

The VRIO Framework: An Overview

¹Barney and Hesterly (2006), describe the VRIO framework as a good tool to examine the internal environment of a firm. They state that VRIO “stands for four questions one must ask about a resource or capability to determine its competitive potential:

1. **The Question of Value:** Does a resource enable a firm to exploit an environmental opportunity, and/or neutralize an environmental threat?
2. **The Question of Rarity:** Is a resource currently controlled by only a small number of competing firms? [are the resources used to make the products/services or the products/services themselves rare?]
3. **The Question of Imitability:** do firms without a resource face a cost disadvantage in obtaining or developing it? [is what a firm is doing difficult to imitate?]
4. **The Question of Organization:** Are a firm’s other policies and procedures organized to support the exploitation of its valuable, rare, and costly-to-imitate resources?”

What types of resources should we evaluate (e.g., what types of resources lead to a competitive advantage)? 1) tangible resources, 2) intangible resources, 3) organizational capabilities.

Tangible Resources	
Financial	<ul style="list-style-type: none"> • Firm’s cash and cash equivalents • Firm’s capacity to raise equity • Firm’s borrowing capacity
Physical	<ul style="list-style-type: none"> • Modern plant and facilities • Favorable manufacturing locations • State-of-the-art machinery and equipment
Technological	<ul style="list-style-type: none"> • Trade secrets • Innovative production processes • Patents, copyrights, trademarks
Organizational	<ul style="list-style-type: none"> • Effective strategic planning process • Excellent evaluation and control systems
Intangible Resources	
Human	<ul style="list-style-type: none"> • Experience and capabilities of employees • Trust • Managerial skills • Firm-specific practices and procedures
Innovation and Creativity	<ul style="list-style-type: none"> • Technical and scientific skills • Innovation capacities
Reputation	<ul style="list-style-type: none"> • Brand name • Reputation with customers for quality and reliability • Reputation with suppliers for fairness, non-zero-sum relationships
Organizational Capabilities	
<ul style="list-style-type: none"> • Firm competences or skills the firm employs to transfer inputs to outputs • Capacity to combine tangible and intangible resources, using firm processes to attain desired end. 	
Examples	
<ul style="list-style-type: none"> • Outstanding customer service • Excellent product development capabilities 	<ul style="list-style-type: none"> • Innovativeness or products and services • Ability to hire, motivate, and retain human capital

¹ Note that the material presented in this handout are adapted from J.B. Barney, “Firm resources and sustained competitive advantage,” *Journal of Management* 17 (1991), p. 101; R.M. Grand, *Contemporary Strategy Analysis* (Cambridge, England: Blackwell Business, 1991), pp. 100-102; M.A. Hitt, R.D. Ireland, and R.E. Hoskisson, *Strategic Management: Competitiveness and Globalization*, 4th ed. (Cincinnati, OH: South-Western College Publishing, 2001); G.G. Dess, G.T. Lumpkin, M.L. Taylor, A.A. Thompson, and A.J. Strickland III, *Strategic Management* (Boston, McGraw Hill, 2004) pp. 141-148.

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Applying the VRIO framework. According to the VRIO framework, a supportive answer to each questions relative to the firm being analyzed would indicate that the firm can sustain a competitive advantage. Below is an example of how to apply the VRIO framework and the likely outcome for the firm under varying circumstances.

Applying the VRIO Framework—the value and rarity of a firm’s resources		
If a firm’s resources are:		The firm can expect:
Not valuable	—————→	Competitive Disadvantage
Valuable, but not rare	—————→	Competitive parity (equality)
Valuable and rare	—————→	Competitive advantage (At least temporarily)

Then, if there are high costs of imitation, the firm may enjoy a period of sustained competitive advantage. Costs of imitation increase due to some combination of the following: 1) **Unique Historical Conditions** (path dependence; first mover advantages), 2) **Causal Ambiguity** (links between resources and advantage foggy), 3) **Social Complexity** (social relationships not replicable), 4) **Patents** (double-edged sword since period of protection eventually runs out).

Applying the VRIO Framework, integrating the notion of Inimitability		
If a firm’s resources are:		The firm can expect:
Valuable, rare, but <i>not</i> costly to imitate	—————→	Temporary competitive advantage
Valuable, rare, <i>and</i> costly to imitate	—————→	Sustained competitive advantage (if organized properly)

Organized properly deals with the firm’s structure and control (governance mechanisms—compensation, reporting structures, management controls, relationships, etc).

These must be aligned so as to give people ability and incentive to exploit the firm’s resources.

Summary of VRIO, Competitive Implications, and Economic Implications					
Valuable?	Rare?	Costly to Imitate?	Organized Properly?	Competitive Implications	Economic Implications
No			No	Disadvantage	Below Normal
Yes	No		↑	Parity	Normal
Yes	Yes	No	↓	Temporary Advantage	Above Normal (at least for some amount of time)
Yes	Yes	Yes	Yes	Sustained Advantage	Above Normal