- 2018 (average) | Export of G&S 2017 | MC turnover \$/1000 inhabitant 2017 | High— tech trade (mill.€) 2017 | Business Expenditure on R&D €/ inhabitant 2017 | NPF to transnationally coordinated R&D (mill.€) 2017 | Technology patents/ million inhabitant 2005-2015 |
|-----------------|--------------------|--|--------------------------|---|--|--|--|--|
| Bulgaria | 9.273 | 2,20 | 67,3% | 35.140 | 1.815 | 38,5 | 5.525 | 2,0 |
| Romania | 12.301 | 2,99 | 41,5% | 99.000 | 6.198 | 27,3 | 29.22 | 11,5 |
| Slovenia | 26.124 | 1,73 | 83% | 134.000 | 1.543 | 290,4 | 6.382 | 63,1 |
| Croatia | 14.910 | 0,78 | 50% | 15.365 | 1.405 | 49,3 | 5.945 | 17,2 |

Source: Eurostat 2020, Consultancy.eu 2020, OECD 2020, World Bank 2020

Both the V4 countries and the southern CEE countries began to set up the conditions for a modern market economy after the regime change in 1989, but their capabilities and geopolitical situation are quite different. In the V4 countries, the inflow of FDI intensified significantly in the 2000s, and were greatly strengthened by the EU accession in 2004 (Poór, 2016). This period has also given a boost to the consulting industry, as consultants are directly involved in entering international markets. Large multinational consulting firms began to settle in the region in the early 1990s, followed by emerging domestic consulting firms, many of which have since strengthened and dominate a segment at the domestic market or entered international markets. Consultants have also played a major role in the transfer of technological competence in recent years. With strong growth of around 5% in 2012-2018, the CEE region's advisory market reached annual revenue of \$ 3.5 billion (Source Global Research, 2020). Hungary has the largest and most developed consulting market in the region, which is also reflected in the relatively high number of technology patents. The extent of the Hungarian consulting industry partly reflects the government's conscious domestic business development policy, however, the demand for consulting can also be explained by socio-cultural factors (Pemer et al. 2014, Pemer-Sieweke-Werr 2018, Barthélemy 2019, Pelczné-Szadai 2004). V4 countries rely heavily on foreign capital investments, so far, the Czech Republic has succeeded most in building its own internal innovation potential. This is partly due to a conscious development policy and partly to continuous development, as the automotive and electronics industry in the Czech Republic has a strong tradition and, thanks to its excellent universities, its developed labor market is well equipped with highly qualified technical professionals.

In the southern countries of the CEE region, the per capita GDP is still slightly below the V4 countries' on average, with the exception of Slovenia, where it is the highest among all the countries studied. The southern countries, except Slovenia, joined the European Union later than the V4, and the inflow of foreign capital investments also started later. This can be seen in the economic performance of Romania and Bulgaria for the time being, but recognizing the potential in technology innovations, Romania consciously supports the creation of scientific and technology. Although the area of the V4 countries is larger with only 100,000 km² than that of the southern countries, its population is still exactly double that of the southern ones. As Table 3 shows, the Visegrad countries also produce slightly more than twice as much income. Their advantage is not only due to the larger population, the Visegrad countries also joined the European Union earlier (in 2004) than Romania and Bulgaria (2007) and Croatia (2013). Slovenia, which joined at the same time as the V4, has a well-developed domestic service industry, and so is able to achieve stable economic growth even without a large inflow of foreign capital. The value of investment made by foreign capital has reached \$ 532 million in Visegrad countries, in the case of southern countries this value is \$ 192 million. For the time being, the time lag and the lower intensity of foreign capital can be seen in the aggregate economic data of the countries. At the same time, despite half the size of the population, the southern countries spend twice as much on business consulting as the Visegrad countries, which clearly indicates the strengthening of domestic companies and the domestic corporate sector. This is because consulting is usually used by entrepreneurs, owners and managers in companies where strategic decisions are made. Managers of assembly-only subsidiaries typically do not apply advisory services.

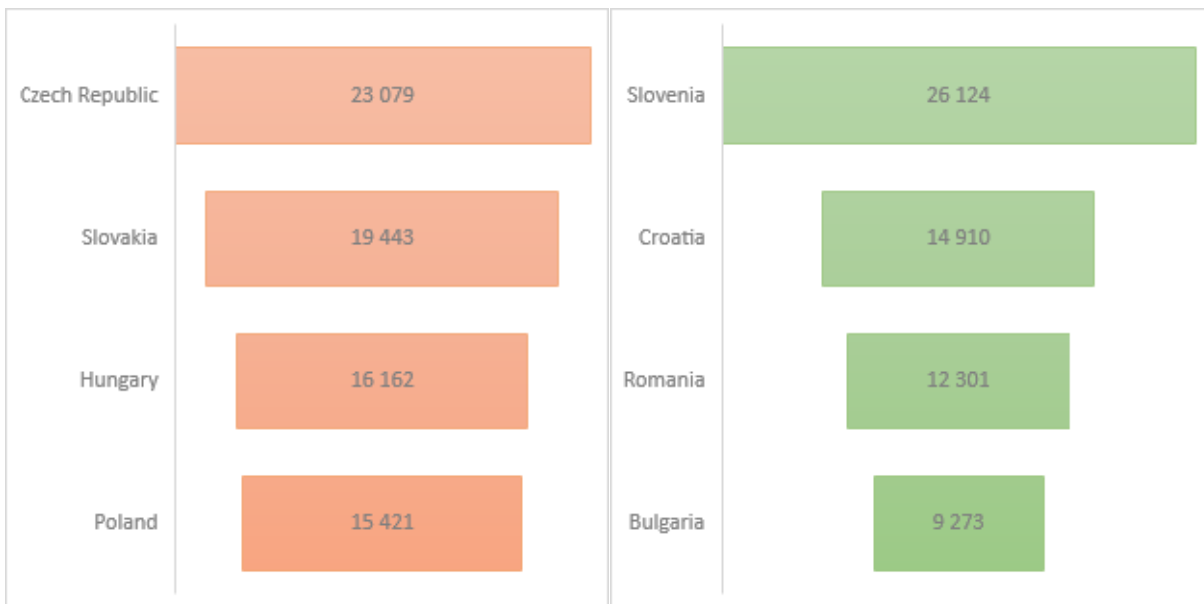


Figure 1: Nominal GDP per capita, 2019
Source: World Bank, 2020

The data of the consulting sector may predict the strengthening of domestic economic actors, but its measurable economic results will appear in the longer term. The development of powerful domestic companies, as well as their entry into foreign markets, will result in greater stability and real prosperity growth in the long run than over-reliance on foreign capital. According to the latest available data (2005-2015), there is no significant difference in the number of technology patents per million inhabitants between the 2 regions. While a total of 102.3 such patents were issued in the V4 countries, 93.8 in the southern ones. Expenditure on R&D averages 0.99% of GDP in the southern countries, compared to an average of 1.26% of GDP in the V4 countries.

Table 3: Key indicators of the CEE country groups

| | CZ-SK- HUN-POL | BUL-ROU- SLO-CRO |
|-----|-------------------|---------------------|
| 👤 | 63,800 | 32,800 |
| € | 1,093,184 B | 419,427 M |
| EXP | 60,5% | 79% |
| M | \$ 2.530 M | \$ 1.242 |
| FDI | \$ 532,717 M | \$ 192,990 M |

Source: Eurostat 2020, Unctad.stat 2020

V4s, on the other hand, already benefit much more from their high-tech industries, with revenues five times higher than those of southern ones (Eurostat, 2020). In terms of outward FDI, the south is also lagging behind for the time being. By 2018, the value of capital investment originated from the V4 countries had reached \$ 96 million, while the value of capital investment originated from the southern CEE had reached \$ 16.8 million (unctad.stat, 2020). An important circumstance is that while the growth and economic results of the V4s are strongly linked to foreign industrial investments, the strengthening of the domestic business sector is pushed into the background. According to the recommendations of international organizations and the commitments of the EU countries, the support system for SMEs has been established, but the programs aimed specifically at domestic enterprises can only be found in the case of Hungary. Based on the data on the size of management consulting industry, it can be concluded that the states of the southern region prioritize the improvement of domestic enterprises and the provision of a suitable environment for their development.

4. IMPLICATIONS AND CONCLUSIONS

Most governments are involved in some way in supporting innovation at regional and / or national level, but there is still a wide range of the underlying philosophy and the mechanisms used. Some countries develop sector- or technology-specific policies that explicitly aim to influence the scale and direction of innovative activity. Others opt for more general infrastructure measures, where the main goal is to create the conditions for innovation to take place. Despite its diversity, policy-making has also shown some degree of convergence in this regard over the past 15-20 years. For the first time, the general and strategic nature of certain technologies was recognized, namely the cluster around information technology (IT), for which action programs have been launched to support priority, even in traditionally non-interventionist economies. This was followed by the adoption of alternative mechanisms to complement the traditional package of investment loans and grants; one of these is the increasing use of consultants as part of an evolving strategy for technology competence building at the national level. Some states seek to involve the consulting sector through a combination of awareness raising, feasibility study and development projects. The involvement of this intermediate sector has an impact not only on aid to SMEs, but also on the rapid expansion of the supply side; many consulting firms have been developed to participate in such systems, and as a result, many hidden technological skills have been mobilized. Experiences regarding various applications of consulting as part of larger promotion and distribution policy programs demonstrates that this model can be a useful complement to economic development policies. Empirical researches on innovation systems strongly supports the view that the quality of the whole system and the connections within it influence the success of technology transfer (Wagner 2012, Carlsson-Jacobsson 1992). The importance to involve more intermediary companies in the technology transfer process is essential. Examples of such intermediaries are technology brokers, university liaison departments, regional technology centers, innovation agencies and transnational networks such as TII (European Alliance for Technology, Innovation and Industrial Information Transfer). A growing number of intermediary agencies, as well as companies and actors involved in providing advice and related services, are of growing political importance. Their inputs may be direct, allowing the transfer of specific technology competence, but they often prefer to engage in a broader and more flexible interaction of the process by providing a range of information and related services to help bridge the gap between technology opportunities and (often poorly articulated) user needs. Nowadays, in the light of empirical experience, it can be said that new companies created using foreign direct investment were in most cases more efficient and effective than the companies that were privatized after the regime change (Tóth et al, 2003). In fact, companies from developed market economies were equipped with greater expertise, more advanced technologies, and technical knowledge than new business owners and managers accustomed to the socialist economic system. Over time, this lag has been significantly reduced or eliminated as a result of the learning process of knowledge and technology transfer integrated into organizations. Increased participation of local SMEs in global markets offers opportunities to increase productivity and accelerate innovation, facilitate technology transfer and managerial know-how, as well as expand and deepen skills. International trade, whether through imports, exports or foreign direct investment, is often associated with higher productivity and can be an important driver of employment growth (Wagner 2012).

The two examined groups of countries are not growing at the same rate and at the same pace. For the Visegrad countries, industry has become the main economic trump, and projects implemented with foreign direct investment have been the main driving force for growth. Foreign capital also plays a significant role in employment, and the governments pursue a policy aimed at attracting and receiving FDI. According to the recommendations of international organizations, the support of the SME sector is provided by the countries, but programs aimed at supporting domestic enterprises, making the domestic corporate sector powerful and competitive, and accessing business consulting for domestic small and micro enterprises are much more common in the southern CEE countries. Among the V4 countries, only Hungary has a conscious program developed for the purpose. In the case of the southern countries, investments made by FDI have not yet reached a level similar to the Visegrad countries, which is reflected in the lower level of income generation. However, these countries place much more emphasis on their domestic industrial and service sectors. Due to their natural advantages the service sector has developed as a result of a long term process and the conscious efforts of governments. The case of Slovenia is the best example of how a strong domestic industry and service sector can achieve the same economic growth in the long run as foreign capital, even a small country. As Slovenia has the lowest inflow of FDI and yet the highest GDP per capita. Among the southern countries, Bulgaria is the weakest performer so far, it has started to grow strongly since 2015 due to the accelerated FDI inflows.

Observing the growth paths of the CEE countries, it can be stated that both foreign capital investment and the development of domestic enterprises play a key role in economic development and prosperity growth, but while external capital provides fast-acting, immediate results, domestically developed capital provides long-term stability and greater independence for such small players of the global economy.

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