# A Triple Bottom Line:
# Apple's Investments in Indonesia

## Executive Summary

Foreign Direct Investment (FDI) can lead to productivity gains and economic development in developing countries. But creating a regulatory framework that both attracts foreign corporates and makes the most of their investments for domestic economic development is challenging. In 2015, Apple wanted access to Indonesia's growing consumer market for smartphones but wasn't willing to meet existing local content requirements. After two years of talks, Indonesia introduced a novel approach that led Apple to invest USD44 million in three training academies, instead of domestic manufacturing capacity, to gain access to the local market. These training Academies have developed Indonesian human capital and had spill-over benefits for the local education and technology sectors. While Apple pursued the Academies to gain market access, it also benefits from the development of local apps that boost the attractiveness of the iPhone to Indonesian consumers. The new regulation has ultimately seen Apple act in ways that are consistent with its loftiest corporate values. This case study will explore the use of local content requirements in Indonesia, how Apple has complied with Indonesian regulations, and the benefits of Apple's training academies. The success of this case is testament to the flexibility of Indonesian regulators and the imagination of Apple in finding overlap between its corporate interests and the long-term economic development needs in Indonesia. The case study will consider the scalability and replicability of Indonesia's approach.

## Section One - Foreign direct investment, local content rules and Indonesia's telecommunications sector

Given the benefits of a foreign presence in supporting economic development, countries compete to attract multinational enterprises to their shores. Since the global financial crisis of 2008, countries around the world are increasingly turning to local content requirements (LCR) to increase domestic production. LCR are policies that demand a certain share of production takes place within a domestic market, typically in exchange for the right to sell goods and services to consumers. LCR are frequently used in Argentina, Brazil, China, India, Indonesia, Russia, Saudi Arabia and the USA.

Empirical research suggests LCR are rarely successful. LCR do little to overcome the underlying conditions that made foreign investment unattractive in the first place. Indonesia's past use of LCR in the telecommunications sector have not successfully supported the technology transfer or domestic productivity gains that regulators might have hoped for. Moreover, LCR are often inconsistent with the nature of contemporary global

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value chains. For Apple, which doesn't directly manufacture the goods it sells, meeting an LCR would have required it to identify new local partners or force its existing suppliers to shift their production facilities. Apple was unable to identify suitable local partners amidst Indonesia's relatively unsophisticated manufacturing sector. Firms such as Satnusa, sometimes referred to as the 'Foxconn of Indonesia', had neither the scale nor the technical know-how to partner with Apple. Meanwhile, Apple lacked influence over the firms that made its products, predominantly multi-billion dollar Taiwanese manufacturers, for whom Apple is merely one of many customers (albeit a very large one) and who make decisions about where to locate manufacturing facilities based on access to human resources, costs of production and the time and expense of shipping goods to market.

**Section Two – Indonesia's new approach to LCR and Apple's Academies**

Following discussions with Apple, Indonesia implemented a new approach to LCR through Ministry of Industry Regulation Number 29 / M-IND / PER / 7/2017. Instead of manufacturing locally, Regulation 29 allowed Apple to meet its local content requirements by investing in local Academies in Jakarta, Surabaya and Batam (Batam's first batch of students will commence in March 2020). Apple provides full scholarships for students, who complete four hours of training five days a week for ten months. Apple's Indonesian Academies are similar in nature to training centres it operates in Brazil and Italy.

Apple Academies are run according to Apple's own pedagogy called Challenge Based Learning. This approach involves supporting students to solve real-world problems through the design and building of apps. Each teacher offers a particular specialisation in app development, such as coding or graphic design, but all are trained to develop a mentor-like relationship with students. In addition to a paid six-month training program before they commence, teachers have intensive engagement with US-based Apple staff and consultants to support on-the-job learning.

**Section Three – The value of the Academies to Indonesia and to Apple**

Apple's Academies will support economic development in Indonesia in a number of ways. The most immediate and tangible impact of the Academies on the Indonesian software industry is the number of patented and commercialised apps developed during the program. Less tangibly, but more importantly, is the career-long impact of Academy graduates on the broader technology sector and any knowledge sharing between them and future co-workers and employers.

Furthermore, the pedagogy in Apple's Academies is spilling over to the local education sector. This horizontal technology transfer happens through formal channels with local partner institutions, such as through regular short courses for staff. But it is also informal. For example, the set-up of the Surabaya Academy was watched with great interest by their local partner, the University of Ciputra, which hopes to incorporate aspects of Apple pedagogy and design into its ongoing construction of classrooms.

It seems unlikely that Apple would have made similar efforts to share knowledge with such a broad spectrum of Indonesian individuals and firms if they had invested in more typical local content production such as a vertical supplier relationship. What's more, given that the dearth of human capital is one of the key challenges facing the development of an Indonesian technology sector, these direct technology transfers to the education sector and contribution to the talent pool may prove to be very well targeted in supporting Indonesia's long-term economic development agenda. It is, however, difficult to quantify these gains.

The benefits to Apple of its investments in the Academies are considerable, if largely unmeasurable. First and foremost, Apple's investments in the Academies grant it access to Indonesia's large and growing consumer market at a time when global smartphone sales are levelling off. The Academies are akin to a corporate social responsibility program in their value to Apple's brand development. The apps developed through the Academies and by alumni will contribute to the broader ecosystem of services available on Apple devices. Increasing the availability of local apps on the Appstore will boost the saleability of Apple's core product, the iPhone, and also be a source of services revenue for Apple. The difficulty of quantifying these long-term benefits for Apple as a company is problematic given this is essential to inform Apple's decision about how much to invest in the Academies over the long term.

**Section Four – Local Content Rules and Ethical Corporate Behaviour**

The long-term approach inherent in the Apple Academies reflects the sort of corporate behaviour companies like Apple aspire to. While there is precedent for corporates providing training, and for corporates shaping the education of Indonesian students, Apple's approach is novel in providing so much funding for quality education at a scale far in excess of their own human resource requirements, and because of the transparency with which it is taking place. Apple's commitment to the Academies is a testament to the power of regulations to lead international corporates to behave in a way that goes beyond the short term and aligns with the economic development needs of the host country.

**Section Five – Replicability and Scalability**

Regulation 29 works for Apple because it is selling a platform, not just a product. While it is difficult to imagine ways in which companies selling traditional products can use Regulation 29 to find win-win investments, the basic framework outlined in Regulation 29 provides considerable opportunity for creative thinking. Both corporates and the Indonesian government will need to exercise considerable creativity in the use of Regulation 29. To date, however, the Indonesian Government appears to be taking a one-size-fits-all approach to the implementation of Regulation 29.

Regulation 29 has allowed Apple to propose and carry out its investment in the domestic market with considerable freedom. Apple's scope to abuse this flexibility is lessened by the high-level political oversight it informally receives as a first mover. But direct political oversight is difficult to scale; the more projects that take place under Regulation 29 the more the bureaucracy would need to ensure corporate accountability.

The size and potential of the Indonesian market surely increased Apple's willingness to pay for market entry. The ability of Indonesia to extract this price from corporates operating in other sectors – or indeed the ability of other countries to extract this price from Apple or other corporates – may need to take into consideration not only the value of the domestic market, but also its competitiveness in relation to other global opportunities vying for their FDI.

Indonesia's new approach still has many of the drawbacks of traditional LCR. Regulation 29 imposes a cost on corporates that may deter them from entering the Indonesian market or push up the price of domestic consumer goods when they do. Moreover, these costs are not imposed on domestic producers, distorting the market and potentially leaving Indonesia at odds with its WTO commitments. More broadly, while the engagement of international corporates in domestic policy processes in this case has been broadly positive, regulatory capture can be devastating.

**Conclusion**

Regulation 29 has led Apple to find overlap between its corporate interests and broader development needs in Indonesia, and in doing so, delivered benefits for the Indonesian economy and for Apple, while also seeing Apple act in a way that is consistent with its highest corporate values. While traditional LCR often do little to improve the competitiveness of a local market, Indonesia's new approach is a case study in how flexibility and imagination can lead to win-win outcomes. This case study, however, has also raised several issues in scaling and replicating Regulation 29, including the challenges of applying the approach in other sectors and ensuring corporate accountability.