Territorial capital as a source of firm competitive advantage: evidence from the North and South of Italy

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Abstract. This paper investigates how territorial capital, defined as a *mix* of tangible and intangible local resources accumulated over time across different territories, becomes a source of competitive advantage for firms. The study draws upon semi-structured interviews with firms' owner-managers operating in the North and South of Italy and shows how local resources generate firms' costs and differentiation advantages through acting as territorial externalities or becoming an essential core asset to the firm. Results demonstrate how local resources are highly interconnected, making territorial capital unique in each place and not easily imitable, which ensures long term competitive advantages for those firms that benefit from its endowment. A mix of advanced local resources developed through long term investment is shown to be more valuable for firms than inherited resources, provided by 'God' or 'ancestors'. Using the concept of territorial capital in this manner provides insights into understanding sources of firm competitiveness related to location and the persistence of territorial economic disparities.

***Keywords**:* Competitive advantage, Territorial Capital, Firm strategy, Local resources, Resource Based View.

JEL Classification: L10; L19; R10; R11

1. Introduction

Researchers within the field of economic geography have routinely investigated sources of firm competitiveness related to location factors (Malmberg and Maskell, 2018; Ferreira et al., 2017; Audretsch et al., 2015; Maskell and Malmberg, 1999). Concepts such as industrial districts, clusters, industrial atmosphere, local milieu and, more recently, entrepreneurial ecosystems (Aydalot and Keeble, 2018, Alvedalen and Boschma, 2017; Branzanti, 2015; Sforzi, 2002), are hugely influential in the field and represent important contributions to understanding the link between firms' competitiveness and their local environment. Nevertheless, a limitation of these theories is their focus on only certain aspects of the territory, most commonly on the interactions established among economic actors or other intangible factors enabling economic activities, such as human and social capital (Malecki, 2012). As a result, these theoretical approaches often fail to take into account a wider and more comprehensive set of tangible and intangible resources that may be available within different places, and that could be jointly important to firm competitiveness (Kitson et al., 2004; Camagni and Capello, 2013).

The concept of *territorial capital* has been developed to address this limitation and refers to the stock of assets that form the basis for endogenous local development in localities, cities and regions (EU, 1999; OECD, 2001; Camagni, 2008). This concept incorporates several notions which have been extensively studied within the field of economic geography, such as human, social or institutional capital among others, but provides, a distinctive emphasis upon the co-existence and complementarity of such capital assets as a defining characteristic of different territories. In fact, it is argued that none of these factors can be studied in isolation but their combination gives new meaning to the territory and shapes new regional spaces (Keating, 2001).

Research has shown that territorial capital is fundamental to improve territorial competitiveness and to promote local economic development (Camagni, 2008; Servillo et al., 2012; Camagni and Capello, 2013; Perucca, 2013; Tóth, 2015). Complementary territorial capital assets are also important to regional resilience in times of crisis and making local policies more effective (Fratesi and Perucca, 2018a; 2018b). However, its effect on firm competitiveness has been under-explored within existing research. Furthermore, the vast majority of studies on territorial capital employ quantitative techniques which encounter limitations in measuring this nebulous and complex concept through the use of secondary data. In contrast, this research uses a qualitative method which aims to gain deeper insights into the interdependency, interconnections and complementarity of different elements of territorial capital to explain how, in practice, it influences firm competitiveness. This paper, therefore seeks to answer the question: *How does territorial capital become a source of competitive advantage for firms?*

The analysis presented here is based on a qualitative study of 26 Italian firms. The case of Italy is particularly interesting given the persistent socio-economic territorial disparities between its regions, in particular the North versus the South (Capello, 2016). Hence, this study also provides insights into how the well-known economic divide between the North and South of Italy is affected by the way in which firms are influenced by, and take advantage of, their territorial capital.

The paper is organized as follows. Section two reviews the concept of competitive advantage by explaining the main features of territorial capital from a Resource Based View (RBV) perspective. Section three introduces the method adopted. Section four describes the two case study provinces and section five presents and discusses the main findings of the research. The practical and theoretical contributions of the study are then discussed in relation to policy considerations (section six) and overall conclusions (section seven).

2. Territorial sources of firm's competitive advantages and territorial capital

The study of sources of firms' competitive advantage became popular following the seminal studies of Porter (1980, 1985). Here, firms gain superior performance to overcome their competitors in two main ways: cost leadership, through which firms become the low-cost producers in the industry, and differentiation, through which they are able to offer unique products/services and are rewarded for this uniqueness with a premium price (Porter, 1985). Preeminent RBV theory argues that firms may develop a competitive advantage when owning, developing and exploiting resources that are valuable, rare, not imitable and not substitutable: resources are *valuable* when they can improve firms' efficiency and effectiveness; *rare* when they cannot be owned by a large number of competitors; *not imitable* when developed thanks to a unique historical condition, casual ambiguity or complex social phenomena; and *not substitutable* when not equivalent to any other resource (Barney, 1991; Barney et al., 2001).

According to the strategic management literature, such resources are typically *internal* to the firm meaning they can be directly developed, controlled and exploited by the firm itself, for example through management skills, marketing and organizational capabilities or acquired knowledge (Barney et al., 2001; Nath et al., 2008). However, a number of authors have also found sources of competitiveness *within* the environment where the firm operates, extending the RBV to factors residing outside the firm across a range of tangible and intangible territorially based resources. (Maskell and Malmberg, 1999; Camisón, 2004; Gordon et al., 2005; Wan, 2005; Schilke, 2014).

Such intangible and tangible resources can be considered as important components of territorial capital and may influence firms located within particular territories. In particular, intangible territorial assets belong to the sphere of *local capabilities* and their importance for territories and local firms has been emphasized by a number of authors (Huggins, 2016; Camagni and Capello, 2013; Foss, 1996; Maskell and Malmberg, 1999). One of the most important sources of competitive advantage for companies is identified as *human capital*, which includes the knowledge and skills, competencies and attributes embodied in individuals (Wright et al., 1994). The capability of the local context to generate and/or attract human capital facilitates firms in the process of acquiring valuable human resources, supporting productivity and gaining cost/differentiation advantages (Backman, 2014). *Creative capital* is another important component of territorial capital and related to the local capability to produce new ideas, organise events, and generate new economic activities (Florida, 2002; Piergiovanni et al., 2012). When the local creative environment is vibrant, firms are also more likely to attract creative workers and find creative stimulus from the surrounding environment (Florida, 2003). New ideas, generated within the local milieu may translate into innovative managerial and organisational practices, products and services, generating cost/differentiation advantages.

Social capital, mainly identified with the capability of economic actors within the local context to cooperate and establish profitable relations, is another important component of territorial capital essential to a firms' functioning (Malecki, 2012; Crisholm and Nielsen, 2009). Operation within a collaborative and trustful environment can help firms overcome barriers caused by their small size, improve their relations with suppliers, reduce costs and generate innovation (Westlund and Bolton, 2003; Cooke et al., 2005). Camagni (2008) focuses on a particular component of social capital in regard to territorial capital, that of *relational capital*, which comprises the set of relations at the micro level and equates to the concept of *local milieu*.

Closely linked to social capital, *cultural capital* is defined as the set of ideas, practices, belief, traditions and values which identify a group of people (Throsby, 1999). This heterogeneous concept may raise the economic value of tangible capital (Throsby, 1999), for example through the existence of a rich cultural heritage which increases place attractiveness and generates differentiation advantages in the tourism sector. Other aspects of local culture linked to people's ideas, habits or values, can also influence firms in different ways; for instance, entrepreneurship and the presence of risk-taking and competitive firms also have cultural foundations (Fredin and Jogmark, 2017; Audretsch and Keilbach, 2007; Cochrane, 2006).

Alongside social and cultural capital, both informal norms and formal institutions, known as *institutional capital,* influence economic activities and can become a source of firm competitive advantage (Oliver, 1997; Fernández-Esquinas, et al., 2017). Efficient institutions promote trust and transparency, reduce transaction costs, stimulate innovation and often drive the accumulation process and the efficient use of other territorial resources (Huggins, 2016; Rodríguez-Pose, 2013).

With respect to tangible forms of capital, the literature has underlined their importance to firm performance. For example, *physical or anthropic capital* (Servillo et al., 2012) includes the built environment and represents an important component of the economic infrastructure. Infrastructures such as transportation and communication facilities are crucial to reducing costs and facilitating firms' output growth and productivity (Isaksson, 2007).

Other forms of tangible capital are 'inherited', such as natural and in some cases artistic capital. *Natural capital* comprises the endowment of renewable and non-renewable stocks of natural assets and can become a source of competitive advantage both in terms of cost and differentiation. Natural ecosystems can be seen too as production factors themselves (Throsby, 1999; Isaksson, 2007), with the development of competitive advantage increasingly based on capabilities linked to environmentally friendly activities; what has been called the 'natural resource based view' of the firm (Hart, 1995). *Artistic capital*, defined as the set of monuments, sites, artworks and landscapes, represents an important source of attraction of people and business in the tourist sector (Throsby, 1999). This form of capital, which incorporates an intangible component, is highly important for certain territories and generates differentiation advantages in specific sectors such as tourism and entertainment.

Although the extension of the RBV principles to outside the firm is well-established, a limitation of existing studies is their inability to shed light upon the potential complementarities and concurrent effect of this wide variety of tangible and intangible resources on firm competitiveness. In fact, as with a firm's internal resources, territorial resources are seldom valuable in isolation and should be considered in combination as a 'bundle' of resources (West and Bamford, 2005; Keating, 2001). The concept of *territorial capital* (OECD, 2001; Camagni, 2008) attempts to consider all the tangible and intangible resources available in an area, to provide a basis for a more holistic approach to the study of competitiveness. Camagni's (2008) classification of territorial capital includes components not only of materiality (tangible plus intangible) but also according to degrees of rivalry (public plus private). He considers here public resources, such as public infrastructure or social overhead capital, private resources, such as private fixed capital or private know-how, and mixed resources (e.g. the existence of public-private strategic alliances in the territory). In his taxonomy, mixed resources in terms of materiality and rivalry, such as agglomeration and district economies or club goods, are considered the most innovative components of territorial capital (Camagni, 2008).

From a RBV perspective, territorial capital is not only valuable since it may enable economic activities (Camagni and Capello, 2013), it is also ‘unique’ and not easy to reproduce and imitate, due to a number of distinctive characteristics related to its peculiar process of accumulation, across space and over time (Dierickx and Cool, 1987). Territorial resources accumulate locally in the form of capital over the course of several generations, therefore making them difficult to create from scratch. In particular intangible resources and localized capabilities which are linked to the institutional endowment, or to the knowledge and skills available in the local area, are deeply spatially embedded and hence difficult to imitate (Maskell and Malmberg, 1999). Building capital assets can be difficult because “*adding increments of an existing stock of assets is facilitated by possessing high level of that stock*” (Dierickx and Cool, 1987: 5). This is the case, for example, of firms located in territories where the quality of human capital is high and which, for this reason, are more able to attract skilled human resources from other places (Backman, 2014). The accumulation of one stock of territorial assets often depends on the level of accumulation of other assets, for example when the accumulation and effectiveness of transport infrastructure is facilitated by the quality of regional governments which reinforce institutional capital (Crescenzi et al., 2016). This process of accumulation is stochastic and discontinuous and this causal ambiguity makes it difficult to identify and control relevant variables (Dierickx and Cool, 1987).

The interconnection and interdependence existing in the process of accumulation of different elements of territorial capital highlight the importance of considering them jointly in order to fully understand their impact on firm competitiveness. However, while the concept of territorial capital has a certain political appeal, the possibility of its empirical quantification remains limited. Measuring territorial capital is problematic given it is difficult to describe and measure precisely the complexity of local contexts and capture this ‘bundle’ of resources which characterizes different places. Its operationalization via quantitative analysis is characterized by a number of constraints and often fails to draw out the precise process through which it contributes to firm competitiveness. In this respect, this research delivers a deeper level of analysis by studying *how* territorial capital becomes a source of competitive advantage via qualitative analysis.

3. Research method

The qualitative approach adopted in this study enabled exploration of the way in which territorial capital became a source of firm competitive advantage across two very different geographical areas. The data collection consisted of semi-structured interviews with owners/managers from a purposively selected sample of 26 small and medium-sized enterprises (SMEs). With between 10 and 250 employees, SMEs are considered the cornerstone of the Italian economic system and often strongly embedded within the local context. The selected firms were located in the provinces of Milan (Lombardia) and Palermo (Sicily), (see Figure 1) two geographical areas chosen because of the strong differences in their economic performance and territorial capital endowment. These two provinces represent 'extreme cases' exemplifying the Italian socio-economic divide where the North has historically demonstrated a superior economic performance to the South.

Firms were selected from three different sectors: Accommodation and Food (A&F), Information, Communication Technology (ICT) and Manufacturing (Man.), in order to include sectors which embodied the long historical and economic tradition of the country alongside a new rapidly expanding sector. Table 1 presents a list of the 26 firms interviewed in Milan and Palermo (11 and 15 respectively) and their profile.

The semi-structured interviews were guided by an interview schedule which investigated the role of different components of territorial capital upon firm competitiveness and acted as a basis to pursue salient aspects related to the role of territorial capital as a whole. After recording and transcribing the interviews, a coding system was developed to analyse the data collected. First level codes were directly developed from responses to interview questions following a deductive top-down approach (Braun and Clarke, 2006) and related to the identification of the relative importance of different components of tangible and intangible territorial capital (human, creative, social, cultural, institutional, physical, natural, artistic). Second level codes were inductively developed from the emerging findings and related to the nature of the interaction and interdependence between different elements of territorial capital, their localised accumulation over time, and impact on firm competitiveness. First and second level codes were then grouped into three key themes: 'territory-firm relations as a source of cost and differentiation advantage; 'interconnectivity between different forms of territorial capital' and 'advanced and inherited territorial resources'. These themes each displayed a level of homogeneity and were organized following a semantic approach, allowing data interpretation to remain linked to the words of the participants (Braun and Clarke, 2006). The findings related to these three themes are discussed in detail in section five.

<INSERT TABLE 1 HERE>

4. The provinces of Milan and Palermo

The provinces studied included two important Italian metropolitan cities: Milan which comprises a medium-large urban core and a surrounding area of 133 municipalities with a resident 3.2 million population; and Palermo, consisting of a smaller urban core and 81 municipalities, with a total population of 1.3 million residents[1]. The province of Milan was characterised by higher income per capita and stronger performance in terms of productivity, employment and innovation, compared to Palermo. In Milan province, in 2017 the Gross Domestic Product (GDP) per capita was EUR 52,400 with an unemployment rate of 6.4%, in contrast to the GDP per capita of EUR 18,100 and an unemployment rate of 19.8% in the province of Palermo[2]. Analysis here related to the administrative areas of the provinces, with the majority of interviews conducted within the two 'city-regions' which took into account the urban cores and their commuting zones[3].

The economic specialization of the two provinces was best analysed in relation to urban local systems which represented delimited geographical areas identified on the basis of where most of the resident population work and carry out their main social and economic relationships (ISTAT, 2015). Milan is one of the most important and dynamic urban local systems in Italy (ISTAT, 2015). Its economy is highly specialized in publishing activities, advertising and market research but includes too traditional manufacturing production and related "Made in Italy" activities, such as textiles, leather, and furniture (ISTAT, 2015). In contrast, the urban local system of Palermo has no particular specialization, besides its harbor, which is important for maritime transport and logistics. Where specialization has emerged (trade, insurance, public services) this is linked principally to the distribution of the population within the territory rather than specific localization factors (ISTAT, 2015). Although only one firm selected here enjoyed the particular benefits of being located within an industrial district (a fashion manufacturing firm in the province of Milan), the rest did benefit from being located within metropolitan cities and their associated urban agglomeration economies.

<INSERT FIGURE 1 HERE>

5. Main Findings

The findings presented here relate to the three key themes identified through the process of qualitative interview analysis: indirect and direct territory-firm relations as a source of firm competitive advantage; interconnectivity between different forms of territorial capital, and the role of advanced territorial resources compared to inherited resources.

[1] http://dati.istat.it/Index.aspx?DataSetCode=DCIS_POPRES1

[2] See https://ec.europa.eu/eurostat/news/themes-in-the-spotlight/regional-gdp and http://dati.istat.it/Index.aspx?QueryId=20745

[3]https://stats.oecd.org/Index.aspx?DataSetCode=CITIES

5.1 Indirect and direct territory-firm relations as a source of cost and differentiation advantage

A key theme that emerged from the interview analysis was how different elements of territorial capital affected firms to bring cost and/or differentiation advantages both through the role of indirect and involuntary territory-firm relations in developing *territorial externalities,* and in certain cases, through direct and voluntary territory-firm relations becoming an essential *core asset* of the business.

Indirect, involuntary territory-firm relations referred to the generation of territorial externalities that brought cost and, sometimes, differentiation advantages. From this perspective, firms benefited from territorial capital simply from deciding to locate in a particular area. For example, the strength of social capital characterizing the province of Milan, facilitated cooperation among firms (or relational capital) in all sectors, with the possibility of reducing their production and distribution costs, improving the quality of products and services and increasing their reputation. Such relations were exemplified by the case of a Milan hotel: *"Relations with local providers have a primary role…we can avoid big distribution networks that bring low cost products but pollute the planet, and increase our reputation* (CentralHotel(MI)).

In our analysis, territorial spillovers apparent from indirect and involuntary relations were predominantly, but not exclusively, related to urban externalities (e.g. the advantage for most firms of location close to the city) and to a lesser extent, location externalities (e.g. the advantage for a firm from location within an industrial district). Whereas existing theories of spatial spillovers conceive of space purely as a physical container where firms interact with each other to generate externalities via knowledge, industrial and growth spillovers (Capello, 2009), here, following Capello (2011), 'territory' was conceived and demonstrated to be an economic resource in itself. Consequently, territorial spillovers did not necessarily flow from one firm to another, or from one local system to another, but instead emerged from the local context with its specific resource endowment to firms. Further examples of how different elements of territorial capital influenced firms as territorial externalities are discussed in the following section (5.2).

A second type of 'direct and voluntary' territory-firm relation was identified, which comprised the conscious exploitation of territorial assets as theorized by Camagni (2008). In these cases, firms consciously decided to incorporate the exploitation of a particular element of territorial capital into their core business. This was the case, for example, of firms operating in food related industries that made use of typical local agricultural production to enable them to offer 'unique' products and services to gain differentiation advantages: *"Mountains and sea give us amazing products; the weather enhances these products...we have a head start in the agricultural raw materials"* (CastleRestaurant(PA)). The unique natural and artistic capital and 'cultural heritage' were essential assets for all the entrepreneurs operating in the A&F sector in Palermo, who delivered specific products, services and experiences directly linked to the exploitation of these assets and hence were unable to be imitated elsewhere. These assets were also exploited in other sectors, for example two ICT companies developed and sold unique IT solutions to map and exploit the rich and diverse natural, cultural and artistic resources of the province.

Indirect and direct territory-firm relations were not mutually exclusive, as certain resources affected firms in relation to both. This was the case of digital design companies in Milan who took (indirectly) advantage of the creative and stimulating environment of Milan's design industry in the form of urban and localization externalities, but also (directly) exploited the worldwide-recognized design tradition of Milan in their branding strategy, to differentiate their products from other national and foreign competitors.

Across the cases analysed it was possible to identify different types of firm-territory relations used by owner-managers which provided the basis for distinctive business strategies. For instance, one firm strategy adopted was to exploit a specific territorial asset which was peculiar and unique, in order to compete in national and international markets. This was the case of BeverageManu(PA) that exploited the ancient tradition of the province of Palermo in citrus fruit manufacturing rooted in the high quality of local citrus, to produce unique products for large multinationals and gain a strong national and international reputation. Different strategies included where firms decided to de-territorialize some of their activities to overcome territorial weaknesses or invest in the internal development of those resources lacking in the local context. For example in order to develop creativity outside the sluggish context of Palermo, DataProtection(PA), opened a new branch in the UK to keep up to date with cutting edge products and services,

5.2 The interconnection of different elements of territorial capital upon firm competitiveness in Milan and Palermo.

Findings from the interviews demonstrated how different elements of territorial capital came together in each place and how this unique bundle of local resources influenced firms' competitiveness in diverse ways in each province (see Box 1 and Box 2 below). In the province of Milan, the vast majority of owner-managers explained how their firms benefited from the simultaneous presence of a stimulating creative atmosphere, the availability of skilled human capital, a strong collaborative environment, a widespread open-minded and productive culture and an efficient transport/digital infrastructure network. The case analysis illustrated how these elements were fundamentally interconnected to each other, with the presence of one element dependent upon the level of accumulation of other elements. For instance, in Milan, the majority of firm owner-managers identified the strong creative environment of the territory as an important source for their innovation. According to respondents, across all sectors, this vibrant atmosphere was generated through a number of factors such as a dynamic competitive environment, the organization of numerous events and the vitality of the social capital that characterize the province. As the owner of Digital studio B(MI) observed: *"The network of contacts that Milan offers is useful to speed up many processes of thought and reflection…there is cross-fertilisation and exchange…Milan certainly favours this; it stimulates creativity and facilitates business development".*

Across all sectors, respondents identified the relative ease in establishing social relations as an important asset to offer superior products/services, facilitate production/sales, promote new business opportunities, reduce distribution costs and also favour creativity. The strength of this local social and relational capital was facilitated by the existence of a generalized sense of trust, an open-minded culture among entrepreneurs and willingness to collaborate. Crucially, it was complemented by the presence of physical capital in the form of a well-developed transport infrastructure: "*The public transport of Milan is excellent and this has a decisive impact on business, it is easy to move around and meet people.* (Microsoft(MI)). Efficient public transport, digital networks, and air transport not only facilitated interchange and network connections but also drastically reduced transport costs, in particular in the manufacturing and A&F sectors.

In terms of local culture, firm respondents routinely commented that Milan showed a strong 'entrepreneurial propensity' and a 'work-oriented' and 'open-minded' identity, where clients were able to accept and understand new trends and innovation. This positively affected businesses in all sectors, promoting the supply of new products/services and favoured a productive culture. Moreover, a dynamic 'entrepreneurial culture' was widespread throughout the province, which helped firms to become more competitive and attract human resources, clients and potential partners from other places.

The existence of such a vibrant and creative environment also contributed to the accumulation of human capital across all sectors. This was set out by the manager of CentralHotel(MI) who stated: *"The city is always a few years ahead compared to the rest of Italy, with respect to adoption of technologies and buy/sell philosophies…this represents a strong attraction for mid-top management profiles… the supply of workers is huge"*. Milan's labour market was a rich source of human capital for firms, not only due to the existence of good schools and universities but also as a result of its capability to attract people from other regions due to its creative and entrepreneurial atmosphere. This positively influenced firms' competitiveness by ensuring a highly diversified supply of qualified workers which contained their recruitment and training costs.

Box 1: The case of Digital Studio A, Milan (interview extract with owner-manager)

Being in Milan gives us immediate access to certain customers. Compared to Brescia, where we have the legal office, being in Milan, in this creative sphere, it is more inspiring because many events are organized and more things happen. It is easier getting information, accessing books, courses and workshops etc., and then people who come from Polytechnic of Milan have the approach that we look for. And also, the environment of competitors is wide; we have friendly relationships and collaborations with our competitors (…) Over the years, we have been collaborating with many companies that do similar things, that have been giving us work to do…thus, being in Milan was important (...) The stereotype of Milanese people, work-oriented, very fast, hasty with a very practical approach, sets our work rhythm. Other colleagues who work in other cities do not have the same rhythms or working times; they do not have the same deadlines, contacts or prices (…) The fact that Milan is one of the most organized cities definitely helps. I do not believe that in other cities it is so easy to go to work by public transport or by bike. It is not essential to stay in Milan but certainly, if we changed place, so many things would change (…) many things would be different even, for example, the fact that there is no public transport to go around and also less external stimulus. Surely the fact that, among all Italian cities, Milan is the most creative, very close to the world of fashion design, helps. It means that we are contacted by companies in other cities just because we are from Milan.... so, the best environment for a creative company is certainly Milan.

In the province of Palermo, the majority of owner-managers explained how their firms had benefited from the simultaneous presence of natural, cultural and artistic heritage, particularly those from the tourism sector. However, a weak entrepreneurial culture, a lower propensity in establishing collaborations, and few stimuli arising from the local context (creative capital), together with the absence of efficient transport infrastructure and effective local institutions, were considered important constraints on firms' competitiveness. Once again, case analysis demonstrated how these elements were strongly interconnected to each other.

In Palermo, the natural and artistic capital were highly valuable assets to a number of respondent firms in the A&F sector, providing strong potential to attract tourists and customers. These assets played a role in stimulating firm creativity to make unique products and places, as described by the owner of IslandRestaurant(PA): "*…territory stimulates a lot my creativity because we have products that you cannot find anywhere else, lentils, wild fennel, and we need to discover how these things can be transformed*". The importance of natural and artistic capital in stimulating firm creativity was not restricted only to the A&F sector, as the manager of SocialInnovationICT(PA) pointed out: "*Palermo inspires and stimulates less than other places…but walking in the historic centre and looking at amazing historic monuments is a strong source of inspiration*". Natural resources also play a role in attracting and retaining human capital given that: "*An increasing number of people, also from other regions, want to live here because of the sea, the beauty of the landscape, good weather…*"

(SocialInnovationICT(PA)). However, more broadly, such natural attractions were unable to compensate for the brain drain caused by low salaries and poor job opportunities, particularly in the ICT sector.

However, other than in relation to natural and artistic capital, owner-managers stressed how the province of Palermo seemed unable to promote innovation. This was frequently attributed to the apparent predominance of a 'closed-mind' culture and lack of entrepreneurial values; an attribute that was identified as a severe problem across all sectors. A general attitude of mistrust and suspiciousness towards strangers also constrained the development of bridging social and relational capital, which in turn limited the development of a more stimulating creative environment. Social capital here was mainly based upon 'bonding' and 'linking' relations, meaning that collaborations relied on immediate connections, such as family or friends, or on people in positions of authority (Woolcock, 2004; Malecki, 2012). Although there were cases of fruitful collaboration, the widespread dominance of forms of bonding and linking social capital was fundamental to problems of corruption and clientelism and their negative effects upon the wealth of institutional capital. Notably, almost all firms stressed how ineffective and inefficient institutions represented the main obstacle to the adequate accumulation of Sicilian territorial capital. As the owner of FurnitureManu(PA), stated: "*I believe that Sicilian artistic patrimony is priceless but it is not considered by the local government; it is in decay*". The owner of FoodManu(PA) believed that a weak collaborative culture depended on the fact that ..."*Institutions did not make any effort to put all firms together*". Moreover, a Mafia protection bribe (*pizzo*) often had to be paid by local entrepreneurs to local criminals, an issue discussed spontaneously by a number of firms, which increased their costs. Weak institutions were also considered responsible for the lack and backwardness of transport infrastructure which translated into higher costs and lost business opportunities.

Box 2: The case of Hotelbythesea in Palermo, Sicily (interview extract with owner-manager)

My hotel is located in an extraordinary location in the middle of Castellammare Gulf. I can say that the Sicilian market has plenty of capable people. Tourism has always been a key activity in Sicily and many people that gain experience abroad decide to return here. So, there is no shortage of skills. Creativity and innovation in the field of tourism is difficult because everything has already been said (...) Of course, I travel all over the world so I can see what others do. Sicilian people do not cooperate that much. We have nice relationships with some entrepreneurs but this is driven more by personal friendship relationships rather than a strategic approach; this is a pity. Everyone looks at his own business; everyone is scared that you steal clients.

Sicily is full of cultural attractions. Who comes here is not only interested in swimming in the sea but wants to discover our cultural patrimony which is one of the richest in the world. Culinary traditions, monuments. The mix of things here cannot be found in other places(...)

Even if we have a lot of opportunities, we are not able to promote tourism and this is mainly caused by the public administration. Transport infrastructures are a huge problem. Sicily is far from other markets. Apart from flight charters, there are very few flights. Then bureaucracy and mentality is amazing. People do not work to receive their salary but they look always for something else…if you need a licence, you need 15 signatures and so it means 15 gibbets (…) there is nothing here to help; you can just help yourself. Local policy should intervene in providing better infrastructure, road cleaning services, landscaping, precise rules, valorising our assets such as decorating roads with flowers, facilitating the credit access for entrepreneurs; then we should also think about the Mafia…..

Results from the interviews showed how each province was endowed with an idiosyncratic mix of assets which comprised its specific territorial capital. Such assets were routinely interconnected to each other in significant ways. For example, in Milan, high quality social capital was fostered by the presence of open-minded and dynamic cultural capital, which contributed to enrich the local creative capital, and in turn, facilitated further accumulation of human capital. In Palermo, the natural and artistic capital contributed to the accrual of human and creative capital while weak institutions negatively affected the preservation of these inherited resources, the accumulation of public infrastructure and social capital. Frail social capital was also caused by a closed-mind culture and negatively contributed to relational and creative capital and so on.

The interdependence and interconnection of such assets make attempts to build territorial capital from scratch, or reproduce it with similar characteristics in different places, a formidable task. From an RBV perspective, the analysis showed how particular conjunctions of territorial capital provided a valuable, unique and not easily replicable resource, and firms that benefited from its particular characteristics, as in the case of ICT firms in Milan, enjoyed long-term competitive advantages compared to other territories. Given the persistently uneven distribution of territorial capital and that not all regions, provinces or cities have the necessary preconditions for firms to take advantage of it (i.e. due to the lack of human capital, entrepreneurship skills, or social capital), its effect on firm competitiveness can be fundamental to explaining persistent economic disparities between regions.

5.3 Advanced and inherited territorial resources

The results from interviews showed that firms in the provinces of Milan and Palermo benefited from a ‘bundle’ of both tangible and intangible territorial resources. These resources included traditional factors of territorial capital, such as public infrastructures and human and creative capital, alongside innovative factors rooted in mixed resources (tangible plus intangible), and demonstrated firm capability to translate intangible elements into 'effective action', cooperation and connectivity (Camagni, 2008).

Building on the idea of Fahy (2002), two different bundles of resources were particularly apparent: 'inherited basic resources', such as natural, artistic and cultural heritage (those mainly provided by 'God' or ancestors) and 'created advanced resources' or 'capabilities' which are produced by long-term investment within the territory. Although the analysis showed that both tangible and intangible resources were valuable, immaterial forms of territorial capital or territorial capabilities, were essential to producing advanced resources and maximizing the benefit of inherited resources, in order to overcome territorial weaknesses and generate territorial competitive advantages that firms could exploit, either indirectly or directly.

In this respect, the province of Palermo was particularly blessed with a rich endowment of 'inherited resources', that were able to become an important source of cost and differentiation advantages for firms, particularly in the A&F sector. However, merely possessing these inherited resources did not guarantee the development of competitive advantages (Sirmon et al. 2007; Barney and Arikan, 2001). For example, despite the beauty of the landscape and rich artistic and cultural heritage, the lack of social capital, transport infrastructure, entrepreneurial mindset and weakness of the institutional capital, did not allow entrepreneurs to fully exploit the tourism potential of the province.

In contrast, more 'advanced resources' such as creative, social and relational capital, entrepreneurial culture and the capability to build and maintain efficient infrastructure, strongly supported the development of positive territorial externalities in the province of Milan and the competitiveness of its firms. This allowed the Milanese firms to compete effectively in the tourism sector despite the relative absence of the inherited resources available to firms in Palermo province. Although one might expect the province of Palermo to outperform Milan in terms of cultural heritage and natural capital compared to Milan, its rich heritage has not proved sufficient to build the image, prestige and influence required to succeed at the national and international levels (ISTAT, 2015). On the contrary, the Milanese capacity to promote culturally-related productions (e.g. typical traditional crafts), support cultural and creative industries and associated business chains (e.g. in the fields of design, fashion, advertising), cultural training activities (e.g. university courses with an artistic and cultural interest), and cultural and artistic non-profit institutions which operate in the management, preservation, enhancement and promotion of natural and cultural heritage, have together become crucial advantages for firms operating in Milan (ISTAT, 2015). Long-term investments in advanced resources or 'capabilities' therefore become essential to support local firms and fully realize local economic development potential.

Unpacking the multidimensionality of territorial capital through in-depth analysis enabled the research to gain also some understanding of its impact at the sector level. While advanced territorial resources were important regardless of the sector, the process through which different forms of territorial capital affected firms differed significantly across industries. For instance, the endowment of 'inherited resources' in the form of natural, cultural and artistic heritage, had an immediate impact upon A&F firms through attracting customers and generating differentiation advantages. These assets ultimately also influenced ICT and Manufacturing firms, by attracting skilled human resources from other regions, as was apparent in Palermo, stimulating entrepreneurial creativity, and acting as a marketing tool to promote the image of 'Made in Italy' products and services, as occurred in both provinces. Valuable territorial resources which were important drivers of competitiveness in particular sectors, therefore could be potentially useful also to other industries, although their influence here was variable and mediated through a range of development processes.

6. Some considerations about territorial policies

The process of recognizing territorial capital supports policymakers in their understanding of the specificities of different territories and the identification of appropriate policies to promote particular sectors within places, as well as reduce territorial disparities and obstacles to development. Furthermore, it supports understanding that the design of policies to increase and strengthen the territorial capital of deprived areas needs to be pursued within a long term framework (Fratesi and Perucca, 2018a; 2018b).

Results here have shown that the province of Palermo continues to lag far behind in terms of innovation capacity compared to the province of Milan and this negatively affect firms, particularly in the ICT and manufacturing sectors. In this vein, smart growth and specialization[4] that aim to boost growth and jobs at the local level by prioritizing research and innovation in competitive areas, have been set as a priority of the current European cohesion policy programming period (2013-2020). As a result, almost 20 per cent of the European Regional Development Fund (ERDF) spending assigned for the region of Sicily has been allocated to R&D, technology and innovation, and the digital agenda[5].

[4] *Smart Specialisation* is an innovative policy approach of the Euroepan Union (EU) https://ec.europa.eu/regional_policy/sources/docgener/guides/smart_spec/strength_innov_regions_en.pdf.,

[5] https://www.euroinfosicilia.it/po-fesr-sicilia-2014-2020/,

However, the analysis here shows that in the province of Palermo, smart specialization policies need to be oriented not only to supporting research infrastructures, incentivizing investments in R&D and supporting start-ups but, above all, to activities that will produce a more vibrant atmosphere of creativity through promoting occasions of networking and cross fertilization among firms, exploiting synergies between different technological domains (Cooke, 2016; Iacobuggi and Guzzini 2016), encouraging cultural change and entrepreneurship, and investing in education, cultural and institutional change. Institutional strengthening and renovation should be considered the main strategy for achieving such a transformation, but notably only 2.3% of ERDF funding earmarked for Sicily has been allocated to capacity building and technical assistance to implement the operational programme[6].

Analysis here also demonstrates that to promote the tourist sector adequately, as occurs in Milan, it is not enough to maintain and valorize artistic, cultural and natural resources but also requires stimulating bridging social capital and entrepreneurial culture, and strengthening inadequate infrastructure and the capacity of local institutions to valorize this heritage. To exploit fully the rich endowment of inherited resources, policymakers need the ability to identify and contrast regional weaknesses through long-term investment in advanced resources, by adopting a 'whole-of-government' approach (BDI, 2019). Such an approach is characterized by both vertical integration between the different levels of government (e.g central, regional, provincial) and horizontal co-ordination across areas such as tourism, infrastructures, culture, etc., in the pursuit of achieving integrated policies able to overcome territorial weaknesses and unleash local potential (see Cooke, 2016).

6. Conclusions

Through combining the Resource Based View theory of the firm with a conception of territorial capital as a bundle of local resources, this paper provides new insights into understanding sources of firm competitiveness related to location and reasons for persistent economic disparities among territories. Whilst previous research has tended to focus on a limited set of assets, such as human, social or natural capital (e.g. Crisholm and Nielsen, 2009), this research has considered the wide range of territorial capital assets and shown how sources of firm competitiveness can be found in the *mix* of all valuable tangible and intangible resources which characterize each place and which are jointly important for competitiveness.

[6] https://www.euroinfosicilia.it/po-fesr-sicilia-2014-2020/

In answering the central research question, *how does territorial capital, in practice, become a source of competitive advantage for firms*? results from the two provinces highlighted three main findings.

First, findings demonstrated, from an owner-manager's perspective, how local resources could become a source of competitive advantage in terms of cost and/or differentiation. Firms took advantage of territorial capital assets through location in a particular area, benefitting from territorial externalities or purposively deciding to incorporate specific local resources into their core business. This was critical for entrepreneurs to better understand the consequences of their location choices and opportunely select a business strategy appropriate to their province and sector. As a result, firms focused their business on specific territorial assets, where tacit knowledge or reputational advantage was strong, or looked outside the local spatial context to find those elements of territorial capital which they lacked.

Second, territorial capital was produced by the accrual and interaction of different tangible and intangible local resources that accumulated over space and time in different ways, and were frequently interdependent, making territorial capital difficult to reproduce or imitate and inherently uneven in distribution. This inimitability represented a source of long-term competitive advantage for firms located in more favourable environments, where territorial capital was rich and vibrant, in particular in its intangible components, as was the case in the province of Milan, and in direct contrast to the situation in the province of Palermo. Analysis of how firms were influenced by, or took advantage of territorial capital, alongside recognition of the inimitability of territorial capital and its different constitution in the North and South of Italy, provides an important component in explaining the persistent Italian regional economic divide.

Lastly, analysis showed how the endowment of 'advanced resources', such as creative, social and relational capital, culture and the capability to build efficient infrastructure, strongly represented a source of competitive advantage for firms in Milan. In comparison, Palermo, despite its rich endowment of 'inherited resources', has been incapable of developing adequate advanced resources to date. A set of spatially sensitive long-term, concurrent and coordinated policies that seek to enrich valuable and complementary territorial capital assets would, therefore, be more effective in reducing persistent territorial inequalities rather than past reliance upon isolated policy responses. In this respect, analysis of territorial capital can support policymakers to recognize the specificities of each territory and design appropriate place-based policies to promote particular sectors and firm types within different local areas.

Future research into territorial capital should further examine the process of accumulation of different local resources from an evolutionary perspective, looking at their interconnections and cause-effect relations in line with similar critiques of the notion of entrepreneurial ecosystems (Alvedalen and Boschmaa, 2017). A stronger focus of this analysis at the sector level would also be highly beneficial, both by looking in greater depth within particular sectors and developing a more comprehensive comparative sector analysis.

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