The Czech Republic (Czechoslovakia until the end of 1992) was the most centrally planned and furthest from a market economy of any of the communist-governed states under Soviet Union influence. It adopted the most radical transition plan with early liberalizations of prices and markets and rapid and complete mass privatization of state-owned assets. It was praised in the early 1990s as a model of shock therapy, and it was criticized in the late 1990s for its failures, one of which was the failure to create institutions. It makes an extreme test case for McDermott's central questions: How do economic governance institutions develop? and "What kinds of institutions help countries restructure their economies, improve growth, and promote democracy?" (p. 1).

The Czech government got it wrong, in McDermott's view. The Klaus government sought to depoliticize the transition, to prevent interest groups from influencing it, and to make the rules and control the transition from the center without the aid of any government-related workouts for privatized enterprises. In the end, the macro politics of state designs and the micro politics of intranet work struggles came together, out of the background of past interdependencies, to determine transition outcomes. A better way was the Polish way in which there were iterative negotiations among stakeholders about the restructuring of assets, with less central control.

The role that governments should play in the transition is neither to make a set of rules centrally and withdraw (the Czech way) nor to manage the transition actively itself (the statist alternative), but rather to facilitate decentralized multiparty negotiations.

The embedded politics approach that McDermott advocates focuses on the firm and investigates how firms are embedded in social and political relations. There were extensive networks of business relationships during the communist era (perhaps in response to the totality of official control from the center), and McDermott asks how these networks evolved during the transition to influence decisions and change organizations. The networks are socio-political and occupy space between public and private domains.

The book sketches in considerable detail the ways in which the production system in the Czech Republic developed differently from the highly centralized mass production communist ideal (Chapter 2). The key feature was the rise of industry associations and concerns that took on a range of decentralized management roles and in so doing developed elaborate networks of inter-firm, interpersonal, and firm-state relationships. It was a feature that figures prominently in McDermott's analysis of the transition experience in the Czech Republic.

After the Velvet Revolution in November 1989, the Czech government led by Vaclav Klaus faced three enabling conditions for its transition plan – decent macroeconomic outcomes, no previous partial economic reforms, and no organized political resistance. The transition plan, implemented beginning in 1991, is characterized by McDermott as one to "depoliticize institution building and restructuring" (p. 73). The idea was to privatize most state-owned assets
quickly by means of vouchers (each citizen could buy an allotment of vouchers for a low price equivalent to about one week's average wages), and thereby transfer ownership into private hands quickly. Meanwhile the state liberalized prices and took bad loans from the communist era off banks' balance sheets to give them a fresh start. Restructuring was to be accomplished through market processes without state involvement. It didn't work out that way, McDermott asserts, in part because of a banking sector that was interdependent with the industrial firms, the lack of well-functioning capital markets, and the absence of foreign direct investment.

FDI did not come in because most Czech firms the beginning of the transition were unattractive investments (heavily indebted and technologically obsolete) and interdependent with other firms. In cases where FDI occurred it was usually for just part of an enterprise – the productive bits without the social overhead.

The story about what went wrong in the Czech banking sector is one that can be told many different ways. McDermott’s view is that the government established a proper legal framework including bank supervision, bankruptcy, and capitalization, but that the banks did not use their creditors’ rights to enforce restructuring of industrial enterprises because of their interdependencies with the industrial firms and the lack of state-assisted workouts. Instead, the banks chose to protect and preserve asset values to the extent they could. Rather than close down badly managed or failing firms and reallocate capital elsewhere, the banks kept them going. Bank managers did not know how to manage industrial firms, hadn't the capital to rescue them, and did not want to liquidate a string of interdependent firms that were their loan customers. Investment privatization funds arose from voucher privatization, and the banks themselves owned many of them. These closed-end funds owned substantial blocs of the industrial firms, but they were passive investors not susceptible to outside pressure. They did not focus on share value and were not active in corporate governance because, in McDermott’s analysis, they could make money with little risk and low cost in arbitrage between the nascent and illiquid Prague Stock Exchange and the over-the-counter (RMS) system.

The large industrial concerns – holding companies comprising several related producing units and support services – were ill equipped to restructure. They had a history of intra-concern economic relationships that constituted their linkages to the sociopolitical environment. Each unit was partly dependent on other units for supply of inputs or sale of output. The shortage of short-term finance from the banking sector led to inter-firm financing (not paying suppliers and letting payables increase). These firms did not succeed in attempts to diversify into new markets or create new products, and they did not solve their cash flow problems. To do so would require downsizing existing units amidst uncertainty about the new ventures. Two of the main tasks of the transition – reordering property rights through privatization, and maintaining asset values – were simultaneous, not separate issues because of the interdependencies among firms in the industrial holdings. Because the state centralized the transition process, there was no meso-level state source of sociopolitical power to resolve the micro politics of intranet work conflicts. The way in which these conflicts were ultimately resolved was through “delegated deliberative restructuring” (DDR) – McDermott’s term for the torturous and lengthy process in which the government re-engaged with enterprise managers and banks to decide restructuring decisions. DDR was at odds with the depoliticization model originally adopted by the Klaus government.

In each of two chapters, we learn the story of the troubled transition of each of two different types of concerns in the engineering sector. Škoda Plzeň was an example of a hierarchical network, and SST was an example of a polycentric network, and these differences affected the dynamics of their restructuring. McDermott draws lessons from each.

We read in this book about one point of view of the Czech transition. It has its own key variables and themes, just as other approaches do, such as an industrial organization approach that relies more on economics and finance than political science. It enriches our understanding of this rich and complex period of time, but it does not replace or subsume other ways of understanding the transition. Of course, unanswered questions remain. One of them is lessons for how formal institutions for economic governance – legal, financial, regulatory – can or should emerge in a transition country, in addition to informal institutions of the delegated, deliberative restructuring type.